

## **“Ltd. & Co.”: Anglo-German Partnerships and Regulatory Competition**

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### ***Abstract***

The European Court of Justice supports free choice of incorporation: Corporate governance modes are established ex ante; the applicable legal regime addresses the outcome of private ordering ex post. Regulatory competition brings about new forms of corporate organization hitherto unknown in Europe, including crossovers between national company law rules. Current practice in Germany suggests that Partnerships with English and German implants (i.e. an English Private Limited Company as the General Partner and German Limited Partners) are spreading, thereby challenging established concepts under German company, insolvency and tort laws. As ‘Anglo-German Partnerships’ accommodate new forms of entrepreneurial activities, evolutionary processes of traditional regulatory concepts are initiated. European countries with bank-oriented capital market systems (such as Germany) have to master transition processes, deemphasizing path dependency for mature companies and offering attractive legal regimes for start-ups. A political economy analysis is to lay the foundations for a decentralized development of corporate law rules. Issues of self-regulation and state intervention, but also the separation of powers between the European Union and its Member States will be discussed. The implications of this approach will be tested in the context of the developing judge-made law on Anglo-German Partnerships.

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## I. Introduction

### 1. Company Law after *Tiebout* and the European Court of Justice

The production of European company law is largely decentralized<sup>1</sup>. If freedom of movement exists, investors will behave as *Charles Tiebout*<sup>2</sup> predicted and shy away from countries with over-regulation. The European Court of Justice (ECJ) is instrumental in translating *Tiebout*'s insights into practical company law: A series of path-breaking rulings has brought company mobility to Europe<sup>3</sup>: The Member States will have to respect the freedom of establishment of foreign business organizations, even if the host state disagrees with the business organization laws of the country of origin. This introduces pseudo-foreign companies to corporate Europe. Absent fraud, it is a legitimate aim of corporate planning to circumvent restrictive laws of one Member State and resort to the more liberal company law regime of another<sup>4</sup>. Ideally, the ECJ's cases on company mobility operate as a powerful incentive for Member States to re-evaluate their national company laws<sup>5</sup>, bringing forth corporate law standards attractive to investors.

Regrettably, the *Tiebout* model does not specify the properties of the general competitive equilibrium that it seeks to promulgate by delegating rule-making to local authorities<sup>6</sup>. It

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<sup>1</sup> See *Heine/Kerber*, European Corporate Laws, Regulatory Competition and Path Dependence, Eur. J. L. & Econ. 13, 47 (60 et seq.) (2002); on the uneasy relationship between harmonization and regulatory competition: *Kübler*, A Shifting Paradigm of European Company Law?, Col. J. Eur. L. 11, 219 (222 et seq.) (2005); *Deakin*, Legal Diversity and Regulatory Competition, Eur. L. J. 12, 440 (442) (2006); *Zumbansen*, Spaces and Places: A Systems Theory Approach to Regulatory Competition in European Company Law, Eur. L. J. 12, 534 (538 et seq.) (2006).

<sup>2</sup> *Tiebout*, A Pure Theory of Local Expenditures, J. Pol. Econ. 64, 416 (419 et seq.) (1956); cf. *Oates*, An Essay on Legal Federalism, J. Econ. Lit. XXXVII, 1120 (1121 et seq.) (1999)

<sup>3</sup> ECJ judgments of March 9, 1999, C-221/97, *Centros Ltd. v. Erhvervs- og Selskabstyrelsen*, [1999] E.C.R. I-1459 et seq.; May 11, 2002, C-208/00, *Überseering B.V. v. Nordic Construction Company Baumanagement GmbH (NCC)*, [2002] E.C.R. I-9919 et seq.; September 30, 2003, C-167/01, *Kamer van Koophandel en Fabrieken v. Inspire Art Ltd.* In *SEVIC Systems AG*, judgment of December 13, 2005, C-411/03, the ECJ has held that the freedom of establishment includes the right to undertake cross-border merger operations (accessible via: [http://curia.eu.int/en/content/juris/index\\_form.htm](http://curia.eu.int/en/content/juris/index_form.htm)).

<sup>4</sup> See para. 95 et seq. of the ECJ's judgment of September 30, 2003, C-167/01, *Kamer van Koophandel en Fabrieken v. Inspire Art Ltd.*, "... *The reasons for which a company chooses to be formed in a particular Member State are, save in the case of fraud, irrelevant with regard to application of the rules on freedom of establishment. ... (T)he fact that the company was formed in a particular Member State for the sole purpose of enjoying the benefit of a more favorable legislation does not constitute abuse even if that company conducts its activities entirely or mainly in that second State ...*". Some restrictions apply on grounds of public policy, such as health standards, creditor protection and workers' rights.

<sup>5</sup> See para. 43 to the Opinion of Advocate-General *Geelhoed* of February 23, 2006, Case No. C-374/04, *Test Claimants in Class IV of the ACT Group Litigation v. Commissioners of Inland Revenue*: "*Indeed, in itself, the existence of disparities may well have a positive effect on Member States' economies and benefit the internal market. With the exception of certain extreme cases – for example, the cases of 'harmful tax competition' – there is a powerful argument that transparent regulatory competition in tax regimes, as in other spheres, gives Member States an incentive to be as efficient as possible in the administration and structure of their tax systems and in the use of their direct tax receipts.*"

<sup>6</sup> *Bratton/McCahery*, The New Economics of Jurisdictional Competition: Devolutionary Federalism in a Second-Best World, Geo. L. J. 86, 201 (226 et seq.) (1997).

does not account for rent-seeking<sup>7</sup> and externalities that may arise under decentralization<sup>8</sup>. There is a trade-off between the informational advantages of regional government and the externalization effects of national legal systems<sup>9</sup>. The ECJ's jurisprudence calls for an analysis of the externalities of regulatory competition and national mechanisms intended to contain negative effects of foreign business laws<sup>10</sup>.

## 2. Why Focus on Anglo-German Partnerships?

History suggests that the corporate law policies of the Member States of the European Union (EU) tend to establish a non-cooperative equilibrium, foreclosing long-term competition. National corporate law systems are marked by path dependence, relatively high switching costs and tax law obstacles<sup>11</sup>. Nonetheless, in assessing the competitive effects of the ECJ's cases on company mobility greater attention should be paid to the differences between publicly traded corporations and private companies<sup>12</sup>. Regulatory policies are less restrictive on private

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<sup>7</sup> Cf. *Laffont*, Incentives and Political Economy (2000), 46 et seq., 99 et seq.; *Kamar*, A Regulatory Competition Theory of Indeterminacy in Corporate Law, 98 Colum. L. Rev. 1908 (1949) (1998), and *Thomsen*, The Hidden Meaning of Codes: Corporate Governance and Investor Rent-Seeking, 7 Eur. Bus. Org. L. Rev. (EBOR) (2006) (forthcoming), arguing that the existence of non-binding corporate governance codes should be understood as evidence of private rent-seeking.

<sup>8</sup> Cf. *Easterbrook*, Antitrust and the Economics of Federalism, J. L. & Econ. 26, 23 (33 et seq.) (1983), warning that there is no necessary congruence between exit and economic markets, or between voice and politics. Also, in the European context, the costs of switching from one legal norm to another may be prohibitively high: *Carbonara/Parisi*, The Economics of Legal Harmonization, George Mason University Law and Economics Research Paper Series 05-40 (2005), download at <http://ssrn.com/paper=870519>.

<sup>9</sup> *Laffont/Zantman*, Information acquisition, political game and the delegation of authority, Eur. J. Pol. Econ. 18, 407 (417 et seq.) (2002).

<sup>10</sup> Cf. *Laffont/Zantman*, Eur. J. Pol. Econ. 18, 407 (423 seq.) (2002); *Ulen*, Economic and Public-Choice Forces in Federalism, George Mason L. Rev. 6, 921 (926 et seq.) (1998); *O'Hara*, Opting out of Regulation: A Public-Choice-Analysis of Contractual Choice of Law, Vanderb. L. Rev. 53, 1551 (1570 et seq.) (2000); *Schön*, Playing Different Games? Regulatory Competition in Tax and Company Law Compared, Com. Mkt. L. Rev. 42, 331 (355) (2005); *Charny*, Competition Among Jurisdictions in Formulating Corporate Law Rules: An American Perspective on the "Race to the Bottom" in the European Communities, Harv. Int'l. L. J. 32, 423 (454 et seq.) (1991); *Carney*, The Political Economy of Competition for Corporate Charters, J. Leg. Stud. 26, 303 (311 et seq.) (1997). This may also include legislative reform: cf. *Casagrande/Spallone*, Relaxing Liquidity Constraints for Start-Ups: A Welfare Analysis Over the Italian Revised Corporate Law, Eur. J. L. Econ. 20, 339 et seq. (2005).

<sup>11</sup> Cf. *McCahery/Vermeulen*, Does the European Company prevent the 'Delaware-effect'?, Tilburg University, TILEC Discussion Paper DP 2005-10 (March 2005), arguing that "there are few political incentives for lawmakers to pass legislation that might serve to disrupt the EU's non-competitive equilibrium in company law"; and *Kirchner/Painter/Kaal*, Regulatory Competition in EU Corporate Law after *Inspire Art*: Unbundling the Delaware's Product ECFR 2, 159 (176 et seq.) (2005), pointing out to the switching costs an established company would face in migrating from national legal order to another.

<sup>12</sup> It is one of the astonishing aspects of the debate on company mobility in the EU that the factual settings of the cases before the ECJ are often overlooked: The *Centros*, *Überseering* and *Inspire-Art* rulings dealt with close corporations or private companies. See also: *McCahery*, Harmonization in European Company Law: The Political Economy of Economic Integration, in: Curtin/Smits/Klip/McCahery, European Integration and the Law – Four Contributions on the Interplay between European Integration and National Law to celebrate the 25<sup>th</sup> Anniversary of the Maastricht University's Faculty of Law (2006), 155 (182 et seq.).

companies and partnerships<sup>13</sup>. To calibrate divergent interests, management, shareholders and lenders test various organization forms<sup>14</sup>. This includes cross-overs between national legal systems.

Current German business practice suggests that – under the influence of the ECJ’s jurisprudence on company mobility – Ltd. & Co. partnerships with English and German implants are spreading<sup>15</sup>: A Ltd. & Co. KG partnership is set up under German partnership law<sup>16</sup>, usually including an English Private Limited Company as a (managing) general partner and (German) individuals as limited partners. This draws on a legal options model with opt-in and opt-out clauses<sup>17</sup>, as principles of English and German company law are combined. Established concepts under German company, insolvency and tort laws are challenged, begging the question whether the Ltd. & Co. KG fully internalizes its costs. It will be shown that the Ltd. & Co. KG has the potential to unleash evolutionary processes in German law without legislative intervention.

### 3. Outline of the Paper

This paper will first outline the framework for regulatory competition as developed by the ECJ. It will then introduce the German GmbH & Co. KG as the organizational pattern against which private practice devised the Ltd. & Co. The managing general partner of the Ltd. & Co. KG, the English Private Limited Company operates on radically different concepts of solvency and creditor protection. This suggests that information costs may arise when a partnership with a foreign managing general partner operates on the German market. A trade-off is found to exist between the requirements of company mobility and cost internalization. In the vicinity of insolvency, the Ltd. & Co. KG requires German law to move from an *ex ante* ap-

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<sup>13</sup> Cf. *Ribstein*, Why Corporations?, Berkeley Bus. L. J. 1, 183 (191 et seq.) (2004), analyzing the choice between corporation and partnership from a US perspective; and *McCahery/Vermeulen*, Understanding (Un)incorporated Business Forms – Topics in Corporate Finance 12, 9 et seq. (2005), assessing the legal regime for closely held firms.

<sup>14</sup> See *McCahery/Vermeulen*, Limited Partnership Reform in the United Kingdom: A Competitive, Venture Capital Oriented Business Form, Tilburg University, TILEC Discussion Paper, DP 2004-024, p. 20 et seq., analyzing the competitive ‘race’ between European jurisdictions with respect to optimal legislation for venture capital business organizations.

<sup>15</sup> Cf. *Schlichte*, Kapitalerhaltung in der Ltd. & Co. KG, Der Betrieb 59, 1357 et seq. (2006); *Kowalski/Bormann*, Beteiligung einer ausländischen juristischen Person als Komplementärin einer deutschen KG – zugleich Besprechung des Beschlusses AmtsG Bad Oeynhausen vom 15.5.2005 – 16 AR 15/05, GmbH-Rundschau 96, 1045 et seq. (2005); *Binz/Mayer*, Die ausländische Kapitalgesellschaft & Co. KG im Aufwind? – Konsequenzen aus dem „Überseering“-Urteil des EuGH v. 5.11.2002 – Rs. C-208/00, GmbH-Rundschau 94, 94 et seq. (2003).

<sup>16</sup> Under German law, partnerships are part of the law on private companies.

<sup>17</sup> *Hertig/McCahery*, A Legal Options Approach to EC Company Law, Amsterdam Center for Law & Economics Working Paper N. 2006-01 (<http://ssrn.acle.nl>); but consider the skeptical approach by *Schön*, Com. Mkt. L. Rev. 42, 331 (337) (2005), with respect to ‘cherry picking’ business strategies towards the various jurisdictions of the European Union. See *infra*, sub II.4.b.

proach to an *ex post* perspective. These findings will be discussed in the context of the European Insolvency Regulation (EIR)<sup>18</sup>. A section on regulatory implications concludes.

## II. A Challenge for German Law

### 1. National Company Laws – Competition as Defined by the ECJ

The ECJ's jurisprudence on artt. 43, 48 of the EC Treaty<sup>19</sup> stimulates regulatory competition among the corporate law systems of the Member States. But it does not deliberately foster a *Tiebout* model of local production of company law. At the outset, the ECJ wanted to attack negative externalities of national corporate law systems by requiring Member States to recognize non-domestic European companies without re-incorporation<sup>20</sup>. Technically, this addresses a choice of law issue, as firms will be able to arbitrage among different legal systems<sup>21</sup>. Member States which have applied the seat theory in corporate law are to liberalize their restrictive regimes on companies from the so-called incorporations states of the EU. In insisting on the freedom of establishment the ECJ focuses on reducing the costs of company mobility within the EU<sup>22</sup>. The court is aware of the trade-off between company mobility and the externalities of regulatory competition<sup>23</sup>. The ECJ's holdings intuitively invoke an

<sup>18</sup> Council Regulation (EC) No. 1346/2000 of May 29, 2000 on insolvency proceedings, O.J. L 160/1 of June 30, 2000.

<sup>19</sup> Art. 43 of the EC Treaty:

*Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of Member States in the territory of another Member State shall be prohibited. Such prohibition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any other Member State established in the territory of any Member State.*

*Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of 48, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the chapter relating to capital.*

Art. 48 of the EC Treaty:

*Companies or firms formed in accordance with the law of a Member State having their registered office, central administration or principal place of business within the Community shall, for the purposes of this chapter, be treated in the same way as natural persons who are nationals of Member States.*

*'Companies or firms' means companies or firms constituted under civil or commercial law, including cooperative societies, and other legal persons governed by public or private law, save for those which are non-profit making* (Consolidated Version of the Treaty Establishing the European Community, O.J. C 325/33 of December 24, 2002).

<sup>20</sup> Cf. Roth, *From Centros to Überseering: Free Movement of Companies, Private International, and Community Law*, I.C.L.Q. 52, 177 et seq. (2003); Micheler, *The Impact of the Centros Case on Europe's Company Laws*, Comp. Law. 21 (6), 179 (180 et seq.); Eidenmüller, *Europäisches und deutsches Gesellschaftsrecht im europäischen Wettbewerb der Gesellschaftsrechte*, in: Festschrift Heldrich (2005), 581 (582); Grundmann, *The Structure of European Company Law: From Crisis to Boom*, Eur. Bus. Org. L. Rev. (EBOR) 5, 601 (611 et seq.) (2004): "functioning jurisdictional competition as a goal".

<sup>21</sup> Enriques, *Silence Is Golden: The European Company as a Catalyst for Company Law Arbitrage*, J. Corp. L. Stud. 4, 77 (83 et seq.) (2004); cf. Ribstein, *The Important Role of Non-Organizational Law*, Wake Forest L. Rev. 40, 751 (756) (2005).

<sup>22</sup> Cf. Trachtman, *International Regulatory Competition, Externalization, and Jurisdiction*, Harv. Int'l. L. J. 34, 47 (65 et seq.) (1993), on the cost aspects of regulatory competition.

<sup>23</sup> US experience with pseudo-foreign corporations highlights the potential for political debate on company mobility issues. See: *Western Airlines v. Sobieski*, 191 Cal. App. 2d 399 (412 et seq.) (Cal. App. 2<sup>nd</sup> Dist.,

informational model that balances the interests of companies against those of creditors and employees<sup>24</sup>. The Member States may limit the freedom of establishment of non-domestic companies for public policy reasons, but must observe the principles of proportionality and non-discrimination. As long as there is enough information on the market, restrictions on company mobility are unacceptable<sup>25</sup>. This puts some confidence in the abilities of the creditors to detect the risks in dealing with a non-domestic company<sup>26</sup>. It also instructs (national and EU) lawmakers and judges to analyze cost internalization aspects of cross-border mobility and regulatory arbitrage<sup>27</sup>.

Currently, there is no clear evidence on whether cost effects of regulatory competition require EU-wide harmonization<sup>28</sup>. The ECJ has indicated that some of the EU Company Law Directives might offer guidance in addressing problems of externalization<sup>29</sup>. In this context, a Council Directive lays down the ground rules for disclosure requirements in respect of non-domestic branches of companies from other Member States<sup>30</sup>. German branches of English Private Limited Companies which observe the regulatory regime of this EU Directive have to

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1961); *Wilson v. Louisiana-Pacific Resources, Inc.*, 187 Cal. Rptr. 852 (860 et seq.) (Cal. App., 1982), *Broida v. Bancroft*, 478 N.Y.S. 2d 333 (336 et seq.) (N.Y.A.D. 2<sup>nd</sup> Dept., 1984); *Nagy v. Riblet Products Corp.*, 79 F.3d 572 (576 et seq.) (9<sup>th</sup> Cir., 1996), discussing California and New York pseudo-foreign corporation statutes respectively; *Palmer v. Arden-Mayfair, Inc.*, 1978 WL 2506 (Del. Ch., 1978) and *Paul N. Gardner Defined Plan Trust v. Draper et al.*, 1993 WL 125517 (Del. Ch., 1993), rejecting pseudo-foreign corporation statutes as contrary to the constitutionally-mandated 'internal affairs' rule; *Latty*, Pseudo-foreign Corporations, Yale L. J. 65, 137 (148 et seq.) (1955); *Greenwood*, Democracy and Delaware: The Mysterious Race to the Bottom/Top, Yale L. & Pol'y. Rev. 23, 381 (386) (2005).

<sup>24</sup> Cf. *Eidenmüller*, in: *Eidenmüller* (ed.), *Ausländische Kapitalgesellschaften im deutschen Recht* (2004), § 3, 32; *Grundmann*, Ausbau des Informationsmodells im Europäischen Gesellschaftsrecht, *Deutsches Steuerrecht* 42, 232 (235 et seq.) (2004).

<sup>25</sup> See the ECJ's reasoning in para. 36 of its judgment of March 9, 1999, C-221/97, *Centros Ltd. v. Erhvervs- og Selskabsstyrelsen*, [1999] E.C.R. I-1459 (1495): "*Since the company concerned in the main proceedings [in Denmark] holds itself out as a company governed by the law of England and Wales and not as a company governed by Danish law, its creditors are on notice that it is governed by laws different from those which govern the formation of private limited companies in Denmark and they can refer to certain rules of Community law which protect them such as the Fourth Council Directive ... on the annual accounts of certain companies ... and the Eleventh Council Directive ... concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State*".

<sup>26</sup> Cf. *Goette*, Wo steht der BGH nach "Centros" und "Inspire Art"?, *Deutsches Steuerrecht* 43, 197 (198) (2005), chiding the ECJ for relying solely on the principle of *caveat creditor*. Professor *Goette* is a member of the German Federal Supreme Court. See also from a creditor protection perspective: *Bitter*, Flurschäden im Gläubigerschutzrecht durch "Centros & Co."?, *Wertpapier-Mitteilungen* 58, 2190 (2193) (2004).

<sup>27</sup> Cf. *Ulen*, *George Mason L. Rev.* 6, 921 (926 et seq.) (1998); and *Trachtman*, *Harv. J. Int'l. L.* 34, 47 (65 et seq.) (1993); *id.*, *Economic Analysis of Prescriptive Jurisdiction*, *Va. J. Int'l. L.* 42, 1 (74) (2001), addressing safeguards against externalization in a European context. This includes the risks of a restrictive regime forcing firms to withdraw business and assets from a Member State: cf. *Ribstein*, *Wake Forest L. Rev.* 40, 751 (788) (2005).

<sup>28</sup> Cf. *Schön*, Mindestharmonisierung im europäischen Gesellschaftsrecht, *Zeitschrift für das gesamte Handels- und Wirtschaftsrecht* 160, 221 (238) (1996); *Trachtman*, *Va. J. Int'l. L.* 42, 1 (74) (2001).

<sup>29</sup> Cf. the ECJ's judgment in the *Centros* case, *supra* N. 25; *Schön*, Zur "Existenzvernichtung" der juristischen Person, *Zeitschrift für das gesamte Handels- und Wirtschaftsrecht* 168, 268 (293) (2004).

<sup>30</sup> Eleventh Council Directive 89/666/EEC of December 21, 1989, concerning disclosure requirements in respect of branches opened in a Member State by certain types of company governed by the law of another State, O.J. L 395/36 of December 30, 1989.

be entered into the commercial register<sup>31</sup>. This is to accommodate discrepancies between the various national orders, putting a cap on administrative measures designed to ‘warn’ the general public about the perceived dangers of an English Private Limited Company entering the German market.

## 2. Contracting around Regulations I: The GmbH & Co. KG

### a. Basics

German company law emphasizes creditor protection<sup>32</sup>. In making their choices investors have to decide whether to opt for a corporate form that combines limited liability with a statutory minimum capital requirement and strict capital maintenance rules<sup>33</sup>. Statutory minimum capital requirements can be avoided by choosing a partnership without comprehensive legal capacity<sup>34</sup>. Under these circumstances asset partitioning and owner shielding are weak<sup>35</sup>. Liability is imposed on the partners if the partnership is unable to fulfill its financial obligations. However, the creditor normally must exhaust his remedies against the firm before taking direct action against the partners<sup>36</sup>.

A Kommanditgesellschaft (KG) combines limited liability for the limited partners with unlimited liability for the managing general partner<sup>37</sup>. In order to reduce the risks of exposing the managing general partner to third party claims German company law practice has come up with an innovative organizational form: A close corporation with limited liability, the GmbH, assumes the role of the managing general partner, whereas the limited partners continue to observe their statutory role model. This organizational form – generally known under its acronym GmbH & Co. KG – brings limited liability to general partnerships while preserving freedom of contract for devising governance structures specifically tailored to the needs of the

<sup>31</sup> BayObLG (Bavarian Supreme Court), Decision of May 12, 2004, Case No. 2Z BR 019/03.

<sup>32</sup> See Haas, Reform des gesellschaftsrechtlichen Gläubigerschutzes, Gutachten E zum 66. Deutschen Juristentag, Stuttgart 2006, 12 et seq., analyzing the need for legislative reform of creditor protection through company law in the age of regulatory competition in a study prepared for the German Lawyers’ Association.

<sup>33</sup> German statutory company law does not provide for partnerships or private companies, which – like the English Limited Liability Partnership or the US Limited Liability Company – confer limited liability on every partner or shareholder of a private company.

<sup>34</sup> Cf. on the trade-off between the freedom of contract, asset partitioning and creditor-protection measures: Hansmann/Kraakman/Squire, The New Business Entities in Evolutionary Perspective, U. Ill. L. Rev. 2005, 5 (10).

<sup>35</sup> Cf. Hansmann/Kraakman, The Essential Role of Organizational Law, Yale L. J. 110, 387 (393 et seq.) (2000), and Hansmann/Kraakman/Squire, Law and the Rise of the Firm, Harv. L. Rev. 119, 1333 (1338 et seq.) (2006), on the various forms of asset partitioning and entity shielding.

<sup>36</sup> K. Schmidt, Gesellschaftsrecht (4<sup>th</sup> ed. 2002), 1415 et seq; for a US perspective see Ribstein/Keatinge on Limited Liability Companies (2006 Update), § 12:8, comparing members’ limited liability in limited liability companies with that in general partnerships.

<sup>37</sup> The limited partners can only be held liable up to the amount they paid in when they joined the partnership. Contrary to the *Kommanditgesellschaft*, the *offene Handelsgesellschaft* (oHG) imposes unlimited liability on all partners.

partners. Moreover, the GmbH & Co. KG, like any other partnership is exempt from the mandatory codetermination schemes that have been implemented over the last 60 years<sup>38</sup>. Historically, the GmbH & Co. KG attempted to reap tax benefits<sup>39</sup> and achieve greater flexibility for raising capital<sup>40</sup>. Nowadays, its structure is of considerable appeal to family businesses, new firms and more advanced start-ups<sup>41</sup>.

## **b. Asset Partitioning and Capital Maintenance**

The GmbH & Co. KG is a successful attempt to improve asset partitioning and owner shielding for partnerships. It is a cross-over between the law on close corporations and partnerships. The owners of the managing general partner, the GmbH, enjoy legal protection from the creditors of the partnership. This introduces an element of stability into the partnership, but it also creates specific risks (including withdrawal of funds)<sup>42</sup>. Limited liability renders corporate general partners less averse and less inclined to initiate insolvency proceedings for ‘their’ partnership<sup>43</sup>. German courts have acquiesced in the contractual extension of limited liability, building on a mechanism that applies corporate incentive structures to the GmbH & Co. KG: As the GmbH is subject to the statutory rules on capital maintenance this regime is extended to the partnership. The director of the GmbH has to observe a duty of care for the benefit of the close corporation *and* the partnership<sup>44</sup>. The limited partners of the GmbH & Co. KG have been held to be under individual capital maintenance duties with respect to the managing general partner. This is not just a whistle-blowing rule. A limited partner is liable for having received funds from the general managing partner, as this may jeopardize the very existence of the general partner<sup>45</sup>. The limited partner must restitute funds to the general partner, needed to

<sup>38</sup> For a survey of the German rules on codetermination: *Pistor*, Codetermination: A Sociopolitical Model with Governance Externalities, in: Blair/Roe (eds.), *Employees and Corporate Governance* (1999), 163 et seq.; *Siebert*, Corporatist versus Market Approaches to Governance, in: Hopt/Wymeersch/Kanda/Baum (eds.), *Corporate Governance in Context* (2005), 281 et seq.

<sup>39</sup> German tax law does not treat the profits of this partnership as those of a separate corporate entity. Instead, each member will have to pay income tax on his or her share in the profits of the partnership.

<sup>40</sup> See the detailed analysis by *K. Schmidt*, supra N. 36, 1023 et seq.; *Liebscher*, in: Sudhoff, *Die GmbH & Co KG* (6<sup>th</sup> ed. 2005), 27 et seq.; *Binz/Sorg*, *Die GmbH & Co KG* (9<sup>th</sup> ed. 2003), 6 et seq.

<sup>41</sup> *K. Schmidt*, supra N. 36, 1628; *Liebscher*, in: Sudhoff (N. 40), 27; cf. passim *McCahery/Vermeulen*, (Un)incorporated Business Forms (N. 13), 41 et seq.

<sup>42</sup> Cf. *Hansmann/Kraakman/Squire*, Harv. L. Rev. 119, 1333 (1346 et seq., 1351) (2006). See also the *ratio decidendi* in: BGH (German Federal Supreme Court), Judgment of March 29, 1973, BGHZ 60, 324 (at p. 332); and in: OLG (Court of Appeal) Celle, Judgment of June 18, 2003, GmbH-Rundschau 93, 901 (2002).

<sup>43</sup> Cf. *Haas*, supra N. 32, 20 et seq.

<sup>44</sup> BGH (German Federal Supreme Court), Judgment of March 29, 1973, BGHZ 60, 324 (at p. 332); *K. Schmidt*, supra N. 36, 1653 et seq.; cf. *Duys*, *Auslands-Kapitalgesellschaft & Co KG – Systemimmanente Grenzen – Europarechtliche Einflüsse* (2001), 43 et seq.

<sup>45</sup> BGH (German Federal Supreme Court), Judgment of February 19, 1990, Der Betrieb 43, 980 (981) (1990).



stave off illiquidity<sup>46</sup>. This reimbursement duty is jointly owed by all limited partners<sup>47</sup>. If a limited partner exerts direct influence over the management of the day-to-day business of the GmbH & Co. KG, liability lies for damages arising from the belated commencement of insolvency proceedings<sup>48</sup>.

The capital maintenance rules for the GmbH & Co. KG are insolvency-driven. *Ex ante*, they facilitate calculations on the cost of operating a GmbH & Co. KG. They set the scenery for triggering the duty to file for insolvency<sup>49</sup>, but they do not encourage rescue attempts to save the value of the firm. Nor do they address the issue of perverse incentives by introducing trading standards on how to assure solvency<sup>50</sup>. The delicate system of judge-made rules is upset by the managing general (corporate) partner from a jurisdiction which dispenses with statutory minimum capital for the benefit of statutory incentive structures, pursuing an *ex post* approach<sup>51</sup> in the vicinity of insolvency<sup>52</sup>.

### 3. Contracting around Regulations II: The Ltd. & Co. KG

#### a. A Better Choice?

As soon as the ECJ had handed down its judgments on company mobility contracting around the traditional GmbH & Co. KG became a viable alternative. German investors came to rely on the ECJ's disapproval of outright hostility towards pseudo-foreign corporations. An English Private Limited Company was chosen to replace the GmbH as the managing general partner. In this context, the English Private Limited Company demonstrates 'company mobility' by relocating its headquarters while remaining formally incorporated in the United Kingdom

<sup>46</sup> BGH (German Federal Supreme Court), Judgment of March 29, 1973, BGHZ 60, 324 (at p. 332). Conversely, a general duty of loyalty may require that a partner refrains from exercising a contractual right to a pay-out from the funds of the GmbH & Co. KG if the partnership is in crisis: OLG (Court of Appeal) Karlsruhe, Judgment of February 28, 2003, GmbH-Rundschau 94, 1359 (1360 et seq.) (2003). Under certain circumstances this may amount to a duty owed to the creditors as well: BGH judgment of September 20, 2004, Case No. II ZR 302/02.

<sup>47</sup> BGH (German Federal Supreme Court), Judgment of February 5, 1990, Neue Juristische Wochenschrift 43, 1730 (1731 et seq.) (1990); and BGH judgment of February 25, 2002, Case No. II ZR 196/00.

<sup>48</sup> BGH (German Federal Supreme Court), Judgment of March 21, 1988, Neue Juristische Wochenschrift 41, 1789 (1790) (1988); cf. BGH judgment of February 5, 1990, Neue Juristische Wochenschrift 43, 1730 (1731 et seq.) (1990); and judgment of June 27, 2005, Case No. II ZR 113/03. The application of capital maintenance rules to the GmbH & Co. KG is fairly complete: In amending the German Commercial Code the legislator has decided that loans made by the corporate general partner or one of the limited partners may, in times of crisis, deemed to constitute direct contributions of capital.

<sup>49</sup> See *infra* sub II.5.a.

<sup>50</sup> Cf. *Davies*, Directors' Creditor-Regarding Duties in Respect of Trading Decisions Taken in the Vicinity of Insolvency, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (310) (2006), distinguishing between *ex ante* and *ex post* controls in the context of perverse incentives in the pre-insolvency setting.

<sup>51</sup> Cf. *Goette*, Zu den Folgen der Anerkennung ausländischer Gesellschaften mit tatsächlichem Sitz im Inland für die Haftung ihrer Gesellschafter und Organe, Zeitschrift für Wirtschaftsrecht 27, 541 (544) (2006).

<sup>52</sup> See the title of Professor *Davies*' article, *supra* N. 50.

(UK)<sup>53</sup>. The Ltd. & Co. KG has emerged as a new type of business organization shielding the partners from third party claims at lower cost than the traditional GmbH & Co. KG<sup>54</sup>. The current potential of Ltd & Co. KG lies in its attractiveness for private ordering and well-tailored business solutions for new firms and start-ups<sup>55</sup>. Anecdotal evidence suggests that the Ltd. & Co KG is also appropriate for larger and complicated investments<sup>56</sup>.

In the past, German courts had no difficulty in accepting partnerships with a foreign corporate general partner from the European continent<sup>57</sup>. But this may have been due to the fact that there was no open conflict with traditional capital maintenance rules as most continental European jurisdictions still had a statutory minimum capital requirement<sup>58</sup>. It is the English general partner of the Ltd. & Co. KG which calls for a re-assessment of creditor protection in the age of regulatory competition.

## **b. A Necessary Ingredient: The English Private Limited Company**

English law does not impose a minimum capital requirement on private limited companies<sup>59</sup>. There is no duty to pay in the full amount of the authorized capital<sup>60</sup>. The Company Act pre-

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<sup>53</sup> It is estimated that some 30,000 Private Limited Companies have now moved their headquarters to Germany: *Westhoff*, Die Verbreitung der *limited* mit Sitz in Deutschland, *GmbH-Rundschau* 97, 525 (528) (2006); *Becht/Mayer/Wagner*, Corporate Mobility Comes To Europe: The Evidence, Working Paper, Université Libre de Bruxelles/Saïd Business School, Oxford University (October 2005); *Rajak*, The English Limited Company as an Alternative Legal Form for German Enterprise, *EWS* 16, 539 et seq. (2005).

<sup>54</sup> Cf. *Schlichte*, Kapitalerhaltung in der Ltd. & Co. KG, *Der Betrieb* 59, 1357 et seq. (2006); *Werner*, Die Ltd. & Co. KG – eine Alternative zur GmbH & Co. KG?, *GmbH-Rundschau* 96, 288 et seq. (2005).

<sup>55</sup> Cf. *Wachter*, Aktuelle Probleme bei der Ltd. & Co. KG – Gleichzeitig Anmerkungen zu LG Bielefeld v. 11.8.2005 – 24 T 19/05, *GmbH-Rundschau* 97, 79 (85) (2006). There is also evidence of a Ltd. & Co. KG operating as an investment fund: cf. BGH (German Federal Supreme Court), Judgment of September 13, 2004, Case No. II ZR 276/02.

<sup>56</sup> *Süß*, Muß die Limited sich vor der Gründung einer Ltd. & Co. KG in das deutsche Handelsregister eintragen lassen?, *GmbH-Rundschau* 96, 673 (674) (2005).

<sup>57</sup> OLG (Court of Appeal) Saarbrücken, Decision of April 21, 1989, *GmbH-Rundschau* 81, 348 (1990); OLG (Court of Appeal) Stuttgart, Decision of March 30, 1995, *Juristenzeitung* 50, 795 et seq. (1995); *Kowalski/Bormann*, *GmbH-Rundschau* 96, 1045 (1048) (2005).

<sup>58</sup> Cf. *Binz/Mayer*, *GmbH-Rundschau* 94, 249 (250 et seq.) (2003), analyzing the ‘multi-national’ partnerships from a perspective before the ECJ handed down its judgment in the *Inspire Art* case (see supra N. 3). It would seem that reputation plays a decisive role in deciding for a foreign entity as a corporate general partner for a German partnership: Liechtenstein is a member of the European Economic Area and therefore, comparable recognition rules as those under artt. 43, 48 of the EC Treaty apply. Although there are no language barriers between Germany and Liechtenstein, it appears that investors favor partnership structures that do not include Liechtenstein entities as corporate managing general partners. Switzerland is not a member of the European Union, therefore partnerships with a Swiss corporate general managing partner cannot invoke the jurisprudence of the ECJ under artt. 43, 48 of the EC Treaty. Language barriers are major obstacle to a broader acceptance of the French *Sarl* or the Dutch *Besloten Vennootschap* (B.V.) as managing general partners. The decision of the French legislator to allow for a *Société à responsabilité limitée* (*Sarl*) with statutory minimum capital is relatively new (cf. *Cozian/Viandier/Deboissy*, *Droit des sociétés* (18<sup>th</sup> ed. 2005), 405) and does not appear to have created substantial problems for trans-border business.

<sup>59</sup> Private Limited Companies may either register as companies limited by shares or as legal entities limited by guarantee. If a private company is limited by guarantee the commencement of business activities does not depend on shareholders making an immediate financial contribution. The liability of a member is limited to the amount he has undertaken to contribute in the event the company is being wound up.

fers a more flexible approach towards capital maintenance<sup>61</sup>. When dividends are distributed no provision need be made for unrealized capital. There is greater leeway for directors in their financial dealings with the company, and assistance may be provided for the purchase of the company's own shares<sup>62</sup>.

The Insolvency Act of 1986 takes an *ex post* approach towards companies facing insolvency. From the perspective of creditor protection, this has a significant impact on asset partitioning and owner shielding schemes<sup>63</sup>. Company directors are encouraged to undertake rescue attempts, only to put their company into liquidation when there is no reasonable hope of saving it. When a company has gone into insolvent liquidation, a case of wrongful trading lies if the director, prior to liquidation, had known or ought to have known that there was no hope for going on, and had taken insufficient steps to minimize the potential loss<sup>64</sup>. A wrongful trading claim against the insolvent company's director is a collective one. It can only be pursued by the liquidator, hoping to add further funding to the distributable assets. Such a claim does not exist when there are no distributable assets and the company is struck off the register without liquidation proceedings. In applying common law principles courts have further buttressed the *ex post* approach towards rule-making. Returns of capital are unlawful if the payout of funds exceeds the distributable profits or sales occur under value<sup>65</sup>. Common

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<sup>60</sup> Research undertaken in the United Kingdom reveals that small businesses rely initially on internal funds for operating and investment purposes. Bank credits provide additional funding to these businesses, whereas investors in high-risk ventures would normally demand significant equity participation in return (*Finch*, Corporate Insolvency Law – Perspectives and Principles (2002), 69 et seq.

<sup>61</sup> *Davies*, in: Gower and Davies' Principles of Modern Company Law (7<sup>th</sup> ed. 2003), 253 et seq.; *Morse*, in: Charlesworth's Company Law (17<sup>th</sup> ed. 2005), 44 et seq.

<sup>62</sup> *Morse*, in: Charlesworth's Company Law (N. 61), 182 et seq.

<sup>63</sup> Cf. *Ribstein*, Wake Forest L. Rev. 40, 751 (762, 773 et seq.) (2005); *Schön*, Die Zukunft der Kapitalaufbringung/-erhaltung, Der Konzern 2, 162 (170) (2004).

<sup>64</sup> S. 214 of the UK Insolvency Act of 1986 (Wrongful trading):

(1) *Subject to subsection (3) below, if in the course of the winding up of a company it appears that subsection (2) of this section applies in relation to a person whom is or has been a director of the company, the court, on the application of the liquidator, may declare that that person is liable to make such contribution (if any) to the company assets as the court thinks proper.*

(2) *this subsection applies in relation to a person if –*

(a) *the company has gone into insolvent liquidation,*

(b) *at some time before the commencement of the winding up of the company, that person knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation, and*

(c) *that person was a director of the company at that time; ...*

(3) *The court shall not make a declaration under this section with respect to any person if it is satisfied that after the condition specified in subsection (2)(b) was first satisfied in relation to him that person took every step with a view to minimizing the potential loss to the company's creditors as (assuming him to have known that there was no reasonable prospect that the company would avoid going into insolvent liquidation) he ought to have taken. ...*

(7) *In this section 'director' includes a shadow director. ... See on directors' liability for wrongful trading: Davies, in: Gower and Davies, supra N. 61, 198 et seq.; id., Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (316 et seq.) (2006); Finch, supra N. 60, 413 et seq.; Morse, in: Charlesworth's Company Law, supra N. 61, 317 et seq.*

<sup>65</sup> *Aveling Barford Ltd. v. Perion*, [1989] B.C.L.C. 626 (Ch. D., 1989); *Clydebank Football Club Ltd. v. Steedman*, 2002 S.L.T. 109 (OH, 2000).

law principles developed in non-UK common law jurisdictions might further clarify the duties UK directors owe towards creditors in the vicinity of insolvency<sup>66</sup>.

#### 4. Integrating the Ltd. & Co. KG into the German Legal System

##### a. Disclosure

Technically, a Private Limited Company relocating its headquarters to do exclusively business in Germany is required to establish a local branch by filing a petition with the commercial register<sup>67</sup>. Many private limited companies ignore this duty<sup>68</sup>, but the director of the managing general partner of a Ltd. & Co. KG will comply in order to get the partnership operational. Some disclosure rules apply in order to minimize the effects of regulatory arbitrage<sup>69</sup>. The majority of the German courts have resisted the temptation of forcing labels on the branches of Private Limited Companies which would have indicated that the company was established under English law with corresponding powers of the director. Rather, it is for the market to detect regulatory differences<sup>70</sup>. This begs the question to what extent Member States may still police disqualified directors of English Private Limited Company operating as a pseudo-foreign corporation: In the past, German individuals have been barred from undertaking certain business activities<sup>71</sup>, only to reappear on the marketplace in the capacity of the

<sup>66</sup> *Davies*, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (329 et seq.) (2006).

<sup>67</sup> The company's incorporation in the UK remains unaffected as 'only' its headquarters relocate to Germany. Cf. *Liese*, Die Handelsregistereintragung Europäischer Aktiengesellschaften in Deutschland – oder Ceci n'est pas une pipe?, *Neue Zeitschrift für Gesellschaftsrecht* 9, 201 et seq. (2006).

<sup>68</sup> *Becht/Mayer/Wagner*, Corporate Mobility and the Costs of Regulation, European Corporate Governance Institute Law Working Paper No. 70/2006 (May 2006)

<sup>69</sup> This includes disclosure rules under German securities regulation. In departing from domestic English practice, private limited companies – whether in their individual capacity or as the general managing partner of a Ltd. & Co. KG – have access to the German capital market. Failure to observe securities regulations on investor information may give rise to a claim for damages against the company's local representative, irrespective of whether a breach of English company can be established: see BGH (German Federal Supreme Court), Judgment of September 13, 2004, Case No. II ZR 276/02, involving a partnership between a British Virgin Islands Private Limited Company and German investors. Under EU law, British Virgin Islands companies have to be given the same treatment as United Kingdom companies.

<sup>70</sup> OLG (Court of Appeal) München, Decision of August 17, 2005, *Der Betrieb* 58, 1955 (2005); OLG (Court of Appeal) Düsseldorf, Decision of February 21, 2006, *Der Betrieb* 59, 1102 (2006); LG (District Court) Frankfurt, Decision of February 15, 2005, *GmbH-Rundschau* 96, 1135 (2005). On the cost aspects of having a local branch of an English Private Limited Company entered into the commercial register: OLG (Court of Appeal) Frankfurt, Decision of December 29, 2005, *Der Betrieb* 59, 269 (270 et seq.) (2006); OLG (Court of Appeal) Hamm, Decision of June 28, 2005, *GmbH-Rundschau* 96, 1130 et seq. (2005); LG (District Court) Cottbus, Decision of February 14, 2005, *Entscheidungen zum Wirtschaftsrecht* 21, 733 (2005); LG (District Court) Berlin, Decision of June 22, 2004, *Zeitschrift für Wirtschaftsrecht* 25, 2380 (2381 et seq.) (2004); LG (District Court) Bielefeld, Decision of July 8, 2004, Case No. 24 T 7/04; and the recent preliminary ruling by the ECJ, judgment of June 1, 2006, Case No. C-452/04, *In the Matter of innoventif Limited*, reference from LG (District Court) Berlin, Decision of August 31, 2004, Case No. 102 T 57/04. See, however, the isolated attempts to play reputation games by the district courts: of Freiburg and Ravensburg: LG Freiburg, decision of July 22, 2004, Case No. 10 T 5/04, and LG Ravensburg, decision of February 14, 2005, *GmbH-Rundschau* 96, 489 (2005).

<sup>71</sup> OVG (Court of Administrative Law Appeals) Münster, Decision of September 9, 2005, Case No. 4 A 1468/05, *EWiR* 22, 17 (2006); OLG (Court of Appeal) Jena, Decision of March 9, 2006, *Neue Zeitschrift für Gesellschaftsrecht* 9, 434 et seq. (2006).

director of English Private Limited Company with its headquarters in Germany. As this issue is pending before the German Federal Supreme Court, it would seem that, in accordance with the ECJ's rulings on company mobility, registration cannot be denied, but a prohibition on soliciting business is appropriate<sup>72</sup>.

## **b. Constraints Imposed by the ECJ**

The Ltd. & Co. KG marks yet another attempt to redesign (statutory) asset partitioning and owner shielding schemes. As its managing general partner relies on different (internal) incentive structures, Anglo-German Partnerships are often accused of 'cherry picking'<sup>73</sup>. The main criticism is that the freedom to opt-out of the statutory minimum capital requirement is not adequately matched by a forth-coming attitude towards German insolvency law rules<sup>74</sup>. Meanwhile, outright rejection has given way to a more balanced approach suggesting that English law rules might be integrated into German legal reasoning<sup>75</sup>. This attitude is not instructed by notions of intra-European comity; instead it is mandated by the ECJ's externalization cost analysis<sup>76</sup>. The ECJ proscribes restrictive national measures that raise the cost of relocating companies within the EU. Obviously, national rules on statutory minimum capital and capital maintenance affect the asset partitioning agreed upon by the founders of the company, thereby constituting an 'entry fee'. Although a Ltd. & Co. KG is a partnership established under German law, this argument applies with equal force. Invoking the capital maintenance rules developed for the GmbH & Co. KG would affect the Ltd. & Co. KG as this would re-draw the asset partitioning scheme of its corporate general partner, an English Pri-

<sup>72</sup> *Mankowski*, Die deutsche Ltd.-Zweigniederlassung im Spannungsverhältnis von Gewerbe- und Registerrecht, *Betriebs-Berater* 61, 1173 (1174 et seq.) (2006).

<sup>73</sup> Cf. FG (Tax Law Court) Rheinland-Pfalz, Judgment of June 22, 2004, Case No. 2 K 2455/02, and *Schön*, *Com. Mkt. L. Rev.* 42, 331 (337) (2005).

<sup>74</sup> The upshot of this criticism is that the English corporate managing partner should be subject to the statutory minimum capital rules applicable to close corporations: *Duys*, supra N. 44, 67 et seq.; *K. Schmidt*, supra N. 36; cf. *Altmeppen*, Schutz vor „europäischen“ Kapitalgesellschaften, *Neue Juristische Wochenschrift* 57, 97 et seq. (2004).

<sup>75</sup> BGH (German Federal Supreme Court), Judgment of March 14, 2005, *Zeitschrift für Wirtschaftsrecht* 26, 805 (806) (2005); *Goette*, Zu den Folgen der Anerkennung ausländischer Gesellschaften mit tatsächlichem Sitz im Inland für die Haftung ihrer Gesellschafter und Organe, *Zeitschrift für Wirtschaftsrecht* 27, 541 (544) (2006); *id.*, Krisenvermeidung und Krisenbewältigung in der GmbH – Überblick, *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 35, 261 (265) (2006); *Schall*, Englischer Gläubigerschutz bei der Limited in Deutschland, *Zeitschrift für Wirtschaftsrecht* 26, 965 (974 et seq.) (2005).

<sup>76</sup> The majority of German commentators makes an implicit cost argument by explaining that, in deference to the ECJ, the national law of the country of incorporation should apply: *Rönnau*, Haftung der Direktoren einer in Deutschland ansässigen englischen *Private Company Limited by Shares* nach deutschem Strafrecht – eine erste Annäherung, *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 35, 832 (834) (2006); *Forsthoff/Schulz*, Gläubigerschutz bei EU-Auslandsgesellschaften, in: Hirte/Bücker (eds.), *Grenzüberschreitende Kapitalgesellschaften – Praxishandbuch für ausländische Kapitalgesellschaften mit Sitz im Inland* (2005), § 15, 1; cf. *Sandrock*, Sitzrecht contra Savigny? – Zum angeblichen Chaos im internationalen Gesellschaftsrecht, *Betriebs-Berater* 59, 897 (899 et seq.) (2004).

vate Limited Company<sup>77</sup>. Conversely, the German limited partners cannot be subjected to the traditional capital maintenance schemes either<sup>78</sup>. Moreover, the directors of the corporate general partner should not be required to fulfill duties in conflict with the English concept of *ex post* rules in the vicinity of insolvency. It is at this stage where externalities of regulatory competition are most likely to occur. It is also at this stage where regulatory competition unleashes evolutionary processes in German company law.

## 5. The Ltd. & Co. KG in Insolvency

### a. *Caveat creditor*

Under s. 11 (2) of the German Insolvency Law (*Insolvenzordnung*) insolvency proceedings may also be brought against a Kommanditgesellschaft<sup>79</sup>. In comparing English and German approaches towards corporate insolvency Professor *Davies* has pointed out that English insolvency law focuses on furthering a rescue culture which considers the untimely liquidation of a company as wasteful<sup>80</sup>. German scholars perceive the English law on Private Limited Companies as an attempt to reinforce the principle of *caveat creditor*, setting statutory incentives for private contracting for creditor protection<sup>81</sup>. A similar criticism has been voiced against the ECJ which is thought to favor adjusting over non-adjusting creditors<sup>82</sup>. Admittedly, large, sophisticated adjusting creditors are in a much better position to address problems of regulatory arbitrage and moral hazard by negotiating covenants<sup>83</sup>. But it does not follow from this argument that an English Private Limited Company doing business in Germany should be subject to a statutory regime of *ex ante*-rules in the vicinity of insolvency.

Current German law on the GmbH and the GmbH & Co. KG does not guarantee complete reimbursement to creditors faced with insolvency<sup>84</sup>. Statutory capital maintenance rules and the duty to file for insolvency proceedings are intended to establish a comprehensive

<sup>77</sup> Non-organizational bankruptcy law has the potential to affect the structure of partnership-based business organizations. *Ribstein*, Wake Forest L. Rev. 40, 751 (773 et seq.) (2005); *Schön*, Der Konzern 2, 162 (170) (2004).

<sup>78</sup> However, they may owe fiduciary duties to ,their' partnership: See infra sub II.5.a.

<sup>79</sup> This includes a Ltd. & Co. KG even if the corporate general partner is a so-called ,pseudo-foreign' corporation: cf. AG (Magistrate's Court) Saarbrücken, Decision of February 25, 2005, Entscheidungen zum Wirtschaftsrecht 25, 701 et seq. (2005).

<sup>80</sup> *Davies*, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (329 et seq.) (2006).

<sup>81</sup> See *Fleischer*, Gläubigerschutz in der kleinen Kapitalgesellschaft: Deutsche GmbH versus englische private limited company, Deutsches Steuerrecht 38, 1015 (1021) (2000).

<sup>82</sup> *Goette*, Deutsches Steuerrecht 43, 197 (198) (2005); *Eidenmüller*, in: Eidenmüller (ed.), Ausländische Kapitalgesellschaften (supra N. 24), § 3, 37 et seq.

<sup>83</sup> *Enriques/Gelter*, Regulatory Competition in European Company Law and Creditor Protection, Eur. Bus. Org. L. Rev. (EBOR) 7, 417 (435) (2006); cf. *Fleischer*, Legal Capital: Navigation System for Corporate Law Scholarship, Eur. Bus. Org. L. Rev. (EBOR) 7, 29 (32 et seq.) (2006).

<sup>84</sup> *Haas*, supra N. 32, 13; *Kleindiek*, Krisenvermeidung in der GmbH: Gesetzliches Mindestkapital, Kapitalschutz und Eigenkapitalersatz, Zeitschrift für Unternehmens- und Gesellschaftsrecht 35, 335 (339) (2006).

regulatory system on the costs and benefits of asset partitioning<sup>85</sup>. Nonetheless, the system of imposing *ex ante* capital maintenance rules is incapable of providing adequate creditor protection<sup>86</sup>. Nor does it address incentive problems arising in the vicinity of insolvency when directors of a company might disregard creditors' interests<sup>87</sup>. The courts have developed rules to impose liability for withdrawing funds which could have been used for keeping the company in business<sup>88</sup>. This does not amount to a coherent *ex post* set of directors' duties whether to negotiate for a rescue scheme or to file for insolvency<sup>89</sup>. In the UK, common and statutory law requires directors to discontinue trading if under-capitalization would lead to insolvency<sup>90</sup>. This *ex post* approach, however, should not be taken as to discourage risky business decisions undertaken in an attempt to rescue the company in the wake of insolvency<sup>91</sup>.

In assessing the legal insolvency regime for a Ltd. & Co. KG German courts will have to establish an interface between English and German law, ushering in a move from an *ex ante* to an *ex post* perspective in the wake of insolvency. With respect to the Ltd. & Co. KG, special duties for the director of the managing general partner will have to be developed. As to capital maintenance it would seem that the traditional partnership law duties of loyalty and good faith might be construed as to sanction undue distributions, engineered by the general or limited partners. The limited partners of a Ltd. & Co. KG will, of course, continue to be directly liable for participating in a scheme to defraud the creditors. A recent project on reforming the law on close corporations confirms that even statutory models on legal capital

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<sup>85</sup> Cf. Fischer, Die Verlagerung des Gläubigerschutzes vom Gesellschafts- in das Insolvenzrecht nach „Inspire Art“, Zeitschrift für Wirtschaftsrecht 25, 1477 (1478) (2004); Goette, Deutsches Steuerrecht 43, 197 (198) (2005); *id.*, Zeitschrift für Unternehmens- und Gesellschaftsrecht 35, 261 (263 et seq.) (2006); Fleischer, Deutsches Steuerrecht 38, 1015 (1016 et seq.) (2000).

<sup>86</sup> Engert, Solvenzanforderungen als gesetzliche Ausschüttungssperren bei Kapitalgesellschaften, Zeitschrift für das gesamte Handels- und Wirtschaftsrecht 170, 298 (3189) (2006), offers a realistic explanation why the current system does not cause too much havoc in the business community: Companies have chosen relatively low levels of minimum capital and there are largely accepted possibilities to circumvent the current regime capital maintenance.

<sup>87</sup> Davies, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (309 et seq.) (2006).

<sup>88</sup> Goette, Zeitschrift für Unternehmens- und Gesellschaftsrecht 35, 261 (265) (2006); Kleindiek, Zeitschrift für Unternehmens- und Gesellschaftsrecht 35, 335 (359 et seq.) (2006); Schön, Zur „Existenzvernichtung“ der juristischen Person, Zeitschrift für das gesamte Handels- und Wirtschaftsrecht 168, 268 (372 et seq.) (2004); Haas, *supra* N. 32, 18 et seq.

<sup>89</sup> Cf. Veil, Krisenbewältigung durch Gesellschaftsrecht- Verlust des halben Kapitals, Pflicht zu ordnungsgemäßer Liquidation und Unterkapitalisierung, Zeitschrift für Unternehmens- und Gesellschaftsrecht 35, 374 (376 et seq.) (2006); Eidenmüller, Trading in Times of Crisis: Formal Insolvency Proceedings, Workouts and the Incentives for Shareholders/Managers, Eur. Bus. Org. L. Rev. (EBOR) 7, 239 (251) (2006); BGH (Federal German Supreme Court) Judgment of May 24, 2005, Betriebs-Berater 60, 1923 et seq. (2005).

<sup>90</sup> Morse, in Charlesworth's Company Law (N. 61), 317 et seq.; Finch (N. 60), 512 et seq.

<sup>91</sup> Cf. Davies, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (310) (2006). Moreover, the regulatory effects of restrictions on distributions have *ex ante* and *ex post* aspects. *Ex ante*, they protect adjusting creditors against opportunistic shareholders. *Ex post*, they are intended to foreclose social losses which might occur if assets are withdrawn from valuable projects: Armour, Legal Capital: An Outdated Concept?, Eur. Bus. Org. L. Rev. (EBOR) 7, 5 12 et seq. (2006).

have to be supplemented by *ex post* rules to adequately address the risks of asset partitioning<sup>92</sup>.

#### **b. Insolvency under the EIR**

Company mobility in the EU critically depends on the insolvency regime under the EIR. Under artt. 3(1), 4 (1) EIR the insolvency law of the Member State applies where the insolvent company has its main interests<sup>93</sup>. This mandatory choice of law rule is doubly inefficient: In times of crisis it invites *ex post* forum shopping<sup>94</sup>, whereas it forecloses the positive effect of *ex ante* contracting for an optimal insolvency law regime for a corporate entity<sup>95</sup>. Arguably, the application of national insolvency law to pseudo-foreign corporations might be justified as a policy device to internalize the costs of regulatory competition<sup>96</sup>. This ignores that organizational aspects of bankruptcy law may also destabilize the asset partitioning schemes of partnerships<sup>97</sup>. The administration of national insolvency law is therefore subject to the ECJ's jurisprudence on company mobility<sup>98</sup>. Under these circumstances it would seem that the EIR has to recognize a *de facto* choice of law for a corporate entity.

Critics of Private Limited Companies operating as pseudo-foreign corporations in Germany point with some justification to the fact that s. 214 of the British Insolvency Act<sup>99</sup> can only be invoked in insolvency proceedings in the UK. Thus, it is assumed that in case of a 'German insolvency' of a Ltd. & Co. KG or its managing general partner, there would be no statutory incentive to undertake rescue attempts, or alternatively, to desist from diverting

<sup>92</sup> Cf. *Bundesministerium der Justiz* (German Federal Ministry of Justice), *Zeit für Gründer – die GmbH-Reform*, Mitteilung für die Presse (Berlin, May 29, 2006); and *infra* sub III.2.

<sup>93</sup> Art. 3(1) EIR:

*The courts of the Member State within the territory of which the center of the debtor's main interests is situated shall have jurisdiction to open insolvency proceedings. In the case of a company or a legal person, the place of the registered office shall be presumed to be the center of its main interests in the absence of proof to the contrary* [It is obvious that this rebuttable presumption is not available to the 'German' type of the Ltd. & Co. KG – a pseudo-foreign corporation – .].

Art. 4(1) EIR:

*Save as otherwise provided in this Regulation, the law applicable to insolvency proceedings and their effect shall be that of the Member State within the territory of which such proceedings are opened, hereafter referred to as the 'State of the opening the proceedings'.*

<sup>94</sup> Cf. on forum shopping under a federal bankruptcy law: *LoPucki*, *Courting Failure: How Competition for Big Cases is Corrupting the Bankruptcy Courts* (2005); *Zywicki*, *Is Forum Shopping Corrupting America's Bankruptcy Courts?*, *Geo. L. J.* 94, 1141 (1160 et seq.) (2006).

<sup>95</sup> *Eidenmüller*, *Wettbewerb der Insolvenzrechte?*, *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 35, 467 (474 et seq.) (2006); *id.*, *Free Choice in International Company Insolvency Law*, *Eur. Bus. Org. L. Rev. (EBOR)* 6, 424 (429 et seq.) (2005).

<sup>96</sup> *Vallander*, *Die Insolvenz von Scheinauslandsgesellschaften*, *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 35, 425 (454) (2006).

<sup>97</sup> See *supra* N. 77.

<sup>98</sup> *Armour*, *Eur. Bus. Org. L. Rev. (EBOR)* 7, 5 (25) (2006).

<sup>99</sup> See *supra* N. 64.



funds otherwise available to the creditors<sup>100</sup>. It is not foregone conclusion, though, that as a consequence German law should prevail in order to fill a ‘regulatory gap’. The ECJ’s jurisprudence protects the asset partitioning scheme the members agreed upon at the time they established the partnership. Thus, German courts – faced with an insolvent Ltd. & Co. KG or a Ltd. & Co. KG close to insolvency – are under an obligation to develop legal rules that do not thwart regulatory competition among business organization laws.

### c. English Law ‘Infects’ German Law

In coming to terms with an English Private Limited Company German courts are mindful of distinguishing adjusting from non-adjusting creditors. The German Federal Supreme Court has held that English law determines directors’ liability for contractual obligations of a Private Limited Company<sup>101</sup>. Statutory English law provides for a catalogue of criteria disqualifying the director of private limited company from discharging his duties for the company. There is no major difficulty in translating this statutory list into German law in order to ban a disqualified director from heading the general managing partner of a Ltd. & Co. KG<sup>102</sup>.

As the Ltd. & Co. KG is under no capital maintenance obligation, creditors may wish to know what triggers insolvency proceedings in Germany. S. 214 of the Insolvency Act addresses the perverse incentives for directors of a company in the vicinity of insolvency. A (costly) rescue attempt is acceptable as long as information available on cash flow and balance sheet tests had not established a case for liquidation<sup>103</sup>. Theoretically, s. 64 (1) of the German statute for close corporations has the potential to become ‘infected’ by English regulatory policies<sup>104</sup>. At first look, s. 64 (1) appears to be an unlikely candidate to implement English regulatory policy decisions as it confers an individual claim on a creditor if the di-

<sup>100</sup> See the arguments advanced in the judgment of the LG (District Court) Kiel of April 20, 2006, GmbH-Rundschau 97, 710 (711) (2006), and in: *Wachter*, Persönliche Haftung des Gründers einer englischen *private limited company*, Betriebs-Berater 61, 1463 (1464 et seq.) (2006).

<sup>101</sup> BGH (Federal German Supreme Court); Judgment of March 14, 2005, Zeitschrift für Wirtschaftsrecht 26, 805 (806) (2005): The mere fact that the director of the company failed to comply with the registering requirements for branch offices does not establish liability under the provisions of the German statute on close corporations. The BGH has taken a similar approach towards the director of a French Sarl registered in France: Judgment of July 15, 2004, Case No. III ZR 315/03.

<sup>102</sup> Cf. *Haas*, Die Disziplinierung des GmbH-Geschäftsführers im Interesse der Gesellschaftsgläubiger, Wertpapier-Mitteilungen 60, 1369 (1372 et seq.) (2006), and the in-depth analysis of English law on the disqualification of company directors by *Davies*, in: Gower and Davies, supra N. 61, 211 et seq.

<sup>103</sup> *Davies*, Eur. Bus. Org. L. Rev. (EBOR) 7, 301 (319 et seq.) (2006).

<sup>104</sup> The judgment of the LG (District Court) Kiel of April 20, 2006, GmbH-Rundschau 97, 710 (711) (2006), is the first case where a German court held s. 64 (1) of the close corporation to apply to the director of a (pseudo-foreign) English Private Limited Company, taking a rather broad brush approach towards liability without evaluating the underlying regulatory policy of s. 214 of the English Insolvency Act. In the end, the court skirted the issue by deciding that there was also a clear case of fraud so that the relevant German tort statute would apply. Cf. *Wachter*, Persönliche Haftung des Gründers einer englischen *private limited company*, Betriebs-Berater 61, 1463 (1464 et seq.) (2006).

rector of close corporation fails to file a petition for the commencement of an insolvency proceeding<sup>105</sup>. In fact, s. 64 (1) operates as a ‘safe harbor’ provision for the director as the insolvency petition will exonerate him from personal liability. But, in construing s. 64 (1) German courts would have sufficient leeway to exempt a director who made a reasonable rescue attempt<sup>106</sup>. Conversely, the director who distributed funds after the company became insolvent may be held liable on an analogy with the norm applicable to close corporations (i.e. s. 64 (2) of the German law on close corporations)<sup>107</sup>. The limited partners of a Ltd. & Co. KG may be under a similar obligation if they *de facto* dominate the management of the company<sup>108</sup>, or if they participate in acts detrimental to the interests of the creditors<sup>109</sup>. The German statute on close corporations and general tort law concepts are sufficiently broad to incorporate English law concepts developed under s. 214 of the Insolvency Act or under common law<sup>110</sup>. This does, of course not apply to the English preference for collective claims to be raised against the director in insolvency proceedings. It is perhaps too early to determine whether this would create a serious disincentive for the directors of the managing general partner as (yet dormant) common law duties may come to unfold parallel effects.

There is a major difference between English and German regulatory tests as to ascertain solvency issues: S. 214 of the Insolvency Act operates on a balance sheet test whereas, under the German statute, creditor-regarding duties arise under the cash flow *and* balance sheet tests<sup>111</sup>. Arguably, these English law concepts can be translated into the interpretation of the relevant German statutes. But there is always the risk that courts, in relying on German law concepts exclusively, will be in breach of the ECJ’s jurisprudence on company law<sup>112</sup>. This is not so much a matter of whether company or insolvency law approaches should be controlling. It is rather more a question of whether the founders of a Ltd. & Co. KG are willing to incur the costs of buying English law expertise to persuade the court to apply English

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<sup>105</sup> S. 64 (1) of the German statute on close corporations (*GmbH-Gesetz*) requires the director of an insolvent or illiquid close corporation to commence insolvency proceedings without undue delay. The maximum statutory delay is three weeks. Failure to comply with this duty may also give rise to a claim for damages under Germany’s tort law statute.

<sup>106</sup> Cf. BGH (German Federal Supreme Court), Judgment of May 24, 2005, *Betriebs-Berater* 60, 1923 (1925 et seq.) (2005); *Flitsch*, Case Note, *Betriebs-Berater* 60, 1928 (2005).

<sup>107</sup> Cf. *Goette*, Zur systematischen Einordnung des § 64 Abs. 2 GmbHG, in: *Festschrift für Kreft* (2004), 53 et seq.

<sup>108</sup> Cf. BGH (German Federal Supreme Court), Judgment of June 27, 2005, Case No. II ZR 113/03.

<sup>109</sup> Cf. BGH (German Federal Supreme Court), Judgment of September 20, 2004, Case No. II ZR 302/02.

<sup>110</sup> Cf. *Schall*, *Zeitschrift für Wirtschaftsrecht* 26, 965 (975) (2005); *Goette*, *Zeitschrift für Unternehmens- und Gesellschaftsrecht* 35, 261 (279) (2006).

<sup>111</sup> See *Davies*, *Eur. Bus. Org. L. Rev. (EBOR)* 7, 301 (318 et seq.) (2006).

<sup>112</sup> *Just*, Case Note, *Zeitschrift für Wirtschaftsrecht* 27, 1251 (1253) (2006).

corporate law principles<sup>113</sup>. Apparently, the proponents of German close corporations are hoping for prohibitive transaction costs so that in the long run, the GmbH & Co. KG will prevail. But many of these difficulties can be overcome by private ordering and a well written contract establishing a Ltd. & Co. KG.

### III. Is there a Regulatory Message?

#### 1. Regulatory Competition Unleashed by the Ltd. & Co. KG

Statements on the quality of regulatory competition are, at best, inconclusive, unless the cost effects of the ECJ's jurisprudence are evaluated. Empirical evidence suggests that the cost of regulation determines the business decision where to incorporate in Europe<sup>114</sup>. There is an element of signaling in the decision to use a 'pseudo-foreign corporation' as a managing general partner, operating exclusively in Germany<sup>115</sup>. The Ltd. & Co. KG combines the advantages of incorporating in the UK with the freedom of German partnership law to devise a business organization tailored to the needs of start-up companies and sophisticated investment projects independent of comprehensive codetermination laws. The Ltd. & Co. KG is a case of first application of a company law model that confers the right to choose freely from statutory opt-in and opt-out clauses<sup>116</sup>. In relying on their freedom of contract the members of a Ltd. & Co. KG add an innovation to the asset-partitioning structures of partnership law, thereby increasing the competitive pressure on the German legal system<sup>117</sup>.

The ECJ indicates that regulatory competition is based on a trade-off between company mobility and cost internalization. From the perspective of regulatory policy EU law is based on a presumption against mandatory cost internalization rules as long as national information-rules are effective. The Ltd. & Co. KG is found to sufficiently internalize the costs of its business activities in Germany. In this, the advent of the Ltd. & Co. KG unleashes evolutionary processes in German law which is edging from an *ex ante* to an *ex post* approach in creditor protection. Traditional rules of partnership law are 'infected' with English law con-

<sup>113</sup> Griffiths/Tschentscher, The Straw Dogs of Europe, *Insolvency Intelligence* 17 (4), 57 (61) (2004); cf. Goette, *Zeitschrift für Wirtschaftsrecht* 27, 541 (544) (2006).

<sup>114</sup> See the study by Becht/Mayer/Wagner, Costs, supra, N 68.

<sup>115</sup> Cf. Fluck/Mayer, Race to the Top or Bottom? Corporate Governance, Freedom of Reincorporation and Competition in Law, European Corporate Governance Institute Law Working Paper No. 90/2005 (July 2005), emphasizing that certain norms of conduct of firms are sought irrespective of the location of their operations; and Iacobucci, Toward a Signaling Explanation of the Private Choice of Corporate Law, *Am. L. & Econ. Rev.* 6, 319 et seq. (2004), applying a signaling analysis to private choice of securities regulation domicile.

<sup>116</sup> See supra N. 17.

<sup>117</sup> Cf. the competitive assessment analysis by the Head of the Corporate Law Division of the German Ministry of Justice: Seibert, GmbH-Reform: Der Referentenentwurf eines Gesetzes zur Modernisierung des GmbH-Rechts und zur Bekämpfung von Missbräuchen – MoMiG, *Zeitschrift für Wirtschaftsrecht* 27, 1157 (1158) (2006).

cepts, creating a potential for rebalancing the incentives of the general managing partner and the limited partners in the vicinity of insolvency. Currently, this regulatory evolution has its shortcomings. There is considerable uncertainty on how to introduce a meaningful solvency concept into German law and whether creditors' rights of action pose a serious threat to the director of the managing general partner<sup>118</sup>. On the other hand, the current state of law considerably enlarges the opportunity for private ordering in company law.

## 2. Whither National and/or European Company Law?

The flexibility of partnerships makes this type of business organization notoriously hard to regulate<sup>119</sup>. Germany has currently to master a transition process that should facilitate entrepreneurial activities in start-up businesses without destabilizing mature companies. Under these circumstances it is conceptually difficult to develop a coherent regulatory policy that achieves optimal social welfare for mature *and* start-up companies<sup>120</sup>. With respect to the Ltd. & Co. KG, freedom of contract and self-regulation appear to be preferable.

The German government perceives the English Private Limited Company as a competitive threat and has reacted by introducing a project of law reform for the close corporation (GmbH) which would also affect the Ltd. & Co. KG<sup>121</sup>. The proposal provides for 'pseudo-foreign corporations' of German origin<sup>122</sup>. Without sacrificing the statutory concept of capital maintenance the threshold for new business activities is lowered. The German government implicitly makes a cost argument by weighing the (reduced) statutory minimum capital against the transaction costs of using an English Private Limited Company as the general partner of a Ltd. & Co. KG. It remains to be seen whether this new law staves off competitive pressures<sup>123</sup>, as the UK Parliament prepares for a law reform that would further deregulate the law of small and private companies<sup>124</sup>.

<sup>118</sup> The application of English law principles will not affect German regulatory policy in favor of individual enforcement of creditors' claims against the director of company in insolvency (cf. the claim for wrongful trading under s. 214 of the English Insolvency Act).

<sup>119</sup> Cf. *Ribstein*, Berkeley Bus. L. J. 1, 183, (216) (2004).

<sup>120</sup> *Fluck/Mayer*, supra N. 115; on the appropriate corporate law design for start-ups cf. *Hyytinen/Takalo*, Corporate Law and Small Business Finance: Mandatory v. Enabling Rules, Eur. Bus. Org. L. Rev. (EBOR) 6, 449 (459 et seq.) (2005).

<sup>121</sup> Cf. *Seibert*, Zeitschrift für Wirtschaftsrecht 27, 1157 (1161) (2006).

<sup>122</sup> Under the new law a GmbH would be allowed to relocate its headquarters to another country while formally remaining in Germany.

<sup>123</sup> *Dierksmeier/Scharbert*, GmbH und englische Reformen im Wettlauf der Reformen 2006, Betriebs-Berater 61, 1517 et seq. (2006); see the criticism by *Triebel/Otte*, Reform des GmbH-Rechts: MoMiG – ein vernünftiger Schritt zur Stärkung der GmbH im Wettbewerb oder Kompromiss auf halber Strecke?, Zeitschrift für Wirtschaftsrecht 27, 1321 (1326 et seq.) (2006).

<sup>124</sup> *Library of the UK House of Commons*, Research Paper 06/30 on The Company Law Reform Bill [HL] (London, June 2, 2006); *Henning*, The Company Law Reform Bill, Small Businesses and Private Companies, Comp.

It is a matter of political controversy whether EU legislative action should address market failure during competitive regulatory processes<sup>125</sup>. When the *High Level Group of Company Law Experts* submitted its report on European company law to the EU Commission, it questioned the urgency of introducing a European statute on private companies<sup>126</sup>. Much more empirical analysis is necessary to ascertain whether regulatory competition between national laws produces externalities that harmonization should contain<sup>127</sup>. The Ltd. & Co. KG suggests that regulatory competition, private ordering and evolutionary processes are capable of establishing a balance between company mobility and creditor protection<sup>128</sup>.

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L. 27 (4), 97 et seq. (2006); *Sheikh*, Company Law Reform (Part II), Int'l. Comp. & Com. L. Rev. 17 (3), 96 et seq. (2006).

<sup>125</sup> Cf. *Pistor/Xu*, Incomplete Law, N. Y. U. J. Int'l. L. & Pol. 35, 931 (1962) (2003); *Gerardin/McCahery*, Regulatory co-opetition: transcending the regulatory competition debate, in: Jordana/Levi-Faur (eds.), *The Politics of Regulation* (2004), 90 (99 et seq.).

<sup>126</sup> Report of the High Level Group of Company Law Experts on *A Modern Regulatory for Company Law in Europe*, Brussels, November 4, 2002 (Chairman: Jaap Winter, Other Members: Klaus J. Hopt; Jonathan Rickford; Guido Rossi; Jan Schans Christensen; Joëlle Simon; Rapporteur: Dominique Thienpont; Secretariat: Karel Van Hulle), 23 et seq., 113 et seq. ([http://www.europa.eu.int/comm/internal\\_market/en/company/company/modern/consult/report\\_en.pdf](http://www.europa.eu.int/comm/internal_market/en/company/company/modern/consult/report_en.pdf)).

<sup>127</sup> For a more optimistic approach see *Drury*, The European Private Company, Paper submitted for the Public Hearing by the European Parliament Committee on Legal Affairs (June 22, 2006); *Eidenmüller*, Free Choice in International Corporate Law: European and German Corporate Law in European Competition between Corporate Law Systems, in: Basedow/Kono (eds.), *Economic Analysis of Private International Law* (2006); *Schön*, Mindestharmonisierung im europäischen Gesellschaftsrecht, *Zeitschrift für das gesamte Handels- und Wirtschaftsrecht* 160, 221 et seq. (1996). A public policy assessment is undertaken by: *Deakin*, Eur. L. J. 12, 440 et seq. (2006); van den Bergh, Towards an Institutional Legal Framework for Regulatory Competition in Europe, *KYKLOS* 53, 435 et seq. (2000); *Hopt*, Company Law in the European Union: Harmonization and/or Subsidiarity?, Int'l. & Comp. Corp. L. J. 1, 41 et seq. (1999).

<sup>128</sup> Cf. *Armour*, Who Should Make Corporate Law? – EC Legislation versus Regulatory Competition, Current Legal Problems 58, 369 et seq. (2006). In discussing the regulatory approach towards publicly-traded corporations Professor *Schön*, The Market for Corporate Law – Comment, *J. Inst'l. & Theor. Econ. (JITE)* 162, 168 (170) (2006), envisages a federal legislator introducing substantive minimum rules or opt-in solutions available to shareholders.