Turiba University

Gvido Lošaks

SYNOPSYS OF THE DOCTORAL THESIS

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

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Scientific supervisor:
Dr. iur.: **Dalia Perkumienė**

Scientific advisor (if any):
Dr. ___: *(**name, surname**)*

Thesis reviewers:
1) Dr.hist. **Valdis Blūzma**, Turiba Unversity
2) Dr.iur. **Jānis Grasis**, Rīgas Stradiņš University
3) Assoc. prof dr. **Jurgita Grigienė**, Vytautas Magnus University, Kaunas, Lithuania

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Head of Doctoral Council of Law Science:
Dr.iur.: **Ingrīda Veikša**

Secretary of Doctoral Council of Law Science:
Dr. iur: **Kristīne Neimane**

INTRODUCTION

The 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. National and international economic markets are dominated by groups of companies.[1] 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. The legal fragmentation in recognition of the interests of the group can become as an obstacle or barrier to functioning of the Internal Market.

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 competition law. In the view of all foregoing, current company law literature, while identifying the issue, fails to provide a comprehensive analysis from a company law perspective. The novelty of the research is reflected in the development of the theory of group companies. Theoretical contribution to this research is found in the 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, the analysis investigates whether the diverse legal approaches to recognition of the interest of the group within the EU promote or hinder 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.

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;

[1] Hadden, T. (1984). Inside Corporate Groups. *International Journal of the Sociology of Law.* Volume 12. P. 271.

4. To research the impact of Member States practises' of recognition of the interests of the group on the Internal Market;

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

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 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. Additionally, the research on the reform agenda will be utilized to rigorously evaluate the effectiveness of existing rules, contributing to the development of comprehensive conclusions.

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 the founder of the "group defence" or "safe harbour" and the Netherlands has subsequently adopted and expanded upon this model. Germany is the founder of the compensatory model and Latvia has simply translated it, but in addition increased the scope of the 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.

The doctoral thesis consists of 130 pages The thesis is structured into an introduction, four main research sections, concluding with a summary and recommendations. 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 the 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 operation of the Internal Market.

CONTENTS OF THE THESIS

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

The first section of the thesis assesses whether the group of companies are regulated at the EU level. 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. However, 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 Accounting Directive defines group of companies (Article 2, paragraph 9, 10, 11 and Article 22).[2] The Accounting Directive's definition is based on the concept of the control. The same concept is used also for defining "controlled undertaking" in Article, paragraph 1, subparagraph f of the Transparency Directive,[3] "controlling undertaking" in Article 3 of the Directive on European Works Council,[4] as well as for "single undertaking" in Article 2,

[2] 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.

[3] 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.

[4] 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

paragraph 2 of the de minimis Regulation.[5] 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 the General Data Protection Regulation establishes group privilege, which is characterised by a pursuit of the interest of the group.[6]

In the EU competition law, the Court of Justice of the European Union (CJEU) interpreting Article 101 and 102 of the Treaty on the Functioning of the European Union (TFEU) has concluded that group of companies should be treated as a single undertaking,[7] but it is not sufficient that a control exists; it must be in fact be actively exercised.[8] The EU competition law introduces the doctrine of a single economic entity for the purpose 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: 1) in a case, if the subsidiary acts as an auxiliary organ of its parent;[9] 2) closely connected transactions between companies.[10] In the EU insolvency law the CJEU has stated that the fact the company is controlled by another company is not enough to overturn the presumption that the company's main interest is in the place of the company's registered office.[11] Moreover, the presumption of the main interests cannot be overturned also by intermixing of assets or financial accounts.[12] It is important to highlight that the control over a company is not particularly visible to third parties.

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.

[5] 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.

[6] 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.

[7] 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.

[8] 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.

[9] 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.

[10] 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.

[11] Judgment of the Court (Grand Chamber) of 2 May 2006 in the case C - 341/04, Eurofood IFSC Ltd. (Eurofood case), paragraph 36.

[12] 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.

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.[13] In transfer of undertaking in labour law the CJEU considers even fully integrated groups of companies to be distinct legal persons.[14] 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. To ensure legal certainty and security in commercial transactions, the CJEU found that a group of companies cannot be treated as a single economic entity when determining compensation for self-employed commercial agents upon termination of their agency contracts.[15] The CJEU for jurisdiction for being sued in cross-border cases 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.[16]

While traditional company law adheres to the concept of separate legal personality, other EU laws, notably the Accounting Directive, primarily employ the concept of control. 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.

[13] 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.
[14] 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.
[15] Judgment of the Court (First Chamber) of 26 March 2009 in the case C-348/07, Turgay Semen v Deutsche Tamoil GmbH, paragraph 31.
[16] Judgment of the Court (Sixth Chamber) of 9 December 1987 in the case 218/86, SAR Schotte GmbH v Parfums Rothschild SARL, paragraph 15

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

The second section analyses how Member States recognise the interest of the group and investigates the legal fragmentation of the recognition of the interest of the group. Concerning the definition of the group of companies at the national level of the Member States, two particular concepts prevail. The most used concept is that of control, 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 in Article 22 paragraph 1 of the Accounting Directive as well. 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 they possess special rights.[17] The concept of dominance and dependence focuses beyond the basic presumption of the control 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 differs. 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; In Latvia, it is extended also to natural persons (Article 1, subparagraph 8 of *Koncernu likums*);[18] In Portugal according to Article 481 of CSC this concept is applicable only to limited liability companies - private limited liability companies (*sociedades por quota*), public limited liability companies (*sociedades anónimas*), limited liability partnerships by shares (*sociedade em comandita por acções*) and a parent company and a subsidiary have to be in a prescribed legal form.[19] Member States without statutory group law, such as France and Netherlands, stick with the concept of

[17] 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.

[18] 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.

[19] 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.

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.

Concerning the interest of the group of companies at the Member State's national level, two approaches of recognising the interests of the group can be distinguished. The understanding in countries that follow French *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 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.

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*[20] as well as applicable to GmbH contractual groups, in Latvia Article 20 of *Koncernu likums*, [21] in Portugal Article 502 of CSC[22] or cover losses for those transactions that are detrimental or

[20] 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.

[21] 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.

[22] 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.

disadvantageous in - Germany Article 317 of *AktG*,[23] in Latvia Article 33 of *Koncernu likums*.[24] 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 maintained, insolvency cannot be triggered or harm caused must be removed or protected against. 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 a different approach is applicable (sufficient consideration of subsidiary's interests and capital maintenance). Similiarly, in Portugal de facto groups are excluded from the 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 the suffered negative consequences must be compensated, 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. The exception can be found in Italy, where the parent company is directly liable to creditors for pursuing the interest of the group. Moreover, Member States with compensatory mechanism have additional transparency

[23] 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.
[24] 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.

rules, e.g., dependency report in Germany Article 312 of *AktG* [25] and in Latvia Article 30 of *Koncernu likums*;[26] 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*.[27] 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.

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 a company's autonomous interests is limited, i.e., minority shareholder interests stay intact. Nevertheless, this perception does not resemble the 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* provides a wide range of legal instruments (exit rights, compensation for staying in the group, buy out rights) for minority shareholder interest protection by establishing an organised system of checks and balances.

[25] 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.
[26] 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.
[27] Codice Civile. REGIO DECRETO 16 marzo 1942, n. 262. Approvazione del testo del Codice civile. (042U0262) (Gazzetta Ufficiale n.79 del 4-4-1942).

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

The third section researches the impact of Member States practises' of recognition of the interests of the group on the Internal Market. In a cross-border group of companies each national law must be separately examined, therefore investments for founding or managing such establishments are higher. 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. 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.

Normally, members of the group (legal entities) manage their liquidity autonomously. This approach is significantly disadvantageous for both the group and autonomous interests of each member of the group because each company pays separate 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). However, absence of enabling law makes cross-border cash pooling challenging.

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. However, 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. Consequently, the legal fragmentation in Member State practices 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.

The EU general regulatory framework creates a legal environment of regulatory competition between Member States. Regulatory competition can have the effect of the race to the top or the race to the bottom. 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. 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 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.

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.[28] The parent company, as any other rational investor, before setting up a subsidiary or a branch will consider advantages of respective jurisdiction. 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. Enjoying the benefit of more favourable legislation of a Member State does not constitute abuse of EU law rights.

[28] 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

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

The fourth section explores the EU intervention in Member State's recognition of 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. 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[29] it is very unlikely that there will be unanimous consensus in the Council. 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. A Recommendation in the recognition of the interest of the group is better suited to be an intermediate legal instrument rather than final.

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. 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 companies 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

[29] 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.

concepts of control and dominance/dependency are used in Member States. 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 used concept is control.

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. Contractual groups can be found only in those Member States that have implemented German *Koncernrecht* and are rarely 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.

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 from forcing the subsidiary to meet their interests. All it does is impede consideration of group interests, therefore, the right to give instructions must be legitimised. Under the concept of the control, the parent company's issued instructions have binding nature. Benefit and burden sharing in group of companies implies that detrimental or disadvantageous instructions to the subsidiary should also be binding.

The creditor protection is of great importance because low-cost capital flows where it is best protected. 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. 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. 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. The legal personality of a subsidiary must be respected, and creditors protection does not justify disregarding it in all circumstances.

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. 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. 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. Otherwise, a parent company could extract benefits for itself without sharing it with other shareholders by taking advantage of a control on a subsidiary. 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.

APPROBATION OF RESEARCH RESULTS

A list of scientific papers published for the topic of the recognition of the interest of the group:

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. PP. 106 – 113. 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.

THE MAIN SOURCES OF LITERATURE

1. 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’). PP. 165.

2. Embid Irujo, J.M. (2005). Trends and Realities in the Law of Corporate Groups. *European Business Organization Law Review (EBOR)*. Volume 6, Issue 1. PP. 65 – 91.

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4. European Company Law Experts (ECLE). (2012). The Future of European Company Law (response to the European Commission’s Consultation).

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6. Hopt, K.J. (2015). A comparative Study on the Economics, Law and Regulation of Corporate Groups. European Corporate Governance Institute (ECGI) Working Paper Series in Law No. 286/2015. PP. 40;

7. European Company Law Experts (ECLE). (2016). A proposal for reforming group law in the European Union – Comparative observations on the way forward.

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9. The Informal Company Law Expert Group (ICLEG). (2016). Report on the recognition of the interest of the group.

10. Manóvi, R. M. (2020). Groups of Companies: A Comparative Law Overview. *Ius Comparatum - Global Studies in Comparative Law.* Springer. PP. 694.

CONCLUSIONS AND RECOMMENDATIONS, AS WELL AS THESES PUT FORWARD FOR DEFENCE

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. The doctoral thesis not only comes up with conclusions and proposals, but in addition provides drafted the EU legislative act for recognising the interest of the group.

Based on the research conducted, following conclusions and proposals are put forward for defence:

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 a cross- border effect and a Member States by themselves 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.

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.

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.

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.

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.