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# THE APPROPRIATE RECOGNITION OF THE INTEREST OF THE GROUP OF COMPANIES IN THE EUROPEAN UNION

## DOCTORAL THESIS

**Study programme: Law**

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**ANNOTATION**

This doctoral thesis examines the appropriate recognition of the interest of the group in the European Union (EU). There is no recognition of the interest of the group at the EU level and Member States have conflicting mechanisms of regulating it. This doctoral thesis comes to the conclusion that the legal environment is fragmented and demoting for a positive EU wide business environment, which threatens the well-functioning of the Internal Market and the Regulation has to be adopted for the recognition of the interests of the group.

The objective of this research is to determine the appropriate recognition of the interests of the group in the EU. The methodology used will be that of legal doctrinal, comparative, reform agenda research and legal theory, as well as methods of legal norm interpretation such as grammatical, historical, teleological and systemic.

The doctoral thesis consists of 130 pages.

**Keywords:** *group of companies, creditor protection, minority shareholder protection*.

## ANMERKUNG

Die Doktorarbeit untersucht die angemessene Anerkennung der Interessen der Gruppe in der Europäischen Union (EU). Die Interessen der Gruppe werden auf EU-Ebene nicht anerkannt und die Mitgliedsstaaten verfügen über widersprüchliche Regulierungsmechanismen. Die Doktorarbeit kommt zu dem Schluss, dass das rechtliche Umfeld fragmentiert ist und ein positives EU-weites Geschäftsumfeld beeinträchtigt, was das reibungslose Funktionieren des Binnenmarktes gefährdet, und die Verordnung zur Anerkennung der Interessen der Gruppe angenommen werden muss.

Ziel der Forschung ist es, die angemessene Anerkennung der Interessen der Gruppe in der EU zu bestimmen. Die verwendete Methodik umfasst rechtsdoktrinäre, vergleichende, reformagendawissenschaftliche und rechtstheoretische Methoden sowie Methoden der Rechtsnorminterpretation wie grammatikalische, historische, teleologische und systemische Methoden.

Die Doktorarbeit umfasst 130 Seiten.

**Schlüsselwörter:** *Unternehmensgruppe, Gläubigerschutz, Schutz von Minderheitsgesellschaftern.*

## ANOTĀCIJA

Promocijas darbā tiek pētīta grupas uzņēmumu interešu atbilstoša atzīšana Eiropas Savienībā (ES). Grupas uzņēmumu intereses ES līmenī netiek atzītas un Dalībvalstīm ir pretrunīgi mehānismi tās regulēšanai. Promocijas darbā tiek secināts, ka grupas uzņēmumu interešu atzīšanas tiesiskais regulējums ir fragmentēts un negatīvi ietekmē ES uzņēmējdarbības vidi, kas apdraud Iekšējā tirgus darbību, līdz ar ko ir jāpieņem Regula, kas atzītu grupas uzņēmumu intereses.

Darba mērķis ir noteikt grupas interešu atbilstošu atzīšanu ES. Promocijas darba izmantotās pētījuma metodes ir analītiskā, loģiskā, salīdzinošā un sistemātiskā, kā arī tiesību normu interpretācijas metodes: gramatiskā, vēsturiskā, teleoloģiskā, sistemātiskā.

Promocijas darba apjoms ir 130 lappuses.

**Atslēgas vārdi:** *grupas uzņēmumi, kreditoru aizsardzība, mazākuma dalībnieku aizsardzība*

## List of Abbreviations

**Accounting Directive** – The Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance

**AG** - Aktiengesellschaft – German Stock Company

**AktG** - Aktiengesetz – German Stock Corporation Act

**BW** - Burgerlijk Wetboek – Dutch Civil Code

**Capital Requirement Regulation** – The Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

**CJEU** - The Court of Justice of the European Union

**Convention of Jurisdiction** - 1968 Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters

**Council** - The Council of the European Union

**CSC** - Código das Sociedades Comerciais – Portuguese Code of Commercial Companies

**CSO** - Chief Sales Officer -

**de minimis Regulation** – The COMMISSION REGULATION (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid (Text with EEA relevance)

**Directive on European Works Council** – The Directive 2009/38/EC of the European Parliament and of the Council of 6 May 2009 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees (Recast) (Text with EEA relevance)

**EC** - The European Commission

**ECLE** – The European Company Law Experts

**EEIG** - The European Economic Interest Grouping

**EU** - The European Union

**GDP** - Gross domestic product

**General Data Protection Regulation** – The REGULATION (EU) 2016/679 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 April 2016 on the protection

of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (Text with EEA relevance)

**GmbH -** Gesellschaft mit beschränkter Haftung – German Limited Liability Company

**GmbHG -** Gesetz betreffend die Gesellschaften mit beschränkter Haftung – German Act on Limited Liability Companies

**IAS** – The International Accounting Standard

**IASB -** The International Accounting Standards Board

**ICLEG** – The Informal Expert Group on Company law

**IFRS** – The International Financial Reporting Standard

**Insolvency Regulation** – The Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast)

**LSE -** Large Sized Enterprises

**öAktG -** ÖsterreichischesAktiengesetz – Austrian Stock Corporation Act

**SE -** Societas Europaea – The European Company (public company)

Shareholders Rights Directive – The Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies

**SMEs -** Small and Medium Sized Enterprises

**SPE -** Societas Privata Europaea – The European Private Company (limited liability company)

**SUP -** Societas Unius Personae – The Single – Member private limited liability Company

**Takeover Bids Directive -** Directive 2004/25/EC of the European Parliament and of the Council of 21 april 2004 on takeover bids

**TFEU -** The Treaty on the Functioning of the European Union

**Transfer of Undertaking Directive -** The Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses

**Transparency Directive** – The Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC

**VAT** – The value added tax

## TABLE OF CONTENTS

## INTRODUCTION

The introduction of the concept of "company" is a key factor in the development of economic markets and its importance cannot be exaggerated. Freedom of establishment promotes cross-border corporate growth and new challenges appear in Europeanisation of companies and groups of companies.[1] National and international economic markets are dominated by groups of companies, furthermore, autonomous and independent companies have lost their importance.[2] The spirit of European company law must reflect the spirit of the new economic order.[3]

The cornerstone of the Internal Market of the Union is the European Union's (EU) company law. The Internal Market renders the national systems of company law of the Member States to be coherent.[4] However, the national company laws of the EU Member States have great importance in that they structure the constitution of civil society and establish social justice.[5] Company law is characterised by a need for exercising sovereignty in this matter. The Treaty on the Functioning of the European Union (TFEU), being in line with the principle of conferral, gives no general competence to the EU to regulate company law in its entirety, which is why Member States continue to operate based on individual company law systems. The group of companies rather than the single company has become the predominant structure of large–sized enterprises in the EU.[6] Moreover, the main objective of the Internal Market is to further economic integration, so that market participants can act freely across borders without being hindered by any barriers and obstacles, to benefit fully from the economy of scale.

Traditionally, national company law is based on the notion of a separate legal personality approach where the company is perceived as an independent and autonomous legal entity. Nevertheless, in a group a company can be under strict instructions. In this latter, a company, which issues instructions is called a parent company, while the former are called subsidiaries. The interest of each member of the group is independent profitability and

[1] Kirkbride, J. (1994). European company law harmonisation: a study. *International Company and Commercial Law Review.* Volume 5, issue 8. PP. 282 – 284.
[2] Hadden, T. (1984). Inside Corporate Groups. *International Journal of the Sociology of Law.* Volume 12. P. 271.
[3] Kirkbride, J. (1994). European company law harmonisation: a study. *International Company and Commercial Law Review*. Volume 5, issue 8. P. 281.
[4] Roth, H., R., Kindler P. (2013). The Spirit of Corporate Law: Core Principles of Corporate Law in Continental Europe. Bloomsbury Publishing. P.211.
[5] Manko, R. (2015). EU competence in private law. The Treaty framework for a European private law and challenges for coherence. *European Parliamentary Research Service (EPRS).* P. 1. https://doi.org/10.2861/292462
[6] Reflection Group on the future of EU company law. (2011). Report of the Reflection Group on the Future of EU Company Law ('Reflection Group Report'). P. 59. http://dx.doi.org/10.2139/ssrn.1851654

sustainability, while the interest of the group is the economic well-being of an organisation, which points to potential differences in concerns. There is no recognition of the interest of the group at the EU level and Member States have contrasting and even conflicting mechanisms for regulating it. It creates islands of unified company law within the sea of differing approaches of national law on the issue of the recognition of the interests of the group. The legal fragmentation in recognition of the interests of the group can become as an obstacle or barrier to functioning of the Internal Market.

French law has no specific rules on groups of companies, in spite of repeated parliamentary attempts (*Cousté* proposals).[7] It is rather established by case law.[8] The concept of the group is perceived as an economic rather than a legal concept, therefore, a group of companies does not exist as a legal entity, cannot be sued and has no capacity to sign agreements on its own.[9] Only in exceptional cases might a court might recognise the parent company and its subsidiary as a single unit. Moreover, in France, a person may be held criminally liable for abuse of corporate assets (*abus de biens sociaux*) of a public limited company (*Société Anonyme*) or a private limited liability company (*La société à responsabilité limitée*).[10] The abuse of corporate assets constitutes a use of a company's credit or property in bad faith that is contrary to the interests of the company, for personal reasons or in order to benefit another undertaking or company, in which it has direct or indirect interest. Concerning a group of companies there is a "group defence" or "safe harbour." Group defence or safe harbour was established in 1985 in the French *Cour de Cassation* in the *Rozenblum* case. The appeal court ruled that the interest of the group could prevail over the interest of the subsidiary without criminal liability for abuse of corporate assets, if: 1) a group is characterised by firm structural establishment of the group; 2) there is effective and strong business integration; 3) financial equilibrium is preserved; 4) actions are not exceeding the possibilities.[11] Above-mentioned criteria are called *Rozenblum* doctrine. Although the *Rozenblum* case was a criminal prosecution for abuse of corporate assets, the doctrine is applied also in corporate law.[12] The

[7] Proposition de loi sur les groupes de sociétiés et la protection des actionnaires et du personnel, submitted to Parliament on 19 February, 1970 (no. 1055) and on 12 April 1973 (no. 52).
[8] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 170.
[9] Desjardins, I., Damien, F., Delogu Bonan, S. (2007). Report from France. Country Status Reports. *European Company Law*. Volume 4, Issue 5. P. 227. https://doi.org/10.54648/eucl2007054
[10] Private Limited Companies Article L. 241-3 of *Code de commerce*. Public Limited Companies Article L. 242-6 of *Code de commerce*.
[11] Cour de Cassation, Chambre criminelle, du 4 février 1998, 97-82.417 (Rozenblum). Publié au bulletin.
[12] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. *Kluwer Law International*. P. 227.

*Rozenblum* doctrine recognises the interest of the group and has been used in several responding jurisdictions, such as Belgium, Estonia, Italy, Netherlands. Nevertheless, the *Rozenblum* doctrine has been criticised for being vogue with regards to the recognition of the interest of the group.[13]

In the Netherlands it is acknowledged that companies do not always operate on a stand-alone basis. Corporations can and do form a group of companies. Groups of companies can be arranged in different patterns. The concept of a group of companies is labelled as *Concernrecht*.[14] There is a lack of consolidated statutory group law, it is rather established by *ad hoc* provisions in separate fields. Dutch group law has increasingly been challenged and regulatory gaps are filled with case law.[15] Legal theorists for the necessity of codification refer to the EC's right of harmonisation. [16]

Italy takes the notion that a legal person as a natural person is entitled to rights and obligations, therefore, the company may become a shareholder.[17] In Italy it is accepted as a matter of fact that group company structure exists, but there must be granted protection for minority interests (e.g., for minority shareholders, creditors etc.). The 1942 Italian Civil Code (*Codice Civile*), its amendments and complementary laws did not address appropriately a group of companies; these rules did not cover any of the issues of pursuing the interests of the group. The 2004 Company law reform changed the regulatory framework of recognition of the interest of the group in Italy. It introduced statutory *Rozenblum* doctrine. Besides, more detailed rules were materialised by: enhancing transparency; introducing direction and coordination (*direzione e coordinamento)* of group of companies; requiring reasoned decisions for pursuing the interest of the group; advancing publicity of the participation in groups of companies; broadening protection for minority shareholders in case of leaving or entering a group of companies; instituting the right of withdrawal when a takeover bid is not compulsory. The 2004 Company law Reform was implemented by amending Articles 2325 – 2554 of *Codice Civile.*[18]

[13] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 218. https://doi.org/10.1515/ecfr-2013-0194

[14] Schuit, S. R., Bier B., Verburg L. G., Wisch J. A. T. (2002). Corporate Law and Practice of the Netherlands. *Kluwar Law International*. PP. 57-58.

[15] Potjewid, G., Van Der Kroon J. (2007). Report from the Netherlands. Country Status Report. *European Company Law*. Volume 4, Issue 5. P 235. https://doi.org/10.54648/eucl2007056

[16] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. PP. 233 and 276-277.

[17] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. P. 121. https://doi.org/10.54648/eucl2019018

[18] Ibid, P. 123.

However, 2004 reform has been criticised for being incomplete and an unnecessary derogation of long legal tradition.[19]

In 1965 Germany introduced "the law on affiliated companies" (*Konzernrecht*).[20] It was estimated that in 1965 70 % of German Stock Corporations (*Aktiengesellschaft*) were part of groups of companies.[21] In 2016 it was estimated that already 75% of *Aktiengesellschaft* (*AG*) and 50% of German Private Limited Liability Companies (*Gesellschaft mit beschränkter Haftung*) were part of corporate groups.[22] Blumberg expresses the position that *Konzernrecht* is "the most advanced in the world."[23] Antunes acknowledges that *Konzernrecht* "represents the most pioneering, elaborated and complex attempt so far developed at a general regulation of corporate groups."[24] Meanwhile Hommelhoff points out that *Konzernrecht* is "costly, complicated and ineffective."[25] *Konzenrecht* can be effective for large groups, however, it is debatable for smaller groups of companies.[26] Regardless, the German approach has influenced the legislation of Croatia, the Czech Republic, Hungary, Latvia, Slovenia and Portugal. On the other hand, Austria and Poland have chosen not to adopt it despite being very close in legal tradition to Germany.[27] Lastly, in 1974, a draft for a ninth EU company law Directive was dropped due to the lack of support because it was too similar to the German model of codification of the group of companies.[28] The provisions of *Konzernrecht* are laid down in

[19] Fasciani, P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, issue 2. Volume 4, issue 2. P. 231. https://doi.org/10.1515/ECFR.2007.013

[20] Hommelhoff, P. (2001). Protection of Minority Shareholders, Investors and Creditors in Corporate Groups: the Strengths and Weaknesses of German Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 2. P. 61. https://doi.org/10.1017/S1566752900000331

[21] Böhlhoff, K., Budde, J. (1984). Company Groups - The EEC Proposal for a Ninth Directive in the Light of the Legal Situaiton in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 164.

[22] Scheuch, A. (2016). Konzernrecht: An Overview of the German Regulation of Corporate Groups and Resulting Liability Issues. *European Company Law*. Volume 13, issue 5. P. 191. https://doi.org/10.54648/eucl2016027

[23] Blumberg, P. I. (1987). The law of corporate groups: tort, contract, and other common law problems in the substantive law of parent and subsidiary corporations. Boston: Little Brown. P. 55.

[24] Engrácia, Antunes, J. (1994). Liability of Corporate Groups: Autonomy and Control in Parent-Subsidiary Relationships in US. German and EU Law An International and Comparative Perspective. Deventer: Kluwer Law and Taxation. P. 314.

[25] Hommelhoff, P. (2001). Protection of Minority Shareholders, Investors and Creditors in Corporate Groups: the Strengths and Weaknesses of German Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 2. P. 68. https://doi.org/10.1017/S1566752900000331

[26] Hopt, K. J., Pistor, K. (2001). Company Groups in Transition Economies: A Case for Regulatory Intervention? *European Business Organization Law Review (EBOR)*. Vol. 2. P. 10. https://doi.org/10.1017/S1566752900000318

[27] Conac, P. H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 200. https://doi.org/10.1515/ecfr-2013-0194

[28] Draft Proposal for a Ninth Council Directive pursuant to Article 54(3)(g) of the EEC Treaty relating to links between undertakings and in particular on groups. Accessed 26 May 2024. Available at: https://www.mhc.ie/uploads/9th_proposal.pdf

*Aktiengesetz (AktG)*. Accordingly, it is then applied to *AG*. The reason for installing *Konzernrecht* in *AktG* is that the management board (*Vorstand*) of an *AG* acts on its own responsibility, under Article 76, paragraph 1 of *AktG.*[29] Consequently, in an *AG* subsidiary the parent company does not necessarily imply a power or a control. German Private Limited Liability Companies (*Gesellschaft mit beschränkter Haftung*) are regulated by the Limited Liability Companies Act (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung*).[30]*Konzenrechts* provisions are not introduced in *Gesetz betreffend die Gesellschaften mit beschränkter Haftung* (*GmbHG*). The group law for *Gesellschaft mit beschränkter Haftung* (*GmbH*) is developed by case law.[31] Despite the fact that *Konzenrecht* provisions are designated for *AG* subsidiaries, they are formed as private limited liability companies (*GmbH*).[32] In 1988, there were 2373 *AG* and 400 000 *GmbH* from, of which an estimated 60 000 were part of a group of companies.[33]

In the company law field Portugal is considered as a legal system that is heavily inspired by foreign models (mainly French and German company laws) and is very dependent on the EU binding subordination and harmonization. In Portugal the Code of Commercial Companies (*Código das Sociedades Comerciais*) regulates all commercial companies, which operate in its jurisdiction. Although small and medium sized companies are still the backbone of the Portuguese economy, the group of companies' economic concentration has progressed significantly.[34] *Código das Sociedades Comerciais* (*CSC*) Part IV, Articles 481–508-E specifically governs groups of companies.[35] The goal of specific rules applicable to a group of companies is to endow the subsidiary's interests, minority shareholders and creditors protection by minimizing the regulatory gap between autonomous or independent companies and the dependent companies. Undoubtedly, the German (*AktG*) approach has influenced Portugal's initiative to regulate groups of companies separately. Similar to Germany (*AktG*) in *CSC*,

[29] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[30] Act on Limited Liability Companies. Consolidated and published in the Federal Law Gazette III, Index No. 4123-1. Amended by Article 10 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[31] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 7.
[32] Zöllner, W. (1992). Inhalt und Wirkungen von Beherrschungsverträgen bei der GmbH. Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR). S. 177-179. https://doi.org/10.1515/zgre.1992.21.2.173
[33] Hopt, K. J. (1991). Legal Elements and Policy Decisions in Regulating Groups of Companies. London: Sweet & Maxwell. P. 82
[34] Engrácia, Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review (ECFR)*. Volume 2, Issue 3. PP. 324-325 and 373. https://doi.org/10.1515/ecfr.2005.2.3.323
[35] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

legitimization of the parent company's power of control or direction of the group of companies is linked with the corresponding protection of a subsidiary's interests, minority shareholders and creditors.

In Latvia, a group of companies is regulated by a specially designed code of Group of Companies Law (*Koncernu likums*).[36] The regulatory basis for *Koncernu likums* is " the law on affiliated companies" (*Konzenrecht*) laid down in German *AktG*.[37] Interestingly, *Koncernu likums* was adopted on 23 March 2000, but Commercial law (*Komerclikums*) was adopted later on 13 April 2000.[38] On 14 April 2006 *Koncernu likums* was amended (minor changes). The main purpose of separately regulating a group of companies is protection of creditors and minority shareholders;[39] less concerned with pursuing an interest of the group. Unfortunately, the wording of *Koncernu likums* is vague and ambiguous, as well as lack of case law in respective fields.[40] Distinguished law of a group of companies causes practical difficulties in applying it within the framework of *Komerclikums* (general company law rules). In 2009, the initiative was taken to implement rules of *Koncernu likums* into *Komerclikums* (with amendments) and afterwards repeal *Koncernu likums.*[41] Such an initiative has not been materialised.

Spain regulates independent, legal and economic companies only. Due to this fact, Spanish law does not contain a specific regime for groups of companies, nor does it govern any of the problems linked to the group of companies' structure. [42] Nevertheless, corporate freedom is attributed, thus the group of companies exist.[43] No distinct governance of the group of

[36] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[37] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[38] Komerclikums. Pieņemts 13.04.2000. Stājies spēkā 01.01.2002. Publicēts: Latvijas Vēstnesis, 158/160, 04.05.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 11, 01.06.2000. Pēdējie grozījumi 01.08.2023.

[39] Ministru kabineta 2009.gada 6.maija rīkojums Nr.292. Par koncepciju "Par koncernu tiesiskā regulējuma efektivitātes uzlabošanu." Accessed 27 May 2024. Available at: http://tap.mk.gov.lv/mk/tap/?pid=40090714

[40] Grīnberga, I. (2020). Vai pastāv ierobežotas atbildības robežas attiecībā uz kapitālsabiedrību daļu īpašniekiem? *Jurista Vārds*, Nr. 36(1146). 5. lpp.

[41] Ministru kabineta 2009.gada 6.maija rīkojums Nr.292. Par koncepciju "Par koncernu tiesiskā regulējuma efektivitātes uzlabošanu." Accessed 27 May 2024. Available at: http://tap.mk.gov.lv/mk/tap/?pid=40090714

[42] Fuentes, M. (2007) Corporate Groups and Creditors Protection: An Approach From a Spanish Company Law Perspective. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 4. P. 530. https://doi.org/10.1515/ECFR.2007.026

[43] Girgado, P. (2006). Legislative Situation of Corporate Groups in Spanish Law. *European Company and Financial Law Review (ECFR)*. Volume 3, Issue 4. P 368. https://doi.org/10.1515/ECFR.2006.016

companies leads to a wide diversity of rules applied from different parts of the legal system and makes it more difficult to operate within it.[44] Such a system has been heavily criticized.[45]

In the 1970s the European Commission proposed three significant attempts for regulating a group of companies. The first attempt in 1972 was the proposed fifth directive on company law to govern joint – stock corporations. In 2001 the proposal was withdrawn.[46] The second attempt in 1974 was a draft for a ninth company law directive based on the German model (*AktG*). In the 1980s the ninth company law directive was dropped due to the lack of support.[47] It was argued that German law for a group of companies was too rigid and not particularly effective.[48] The third attempt was to implement a chapter for a group of companies in a Regulation of *Societas Europaea* (SE), but it was also dropped in 1980s.[49] Instead in 1983 the Directive on consolidated accounts was adopted.[50]

The object of this research is the group of companies in the EU. The subject of the research is the recognition of the interests of the group in the EU. The research question is by what means the EU intervention in the recognition of the interest of the group affects the group of companies? The objective of research is to determine the appropriate recognition of the interest of the group in the EU. The following research tasks are defined:

1. To assess whether the group of companies are regulated at the EU level;
2. To analyse how Member States recognise the interest of the group;
3. To investigate the legal fragmentation of the recognition of the interest of the group;
4. To research the impact of Member States practises' of recognition of the interests of the group on the Internal Market;

[44] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 139.
[45] Embid Irujo. J.M. (2003). Introduccion al derecho de los grupos de sociedades. Comares, Granada. P. 41.
[46] Proposal for a Fifth Directive on the Coordination of Safeguards which for the Protection of the Interests of Members and Outsiders, are Required by Member States of Companies within the Meaning of Articles 59, second paragraph, with respect to Company Structure and the power and responsibilities of Company Boards. Submitted by the European Commission to the Council on 9 October 1972. Accessed 27 May 2024. Available at: https://op.europa.eu/en/publication-detail/-/publication/e626eaef-4c67-4f34-992f-5191cf8c682b/language-en
[47] Draft Proposal for a Ninth Council Directive pursuant to Article 54(3)(g) of the EEC Treaty relating to links between undertakings and in particular on groups. Accessed 27 May 2024. Available at: https://www.mhc.ie/uploads/9th_proposal.pdf
[48] Conac, P.H. (2013) Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 196.
[49] Proposal for a Council Regulation embodying a Statute for the European Company (COM/70/600/FINAL). Submitted to the Council on 30 June 1970.
[50] Seventh Council Directive 83/349/EEC of 13 June 1983 based on Article 54(3)(g) of the Treaty on consolidated accounts. Adopted on 29 June 1983. Published in Official Journal of the European Union L 193.

5. To explore the EU intervention in Member State's recognition of the interest of the group.

The methodology used will be that of legal doctrinal research. The EU Member States recognition of the interests of the group can be classified in various models, therefore comparative research method will assist in determining the differences in the development of the recognition of the interest of the group in the EU Member States' national laws. In order to comprehend the meaning and purpose of legal norms, as well as conflict of laws, the following methods of interpretation were applied: 1) grammatical; 2) historical; 3) teleological; 4) systemic. To comprehensively examine the legally diversified environment and context of the recognition of the interest of the group, the legal theory method will support the research beneficially. In addition, in the development of the conclusions, the reform agenda research also will be used in order to intensively evaluate the adequacy of existing rules.

Due to the limited scope of the thesis, the section 2 of the Recognition of the Interest of the Group at the National Level of Member States is limited to French, Dutch, Italian, German, Portuguese, Latvian and Spanish practices. However, three types of models of recognition of the interests of the group prevail, and researched Member States practices covers it. France is founder of the "group defence" or "safe harbour" and Netherlands follows it and has even new developments of it. Germany is founder of the compensatory model and Latvia has simply translated it, but in addition increased the scope of legal act's application. Portuguese also follows the German compensatory model, but has implemented it with significant differences. Italy has moved from the German compensatory model to the French "group defence" or "safe harbour", but has it made as statutory law. Spain represents the third model that does not recognise the interest of the group and relies on traditional company law presumptions. Hence, the findings of the research are validated and reliable, which is appropriate to make generalization of results across the EU.

In 2002 the Report of The High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe suggested establishing at the EU level provisions for management of groups companies.[51] In 2011 the Report of the Reflection Group on the Future of EU Company Law advised the Commission to consider taking action at the

[51] The High Level Group of Company Law Experts. (2002). Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe ('Winter Group Report'). P. 17. Accessed 27 May 2024. Available at: https://ecgi.global/content/winter-group-2002

EU level for recognizing the interests of the group.[52] European Company Law Experts (ECLE) conducted the work resulting in the previously mentioned Report. The ECLE is an independent a non- profit organization that consists of European Company and Financial law experts. In 2012 the Commission's action plan on European Company law and corporate governance announced an initiative on recognition of the interest of the group.[53] In 2014 The EU created the Informal Expert Group on Company law (ICLEG) in order to assist the Commission in the Company law field. In 2016 the ICLEG published a report on the recognition of the interests of the group.[54] The ICLEG report exposed legal fragmentation and its cause. The recognition of the interests of the group still remains the agenda for the ICLEG. The development has been reluctant and in 2024 the concern of appropriate recognition of the interests of the group continues to be a challenge.

There are no academic studies on group companies in Latvia. There is no recognition of the interests of the group at the EU level, therefore, literature focuses more on matters that are harmonized, such as formation, capital and disclosure requirements in the fields of banking law, tax law, and accounting. In the view of all foregoing, from a Company law perspective present literature does not address the issue in a satisfactory manner despite the identification of the problem. The novelty of the research is reflected in the development of the theory of group companies. Theoretical contribution to this research is found in establishment of conclusions. Practical contribution to this research is comprehensive comparative analyses of French, Dutch, Italian, German, Portuguese, Latvian and Spanish practices of recognition of the interests of the group, which covers doctrinal or jurisprudential group law, systematized group law and absence of group law. Moreover, this research investigates legal fragmentation in recognition of the interests of the group impact on the Internal Market. In other words, in depth it examines whether legal fragmentation in recognition of the interest of the group is welcomed or is an obstacle or barrier to the Internal Market. Furthermore, the research provides steps of action for the EU to establish the appropriate recognition of the interests of the group, which may take the form of regulatory and administrative solutions.

[52] Reflection Group on the future of EU company law. (2011). Report of the Reflection Group on the Future of EU Company Law ('Reflection Group Report'). P. 79. Accessed 27 May 2024. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1851654

[53] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee of the Regions. (2012). Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies. P. 14. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A52012DC0740

[54] The Informal Company Law Expert Group (ICLEG). (2016). Report on the recognition of the interest of the group. http://dx.doi.org/10.2139/ssrn.2888863

The structure of the thesis consists of the introduction, 4 sections of the main research, as well as conclusions and proposals. The introduction is devoted to describing the current legal environment in recognition of the interests of the group at the Member State national and EU level for establishment of the object, subject, the objective and the novelty of the research, as well as the research question of the thesis. The first section of thesis is analysis of the regulatory framework of the recognition of the interests of the group at the EU level. The second section deals with member state practices in recognition of the interests of the group and determines whether there is legal fragmentation. The third section evaluates the effect of respective legal fragmentation on the well – functioning of the Internal Market. The fourth section investigates the rights of the EU to eliminate legal fragmentation, which hinders sound operating of the Internal Market.

A list of scientific papers published for the topic of the recognition of the interest of the group (approbation of research results) includes:

1. Losaks, G, Perkumienė, D. (2023). Recognition of group interest and its impact on creditor and minority shareholder protection/ Grupės interesų pripažinimas ir jo poveikis kreditorių ir smulkiųjų akcininkų apsaugai. Kaunas Forestry and Environmental Engineering University of Applied Sciences: Forestry and landscape management. Volume 22, issue 2. PP. 215 – 222. Available at: https://www.kmaik.lt/uploads/BIBLIOTEKA/MK/Mi%C5%A1kininkyst%C4%97_ir%20_krastotvarka_2023_2_(22)P.pdf

2. Losaks, G (2023). Legal Act for Recognising the Interest of the Group. Journal of Turiba University: *Acta Prosperitatis.* Volume 14, issue 1. PP. 112 – 122. https://doi.org/10.37804/1691-6077-2023-14-112-122

3. Lošaks, G. (2022). The regulation issues of a group of companies in Latvia/ Įmonių grupės Latvijoje reguliavimo klausimai. Kaunas Forestry and Environmental Engineering University of Applied Sciences: Forestry and landscape management. Volume 20, issue 1. Availabe at: https://www.kmaik.lt/uploads/BIBLIOTEKA/MK/Mi%C5%A1kininkyst%C4%97_ir%20_krastotvarka_2022_1_(20)P.pdf

4. Lošaks, G. Perkumienė, D. (2022). LATVIAN APPROACH OF RECOGNISING THE INTEREST OF THE GROUP. IS THERE A NEED FOR AMMENDMENTS? Zaporizhzhia National University in HUMANITIES STUDIES. PP. 146 – 152. https://doi.org/10.26661/hst-2022-11-88-15

5. Lošaks, G. (2022). The recognition of the interest of the group in Latvian Group of Companies Law. Journal of Turiba University: *Acta Prosperitatis,* Volume 13, issue 1. PP. 63-75. https://doi.org/10.37804/1691-6077-2022-13-63-75

Scientific papers presented at international conferences:

1. The presentation of "The definition of the group of companies in European Union" in the international scientific conference Contemporary legal problems and challenges in the context of international law 2024, in Lithuania, Vilnius, January 7, 2024.

2. The presentation of "Recognising the Interest of the Group at the European Union's Level" in the International Scientific Conference RELEVANT ISSUES OF ENVIRONMENT MANAGEMENT 2023, in Lithuania, Kaunas, on 27th and 28th April, 2023.

3. The presentation of "The Legal Act for Recognising the Interest of the Group" in the XXIV International Scientific conference CHANGE – THE BASIS OF A SUSTAINABLE SOCIETY, in Latvia, Riga, on 19th April, 2023.

4. The presentation of "The Concept of the Interest of the Group and Its Impact on the European Union Business Environment" in the 4th Edition of the International Conference on Tourism Research, under the theme of "Renewing Tourism in Post Crisis Times Between the Right to Travel and Sustainability" in Marrakech, Morocco on October 10th and 12th, 2022

5. The presentation of "The recognition of the interest of the group and its impact on creditor and minority shareholder protection" in Kazimieras Simonavicius University the 2nd International Conference "Problems and Challenges of Contemporary Law in the Context of International law" in Vilnius, Lithuania on 4th and 5th May, 2022.

6. The presentation of "The Regulation Issues of Group of Companies in Latvia" in the Kaunas Forestry and Environmental Engineering University of Applied Science International Scientific Conference "Relevant Issues of Environment Management" in Lithuania, Kaunas, on 2nd and 3rd May, 2022.

7. The presentation of "The recognition of the interest of the group in Latvian Group of companies law" in the Turiba University XXIII International Scientific Conference "Communication and Development of Interdisciplinary Competences in the Digital Age" in Latvia, Riga, on 20th and 21th April, 2022.

# 1. THE DEFINITION OF THE GROUP OF COMPANIES AT LEVEL OF THE EUROPEAN UNION

A company is a legal entity that is distinct from its members. In other words, a company has a separate legal personality from its shareholders. The legal entity is capable of enjoying rights and being subject to duties. This premise is described as a legal personality.[55] The development of companies acquiring ownership or shares in other legal entities paved the way for the emergence of groups of companies.[56]

According to the Treaty on the Functioning of the European Union (TFEU) Article 49, freedom of establishment includes the right to set up and manage companies by the law of the Member State, where such establishment is affected.[57] However, EU law refrains from establishing the definition of the group of companies in company law and the respective question has been left to Member States national law to regulate. It has led to a situation where the legal framework surrounding groups of companies is defined differently across the legal systems of various Member States. Even internationally recognised guidelines avoid laying out a uniform definition of a group companies.[58]

The group of companies can be set up as a new incorporation, joint venture, acquisition or merger. Further characterised by organisational structure – investments, ownership patterns, transactions, technical circumstances and territorial distance.[59] Relation to the group can mean application of the group's organisational and commercial policies, centralisation of liquidities etc. The membership in the group may as well posses' advantages such as financing, management and commercial support, name and credibility.[60] Furthermore, horizontal and vertical groups of companies can be distinguished.[61] In a horizontal group structure companies are linked by cross–shareholding, which means mutual participation in each other's capital.

[55] Davies, P. L. (2008). Gower and Davies' Principles of Modern Company Law. 8th edition. Sweet & Maxwell. P. 33.
[56] Blumberg, P. I. (1987). The law of corporate groups: tort, contract, and other common law problems in the substantive law of parent and subsidiary corporations. Boston: Little Brown. P. 55.
[57] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal of the European Union C 326.
[58] See e.g. The Declaration of International Investment and Multinational Enterprises. Adopted on 21 June 1976. Amended on 25 May 2011. Accessed 27 May 2024. Available at: https://legalinstruments.oecd.org/en/instruments/OECD-LEGAL-0144
[59] Blumberg, P. I. (1987). The law of corporate groups: tort, contract, and other common law problems in the substantive law of parent and subsidiary corporations. Boston: Little Brown. P. 55.
[60] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19
[61] Avgitidis, D. K. (1996). Groups of Companies, The Liability of the Parent Company for the Debts of its Subsidiary. Ant. N. Sakkoulas Publisher. PP. 70-71.

Hence, there is no superior company that coordinates group relations.[62] A defining characteristic of vertical group structure is the presence of a corporate group.[63]

The legal entity that controls other companies is called the parent company, while the former are called the subsidiaries.[64] It is argued that members of a group of companies have common economic interests and they create a single economic unit.[65] If autonomous legal entities create one enterprise (single economic unit), then in this latter case the subsidiaries can be under strict instructions from the parent company.[66] The interest of the autonomous legal entity is independent profitability and sustainability, but the interest of the group is financial well - being of an organisation. The parent company should not be treated as a "rational" investor with the sole purpose to reap the benefits of its investment. [67] This points to potential differences in concerns between the interest of the group and the interest of the subsidiary.

Substantive group matters at the EU level are codified in other fields, e.g., accounting, tax, competition, state aid, data protection, public procurement, employment, etc. The definition of the group of companies at the EU level can be found there as well. It is important to highlight that given definitions of the group of companies in other fields do not require Member States to apply it in national company law. The Court of Justice of the European Union (CJEU) upholding the right of freedom of establishment distinguishes that in a subsidiary a national of a Member State has a holding in the capital of a company, which gives certainty over the company's decisions and allows it to determine its activities.[68]

The International Accounting Standards Board (IASB) has published International Financial Reporting Standard (IFRS) 10 of Consolidated Financial Statements, which supersedes International Accounting Standard (IAS) 27 of Consolidated Financial Statements and Accounting for Investments in Subsidiaries. The IFRS 10 objective is to establish principles for consolidated financial statements. To meet the objective the control is also

[62] Dine, J. (2006). The Governance of Corporate Groups. Cambridge Studies in Corporate law. Cambridge University Press. P. 43.
[63] Andenas, M., Wooldridge F. (2009). European Comparative Company Law. 1st edition. Cambridge: Cambridge University Press. P. 448.
[64] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 195. https://doi.org/10.1515/ecfr-2013-0194
[65] Rehbinder, E. (1969). Konzernaußenrecht und allgemeines Privatrecht. Eine rechtsvergleichende Untersuchung nach deutschem und amerikanischem Recht. Berlin/Zürich, Verlag Gehlen. S. 23.
[66] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 195. https://doi.org/10.1515/ecfr-2013-0194
[67] Dine, J. (2006). The Governance of Corporate Groups. Cambridge Studies in Corporate law. Cambridge University Press. P. 43.
[68] Judgment of the Court (Fifth Chamber) of 13 April 2000 in the case C-251/98, C. Baars v Inspecteur der Belastingen Particulieren/Ondernemingen Gorinchem, paragraph 22.

defined. The parent company controls the subsidiary, if it has power, receives returns and provides a link between power and returns.[69]

A power arises from rights, i.e., it gives the ability to direct the relevant activities and affect returns. The purpose and the design of a company has great importance for determining the relevant activities, how decisions are made, who can direct them, who receives returns and exposure to the risk. The assessment of a power is a more complex process than merely counting voting rights for shareholding, e.g., contractual arrangements should be also taken into consideration. The power exists, even if it is not exercised, but directing relevant activities is not a conclusive factor to determine power. If a company determines another company's financing and operations, it can be concluded that there is a control. The IFRS 10 names relevant activities of operating and financing, but highlights that it is not an exhaustive list: 1) controlling financial assets; 2) selling, acquiring and/or disposing assets; 3) purchasing and/or selling services or goods; 4) organizing funding and determining a funding structure; 5) developing and/or researching process and products. Decisions about relevant activities are emphasized (not limited to) following: 1) establishing capital and operating decisions including budgeting; 2) appointment, termination and remuneration of management. To decide whether a company has rights sufficient to present power substantive rights should be distinguished from protective rights. For a right to be substantive, the holder must be able to exercise it effectively. Factors to be considered (not limited to): 1) financial penalties; 2) cost 3) terms and conditions; 3) ambiguity and vagueness of framework; 4) asymmetry of information; 5) operational barriers; 6) compliance and legal requirements; 7) joint or separate exercise of rights. Protective rights safeguard the interests of their holder without giving the power over the company those rights relate, e.g., a lender restricts the borrower from commencing activities that increase the risk, approval of capital expenditures, seizure of assets, if loan repayment conditions are not met. Often a company has a power over another company through voting, more precisely, holds more than half of voting rights. However, a company can hold majority voting rights, but can have no power, because it cannot direct relevant activities and determine operating and financing policies (rights are not substantive). Further, a company can have a power without majority voting rights through a contractual arrangement and the size of voting rights to compare to other shareholders. Contractual arrangement between shareholders can prescribe on how to vote, enabling the power to decide about the relevant activities. Also,

[69] The International Accounting Standards Board's International Financial Reporting Standard (IFRS) 10 of Consolidated Financial Statements. Adopted on 12 May 2011. Accessed 27 May 2024. Available at: https://www.ifrs.org/issued-standards/list-of-standards/ifrs-10-consolidated-financial-statements/#about

contractual arrangements can allow shareholders to direct relevant activities without voting. If shareholding is widely dispersed and the direction of relevant activities is determined by the majority, a company holding significantly more voting rights can have power, especially; if other shareholders are passive. Potential voting rights arising from substantive rights, e.g., convertible instruments or options, should also be taken into consideration. Voting rights are not the only source of shareholder power They can also leverage: 1) financing; 2) guarantees; 3) build upon their services or products; 4) licences and/or trademarks; 5) know how.[70]

The return of the parent company must depend on the subsidiary's performance for the purpose of establishing a control. The return can be not only positive, but also negative, as well as there can be downside risk and potential for upside.[71] The assessment should be made on how variable these returns are regardless of a legal form: 1) dividends or other economic distributions; 2) remuneration of services; fees, liabilities etc.; 3) other returns, which are not accessible to other shareholders. In order to check whether there is a link between power and returns it should be examined whether a company acts as an agent or a principal. Only the ultimate principal has power.[72]

The IFRS 10 is soft law, though it has been endorsed by the European Commission (EC)[73] and is basis for the notion of control in Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance (Accounting Directive).[74]

Article 2, paragraph 11 of the Accounting Directive states that the group is "a parent undertaking and all its subsidiary undertakings." The Accounting Directive Article 2 paragraph 9 provides that parent undertaking is "an undertaking which controls one or more subsidiary

[70] Ibid.
[71] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97. P. 9. http://dx.doi.org/10.2139/ssrn.1115737
[72] Ibid.
[73] Commission Regulation (EU) No 1254/2012 of 11 December 2012 amending Regulation (EC) No 1126/2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Financial Reporting Standard 10, International Financial Reporting Standard 11, International Financial Reporting Standard 12, International Accounting Standard 27 (2011), and International Accounting Standard 28 (2011) (Text with EEA relevance). Adopted on 29 December 2012. Published in the Official Journal of the European Union L 360/1. Repealed on 15 October 2023.
[74] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.

undertakings." The Accounting Directive Article 2 paragraph 10 determines that subsidiary undertaking is "an undertaking controlled by a parent undertaking, including any subsidiary undertaking of an ultimate parent undertaking." The Accounting Directive considers the group of companies as if they were one single enterprise. The control is defined in Article 22 of the Accounting Directive if one of the following conditions are met: 1) majority voting rights; 2) appointment or removal of majority of administrative, management or supervisory board; 3) dominant influence based on a contract or articles of association.[75] The same concept has been applied for defining "controlled undertaking" in Article 2, paragraph 1, subparagraph f of Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (Transparency Directive),[76] "controlling undertaking" in Article 3 of Directive 2009/38/EC of the European Parliament and of the Council of 6 May 2009 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees (Recast) (Text with EEA relevance) (Directive on European Works Council),[77] as well as for "single undertaking" in Article 2, paragraph 2 of COMMISSION REGULATION (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to *de minimis* aid (Text with EEA relevance) (de minimis Regulation).[78] Noteworthy is that Article 48 of the Preamble (controllers right to transmitting personal data within the group of companies) and Article 37, paragraph 2 (single data protection officer for whole group) of REGULATION (EU) 2016/679 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 April 2016 on the protection

[75] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.

[76] Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC. Latest Amendments on 5 January 2023. Adopted on 31 December 2004. Published in the Official Journal of the European Union L390/38.

[77] Directive 2009/38/EC of the European Parliament and of the Council of 6 May 2009 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees (Recast) (Text with EEA relevance). Adopted on 16 May 2009. Latest Amendments on 9 October 2015. Published in the Official Journal of the European Union L 122/28.

[78] Commission Regulation (EU) No 1407/2013 of 18 December 2013 on the application of Articles 107 and 108 of the Treaty on the Functioning of the European Union to de minimis aid Text with EEA relevance. Adopted on 24 December 2013. Last amendments on 27 July 2020. Published in the Official Journal of the European Union L 352/1.

of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (Text with EEA relevance) establishes group privilege, which is characterised by a pursuit of the interest of the group.[79]

In the EU competition law, the CJEU interpreting Article 101 and 102 of the TFEU has concluded that used term "undertaking" covers also a group of companies (regardless of legal status and financing)[80] and they should be treated as a single undertaking, since an economic entity is created, in which members of the group (subsidiaries) have no autonomy to install their own market policies.[81] The term of an undertaking in EU competition law is a broader term in comparison to "legal personality" in civil law. The group of companies are considered as a single economic entity, if one company is controlled by another company or several companies are controlled by the same company or person. However, it is not sufficient that a control exist; it must be in fact be actively exercised. Affected market conduct and determination of commercial policy (encompasses numerous business activities) is strong indications of the control rather than involvement in day-to-day management of a company or issuing of specific instructions.[82] There is a presumption that control is exercised, if a company directly or indirectly holds all or nearly all shares of a company.[83] The presumption of the control cannot be rebutted merely by the fact that the parent company has not held a general meeting or board of directors meeting or taken any other formal decision, which impacts a subsidiary because control can be also exercised informally.[84] If the parent company holds 51% of shares in a subsidiary, they should be considered as a single economic entity.[85] The presumption can be rebutted if: 1) the parent holds shares in a subsidiary temporarily (for a short period of time); 2) the parent company is legally prevented from exercising the control;

[79] Regulation (EU) 2016/679 of the EUROPEAN Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (Text with EEA relevance). Adopted on 4 May 2016. Published in the Official Journal of the European Union L 119/1.
[80] Judgment of the Court (Sixth Chamber) of 23 April 1991 in the case C-41/90, Klaus Höfner and Fritz Elser v Macrotron GmbH, paragraph 21.
[81] Judgment of the Court (Sixth Chamber) of 24 October 1996 in the case C-73/95 P, Viho Europe BV v Commission of the European Communities, paragraph 51.
[82] Judgment of the General Court (Second Chamber) of 12 July 2011 in the case T-132/07, Fuji Electric Co. Ltd (anciennement Fuji Electric Holdings Co. Ltd) v European Commission, paragraphs 182 – 183.
[83] Judgment of the Court (Third Chamber) of 10 September 2009 in the case C-97/08 P, Akzo Nobel NV v Commission of the European Communities, paragraph 60.
[84] Judgment of the Court (Third Chamber) of 11 July 2013 in the case C-440/11 P, European Commission v Stichting Administratiekantoor Portielje and Gosselin Group NV, paragraph 109.
[85] Judgment of the Court of 6 March 1974 in joined cases 6 and 7-73, Istituto Chemioterapico Italiano S.p.A. and Commercial Solvents Corporation v Commission of the European Communities, paragraph 6.

3) the parent company is an investment company, which acts purely as investor.[86] Beyond the presumption, control can be also indicated by decisions made in a company, which prompt other companies in a group, and legal, economic and organisational links between companies,[87] e.g., an overlap of management between companies,[88] group policy, [89] pursuit of a single economic goal.[90] Minority shareholding by itself does not exclude a control because these shares can be allied to rights greater than those normally granted to minority shareholders and formation of legal, economic or organisational links between companies.[91] The purpose for introducing the doctrine of single economic entity is imposition of joint and several liability.

In the EU tax law, each company is recognised as a separate tax subject, but in some cases for group of companies the CJEU has derogated from this. For determining the place of taxation of service of value added tax (VAT) fundamental criterion is consideration of the economic relationship between companies. If a subsidiary is wholly owned by a parent company and various contractual obligations are imposed, it shows that the subsidiary acts as an "auxiliary organ of its parent."[92] The CJEU has established, in a previous case, that while belonging to the same group is not a sole indicator, it can be one element that suggests a potential abuse of the VAT framework in closely connected transactions between companies.[93] Article 3, paragraph 1 of Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) (Insolvency Regulation) prescribes that international jurisdiction of insolvency proceedings is established by the concept of the centre of main interests, which shall be the place where the company's registered office is located, if the presumption is not rebutted.[94] The CJEU has stated that the presumption cannot

[86] Opinion of Advocate General Kokott delivered on 23 April 2009 in the case C-97/08 P, Akzo Nobel NV and Others v Commission of the European Communities, paragraph 75.
[87] Judgment of the Court (Third Chamber) of 10 September 2009 in the case C-97/08 P, Akzo Nobel NV v Commission of the European Communities, paragraph 58.
[88] Judgment of the Court (Second Chamber) of 16 December 2010 in the case C-480/09 P, AceaElectrabel Produzione SpA v European Commission, paragraph 51.
[89] Judgment of the Court (Fifth Chamber) of 18 July 2013 in the case C-501/11 P, Schindler Holding Ltd and Others v European Commission, paragraphs 113 and 114.
[90] Judgment of the Court of First Instance (First Chamber) of 17 December 1991 in the case T-6/89, Enichem Anic SpA v Commission of the European Communities, paragraph 235.
[91] Judgment of the General Court (Second Chamber) of 12 July 2011 in the case T-132/07, Fuji Electric Co. Ltd (anciennement Fuji Electric Holdings Co. Ltd) v European Commission, paragraphs 182 and 183.
[92] Judgment of the Court (Fifth Chamber) of 20 February 1997 in the case C-260/95, Commissioners of Customs and Excise v DFDS A/S, paragraphs 23 and 26.
[93] Judgment of the Court (Second Chamber) of 21 February 2008 in the case C-425/06, Ministero dell'Economia e delle Finanze v Part Service Srl., paragraphs 51 and 57.
[94] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast). Adopted on 5 June 2015. Published in the Official Journal of the European Union. L 141/19.

be rebutted only based solely on the fact that the company is controlled by another company.[95] Furthermore, neither intermixing of assets nor financial accounts are neither sufficient to rebut the presumption.[96] In the EU insolvency law in the setting of group of companies a factor of appearance to third parties prevails over that of single economic entity. It is important to highlight that the control over a company is not particularly visible to third parties.

In the EU public procurement law the CJEU has ruled that a group of companies can have various forms and objectives, which *per se* does not stipulate that a subsidiary does not enjoy autonomy and independence to set their economic activities and commercial policy, inter alia, in the area of receiving of public contract. Furthermore, merely determining control by evaluating ownership or voting rights does not automatically stipulate coordinated competitive conduct of a group of companies in the public procurement procedure.[97] In transfer of undertaking in labour law the CJEU considers even fully integrated groups of companies to be distinct legal persons.[98] The competition law doctrine of a single economic entity is not applied in labour law for transfer of undertakings because it would mean that a group of companies are acknowledged as one employer and it would limit the scope of the Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses (The Transfer of Undertaking Directive).[99] For determination of self-employed commercial agents' compensation in a case of termination of the agency contract the CJEU found that for the legal certainty and security of commercial transactions group of companies under Article 17 of Council Directive 86/653/EEC of 18 December 1986 on the coordination of the laws of the Member States relating to self-employed commercial agents should not be treated as single economic entity.[100] Jurisdiction for being sued in cross-border cases is regulated by 1968 Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters (Convention of Jurisdiction). Under

[95] Judgment of the Court (Grand Chamber) of 2 May 2006 in the case C - 341/04, Eurofood IFSC Ltd. (Eurofood case), paragraph 36.
[96] Judgment of the Court (First Chamber) of 15 December 2011 in the case C-191/10, Rastelli Davide e C. Snc v Jean-Charles Hidoux, paragraphs 37 – 38.
[97] Judgment of the Court (Fourth Chamber) of 19 May 2009 in the case C-538/07, Assitur Srl v Camera di Commercio, Industria, Artigianato e Agricoltura di Milano, paragraphs 31 and 32.
[98] Judgment of the Court (Fifth Chamber) of 2 December 1999 in the case C-234/98, G. C. Allen and Others v Amalgamated Construction Co. Ltd, paragraph 17.
[99] Council Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses. Adopted on 11 April 2001. Last amendments on 9 October 2015. Published in the Official Journal of the European Union L 263.
[100] Judgment of the Court (First Chamber) of 26 March 2009 in the case C-348/07, Turgay Semen v Deutsche Tamoil GmbH, paragraph 31.

Article 5, paragraph 5 of Convention of Jurisdiction enables suing a company in a country where it has a branch, agency or other establishments.[101] A subsidiary as an independent company is out of the scope of Article 5, paragraph 5 of Convention of Jurisdiction. However, the CJEU has stated that, although from the perspective of company law a subsidiary and a parent company are independent from each other, the same name and the same management creates the appearance that business is done with a branch, agency or other dependent establishment, which is merely an extension of another company[102], therefore, Article 5, paragraph 5 of Convention of Jurisdiction could be applied also to a subsidiary and a parent company. However, the CJEU has also noted that a loss of a subsidiary can be only an indirect consequences for losses suffered by a parent company, therefore, is not closely linked to a place of a dispute and is out of the scope of the purpose of Article 5, paragraph 3 of Convention of Jurisdiction.[103]

Still, in company law, the traditional separate legal personality approach prevails. However, the separate legal personality approach has been critiqued for bearing no resemblance to economic reality.[104] Based on the doctrine of separate legal personalities, assets and liabilities of the group of companies are compartmentalised, but the mind of a board of directors cannot be compartmentalised in this way.[105] In the light of all the foregoing, at the EU level predominantly the concept of the control stipulated in the Accounting Directive is used. Further, the competition law's single economic entity doctrine has a functional approach, which targets economic identity by piercing its doctrine of separate legal personalities, more precisely, assesses comprehensively the impact of the parent company's control of a subsidiary's market conduct. From CJEU case law it can be concluded that the competition law's single economic entity doctrine can be applied interdisciplinarily, if it is compatible with legal frameworks' purpose and aim.

[101] 1968 Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters. Adopted on 1 February 1973. Published in the Official Journal L 299, 31/12/1972 P. 0032 – 0042.
[102] Judgment of the Court (Sixth Chamber) of 9 December 1987 in the case 218/86, SAR Schotte GmbH v Parfums Rothschild SARL, paragraph 15.
[103] Judgment of the Court (Sixth Chamber) of 11 January 1990 in the case C-220/88, Dumez France SA and Tracoba SARL v Hessische Landesbank and others, paragraph 14.
[104] Blumberg, P. I. (2001). Accountability of multinational corporations: the barriers presented by concepts of the corporate juridical entities. Hastings International and Comparative Law Review. Volume 24, issue 3. P. 301.
[105] Busch, D., Macgregor, L., Watts P. (2016). Agency Law in Commercial Practice. Oxford University Press. P. 219.

## 2. THE RECOGNITION OF THE INTEREST OF THE GROUP AT THE NATIONAL LEVEL OF THE MEMBER STATES

In the 1970s the European Commission (EC) proposed 3 significant attempts for regulating the group of companies. The first attempt in 1972 was the proposed fifth directive on company law to govern joint – stock corporations. In 2001 the proposal was withdrawn.[106] The second attempt in 1974 was a draft for a ninth company law directive based on the German model. The ninth company law directive proposed an autonomous body of law specifically dealing with a group of companies. In the 1980s the ninth company law directive was dropped due to the lack of support.[107] It was challenged that the ninth company law directive was out of the scope of removal of restrictions of the freedom of establishment,[108] as well as there was no apparent necessity to harmonise group law[109] and it was not clear on which principles legal acts should be based.[110] Furthermore, it was argued that German law for a group of companies was too rigid and not particularly effective.[111] The third attempt was to implement a chapter pertaining to of a group of companies in a Regulation of *SE*, but was also dropped in the 1980s.[112] Instead in 1983 the Directive on consolidated accounts was adopted.[113] Member States' company laws are left to deal with recognition of the interests of the group at national level.

In 2008 the EC again attempted to regulate groups of companies. The EC undertook the task to reach a compromise on the European Private Company (*Societas Privata Europaea*) as the "European" private limited liability company that can be suitable for establishing a cross-

[106] Proposal for a Fifth Directive on the Coordination of Safeguards which for the Protection of the Interests of Members and Outsiders, are Required by Member States of Companies within the Meaning of Articles 59, second paragraph, with respect to Company Structure and the power and responsibilities of Company Boards. Submitted by the European Commission to the Council on 9 October 1972. Accessed 27 May 2024. Available at: https://op.europa.eu/en/publication-detail/-/publication/e626eaef-4c67-4f34-992f-5191cf8c682b/language-en

[107] Draft Proposal for a Ninth Council Directive pursuant to Article 54(3)(g) of the EEC Treaty relating to links between undertakings and in particular on groups. Accessed 27 May 2024. Available at: https://www.mhc.ie/uploads/9th_proposal.pdf

[108] Lutter, M. (1979). Europisches Gesellschaftsrecht. Sonderheft I der *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. S. 6.

[109] Immenga, U. (1978). Konzernverfassung ipso facto oder durch Vertrag? – Zum Stand der Konzernrechts-diskussion in der Europäischen Gemeinschaft. *Europarecht.* S. 242.

[110] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. Journal of Comparative Business and Capital Market Law. Volume 6. P. 164.

[111] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 196. https://doi.org/10.1515/ecfr-2013-0194

[112] Proposal for a Council Regulation embodying a Statute for the European Company (COM/70/600/FINAL). Submitted to the Council on 30 June 1970.

[113] Seventh Council Directive 83/349/EEC of 13 June 1983 based on Article 54(3)(g) of the Treaty on consolidated accounts. Adopted on 29 June 1983. Published in the Official Journal of the European Union L 193.

border subsidiary. In 2012 the EC started to doubt the possibility of reaching the agreement on *Societas Privata Europaea* (SPE) regulation.[114] In 2013 the *SPE* project was dropped[115] and as an alternative the *Societas Unius Personae* (*SUP*) Directive was proposed, which remains in legislative process. Article 23 of the *SUP* Directive proposal implies that the parent company has the right to give instructions to its subsidiary's management body under the *SUP* framework. However, the precondition for exercising this respective right is that the parent company in a subsidiary is single-member (shareholder). [116] Moreover, issuing instructions is not established as the supranational right, therefore, it is restricted to applicable Member State's national law. Lastly, the scope of application is not defined because Article 22 paragraph 7 of the SUP Directive proposal determines that the parent company, if it gives directions or instructions, which the subsidiary is accustomed to follow, shall be considered a director of the respective subsidiary.[117] It raises a concern whether under the *SUP* framework the parent company will become automatically become a shadow director and liable for all subsidiary's debts and conducts of misbehaviour.

### 2.1. The definition of a group of companies

French commercial code (*Code de commerce*) merely defines that a subsidiary is a company, in which more than 50 % capital is owned by another company, as provided by Article L. 233-1 *Code de commerce*). Capital ownership between 10 % up to 50 % is called a holding, instituted by Article L. 233-2 *Code de commerce*. A holding company can become a controlling company under certain conditions. Article L. 233-3 *Code de commerce* ascertain**s** that **a** company controls another company: if it has directly or indirectly a majority of the voting rights in the general meeting; by virtue of an agreement holds a majority voting rights; when it effectively determines the decisions taken at the general meeting (through voting rights); possesses the power to appoint or dismiss the majority of management or supervisory bodies.

[114] European Commission. (2012). Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee of the Regions. (2012). Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies. COM(2012) 740 final. P. 13. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=celex%3A52012DC0740

[115] European Commission. (2013). Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee of the Regions. Regulatory Fitness and Performance (REFIT): Results and Next Steps. COM(2013) 685 final. P. 9. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52013DC0685&from=EN

[116] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

[117] Ibid.

Furthermore, in Article L. 234-3 *Code de commerce* it is inferred that an indirect holding is considered to exist, if any capital is held by the controlling company (even if it is less than 10 %).[118] In 1986 – 1987 a series of cases questioned the validity of the group of companies' structure. The court clarified that French law does not prohibit the group of companies' structure and the parent company's role is to exercise control over the subsidiary. The right of vote has not been infringed because it is clear that shareholders have been participating in the company according to the amount of shares held.[119] Moreover, a management contract, in which a company voluntarily transfers its management to another company, is generally disallowed, but voting rights can be assigned to another person.[120]

Civil Code of Netherlands (*Burgerlijk Wetboek*) Book 2 defines the term subsidiary, group, participation and dependent company. Article 2:24a of *Burgerlijk Wetboek* (*BW*) provides that a subsidiary (*dochtermaatschappij*) is a legal person, in which another legal person: can exercise more than 50 % of the voting rights at general meeting; can remove or appoint more than 50 % of officers, directors or supervisory board members. The right to vote or remove or appoint officers, directors or supervisory board members can be exercised through other subsidiaries or by virtue of an agreement. The bar of 50 % of removal or appointment of officers, directors or supervisory board members is calculated as, if all entitled persons casted their vote. Article 2.24b of *BW* institutes that a group of companies (*groep*) is an economic unit. Legal persons and partnerships are united in one group.[121] Centralised management with the meaning of majority control construes a group, but an equity interest does not automatically impute a group structure. In a participation of 50 % or minority participation a group can be established, if power of decision-making exists. A company can be a member of a group in more than one group.[122] According to Article 2:24c of *BW*, participating interest (*deelneming*) means contribution (provided or have caused) of capital in a legal person for the purpose of interconnection for a long – lasting period of time for furthering their own activities. Contribution of 20 % or more of issued share capital is presumed to be participation. Also the

[118] Code de commerce. Dernière modification le 26 février 2022. Document généré le 25 février 2022. Legifrance. English translation of cited Articles: Raworth P. (2006). The French Commercial Code in English. Oxford University Press. P. 242.
[119] Cour de Cassation, Chambre commerciale, du 24 février 1987, 86-14.951. Publié au bulletin.
[120] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. PP. 155 – 156.
[121] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P. 184.
[122] Schuit, S. R., Bier B., Verburg L. G., Wisch J. A. T. (2002). Corporate Law and Practice of the Netherlands. Kluwar Law International. P. 58.

participation interest is present if: a company is fully liable for its partner's debts; is otherwise a partner for a long–lasting period of time with for its own business support. Participation can be carried out through a legal person or partnership, for their own account and either jointly or solely. The dependent company (*afhankelijke maatschappij*) in Article 2 of *BW* and Article 2:262, paragraph 3 (a) of *BW* is determined as legal person that contributes at least 50 % of capital or partnership that is registered in Commercial Register fully liable towards a partner's third parties or partnership. A legal person can establish another company's dependency also through their dependent companies, for their own account and jointly or solely.[123]

In Italy Article 2359 of *Codice Civile* defines controlled and affiliated companies. The controlled companies are considered, be when another company: has majority of the votes at a regular meeting; has sufficient votes that provide a dominant influence; by virtue of contractual bonds has a dominant influence. Voting can be exercised also through fiduciary companies and interposed persons. Affiliated companies are identified as a company, in which another company has a considerable influence. Considerable influence is presumed when at least 20 % of the votes in a regular meeting belong to another company. If a company has shares listed on a stock exchange, then considerable influence is presumed at 10 % of votes. [124] Controlled and affiliated companies and companies, which have influence over them, create the latter of the subsidiary and the parent company. The 2004 Company law Reform did not provide definition of a group of companies.[125] Nor did it require a group of companies to be formed by a contract or another legal act.[126] It only regulates some relevant aspects of the group of companies. The concept of the group as a new and different entity is rejected. It is understood to be an approach for forming a single economic unity between a group of companies.[127] Italian group law enables only operations of a single economic unit through separate legal personalities. Thereupon it should not be mistaken with a single economic unit, which creates one enterprise. A group of

[123] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. PP. 185, 258 and 308.

[124] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942). English translation of cited Article:
Beltramo, M. (1996). The Italian Civil Code. Ocean Publications Inc. P. 86.

[125] OECD. (2020). Overview of the Legal/Regulatory Framework with Respect to the Duties and Responsibilities of Boards in Company Groups. Corporate Governance. https://doi.org/10.1787/55ea4b91-en

[126] Fasciani, P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, issue 2. Volume 4, issue 2. P. 202. https://doi.org/10.1515/ECFR.2007.013

[127] Montalenti, P. (2011). Direzione e coordinamento nei gruppi societari: i principi e problemi, in Società per azioni, corporate governance e gruppi finanziari. Milano. P. 234.

companies is set of legally connected companies, but economically and technically separated structures, which are directed and coordinated in pursuit of the interest of the group.[128]

In Germany *AktG,* a group of companies consists of dominant and dependent companies. The dominant company participates in the dependent company together with other economic interests that may prejudice the dependent company. A dependent company has separate assets and is an independent legal person.[129] The regulatory perspective in Germany is the commencement of welfare of the dependent company.[130] A dominant and a dependent company create the latter of a parent and a subsidiary company. Articles 15-19 of *AktG* define different types of formations of parent and subsidiary companies – majority participation (Article 16 of *AktG*), control (Article 17 of *AktG*), common management (Article 18 of *AktG*) and cross-shareholding (Article 19 of *AktG* ).[131] Majority participation in Article 16 of *AktG* is exercised by majority ownership or majority voting rights. Majority participation and control establish presumption of a subsidiaries' dependency on a parent company. Article 18 of *AktG* is concerned with subordination and coordination. Subordination is based on the dependency, while coordination does not rely on dependency, even though common control can be identified.[132] The concept of dependency between a subsidiary and a parent company is the key element of *Konzernrecht* for *AG*.[133] Further, a group of companies is classified as a formal or an informal group. A formal group consists of a contractual group (*Vertragskonzerne*) Articles 291 – 310 of *AktG* and the integrated entities (*Eingliederung*) Articles 319 – 327 of AktG. The informal groups (*Faktische Konzerne*) or *de facto* groups are regulated in Articles 311 – 318 of *AktG*.[134]

Governance of contractual groups is based on the assumption that in such structure the subsidiary cannot operate solely for its own benefit. In line with *AktG,* a contractual group is found only, if the subsidiary is *AG*. The parent company can be registered abroad and the legal

[128] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. PP. 123 -124. https://doi.org/10.54648/eucl2019018

[129] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 32 und 34.

[130] Wiedemann, H. (2021). The German Experience with the Law of Affiliated Enterprises. *Groups of companies in European Laws*. Volume 2. De Gruyter. P. 22. https://doi.org/10.1515/9783110902167-004

[131] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[132] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. Kluwer Law International. P. 49.

[133] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 40.

[134] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

status has no meaning.[135] According to Article 291 of *AktG*, the contractual group is formed by the control agreement (*Beherrschungsvertrag)* or the profit and loss absorption agreement (*Gewinnabführungsvertrag*).[136] With the control agreement another company performs *AG's* management. With the profit and loss absorption agreement all profits of the *AG* are transferred to another company. Respective agreements were introduced in *Konzernrecht* because they were commonly used in practice.[137] Article 292 of *AktG* enact that the contractual group is constructed by the profit pool agreement (*Gewinngemeinschaft*), the partial absorption of profit and loss agreement (*Teilgewinnabführungsvertrag*) and the company lease agreement (*Betriebspachtvertrag*)/ the company surrender agreement (Betriebsüberlassungsvertrag).[138] With the pool agreement the *AG* enters into an obligation to distribute pooled profits. With the partial absorption of profit and loss agreement, the *AG* enters into an obligation to partially transfer its profits to other company. With the company lease agreement, the company surrenders the agreement, the *AG* leases or surrenders its operations to another company. Contractual agreements have to be: 1) written (Article 293, paragraph 3 of *AktG);* 2) accepted in general meeting by three – quarters of the share capital represented, if the articles of association do not stipulate a higher majority ratio of capital (Article 293, paragraph 1 of *AktG*); 3) entry in the Commercial Register of the existence and the nature of the agreement (Article 294 of *AktG).*[139] Agreements of Article 291 of *AktG* are considered to bring both legal and economical structural changes, but agreements of Article 292 of *AktG* bring only economic structural change.[140]

The integration of a company comes "near to a merger." Companies become a single economic unit. However, both companies retain legal independence.[141] Stock companies can be integrated into some other stock corporation that has a seat in Germany (principal company). The principal and integrated companies create the latter of a parent and subsidiary companies.

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[135] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. Kluwer Law International. P. 50.
[136] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[137] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 166.
[138] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[139] Ibid.
[140] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. S. 236-238.
[141] Ibid. P. 51.

It means that the *AG* subsidiary can be integrated into the *AG* parent company. The issue of integration is decided in the general meeting of a stock company, which will be integrated. The subsidiary can be integrated, if the parent company holds all shares or 95 %. Integration of wholly owned stock companies is described in Article 319 of AktG and 95 % owned stock companies in Article 320 of AktG.

A subsidiary's dependency on a parent company can also be established also without contractual agreements or integration. The ability to steer the group is supposed to be an attractive incentive for the parent company to form a contractual group. Yet this anticipation turned out to be vain. The contractual groups are rare. The *de facto* group structure is organised in accordance with general notion of Article 17 of *AktG* (indirectly or directly exerts a controlling influence).

*GmbH* can be a member of a legally binding contractual group (formal group) in spite of absence of statutory rules.[142] The parent company is entitled to similar control and power over the *GmbH* subsidiary as provisions of *AktG* provided by virtue of the agreement and the board of directors subject to the directions of shareholders. The conclusion of the control agreement or the profit or loss absorption agreement with the *GmbH* subsidiary may be useful for the intent to prioritize the interest of the group or tax benefits.[143] In the case law, it is settled that *AktG* rules for *AG* contractual groups are applicable also to *GmbH* in an analogous matter.[144]

In Portugal the group of companies' relationship is systematized under the concept of affiliated companies (*sociedades coligadas*). Based on the Article 481 of *CSC sociedades coligadas* can be applied only to limited liability companies - private limited liability companies (*sociedades por quota*), public limited liability companies (*sociedades anónimas*), and limited liability partnerships by shares (*sociedade em comandita por acções*).[145] Other forms of companies are excluded from the scope of *sociedades coligadas*. Antunes outlines that *sociedades coligadas* "is a strict legal concept, not a factual one." Further, its function is "general legal term of reference" for the rules of a group of companies, whose application is limited to *CSC* prescribed relationships. On the one hand, the purpose of limiting the scope is to enhance judiciary certainty, on the other hand, it creates a regulatory gap. Contrary to

[142] Alting, C. (1994). Piercing the Corporate Veil in American and German Law - Liability of Individuals and Entities: A Comparative View. *Tulsa Journal Comparative and International Law*. Volume 2, article 4. P. 237.
[143] Lennarts, M. L. (1999). *Concernaansprakelijkheid*. Deventer. Kluwer Law. P. 74-75.
[144] Ulmer, P. (1986). Gläubigerschutz im 'qualifizierten' faktischen GmbH-Konzern. Bemerkungen zum 'Autokran'- Urteil des BGH vom 16.9.1985. *Neue Juristische Wochenschrift (NJW)*. S. 1580.
[145] Ibid.

Germany (*AktG*), where only one company has to be in prescribed legal form, *CSC* group law can be applied only, if all concerned companies are in Article 481 of *CSC* mentioned legal structures. Limited scope is vastly criticised because of practical inefficiency, since group law can be easily avoided by arranging for one of the group members to fall out of the scope of Article 481 of *CSC.*[146]

*CSC* does not provide a definition of *sociedades coligadas,* but right away describes 4 types of relationships that can be formed – simple participation, mutual participation, domination and relationship of a group, according to Article 482 of *CSC*.[147] *CSC* establishes the "dualistic approach"[148] of Germany (*AktG*), where distinction is made between contractual (formal) group and a factual (informal or *de facto*) group. Antunes argues that *CSC* regulations on autonomy and control are "artificial oversimplification" because it does not take into account the "hybrid" (very flexible governance structure) nature of the group.[149]

Article 483 of *CSC* provides that a simple participation (*sociedades em relação de simples participação*) exists when a company holds at least 10 % of the shares of another company and other types of relationship provided in Article 482 of *CSC* are not formed between the companies. Further, Article 485 of *CSC* determines that a mutual participation or reciprocal shareholding (*sociedades em relação de participações recíprocas*) exists when companies are in cross holding of at least at 10 % of each other shares.[150] In small equity participation, normally the parent company behaves like a "rational investor" by maximizing capital return. Passing 10 % of equity participation is perceived as an attempt to gain control, therefore, should be separately regulated. Equity participation only up to 50 % is relevant for simple or mutual participation because for majority participation, rules of relationship of domination are applicable. The concern is whether a subsidiary's self - participation (shares or part held by the subsidiary as its own capital) should be deducted from the nominal amount of

[146] Engrácia, Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. PP. 4 and 11.
[147] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[148] The concept of dualistic approach: Wiedemann, H. (1982). The German Experience with the Law of Affiliated Enterprises. Volume 2. Groups of Companies in European laws / Les groupes de sociétés en droit européen. P. 33. https://doi.org/10.1515/9783110902167
[149] Engrácia, Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review (ECFR)*. Volume 2, Issue 3. PP. 375 and 377. https://doi.org/10.1515/ecfr.2005.2.3.323
[150] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

shares (this problem is significant in all types of equity holdings). In the literature, there is understanding that self – participation should not be deducted from nominal capital prevails.[151]

A relationship of domination (*sociedades em relação de domínio*) exists when one company can exercise directly or indirectly a dominant influence over another company. According to Article 486 of *CSC*, the domination is presumed in the case of direct or indirect holding of a majority of shares, of a majority of voting rights and the right to appoint the majority of the management board or supervisory board.[152] Portuguese concept of domination is similar to Italian dominant influence (Article 2359 of *Codice Civile)*[153] and German controlling influence (Article 17 of *AktG*).[154] A domination can be set up through a diversity of mechanisms and can assume various forms and degrees of intensity.[155]

There is no definition in *CSC* of what is a group of companies,[156] yet there is provision for creation and organisation of a group by the total domination (*domínio total inicial*) in Articles 488 – 491 of *CSC*, by the contract of a horizontal group (*regime do contrato*) in Article 492 of *CSC* and by the contract of subordination in Articles 493 – 508 of *CSC*.[157] *CSC'*s total domination is similar to German integration (Article 319 of *AktG*).[158] In Portugal the majority of groups are formed via total domination.[159] Total domination occurs when 100 % of shares are held and this group can be created in two ways: with the sole shareholder (Article 270 – A of *CSC* and Article 488 of *CSC*); by acquiring shares (Article 489 of *CSC*). The difference from German integration (Article 319 of *AktG*) is that according to Article 490 of *CSC* a company owning 90 % or more of shares of another company has the duty to acquire remaining shares or parts.[160] There are no specific rules on management and organisation of horizontal groups

[151] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. PP. 14-16.
[152] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[153] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942). English translation of cited Article: Beltramo, M. (1996). The Italian Civil Code. Ocean Publications Inc. P. 86.
[154] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[155] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 23.
[156] Manóvi, R. M. (2020). Groups of Companies: A Comparative Law Overview. Ius Comparatum - Global Studies in Comparative Law. Springer. P. 80.
[157] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[158] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 30.
[159] Manóvi, R. M. (2020). Groups of Companies: A Comparative Law Overview. Ius Comparatum - Global Studies in Comparative Law. Springer. P. 80.
[160] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

because Article 492 of *CSC* provides merely essential elements of this specific type of contract. Instituted by Article 493, paragraph 1 of the *CSC* based on the subordination contract the parent company has a broad legal power of direction over the subsidiary's management. Furthermore, the profit transfer contract (*contrato de transferência de lucros*) outlined in Article 508 of *CSC* can be concluded, if a subordination contract exists. [161] Other contracts are not regulated in *CSC*, which is opposite from German law (Article 292 of *AktG)*.[162]

In Latvia Article 2, paragraph 1 of *Koncernu likums* defines a group of companies as a dominant undertaking and one or more dependent companies.[163] A dominant undertaking with dependent companies creates the respective of parent and subsidiary companies. It is important to highlight Article 1, subparagraph 8 of *Koncernu likums,* which provides that under the scope of *Koncernu likums* an undertaking can be any type of commercial or capital company and a natural person.[164] A capital company or commercial company is a private limited liability company or a stock company determined by Article 134 of *Komerclikums.*[165] Hence, *Koncernu likums* applicability compared to German model (*AktG*) is extended to private limited liability companies and natural persons. A parent company (a dominant company) is a company with the decisive influence over one or more companies (Article 2, paragraph 2 of *Koncernu likums*) and a subsidiary (a dependent company) is a company under the decisive influence (Article 2, paragraph 3 of *Koncernu likums*).[166] Moreover, the subsidiary can be under the decisive influence of multiple companies (Article 2, paragraph 3 of *Koncernu likums*) and *Koncernu likums* is not applicable, if a natural person holds all stock or shares of a company (Article 2, paragraph 4 of *Koncernu likums),* as well as in the case of mutual participation the decisive influence can be also present (Article 5 of *Koncernu likums*).[167]

According to Article 3, decisive influence is established by a group of companies' contract or participation. A group of companies contract is a management contract, a transfer

[161] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. Pp. 27-28 and 30.
[162] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[163] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[164] Ibid.
[165] Komerclikums. Pieņemts 13.04.2000. Stājies spēkā 01.01.2002. Publicēts: Latvijas Vēstnesis, 158/160, 04.05.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 11, 01.06.2000. Pēdējie grozījumi 01.08.2023.
[166] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[167] Ibid.

of profit contract or both contracts included in one (a management and transfer of profit contract). The management contract (*pārvaldes līgums*) determines that a company subjects its management to another company and shall be entered into writing. The transfer of profit contract (*peļņas nodošanas līgums*) determines that all or part of profits is transferred to another company and shall be entered into writing.[168] Article 291 of German *AktG* (the control agreement and the profit or loss absorption agreement)[169] has been conveyed as a group of companies' contracts described in Article 3, paragraph 2 of *Koncernu likums.*[170] Article 292 of German *AktG* (other inter – company agreements) of agreements of profit pooling and the company lease or surrender has not been transposed in *Koncernu likums,* exception is Article 292 of German *AktG* of partial absorption of profit or loss agreement because a transfer of profit contract in Article 3, paragraph 2 of *Koncernu likums* covers it.[171] A participation in Article 3, paragraph 3 of *Koncernu likums* should not be interpreted as simple participation as in Portuguese group law (Article 483 of *CSC*)[172] or as a participation under Dutch group law provisions (Article 2:24c of *BW*),[173] but rather as German majority participation (Article 16 of *AktG*).[174] The decisive influence in participation stands, if at least one of these circumstances is present: majority voting; control over majority of votes; has the right to appoint or remove majority of members of supervisory or executive body; has exercised the right to appoint majority of members of supervisory or executive body during the accounting year.[175] Additional conditions shall be taken into account in order to determine the company's "majority' voting, appointing and removal rights: other rights of companies' or persons which/who act in its interests (Article 3, paragraph 4 of *Koncernu likums*); held shares or stock

[168] Ibid.
[169] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[170] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[171] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[172] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[173] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer: -). English translation of Article 2:24c: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P. 184.
[174] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[175] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

on behalf of another company or person, as well as shares or stock held as collateral should be excluded (Article 3, paragraph 5 of *Koncernu likums)*; shares or stock held by the company itself; its subsidiary or person acting in its interests should be excluded from total voting rights (Article 3, paragraph 6 of *Koncernu likums)*.[176] A participation group of companies is created more often than contractual one.[177] The decisive influence can be direct or indirect. It can be complicated to identify indirect decisive influence. The reason for that is Article 4, paragraph 3 of *Koncernu likums,* which specifies that indirect decisive influence be exercised through another subsidiary company or a person who acts in the parent company's interests.[178] Indirect decisive influence is generally and broadly defined, therefore, covers all possible indirect groups of companies' subjects, with no specific criteria or case – law established. The main tool to interpret indirect decisive influence is Article 3, paragraph 3 of *Koncernu likums*. As a result, actions and rights are assessed in a diverse and complex environment of group of companies, which makes it difficult to identify the parent company in an indirect decisive influence relationship.

Take – over of a company is an instrument for creating and organising a group structure. *Koncernu likums* company take – over is comparable to German integration (Articles 319 and 320 of *AktG*)[179] and Portuguese total domination (Articles 488 – 491 of *CSC*).[180] In the take – over, corresponding companies retain legal independence, therefore, it is not a direct analogue to reorganisation in the general company law (*Komerclikums*) or amendments to the articles of association. Article 35, paragraph 1 of *Koncernu likums* provides that a take – over of a company can take place, if one company owns 100 % of shares or the stock.[181] Besides that, Article 36, paragraph 1 of *Koncernu likums* institutes that a take – over of company can be possible, if 90 % or more of shares or the stock is owned.[182] *Koncernu likums* as compared to German model (Article 320 of *AktG)*[183] has a lower level of the share or the stock

[176] Ibid.
[177] Grīnberga, I. (2020). Vai pastāv ierobežotas atbildības robežas attiecībā uz kapitālsabiedrību daļu īpašniekiem? *Jurista Vārds*, Nr. 36(1146). 8. lpp.
[178] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[179] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[180] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[181] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[182] Ibid.
[183] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

concentration necessary for performing a take – over (integration) of the company. The duty to acquire remaining shares or parts of a company, whenever owning 90 % of shares (as it is in Portuguese system (Article 490 of *CSC*))[184] is not implemented in *Koncernu likums*. Wholly owned or 90 % owned subsidiary's take – overs outcome is the same; all shares or the stock of the subsidiary are owned by the parent company set by Article 37 of *Koncernu likums.*[185] Article 38 of *Koncernu likums* prescribes compensation as remedy for excluded shareholders. Compensation shall be in the form of a stock or shares of the parent company.[186]

Article 42 of Spanish Commercial Code (*Código de Comercio*) defines a group by a concept of a control. The control in a company is deemed to exist when another company: 1) holds a majority of the voting rights; 2) has the right to remove or appoint a majority of members of the governing body; 3) a majority of voting is established by virtue of an agreement; 4) exercises voting rights and appoints majority of governing body for two financial years when consolidated accounts have to be prepared. The control can be exercised directly or indirectly.[187] Further, the group consists of diverse companies subjected to the same unitary decision – making (emphasis on unified economic management). Existence of mere control does not suffice; there has to be subordination and coordination.[188] In the determination of voting rights, those voting rights indirectly owned through other dependent companies and persons who act on behalf of dependent or dominant companies are also included. The prerequisite of unity of decision has been revoked and definition of the group relies only on the concept of control. [189] Article 42 of *Código de Comercio* covers hierarchic (vertical) and parity based (horizontal groups), similar to the Article 18 of German *AktG.*[190] Although the definition of a group of companies stipulated in Article 42 of *Código de Comercio* is set forth for the purpose of installing an obligation to draft consolidated accounts, it has been commonly

[184] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[185] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[186] Ibid.
[187] Real Decreto de 22 de agosto de 1885 por el que se publica el Código de Comercio. Oficina de D.E. Aguado, 1829.
[188] Girgado, P. (2006). Legislative Situation of Corporate Groups in Spanish Law. *European Company and Financial Law Review (ECFR)*. Volume 3, Issue 4. PP. 365 – 366. https://doi.org/10.1515/ECFR.2006.016
[189] Barona, J., Concha, R. (2007). Report from Spain. Country Status Reports. *European Company Law.* Volume 4, Issue 5. P. 239. https://doi.org/10.54648/eucl2007057
[190] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

applied in other contexts as an indication that a group of companies structure is deemed to exist.[191]

Although Member States have various definitions for a group of companies, two particular concepts prevail. The most used concept is that of control,[192] under which a group of companies' structure exists, if at least one of these circumstances is present: 1) on company holds a majority of the voting rights; 2) an agreement exist with other shareholders providing a majority of the voting rights; 3) it is possible to appoint or remove a majority of members of the board of directors or supervisory board. Such features can be found also in Article 22 paragraph 1 of the Accounting Directive.[193] The CJEU has settled that the control normally arises from ownership of a majority of shareholdings, though minority shareholding can also give a control, if a special rights are provided.[194] The concept of dominance and dependence focuses beyond the basic presumption of the control[195] and it distinguishes between different forms of it, e.g., the management agreement, the profit and loss absorption agreement and the participation. Indeed, the participation stands on the concept of control, which means that both concepts can coexist even in one jurisdiction. The concept of dominance and dependency extend the definition of the group of companies. The concept of dominance and dependency is only applied in Member States that have the legal provisions of a group of companies, e.g., Germany, Latvia and Portugal, but the application scope changes. In Germany, the concept of dominance and dependency is applied to the stock corporations and the private limited liability companies because *AktG* rules for *AG* contractual groups are applicable also to *GmbH*;[196] In Latvia, it is extended also to natural persons (Article 1, subparagraph 8 of *Koncernu likums*);[197] In Portugal according to Article 481 of *CSC* this concept is applicable only to limited liability

[191] Barona, J., Concha, R. (2007). Report from Spain. Country Status Reports. *European Company Law*. Volume 4, Issue 5. P. 238.

[192] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P.176. https://doi.org/10.1017/S1566752900000148

[193] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19

[194] Judgment of the General Court (Second Chamber) of 12 July 2011 in the case T-132/07, Fuji Electric Co. Ltd (anciennement Fuji Electric Holdings Co. Ltd) v European Commission, paragraph 183.

[195] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P.176. https://doi.org/10.1017/S1566752900000148

[196] Ulmer, P. (1986). Gläubigerschutz im 'qualifizierten' faktischen GmbH-Konzern. Bemerkungen zum 'Autokran'- Urteil des BGH vom 16.9.1985. *Neue Juristische Wochenschrift (NJW)*. S. 1580.

[197] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

companies - private limited liability companies (*sociedades por quota*), public limited liability companies (*sociedades anónimas*), limited liability partnerships by shares (*sociedade em comandita por acções*)[198] and a parent company and a subsidiary have to be in a prescribed legal form. Member States without statutory group law, such as France and Netherlands, stick with the concept of the control and have common application of the scope – all commercial companies. In adverse manner, in Spain, where group law is missing, in addition to the concept of the control, the group of companies must be subjected to subordination and coordination, which categories it as the dominance and dependency of a Member State. The reason for various definitions of the group in Member States under the concept of control and the concept of dominance and dependency is that the Accounting Directive harmonises cross-border definitions of the group, but statutory group law independently balances national patterns of business conduction with protection of external shareholders and creditors.

### 2.2. The interest of the group

In France shareholders, directors, chief executive officers and supervisory board members act in the best interest of the company (*l'intérêt social*) conferred by Article 1833 of the French Civil Code (*Code Civil des Français*),[199] Article L. 241-3 of *Code de commerce* and Article L. 242-6 of *Code de commerce.*[200] There is no statutory or case law based definition of the l'intérêt social.[201] Some argue that *l'intérêt social* is distinct (greater) than the interest of shareholders.[202] Others disagree because the principle of shareholders wealth maximisation should interpret *l'intérêt social*, which means shareholders' and company's interests coincide.[203] An alternative position is that *l'intérêt social* depends on circumstances and can have variable meaning. It could either be the interest of shareholders or the sole interests of the company.[204] The understanding of the definition of a company's interest is significant because transactions that violate the interest of the company may be declared null and void. Regardless

[198] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[199] Code civil. Dernière mise à jour des données de ce code : 07 octobre 2022. Version en vigueur au 25 novembre 2022. Legifrance. English translation of cited Articles: Crabb. J., H. (1995). The French Civil Code. Revised Edition (as amended to 1 July 1994). Kluwer Law and Taxation Publishers Deventer. P. 340
[200] Code de commerce. Dernière modification le 26 février 2022. Document généré le 25 février 2022. Legifrance. English translation of cited Articles: Raworth P. (2006). The French Commercial Code in English. Oxford University Press. PP. 278 and 281.
[201] Couret, A. (2002). Le désintérêt social. Mélanges P. Bézard. Montchrestien. P. 63.
[202] Constantin, A. (2002). L'intérêt social: quel intérêt? In Mélanges offertes à B. Mercadal. Paris, France. P. 317-338.
[203] Martin, D. (2005). L'intérêt des actionnaires se confond-t-il avec l'intérêt social? Mélanges D. Schmidt éditions Joly. P. 359-370
[204] Bertrel, J.-P. (1997). La position de la doctrine sur l'intérêt social. Droit & patrimoine. P. 42-47.

of the definition of a company's interests, directors must make independent judgment on the balance of interests.[205] In a group of companies setting, on the one hand a board of directors of a subsidiary have overriding responsibility to the interests of the company rather than personal interests of any shareholder, even if they be the parent company's (majority shareholder), but on the other hand a board of directors of a subsidiary may determine (in some cases may even be required) to conclude transactions disadvantageous to the company by pursuing the interest of the group based on the fiduciary relationship with a parent company.[206] In favour of safeguarding legal independence of companies, the parent company cannot issue legally binding instructions nor can it represent the subsidiary in relations with third parties. However, directors of a subsidiary do in fact follow the instructions of the parent company to simply avoid termination of their appointment or to maintain financing.

In France the *Rozenblum* doctrine establishes group defence or safe harbour for pursuing the interest of the group, if: a group is characterised by firm structural establishment of the group; there is effective and strong business integration; financial equilibrium is preserved; actions do not exceed the possibilities.[207] *Rozenblum* doctrine does not cover personal groups, private equity groups and tax optimisation structures. The group of companies for invoking the *Rozenblum* doctrine must have capital links between them. Merely participation without mutual coordination, even with drafted consolidated annual accounts, does not create firm structural establishment between a group of companies. Interrelated commercial activities and sharing of their negative and positive impacts forms firm structural establishment between a parent company and a subsidiary. Well-balanced burden and benefit sharing retains certain autonomy, so that a subsidiary does not become a branch of a parent company, as well as restricts abuse of influence.[208] Business integration means a common interest and coherent policy. The reference to common interests suggests that the interests of the group does not coincide with the interest of the parent company. The common interests consist of profitability as a group rather than achievement of separate opportunities. It can be economic, social or financial interest. Without common interest there is no justification for granting any advantages to another company.[209] Commercial activities for a group of

[205] Cozian, M., Viandier, A., Deboissy, F. (2001). Droit des societies. 14ème édition. Paris. P. 128.
[206] Cour de Cassation, Chambre commerciale, du 12 février 1968, Publié au bulletin.
[207] Cour de Cassation, Chambre criminelle, du 4 février 1998, 97-82.417 (Rozenblum). Publié au bulletin.
[208] Corporate Group Law for Europe: Forum Europaeum Corporate Group Law (2000). *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 180. doi:10.1017/S1566752900000148
[209] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 218. https://doi.org/10.1515/ecfr-2013-0194

companies are fostered and set out in long term and directed towards a stable balance between autonomous interests of a subsidiary and group interests. The parent company is at the centre of determining coherent policy, but it is not clear what role does a subsidiary play in setting group interests.[210] Financial equilibrium can be achieved by compensation, and it can be also non-monetary or future compensation. Artificial support of a member of the group is prohibited.[211] Achievement of group interest is not exceeding its possibility, if insolvency risk is not triggered for either company. Nevertheless, the question arises how the consideration of the subsidiaries and group's interests should be measured and over which time period it should be weighted. If a group of companies stay clear from insolvency the *Rozenblum* doctrine for rational intra-group transactions creates a flexible group defence or safe harbour.[212]

In the Netherlands it is recognised that the parent company can exercise the influence over its subsidiary regardless of the fact that the corporate body of the board of directors is not subordinated to shareholders or a supervisory board.[213] It is based on the view that group influence is self-evident.[214] A subsidiary's board of directors has no right to refuse a parent company's requests: 1) to give information; 2) to follow guidelines 3) to follow instructions to start projects. The refusal can be grounds for instant removal of a director from the board.[215] Directors of the board may be required to receive the prior approval of the supervisory board or general meeting of shareholders for executing certain tasks.[216] Article 2:129, paragraph 4 of *BW* and Article 2:239, paragraph 2 establish that the management must conduct itself in accordance with the directions of another body of the corporation, if it is provided by the articles of association.[217] The right to give instructions is restricted to the scope of the articles of association and the general nature (opposite of specific directions). [218] The duty of the

[210] Corporate Group Law for Europe: Forum Europaeum Corporate Group Law (2000). *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 180. doi:10.1017/S1566752900000148
[211] Guyon, Y. (2003). Droit des affaires. Droit commercial général et sociétés. Tome 1. 12ème édition. Paris. Economica. P. 670.
[212] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 218. https://doi.org/10.1515/ecfr-2013-0194
[213] Hoge Raad 21 January 1955, N.J. 1959. ECLI:NL:PHR:1955:AG2033
[214] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 261.
[215] Calkoen, W. J. L. (1980). The Netherlands. International Business Lawyer. Volume 8. P. 223.
[216] Schuit, S. R., Bier B., Verburg L. G., Wisch J. A. T. (2002). Corporate Law and Practice of the Netherlands. Kluwar Law International. P. 150.
[217] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. PP. 252 and 302.
[218] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 265.

supervisory board is stipulated in Article 140, paragraph 2 of *BW* and Article 250, paragraph 2 of *BW* and it is to oversee affairs of a company and its business.[219] The reference to the company's business extends the parent company's board's the duty to also oversee its subsidiaries.[220] Accordingly, it is generally accepted that the board of directors also has duties to the more complex interests, such as a group of companies, and should not restrict itself to the interests of shareholders alone.[221]

In Dutch case law it was confirmed that the parent company can give its subsidiary instructions or directions, which the subsidiary will find difficult to bypass because of its dependency. The same judgment also lays down the limit for the exercise of group influence. A subsidiary company's own duties and rights should be intact. On its own responsibility the subsidiary company must ensure that it complies with Dutch legislation.[222] Moreover, the subsidiary's minority shareholders, creditors and employees interests cannot be violated.[223] The case law upholds rejection of the opinion that a subsidiary should be concerned exclusively with its own interests. In a group structure, group interests can prevail, if they do not damage the subsidiary's corporate interests - minority shareholders, employees, creditors. The influence of the parent company cannot be used to the extent that it distorts sufficient balancing of the interest of the subsidiary and the interests of the group.[224] The interest of a group that damages a subsidiary's corporate interests may be pursued, if the parent company removes or protects against the harm caused to those parties whose legal position depends on the subsidiary's autonomous well-being. Interests of the subsidiary could be closely linked to other subsidiaries within the same group. Hence a subsidiary's interest could be to ensure or complement another subsidiary's (within the group) commercial activities. It is delineated in case law that granting security on a reciprocal basis and acceptance of liability (to another subsidiary within the group) is not regarded as conflicting with the subsidiary's objects.[225] Later in the case law it was clarified that the parent company does not possess the right to issue binding instructions unless articles of association of the subsidiary stipulate to the contrary.

[219] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. PP. 256 and 305.
[220] Hoge Raad 10 januari 1990, NJ 1990, 466. ECLI:NL:PHR:1990:AC1234
[221] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 241.
[222] Ibid, P. 275.
[223] Hoge Raad 25 september 1981, N.J., 1982, 443. ECLI:NL:HR:1981:AG4232
[224] Calkoen, W. J. L. (1980). The Netherlands. *International Business Lawyer*. Volume 8. P. 225.
[225] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 261.

Also, it was acknowledged that binding instructions could be enforced through *de facto* control simply by removal or appointment of the board.[226]

In Italy before the 2004 Company law reform, it was recognised that legal entities may be under dominant influence and unitary direction.[227] The rules regulated only static control (central control and dominance/dependence between two companies) without considering exercise of unitary direction.[228] Hence, the unitary direction of a group had to conform to the company's purpose. The company's purpose was highlighted as long-term profitability, shareholders' benefit and consideration of market opportunities at every point.[229] Subordination of a subsidiary could not be imposed, even with the conclusion of an agreement.[230] The 2004 Company law reform changed the regulatory framework of recognition of the interest of the group in Italy. It introduced statutory French *Rozenblum* doctrine. The interests of the group can be pursued, if: a firmly established group is organised; an action taken confirms with the group's coherent policy and is in the interest of the group; financial equilibrium is preserved i.e., compensation for suffering the negative consequence. [231]

In order to establish applicability of Italian group law Article 2497, paragraph 6 of *Codice Civile* states that a company that must draft consolidated accounts or controls another company in light of Article 2359 of *Codice Civile* is deemed to exercise direction and coordination.[232] The presumption can be rebuttable. Direction and coordination may arise from articles of association and contracts, which bestow dominant influence.[233] The control and unitary direction and coordination are differentiated. In practice it is uncertain how to distinguish mere control from unitary direction and coordination.[234] The rights, responsibilities and obligations concerning direction and coordination of group companies are applicable also to foreign parent companies and Italian subsidiaries and Italian parent companies and foreign

[226] Hoge Raad 21 december 2001, NJ 2005, 96. ECLI:NL:PHR:2001:AD4499
[227] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, issue 2. PP. 196 -199. https://doi.org/10.1515/ECFR.2007.013
[228] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. P. 122. https://doi.org/10.54648/eucl2019018
[229] Cossu, M. (2013). The "company's interests" of the "società aperte" under Italian Corporate Laws. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 1. P. 73. https://doi.org/10.1515/ecfr-2013-0045
[230] Fasciani, P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, issue 2. Volume 4, issue 2. P. 190. https://doi.org/10.1515/ECFR.2007.013
[231] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. European Company Law. Volume 16, Issue 4. P. 123. https://doi.org/10.54648/eucl2019018.
[232] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[233] Fasciani, P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 203. https://doi.org/10.1515/ECFR.2007.013
[234] Ferrarini, G., Giudici, P., Richter, M.S. Company Law Reform in Italy: Real Progress? *Rabels Zeitschrift Für Ausländisches Und Internationales Privatrecht / The Rabel Journal of Comparative and International Private Law* 69, no. 4. P. 697.

subsidiaries. Although natural persons control many groups of companies, the scope of Article 2497 of *Codice Civile* does not cover them.[235]

Article 2497 of *Codice Civile* does not determine explicit rules of how direction and coordination of subsidiaries must be carried out; instead, it defines situations when direction and coordination do not meet the conditions established by the law. The parent company is directly responsible for exercising direction and coordination. Exercising of direction and coordination must be in line with the principles of correct corporate management, cannot cause prejudice of the profitability to other shareholders and the value of their shares, as well as damage the integrity of corporate assets.[236] The parent company may not legally force the subsidiary to act contrary to its own interests. It is believed that the interest of the group coincides with the independent interest of the subsidiary.[237]

Subsidiary's profitability and a value of shares are examined in light of "global result" or in other words the interest of the group. Damages occurred by endeavour of group interests are justified by achievement of global result or by necessity of performance of specific transactions for this purpose. If damages are not compensated by the benefit of global results, then the parent company is obliged to eliminate those. Elimination of damages caused must be inferior to the profit of the group. Correct corporate management is interpreted in the sense that the parent company's exercise of direction and coordination must be in conformity with not only legal rules governing their own activities, but also subsidiaries.[238] From the perspective of legal theory of compensatory advantages, if an imbalance between benefits and burdens exist, the compensation for damages suffered must be received. Appropriate compensation alleviates the parent company from the liability. The advantages gained from simply belonging to a group of companies are not sufficient.[239] It is uncertain how to determine whether satisfactory compensation has been made.[240] Minority shareholders and creditors have the right to directly bring an action against the parent company.[241] Nevertheless, the parent company

[235] Kousedghi, S. (2007). Protection of Minority Shareholders and Creditors in Italian Corporate Group Law. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 5. P. 220.
[236] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[237] Fasciani, P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 211. https://doi.org/10.1515/ECFR.2007.013
[238] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law.* Volume 16, Issue 4. P. 124. https://doi.org/10.54648/eucl2019018
[239] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 211 and 219. https://doi.org/10.1515/ECFR.2007.013
[240] Kousedghi, S. (2007). Protection of Minority Shareholders and Creditors in Italian Corporate Group Law. *European Company and Financial Law Review (ECFR).* Volume 4, Issue 5. P. 220.
[241] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. P. 124. https://doi.org/10.54648/eucl2019018

cannot be held liable for "passive role" or merely for presumption of control.[242] It shifts the burden of proof to creditors and minority shareholders.

In Article 2497 , paragraph 3 of *Codice Civile* is specified the parent company's influence of direction and coordination does not entail the right of the parent company to impose instructions or that they must be legally binding. The board of directors' act in accordance with Article 2380, paragraph 2 of *Codice Civile*, therefore are exclusively responsible for managing the company.[243] On the one hand, the parent company must consider how and whether the interests of the group will affect the specific interests of the subsidiary, to which its direction and coordination is addressed. On the other hand, the board of directors have the duty to consider how and if direction and coordination is fitting with the interests of the subsidiary.[244]

In Germany Article 308 of *AktG* institutes power of directions for contractual groups under the control agreement. [245] Meaning that a parent company shall be entitled to issue instructions to its *AG* subsidiary, based on the control agreement. Issued instructions can also be detrimental to the subsidiary, if they do not threaten the existence of it and are in the interest of the *Konzern*. Illegitimate instructions cannot be justified. Illegitimate instructions are disproportionate between the benefit of a group and prejudice of a subsidiary or breach of a law, a morality, a charter of a company or the control agreement.[246] Article 309, paragraph 1 of *AktG* determines that the control of management should be exercised with due care of a prudent manager faithfully complying with his duties.[247] The contractual groups that are formed under the Article 292 of *AktG* remain subject to general company law rules.[248] From the perspective of recognition of the interests of the group, integration has significant importance because Article 323 of AktG outlines that the parent company is entitled to issue directions to the subsidiary's management board without considering disproportionality

[242] Ventoruzzo, M. (2005). Experiments in Comparative Corporate Law: The Recent Italian Reform and the Dubious Virtues of a Market for Rules in the Absence of Effective Regulatory Competition. *European Company Law Review*. Volume 2, Issue 2. P. 251. https://doi.org/10.1515/ecfr.2005.2.2.207
[243] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 202. https://doi.org/10.1515/ECFR.2007.013
[244] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. P. 124. https://doi.org/10.54648/eucl2019018
[245] Ibid
[246] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 40.
[247] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[248] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. Kluwer Law International. P. 50.

between the benefit of a group and prejudice of a subsidiary.[249] In *de facto* groups, Article 311 of *AktG* prohibits use of influence to enter into transactions that are detrimental to a subsidiary.[250] However, Article 311 of *AktG* entitles the parent company in *de facto* group structure to give instructions to the subsidiary, but these instructions are not binding.[251] In *GmbH* group the board of director's autonomous power is restricted by resolutions of shareholders, under Article 37, paragraph 1 of *GmbHG*.[252] The parent companies' right to give directions can be enhanced by the control agreement or the profit or loss absorption agreement.

In Portugal the issue of the parent company to give instructions or directions are regulated by the general principles of company law, which is contrary to the German (*AktG*) model that has distinct statutes on this matter. The parent company can only exercise its power within limitations of : respecting subsidiary's autonomous or independent interests (Article 64 of *CSC*);[253] protecting subsidiary's property;[254] in line of fiduciary duties of members of the company boards (Article 72 of *CSC*); limits of damaging influence of majority shareholder (Article 83, paragraph 4 of *CSC*); annulment of any advantages gained by the parent company, which are detrimental to the subsidiary or its minority shareholders (Article 58, paragraph 1, subparagraph b of *CSC*).*[255]* The power to give instructions or directions can be exercised only at arm's length with limited central control in order to maintain autonomy and independence of the subsidiary. The subsidiary's board of directors' duty to act with due care of a prudent manager does not exclude the liability of the parent company.[256] However, in the subordination group, the parent company, in line with Article 503 of *CSC* has the right to give disadvantageous and binding instructions, as long as those instructions serve the interests of the parent company or any other member (company) of the group. The parent company's broad legal power of direction in the subordination group is limited only to matters of management

[249] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[250] Hopt, K. J. (2015). Groups of Companies: A Comparative Study on the Economics, Law and Regulation of Corporate Groups. European Corporate Governance Institute. Law Working Paper No. 286/2015. P. 10.
[251] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 413.
[252] Act on Limited Liability Companies. Consolidated and published in the Federal Law Gazette III, Index No. 4123-1. Amended by Article 10 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[253] Engrácia Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review (ECFR)*. Volume 2, Issue 3. P. 374. https://doi.org/10.1515/ecfr.2005.2.3.323
[254] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 25.
[255] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[256] Azeredo Perdigao, M. (1995). Groups of companies in Portugal: a parent's liability for debts of its subsidiaries. *International Company and Commercial Law Review*. Volume 6, issue 4. Sweet & Maxwell. P. 6.

and cannot violate other fields of law. In the light of all foregoing, subordination groups can be characterised as central management models, and other groups as decentralised management models.[257]

In Latvia based on the Article 26 of *Koncernu likums*, a parent company has the right to give binding instructions, which can be detrimental to a subsidiary's independent or autonomous interests. Precondition for exercise of such right is conclusion of a management contract or a management and transfer of profit contract. Instructions can be detrimental with the meaning of losses caused to the subsidiary, but still within the interests of the parent company or any other company in the group. Instructions are binding because a subsidiary is not entitled to refuse to comply with issued instructions, even if a subsidiary considers oppositely. Exception for refusing to comply with given instructions is "manifestly" not in the interests of a parent company or a group. In the event the supervisory board does not give required consent, the parent company shall be notified. The parent company can issue repeatedly respective instructions and required consent of the supervisory board is not needed anymore.[258] Furthermore, Article 18 prohibits a parent company to give instructions to a subsidiary in order to terminate, amend or keep in effect a group of companies' contract. Article 27 of *Koncernu likums* clarifies that binding instructions shall be given with the care of an honest and conscientious manager with respect to a subsidiary. Instructions inducing suspension of operations (administrative procedure), insolvency or liquidation (by a court order) is prohibited.[259] Obligation of the care of an honest and conscientious manager is analogous to Article 169 of *Komerclikums* performance of obligations as an honest and careful manager would. The power to give instructions is not far – off from the framework for limited liability companies in general company law (Article 210, paragraph 2 of *Komerclikums*), which grant the right to the meeting of shareholders to take decisions on issues that are in the competence of the board of directors or the council.[260] It shall be acknowledged that a transfer of profit contract without an added management contract brings only economical changes.[261]

[257] Engrácia Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review (ECFR)*. Volume 2, Issue 3. P. 376. https://doi.org/10.1515/ecfr.2005.2.3.323

[258] Ibid.

[259] Ibid.

[260] Komerclikums. Pieņemts 13.04.2000. Stājies spēkā 01.01.2002. Publicēts: Latvijas Vēstnesis, 158/160, 04.05.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 11, 01.06.2000. Pēdējie grozījumi 01.08.2023.

[261] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. S. 236 – 238.

Therefore, in the absence of legal structural changes, the right to give binding instructions is not bestowed on the parent company in the respective group of companies' relationship.

According to Article 41, paragraph 1 of *Koncernu likums,* the right to issue binding instructions is provided in case of a take-over of companies, if 1) a management contract or 2) a management and transfer of profit contract is concluded.[262] Similar to Germany the difference is the parent company is entitled to give binding instructions to the taken over subsidiary without considering disproportionality between the benefit of a group and prejudice of a subsidiary.

The parent company's right to give instructions to a *de facto* group of companies is regulated differently than a contractual group of companies. Article 29, paragraph 1 of *Koncernu likums* construes the restriction to induce a subsidiary to enter into disadvantageous transactions or any other detrimental measures, unless compensation for losses incurred as a result of disadvantageous transactions or detrimental measures is made.[263] Article 29 of *Koncernu likums* is identical to German Article 311 of *AktG*.[264] In the literature it is understood that German Article 311 of *AktG* entitles the parent company in a *de facto* group structure to give instructions to the subsidiary, but these instructions are not binding.[265] The same conclusion can be made for Article 29 of *Koncernu likums* because the board of directors of a subsidiary is induced merely by the parent company's issued instructions. Consequently, Article 29 of *Koncernu likums* indirectly recognises the power to give instructions by the parent company by limiting scope of them. The aforementioned instruction issuing is opposite from Portuguese (*CSC*) system, where in a *de facto* group of companies' the power to give instructions is governed by general company law rules. In order to maintain autonomy and independence of the subsidiary, power to give instructions or directions can be exercised only at arm's length with limited central control.[266] In contrast, *Koncernu likums* allows the exercise of a centralized management model to the greater extent in *de facto* group structure.

In Spain the pursuit of the group interest was not legitimised because it contravened

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[262] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[263] Ibid.

[264] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[265] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 413.

[266] Engrácia, Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review.* Volume 2, Issue 3. P. 376. https://doi.org/10.1515/ecfr.2005.2.3.323

with the generally accepted notion that company must always act in its own interest.[267] A 2002 proposal for *PCSM*, which has not been enacted, granted the parent company the right to issue binding instructions.[268] It was clarified that the given instructions can never breach the law or the articles of association. In the *PCSM* it was not clear that a connection between the control and the accountability was made. The positive effect of being in the group was disregarded; it rather focused on the individualized nature of instructions than considering them as a whole.[269]

However, in 2015 in case law the pursuit of the interest of the group was acknowledged by stating that a subsidiary can be under coordinated or unified management by a parent company, receive instructions that have to be followed and which would pursue the group's best interest, which can be detrimental to the interest of a subsidiary. In the case law was clarified that a subsidiary being controlled by a parent company does not mean complete loss of its identity and autonomy (legal personality), as well as it cannot be removed from receiving benefits from pursuing the interest of the group. The reasonable balance of economic value between the interest of a subsidiary and a group should be found so that benefits offset the consequences (harm), i.e., an external shareholder (a shareholder who does not have an interest in a group of companies or in a company with whom the conflict of interest has risen) and creditor interests should be attached. Particularly, the protection of company's solvency has been highlighted.[270]

In the view of all foregoing, two approaches of recognising the interests of the group can be distinguished. The understanding in countries that follow *Rozenblum* doctrine has developed to consider that specific codification of pursuit of the interests of a group would deprive the group of the company structure's effectiveness and a subsidiary would become a branch of the parent company. Interests of a group must be respected and creditor and minority shareholder protection does not justify disregarding it in all circumstances. These countries have accomplished a more flexible regulatory framework for pursuing the interests of the group. Countries, which follow the German *Konzernrecht* model of specific codification of groups of companies, are less concerned with the recognition of the interests of the group, but rather focus on the protection of creditors and minority shareholders. It is based on the notion

[267] Fuentes, M. (2007) Corporate Groups and Creditors Protection: An Approach From a Spanish Company Law Perspective. *European Company and Financial Law Review (ECFR).* Volume 4, Issue 4. P. 535. https://doi.org/10.1515/ECFR.2007.026

[268] Embid Irujo, J.M. (2005). Trends and Realities in the Law of Corporate Groups. *European Business Organization Law Review (EBOR).* Volume 6, Issue 1. P. 86. https://doi.org/10.1017/S1566752905000650

[269] Girgado, P. (2006). Legislative Situation of Corporate Groups in Spanish Law. *European Company and Financial Law Review (ECFR)*. Volume 3, Issue 4. P. 379. https://doi.org/10.1515/ECFR.2006.016

[270] Sentencia del Tribunal Supremo - Sala Primera, de lo Civil, 11 de Diciembre de 2015. STS 5151/2015 - ECLI:ES:TS:2015:5151

that in a single company the interests of shareholders and creditors are similar, but in a group of companies' dependent corporations are subordinated to the interests of the company with dominant influence, which creates conflict of economic interests and is a source of risk. A subsidiary's isolation from the group and its shielding from any burdens also reduces benefit sharing irrespective how those are attained.

### 2.3. The creditor protection

In order to facilitate capital accumulation, the separate legal personality was supplemented with limited liability. Limited liability provides that shareholders of the company risk only with their capital contribution.[271] The risk for shareholders can be limited, while rewards are unlimited. There is disparity between risks and rewards.[272] On the one hand, such investment regulation stimulates passive investors that do not participate in management to invest,[273] is more practical for large numbers of investors in one company,[274] encourages economically useful risk taking,[275] reduces monitoring cost,[276]promotes free transfer of shares,[277] facilitates operations in public securities markets[278] and creditors do not have to bring claims against numerous shareholders for unfulfilled or unsatisfied obligations.[279] On the other hand, limited liability shifts the risk from shareholders to creditors,[280] increases riskier actions and discourages the company from appropriate risk measures.[281]

Mainly the group of companies consists of several limited liability corporations. The separate legal personality and limited liability was introduced at the time when independent companies existed.[282] The rationale for limited liability for group of companies is justified by

[271] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. Kluwer Law International. P. 1.
[272] Davies, P. L. (2008). Gower and Davies' Principles of Modern Company Law. 8th edition. Sweet & Maxwell. P. 194.
[273] Posnar, R.A. (1986). Economic Analysis of Law. 3rd edition. Boston, Little Brown. P. 503.
[274] Manne, H.G. (1967). Our two corporation systems: law and economics. Virginia Law Review. Volume 53. P. 262.
[275] Easterbrook, F.H., Fischel D.R. (1985). Limited liability and the corporation. *University of Chicago Law Review.* Volume 52. PP. 96-97.
[276] Manne, H.G. (1967). Our two corporation systems: law and economics. *Virginia Law Review*. Volume 53. PP. 262-263.
[277] Easterbrook, F.H., Fischel D.R. (1985). Limited liability and the corporation. *University of Chicago Law Review*. Volume 52. P. 92.
[278] Davies, P. L. (2008). Gower and Davies' Principles of Modern Company Law. 8th edition. Sweet & Maxwell. P. 194.
[279] Clark, R.C. (1979). The regulation of financial holding companies. Harvard Law Review. Volume 92. P. 789.
[280] Landers, J.M. (1975). A unified approach to parent, subsidiary and affiliate questions in bankruptcy. *University of Chicago Law Review*. Volume 42. P. 589.
[281] Heitland, A.R. (1979). Survival of products liability claims in asset acquisition. *Business Law*. Vol. 34. P. 498.
[282] Vandekerckhove, K. (2007). Piercing the Corporate Veil: A Transnational Approach. Kluwer Law International. P. 4.

segregation of collections of assets that benefits creditors. Creditors of shareholders cannot assert their claims against the company and vice versa. Each set of creditors is safe in confining their creditors' claims and they do not face competition.[283]

In the group of companies structure the parent company is not a passive investor, uses *de facto* control and spreads the risk onto subsidiaries. The application of limited liability to group companies is criticized to be immoral and unfair. Blumberg appeals that the limited liability for the group of companies is not deliberate choice, but is actually a historical accident.[284] Guyon expresses that commercial law is more open to risk, and civil law is rather protective, therefore, unlimited liability should have been an exception in civil law and rule in commercial law. Moreover, the corporate debt should be proportionate to the size of the company. However, liability is heaviest in small companies and limited liability being at its top in stock corporations.[285]

In France the parent company by not respecting *Rozenblum* doctrine, risks assuming liability of the latter. Additionally, under *Rozenblum* doctrine the parent company can become *de facto* directors and/or the subsidiary can be a fictitious corporation (*société fictive*). *De facto* directors may be individuals, legal entities or individuals who act as legal representatives of legal entities, under Article L. 651-1 of *Code de commerce*.[286] According to Article L. 651-2 of *Code de commerce,* shareholders are qualified as *De facto* directors, if it can be demonstrated that they serve as directors of a company, therefore the parent company can become liable for mismanagement of a subsidiary as its board of directors.[287] In case law *de facto* directors conducts are interpreted as infringement of decision-making and independence of appointed directors.[288] Isolated, occasional and unspecific conduct does not demonstrate preconditions for shareholders qualification as *de facto* directors.[289] In a group of companies *de facto* directors have a dominant influence over subsidiaries' management. Furthermore, in the same case an important circumstance was highlighted that the parent company was sole master of the

[283] Davies, P. L. (2008). Gower and Davies' Principles of Modern Company Law. 8th edition. Sweet & Maxwell. P. 196.
[284] Blumberg, P. I. (1987). The law of corporate groups: tort, contract, and other common law problems in the substantive law of parent and subsidiary corporations. Gaithersburg/ New York, *Aspen Law & Business*. P. 56.
[285] Guyon, Y. (2002). Traité des contrats. Les sociétés. Aménagements statutaires et conventions entre associés. 5ème édition. L.G.D.J. Paris. P. 81-82.
[286] Code de commerce. Dernière modification le 26 février 2022. Document généré le 25 février 2022. Legifrance. English translation of cited Articles: Raworth P. (2006). The French Commercial Code in English. Oxford University Press. P. 489.
[287] Ibid.
[288] Cour de Cassation, civile, Chambre commerciale, 10 juillet 2008. Publié au bulletin.
[289] Cour de Cassation, civile, Chambre commerciale, du 26 octobre 1999, 96-20.488. Publié au bulletin.

subsidiary's economic and financial policies.[290] The relationship of complete subordination is grounds for qualifying the parent company as *de facto* director for the subsidiary. Complete subordination institutes: the place of general meetings; power of attorney over the account; to whom auditors report; solvency dependency; guarantees of creditworthiness. For qualifying the parent company as *de facto* director, a strict and demanding standard is imposed. A simple group of companies latter does not create a basis for the parent company qualification as *de facto* director. A parent company's liability for being *de facto* director is to a subsidiary, therefore does not create direct liability to creditors.[291]

A *Société fictive* is a company that exclusively serves the interests of the real beneficiary (natural or legal person) behind it. A *Société fictive* is set up in order to engage in high-risk activities and to protect the real beneficiary's interests under the corporate veil of the respective company.[292] When a subsidiary's assets cannot be distinguished from the parent company's it is described as commingling of assets (*confusion des patrimoines).*[293] Abnormal financial relations between a group of companies also constitute *confusion des patrimoines.* Financial assistance itself does not institute abnormal financial relations; instead, great importance is given to the conditions under which benefit is granted.[294] If a subsidiary is determined to be *société fictive* or *confusion des patrimoines* occurs with the subsidiary's assets, the parent company may be held liable for debts of a subsidiary.[295] *Société fictive* and *confusion des patrimoines* is still in the framework of insolvency. Nevertheless, *Société fictive* and *confusion des patrimoines* constitutes a respective group of companies as a single entity.

In Netherlands in a group structure of separate legal personalities can be pierced, and a subsidiary's liability can be extended to a parent company by identification (*vereenzelviging*) or a tort (*onrechtmatige daad*). Under the concept of identification the two companies can be regarded as one and the liability of the one company can be attributed to the other company.[296] The mere exercise of influence by itself does not stipulate grounds for piercing the corporate

[290] Cour de Cassation, civile, Chambre commerciale, 10 juillet 2008. Publié au bulletin.
[291] Cour de Cassation, civile, Chambre commerciale, du 13 décembre 2005, 04-19.234, Publié au bulletin.
[292] Kuckertz, W. (2002). Der Haftungsdurchgriff auf ausländische Unternehmen und Geschäftsleiter nach französischem Recht. Heidelberg. Verlag Rechts und Wirtschaft. S. 41.
[293] Cozian, M., Viandier, A., Deboissy, F. (2001). Droit des societies. 14ème édition. Paris. P. 605-606.
[294] Sorensen, A. (2016). France: "confusion des patrimoines" - the commingling of assets, another way of piercing the corporate veil. *International Company and Commercial Law Review*. Volume 27, issue 9. Sweet & Maxwell. P. 5.
[295] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. S. 488.
[296] Bartman S.,M., Dorresteijn, A., F., M. (2006). Van het concern. Deventer. P. 234-239.

veil because it is permissible for the parent company to be involved in subsidiary's affairs.[297] It is rather established on case-by-case basis in exceptional circumstances, where separate personality is abused.[298] On a basis of a tort the parent company can incur the liability for given instructions, if it was aware or should have been aware of actions detrimental effect to the interests of creditor,[299] e.g. limiting creditors' ability to satisfy its claims.

Like French regulation Dutch Article 138, paragraph 7 *BW* and Article 248, paragraph 7 of *BW* regulates that any person who has determined the policy of the business will be treated as a director. The determination of the policy of business can also be carried out jointly.[300] The parent company can become a *de facto* director in case of a subsidiary's insolvency. Similarly as for piercing the corporate veil for exercise of influence *de facto* director status does not automatically lead to liability. In order to trigger the liability, it is necessary to prove that the parent company actually used its group influence to directly impose its instructions or directions. The parent company will not be liable for improper management by a formal board of directors.[301]

In Italy in addition to statutory *Rozenblum* doctrine access to accurate information about the group of companies (its structure and financial results) there is a protective measure for parties involved in a group of companies and third parties outside of the group of companies.[302] Article 2497, paragraph 3 of *Codice Civile* grants transparency in the decision-making process. When the decision of a subsidiary is influenced by the parent company's direction and coordination, it shall be motivated (analytically), as well as the reason and the interests concerned shall be indicated. The board of director's annual report shall consider such decisions.[303] Anyone who is interested may obtain this information. The reasoning provided must be concrete and not merely hypothetical. Furthermore, it is an important mechanism for revealing information regarding conflicts of interests and receiving compensation for damages suffered. Nonetheless, for decisions, which do not directly concern direction and coordination, respective rules of disclosure are not applicable. Of significant importance is the flow of data

[297] Hoge Raad 2 november 1984, N.J., 1985, 446. ECLI:NL:PHR:1984:AG4892
[298] Hoge Raad 13 oktober 2000, NJ 2000, 698. ECLI:NL:PHR:2000:AA7480
[299] Hoge Raad 19 februari 1988, NJ 1988, 487. ECLI:NL:PHR:1988:AG5761
[300] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. PP. 255 and 305.
[301] Bartman S.,M., Dorresteijn, A., F., M. (2006). Van het concern. Deventer. PP. 251-258.
[302] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 202. https://doi.org/10.1515/ECFR.2007.013
[303] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).

and information between the parent company and the subsidiary. Without appropriate data and information flow from the parent company the subsidiary would not be able to analytically motivate, provide the reason and determine the interests concerned for decisions based on direction and coordination. The board of directors has the right to demand data and information regarding direction and coordination.[304]

Article 2497, paragraph 2 of *Codice Civile* provides further transparency. A subsidiary must be registered in Companies Registry (in a special section) as a subsidiary of a group, as well as the parent company must be revealed under whose direction and coordination the subsidiary is a subject.[305] For that reason third parties are deemed to have effective knowledge.[306] If the board of directors of a subsidiary fail to disclose this information, they are liable for any harm caused by the misinformation to third parties or shareholders, according to Article 2497, paragraph 2, subparagraph 3 of *Codice Civile.*[307] It is questionable whether the liability can be extended to the parent company for forcing the board of directors not to disclose information because of the flexible nature of direction and coordination.[308]

In Germany, Article 20 of *AktG* provides that as soon as any company holding more than one quarter of the shares of an *AG* is required to notify in writing. The notification must also be made for acquiring a majority of shares or votes or subsequently when the interests fall below these levels. An *AG* is obligated to publish notification. Failure to comply with the obligation to notify is suspension of shareholders rights. [309] The purpose of such provision is to inform creditors and the public and to ensure enforceability of all rules of *Konzernrecht.*[310]

As stated in Article 302 of *AktG,* any damages or losses to a subsidiary originating from the control agreement or the profit and loss absorption agreement has to be compensated by a parent company. On the one hand, Article's 302 of *AktG* framework of compensation for any damages or losses has been criticised as being "far reaching" because the causal link resulting

[304] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. PP. 207- 208. https://doi.org/10.1515/ECFR.2007.013
[305] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[306] Rosa, A. P. L. (2001). Trattato di diritto commerciale. Buonocore. Trattato di diritto commerciale. Torino. P. 107.
[307] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[308] Fasciani P. (2007). Groups of Companies: The Italian Approach. *European Company and Financial Law Review (ECFR)*. Volume 4, Issue 2. P. 205. https://doi.org/10.1515/ECFR.2007.013
[309] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[310] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 165.

from exercised control is not taken into account. On the other hand, the parent company by entering into contractual agreement of Article 291 of *AktG* is voluntarily piercing the corporate veil. Additionally, an appropriate compensation mechanism for minority stockholders (stockholders outside of the group) is provided in Article 304 of *AktG* in case of a profit and loss absorption agreement.[311] Moreover, Article 300 of *AktG* exist to ensure safeguarding of a legal reserve, if the profit and loss absorption agreement is concluded, but Article 301 limits the maximum amount transferable, if the profit and loss absorption agreement exist.[312] While the provisions of Article 300 and 301 of *AktG* protects subsidiaries from financial positions deterioration, if the profit and loss absorption agreement is concluded, they do not assure subsidiary's well-being in the event the group of companies contract is terminated.[313]

In *de facto* group the piercing of corporate veil arises from statutory obligation. If issued instructions are causing a disadvantage to the subsidiary, the parent company has to compensate the loss or damages, in accordance with Article 317 of *AktG.*[314] The subsidiary's recovery is limited to those transactions that the parent is responsible for[315] and could foresee a detrimental nature.[316] It is measured against how two completely independent companies would act[317] and offsetting advantages should be also taken into account,[318] e.g., secured credit can be deducted from the compensation payable.[319] It is contrary to contractual group compensation, where the parent company is liable for all a subsidiary's debts. In order to determine, which transactions the parent company can be liable for, Article 312 of *AktG* states that the subsidiary must disclose all legal transactions with members of the group.[320] Liability in the *de facto* group is case–by-case analysis. Preparation of the report of all legal transactions with group companies and separate liability for each transaction has been criticised for being too burdensome and often it cannot be anticipated whether or not transactions will be

[311] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[312] Ibid
[313] Biedenkopf, K., Koppen-Steiner, H. (1971). Kölner Kommentar zum Aktiengesetz. Köln: Carl Heymanns Verlag. S. 70.
[314] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[315] Alting, C. (1994). Piercing the Corporate Veil in American and German Law - Liability of Individuals and Entities: A Comparative View. *Tulsa Journal Comparative and International Law*. Volume 2, article 4. P. 238.
[316] Biedenkopf, K., Koppen-Steiner, H. (1971). Kölner Kommentar zum Aktiengesetz. Köln: Carl Heymanns Verlag. S. 135, 146 und 155.
[317] Reinhard von Godin, R., von, Wilhelmi, H. (1967). Aktiengesetz vom 6. September 1965. De Gruyter. 3. Auflage. S. 1631.
[318] Würdinger, H. (1973). Aktien- und Konzernrecht : eine systemat. Karlsruhe : Müller. 3. Auflage. S. 94.
[319] Bonanno, J. (1977). Protection of minority shareholders in konzern under german and united states law. *The Harvard International Law Journal*. Volume 18, issue 1. P. 156.
[320] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

disadvantageous to the subsidiary and if so, which particular transaction and to what extent.[321] However, without flow of information, those who are the most affected by these transactions might never learn that their rights were violated and would not be able to prove it. Moreover, it is confidential information, therefore outside of shareholders it is difficult to access it.[322] Nevertheless, in legal reality the limited scope of a parent company's liability is a prevailing criticism of *de facto* groups.

*GmbHG* does not contain provisions that govern *de facto* group structure. The protection of *GmbH* subsidiaries in *de facto* group structure is developed by case law. Articles 311 – 318 of *AktG* for *de facto* group structure are not applicable for *GmbH* subsidiaries.[323] The *AktG de facto* group regime is not applicable because of significant differences between *AG* and *GmbH* regimes, i.e. even without contractual agreement in the *GmbH de facto* group the parent company has the right to issue binding instructions. Consequently, there is no need to transpose Articles 311 – 318 of *AktG* of *de facto* groups to legitimize a parent company's control and power over *GmbH* subsidiaries.[324] Capital maintenance provisions in Article 30 of *GmbHG* safeguard creditor protection. [325]

Until recently simple *de facto* groups (*einfache faktische Konzerne)* and qualified *de facto* groups (*qualifizierte faktische Konzerne)* were distinguished. In simple *de facto* groups the parent company occasionally interferes with management of subsidiaries and each detrimental direction can be separately identified and compensated. In qualified *de facto* groups the parent company interferes by centralized group management and prioritizes group's interests over subsidiaries.[326]

First developments in case law established that majority shareholders in simple *de facto* group structure have a duty to act in accordance with corporate good faith

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[321] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. P. 236-238.

[322] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 165.

[323] Bundesgerichtshof in Zivilsachen [BGHZ] Urteil vom 5 Juni 1975. (ITT).

[324] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. PP. 240 – 241.

[325] Act on Limited Liability Companies. Consolidated and published in the Federal Law Gazette III, Index No. 4123-1. Amended by Article 10 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[326] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. P. 243.

(*gesellschaftsrechtliche Treue).*[327] Corporate good faith forbids detrimental actions against the interest of the subsidiary and it can be applied up to the latter.[328] A subsidiary's board of directors is not obligated to fulfil directions from the parent company that are prejudiced to independent interests in *de facto* group structure. If the parent company violates corporate good faith, it is required to compensate for the damages or losses caused.[329]

Further, in case law it was determined that for qualified *de facto* groups specific contractual *AG* groups' rules can be applicable, such as Articles 302, 303 and 322 of *AktG*. Articles 311 – 318 of *AktG* of *de facto* groups still remain inapplicable to *GmbH* subsidiaries.[330] Thus any damages or losses caused to *GmbH* subsidiaries by the parent company in a qualified *de facto* group structure arising from the exercise of permanent and all – embracing control must be compensated. The obligation to compensate can be rebutted by convincing that a prudent businessman with due care would act exactly in given circumstances. [331]

Later in case law was vested the concept that dominant control over the *GmbH* subsidiary's financial policies without assertive management control is enough to label a *de facto* group structure as qualified. However, the parent company is not liable for losses or damages of *GmbH* subsidiaries that are not connected to exercised control or power. More recently in case law it was reasoned that the parent company's detrimental effect on *GmbH* subsidiaries should not be presumed in case of permanent and all – embracing control. The parent company is not required to prove that losses or damages have occurred unrelated to the exercise of power or control.[332]

In the light of all the foregoing, case law settled that there are no differentiating liability criteria for qualified *de facto* group and simple *de facto* group interest enactment and *GmbH* subsidiaries altogether are protected by a new concept of existence destroying encroachments (*Existenzvernichtende Eingriffe).* Existence destroying encroachments is present, if assets are withdrawn from *GmbH* subsidiary by the parent company and it provokes insolvency. [333] *AktG*

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[327] Schmidt,, K. (2002).*Gesellschaftsrecht*. 4. Auflage. Köln/Berlin/Bonn/München. Carl Heymanns Verlag KG. S. 1220.

[328] Stimpel, W. (1986). Die Rechtsprechung des Bundesgerichtshofes zur Innenhaftung des herrschenden Unternehmens im GmbH-Konzern. S. 118 – 120.

[329] Ulmer, P. (1986). "Gläubigerschutz im 'qualifizierten' faktischen GmbH-Konzern. Bemerkungen zum 'Autokran'- Urteil des BGH vom 16.9.1985. *Neue Juristische Wochenschrift (NJW)*. S. 412 und 1581.

[330] Schmidt, K. (1981). Abhängigkeit, faktischer Konzern, Nichtaktienkonzern und Divisionalisierung im Bericht der Unternehmensrechtskommission. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. S. 473. https://doi.org/10.1515/zgre.1981.10.3.455

[331] Lennarts, M.L. (1999) Concernaansprakelijkheid. Deventer. Kluwer Law. P. 77.

[332] Krieger, G. (1994). Kann die Praxis mit TBB leben? *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. S. 375 - 394. https://doi.org/10.1515/zgre.1994.23.3.375

[333] Bundesgerichtshof (BGH) Urteil vom 17 September 2001 (Bremer Vulkan). *Neue Juristische Wochenschrift (NJW)*, 54 (2001), 3622.

articles of formal group application to *de facto* qualified groups are replaced by the concept of existence destroying encroachments. Remaining is that permanent and all – embracing control by itself does not constitute liability (*Strukturhaftung).* The parent company can be liable only for wrongfully exercised power or control (*Verhaltenshaftung).*[334] The parent company has to show sufficient consideration (*angemessene Riicksicht)* for interests of the subsidiary *(Eigenbelange).*[335] Existence destroying encroachments is closely linked with capital maintenance rules of Articles 30 and 31 of *GmbHG.* If capital maintenance rules of *GmbHG* cannot provide an appropriate solution, the concept of existence destroying encroachments is applied.[336] Existence destroying encroachments are found in the doctrine of abuse of the corporate form of *GmbH* (*Mif3brauch der Rechtsform der GmbH).*[337]

In Portugal the subsidiary itself and its creditors in a subordination group is protected by: the parent company's direct and joint liability of the subsidiary's obligations (Article 501 of *CSC*); the duty of the parent company to compensate the annual losses suffered, whenever it cannot be recovered from reserves (Article 502 of *CSC*).[338] Article 501 of *CSC* provides automatic and direct protection based on management control, in which the parent company is liable for the subsidiary's debt irrespective of the amount, the origin, the accountability or legal nature. There is no requirement of direct cause between shareholder control and loses suffered of the company, which means that the parent company will be liable even for losses caused by circumstances outside of its influence. The guarantee of recovery of debts potentially can be extended to the group as a whole. Article 502 of *CSC* ensures financial solvency of a subsidiary in a subordination group.[339] Financial burden is shifted to the parent company. However, in determining the compensation the loss of profits should be taken into consideration.[340] Moreover, the parent company should exercise their duties and responsibilities in the subsidiary with the same diligence as in their own company (Article 504 of *CSC*) and in the subordination

[334] Schmidt,, K. (2002).Gesellschaftsrecht. 4. Auflage. Köln/Berlin/Bonn/München. Carl Heymanns Verlag KG. S. 1230.
[335] Alting, C. (1994). Piercing the Corporate Veil in American and German Law - Liability of Individuals and Entities: A Comparative View. *Tulsa Journal Comparative and International Law*. Volume 2, article 4. P. 801.
[336] Lutter, M., Hommelhoff, P. (1995). GmbH-Gesetz. Kommentar. 14. Auflage. Köln. Verlag Dr. Otto Schmidt. S. 307.
[337] Alting, C. (1994). Piercing the Corporate Veil in American and German Law - Liability of Individuals and Entities: A Comparative View. *Tulsa Journal Comparative and International Law.* Volume 2, article 4. P. 802.
[338] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[339] Manóvi, R. M. (2020). Groups of Companies: A Comparative Law Overview. Ius Comparatum - Global Studies in Comparative Law. Springer. P. 84.
[340] Azeredo Perdigao, M. (1995). Groups of companies in Portugal: a parent's liability for debts of its subsidiaries. *International Company and Commercial Law Review*. Volume 6, issue 4. Sweet & Maxwell. P. 4.

contract group the parent company cannot issue binding instructions of asset stripping (Article 503 of *CSC*).[341]

In Latvia *Koncernu likums* devotes a great significance to symmetry of information. Regarding transparency the duty to disclose information is ascertained. The notification in writing within 2 weeks is necessary, if: at least of 10 % of the stock or shares are acquired (Article 6, paragraph 1 of *Koncernu likums*); every 5 % increase (above 10 % mark) in the stock or shares (Article 6, paragraph 2 of *Koncernu likums)*; every 5 % decrease (above 10 % mark) of the stock or shares (Article 6, paragraph 3 of *Koncernu likums)*; in any case of decrease of total stocks or shares below 10 % (Article 6, paragraph 3 of of *Koncernu likums*); a person (natural or legal) holds the stock or shares for the benefit of another person (Article 6, paragraph 5 of *Koncernu likums*).[342] The notification of participation should also include voting rights attached to it. The transparency is achieved by reporting respective participation and the decisive influence in an Annual Financial Statement (Article 8, paragraph 1 of *Koncernu likums*) and by notifying the Enterprise Register of participation exceeding or decreasing below 10 %; 25 %; 50 %; 75 %; 90 % (Article 8, paragraph 2 of *Koncernu likums*).[343] A change in participation up to 25 % is of unimportant magnitude, therefore, a reasonable objection for unnecessary or impractical burden is argued.[344] Before entering a group of companies contract involved companies notify all respective (known) shareholders for intention to conclude the respective agreement. Article 11, paragraph 1 of *Koncernu likums* imposes this obligation[345]. In this article, as subjects of notification for intention of entering a group of companies' contracts are mentioned employees, though in the context of Latvian version of *Koncernu likums* it is translation error and should be applied for involved companies' shareholders. Whenever a group of companies' contract has not been entered into, the executive body of a subsidiary prepares a report on dependency, according to rules mentioned in Article 30 of *Koncernu likums.* A report on dependency shall represent an overview of relations between a

[341] Engracia Antunes, J. (2005). Law &(and) Economics Perspectives of Portuguese Corporation Law - System and Current Developments. *European Company and Financial Law Review*. Volume 2, Issue 3. P. 376. https://doi.org/10.1515/ecfr.2005.2.3.323

[342] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[343] Ibid.

[344] Strupišs, A. (2007). Koncernu likuma darbības efektivitātes problēmas un to iespējamie risinājumi. Pētījums pēc Tieslietu Ministrijas pasūtījuma. 10. lpp. Accessed 27 May 2024. Available at: https://www.tm.gov.lv/sites/tm/files/2020-01/Documents/lv_documents_petijumi_koncerni.pdf

[345] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

parent company and its subsidiary. In a report of dependency among other things should be included a notice of: whether the subsidiary has carried out any transactions in an interest of the parent company or the group; whether these transactions have been disadvantageous or detrimental to the subsidiary's interests; whether losses caused to the subsidiary have been compensated or reciprocal performance has been received in return.[346] The transparency in take – overs of company is achieved by notifying the Enterprise Register and publication in the official gazette " Latvijas Vēstnesis" (Article 35, paragraph 5 and 6 of *Koncernu likums;* Article 39, paragraph 1 of *Koncernu likums*).[347]

Creditors' interests' protection in a group of companies' structure is linked with preservation of subsidiary's own independent and autonomous interests. By virtue of the inability of *Komerclikums* as general company law to safeguard those interests, a separate framework for protection of creditors in a group of companies' structure has been established in *Koncernu likums*. Article 19 of *Koncernu likums* set the maximum amount transferable by a subsidiary to a parent company on the basis of an agreement on the transfer of profit contract. The maximum amount cannot exceed the profit of the reporting year prior to the transfer. As stated in Article 20, paragraph 1 of *Koncernu likums,* in a relationship of a group of companies contract a parent company has the duty to compensate losses incurred by a subsidiary in a reporting year, unless it can be indemnified from reserves (profit deduction). Losses of a subsidiary may be compensated only from those reserves, which are accumulated during the term of the group of companies' contract.[348] This is an obvious deviation from general company law principle of limitation of liability of the company settled in Article 137, paragraph 2 and 3 of *Komerclikums,* i.e. the company is not liable for the obligations of its shareholders and vice versa.[349]

The notion of losses in a reporting year is fitting for transfer of profits, but is in question for safeguarding other interests of subsidiary. Article 20, paragraph 1 of *Koncernu likums* is matching Article 302 of German *AktG*[350] and Article 502 of Portuguese *CSC*.[351] In Germany, it is determined that losses from withdrawing assets that value increases over time can stretch

[346] Ibid.
[347] Ibid.
[348] Ibid.
[349] Komerclikums. Pieņemts 13.04.2000. Stājies spēkā 01.01.2002. Publicēts: Latvijas Vēstnesis, 158/160, 04.05.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 11, 01.06.2000. Pēdējie grozījumi 01.08.2023.
[350] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[351] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

to multiple years, e.g. immovable property, participation in different companies, as well as profitable production plant.[352] According to the Portuguese (*CSC*) system, transfer – pricing, profit manipulation and use of subsidiary's facilities without payment are also considered as actions outside of the framework of the concept of losses in a reporting year.[353] It is concerning whether Article 20, paragraph 1 of *Koncernu likums* will cover losses from withdrawing assets and accounting manipulation.

According to Article 27, paragraph 5 of *Koncernu likums,* a creditor can raise a claim for losses suffered, insofar as satisfaction of his or her claim is not covered by the subsidiary, if a management contract or a management and transfer of profit contract has been entered into.[354] From the wording of Article 27, paragraph 5 of *Koncernu likums* it is not clear whether a creditor can claim losses suffered only from the parent company's lawful representatives or also from the parent company itself. Important consideration can be given to the argument that Article 27, paragraph 5 of *Koncernu likums* is under the section of liability of lawful representatives of a dominant undertaking (parent company). German Article 309, paragraph 4 of *AktG* is identical to Article 27, paragraph 5 of *Koncernu likums.*[355] In the German case law an extension of the creditor's right to directly satisfy claims for losses suffered against the parent company itself is established, based on Article 309, paragraph 4 of *AktG*.[356] Latvian lower court case law reflects an approach of limiting rights of subsidiary's creditors only to satisfaction of losses suffered from parent company's lawful representatives, therefore, excluding the parent company itself.[357] Recently, the Supreme Court has overturned lower court case law by referencing German legal literature of Article 309 of *AktG* and settling that creditors of a subsidiary can directly satisfy claims for losses suffered against the parent company itself.[358]

If a management contract has not been entered into, the parent company, in line with Article 33, paragraph 1of *Koncernu likums* has the duty to compensate or grant the relevant

[352] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P.104.
[353] Engrácia, Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 29.
[354] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[355] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[356] Bundesgerichtshof in Zivilsachen [BGHZ] Urteil vom 24 Juni 2002 – II ZR 300/00.
[357] Rīgas apgabaltiesas Civillietu tiesas kolēģijas 2013. gada 17. septembra spriedums lietā Nr. C04243706.
[358] Latvijas Republikas Senāta Civillietu departamenta 2022.gada 31.maija spriedums lietā Nr. C28208416, SKC-44/2022, ECLI:LV:AT:2022:0531.C28208416.28.S, 11.3. punkts.

right to claim compensation for losses caused for disadvantageous transactions (or any other disadvantageous measurers) within a reporting year. A parent company cannot circumvent previously mentioned obligation on grounds of suffered losses by the same transactions.[359] The difference with Article 20, paragraph 1 of *Koncernu likums* is that the scope of Article 33, paragraph 1 of *Koncernu likums* is narrowed down to disadvantageous transactions or other detrimental measures only. Disadvantageous transactions or other detrimental measures are not analogous to losses in Latvian Civil law.[360] The latest case law clarifies that any transaction, which reduces or endangers a property or a cash-flow is disadvantageous or other detrimental measure to a subsidiary. The burden of proof as to compatibility of transactions or other measures with the interests of a subsidiary liaises on a parent company. A creditor has to refer to the alleged disadvantageous or other detrimental measure to a subsidiary.[361] Furthermore, transaction's disadvantageous or detrimental impact can be determined at the time of conclusion and relevance may also be considered whether a third person would enter into such transaction despite disbalance between benefits and burdens.[362] Referring to transparency rules of Article 30 of *Koncernu likums,* in a report on dependency, disadvantageous transactions or any other detrimental measures should be singled out. However, Article 33 of *Koncernu likums* is identical to German Article 317 of AktG.[363] The same criticism of the German (*AktG*) model of subsidiary's interest protection in *de facto* group can also be applied to Article 33 of *Koncernu likums*. It is not always evident, whether a transaction or a measure will be detrimental, which explicit transaction and to what extent.[364] Moreover, it is confidential information, therefore, other than shareholders, it is difficult to access.[365] To counterbalance opacity of the report on dependency Article 31 of *Koncernu likums* constitute mandatory

[359] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[360] Grīnberga, I. (2020). Kreditoru interešu aizsardzība strīdos, kas izriet no koncernu tiesību pārkāpumiem. *Jurista Vārds*, Nr. 38(1148). 2. lpp.

[361] Latvijas Republikas Senāta Civillietu departamenta 2022.gada 31.maija spriedums lietā Nr. C28208416, SKC-44/2022, ECLI:LV:AT:2022:0531.C28208416.28.S, 12. punkts.

[362] Latvijas Republikas Senāta Civillietu departamenta 2022. gada 22. decembra spriedums lietā Nr. C32267917, SKC-94/2022, ECLI:LV:AT:2022:1222.C32267917.18.S , 12.1. punkts.

[363] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[364] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. S. 236 – 238.

[365] Böhlhoff, K., Budde, J. (1984). Company Groups – the EEC Proposal for Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany. *Journal of Comparative Business and Capital Market Law*. Volume 6. P. 165.

examination by an auditor.[366] In the case law it is settled that the auditor has to prepare written statement of the report on dependency compatibility with conditions stipulated in Article 31 of *Koncernu likums.* If incompatibility has been found it has to be explicitly stated in the statement.*[367]* It is controversial whether auditors will be capable of determining how a subsidiary ought to have behaved or acted because it is not in a competence of an auditor to asses management decisions.[368] The report on dependency together with annual financial statements is submitted to the Enterprise Register, which means the report on dependency is kept in the respective subsidiary's Enterprise Register case file.[369] The dependency report is not included in the list of restricted accessibility information.[370] By submitting a written statement of reason, creditors can receive the report of dependency. However, accessibility of the report of dependency can jeopardise group business strategy by exposing valuable information.[371] According to Article 33, paragraph 4 of *Koncernu likums*, even though a group of companies contract has not been entered into Article 27, paragraph 5 of *Koncernu likums* shall apply.[372] Nevertheless, Article 33, paragraph 3 of *Koncernu likums* precisely determines joint liability of parent company itself and its lawful representatives.[373]

In Spanish case law, it is confirmed that their commercial law has no rules governing the group of companies with separate legal personalities, which exercise unitary decision–making.[374] The court regards the controlled companies as being a source of a risk for creditors.[375] 2002 proposal for *PCSM*, which has not been enacted, recognised the management power to pursue the interest of the group and the obligation of the parent company to

[366] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[367] Latvijas Republikas Senāta Civillietu departamenta 2022. gada 21. decembra spriedums lietā Nr. C31344616, SKC-54/2022 ECLI:LV:AT:2022:1221.C31344616.14.S ,12.2. punkts.
[368] Farmery, P. (1986). The EC Draft Proposal For a Ninth Company Law Directive on Groups: A Business Viewpoint. *Business Law Review*. Volume 7, Issue 3. P. 89. https://doi.org/10.54648/bula1986030
[369] Strupišs, A. (2007). Koncernu likuma darbības efektivitātes problēmas un to iespējamie risinājumi. Pētījums pēc Tieslietu Ministrijas pasūtījuma. 13. lpp. Accessed 27 May 2024. Available at: https://www.tm.gov.lv/sites/tm/files/2020-01/Documents/lv_documents_petijumi_koncerni.pdf
[370] Latvijas Republikas Uzņēmumu reģistra galvenā valsts notāra 2021. gada rīkojums Nr. 1-7/68.
[371] Farmery, P. (1986). The EC Draft Proposal For a Ninth Company Law Directive on Groups: A Business Viewpoint. *Business Law Review*. Volume 7, Issue 3. P. 89. https://doi.org/10.54648/bula1986030
[372] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[373] Ibid.
[374] Sentencia del Tribunal Supremo - Sala Primera, de lo Civil, 29 de Abril de 1985. ECLI - ES:TS:1985:1018.
[375] Sentencia del Tribunal Supremo - Sala Primera, de lo Civil, 2 de Diciembre de 1988. Juicio declarativo ordinario de mayor cuantía.

compensate for damages caused was embodied. [376] In case of insolvency the parent company shall be held liable. The *PCSM* preferred to avoid distinguishing between the liability of the board of directors of the subsidiary and the parent company. Such accountability is based on the objective or the structure, therefore, is far from behavioural liability. The parent company would be liable to compensate the subsidiary's damages, whether it is a consequence of legitimate or illegitimate instruction. [377] Liability simply depends on connection to the group when the debt is incurred.[378] However, later in the case law was established that the pursue of the interest of the group does not exclude a liability of a board of directors for violating the duty of loyalty, if sufficient offsetting benefits has not been received. Given that there is no group of companies' specific codification, in the case law was expended the board of director's liability rather than direct liability of a parent company.[379]

In consideration of the foregoing, Member States' creditor protection systems that have implemented German *Konzernrecht* can be described as compensatory mechanism because all annual losses suffered by a subsidiary must be compensated by a parent company in - Germany Article 302 of *AktG*[380] as well as applicable to *GmbH* contractual groups, [381]in Latvia Article 20 of *Koncernu likums,*[382] in Portugal Article 502 of *CSC*[383] or cover losses for those transactions that are detrimental or disadvantageous in - Germany Article 317 of *AktG,*[384] in Latvia Article 33 of *Koncernu likums*.[385] Member States' creditor protection systems that have implemented French *Rozenblum* doctrine are more flexible and can be characterised as safe harbour for pursuing the interest of the group because financial equilibrium must be

[376] Girgado, P. (2006). Legislative Situation of Corporate Groups in Spanish Law. *European Company and Financial Law Review (ECFR)*. Volume 3, Issue 4. P 379. https://doi.org/10.1515/ECFR.2006.016
[377] Ibid.
[378] Embid Irujo, J.M. (2005). Trends and Realities in the Law of Corporate Groups. *European Business Organization Law Review (EBOR)*. Volume 6, Issue 1. P. 86. https://doi.org/10.1017/S1566752905000650
[379] Sentencia del Tribunal Supremo - Sala Primera, de lo Civil, 11 de Diciembre de 2015. STS 5151/2015 - ECLI:ES:TS:2015:5151
[380] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[381] Ulmer, P. (1986). Gläubigerschutz im 'qualifizierten' faktischen GmbH-Konzern. Bemerkungen zum 'Autokran'- Urteil des BGH vom 16.9.1985. Neue Juristische Wochenschrift (NJW). S. 1580.
[382] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[383] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[384] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[385] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

maintained,[386] insolvency cannot be triggered[387] or harm caused must be removed or protected against.[388] The compensatory mechanism protects explicitly creditor interests before insolvency, while in the *Rozenblum* doctrine creditor interest protection before insolvency is inferior and to the greater extent safeguarding of creditor interests is left in the framework of insolvency, tort or identification.

On the one hand, there is a common critique of compensatory mechanisms for creditor protection in a group of companies that compensation of all losses suffered is inappropriate since causal link between exercised control and losses suffered is not considered. This is also the reason why contractual or subordination groups are rare. Furthermore, covering losses for those transactions that are detrimental or disadvantageous are considered contention because it is not evident how to measure the effect of specific transaction. It can be concluded that group of companies' compensatory mechanism of creditor protection impose not only further substantial administrative burdens, but also extra cost. In Germany for *GmbH de facto* groups application of *AktG* creditor protection rules are rejected and different approach is applicable (sufficient consideration of subsidiary's interests and capital maintenance), as well as in Portugal *de facto* groups are excluded from compensatory mechanism. Italy in their creditor protection interest in a group of companies has combined elements of compensatory mechanism and safe harbour for pursuing the interest of the group. Italy supplements *Rozenblum* doctrine's requirement to preserve financial equilibrium by explicitly stating that suffered negative consequences must be compensated,[389] but to mitigate compensatory mechanism burdens damages can be compensated by the benefit of global results of pursuing the interests of the group.

On the other hand, the compensatory mechanism prescribes direct liability of a parent company, while *Rozenblum* doctrine yields only indirect liability, except in Italy the parent company is directly liable to creditors for pursuing the interest of the group. Moreover, compensatory mechanism Member States have additional transparency rules, e.g., dependency

[386] Guyon, Y. (2003). Droit des affaires. Droit commercial général et sociétés. Tome 1. 12ème édition. Paris. Economica. P. 670.
[387] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 218. https://doi.org/10.1515/ecfr-2013-0194
[388] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P. 261.
[389] Corapi, D., Benincasa D. (2019). The Law on Groups of Companies in Italy. *European Company Law*. Volume 16, Issue 4. P. 123 - 124. https://doi.org/10.54648/eucl2019018.

report in Germany Article 312 of *AktG*[390] and in Latvia Article 30 of *Koncernu likums;*[391] although Italy has implemented statutory *Rozenblum* doctrine and is considered a safe harbour, it has also introduced an annual report, according to Article 2497, paragraph 3 of *Codice Civile.*[392] These additional transparency rules should safeguard enforceability of direct liability towards creditors. Nevertheless, the issue of singling out a specific transaction, which is detrimental or disadvantageous, jeopardises reporting accuracy as well.

### 2.4. The minority shareholder protection

In France there is absence of supplementary protection for minority shareholders (i.e. not even conferred specific right of withdrawal in a group of companies) by merely relying on sound protection within the parent company depending on general company law regulations that assure prevention of abuse of subsidiaries. Ineptly, minority shareholders of subsidiaries are left to rely on general company law rules on misuse of majority by the parent company to protect themselves.[393] The common will of shareholders prevails over their distinct interests and forms specific interests – the corporate interest (the interest of the company).[394]

For the protection of their interests' minority shareholders depend on prohibition of abuse by the parent company. According to Article 1844 of *Code Civil des Français*, any shareholder has the right to take part in collective decisions.[395] However, the notion of abuse is of judicial origin.[396] The abuse of majority constitutes the decision, which is detrimental to general interests of the company and favours the majority over the minority. The intent to harm does not needed to be determined.[397] On grounds of civil liability of tort law stipulated in Article 1382 of *Code Civil des Français* minority shareholders can claim damages suffered

[390] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[391] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[392] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[393] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. PP. 157 and 161 – 162.
[394] Grelon, B. (2009). Shareholders' Lawsuits against the Management of Company and its Shareholders under French Law. *European Company and Financial Law Review (ECFR)*. Volume 6, issues 2 and 3. P. 206. https://doi.org/10.1515/ECFR.2009.205
[395] Code civil. Dernière mise à jour des données de ce code : 07 octobre 2022. Version en vigueur au 25 novembre 2022. Legifrance. English translation of cited Article: Crabb. J., H. (1995). The French Civil Code. Revised Edition (as amended to 1 July 1994). Kluwer Law and Taxation Publishers Deventer. P. 342.
[396] Grelon, B. (2009). Shareholders' Lawsuits against the Management of Company and its Shareholders under French Law. *European Company and Financial Law Review (ECFR)*. Volume 6, issues 2 and 3. P. 214. https://doi.org/10.1515/ECFR.2009.205
[397] Cour de Cassation, civile, Chambre commerciale, du 18 avril 1961, Publié au bulletin.

from the majority shareholder.[398] The abuse of majority is not limited to only shareholders' meeting, but all collective decisions are under the scope. The parent company can also abuse a subsidiary also by pursuing their own interests (group interest) and destroying equality between shareholders. The abuse of equality exists when there are shareholders with equal shares. Moreover, the abuse of equality occurs when the decision is detrimental to general interests of the company, prevents completion of transactions essential to the company and has the sole purpose of benefiting their own interests, despite the detrimental effect on company's interests. Minority shareholders in the case of the abuse of equality can also claim damages based on the civil liability of tort.[399] In general the articles of association regulate shareholders' rights, but relationship between shareholders further can be delineated with an agreement (shareholders' agreement). Minority shareholders for the violation of the shareholder agreement can seek termination of the agreement, compensation for damages or any other penalties and compulsory enforcement.[400] Moreover, minority shareholders in line with Article 1844-7 of *Code Civil des Français* may apply for the termination of the company on the grounds of either of disagreement between shareholders or non-performance of obligations by other shareholder.[401] The shareholder who is the cause of the dispute does not posses the right to the termination of the company; there must be a legitimate interest.[402] The termination of the company may not be ordered, if there are other solutions that can allow the continuity of normal corporate life.[403]

Minority shareholders can protect their interests also by bringing lawsuits against corporate bodies of company. Article L. 235-1 of *Code de commerce* provide that acts or deliberations can be only found null and void, if mandatory provisions are breached.[404] The lawsuit for claiming acts or deliberations being null and void can be introduced, even if claimant was not a shareholder at the time of respective act or decision or is no longer a shareholder, as long as a shareholder has vested interest in a company. When grounds for

[398] Code civil. Dernière mise à jour des données de ce code : 07 octobre 2022. Version en vigueur au 25 novembre 2022. Legifrance. English translation of cited Article: Crabb. J., H. (1995). The French Civil Code. Revised Edition (as amended to 1 July 1994). Kluwer Law and Taxation Publishers Deventer. P. 252.
[399] Cour de Cassation, Chambre commerciale, du 9 mars 1993, 91-14.685, Publié au bulletin.
[400] Grelon, B. (2009). Shareholders' Lawsuits against the Management of Company and its Shareholders under French Law. *European Company and Financial Law Review (ECFR)*. Volume 6, issues 2 and 3. P. 217. https://doi.org/10.1515/ECFR.2009.205
[401] Code civil. Dernière mise à jour des données de ce code : 07 octobre 2022. Version en vigueur au 25 novembre 2022. Legifrance. English translation of cited Article: Crabb. J., H. (1995). The French Civil Code. Revised Edition (as amended to 1 July 1994). Kluwer Law and Taxation Publishers Deventer. P. 344.
[402] Cour de Cassation, Chambre civile 1, du 25 avril 1990, 87-18.675, Publié au bulletin.
[403] Cour de Cassation, Chambre commerciale, du 13 février 1996, 93-16.238, Publié au bulletin.
[404] Code de commerce. Dernière modification le 26 février 2022. Document généré le 25 février 2022. Legifrance. English translation of cited Articles: Raworth P. (2006). The French Commercial Code in English. Oxford University Press. P. 258.

claiming that acts or deliberations are null and void disappears such lawsuit is no longer admissible, but lawsuit can be transformed to compensation for damages.[405] The interest of the company and the individual interests of the shareholder are distinct, therefore shareholder can claim damages suffered by the company or personal damages. A shareholder may introduce a claim for damages suffered by the company, if company itself has not raised a claim, 5% of registered capital is represented, as well maintains the status of shareholder during the course of proceedings.[406] Article 1843-5 of *Code Civil des Français* install that compensation for damages suffered by the company will benefit only respective company itself and a shareholder cannot not receive any compensation received by the company.[407] Consequently, shareholders prefer to bring personal lawsuits against corporate bodies of a company. In order to receive individual compensation from corporate bodies wrongdoing personal damages, which are separate from the one suffered by the company, must be proven. However, the case-law establishes that company's corporate body's wrongdoing often will have only an impact and harm on the general interests of the company.[408] For the reason of ineffectiveness to satisfy personal claims for damages minority shareholders has to lean on the dispute resolution between shareholders for their interest protection.

Minority shareholder protection has never received much attention in the Netherlands and *ad hoc* provisions do not systematically protect the interest of minority shareholders. Self-exercising exit rights of minority shareholders are not prescribed by Dutch law because all shareholders must be loyal to their company and to the interests pursued by this company. On an opposite note Article 2:201a(92a) of *BW* provides for the parent company to squeeze out the right of a small minority shareholder who holds 5 % or less of the issued capital.[409]

In Italy, Article 2497, paragraph 4 of *Codice Civile* institutes a right of exit for minority shareholders. Shareholders have a right of withdrawal when: the parent company implies changes, which directly alters the economic and financial conditions of the subsidiary; the

[405] Grelon, B. (2009). Shareholders' Lawsuits against the Management of Company and its Shareholders under French Law. *European Company and Financial Law Review (ECFR)*. Volume 6, issues 2 and 3. P. 211. https://doi.org/10.1515/ECFR.2009.205

[406] Private Limited Companies Article L. 223-22 of *Code de commerce*. Public Limited Companies Article L. 225-252 of *Code de commerce*. Partnership (*Société Civile*) Article 1850 of *Code Civil des Français*.

[407] Code civil. Dernière mise à jour des données de ce code : 07 octobre 2022. Version en vigueur au 25 novembre 2022. Legifrance. English translation of cited Article: Crabb. J., H. (1995). The French Civil Code. Revised Edition (as amended to 1 July 1994). Kluwer Law and Taxation Publishers Deventer. P. 342.

[408] Cour de Cassation, Chambre commerciale, du 1 avril 1997, 94-18.912, Inédit

[409] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Article: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P. 223.

parent company is liable for violation of Article 2497 of *Codice Civile* to shareholders; exercising of direction and coordination has begun or ended (if subsidiary is not listed company, alteration of the risk of the investment is no caused and take-over bid is not promoted).[410] For minority shareholders, it has made it easier and more convenient to exit the group.

In Germany, *AktG* prescribes that group minority shareholders are protected by the duty of loyalty, which determines that every shareholder has to act in the interests of the company and must always takes into consideration the interests of other shareholder interests.[411] In a contractual group the subsidiary does not solely act for its benefit, therefore, shareholders in a group of companies' structure are not fully bound by the duty of loyalty. However, Article 309, paragraph 1 prescribes that the parent company in a contractual group must exercise the diligence of an honest and conscientious manager, while exercising decisive influence. Interests of minority shareholders are additionally safeguarded by the compensation payment vested Article 304 of *AktG* and settlement payment is established in Article 305 of *AktG*. If a profit and loss absorption agreement is concluded, minority shareholders shall receive appropriate compensation (annually) proportionate to their shares. The compensation can be also in a form of a due share of the profit for stocks or shares of the parent company. Furthermore, the settlement payment provides the exit right for minority shareholders because, if a group contract has been entered into, minority shareholders have the right to request the parent company to acquire their shares for appropriate settlement payment. Similar to a compensation mechanism, a settlement payment can be also in a form of shares or stock of the parent company or money. In case of expulsion of minority shareholders of the subsidiary as the result of the integration cash settlement is granted.[412]

Required approval for a group of companies agreement by three -quarters of the share capital represented (Article 293 of *AktG*)[413] enables minority shareholders to organize themselves into an coalition of an opposition to oppose a proposed agreement and demand more favourable terms.[414] In case of not being able to block approval of the group of companies

[410] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[411] Hüffer, U. (1990). Zur gesellschaftsrechtlichen Treupflicht als richterrechtlicher Generalklausel. *Festschrift für Ernst Steindorff zum 70. Geburtstag am 13.* Boston: De Gruyter. P.59 https://doi.org/10.1515/9783110894431.59
[412] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[413] Ibid.
[414] Bonanno, J. (1977). Protection of minority shareholders in konzern under german and united states law. *The Harvard International Law Journal*. Volume 18, issue 1. P. 156.

agreement based on Article 243 of *AktG*, minority shareholders can challenge respective general meetings decisions on grounds that majority shareholders have abused the power to the detriment of the company.[415] However, since Article 304 of *AktG* provides compensation and Article 305 of *AktG* installs settlement payments, this remedy of case law is supplanted. Although Article 304 of *AktG* guarantees minority shareholders fair return on shares kept, upon lapse of the group of companies' contract minority shareholder's shares might be worthless because of company's financial well-being. For this reason relevance in minority shareholder protection have also Articles 300 - 302 of *AktG*, which safeguard financial position of a company, if a group of companies contract is concluded.[416] Article 309 of *AktG* not only establishes the liability of the board of directors for the damages caused to the subsidiary under the instructions of the parent company, but also permits each shareholder to raise a claim against the board of directors in a respective scenario. General company law does not recognise the right to raise a claim individually; though this right for shareholders has been implemented in *Konzernrecht* framework. Prior to adopting this right minority shareholders found themselves unable to effectively raise a claim against a subsidiary's board of directors.[417]

In a *de facto* group Article 311 of *AktG* provisions of the parent company's compensation to the subsidiary for disadvantageous transactions are not restricted only to management, but also are applicable to minority shareholders. Disadvantageous transaction can take the form of management and utilization of voting rights at general shareholder meeting.[418] Moreover, in line with Article 311 of *AktG*, the right to raise a claim against the parent company, if a compensation has not been received, has also extended to minority shareholders.[419]

In a *de facto* group issued instructions are not binding and a subsidiary does not suffer any uncompensated disadvantage from being in a group structure, hence minority shareholder interests are respected. The dependency report is the only additional protection for minority shareholders in *de facto* group. Article 312 of *AktG* construes that the dependency report sets out all transactions and measurers taken between the parent company and the subsidiary or in

[415] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[416] Würdinger, H. (1973). Aktien- und Konzernrecht : eine systemat. Karlsruhe : Müller. 3. Auflage. S. 268 und 286
[417] Bonanno, J. (1977). Protection of minority shareholders in konzern under german and united states law. *The Harvard International Law Journal*. Volume 18, issue 1. P. 158.
[418] Reinhard von Godin, R., von, Wilhelmi, H. (1967). Aktiengesetz vom 6. September 1965. De Gruyter. 3. Auflage. S. 1629.
[419] Bonanno, J. (1977). Protection of minority shareholders in konzern under german and united states law. *The Harvard International Law Journal*. Volume 18, issue 1. P. 159.

the interests of these companies, as well as the result of it and details about the compensation given to the subsidiary by the parent company. Articles of 313 and 314 of *AktG* state that the auditors and supervisory board examines the dependency report, which upholds the transparency.

In a *GmbH* group minority shareholders must rely for their interest protection on general company law principles of equal treatment (*Gleichbehandlungsgrundsatz*) and the duty of loyalty (*Treuepflicht*). The principle of equal treatment prohibits unequal treatment against the shareholder either by other shareholders or the company. In a group of companies setting, duty of loyalty checks whether the shareholder has abused his or her position to favour his or her own interests at the cost of the company. The absence of rules of safeguarding minority shareholders is based on the assumption that the articles of association should formulate respective norms and it is expected that minority shareholders would negotiate for themselves.[420] *GmbHG* provides elevated voting thresholds that favour minority shareholders: majority vote of 75% of votes for amending articles of association (Article 53, paragraph 2 of *GmbHG*), majority vote of 75% of votes for winding up the company (Article 60, paragraph 2 of *GmbHG*), no voting rights of shareholders in question of termination or initiation of a lawsuit against respective shareholder (Article 47, paragraph 4 of *GmbHG*), consent of all shareholders to increase obligations under the articles of association (Article 53, paragraph 3 of *GmbHG).*[421] Moreover, minority shareholders can exercise shareholder individual rights that every shareholder enjoys, regardless of their influence or shares. Under the individual rights of a shareholder are the right to information, the right of action against the resolution of shareholders and the right to raise the claim against other shareholders, as well as the withdrawal (the exit right) and the expulsion. The right to information has unrestricted character and can be only refused, if there is legitimate reason that information will be used in order to harm a company or other shareholders.[422] It is an important control instrument between minority shareholders and the parent company. The right of action against resolutions of shareholders are comprehensively regulated in Articles of 241 – 249 of *AktG;* however, these provisions by way of analogy are applied also to *GmbH.*[423] The minority shareholder can

[420] Detlef, K. (1993). Protection of minority shareholders under German law. *International Company and Commercial Law Review*. Volume 4, issue 4. Sweet & Maxwell. P. 4.
[421] Act on Limited Liability Companies. Consolidated and published in the Federal Law Gazette III, Index No. 4123-1. Amended by Article 10 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[422] Lutter, M. (1982). Zum Informationsrecht des Gesellschafters nach neuem GmbH-Recht. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. 11. Auflage. 1. Sonderheft. S. 6 und 8. https://doi.org/10.1515/zgre.1982.11.1.1
[423] Detlef, K. (1993). Protection of minority shareholders under German law. *International Company and Commercial Law Review.* Volume 4, issue 4. Sweet & Maxwell. P. 9.

exercise his right to raise the claim against another shareholder – the parent company without the consensus of the shareholder meeting, but does not have the right to raise a claim against the board of directors without approval of shareholder meeting, as well as submit a claim on behalf of the company without acceptance of shareholder meeting except, if the parent company has blocked the voting in the shareholder meeting against themselves.[424] The exercise of minority shareholder individual rights to raise a claim is limited by competence to shareholder meetings because of its supreme and dominant organ status in a company.

Remedies of the exit rights and the expulsion of shareholders have been developed in case law since Article 61 of *GmbHG* prescribed the dissolution of a company was considered too severe in the most situations. From a macroeconomics' perspective, continuity of a company is as important as minority shareholder protection.[425] Similar to *AktG* framework, a minority shareholder exercising exit rights in *GmbH* group seeks to withdraw from the company and to receive compensation based on the fair market value of his or her interest in the company. If circumstances and conditions of which a long-term relationship was entered have permanently and negatively changed, a shareholder must be able to terminate it by exercising the exit right.[426] Under the expulsion a violated shareholder is seeking to expel other shareholder or shareholders, which receives compensation based on the fair market value of his or her interest in the company. In an adverse manner, the expulsion focuses on removing opposing shareholders say in the company rather than safeguarding the will of the departing shareholder. Moreover, withdrawal offers the dissatisfied shareholder only monetary value of their shares, but forces severing participation in the company and leaves it to the remaining shareholders. To address the problem of a dissatisfied shareholder who wishes to continue to participate in the company, German case law introduced next to the exit right an additional remedy of expulsion. Expulsion of shareholder against its will has been controversial.[427] Nevertheless, over the time the expulsion of shareholder has been accepted as general right in GmbH.[428] In both remedies the standard of conduct expected from all shareholders and their behaviour is analysed.

The ground for exercising the exit right or expulsion of another shareholder or

[424] Grunewald, B. (1990). Die Gesellschafterklage in der Personengesellschaft und der GmbH. JZ-Schriftenreihe 2. Mohr Siebeck. S. 66.
[425] Rüster, B. (1984). Business Transactions in Germany. *International Journal of Legal Information*. Volume 12, Issue 3. P. 140. https://doi.org/10.1017/S0731126500017157
[426] Rowedder, H., (1985). Gesetz betreffend die Gesellschaften mit beschränkter Haftung: GmbHG. Vahlen-Verlag. München. S. 503.
[427] Scogin Jr., H.T. (1993). Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem". *Michigan Journal of International Law*. Volume 15, issue 1. P. 156.
[428] Baumbach, A., Hueck, A. (1985). GmbH – Gesetz. 14. Auflage. Beck. S. 362.

shareholders is *"wichtige Grund"* (substantial basis).[429] A substantial basis can be 1) personal reasons; 2) actions of other shareholders; 3) the situation of the company.[430] The substantial basis of personal reasons include (but not limited to) financial urgency, illness, relocation (especially abroad), as well as obstacles to fulfilment of shareholder duties.[431] The abuse of majority or permanent dispute with other shareholders are actions of other shareholders necessary for forming a substantial basis.[432] Moreover, the breach of the duty of loyalty provide ground for substantial basis of the actions of other shareholders. Change of the company's purpose, additional risk posed to shareholders, as well as undesirable financial return affect the situation in a company to the extent that it creates substantial basis. [433] Neither the exit nor the expulsion can be limited by the articles of association.[434]

For exit rights withdrawn shares can be assigned to a third party or the remaining shareholders, retired or acquired in the name of the company. The articles of association can specify a procedure. If none of stated persons can pay the fair market value of the withdrawn share, then the departing shareholder can request dissolution of the company.[435] Exit rights shareholders can negotiate within the company, but the expulsion of a shareholder is ultimately a court matter.[436] However, the company decides to expel a shareholder by supermajority vote (75%) in shareholders meeting.[437] The subject of expulsion cannot vote his or her shares. In this case notion that the shares inherits the right to vote is not upheld. Consequently, minority shareholders can expel majority shareholder.[438] If a court decides to expel a shareholder, it must be paid the fair value of shares. The means by which the expelled shareholder receives fair value of his or her shares are identical to the exit rights. Exactly like for the exit right, if the expelled shareholder is not paid in one of the ways specified, the alternative is dissolution of

[429] Scogin Jr., H.T. (1993). Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem". *Michigan Journal of International Law*. Volume 15, issue 1. P. 155.
[430] Baumbach, A., Hueck, A. (1985). GmbH – Gesetz. 14. Auflage. Beck. S. 369.
[431] Miller, S.K. (1997). Minority shareholder oppression in the private company in the European Community: a comparative analysis of the German, United Kingdom and French close corporation problem. *Cornell International Law Journal*. Volume 30. Cornell University. P. 397.
[432] Rowedder, H., (1985). Gesetz betreffend die Gesellschaften mit beschränkter Haftung: GmbHG. Vahlen-Verlag. München. S. 508.
[433] Miller, S.K. (1997). Minority shareholder oppression in the private company in the European Community: a comparative analysis of the German, United Kingdom and French close corporation problem. *Cornell International Law Journal*. Volume 30. Cornell University. P. 397.
[434] Baumbach, A., Hueck, A. (1985). GmbH – Gesetz. 14. Auflage. Beck. S. 370 – 371.
[435] Rowedder, H., (1985). Gesetz betreffend die Gesellschaften mit beschränkter Haftung: GmbHG. Vahlen-Verlag. München. S. 514.
[436] Soufleros, I. (1983). Ausschließung und Abfindung eines GmbH-Gesellschafters. Köln. S. 48 – 75.
[437] Baumbach, A., Hueck, A. (1985). GmbH – Gesetz. 14. Auflage. Beck. S. 370 – 371.
[438] Scogin Jr., H.T. (1993). Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem." *Michigan Journal of International Law*. Volume 15, issue 1. P. 157.

the company.[439] Regardless of the payment method chosen for lost shares, an expelled shareholder has to receive "full worth."[440] The full worth of a share is the market value, which third party would pay for it. However, it is complicated to determine full worth of market value because the company itself has to be evaluated first before the value of shares can be assigned. Earning potential assessment is favoured over the balance sheet calculation for determination of market value of a share. [441]

Given the well – known incapacity of traditional company law rules to cope with the issue of safeguarding all those who deeply rely on preservation of independence and autonomy of a company, the corresponding protection of minority shareholders was introduced in Portugal. First line of defence in participation (simple and mutual) relationship is the duty to disclose information of participation (Article 484 of *CSC*) and restrictions to acquire new shares or shares in other companies (Article 485, paragraph 2 of *CSC*). Article 485, paragraph 3 of *CSC* adds that restriction to acquire new shares or shares in another company are applicable to a company, which fulfils the duty to communicate at a later date. The sanction for failure to communicate is prohibition on exercise of the rights attached to shares or parts and liability of damages suffered (important note that acquisitions of shares or parts are still in force).[442] The legal sanctions prevent the parent company through mutual participation in subsidiary to distort internal balance of power in itself.[443]

In a domination relationship is the duty to disclose information of domination (Article 486, paragraph 3 of *CSC*), prohibition to acquire shares of the parent company (Article 487, paragraph 1 of *CSC)*[444] and various compensatory mechanisms that provide protection of the subsidiary itself and its minority shareholders.[445] Based on the Article 494, paragraph 1 of *CSC*, in a subordination contract group of companies minority shareholders have the right to: leave the subsidiarity by selling the shares by fixed payment or trade them for the parent company's shares; stay in the group, but receive guaranteed dividends.

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[439] Soufleros, I. (1983). Ausschließung und Abfindung eines GmbH-Gesellschafters. Köln. S. 130.
[440] Scogin Jr., H.T. (1993). Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem. " *Michigan Journal of International Law*. Volume 15, issue 1. P. 159.
[441] Rowedder, H., (1985). Gesetz betreffend die Gesellschaften mit beschränkter Haftung: GmbHG. Vahlen-Verlag. München. S. 514 – 516.
[442] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[443] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 8.
[444] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[445] Engrácia Antunes, J. (2008). The Law of Corporate Groups in Portugal. Institute for Law and Finance. Working paper series No. 84. P. 8.

In Latvia shareholders of a subsidiary, which are recognised by Article 22, paragraph 1 of *Koncernu likums,* are precluded from receiving minority shareholder status: " the other party" to a group of companies contract; the parent company of "the other party" to a group of companies contract; a shareholder who is associated with " the other party" to a group of companies contract, on the basis of a group of companies contract entered into; a shareholder who holds all shares or stock of "the other party" to a group of companies contract.[446] Interests of minority shareholders in a group of companies are balanced by indemnity, compensation (exit right) and redemption (buy out).

Rules on indemnity are stipulated in Article 23 of *Koncernu likums.* Minority shareholders shall receive appropriate indemnity annually, if a transfer of profit contract has been entered into. A minimum amount of indemnity is the average profit from shares or the stock, which is calculated from profit before the entering a group of companies' contract and further profit prospects. Indemnity payment may also be received as a due share of the profit for stocks or shares of the parent company.[447]

The compensation mechanism instituted in Article 24 of *Koncernu likums* provides minority shareholders the exit right, if a group of companies' contract has been entered into. Minority shareholders' have the right to demand acquisition of his or her shares or the stock for appropriate compensation. The obligation to acquire minority shareholders shares or the stock liaise on the "other party" of the group of companies contract or in other words, correspond to the parent company. Compensation may be in a form of: share or stock of the parent company or money.[448] Article 24 of *Koncernu likums* exit right of minority shareholders is indistinguishable from the settlement payment model vested in German Article 305 of *AktG*.[449] In reference to Article 12, paragraph 3 of *Koncernu likums,* for conclusion of a group of companies contract is required acceptance of three quarters of the equity capital represented at a subsidiary's shareholder's meeting, which means that minority shareholders role for negotiating appropriate compensation are confined.[450]

Nonetheless, minority shareholders can seek judicial review of determination of appropriate compensation, according to Article 24, paragraph 7 and 8 of *Koncernu likums,*

[446] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[447] Ibid.
[448] Ibid.
[449] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[450] Wymeersch, E. (1993). Groups of Companies in the EEC: A Survey Report to the European Commission on the Law relating to Corporate Groups in various Member States. Gruyter, Walter de & Co. P.103.

which balances the interests of the parties affected by the group of companies contract.[451] Moreover, determination of compensation for minority shareholders in the form of money in Article 24, paragraph 4 *Koncernu likums* has been scrutinized for not taking into account further profit prospects of the subsidiary as it is in Article 23, paragraph 3 of *Koncernu likums.* Assessment of profit prospects includes the margin of the subsidiary's future profits, which minority shareholders would be able to receive, if he or she had retained shares or the stock.[452] Precise indicators of the value of further profit prospects *prima facie* cannot be identified; it changes case-by-case.

Notwithstanding, exclusion of further profit prospects brings greater certainty. Reasonably potential financial gains are traded for legal certainty. Further, Article 23 of *Koncernu likums* rules on indemnity and Article 24 of *Koncernu likums* compensation mechanism have significant distinction in application scope. Rules on indemnity govern minority shareholders in circumstances, in which they remain in a participation position, while compensation mechanism regulates minority shareholder exit rights, i.e. withdrawal of participation in a company. This specific discrepancy is grounds for justifying separate settlement arrangements.

Moreover, minority shareholders of a subsidiary may request a buy out in line with Article 47 of *Koncernu likums*, if a parent company has acquired (directly or indirectly) 90 % of shares or a stock of a subsidiary, but is not carrying out take – over.[453] The buy out right is a substantial mechanism for minority shareholder protection because the parent company may choose not to implement the take over of subsidiary (although it has acquired at least 90 % of its shares or a stock) in order to avoid payment of redemption. There are no other remedies available to minority shareholders of the subsidiary to leave the group (assuming that there is not concluded the group of companies' contract).

In Spain minority shareholders of a group are protected by general rules of company law: 1) call a shareholder meeting or demand to include specific matter; 2) request the annual accounts of company are verified by auditors (even, if it is not mandatory); 3) challenge decisions of the board of directors; 4) raise a claim against the board of directors on behalf of

[451] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[452] Strupišs, A. (2007). Koncernu likuma darbības efektivitātes problēmas un to iespējamie risinājumi. Pētījums pēc Tieslietu Ministrijas pasūtījuma. 21. lpp. Accessed 27 May 2024. Available at: https://www.tm.gov.lv/sites/tm/files/2020-01/Documents/lv_documents_petijumi_koncerni.pdf

[453] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

the company; 5) oppose raising the claim against the board of directors.[454] A 2002 proposal for *PCSM*, which has not been enacted, provided exit rights as a protection mechanism for minority shareholders. The protection mechanism of granting periodical compensation was not considered. Interestingly enough, exit rights can be exercised within the 2-year period of forming the group. A different issue is for determining the "real value" of the minority shareholder's stake. According to the *PCSM*, the squeeze out right for the parent company is granted. The squeeze out right can be exercised if: the parent company owns 90% of the subsidiary's stake and the parent company has three quarters of votes in the subsidiary.[455] Exit and buy out rights would be applicable only for listed companies.[456]

All things considered, Member State minority shareholder protection can be categorised under three methods: 1) a restriction of a power of majority; 2) individual rights; 3) minority rights. If the interest of the group is not recognised, there will be no additional protection to minority shareholders in a group of companies based on the perception that the risk of violating company's autonomous interests is limited, i.e., minority shareholder interests stay intact. Nevertheless, this perception does not resemble truth that the subsidiary will find it difficult to bypass the parent company's instructions and minority shareholder interests can be negatively affected. If the interest of the group is not appropriately recognised minority shareholders are left to protect their interests with legal instruments that are not suited to be applied against pursuit of the interests of the group. There are also Member States e.g., France and Netherlands, which recognise the interests of the group, but still rely on general company law rules for minority shareholder protection. Shareholders duty of loyalty, prohibition of abuse and board of directors' due diligence are adaptable legal principles, which are flexible enough to be applicable in group of companies. However, the courts apply these principles carefully and prudently. Besides, exit rights, buy out rights and compensations for remaining in the group are out of the scope of respective principles. In contrary, German *Konzernrecht* provide a wide range of legal instruments (exit rights, compensation for staying in the group, buy out rights) for minority shareholder interest protection by establishing organised system of checks and balances.

[454] Barona, J., Concha, R. (2007). Report from Spain. Country Status Reports. *European Company Law*. Volume 4, Issue 5. P. 240. https://doi.org/10.54648/eucl2007057

[455] Girgado, P. (2006). Legislative Situation of Corporate Groups in Spanish Law. European Company and Financial Law Review (ECFR). Volume 3, Issue 4. PP. 380 - 381. https://doi.org/10.1515/ECFR.2006.016

[456] Embid Irujo, J.M. (2005). Trends and Realities in the Law of Corporate Groups. *European Business Organization Law Review (EBOR)*. Volume 6, Issue 1. P. 86. https://doi.org/10.1017/S1566752905000650

## 3. THE CONCEPT OF THE INTEREST OF THE GROUP AND ITS IMPACT ON THE INTERNAL MARKET

### 3.1. The cost of doing cross–border business and lack of enabling law of centralised management

In a cross-border group of companies each national law must be separately examined, therefore investments for founding or managing such establishments are higher. According to economic theory, the legislator should take on the burden of regulating a company's internal affairs in order to lower the transaction costs and establish the certainty.[457] The decrease of the cost of doing cross-border business activities would benefit Small and Medium Sized Enterprises (SMEs). While a large group of companies can bear the cost of operating in a legally fragmented market and sometimes even gaining benefit from it, SMEs might not always be able to do so.[458] SMEs are the backbone of the EU economy because they represent 99% of all business in the EU, employ around 100 million people and account for more than half of the EU's Gross domestic product (GDP).[459] The political agenda in the EU is to facilitate growth and innovation in SMEs.[460] It can be pointed out that small and medium businesses often operate through a group of companies.[461] Even large companies deter investments by SMEs.[462] Due to the increased cost of cross-border business activities, SMEs are losing their competitiveness against large groups of companies, despite their significant importance. It leads to a situation where SMEs sell their products and services cross-border, but have no resources to establish legal entities in respective Member States.[463] In practice only a small

[457] Hillmann, R., A. (1997). The Richness of Contract Law: An Analysis and Critique of Contemporary Theories of Contract Law. Springer Dordrecht. P. 226.
[458] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 195. https://doi.org/10.1515/ecfr-2013-0194
[459] European Commission. Entrepreneurship and small and medium-sized enterprises (SMEs). Accessed 27 May 2024. Available at: https://ec.europa.eu/growth/smes_en
[460] Neville, M., Sørensen, K. E. (2014). Promoting Entrepreneurship – The New Company Law Agenda. *European Business Organization Law Review (EBOR)*. Volume 15, Issue 4. P. 546. https://doi.org/10.1017/S156675291400127X
[461] Davies, P. L., Worthington S. (2012). Gower and Davies' Principles of Modern Company Law. 9th edition. Sweet & Maxwell. P. 244.
[462] Stolowy, N., Schrameck, S. (2011). The contribution of European law to national legislation governing business law. *Journal of Business Law*. Volume 6. Sweet & Maxwell. P. 623.
[463] Teichmann, C. (2015). Corporate Groups within the Legal Framework of the European Union: The Group-Related Aspects of the SUP Proposal and the EU Freedom of Establishment. *European Company and Financial Law Review (ECFR)*. Volume 12, Issue 2. P. 206. https://doi.org/10.1515/ecfr-2015-0202

number of SMES invests abroad,[464] and thus do not actively create a group of companies' structures. The EC has underlined that decreasing of the administrative burden would enhance Europe's economy, especially it would be beneficial for SMEs. For reduction of administrative burdens, a strong joint effort of the Member States and the EU is necessary. Administrative costs in the cross-border company law area are particularly high.[465] The recognition of the interests of the group would not only decrease the cost of cross-border activities, but also would encourage more effective contracting.[466]

The fact that there are no rules at the EU level of recognition of the interests of the group means that cross–border group of companies subsidiaries' and the parent company's directors have to operate in market with different approaches of protective measures, but without universal enabling law that would permit pursuit of the interest of the group, while maintaining each members' autonomous interests.[467] Even a Regulation of *SE,* which establishes supranational legal person, Articles 15 - 17 of the Preamble for group law refers to Member State's national law.[468] Without enabling law to pursue the interest of the group the parent company's board members are hesitant to coordinate cross–border group structure because, depending on Member State, for intragroup instructions they could be considered as *de facto* or shadow directors and trigger civil or criminal liability. A *de facto* director acts as director of a company although he or she has not properly been appointed as such. A shadow director is a natural or legal person whose instructions directors follow closely.[469] Considering the risk of liability and uncertainty (arising from different approaches), a parent company will more likely issue instructions to a subsidiary, which will maximise short - term profits of shareholders. If a parent company has a decisive influence (which it most often does), it is expected that the subsidiary's directors will follow instructions because otherwise it can result

[464] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. P. 2. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

[465] European Commission. (2007). COMMUNICATION FROM THE COMMISSION on a simplified business environment for companies in the areas of company law, accounting and auditing. COM(2007) 394 final. P. 2. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2007:0394:FIN:EN:PDF

[466] Hertig, G. McCahery, J. A. (2006). Optional Rather Than Mandatory EU Company Law: Framework and Specific Proposals. *European Company and Financial Law Review (ECFR)*. Volume 3, issue 4. P. 342. https://doi.org/10.1515/ECFR.2006.015

[467] Hommelhoff, P. (2012). Förder - und Schutzrecht für den faktischen GmbH - Konzern. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. S. 535. https://doi.org/10.1515/zgre-2012-0535

[468] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE). Adopted on 10 November 2001. Published in the Official Journal of the European Communities, L 294/, p. 1–21.

[469] The Informal Company Law Expert Group (ICLEG). (2016). Report on the recognition of the interest of the group. P. 29. http://dx.doi.org/10.2139/ssrn.2888863

in termination of their appointment.[470] A director's persistence of profit maximisation for shareholders can be detrimental for other company stakeholders, e.g., minority shareholders and creditors. The absence of EU intervention and prevailing social norms of the shareholder primacy encourages directors to pursue merely the interest of the parent company without considering the interests of the group, which stagnates long term sustainability and profitability of a subsidiary. The trend in the EU that directors' focus on short – term profit maximisation for shareholders, rather than long run sustainability and profitability of a company, is continuing to ascend.[471]

Normally, members of the group (legal entities) manage their liquidity autonomously, i.e., have its own bank account and obtain separately credit from the bank, if necessary. This approach is significantly disadvantageous for both the group and autonomous interests of each member of the group because each company pays separately interests on its liability and deposits. To maximize internal funds and decrease the cost the parent company manages the liquidity of the group, but it requires setting up costly and complex infrastructure (e.g., establishing an in-house bank or a treasury management company). However, there is more efficient financial innovation from entering into an inter-company agreement with a bank, in which a group of companies' funds are pooled together and there is created an intra-group position for applying fees and calculating interests (decreasing transaction costs). Additionally, in cash pooling, sometimes also called cash management all companies can jointly negotiate terms and conditions of funding, surplus of funds of members of the group can be aggregated to compensate for the shortages of other members of the group, movement of internal funds is faster than in a traditional system of money transfers, as well as a single electronic platform shows total liquidity of a group and its members. In cash pooling transactional accounts for operations of members of the group and a top or a master account are created, which constitutes obligations to the bank and beneficiaries. Transaction accounts track only members of the group individual positions for internal accounting. The cash pooling might require actual bank transfers, but can also be virtual consolidation.[472] Also from the perspective of a bank there are advantageous to cash pooling agreements, despite reduced interest rates and fees. The cash

[470] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19

[471] European Commission. (2020). Study on director's duties and sustainable corporate governance. Final Report. PP. 61 and 62. Accessed 27 May 2024. Available at: https://op.europa.eu/en/publication-detail/-/publication/e47928a2-d20b-11ea-adf7-01aa75ed71a1/language-en

[472] Colangelo, A. (2016). The statistical classification of cash pooling activities. European Central Bank. Statistics Paper Series. Number 16. PP. 7-9.

pooling reduces the lending risk, gives oversight of client's turnover and limits the outflow of funds to other banks. The downside of a subsidiary for participating in cash pooling is that credit might be extended to a company into financial difficulties or in developing a new product or service, which will take away business from the others.

Cash pooling is very common in Northern and Western European countries, especially in, France and Netherlands. These services are not limited only to Large Sized Enterprises (LSE), but in principle, these companies are the most active to participate in such arrangements.[473] The cash pooling arrangements are not regulated at the EU and is left to Member States to individually deal with it. For this reason, cross-border cash pooling complexity (risks) is increased.[474] How cumbersome is to balance participation in cash pooling depends on recognition of the interest of the group. On the one hand, according to *Rozenblum* doctrine, in France cash pooling within the group does not contradict the interests of a subsidiary[475] and even special provisions have been amended, which prohibited that such services can be offered only by banks.[476] In Netherlands, cash pooling is a relevant phenomenon because cross- financing and cross- collateralisation between companies in the same group is legally accepted, as long as it is disclosed with the Commercial Register and these arrangements do not threaten financial solvency of companies that have contributed in cash pooling.[477] On the other hand, in Germany case law has found that in cash pooling arrangements a company's registered equity can be transferred to the insolvent member of the group and such action raises unlimited personal liability of the board of directors.[478] However, in contractual *AktG* group the parent company compensate all losses suffered and to facilitate respective group's structure to participation in cash pooling, amendments to *AktG* where introduced, which exempt subsidiary's capital from capital maintenance restrictions (Article 57 of *AktG* and Article 291, paragraph 3 of *AktG*).[479] The SUP Directive proposal does not recognise the interests of the group and Article 18 of the SUP Directive proposal provide

[473] Ibid, P. 5.
[474] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19
[475] The Organisation for Economic Co-operation and Development (OECD). (2012). Related Party Transactions and Minority Shareholder Rights. OECD Publishing. P. 68. http://dx.doi.org/10.1787/9789264168008-en
[476] Code monétaire et financier. Version en vigueur depuis le 22 février 2014. Création Ordonnance n°2014-158 du 20 février 2014 - art. 3. Legifrance. Article L511-73.
[477] Schuit, S. R., Bier B., Verburg L. G., Wisch J. A. T. (2002). Corporate Law and Practice of the Netherlands. Kluwar Law International. P. 98.
[478] Bundesgerichtshof (BGH) Urteil vom 16 Januar 2006 - II ZR 75/04.
[479] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

merely for payments to be assessed according to the balance sheet test (liabilities cannot exceed assets) and an insolvency test (payment cannot result in inability to pay debt), which means that Member State national law will be applicable and access to cross-border cash pooling systems will be difficult.[480] Without universal enabling law, which would permit pursue the interest of the group, cross-border cash pooling is challenging.

### 3.2. The freedom of choice between branch and subsidiary

Article 26 (2) of the TFEU ensures that the Internal Market is not confined by internal frontiers and there is free movement of goods, persons, services and capital.[481] The cross–border activity is extended to permanent establishments in other Member States. Article 49 of the TFEU, provides that the freedom of establishment grants the right to set up and manage undertakings, in particular companies or firms.[482] Set up and management of subsidiaries and branches are directly highlighted, thus the freedom of establishment also institutes the freedom of choice between a branch and a subsidiary.

Furthermore, Article 54 of the TFEU, which installs the concept that all companies and firms should be treated in the same way as natural persons who are nationals of Member States, governs Article 49 of the TFEU.[483] The EU treaty protects the formation of cross-border group of companies. There is no legal preference of branch or subsidiary group of companies' structure; Articles 49 and 54 of the TFEU uniformly protect all forms of group of companies' structures.[484] The CJEU has determined that the freedom of establishment grants the right to traders to freely choose the appropriate legal form in which to pursue their activities in another Member State.[485] In line with Article 120 of the TFEU, the freedom of establishment bestows the right to economic operators to choose different forms and degrees of integration, which facilitates efficient allocation of resources or, in other words, fully benefits from the scale of the economy of the Internal Market.

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[480] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. P. 2. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

[481] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal C 326, 26/10/2012 P. 0001 – 0390.

[482] Ibid.

[483] Ibid.

[484] Teichmann, C. (2015). Corporate Groups within the Legal Framework of the European Union: The Group-Related Aspects of the SUP Proposal and the EU Freedom of Establishment. *European Company and Financial Law Review (ECFR)*. Volume 12, Issue 2. P. 215. https://doi.org/10.1515/ecfr-2015-0202

[485] Judgment of the Court of Justice of the European Union of 28 January 1986 in the case 270/83, Commission of the European Communities v French Republic, paragraph 3.

The distinction between establishment of a branch or of a subsidiary has various significant differences. A branch has no independent legal personality from its parent company and it is merely a limb of it, thus, its legal status is governed by the legal system to which the parent company is subject. On the opposite note, a subsidiary has independent legal personality from its parent company, can be an autonomous party to a contract, settles its own debts, therefore, acts as a protective screen between creditors and a parent company.[486] Setting up or management of subsidiaries goes beyond mere capital investment within the meaning free movement of capital settled in Article 63 of TFEU.[487] However, a branch is a less costly establishment and easier to manage.[488] As a result of a legally fragmented market of recognition of the interest of the group, the parent company might be forced to open a branch rather than a subsidiary in order to minimize costs and support the board of directors' actions in the interest of the group. Respective legal fragmentation in Member State national systems shifts parent company's decision making from "real" economic benefits and costs towards aspects of company law, i.e., pursuit of the interests of the group.

The fact there are certain advantages in setting up branches does not mean *per se* that is commercially advisable. As a matter of fact more recent studies shows the cost of registering and managing a branch and limited liability subsidiary has no significant difference.[489] Moreover, founding of a branch can genuinely mean dealing with two legal systems at once because there is no clear dividing line between applicability of rules of the host state and company law of the state of incorporation.[490] The EC even has acknowledged that an establishment of a branch does not overcome lack of trust in foreign companies among customers and business partners. Founding of a subsidiary in another Member State has the advantage of using the parent company's brand or reputation, whilst also customers and partners can deal with a familiar legal status.[491] A subsidiary's legal form offers additional benefits of limited liability. Limited liability promotes economic activity because entrepreneurs

[486] Opinion of Advocate General LA PERGOLA delivered on 16 July 1998 in the case C-212/97, Centros Ltd v Erhvervs- og Selskabsstyrelsen, paragraph 15.
[487] Everling, U. (1963). Das Niederlassungsrecht im Gemeinsamen Markt. Berlin: F. Vahlen. S. 18.
[488]Meyer-Marsilius, H. J. (1960). Das Niederlassungsrecht in der Europäischen Wirtschaftsgemeinschaft. Baden-Baden/Bonn: August Lutzeyer. S. 37.
[489] Becht, M., Enriques, L., Korom, V. (2009). Centros and the Cost of Branching. *Journal of Corporate Law Studies*. Volume 9, Issue 1. P. 171. https://doi.org/10.1017/CBO9780511770456.006
[490] Teichmann, C. (2012). The Downside of being a Letterbox Company. *European Company Law*. Volume 9, Issue 3. P. 180. https://doi.org/10.54648/eucl2012028
[491] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. P. 2. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

are willing to take risks.[492] Efficiency of the group of companies depends on flexible and sophisticated management that provides an optimal combination of local autonomy and central control.[493]

According to settled case-law of the CJEU, all national measurers that render less attractive or prohibit the exercise of the freedom of establishment must be regarded as restrictions,[494] even if of limited scope or minor importance,[495] as well as hindering can occur also in the country of origin[496] or has to limit market access of the host Member State.[497] All things considered, the freedom of establishment has no horizontal effect, therefore, measurers adopted by private parties have no burden on the free movement.[498] In the context of the recognition of the interests of the group, foreign companies cross-border establishment is less attractive merely because of Member State system incompatibility and apply without the distinction between local and foreign companies. Besides, recognition of the interests of the group does not derogate from ordinary group law; it is important part of it. It is not contrary to the freedom of establishment that a Member State legitimately advance group of companies regulations.[499] Member States can define territorial extent of their group laws,[500] but under the freedom of establishment, companies and firms (independent and group structure) are to be acknowledged as creatures of national legislation and exists only by virtue of respective national law, which has jurisdiction over formation, power, structure, liabilities, dissolution etc.[501] As long as Member State practices of recognition of the interests of the group do not seek to safeguard the same interests that are governed by different Member State legal frameworks, no restrictions can be detected. The legal fragmentation in Member State practices

[492] Easterbrook, F., H., Fischel, D., R. (1985). Limited Liability and the Corporation. *University of Chicago Law Review*. Volume 52, Issue 1, Article 3. P. 89.
[493] Reflection Group on the future of EU company law. (2011). Report of the Reflection Group on the Future of EU Company Law ('Reflection Group Report'). P 59. Accessed 27 May 2024. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1851654
[494] Judgement of The COURT (Grand Chamber) 5 October 2004 in the case C-442/02, Caixa-Bank France v Ministère de l'Économie, des Finances et de l'Industrie, paragraph 11.
[495] Judgement of THE COURT (Fifth Chamber) 11 March 2004 in the case C-9/02, Hughes de Lasteyrie du Saillant v. Ministère de l'Économie, des Finances et de l'Industrie, paragraph 43.
[496] Judgment of the Court 27 September 1988 in the case 81/87, The Queen vs. H.M. Treasury and Commissioners of Inland Revenue ex parte Daily Mail and General Trust PLC (Daily Mail case), paragraph 16.
[497] Judgment of The Court of 24 November 1993 in joined cases C-267/91 and C-268/91, Bernard Keck and Daniel Mithouard, paragraph 17.
[498] Judgment of the Court (First Chamber) of 8 July 2010 in the case C-171/08, European Commission v Portuguese Republic, paragraphs 51-56.
[499] Judgement of the court (Ninth Chamber) of 20 June 2013 in the case C-186/12, Impacto Azul Lda, paragraph 35.
[500] Judgment of the Court of 30 September 2003 in the case C-167/01, Kamer van Koophandel en Fabrieken voor Amsterdam v Inspire Art Ltd. (Inspire Art case), paragraph 143.
[501] Judgment of the Court (Third Chamber) of 12 July 2012 in the case C-378/10, VALE Építési kft, paragraph 27.

of recognition of the interest of the group does not favour branches or discriminate subsidiaries by being too remote or indirect; though legal fragmentation impedes efficient allocation of resources of economic operators, which leads to inferior availability of services and goods in the Internal Market.

### 3.3. Regulatory competition

Laws can be seen as products, which states supply through law making process and consumers of the law (natural and legal persons) create the demand.[502] Regulatory competition occurs when states' national legal systems compete to attract more subjects to its jurisdiction. The prerequisites for regulatory competition to take place are natural persons' or legal persons' regulatory arbitrage and states' have to gain something by participating in it or lose something by avoiding it.[503] This presupposes that states have the competence to respond to shifts in demand by amending its laws.[504]

The CJEU in the *Centros* case ruled that based on the freedom of establishment a national of a Member State has the right to freely set up and manage an agency, subsidiary or branch in a Member State with the least restrictive company law rules.[505] Further, in the *Überseering* case CJEU decided that precondition of exercise of freedom of establishment is recognition of companies' legal status of other Member States.[506] Disintegrated recognition of the interest of the group and CJEU case law promotes regulatory arbitrage in respective fields. The TFEU, being in line with the principle of conferral, gives no general competence to the EU to regulate company law in its entirety, which allows Member States to respond to shifts in demand by amending its company laws.

Regulatory competition can create an uneven level of playing field where companies are in a better position in the market because of governing corporate rules rather than their product or service competitiveness.[507] For a group of companies it means that the parent company and its subsidiaries gain advantage over other competitors (groups of companies)

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[502] Cheffins, B., R. (2000). Company Law: Theory, Structure and Operation. Oxford University Press. P. 426.
[503] Armour, J. (2005). Who Should Make Corporate Law. EC Legislation versus Regulatory Competition. European Corporate Governance Institute (ECGI). Working Paper Nº. 54/2005. PP. 8-10. http://dx.doi.org/10.2139/ssrn.860444
[504] Cheffins, B., R. (2000). Company Law: Theory, Structure and Operation. Oxford University Press. P. 426.
[505] Judgment of the Court of Justice of the European Union of 9 March 1999 in the case C - 212/97, Centro Ltd v Erhvervs-og Selskabsstyrelsen (Centros case), paragraph 27.
[506] Judgment of the Court of Justice of the European Union of 5 November 2002 in the case C - 208/00, Überseering BV v Nordic Construction Company Baumanagement GmbH (NCC) (Überseering), paragraph 59.
[507] Enriques, L., Gatti, M. (2006). The Uneasy Case for Top-Down Corporate Law Harmonization in the European Union. *University of Pennsylvania Journal of International Economic Law*. Volume 27. P. 966. Accessed 27 May 2024. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=879804

because Member States where they are incorporated recognise the interest of the group and provide flexible (centralised) management. It is a problem, only if companies are not free to choose their corporate law and relocation is costly.[508] As previously stated, SMEs cannot bear the cost of operating in a legally fragmented market of recognition of the interest of the group and the freedom of the choice between a branch and a subsidiary is distorted, thus the outcome of regulatory competition is uneven. Moreover, regulatory competition in recognition of the interest of the group can lead to a race to the top, i.e., the removal of ineffective rules or a race to the bottom, i.e., the trade – off of public interests (e.g., weaken creditor and minority shareholder protection) to achieve more investments.

Market failure and inability of Member States individually to correct it enhance race to the bottom of regulatory competition.[509] Based on findings in prior sections, there is clear evidence of obstacles to efficient allocation of resources, increased costs of cross-border business activities that cannot be justified by Member State differences in constitution of civil society and social justice, which are sufficient grounds for acknowledgment of market failure of recognition of the interest of the group at the EU level. Respective issue has a cross-border element that cannot be sufficiently settled at Member States' national level. Consequently, it can be concluded that there are factors that facilitate race to the bottom of regulatory competition of the recognition of the interest of the group. Regulatory competition will never achieve uniformity in the area of a need for a single set of rules.[510] This imperfection prevents the Internal Market from arriving at an optimal allocation.

Regulatory competition in the recognition of the interest of the group can also have the effect of race to the top for Member States that do not have such legislation or case law or wish to advance their legal system, but have no knowledge as to the "best" type of regulation. Under such conditions regulatory competition can inspire innovations,[511] e.g., Latvian group of companies' law *Koncernu likums* regulatory basis is the German *Konzernrecht,* Portuguese group of companies' law (*sociedades coligadas*) is also based on the German *Konzernrecht,* Italy has introduced statutory *Rozenblum* doctrine (French system), Netherlands' case law also upholds *Rozenblum* doctrine (French case law). The wider the scope of legal mechanisms, from which solutions can be chosen, the more likely the Internal Market can achieve dynamic

[508] Ibid.
[509] Ibid, P. 957.
[510] Ibid, P. 976.
[511] Armour, J. (2005). Who Should Make Corporate Law. EC Legislation versus Regulatory Competition. European Corporate Governance Institute (ECGI). Working Paper Nº. 54/2005. P.11. http://dx.doi.org/10.2139/ssrn.860444

efficiency – ability to rapidly adapt under constantly changing conditions.[512] It is important to highlight that race to the top happens only on adoption of respective law or case law. Furthermore, the idea that regulatory competition can promote innovations is criticised for being overestimated because new products (legal mechanisms) are not formed, but merely reproduced in other Member State rules,[513] e.g., the Latvian group of companies' law *Koncernu likums* in fact is translated German *Konzernrecht* in the Latvian language.

In consideration of all foregoing and substantial tension to protect public interests,[514] Member States participate in regulatory competition as a defensive mechanism, which means that Member States are not seeking to increase re-incorporation in their jurisdiction, but intend to merely retain all establishments of a group of companies in their jurisdiction.[515] Indeed even with strong legal guarantees of free movement and freedom of establishment cultural, linguistic or other practical barriers exist. The parent company more likely will adapt to particular governance requirements than re-incorporate under a different set of rules[516] because there is no significant switching cost to different exercises of control. The path-dependencies and historical rooted trajectories of development of Member States have stagnated the progress of the recognition of the interest of the group. The regulatory competition by itself without regulatory intervention at the EU level will not solve this stagnation problem.

### 3.4. Abuse of rights

The freedom of establishment facilitates regulatory arbitrage, but also can be abused. Regulatory arbitrage is defined as the conduct, by which economic operators exploit cross-border activities in order to take advantage of Member State regulatory differences.[517] Differences in concerns between the interest of the group and the interest of the subsidiary, as

[512] Deakin, S. (1999). Two Types of Regulatory Competition: Competitive Federalism versus Reflexive Harmonisation. Law and Economic Perspective on Centros. *Cambridge Yearbook of European Legal Studies*. Volume 2. P. 242. https://doi.org/10.5235/152888712802815806

[513] Enriques, L., Gatti, M. (2006). The Uneasy Case for Top-Down Corporate Law Harmonization in the European Union. *University of Pennsylvania Journal of International Economic Law*. Volume 27. P. 976. Accessed 27 May 2024. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=879804

[514] Van den Bergh, R. (1994). The Subsidiarity Principle in European Community Law: Some Insights from Law and Economics. *Maastricht Journal of European and Comparative Law*. Volume 1, Issue 4. P. 346. https://doi.org/10.1177/1023263X9400100402

[515] Enriques, L., Gatti, M. (2006). The Uneasy Case for Top-Down Corporate Law Harmonization in the European Union. *University of Pennsylvania Journal of International Economic Law*. Volume 27. P 953. Accessed 27 May 2024. Available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=879804

[516] Armour, J. (2005). Who Should Make Corporate Law. EC Legislation versus Regulatory Competition. European Corporate Governance Institute (ECGI). Working Paper Nº. 54/2005. PP. 17 and 18. http://dx.doi.org/10.2139/ssrn.860444

[517] Schammo, P. (2008). Arbitrage and Abuse of Rights in the EC Legal System. European Law Journal. Volume 14, Issue 3. P. 353. https://doi.org/10.1111/j.1468-0386.2008.00417.x

well as prescribed limited liability are susceptible to abuse by the parent company. The risk of abuse of rights in a group of companies is high.[518] The CJEU case law distinctly safeguards regulatory arbitrage (even in legally fragmented fields such as company law), but the EU law cannot be exploited for abusive or fraudulent ends.[519]

The prohibition of abuse of rights is a general EU law principle.[520] However, the EU law is concerned only with safeguarding the Internal Market from cross–border situations that discriminate, restrict or otherwise hinders market participants' rights to act freely. Based on the settled CJEU case law, the freedom of establishment does not apply to situations where all the elements are confined within one single Member State.[521] This means that in a group of companies' structure abuse of EU law rights can transpire only, if a parent company and a subsidiary are registered in different Member States.

The CJEU in the *Centros* case concluded that abuse of the freedom of establishment can be fraudulently or improperly take advantage of provisions of the EU law or result in circumvention of national legislation, based on the rights conferred by the Treaty.[522] In the *Emsland-Stärke* case the CJEU clarified that abuse of EU rights must fulfil two conditions. First condition is an objective circumstance, in which the purpose of EU law rules has not been met. The second condition is a subjective element, in which artificial conditions are created in order to obtain an advantage from EU law provisions.[523] Later CJEU case law found that according to the subjective element a conduct has to represent genuine economic activity otherwise it is fictitious establishment or a wholly artificial arrangement.[524]

The abuse of rights in pursuing the interest of the group can be in the form of legitimate control by exercising the right to give instructions and also indirectly affecting decision-making process by limiting the power of subsidiary's board of directors to act autonomously, e.g., for specific operations articles of associations require written consent by general meeting of

[518] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 222. https://doi.org/10.1515/ecfr-2013-0194

[519] Judgment of the Court of 12 May 1998 in the case C-367/96, Alexandros Kefalas and Others v Elliniko Dimosio (Greek State) and Organismos Oikonomikis Anasygkrotisis Epicheiriseon AE (OAE), paragraph 20.

[520] Judgment of the Court (First Chamber) of 5 July 2007 in the case C-321/05, Hans Markus Kofoed v Skatteministeriet, paragraph 38.

[521] Judgment of the Court (Sixth Chamber) of 30 November 1995 in the case C-134/94, Esso Española SA v Comunidad Autónoma de Canarias, paragraph 17.

[522] Judgment of the Court of Justice of the European Union of 9 March 1999 in the case C - 212/97, Centro Ltd v Erhvervs-og Selskabsstyrelsen (Centro case), paragraph 24.

[523] Judgment of the Court of 14 December 2000 in the case C-110/99, Emsland-Stärke GmbH v Hauptzollamt Hamburg-Jonas (Emsland-Stärke case), paragraphs 52 and 53.

[524] Judgment of the Court (Grand Chamber) of 2 May 2006 in the case C - 341/04, Eurofood IFSC Ltd. (Eurofood case), paragraphs 64-71.

shareholders, removal and appointment of board of directors, or extending and discontinuing financial obligations. Creditors', minority shareholders' and other stakeholders' interest protection rely on safeguarding of the subsidiary's autonomous interests in profit and sustainability. Profit shifting, withdrawal of assets and agency problems (self-dealing), which can be carried out in both forms of abuse of rights, disturb a subsidiary's profitability and sustainability that further threatens the interests of creditors, minority shareholders and other stakeholders.

The parent company, as any other rational investor, before setting up a subsidiary or a branch will consider advantages of respective jurisdiction, e.g. rules on capital requirements, capital protection, the internal regulation of the company, conflict of interest resolution etc. The scope of the freedom of establishment provides merely the right to choose not the content of the applicable rules. Based on the applicable rules profit shifting, withdrawal of assets, agency problems or any other abuse of pursuing the interest of the group is carried out. If an exercise of the right of the EU law falls within the scope of the purpose and aim of it, there is no abuse of the EU law because it is a legitimate exercise of rights conferred. Profit shifting, withdrawal of assets and agency problems (self-dealing) does not take place for the purpose of circumventing the parent company's applicable rules, but rather to enjoy subsidiary governing jurisdictions' favourable regulations. Enjoying the benefit of more favourable legislation of a Member State does not constitute abuse of EU law rights.[525] In other abuses of rights in pursuing the interest of the group the parent company can try to set up a subsidiary to circumvent regulations of its applicable rules, therefore abusing the EU law, e.g., avoiding distribution of dividends in a subsidiary in order to avert profit transfer to a parent company. Nonetheless, the CJEU in the *Centros* case sets forth that abuse of the EU law has to be determined on case-by-case conditions.[526] Concerning a subsidiary becoming a fictitious establishment or a wholly artificial arrangement, it should be noted that in a group of companies a parent company is more interested in the extent to which a majority is able to exercise control rather than limiting the risk of liability for misbehaviour. Existence of risks does not challenge a group of companies' legitimacy.[527]

[525] Judgment of the Court of 30 September 2003 in the case C-167/01, Kamer van Koophandel en Fabrieken voor Amsterdam v Inspire Art Ltd. (Inspire Art case), paragraph 96.
[526] Judgment of the Court of Justice of the European Union of 9 March 1999 in the case C - 212/97, Centro Ltd v Erhvervs-og Selskabsstyrelsen (Centro case), paragraph 25.
[527] The High Level Group of Company Law Experts. (2002). Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe ('Winter Group Report'). P 94. Accessed 27 May 2024. Available at: https://ecgi.global/content/winter-group-2002

## 4. RECOGNIZING THE INTEREST OF THE GROUP AT THE LEVEL OF EUROPEAN UNION

Being in line with the principle of conferral, the EU has competence to regulate only selected aspects of Member State private law.[528] An EU primary law protects the creation and recognition of a group of companies under the freedom of establishment. However, an EU secondary law does not address the management of cross–border groups, even though this is the core element of the functioning of such establishments. The principle of conferral governs the limits of competence, but the principle of subsidiarity restricts the use of competence. In areas, which do not fall within its exclusive competence, the principle of subsidiarity limits the regulating power of the EU to a circumstance, in which Member States cannot sufficiently accomplish the purpose of EU law and has "European added value" [529] – the benefit of a legal act at the EU level has to outweigh the preference for the Member State's action.[530] The principle of subsidiarity protects Member States' national interests against EU interference, if common values are shared amongst Member States' national and EU spheres.[531] It is submitted that at least in some areas, the effective legal framework can only be delivered at the EU level. Member States' stance of recognition of the interest of the group at the EU level can separate in two groups. The first group agrees that there is a need to recognise the interest of the group, but disagree about the nature of the legislation to be introduced at the EU level. The second group denies that legal fragmentation in a respective field should be harmonised at all. Depending on the proposed type, content and scope of legal act, Member States' stance can differentiate and switch from one group to another.

The legal fragmentation in Member State practices of recognition of the interest of the group unduly increases the cost of doing cross–border business, creates ambiguity and uncertainty to which transactions or operation can be carried out in a group of companies' structure and alters the freedom of choice between a branch and a subsidiary. Regulatory competition between Member States cannot correct these market failures because uniformity in cross–border conditions is needed. An effective corporate governance framework is crucial

[528] Manko, R. (2015). EU competence in private law: The Treaty framework for European private law and challenges for coherence. European Parliamentary Research Service (EPRS). P. 1. https://doi.org/10.2861/292462
[529] Weatherill, S. (1996). Law and Integration of the EU. Oxford University Press. P. 14.
[530] Barber, N., W. (2005). The Limited Modesty of Subsidiarity. *European Law Journal*. Vol. 11, issue 3. P. 311. https://doi.org/10.1111/j.1468-0386.2005.00261.x
[531] Bernard, N. (1996). The Future of European Economic Law in the Light of the Principle of Subsidiarity. *Common Market Law Review*. Volume 33, issue 4. P.651. https://doi.org/10.54648/cola1996038

for sustainability and competitiveness of companies in the long term.[532] Cross–border business would be enhanced, if at the EU level there were a framework of rules for a group of companies that specifically regulated the interest of the group, if creditors', minority shareholders' and other stakeholders' interests are protected.[533]

The interest of the parent company is to exercise the right to issue instructions to the subsidiary, while remaining the separation of liability.[534] The parent company's right to issue instructions should not be limited to the interests of the subsidiary, as well as to avoid the parent company's duty to oversee the subsidiary's affairs (unified group management duty) and group solidarity (offer support, e.g., financing). In the creditors' point of view the interests of the group may be endangering the solvency of each company (e.g. commingling of assets, risky activities), therefore, if the interest of the group does not coincide with the interest of a subsidiary then a parent company has to have the duty to care and the duty of loyalty to diminish the risk of economic failure.[535] Minority shareholders opposed to creditors are exposed to the risk of detrimental shifts in subsidiaries without triggering insolvency (e.g. profit shifting).[536] Minority shareholders similar to creditors have the interest of imposing on the parent company the duty to care and the duty of loyalty towards its subsidiarity. The group solidarity is not in the interest of minority shareholders because the subsidiarity can be entangled with "other subsidiary's" financial failures. However, it can go the opposite way, i.e., a minority shareholder's subsidiary can receive the support from other subsidiaries. Respective notion of the group solidarity and its impact on minority shareholders can be also applied for creditors.[537] Having regards to the foregoing, for drafting a legal framework, which recognises the interest

[532] European Commission. (2012). Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee of the Regions. (2012). Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies. P. 3. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A52012DC0740

[533] European Company Law Experts (ECLE). (2012). The Future of European Company Law (response to the European Commission's Consultation). Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/the-future-of-european-company-law-response-to-the-european-commissions-consultation-2012/

[534] Fülbier, R.,U., Gassen, J. (2020). Kosten und Nutzen des faktischen Konzerns. Vom Konzern zum Einheitsunternehmen: Aktuelle Entwicklungsperspektiven des deutschen und europäischen Konzernrechts. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*: Sonderheft; 22. Berlin: De Gruyter. S. 48. https://doi.org/10.1515/9783110698077

[535] Krebs, P., Jung, S. (2021). European Group Law reconsidered. *European Business Law Review*. Volume 32, Issue 4. PP.620 and 621. https://doi.org/10.54648/eulr2021022

[536] Fülbier, R.,U., Gassen, J. (2020). Kosten und Nutzen des faktischen Konzerns. Vom Konzern zum Einheitsunternehmen: Aktuelle Entwicklungsperspektiven des deutschen und europäischen Konzernrechts. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*: Sonderheft; 22. Berlin: De Gruyter. S. 49. https://doi.org/10.1515/9783110698077

[537] Krebs, P., Jung, S. (2021). European Group Law reconsidered. *European Business Law Review*. Volume 32, Issue 4. P. 624. https://doi.org/10.54648/eulr2021022

of the group, is to assure that the parent company's impact on subsidiary's performance increase exceeds benefits of control.

Those Member States, which regulate a group of companies either by a legal act or a case law, acknowledge that establishments of groups of companies are common and rational, as well as create challenges for ensuring independent profitability and sustainability, therefore, main focus in respective jurisdictions has been governing creditors', minority shareholders' and other stakeholders' interests. Member States, which do not regulate a group of companies, rely on the presumption that each company has separate legal personality and must always act in its own best interests, therefore, creditors, minority shareholders and other stakeholders' interests are protected from abusive influence by the parent company. In both cases Member States have well – established mechanisms for protection of creditors', minority shareholders' and other stakeholders' interests, e.g. rules of related party transactions and regulations of qualified approval requirements.[538] It follows that Member States efficiently protect interests of creditors, minority shareholders and other stakeholders in its jurisdiction, but are lacking a legal framework that installs efficiency and certainty in organising and managing the cross-border group of companies. [539] Since centralised management cannot be prevented anyway, more efficient corporate governance of the functioning of cross–border groups of companies would also greatly benefit creditors, minority shareholders and other stakeholders.[540] The defence of public interests has to be achieved by legislation that does not hinder and supports the development of economic activity, notably through the completion of the Internal Market.[541] In the light of all the foregoing, at the EU level enabling law is needed for pursuing the interest of the group rather than protective mechanisms for creditors', minority shareholders' and other stakeholders' interests. The EU company law must not only make market operators suitable for the Internal Market, but also facilitate their global competitiveness. It is argued that the capacity of companies to transfer production, corporate

[538] Jung, S., Krebs, P., Stiegler, S. (2019). Gesellschaftsrecht in Europa. Baden-Baden: Nomos. S. 1953.
[539] Teichmann, C. (2016). Towards a European Framework for Cross-Border Group Management. *European Company Law*. Volume 13, issue 5. PP. 150 and 151. https://doi.org/10.54648/eucl2016022
[540] Chiappetta, F., Tombari, U. (2012). Perspectives on Group Corporate Governance and European Company Law. *European Company and Financial Law Review (ECFR)*. Volume 9, issue 3. P. 271. https://doi.org/10.1515/ecfr-2012-0261
[541] European Commission. (2005). COMMUNICATION FROM THE COMMISSION TO THE COUNCIL AND THE EUROPEAN PARLIAMENT: Better Regulation for Growth and Jobs in the European Union. COM(2005) 97 final. P. 2. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX%3A52005DC0097

identity and tax burden on a global scale pressures national jurisdictions to become increasingly standardised as they compete for investments (International and European).[542]

Not only provisions of Treaties, but also the principle of mutual recognition founded in case law [543] has a decisive role in the harmonisation process. Initiatives to harmonise should be directed to matters, which are essential to approximate and other differences could be overcome by mutual recognition.[544] In company law the mutual recognition is a precondition of exercise of the freedom of establishment for the particular reason that companies' legal status of other Member States is recognised.[545] Mutual recognition permits for more flexibility and decentralisation by maintaining Member States' national regulations and standards.[546] In cases where centralisation and uniformity may be hard to achieve, the mutual recognition is the next best solution available.[547]However, companies under the EU law are creatures of national legislation and exist only by virtue of respective national law.[548] Therefore, the recognition of the interest of the group is a substantial matter of the company law, but the mutual recognition exclusively removes technical barriers. Accordingly, that in the recognition of the interest of the group the mutual recognition does not require to member states to apply foreign laws in cross-border situations, thereupon, respective matter is essential to harmonise.

### 4.1. Legal act for recognising the interest of the group

Approximation of legally fragmented Member States' practices of recognition of the interest of the group by establishing enabling law can be achieved only by the harmonisation process. Harmonisation of laws eliminates disparities between Member States' national laws[549]

[542] Rhodes, M., Apeldoorn, B. (1998). Capital unbound? The transformation of European corporate governance. *Journal of European Public Policy*. Volume 5, issue 3. P.407. https://doi.org/10.1080/135017698343893
[543] Judgment of the Court of 20 February 1979 in the case 120/78, ewe-Zentral AG v Bundesmonopolverwaltung für Branntwein (Cassis de Dijon case).
[544] European Commission. (1985). Completing the Internal Market. White Paper from the Commission to the European Council. COM (85)310 final. P. 19. Accessed 27 May 2024. Available at: https://op.europa.eu/en/publication-detail/-/publication/4ff490f3-dbb6-4331-a2ea-a3ca59f974a8/language-en
[545] Judgment of the Court of Justice of the European Union of 5 November 2002 in the case C - 208/00, Überseering BV v Nordic Construction Company Baumanagement GmbH (NCC), paragraph 59.
[546] Van Den Brink, T. (2017). The Impact of EU Legislation on National Legal Systems: Towards New Approach to EU Member State Relations. *Cambridge Yearbook of European Legal Studies*. Volume 19. P. 219. https://doi.org/10.1017/cel.2017.2
[547] Scharpf, F. (1998). Negative and Positive Integration in the Political Economy of European Welfare States. The Future of European Welfare. P. 170. https://doi.org/10.1007/978-1-349-26543-5_8
[548] Judgment of the Court (Third Chamber) of 12 July 2012 in the case C-378/10, VALE Építési kft, paragraph 27.
[549] Judgment of the Court of 16 July 1998 in the case C-355/96, Silhouette International Schmied GmbH & Co. KG v Hartlauer Handelsgesellschaft mbH, paragraph 24.

and ensures that competition is not distorted.[550] The positive harmonisation is entailed by legislative actions at the EU level by the Regulations[551] and the negative harmonisation is driven by case law, prohibitions of policies at Member State's national law and means of Directives and Recommendations and Opinions.[552]

According to Article 288 of the TFEU, a Regulation, a Directive or Recommendations and Opinions can enact the EU's legislation. The Regulation is binding in its entirety and is directly applicable in all Member States. The Directive is binding only to the result achieved and national authorities choose the form and methods. However, Recommendations and Opinions have no binding force.[553] Article 50 of the TFEU prescribes that the European Parliament and the Council, in order to attain freedom of the establishment shall act by means of Directives.[554] Based on the Article 352 of the TFEU (the flexible clause), if the Treaties have not provided the needed powers, but actions by the EU are necessary to reach one of the objectives set out in the Treaties within the framework of the policies defined, appropriate measures shall be adopted by unanimity in the Council of the European Union (Council).[555] Article 352 of the TFEU can be applied for adoption of a Regulation of group of companies with cross-border activities. Consequently, there are legal grounds for enactment of a Regulation, a Directive or Recommendations and Opinions in the European company law.

The positive harmonisation is criticized for creating a single legal system rather than a single market and does not take into account diversity of legal traditions and civil societies, therefore, generating compelling tension between Member States and the EU.[556] The EU company law is intended to be a coherent system of different Member States' laws.[557] In order to reduce the tension between uniform rules and a differentiated normative landscape the policy of minimum harmonisation was intended to resolve by allowing a Member State to take

[550] Order of the Court of First Instance (First Chamber) of 11 September 2007 in the case T-35/06, Honig-Verband eV v Commission of the European Communities, paragraph 17
[551] Scharpf, F. (1998). Negative and Positive Integration in the Political Economy of European Welfare States. The Future of European Welfare. P. 157. https://doi.org/10.1007/978-1-349-26543-5_8
[552] Evans, A. (1996). The Integration of the European Community and Third States in Europe: A Legal Analysis. 1st edition Oxford University Press. P. 231.
[553] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal C 326, 26/10/2012 P. 0001 – 0390.
[554] Ibid.
[555] Ibid.
[556] Kurcz, B. (2001). Harmonisation by means of Directives. *European Business Law Review*. Volume 12, issue 11/12. P. 288. https://doi.org/10.54648/5086942
[557] Van Den Brink, T. (2017). The Impact of EU Legislation on National Legal Systems: Towards New Approach to EU Member State Relations. *Cambridge Yearbook of European Legal Studies*. Volume 19. P. 218. https://doi.org/10.1017/cel.2017.2

independent actions therein.[558] In the light of all foregoing, harmonisation in company law has been largely carried out via Directives.[559] A Regulation in company law has been introduced as the legal act only in the fields where new legal instruments are needed,[560] e.g., *SE* Regulation of a European Company,[561] the European Economic Interest Grouping (EEIG) regulation.[562] However, the harmonisation remains partial, especially in the context of a group of companies. Accomplished company law harmonisation has rendered the Internal Market more accessible (set up group of companies) but falls short of yielding the benefits from the whole scale of the economy (managing group of companies),[563] therefore, the cause of action should change the direction. In the beginning of the harmonisation process by Directives in the field of company law only six Member States' legal systems had to be considered. Those Member States' legal systems were based in part on common European legal principles. The accession of new Member States has made the consideration of legal systems for approximation significantly more complex.

The EU policy-making process has been described as negotiations of reaching agreements and even implementing policies once they are reached.[564] The EU negotiations are determined by bargaining among Member States and generally reach the lowest common denominator.[565] The particular reason is that Member States are primarily concerned with their own interests and will accept policies that are close to their preferences.[566] Policies of groups of companies are no different and so far only rules on transparency and formation of supranational groups of companies has been achieved for the reason that these matters insubstantially affect Member State pre-established civil order. Moreover, the harmonisation

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[558] Dougan, M. (2000). Minimum Harmonization and the Internal Market. *Common Market Law Review*. Volume 37, issue 4. P. 856. https://doi.org/10.54648/272669

[559] Lutter, M.(1995). Europäisches Unternehmensrecht. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. Sonderheft. 4. Auflage. S. 299.

[560] Wymeersch, E. (2001). Company Law in Europe and European Company Law. Financial Law Institute Working Paper No. 2001-06. PP. 13 and 19. http://dx.doi.org/10.2139/ssrn.273876

[561] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE). Adopted on 10 November 2001. Published in the Official Journal of the European Communities, L 294/, p. 1–21.

[562] Council Regulation (EEC) No 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG). Adopted on 31 July 1985. Published in the Official Journal of the European Communities, L 199, p. 1–9.

[563] Wymeersch, E. (2001). Company Law in Europe and European Company Law. Financial Law Institute Working Paper No. 2001-06. P. 16. http://dx.doi.org/10.2139/ssrn.273876

[564] Wallace, H. (1996). Politics and policy in the EU: the challenge of governance. Policy-Making in the European Union. 3rd ed. Oxford: Oxford University Press. P. 32.

[565] Marks, G., Hooghe, L., Blank, K. (1996). European integration from the 1980s: state-centric v. multi-level governance. *Journal of Common Market Studies*. Volume 34, issue 3. P. 345. https://doi.org/10.1111/j.1468-5965.1996.tb00577.x

[566] Scharpf, F. W. (1998). The joint-decision trap: lessons from German federalism and European integration. Public Administration. P. 264. https://doi.org/10.1111/j.1467-9299.1988.tb00694.x

of group of companies' legal framework transfers regulatory sovereignty to the supranational level, thus Member States cannot affect them unilaterally without negotiations at the EU level. However, in removal of alternative solutions to the same legal problem market operators do not face Member States' adaptation costs because harmonisation optimises their trade. The issues of the bargaining arena of the EU policy-making can be resolved by turning it to problem solving type of decision-making.[567] As it is already established that the recognition of the interest of the group at the EU level would provide long-run efficiency of the Internal Market and diversity of Member States' practices are alternative solutions to the same regulatory issue, there is a strong incentive for application of problem solving negotiations, which can result in unanimous or nearly unanimous agreement.

The benefit of choosing a Regulation as the legal act for recognising the interest of the group is that it does not require any form of transformation or implementation, thus limiting diverging approaches. The disadvantage of choosing a Directive as the legal act is that it can only provide minimum standards, which can be amended to the requirements of the national legal system, therefore, interfere with the operation of the enabling law. The issue with adopting a regulation is that it is directly integrated into a Member States' legal order and due to the legal basis of Article 352 of the TFEU it is very unlikely that there will be unanimous consensus in the Council.[568] The requirement of unanimous vote in the Council is the reason why the attempt of *SPE* Regulation failed and as the alternative was a proposed *SUP* Directive.[569] Once the harmonisation affects internal company structure opposition becomes more rigid.[570] Nevertheless, concerns of recognition of the interest of the group are alike in all Member States and there are not that many solutions; differences are more technical than fundamental. Accordingly, if recognition of the interest of the group is separated from other aspects of the group of companies' law, it can significantly increase the chance of the support from Member States. Company law has to constantly evolve due to changes in statutes and new Directives and Regulations are enacted in other sectors, as well as altered business practices developed by the demand of capital markets.[571] The EC has stated that replacing Directives with Regulations when politically acceptable and legally possible would reduce national

[567]Ibid. P. 161.
[568] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 13. https://doi.org/10.1515/ecfr-2013-0194
[569] Jung, S. (2015). Societas Unius Personae (SUP) – The New Corporate Element in Company Groups. *European Business Law Review*. Volume 26, issue 5. P. 645. https://doi.org/10.54648/eulr2015033
[570] Wymeersch, E. (2001). Company Law in Europe and European Company Law. Financial Law Institute Working Paper No. 2001-06. P. 16. http://dx.doi.org/10.2139/ssrn.273876
[571] Ibid, P.21.

divergence (legal fragmentation) and gold plating,[572] in which Member States apply more stricter rules than the ones foreseen at the EU level.[573]

It is controversial that matters of transparency (notification, disclosure and accounting standards) are harmonised, but the recognition of the interest of the group remains legally fragmented. The EU law imposes unified measures of verifying that pursuit of the interest of the group can be achieved; though there is absence of rules on how to execute it cross-border. In a mixed economy such as that of the EU only positive harmonisation combined with negative harmonisation can reduce the impeding effects of legal fragmentation and improve conditions of cross-border activities.[574] The management of the group can be the aspect that is harmonised by a Regulation, while keeping harmonisation of transparency by Directives.

Previous experience of failures of the 1970s of regulating the group of companies can be considered as out of date. There has been steady expansion of the EU powers and now it covers not only broader range of economic matters (e.g. Monetary Union), but also social responsibilities (e.g. employment, consumers, public health), which means that company law harmonisation is currently performing very different functions from those it did previously.[575] The Regulation of SE Articles 15-17 of the Preamble reference to Member States' group law is an incoordination method of indirect harmonisation, which does not unify the subject directly, but it either points to the applicable rules.[576] The same critique of negative harmonisation can be applied to indirect harmonisation. Moreover, to create a supranational body, harmonised group law is not needed. The SUP Directive proposal provides an incomplete framework for pursuing the interest of the group.[577] The boundaries of the right to give are not set in the SUP Directive proposal, but the EU law should draw it.[578] General rights to give instructions without boundaries construct a major regulatory gap, which restricts functioning of enabling law. The SUP Directive proposal is not the appropriate framework for tackling a

[572] European Commission. (2007). Communication from the Commission - A Europe of Results – Applying Community Law. COM(2007) 502 final. P. 5. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/en/TXT/?uri=CELEX%3A52007DC0502
[573] Hatzopoulos, V. (2013). From Hard to Soft: Governance in the EU Internal Market. *Cambridge Yearbook of European Legal Studies*. Volume 15. P. 110. https://doi.org/10.5235/152888713809813503
[574] Kurcz, B. (2001). Harmonisation by means of Directives. *European Business Law Review*. Volume 12, issue 11/12. P. 288. https://doi.org/10.54648/5086942
[575] Dougan, M. (2000). Minimum Harmonization and the Internal Market. *Common Market Law Review*. Volume 37, issue 4. P. 860. https://doi.org/10.54648/272669
[576] Ibid.
[577] Hommelhoff, P. (2014). Die Societas Unius Personae: als Konzernbaustein momentan noch unbrauchbar. GmbH-Rundschau. S. 1065.
[578] Teichmann, C. (2014). Europdiische Harmonisierung des GmbH-Rechts. *Neue Juristische Wochenschrift (NJW)*. S. 3561 und 3564.

group of companies' issues.[579] There is still urgency to deal with recognition of the interest of the group.

The consensus for adoption of a Directive could be reached easier than for a Regulation because, according to Article 50 of the TFEU and Article 294 of the TFEU, only a qualified majority in the Council is required.[580] A Directive could be a choice, if Member States' intervention is limited by intensive harmonisation. In such a case political opposition in the Council still must be expected. The political tension can be reduced by a well-targeted Directive that addresses merely recognition of the interest of the group. By total or maximum harmonisation Member States are deprived of the capacity to derogate from prescribed provisions, if a Directive states precisely which arrangements are allowed and which are not, as well as only application of specific measurers is approved.[581] The CJEU has enabled the EU legislator in the view of the objective achievable to stipulate in Directives exact obligations to be transposed into national law to ensure the absolute identity of national provisions' across all Member States.[582] The well-functioning of the enabling law of pursuit of the interest of the group dependents on uniformity across all Member States. A Directive of partial harmonisation is also a choice, where certain aspects of activity are maximally harmonized, whereas in others Member States' interventions are allowed.[583] A Directive could also introduce options, whereby Member States may choose between several alternatives, but cannot derogate from options provided in a Directive or in an Annex to it. It is well known that options in a Directive are often a way to reconcile different opinions.[584] For the purpose of the enabling law, options and partial harmonisation should not be dedicated to features that directly affect cross border management such as the right to give instructions and its boundaries, direct liability of the parent company and exit rights of minority shareholders, but for technical questions such as formation of a control option or partial harmonisation could be applied.

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[579] Teichmann, C. (2015). Corporate Groups within the Legal Framework of the European Union: The Group-Related Aspects of the SUP Proposal and the EU Freedom of Establishment. *European Company and Financial Law Review (ECFR)*. Volume 12, Issue 2. P. 229. https://doi.org/10.1515/ecfr-2015-0202

[580] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal C 326, 26/10/2012 P. 0001 – 0390.

[581] Van Den Brink, T. (2017). The Impact of EU Legislation on National Legal Systems: Towards New Approach to EU Member State Relations. *Cambridge Yearbook of European Legal Studies*. Volume 19. P. 218. https://doi.org/10.1017/cel.2017.2

[582] Judgment of the Court of 23 November 1977 in the case 38-77, Enka BV v Inspecteur der Invoerrechten en Accijnzen Arnhem, paragraph 12.

[583] Kurcz, B. (2001). Harmonisation by means of Directives. *European Business Law Review*. Volume 12, issue 11/12. P. 295. https://doi.org/10.54648/5086942

[584] Wymeersch, E. (2001). Company Law in Europe and European Company Law. Financial Law Institute Working Paper No. 2001-06. P. 8. http://dx.doi.org/10.2139/ssrn.273876

The establishment of a Recommendation rather than adoption of a Regulation or a Directive would be a more cautious approach in the recognition of the interest of the group.[585] Moreover, a Recommendation is less burdensome to adopt than a Regulation and a Directive, since the EC does not need Member States' approval. A Recommendation could create a whitelist (e.g., cash pooling) and a blacklist of practices of recognition of the interests of the group. Non-constraining legal instruments tend to promote the evolutionary character of the rules.[586] For those Member States, which do not address the interest of the group, a Recommendation would provide practices for completion of their legal system that are already recognised at the EU level. A less binding Recommendation not only gives Member States and market participants more time to adjust to reforms, but also gives preliminary options, which in turn reduce opposition to harmonisation.[587] If a Recommendation of recognising of the interest of the group is applied EU-wide and does not lead to unintended consequences, it could be tuned to a Regulation or a Directive. Non-binding force of a Recommendation does not mean that it cannot be used efficiently for harmonisation purposes.[588] Despite their lack of binding effect, they are not fully without any legal consequences because Recommendations have to be taken into consideration when interpreting national law in light of binding EU legal acts.[589] On the one hand, there are no binding EU legal acts in the field of recognition of the interest of the group. On the other hand, the failure of Recommendations to reduce legal fragmentation of the recognition of the interest of the group would cease to be the confirmation that Member States cannot sufficiently achieve the objective of uniformity of rules and proposed action be better achieved by the EU, as well as have cross-border effect. In the light of all foregoing, a Recommendation in the recognition of the interest of the group is better suited to be an intermediate legal instrument rather than final.

[585] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 213. https://doi.org/10.1515/ecfr-2013-0194

[586] The Committee on Europe of the Club des Juristes. (2015). Towards recognition of the group interest in the European Union? Report from the Club des Juristes. P. 21.

[587] Hertig, G. McCahery, J. A. (2006). Optional Rather Than Mandatory EU Company Law: Framework and Specific Proposals. *European Company and Financial Law Review (ECFR)*. Volume 3, issue 4. P. 345. https://doi.org/10.1515/ECFR.2006.015

[588] Lenaerts, K., Arst, D., Bray, R. (1999). Procedural Law of the European Union. Sweet&Maxwell. London. P. 233.

[589] Judgment of the Court (Second Chamber) of 13 December 1989 in the case C-322/8, Salvatore Grimaldi v Fonds des maladies professionnelle, paragraph 18.

### 4.2. The scope of the legal act for recognising the interest of the group

#### 4.2.1. The definition of the group and its interests

In Germany, a group of companies is referred to as *Konzern* and the term also used widely in Europe, e.g., Austria - *Koncern*, Switzerland - *Konsern*, Latvia – *Koncerns*, Scandinavia – *Concern*. The respective term is closely linked with German *Konzernrecht.* One of the reasons that the proposal for the Ninth Company law Directive, which regulated group of companies, was dropped was too close similarity with *Konzernrecht.*[590] To avoid connotations with failed attempts to regulate a group of companies at the EU level the term *Konzern* should be avoided. The concept of *Affiliated companies* is linked with the Anglo-Saxon system and has strong association with the common law legal system, while the EU Member States are following the civil law system. The term *Group* is well known, but has no precise meaning in any legal system and is open to interpretation. The legal entity that controls other companies and the former are called differently across Member States. Be that as it may the Accounting Directive[591] and the Parent/Subsidiary Directive[592] in the tax law field uses the term the parent company and the subsidiary. Those Member States that do not have group of companies' codification or establish it by the case law tend to shift towards such terminology. Member States that have separate legal acts or rules for a group of companies, e.g. Germany, Latvia, Portugal, favour choice of the words dominant or controlling company and dependent or controlled company, which is a consequent of the fact that the regulatory basis for systemized corporate group legal regime is German *Konzernrecht.* Nevertheless, the term dominant or controlling company and dependent or controlled company has strong connotation with specific rules of German *Konzernrecht*. Although names of the parent company and the subsidiary are already utilized, they have only general meaning in accounting and tax law. The terms used in legal acts for the recognition of the interest of the group have to be neutral in order facilitate problem solving rather than bargaining negotiations in the EU policy-making and eliminate ambiguity of interpretation.

[590] Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 196. https://doi.org/10.1515/ecfr-2013-0194

[591] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.

[592] COUNCIL DIRECTIVE 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States. Adopted on 29 December 2011. Published in the Official Journal of the European Union L 354/8.

A legal act for recognising the interest of the group must prescribe the definition of the group of companies in furtherance of uniformity in application across the EU. In contrary the absence or vagueness of the definition of the group of companies would still maintain national law divergence via different application and Member States could resist harmonisation by amending national provisions. As an example, the United Kingdom with the 1980 Companies Act[593] alleviated conditions for companies to change corporate legal forms with the aim to allow public companies to remove themselves from the scope of the Second Company Law Directive (applicable to public companies)[594] and as a result, only 1% of all companies in the United Kingdom were in the legal framework of respective EU law.[595]

There can be distinguished three types of creation of group of companies: 1) participation; 2) control; 3) exercise of control. Under participation other interests than company's cannot be prioritized. If there is a relationship of control, a person has the possibility to prioritize other interests, but does not exercise it. If a control is exercised then a company becomes an economic unit under single management and other interests are prioritized before the interest of the company. Before constituting the definition of the interest of the group one must firstly clarify, which concept serves as the basis for it. Two different concepts of control and dominance/dependency are used in Member States. The difference is that the control concept is used to identify a group of companies, but the concept of dominance and dependency provide a specific framework, in which centralised management and profit shifting can be carried out. The concept of dominance and dependency is only applied in Member States of the specific code of group of companies, e.g., Germany Article 17 of *AktG*,[596] Portugal Article 486 of *CSC,*[597] Latvia Article 3 of *Koncernu likums* .[598] Between Member States the concept of dominance and dependency still exist legal fragmentation in the scope of application, while among the concept of the control Member States stand harmonisation. The most commonly

[593] Companies Act 1980, chapter 22. An Act to amend the law relating to companies. [1st May 1980].
[594] Second Council Directive 77/91/EEC of 13 December 1976 on coordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent. Adopted on 16 December 1976. Published in the Official Journal of the European Union L 26. No longer in force.
[595] Stolowy, N., Schrameck, S. (2011). The contribution of European law to national legislation governing business law. *Journal of Business Law*. Volume 6. Sweet & Maxwell. P. 630.
[596] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[597] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[598] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

used concept is control.[599] The control concept is already implemented in the IFRS 10 for consolidation purposes[600] and accordingly in Article 22 paragraph 1 of the Accounting Directive,[601] thus already used effectively in supranational legal act in accounting despite differences in regulation of group of companies in Member States. Moreover, the reference to the Accounting Directive's definition of the group are made also in other legal acts, e.g. Article 4, paragraphs 15 and 16 of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Capital Requirement Regulation)[602] and Article 2, paragraph 14 of Insolvency Regulation.[603] For the purpose of establishing the definition of the group of companies at the EU level, the concept of control is more appropriate. Long or short-term holding of shares has no importance because mere participation will not bring any obligations, therefore, there is no need to distinguish between them.

There is a plurality of different corporate forms of companies across the EU and significant disparity between patterns of business conduction in Member States, which affects the scope of application of a legal act for the recognition of the interest of the group. On one side some Member States, e.g., Ireland, Finland, Sweden, distinguish a company's corporate form by the type of investment in their shares, i.e., publicly traded (listed) or private companies. On the other side, Member States, e.g., France, Germany, Italy, Netherlands, Latvia, Spain, Portugal separate a company's corporate form on the basis of their nature, i.e., open or closed companies.[604] That is the reason for the still remaining divergence of substance between types of companies and why universal compatibility cannot be found. Germany has a relatively small proportion of public (open) companies compared to private (closed), in contrast France and Italy use the form of public (open) companies even in small undertakings.[605] The situation in

[599] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 176. https://doi.org/10.1017/S1566752900000148
[600] The International Accounting Standards Board's International Financial Reporting Standard (IFRS) 10 of Consolidated Financial Statements. Adopted on 12 May 2011. Accessed 27 May 2024. Available at: https://www.ifrs.org/issued-standards/list-of-standards/ifrs-10-consolidated-financial-statements/#about
[601] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.
[602] Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012. Adopted on 27 June 2013. Published in the Official Journal of the European Union L176/1.
[603] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast). Adopted on 5 June 2015. Published in the Official Journal of the European Union. L 141/19
[604] Stolowy, N., Schrameck, S. (2011).The contribution of European law to national legislation governing business law. *Journal of Business Law*. Volume 6. Sweet & Maxwell. P. 630.
[605] Edwards, V. (1999). EC Company Law. Oxford EC Law Library. P. 12.

Spain is similar to that in Italy and France and public (open) companies are used more commonly, but Sweden and Latvia are closer to the German patterns of business conduction and a private company's corporate structure is used more frequently. Accordingly, choosing only one legal form might have an insignificant effect on harmonisation.

For the above mentioned reasons and the fact that person based on the freedom of establishment may freely choose from diverse Member States' corporate legal forms for structuring group of companies, a legal act for the recognition of the interest of the group application scope has to cover public and private companies, as well as partnerships because there is substantial number of them.[606] Other corporate forms, e.g. cooperatives, associations, foundations, civil code partnerships, depend to a great extent on particular circumstances of the national legal system and have no compatibility to other Member State legal frameworks. To a legal act for recognising the interest of the group has to be added to the Annex that lists precisely each Member States companies' legal forms that are under the scope forming legal certainty for interpretation and avoiding Member States attempts to diminish the impact on national markets. Taking into consideration that Member States and EU legislation concerning types of companies can change, the EC should be empowered to update the list of Member States companies' legal forms in accordance with Article 290 of the TFEU.[607] Member States can be set free to add additional legal forms of members of group of companies and it will not create national divergence because incompatibility and only local relevance means no cross-border effect and it will not be gold plating, but rather Member States' initiative to promote further harmonisation. The recognition of the interest of the group at the EU level would be by supranational legal act, therefore, foreign companies within the EU can also be covered.

A company is a legal fiction for a means to achieve an economic purpose.[608] A company is attributed a separate legal personality from its members (shareholders) and is capable of enjoying rights and being subject to duties,[609] i.e. to assume a life of its own. A separate legal personality was introduced for individual companies, but later came realisation of the ability of a company to purchase or own the stock of other legal entities and group of companies'

[606] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19. Article 5 of the Preamble.
[607] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal of the European Union C 326.
[608] Whincup, M. (1981). Inequitable Incorporation: the Abuse of a Privilege. Company Lawyer. Volume 2. P. 158.
[609] Blumberg, P. I. (1987). The law of corporate groups: tort, contract, and other common law problems in the substantive law of parent and subsidiary corporations. Boston: Little Brown. P. 55.

structure emerged.[610] A group of companies' structure produces multiple layers of corporate veil and it is concerning. A respective issue is that it does not correspond to a natural person, therefore, there is no demand to deviate from the doctrine of a separate legal personality for a natural person who owns multiple companies. It is well respected in existing group law at the EU level, e.g. drawing consolidated accounts (the Accounting Directive)[611], employment in a group of companies (the Directive on European works council)[612] and should continue to do so in a legal act for the recognition of the interest of the group.

The most often used form of a group of companies' structure (especially for subsidiaries) is limited liability[613] and by virtue of their importance should be included in a legal act for the recognition of the interest of the group. Further, unlimited liability companies possess less risk for creditors than limited liability companies and the rules governing their operations do not differ, therefore, there is no legitimate reason to not include them. Given that listed companies have a prominent role in the Internal Market [614] and a lot of listed companies belong to the group and have subsidiaries in other Member States[615] a legal act for recognising the interest of the group should apply for them and it would be in line with Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids (the Takeover Bids Directive).[616] Since the recognition of the interest of the group would limit

[610] Blumberg, P. I. (1990). The Corporate Entity in an Era of Multinational Corporations. *Delaware Journal of Corporate Law*. Volume 15. P. 324.

[611] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.

[612] Directive 2009/38/EC of the European Parliament and of the Council of 6 May 2009 on the establishment of a European Works Council or a procedure in Community-scale undertakings and Community-scale groups of undertakings for the purposes of informing and consulting employees (Recast) (Text with EEA relevance). Adopted on 29 June 2013. Latest Amendments on 9 October 2015. Published in the Official Journal of the European Union L 122/28.

[613] Davies, P. L. (2008). Gower and Davies' Principles of Modern Company Law. 8th edition. Sweet & Maxwell. P. 196.

[614] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19. Article 28 of the Preamble.

[615] European Company Law Experts (ECLE). (2012). The Future of European Company Law (response to the European Commission's Consultation). Accessed 27 May. Available at: https://europeancompanylawexperts.wordpress.com/publications/the-future-of-european-company-law-response-to-the-european-commissions-consultation-2012/

[616] Directive 2004/25/EC of the European Parliament and of the Council of 21 April 2004 on takeover bids (Text with EEA relevance). Adopted on 30 April 2004. Published in the Official Journal of the European Union L 142/12.

demanding regulatory requirements (administrative burden) it is equally important for micro-undertakings, SMEs and large-undertakings.

Public law entities can structure a group of companies, but unlike private law subjects they provide public services or serve other public interests. The question arises whether public sector companies should be under the scope of a legal act for the recognition of the interest of the group. From creditors' and minority shareholders' point of view whether a company is subjected to private or public law makes no difference because in both cases the protection is needed.[617] The state as a shareholder does not have more or different obligations or rights than private shareholders, as well as public law entities actions in corporate bodies are no different from any other shareholder. Any different treatment of public law companies would distort competition with private law subjects. Favourable treatment of public sector companies contradicts Article 106 of the TFEU.[618] If equal treatment impedes public sector companies from fulfilling their duties, then the choice of corporate form should be reconsidered.[619] Consequently, public sector companies should not be removed from the application scope of enabling law of the pursuit of the interest of the group.

The definition of the interest of the group has significant importance because it sets the first line of defence for safeguarding a subsidiary's autonomy, as well as limits a risk of abuse. German *Koncernrecht,* Latvian *Koncernu likums* and Portugal *sociedades coligadas* stipulate requirements for conclusion of matching contracts and sets only general limits for the pursuit of the interest of the group. Contractual groups can be found only in those Member States that has implemented German *Koncernrecht*[620] and is rarely even used there. General restrictions can be fitting for national application, especially within the framework of compensatory mechanism, but would be exposed to national divergence and gold plating in the supranational enabling law for the recognition of the interest of the group. In an adverse manner French *Rozenblum* doctrine, according to which the interest of the group is interrelated commercial activities in firmly established group structure and business integration by coherent policy and common interest, is flexible enough to apprehend a multitude of a corporate group structures and still creates a universal standard for the definition of the interest of the group. The 2004 Company law Reform of Italy proves that the *Rozenblum* doctrine, which is based on the case

[617] Lutter, M. (1987). 100 Bände BGHZ: Konzernrecht. *Zeitschrift für das gesamte Handelsrecht und Wirtschaftsrecht (ZHR)*. S. 451.
[618] Consolidated version of the Treaty on the Functioning of the European Union. Adopted on 13 December 2007. Published in the Official Journal of the European Union C 326.
[619] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 174. https://doi.org/10.1017/S1566752900000148
[620] Ibid, P. 179.

law, can be implemented in a legal act. The pursuit of the interest of the group should be a right, not a duty because the aspiration of a legal act for recognising the interest of the group is establishment of uniformity in organising and managing the cross-border group of companies rather than creation of new protective mechanisms for creditors', minority shareholders' and other stakeholders' interests.

### 4.2.2. The right to give instructions

In order to pursue the interest of the group the parent company must exercise centralised management. Lack of instruments for directly exerting power do not prevent the parent company to force the subsidiary to meet their interests, but all it does is impede consideration of group interests, therefore, the right to give instructions must be legitimised. If the definition of group of companies is construed by the concept of the control, which relates to majority voting rights and appointment or removal of members of the board of directors or the supervisory board, the subsidiary will find it difficult to bypass the parent company's influence. Shareholders have a strong desire to retain the control over the management of a company, although a board of directors have responsibility to manage a company, the shareholders demand the right to intervene and make ultimate decisions.[621] Shareholders are concerned not only how to control the management of a company, but also how to ensure that their interests receive appropriate attention.[622] The right to give instructions in line with the *Rozenblum* doctrine criteria of the interest of the group (firmly established group structure and business integration) would facilitate long run sustainability and profitability of a subsidiary.

It has been highlighted that the term instructions imply legally binding nature and hierarchical group structure,[623] which does not sit well with traditional understanding of separate legal personalities in group of companies, e.g. Italy with the 2004 Company law Reform has chosen to use terms direction and coordination.[624] Nevertheless, the term instructions are widely used in Member States, e.g. in Netherlands in the case law,[625] Articles

[621] Neville, M., Sørensen, K. (2014). Promoting Entrepreneurship – The New Company Law Agenda. *European Business Organization Law Review (EBOR)*. Volume 15, issue 4. P. 578 doi:10.1017/S156675291400127X

[622] Hopt, K. J., Pistor, K. (2001). Company Groups in Transition Economies: A Case for Regulatory Intervention? *European Business Organization Law Review (EBOR)*. Vol. 2. P. 1. P. 10. https://doi.org/10.1017/S1566752900000318

[623] Conac, P.H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 310. https://doi.org/10.1515/ecfr-2016-0301

[624] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).

[625] Hoge Raad 19 februari 1988, NJ 1988, 487. ECLI:NL:PHR:1988:AG5761

308 and 311 *AktG* in Germany,[626]Articles 26 and 29 of *Koncernu likums* in Latvia,[627] Article 503 of *CSC* in Portugal,[628] and even the *SUP* Directive's proposal at the EU level in.[629] As it is moving forward to a new and enlightened concept and the group of companies are established under the concept of the control, the term instructions do not show misleading connotations, therefore, can be kept in a legal act for recognition of the interest of the group.

Member States mainly have two different sets of models of the board structure: one-tier boards, which consist only of the board of directors, or two-tier boards, which are formed by the board of directors and the supervisory board. Consequently, choosing just one of the board structures would reduce the effect on harmonisation. So far at the EU level, the board structures are not distinguished, e.g., Article 38 of the *SE* Regulation of a European Company.[630]

The notion of giving instructions can take many forms, thus should not be limited to formal directions, e.g., business plan, group strategies, financial plans etc.[631] However, a company that meets the definition of the parent company under the control concept possesses the right to give instructions. Accordingly, the parent company can only exercise the right to give instructions directly and the subsidiary does not have the right to issue instructions to another subsidiary. Additionally, not all instructions are issued by the board of directors of the parent company, e.g., Chief Sales Officer (CSO) of the parent company might be interested in giving instructions directly to the regional subsidiary's CSO.[632] Be that as it may the employees do not represent the company with third person, hence can be attributed to the parent company's legal representatives – the board of directors and the supervisory board. On the opposite end, subjects of instructions also can be only subsidiary's board of directors and supervisory board.

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[626] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[627] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[628] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

[629] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. Chapter 7; Article 22, paragraph 7; Article 23.Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

[630] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE). Adopted on 10 November 2001. Published in the Official Journal of the European Communities, L 294/, p. 1–21.

[631] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19

[632] Conac, P.H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 310. https://doi.org/10.1515/ecfr-2016-0301

Moreover, the intention of the right to give instructions does not fully lift the corporate veil and dismiss separate personalities of companies in the group in its entirety.

The argument has been made that all members of the board of directors and supervisory board of a subsidiary cannot be subjects to instructions because it would contradict some of their specific functions, e.g. representatives of employees or minority shareholders.[633] The Article 23 of *SUP* Directive's proposal takes into consideration potential conflicts of interests and specifies that subjects to instructions are all directors, as long as it does not violate the applicable national law and breach the articles of association.[634] Such regulation may also be adopted in a legal act for the recognition of the interest of the group.

Under the concept of the control, the parent company's issued instructions have binding nature, yet its exercise must comply with the scope of the purpose and the aim of a legal act for the recognition of the interest of the group. Denoting that the right to give instructions cannot breach Member States national law because otherwise the EU legal act for recognising the interest of the group would allow circumvention of national legislation, based on the conferred rights. Furthermore, instructions that are in prescribed interest of the group and do not threaten the existence of a company are binding. The membership of the group poses many benefits,[635] but it comes with the proportionate cost of the interest of the group. Benefit and burden sharing in group of companies implies that detrimental or disadvantageous instructions to the subsidiary should also be binding. Moreover, there is no specific EU law on general duties of directors, which forge a risk that implementation of the right to issue binding instructions can be circumvented by not imposing effective enforcement of it. In contemplation of protection of the biding nature of the instruction from the formally introduced requirement, a failure of the subsidiary's management to follow the parent company's instructions should be acknowledged as valid grounds for their removal. However, the right to give instructions should not mean the duty to manage or oversee a subsidiary's affairs because it would disproportionately contradict the principle of separate legal personality and provoke increased liability of a parent company. If a parent company has an information that a subsidiary takes

[633] Ibid, P. 311.

[634] European Commission. (2014). Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies. COM(2014) 212 final. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014PC0212

[635] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19

unreasonable risk or is mismanaged, as well as breaks the law, a general meeting by being shareholder can be called in order to avert concerns.[636]

### 4.2.3. The creditor protection

The creditor protection is of great importance because low-cost capital flows where its best protected.[637] A subsidiary's creditors have no right to see that a company is always kept solvent. Nevertheless, creditors can reach for self - protection measures. As theory confirms and practice shows, self – protection measures of creditors are not a full substitute to mandatory law for debt recovery.[638] Moreover, established remedies are relevant not only in case of insolvency, but even before that. As a rule, there is no group liability, which undermines the principles of separate legal personality and limited liability. Creditors must satisfy their claims against the company with which they have contracted. The limited liability should protect shareholders from additional liability from rational economic activities; it should not protect shareholders from liability that arises from abuse of it. The parent company is not a passive investor, it uses *de facto* control and spreads the risk onto subsidiaries. A creditor of a subsidiary is exposed to a parent company's opportunism and intra-group transactions, misrepresentation of value, debt dilution, asset transferring etc.[639] In a group of companies setting, the piercing of the corporate veil does not create unlimited liability for the parent company's shareholders; it rather allows it to reach assets of the parent company. The creditor interests outside of general company law are protected whether by German compensatory mechanism or within the legal environment of French safe harbour for pursuing the interest of the group. A parent company's liability for its subsidiaries would not only limit transgression, but also create incentive (not a duty) for supervision.[640]

Extended liability for a subsidiary must be approached with due diligence because a structure of a group of companies is lawful and the rationality for creating it is to limit exposure.

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[636] Sørensen, K.E. (2021). The Legal Position of Parent Companies: A Top–Down Focus on Group Governance. *European Business Organization Law Review (EBOR)*. Volume 22. P. 449. https://doi.org/10.1007/s40804-021-00211-5

[637] Ferran, E. (2006). Place for creditor protection on the agenda for modernisation of company law in the european union. *European Company and Financial Law Review (ECFR)*. Volume 3, issue 2. P. 214. https://doi.org/10.1515/ECFR.2006.008

[638] Mülbert, P.O. (2006). A Synthetic View of Different Concepts of Creditor Protection, or: A High-Level Framework for Corporate Creditor Protection. *European Business Organization Law Review (EBOR)*. Volume 7, Issue 1. PP. 375 – 377. https://doi.org/10.1017/S1566752906003570

[639] Kraakman, R., Armour, J., Davies, P., Et al. (2009). The Anatomy of Corporate Law. Oxford 2nd edition. PP. 116 and 127-128.

[640] Sørensen, K.E.(2021). The Legal Position of Parent Companies: A Top–Down Focus on Group Governance. *European Business Organization Law Review (EBOR)*. Volume 22. P. 449. https://doi.org/10.1007/s40804-021-00211-5

The legal personality of a subsidiary must be respected, and creditors protection does not justify disregarding it in all circumstances. It is also possible that the interest of the group does not coincide with the interest of the parent company, e.g., the parent company's obligation to provide extra funding to a subsidiary to avoid insolvency might be in the interest of the group to save its reputation, but contradicts autonomous interests of the parent company. However, the group of companies' structure is used to obtain advantages, but denied in order to circumvent adverse circumstances, especially financial difficulties. The data of general creditor rights score shows that German creditor right protection is ahead of the French system.[641] Nevertheless, the German compensatory system of creditor protection in a group of companies is heavily criticized for being burdensome, but opposite from French safe harbour framework at the same time offers direct liability of a parent company. In accordance of Article 101 and 102 of the TFEU, direct liability to the parent company as ultimate controller has been implemented already in competition law.[642] Reference to competition law approach has also been made in Article 150 of the Preamble of General Data Protection Regulation for the purpose to ensuring direct liability to the parent company.[643] It can be concluded that there are already legal acts that pierce the corporate veil in order to establish direct liability to the parent company.

To avoid the German compensatory system's burden, but still ensuring long - term sustainability and profitability of a subsidiary, the legal act for recognising the interest of the group could prescribe that a subsidiary's losses suffered could also be compensated in the future. Any other monetary benefit granted to a subsidiary should minimize the compensation's amount payable by a parent company. In the contemplation that no remuneration has been granted the legal act for recognising the interest of the group could determine that the parent company assume subsidiary losses in insolvency proceedings. In pursuance of encouraging the parent company to remunerate subsidiary's losses suffered, the parent company must acknowledge such losses in their annual accounts, therefore, it will be in their interests to minimise the losses in its subsidiaries in order to maximise their profits.[644] German contractual

[641] Ferran, E. (2006). Place for creditor protection on the agenda for modernisation of company law in the european union. *European Company and Financial Law Review (ECFR)*. Volume 3, issue 2. P. 215.
[642] Wils, Wouter P.J. (2000). The undertaking as subject of EC competition law and the imputation of infringements to natural or legal persons. *European Law Review*. Volume 25, issue 2. P. 108.
[643] REGULATION (EU) 2016/679 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) (Text with EEA relevance). Adopted on 4 May 2016. Published in the Official Journal of the European Union L 119/1.
[644] Corporate Group Law for Europe (2000): Forum Europaeum Corporate Group Law (2000). European Business Organization Law Review (EBOR). Volume 1, issue 2. P. 194. https://doi.org/10.1017/S1566752900000148

group compensatory model's criticism for far reaching liability without causal link between issued instructions and losses suffered still is applicable. Furthermore, the duty of a parent company to cover all losses puts a subsidiary's creditors in a position that independent companies' creditors do not enjoy. As a matter of fact, insolvency may be caused by various factors, e.g., financial crisis, changes in legal environment etc., which can also be unrelated to instructions given by the parent company.[645] In order to preserve capital accumulation, liability of a parent company can be scaled down to transactions that are detrimental or disadvantageous to a subsidiary. Nevertheless, German criticism of *de facto* group compensatory mechanism for uncertainty to determine transactions that are disadvantageous to the subsidiary and if so, which particular transaction and to what extent is also relevant in this case.[646] *Rozenblum* doctrine's established maintenance of financial equilibrium is suited to ensure certainty and promotion of relief of administrative burden. It means that a parent company is liable for instructions that exceed a subsidiary's possibilities or, in other words, might trigger the risk of insolvency.

The cash pooling arrangements transmit the risk that subsidiary's funds have been transferred to the insolvent member of the group or liquidity surplus could be invested in more remunerative investments.[647] To safeguard a subsidiary's interests in cash pooling by reducing overall debt and to avoid the risk of being drawn into insolvency proceedings following protective measures should be implemented: 1) debit and credit positions should be distinguished ; 2) remuneration of investment at market rates; 3) guarantees and/or collateral should against the investment should be received; 4) the right to refuse to continue to participate in cash pooling or requiring additional guarantees and/or collateral.

It is presumed that the parent company is informed about the state and affairs of a subsidiary, but genuinely there can still be asymmetry of information, which can also make it difficult to determine an amount of compensation.[648] Article 9 the Transparency Directive

[645] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97/2008. P. 30. http://dx.doi.org/10.2139/ssrn.1115737

[646] Houwen, L.G.H.J., Schoonbrood - Wessels, A.P., Schreurs, J.A.W. (1993). Aansprakelijkheid in concernverhoudingen. Een rechtsvergelijkende studie naar de positie van crediteuren van concern- afhankelijke vennootschappen in Duitsland, Frankrijk, Engeland en Nederland. Deventer. Kluwer Law International. P. 236-238.

[647] Colangelo, A. (2016). The statistical classification of cash pooling activities. European Central Bank. Statistics Paper Series. Number 16. P. 4.

[648] Conac, P.H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 310. https://doi.org/10.1515/ecfr-2016-0301

merely requires that listed companies to notify when a group of companies is formed.[649] However, Article 19 of the Accounting Directive imposes preparation of the management report in the consolidated financial accounts with the purpose of ensuring that the creditors and shareholders are presented with precise information of the group of companies well – being and to prevent asymmetry of information.[650] Consequently, the parent company is able to receive necessary information to calculate and recognise the respective losses of a subsidiary in their annual account. The consolidated financial accounts are prepared at the end of the financial year, but the information might be needed sooner, though the parent company can exercise the right to ask questions in general meetings, which is all around protected by general company law rules in Member States.

Attributing direct liability to a parent company would bring judicial consideration of the parent company's acts and direct remedy to creditors (limits denial of access to remedies). In line with a general principle of abuse of rights, EU law would not protect the legal environment, in which a board of directors' act is prejudicial to a subsidiary's interests, but escapes liability towards the company they manage and its creditors on the basis that they acted in pursuit of the interests of the group and closely under the instructions of the parent company.[651] Further, featured extra liability to a parent company's board of directors would paralyse decision making within the group.[652] Accordingly, the legal act for recognising the interest of the group should include direct liability to a parent company for compensating for instructions that are detrimental or disadvantageous to a subsidiary's interests, but should not exclude the liability of a subsidiary's board of directors; though does not impose additional liability of a parent company's board of directors.

[649] Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC. Latest Amendments on 5 January 2023. Adopted on 31 December 2004. Published in the Official Journal of the European Union L390/38.

[650] Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance. Adopted on 29 June 2013. Published in the Official Journal of the European Union L182/19.

[651] Werlauf, E. (2003). EU Company Law: Common Business Law of 28 Member States. Djoef publishing. 2nd edition. P. 456.

[652] Farmery, P. (1986). The EC Draft Proposal For a Ninth Company Law Directive on Groups: A Business Viewpoint. *Business Law Review*. Volume 7, Issue 3. P. 90. https://doi.org/10.54648/bula1986030

### 4.2.4. Minority shareholder protection

The legal act recognising the group's interest grants the parent company a right to define and pursue that interest. However, this right threatens not only creditor, but also minority shareholder rights.[653] At the EU level it is acknowledged that shareholder protection (especially for those shareholders who are in the weaker position) has great importance for sustainability and profitability of the Internal Market.[654] Thereupon, if a legal act recognises the interest of the group, additional protection for minority shareholder rights are necessary. In a subsidiary, minority shareholder protection is needed against a parent company's conduct that may be detrimental to other shareholders. Although a pursuit of the interest of the group includes burden and benefit sharing, redress should be available for detrimental transactions to a subsidiary and its minority shareholders.[655] Otherwise, a parent company by taking advantage of a control on a subsidiary could extract benefits for itself without sharing it with other shareholders.[656] A key issue with protecting minority shareholders in group of companies is the vast difference in how Member States approach this. These Member State protection mechanisms often rely heavily on judicial discretion, which unfortunately leads to undesirable uncertainty.[657]

Shareholders can be categorised as shareholders outside of the group (external shareholders) and shareholders that are members of the group, as well as minority and majority shareholders. While all shareholders are technically stakeholders in a company, the distinction lies in their involvement. Shareholders, regardless of where they originate (internal or external), rely on the understanding that they represent diverse interests. If multiple shareholders align their interests, they might be considered part of the same shareholder group. Aforesaid division

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653 Conac, P.H. (2013). Director's Duties in Groups of Companies – Legalizing the Interest of the Group at the European Level. *European Company and Financial Law Review (ECFR)*. Volume 10, issue 2. P. 195. https://doi.org/10.1515/ecfr-2013-0194

654 European Commission. (2012). Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies. COM(2012) 740 final. P. 9. Accessed 27 May 2024. Available at: https://eur-lex.europa.eu/legal-content/EN/ALL/?uri=celex%3A52012DC0740

655 European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19

656 Wymeersch, E. (2001). Financial Institutions as Members of Company Groups in the Law of the European Union. *European Business Organization Law Review (EBOR)*. Volume 2, issue 1. P. 84. doi:10.1017/S1566752900000343

657 Miller, S.K. (1997). Minority shareholder oppression in the private company in the European Community: a comparative analysis of the German, United Kingdom and French close corporation problem. *Cornell International Law Journal*. Volume 30. Cornell University. P. 392.

of shareholders is only implemented in German *Konzernrecht* and following systems. Based on the quantitative approach, shareholders can be distinguished by ownership (percentage of the capital) because it determines voting rights, which, in turn, allows them to direct the company. However, rights and obligations of a shareholder can be more complex than one share - one vote, e.g., agreement with other shareholders to provide voting rights or appointment or removal of members of the board directors. A qualitative approach examines the control rather than percentage of the capital. Particularly investigated is its influence on the functioning of the company. Qualitative approach to shareholder categorization also covers a case when legally separate shareholders represent the same interest while independently being minority shareholders. Furthermore, to keep neutrality of a legal act for recognition of the interest of the group dispensable associations to German *Konzernrecht* and a failed attempt to regulate group of companies by the Ninth Company law directive can be avoided by simply using a qualitative approach of distinguishing minority and majority shareholders.

The common denominator is that Member State practices of minority shareholder protection are applicable to both the parent company and the subsidiary. The discrepancy between Member State practices can be found in whether special treatment for minority shareholders is provided. On the one hand, there is the position that minority shareholders in a group of companies in principle is not different from that of any other minority shareholder and general company law rules dealing with minority shareholders are applicable.[658] The *Rozenblum* doctrine in France does not stipulate additional protection to minority shareholders, therefore, they are left to rely on general company law rules on the abuse of majority or equality, the termination/dissolution of the company, declaring acts of corporate body null and void, raising the claim for damages. The Netherlands also follows the notion that there is no need to separately protect minority shareholders, but provides squeeze out rights to the parent company (Article 2:201a(92a) of *BW*).[659] Although Italy also follows the respective notion, after the 2004 Company law Reform minority shareholder protection was expanded and exit rights were implemented (Article 2497, paragraph 4 of *Codice Civile*).[660]

On the other hand, the German *Konzernrecht* model of minority shareholder protection

[658] European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward. Accessed 27 May 2024. Available at: https://europeancompanylawexperts.wordpress.com/publications/reforming-group-law-in-the-eu/#_ftn19

[659] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Article: : Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P. 223.

[660] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).

prescribes a separate legal framework in a group of companies setting because a subsidiary is subordinated to the interests of the parent company, which creates conflict of economic interests.[661] German *Konzernrecht* system provides exit rights for minority shareholders, if a group of companies contract has been concluded (in Germany Article 305 of *AktG*,[662] in Latvia Article 24 of *Koncernu likums*[663]) and also rules on indemnity or appropriate compensation to minority shareholders, if they stay in the company after group of companies contract is entered (in Germany Article 304 of *AktG*,[664] in Latvia Article 23 of *Koncernu likums*[665]). Additionally, buy out rights have been introduced in Latvia (Latvia Article 47 of *Koncernu likums*)[666] and in Portugal (Portugal Article 490 of *CSC*).[667] Nonetheless, neither in Germany, nor Latvia, nor Portugal can squeeze out rights be found specific for group of companies. The squeeze out rights should not be confused with Latvian take-over (Article 35 – 36 of *Koncernu likums*)[668] or German integration (Article 319 – 320 of *AktG*)[669] because those are specific instruments to achieve central management with the cost of additional liability. Also Latvian buy out rights (Article 47 of *Koncernu likums*)[670] and Portuguese (Article 490 of *CSC*)[671] duty to acquire remaining shares are not squeeze out rights because it protects minority shareholders rather than proposes an opportunity for a majority to acquire shares. Even supposing the intent of explicitly protecting minority shareholders still various mechanisms and excessively protracted

[661] Emmerich, V., Sonnenschein, J., Habersack, M. (2001). Konzernrecht: Das Recht der verbundenen Unternehmen beu Aktiengesellschaft, GmbH, Personengesellschaften, Genossenschaft, Verein und Stiftung. 7. Auflage. München. Verlag C.H. Beck. S. 12-13.

[662] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[663] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[664] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[665] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[666] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[667] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

[668] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[669] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[670] Ibid.

[671] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

judicial reviews still exist.[672]

Instruments in a legal act for recognising the interest of the group aimed at the protecting of minority shareholders in a group of companies should cover fundamental rights of exit, buy out, squeeze out and acquiring of information. Minority shareholder protection is not applicable in wholly owned subsidiaries, in which 100% shares are owned by a parent company, but creditor protection is still a concern.

According to corporate opportunity doctrine, the interests of a company have to be protected in a case where members of a management body or members of the group take advantage of a particular business opportunity that the respective company itself could have taken advantage of, e.g., a subsidiary has the opportunity to enter into a profitable agreement, but a parent company decides that different subsidiary should enter into this agreement, therefore, there is loss of revenue, which can be detrimental to minority shareholders.[673] Due to the fact that the interest of the group is pursued, the subsidiary's economic development can be limited. In such a case minority shareholders of the subsidiary should receive appropriate compensation. Such a right should be implemented with caution because it can become very costly and hamper the development of group of companies, if exit rights are applied whenever a control is established. Moreover, those Member States that provide exit rights in a group of companies situation, prescribe different conditions for exercising respective right. In the German *AG* (Article 305 of *AktG*)[674] and the Latvian group of companies (Article 24 of *Koncernu likums*)[675] exit right can be exercised by a minority shareholder, if a group of companies' contract is concluded, but in German GmbH group of companies based on substantial basis.[676] In Italy, minority shareholders can exercise exit rights, if the parent company has violated Article 2497 of *Codice Civile* or direction and coordination (the right to give instructions) has been implemented or ended (Article 2497, paragraph 4 of *Codice Civile*).[677] Czech group of companies law prescribes exit rights, if exercised control

[672] Beyerle, K. (1977). Erfahrungen mit dem Spruchstellenverfahren nach § 306 AktG. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. Band 6, Ausgabe 4. S. 650. https://doi.org/10.1515/zgre.1977.6.4.650

[673] JACKSON, J., E. (1988). Corporate Opportunity Doctrine: A Historical View with a Proposed Solution. *Missouri Law Review*. Volume 53, issue 2. P. 394. https://doi.org/10.2307/1599853

[674] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[675] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[676] Scogin Jr., H.T. (1993). Withdrawal and Expulsion in Germany: A Comparative Perspective on the "Close Corporation Problem". *Michigan Journal of International Law*. Volume 15, issue 1. P. 155.

[677] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).

substantially interferes (damages caused) with a company's autonomous interests.[678] Even though various conditions are stipulated for exercising exit rights, the common measure is implied changes that directly alters economic and financial conditions of the subsidiary, i.e. differences liaise in the form of exercising the right to give instructions. Thereupon, the legal act for recognising the interest of the group should institute that the precondition for the exercising the exit right is pursuit of the interest of the group, which alters economic and financial interests of a subsidiary. Furthermore, preconditions for minority shareholders to exercise exit rights are present because it is unjustifiable to require a company (to a subsidiary or a parent company) to maintain higher level of liquidity just in the case that minority shareholders at any time could demand to buy back its shares. [679]

There are various forms of compensation that can be introduced: 1) shares of a subsidiary are exchanged for the shares of a parent company; 2) guaranteed or reasonable annual dividends; 3) cash.[680] Minority shares can be bought by a subsidiary, a parent company or a third person. Member States have already experience with provided compensation mechanisms in the context of mergers, therefore, the legal act of recognition of the interest of the group should leave to Member States to choose the options mentioned, which compensation forms are the most appropriate for protecting minority shareholders and fit their legal framework. It is important to highlight that guaranteed or reasonable annual dividends have been implemented in Germany (Article 304 of *AktG*)[681] and in Latvia (Article 23 of *Koncernu likums*)[682] in a form of indemnity payment, if group of companies' contract is concluded. However, this is a different instrument than exit rights because minority remains in the company. This does not constitute an appropriate form of compensation for leaving the company and should not be implemented in the legal act for recognising the interest of the group.

The concern is how to determine the price or value of the share. Since most of companies are not listed on the stock exchange it is quite difficult to determine the market value

[678] Havel, B. (2015). Czech corporate law on its way. European Company and Financial Law Review (ECFR). Volume 12, isue 1. P. 36. https://doi.org/10.1515/ecfr-2015-0019

[679] Conac, P. H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 318. https://doi.org/10.1515/ecfr-2016-0301

[680] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 195. https://doi.org/10.1017/S1566752900000148

[681] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[682] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

of shares.[683] The reviewing of the price or value of shares in Germany is in the court's competence (Article 306 *AktG*)[684], in Latvia (Article 24, paragraph 8 of *Koncernu likums)*[685]and Austria (Article 225m of *österreichisches Aktiengesetz* (*öAktG*))[686] an expert commission can assist the court. In Great Britain the court delegates such assessment to an expert.[687] The legal act recognising the interest of the group could set a framework or determine guidelines for establishing the market value of a share, but regardless it cannot replace judicial review.[688] Determining share price or value is not an issue unique to group of companies. The same problem arises in takeovers requiring minimum prices and mergers requiring fixed share exchange rates.[689] Consequently, Member States have experience with dealing with this issue. Therefore, the legal act recognising the interest of the group could leave establishing measurers for determining share price or value to Member States, as long as the compensation is appropriate and ultimately reviewed by a court or official authority.

A company shall not be compelled to deal with minority (small residual) shareholders, if appropriate acquiring of remaining shares is not considered.[690] It is also an approach to promote the creation of fully integrated groups (wholly owned subsidiaries). In a group of companies setting small residual shareholders are burdensome without real economic benefit. It is typical that group of companies are 100% owned by the same shareholder. The squeeze out right means that the majority shareholder can request that a minority shareholder to transfer their shares.[691] The compensation for a transfer of shares must be specified in a squeeze out request. If an agreement is not achieved between a majority and a minority shareholder, the compensation of a transfer of shares should be determined by a court. At the EU level squeeze

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[683] Hopt, K., Pistor, K. (2001). Company Groups in Transition Economies: A Case for Regulatory Intervention? *European Business Organization Law Review* (EBOR). Volume 2, issue 1. P. 11. https://doi.org/10.1017/S1566752900000318

[684] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[685] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[686] Austrian Stock Corporation Act. Adopted on 31 March 1965, BGBI. Nr. 98/1965. Entry into force 1 January 1966. Last amendments BGBI. Nr. 63/2019.

[687] Lutter, M. (1998). Die Funktion der Gerichte im Binnenstreit von Kapitalgesellschaften – ein rechtsvergleichender Überblick. *Zeitschrift für Unternehmens- und Gesellschaftsrecht (ZGR)*. Band 27, Heft 2. S. 191. https://doi.org/10.1515/zgre.1998.27.2.191

[688] Hopt, K., Pistor, K. (2001). Company Groups in Transition Economies: A Case for Regulatory Intervention? *European Business Organization Law Review (EBOR)*. Volume 2, issue 1. P. 11. https://doi.org/10.1017/S1566752900000318

[689] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 195. https://doi.org/10.1017/S1566752900000148

[690] Ibid, P. 271.

[691] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97/2008. P. 264. http://dx.doi.org/10.2139/ssrn.1115737

out rights are considered as must have.[692] The squeeze out right can be found also in Article 15 of the Takeover Bids Directive.[693] If a parent company or a subsidiary itself has the obligation after a minority shareholder's request to acquire its shares then a parent company must have the opportunity to acquire small residual shareholder's shares because exit rights and squeeze out right are corresponding rights.[694] Thereupon, implementation of exit rights provides just legal ground to also introduce squeeze out rights against small residual shareholders as well.

Member States regard a small residual minority as a shareholder who owns between 5-10% of shares, e.g., in Latvian take – over and buy out 10% (Article 36, paragraph 1 and Article 47 of *Koncernu likums*),[695] in German integration 5% (Article 320 of *AktG*),[696] in Portuguese duty for acquiring of shares 10% (Article 490 of *CSC*),[697] in Dutch squeeze outs rights 5% (Article 2:201a(92a) of *BW*).[698] The legal act for the recognition of the interest of the group could grant the right to squeeze out, if majority holding is at least 90%, but not higher than 95% depending on legal traditions of a Member State. Minority shareholder protection is still effective, if 90% majority holding is necessary for exercising squeeze out rights, because it applies only to a specific case of a small residual minority. Similar to exit rights mere establishment of a control does not give the right to oppress minority shareholders. Introduction of the ceiling of 95% of majority holding would avoid a situation where Member States resist unification by increasing the majority holding to the point that it covers only very few cases. Furthermore, identical to exit rights determination of appropriate compensation can be left to Member States. Nevertheless, majority shareholders should not be required to prove any special circumstances for exercising the squeeze out right except majority holding). This is

[692] The High Level Group of Company Law Experts. (2002). Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe ('Winter Group Report'). P 13. Accessed 27 May 2024. Available at: https://ecgi.global/content/winter-group-2002

[693] Directive 2004/25/EC of the European Parliament and of the Council of 21 april 2004 on takeover bids (Text with EEA relevance). Adopted on 30 April 2004. Published in the Official Journal of the European Union L 142/12.

[694] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. PP. 189 - 190. https://doi.org/10.1017/S1566752900000148

[695] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[696] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.

[697] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

[698] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Article: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P. 223.

because balancing of interests is already implicitly assumed by the legal act for the recognition of the interest of the group, i.e., making it more difficult for a small, residual minority to challenge fair compensation in order to block majority shareholder's squeeze out rights.

Additionally, if squeeze out rights are implemented in the legal act for the recognition of the interest of the group, buy out rights should also be provided for minority shareholders. Under buy out rights, a small residual minority can request that the majority holding to acquire its shares, e.g., in Latvia (Article 47 of *Koncernu likums*),[699] in Portugal (Article 490 of *CSC*).[700] Furthermore, buy out rights stipulate supplementary mechanisms for small residual minorities to leave the group, if the majority is not exercising their squeeze out rights to avoid paying compensation for acquiring shares or group interests are not pursued. In contrast, a small residual minority without buy out rights would have no other remedies available, e.g., in a case of lack of payments of dividends. On the grounds that buy out rights are applicable only to a small residual minority, a subsidiary or a parent company would not seek to have excessively higher liquidity. At the EU level, it is considered that buy out rights have to be attributed to small residual shareholders.[701] Buy out rights can be found in Article 16 of the Takeover Bids Directive.[702] Buy out rights like exit rights are corresponding rights to squeeze out rights, thus the regulatory framework for the definition of small residual minority shareholders, balancing interests and appropriate compensation can be kept the same as for exit rights and squeeze out rights.

Shareholder involvement hinges on the ease and cost of exercising their rights. Adequate information provision empowers shareholders to effectively exercise their rights and protect their interests, with their focus extending beyond wealth creation to include competent oversight of company management. [703] In a group of companies the parent company can abuse asymmetry of information. To safeguard minority shareholders, a framework for information

[699] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.

[700] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.

[701] The High Level Group of Company Law Experts. (2002). Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework for Company Law in Europe ('Winter Group Report'). P 13. Accessed 27 May 2024. Available at: https://ecgi.global/content/winter-group-2002

[702] Directive 2004/25/EC of the European Parliament and of the Council of 21 april 2004 on takeover bids (Text with EEA relevance). Adopted on 30 April 2004. Published in the Official Journal of the European Union L 142/12.

[703] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97/2008. P. 256. http://dx.doi.org/10.2139/ssrn.1115737

access is essential.[704] This facilitates informed decisions on buyouts, exits and utilizing general company law to hold majority shareholders accountable.

Obtaining information is also a result of regulation of the group of companies itself. For instance, those Member States that regulate group of companies (group law or case law) transparency and nature and content of the disclosure is ensured by the norms that govern the right to give instructions (central management). In Germany, Latvia, Portugal the duty to cover losses of the subsidiary (Article 302 of *AktG,*[705] Article 20 of *Koncernu likums,*[706] Article 502 of *CSC*)[707] or to compensate disadvantageous transactions (Article 311 of *AktG*[708] and Article 29 of *Koncernu likums)*[709] and dependency report (Article 312 of *AktG*[710] and Article 30 of *Koncernu likums*).[711] In Italy, a motivated annual report of the board directors has to be drafted (Article 2497 – *ter* of *Codice Civile*).[712] In France group of companies related information for the application of *Rozenblum* doctrine is disclosed only in court proceedings.[713]

Accounting and disclosure rules are the most commonly used instruments for minority shareholder protection in autonomous and group of companies.[714] EU accounting and disclosure rules merely identify subsidiaries and the shares held by the parent company. While further information may be available for listed companies, there is no obligation to update this information unless new securities are offered. Shareholders right to ask for information is stipulated in Article 9 of Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies

[704] Corporate Group Law for Europe. (2000). Forum Europaeum Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. P. 185. doi:10.1017/S1566752900000148
[705] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[706] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[707] Código das Sociedades Comerciais Decreto-Lei n.º 262/86 de 2 de Setembro. Alterações: Lei n.º 49/2018, de 14 de Agosto. Diário da República n.º 201/1986, Série I de 1986-09-02.
[708] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[709]Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[710] Stock Corporation Act. Adopted on 6 September 1965, published in Federal Law Gazette I, P. 1089. Amended by Article 9 of the Act of 17 July 2017, published in Federal Law Gazette I P. 2446.
[711] Koncernu likums. Pieņemts 23.03.2000. Stājies spēkā 27.04.2000. Publicēts Latvijas Vēstnesis, 131/132, 13.04.2000.; Latvijas Republikas Saeimas un Ministru Kabineta Ziņotājs, 9, 04.05.2000. Pēdējie grozījumi 14.04.2006.
[712] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).
[713] Reflection Group on the future of EU company law. (2011). Report of the Reflection Group on the Future of EU Company Law ('Reflection Group Report'). P 59. http://dx.doi.org/10.2139/ssrn.1851654
[714] Hopt, K. J. (2015). Groups of Companies A Comparative Study on the Economics, Law and Regulation of Corporate Groups. European Corporate Governance Institute. Law Working Paper No. 286/2015. P. 10.

(Shareholders Rights Directive).[715] Consequently, Member State practices and EU accounting and disclosure rules in group of companies are efficient for transparency of solvency and determination of compensation for pursuing the interest of the group, but are dubious for minority shareholder protection. The problem is even worse for those countries that do not have a group of companies' law because general company law rules for independent companies are not well furnished to deal with disclosure and transparency of central management. The legal act for recognition of the interest of the group should include an obligation to the board of directors to provide in a timely manner coherent and accurate information including, but not limited to company accounts and circumstances, which can affect the company's or group's financial situation.

There can be distinguished two requests of information: 1) downstream; 2) upstream. Under downstream request the parent company's shareholders have the right to information for operations conducted in the subsidiary.[716] The parent company requests information from the subsidiary for legal reasons (e.g. drawing up consolidated accounts).[717] Further, abusive practices and problematic operations can be hidden at the level of a subsidiary (especially in a cross-border group of companies). To prevent situations where questions about the group can be refused to be answered by arguing that information is located at the level of the subsidiary, the parent company should possess the right to obtain any information from a subsidiary, provided such access does not violate the right of third parties or national law. Under upstream request the subsidiary receives the information about operations of the parent company.[718] Traditionally upstream requests of the information are not acknowledged because shareholders of the subsidiary are not shareholders of the parent company (exception is Netherlands Article 2:351 of *BW*). [719] Granted that the interest of the group can be pursued by forming a single economic unit than by minority of shareholders of a subsidiary who are also a part of the group.

[715] Directive 2007/36/EC of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies. Adopted on 14 July 2007. Published in the Official Journal of the European Union L 184/17.

[716] Conac, P. H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 315. https://doi.org/10.1515/ecfr-2016-0301

[717] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97/2008. P. 390. http://dx.doi.org/10.2139/ssrn.1115737

[718] Conac, P. H. (2016). The Chapter on Groups of Companies of the European Model Company Act (EMCA). *European Company and Financial Law Review (ECFR)*. Volume 13, issue 2. P. 316. https://doi.org/10.1515/ecfr-2016-0301

[719] Burgerlijk Wetboek Boek 2. Geldigheidsdatum: 1 januari 1992. Bronpublicatie inwerkingtreding: 20-02-1990, Stb. 1990, 90 (uitgifte: 01-01-1990, kamerstukken/regelingnummer. English translation of cited Articles: Warendorf, H., Thomas R., Curry-Summer I. (2009). The Civil Code of the Netherlands. Kluwer Law International. P.365.

Besides, decisions at the top (the parent company) can be highly disruptive to subsidiaries, causing significant damage. Nevertheless, the right to upstream information can also be abused (e.g., to reveal trade secrets to third parties, outside interests being promoted etc.) therefore, it should be strictly limited to decisions that affect the subsidiary.

A company (especially being a part of the group) should not be able to hide from requests of information in jurisdictions with less demanding national law. If a company refuses of downstream or upstream requests, there should be remedies available for withholding of information. Without extending disclosure and transparency rules the scrutiny of group of companies relations will be difficult to facilitate.[720] The remedies available to a shareholder who has not received the information requested depends upon the judicial system of each Member State (there can be court order to provide information, fine, special investigation etc.).[721] It is noted that disclosure rules on group of companies at the EU level should not be of a technical nature.[722] Member States shall regulate further the details of the procedure for receiving the information and be free to impose regulations, which are more onerous than those proposed here. The scope of right to request information should apply only in a group of companies setting making it more acceptable in Member States where such feature is not implemented.

[720] Windbichler, C. (2000). Corporate Group Law for Europe: Comments on the Forum Europaeum's Principles and Proposals for a European Corporate Group Law. *European Business Organization Law Review (EBOR)*. Volume 1, issue 2. PP. 270 - 271. https://doi.org/10.1017/S156675290000015X

[721] Baums, T., Andersen P.K. (2008). The European Model Company Law Act Project. European Corporate Governance Institute (ECGI). Law Working Paper No. 97/2008. P. 390.

[722] The Informal Company Law Expert Group (ICLEG). (2016). Report on Information on Groups. P. 11. http://dx.doi.org/10.2139/ssrn.2893694

## CONCLUSIONS AND PROPOSALS

There is no recognition of the interest of the group at the EU level and Member States continue to operate based on differing approaches. Three types of models for recognition of the interest of the group prevail. The French model of *Rozenblum* doctrine provides "group defence" or "safe harbour", in which the interest of the group can be considered. The German *Konzernrecht* model is a compensatory model rather than recognition of the interest of the group. The third model is the traditional company law notion of a separate legal personality approach where the company is perceived as an independent legal entity and the interest of the group cannot be pursued. Despite the model chosen for recognition of the interest of the group, the subsidiary will find it difficult to bypass influence from the parent company. There is legal fragmentation because Member States have contrasting and even conflicting mechanisms for recognition of the interest of the group and at the EU level the respective issue is not regulated. This legal fragmentation increases the cost of doing – cross border business, facilitates short – term profit maximisation for shareholders over long – term sustainability and profitability of a company, hinders cash-pooling and impedes efficient allocation of resources. There is demand for uniformity of a single set of rules and the development of recognition of the interest of the group has stagnated at the Member States national law level, therefore, regulatory competition without regulatory intervention at the EU level will not produce common recognition of the interest of the group. In the view of all foregoing, exposed disparities between Member States' national law can be only eliminated by a harmonisation process at the EU level, in which the interest of the group is recognised with additional protection for creditors and minority shareholders.

**Conclusion No.1**

Although there is legal fragmentation in Member State's regulatory framework for recognition of the interest of the group, concerns remain the same, i.e., effective allocation of resources and creditor and minority shareholder protection. Nevertheless, the effect strived for, elimination of diverging approaches, requires not only general recognition of the interest of the group and protection of creditor and minority shareholder interests, but also depend on uniformity of those rules. Moreover, the issue has cross- border effect and a Member States by itself cannot create the required uniformity of rules, therefore, a legal act at the EU level must be adopted. Minimum standards established by the Directive can only partially eliminate respective diverging approaches. Recommendations are not legally binding, would therefore

not force approximation of laws and are better suited to be an intermediate legal instrument rather than final. Instead, the Regulation would enact uniformity of a single set of rules that would remove fully diverging approaches.

**Proposal No.1**

To reduce the impeding effects of legal fragmentation and improve conditions of cross-border activities, the proposed Regulation for recognising the interest of the group must be adopted in special legislative procedure, in accordance with the Article 352 of the TFEU. The title of the Regulation: Recognizing the Interest of the Group of Companies.

**COUNCIL REGULATION (EU) No. xxx/2024 of (date) on recognizing the interest of the group of companies**

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 352 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Parliament,

Having regard to the opinion of the European Economic and Social Committee,

Acting in accordance with the special legislative procedure

Whereas:

(1) In 2012 the Commission's action plan on European Company law and corporate governance announced an initiative on recognition of the interest of the group. In 2014 The EU created the Informal Expert Group on Company law in order to assist the Commission in the Company law field. In 2016 the Informal Expert Group on Company law published the report on the recognition of the interest of the group and concluded that there is legal fragmentation and the EU framework lacks legal certainty.

(2) The legal fragmentation increases the cost of doing cross - border business, facilitates short – term profit maximisation of shareholders over long – term

sustainability and profitability of a company, hinders cash-pooling and impedes efficient allocation of resources.

(3) The group structures have more and more cross - border elements and therefore there is a need to regulate companies by Union law. The proper functioning of the Internal Market requires recognition of the interest of the group.

**Conclusion No.2**

To ensure consistent application across the EU, the Regulation on the recognition of group interests should clearly define both the group of companies and the interests it represents. The definition of the group of companies and its interests establishes the scope of the Regulation. Considering historical development at the EU level of the issue of the recognition of the interest of the group, transposition of a specific Member States group of companies' law as a supranational legal act is not supported by other Member States, therefore, the terms used in the Regulation of the recognition of the interest of the group has to be neutral to avoid connotations with particular Member States' group of companies' codification. The term *Konzern* is closely linked with German *Konzernrecht,* but the term affiliated companies is associated with common law legal systems. The term Group has general meaning and is not connected with a specific legal system. Furthermore, Member States that follow a compensatory model call members of the group as dominant or controlling company and dependent or controlled company, which evidently has strong association with German *Konzernrecht.* The terms parent company and subsidiary have no connection with particular legal systems, but at the same time can be found in the EU's accounting and tax law, i.e., Accounting Directive and Parent/Subsidiary Directive, and Member States are already familiar with it.

For the purpose of enacting the scope of the Regulation for recognising the interest of the group, the basis for the definition of the group must be the concept of the control because it determines group of companies, while the concept of dominance/dependency creates rules for centralised management and profit shifting. The legal framework for recognising the interest of the group must be regulated separately from the scope of the Regulation, i.e., under the right to give instructions and creditor and minority shareholder protection. There is significant disparity between patterns of business conduct and a plurality of different corporate forms of companies in Member States, therefore, to ensure equal effect on application across the EU, the definition group of companies must cover all legal person forms. The definition of the interest of the group must apprehend a multitude of a corporate group structure and still

create universal standards. To safeguard a subsidiary's independence and risk of abuse, the interest of the group can be pursued in interrelated commercial activities by establishing coherent policy to achieve common interest.

**Proposal No.2**

Provide in the Preamble/Recital in the Regulation for the recognition of the interest of the group the legal basis and purpose and nature of the definition of the group of companies and its interests. Implement the definition of the group and its interests as the Article 1 (the scope) in the Regulation for the recognition of the interest of the group. The definition of the group consists of definitions of a company, a parent company and a subsidiary. Additionally, the section of Transitional and Final Provisions prescribes the EC the right to update the list of Member States companies' legal forms, in accordance with the Article 290 of the TFEU.

Whereas:

(4) For compatibility reasons, the group of companies are formed under the concept of the control enshrined in Article 22 of the Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance.

(5) This Regulation shall apply to the laws and regulations of the Member States relating to the types of company listed in Annex A, which covers public and private companies, listed companies, public law entities, as well as partnerships, but natural persons are excluded.

(6) The interest of the group is pursued, if there is proportionate burden and benefit sharing under group strategy that promotes well- being of the group rather than interests of particular member of the group. The pursuit of the interest of the group is a right not a duty.

## CHAPTER 1
## GENERAL PROVISIONS

Article 1

**Scope**

1. This Regulation shall apply for group of companies:

(a) a company means a legal person listed in Annex A;

(b) group of companies means a parent company and all its subsidiaries;

(c) a company is considered a parent company, if one of the following criteria is met:

(i) has majority voting rights;

(ii) can appoint or remove of majority of administrative, management or supervisory board;

(iii) has dominant influence based on a contract or articles of association.

(d) a company is considered a subsidiary, if it is controlled by a parent company, including through another subsidiary (ultimate parent company);

(e) The interest of the group can be pursued by the group of companies in interrelated commercial activities, based on coherent policy and to achieve common interest.

## CHAPTER 2
## TRANSITIONAL AND FINAL PROVISIONS

ARTICLE 6

**Exercise of delegated powers**

1. The Commission is empowered to update the list of Member States companies' legal forms, in accordance with Article 290 of the Treaty on the Functioning of the European Union.

**Conclusion No.3**

The interest of the group can be pursued only, if the group of companies' decisions and actions are fostered and coordinated by the group policy under the centralised management. In other words, for the pursuit of the interest of the group, legal entitlement to control of management must be prescribed. The group of companies is formed under the concept of the control, therefore, the right to give instructions to the management body can be attributed to shareholders, which means that the parent company must be able to issue instructions to its subsidiaries. Instructions issued must be legally binding to safeguard the pursuance of the interests of the group in the Internal Market where there are no common general duties of management. Benefit and burden sharing between companies arrange that instructions can be detrimental or disadvantageous to the subsidiary. However, to avoid abuse of rights, limits to the issuing instructions must also be set 1) cannot breach Member State's national law; 2) cannot violate articles of association; 3) are in the common interest of the group; 4) do not

threaten the existence of a company. The term instructions have no negative connotations (neutral), therefore, can be used in the Regulation for the recognition of the interest of the group.

**Proposal No.3**

Provide in the Preamble/Recital in the Regulation for the recognition of the interest of the group the legal basis and purpose and nature of the right to give instructions. Bestow in the Regulation for the recognition of the interest of the group as the Article 3 the right to give binding instructions to the parent company and set limitations to it.

Whereas:

(7) The notion of giving instructions can take many forms, thus the right to give instructions is not limited only to formal directions. The right to give instructions is recognised on the basis of the concept of t control, therefore, only the parent company can issue instructions. In the view of the benefit and burden sharing concept, issued instructions can be detrimental or disadvantageous to a subsidiary, but to safeguard long – term sustainability it must always be in the common interest of the group and cannot exceed possibilities of a company. Subsidiary's management failure to fulfil legitimate parent company's interests should be recognised as valid grounds for their removal.

## CHAPTER 1
## GENERAL PROVISIONS

Article 3

**Management**

1. The parent company has the right to give instructions to the management body of the subsidiary.
2. Instructions given by the parent company are not binding, if they infringe the applicable national law or articles of association, threaten the existence of a subsidiary or are not in the common interest of the group.

**Conclusion No.4**

The benefit and burden sharing in the pursuit of the interest of the group endangers the creditor position, i.e., affects solvency of a company, especially, if a subsidiary follows disadvantageous or detrimental instructions from a parent company. Consequently, creditor interest must be additionally protected by the Regulation for the recognition of the interest of the group. However, extended liability would facilitate low – cost capital flow, but it must be balanced with the principle of separate legal personality and limited liability in order to protect capital accumulation. While general liability of a parent company for all subsidiary losses disrupts the necessary balance, targeted liability for detrimental or disadvantageous instructions from the parent company would foster the desired level of cohesion.

**Proposal No. 4**

Provide in the Preamble/Recital in the Regulation for the recognition of the interest of the group the legal basis and purpose and nature of the creditor protection, as well as distinguish between liability of board of directors and a company. Introduce the Article 4 in the Regulation for the recognition of the interest of the group, which prescribes direct liability of a parent company, losses suffered can be compensated in the future, but in the case of insolvency, the parent company assumes losses for detrimental or disadvantageous transactions that exceed a subsidiary's possibilities.

Whereas:

(8) Creditors of a subsidiary have the right to directly satisfy claims for losses suffered against the parent company. The parent company acknowledge losses suffered by a subsidiary due to the detrimental or disadvantageous instructions, according to rules of Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC Text with EEA relevance.

(9) The liability framework of the parent company is only applicable, if given instructions are compatible with criteria imposed for pursuing the interest of the group. The parent company's liability does not exclude the liability of a subsidiary's management body. This Regulation does not prescribe additional liability to a parent company's management body.

## CHAPTER 1
## GENERAL PROVISIONS

Article 4

### Creditor protection

1. Direct liability of a parent company is attributed towards a subsidiary's creditors.
2. The parent company is liable to cover losses suffered by a subsidiary for following detrimental or disadvantageous instructions in order to pursue the interest of the group.
3. The parent company must acknowledge such losses in their annual accounts.
4. Losses suffered from pursuing the interest of the group can be compensated in the future. Any monetary benefit granted to a subsidiary reduces the compensation's amount payable by a parent company.
5. In case of insolvency, the parent company assumes losses for detrimental or disadvantageous transactions that exceeded a subsidiary's possibilities.

**Conclusion No.5**

The pursuits of the interest of the group can also affect the interests of minority shareholders, i.e., profitability of a company. Fundamental rights of exit, squeeze out, buy out and acquiring of information would provide checks and balances needed to counterbalance the pursuit of the interest of the group. Minority shareholder protection is concerned at both levels of the parent company and the subsidiary.

Exit rights provide a legal framework, in which minority shareholders can leave the company for appropriate remuneration. However, the capital accumulation would be hampered, if exit rights could be exercised by minority shareholders whenever a control is established. Thereupon, the exercise of exit rights is limited only to cases when the interest of the group is pursued.

Under squeeze out rights majority shareholders can request to minority shareholders to transfer their shares for appropriate compensation. Squeeze out rights are corresponding rights to exit rights. There is no real economic benefit of small residual shareholding. However, it means that squeeze out rights can be exercised only against minority shareholders who are small residual shareholders.

In contrast, majority shareholder can decide not to exercise squeeze out rights to avoid payment of compensation to small residual shareholders who have no decisive influence. If the

interest of the group is not pursued, small residual shareholders cannot exercise exit rights and have no other remedies available. Consequently, small residual shareholders must be able to request that a majority holder to acquire their shares, if the interest of the group is not pursued.

The recognition of the interest of the group fosters asymmetry of information, therefore, the obtaining of information has to be additionally safeguarded. The Regulation for the recognition of the interest of the group must provide the legal obligation on the management body to provide in timely manner coherent and accurate information about accounts and circumstances, which can affect the company's or group's financial situation. Requests to obtain information can be in both directions of upstream and downstream.

**Proposal No. 5**

Provide in the Preamble/Recital in the Regulation for the recognition of the interest of the group the legal basis and purpose and nature of the minority shareholder protection. In the Article 2 of the Regulation for the recognition of the interest of the group, implement the definition of small residual shareholders and upstream and downstream requests of obtaining information. In the Article 5 the Regulation for the recognition of the interest of the group provides exit, squeeze out and buy out rights, as well as the right to obtain the information.

Whereas:

(10) For minority shareholder to exercise the right of exit, the interest of the group pursued must alter the economic and financial interests of a company. The compensation for exit rights can be 1) shares of a subsidiary exchanged for the shares of a parent company; 2) cash. For squeeze out and buy out rights cash shall be the form of compensation.

## CHAPTER 1
## GENERAL PROVISIONS

Article 2

**Definitions**

For the purpose of this Regulation:

(1) "Small residual shareholder" means a shareholder, if the majority holding is at least 90%, but not higher than 95% depending on legal traditions of applicable national law;

(2) “Downstream request” means the parent company’s request to obtain information for operations conducted in the subsidiary;
(3) “Upstream request” means the subsidiary’s request to obtain information for operations conducted in the parent company.

Article 5

**Minority shareholder protection**

1. Minority shareholder has the right to request that parent company acquires it shares for appropriate compensation, if the interest of the group is pursued (exit right);
2. The parent company has the right to request small residual shareholders to transfer their shares for appropriate compensation (squeeze out right);
3. A small residual shareholder has the right to request that the parent company to acquire its shares, if the interest of the group is not pursued (buy out right).
4. The management body has a legal obligation arising from upstream or downstream requests to provide in timely manner coherent and accurate information about accounts and circumstances, which can affect the company’s or group’s financial situation.

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12. Judgment of the Court (Sixth Chamber) of 30 November 1995 in the case C-134/94, Esso Española SA v Comunidad Autónoma de Canarias;

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14. Judgment of the Court (Fifth Chamber) of 20 February 1997 in the case C-260/95, Commissioners of Customs and Excise v DFDS A/S;

15. Judgment of the Court of 12 May 1998 in the case C-367/96, Alexandros Kefalas and Others v Elliniko Dimosio (Greek State) and Organismos Oikonomikis Anasygkrotisis Epicheiriseon AE (OAE);

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23. Judgment of the Court of 30 September 2003 in the case C-167/01, Kamer van Koophandel en Fabrieken voor Amsterdam v Inspire Art Ltd. (Inspire Art case);

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29. Judgment of the Court (First Chamber) of 5 July 2007 in the case C-321/05, Hans Markus Kofoed v Skatteministeriet;

30. Order of the Court of First Instance (First Chamber) of 11 September 2007 in the case T-35/06, Honig-Verband eV v Commission of the European Communities;

31. Judgment of the Court (Second Chamber) of 21 February 2008 in the case C-425/06, Ministero dell'Economia e delle Finanze v Part Service Srl;

32. Judgment of the Court (First Chamber) of 26 March 2009 in the case C-348/07, Turgay Semen v Deutsche Tamoil GmbH;

33. Opinion of Advocate General Kokott delivered on 23 April 2009 in the case C-97/08 P, Akzo Nobel NV and Others v Commission of the European Communities;

34. Judgment of the Court (Fourth Chamber) of 19 May 2009 in the case C-538/07, Assitur Srl v Camera di Commercio, Industria, Artigianato e Agricoltura di Milano;

35. Judgment of the Court (Third Chamber) of 10 September 2009 in the case C-97/08 P, Akzo Nobel NV v Commission of the European Communities;

36. Judgment of the Court (First Chamber) of 8 July 2010 in the case C-171/08, European Commission v Portuguese Republic;

37. Judgment of the Court (Second Chamber) of 16 December 2010 in the case C-480/09 P, AceaElectrabel Produzione SpA v European Commission;

38. Judgment of the General Court (Second Chamber) of 12 July 2011 in the case T-132/07, Fuji Electric Co. Ltd (anciennement Fuji Electric Holdings Co. Ltd) v European Commission;

39. Judgment of the Court (First Chamber) of 15 December 2011 in the case C-191/10, Rastelli Davide e C. Snc v Jean-Charles Hidoux;

40. Judgment of the Court (Third Chamber) of 12 July 2012 in the case C-378/10, VALE Építési kft;

41. Judgement of the court (Ninth Chamber) of 20 June 2013 in the case C-186/12, Impacto Azul Lda

42. Judgment of the Court (Third Chamber) of 11 July 2013 in the case C-440/11 P, European Commission v Stichting Administratiekantoor Portielje and Gosselin Group NV;

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5. Cour de Cassation, Chambre commerciale, du 9 mars 1993, 91-14.685, Publié au bulletin;

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**Spanish case law**

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3. Sentencia del Tribunal Supremo - Sala Primera, de lo Civil, 11 de Diciembre de 2015. STS 5151/2015 - ECLI:ES:TS:2015:5151.