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GROUPS OF COMPANIES IN AUSTRIA AND IN THE EUROPEAN UNION - THE INTEREST OF THE GROUP

Whereas groups of companies are a very common phenomenon in Austria as well as in the entire European Union [1, p. 1], legal grounds for them are largely inexistent. Even if some aspects were regulated in the past years, one of the most important questions, namely whether the parent company can adversely make use of its subsidiaries, remains unaffected so far. This paper addresses how Austria and other European Member States deal with groups of companies and the relationship between parent and subsidiary companies from a legal perspective and gives special regard to cross-border transactions.

A. Corporate Group Law in Austria

I. General Remarks

In Austria, groups of companies are not regulated in corporate law. In competition or tax law there are provisions regulating groups for very specific purposes (e.g. group taxation and certain tax exemptions). Yet, there are no general material rules on typical group-related issues - such as how groups are formed or how conflicts of interest arising between affiliates can be resolved. Corporate group law as such is inexistent in Austria [1, p. 9].

As there is no group law, there are no privileges provided for the group. Accordingly, this requires that every company of a group be regarded as an autonomous legal entity by ignoring the ties between parent and subsidiary companies.Each entity has to be managed according to its own interest. This does not equal just the economic interests of the undertaking, but comprises the interests of different stakeholders, including the employees, the shareholders as well as the public interest [2, § 70]. The so-called *enlightened shareholder* value requires the managing board to consider concerns of many parties besides the enterprise and yet it may not align its company management with another enterprise [3, p. 13].

II. The Interest of the Group

From an economic perspective, however, this approach is neither utterly correct nor adequate[4, p. 195].Companies form groups, irrespective of whether there exists a satisfactory legal foundation for it or not. Steering a

group of companies implies making difficult business judgment decisions that require a difficult balancing of interest between the subsidiary and the parent [1, p. 5].Transactions may be beneficial or even necessary for the entire group while they are disadvantageous or even harmful to one of the subsidiaries.

What is commonly described as the *risk of the group* are the interests of a holding company that deviate from traditional long-term investors, asa group typically has the intent of taking advantage of a subsidiary for group-oriented purposes [5, p. 14;6, mn. 2.5]. Subsidiaries are often exposed to influence from the parent company, which may affect creditors and minority shareholders negatively.The influence can be wielded in different ways, comprising formal instruction rights as well as informal pressure.If the influence is exercised intensively, the subsidiaries' independence can diminish [4, p. 195].

This gives rise to the question whether commercial transactions that are harmful to the subsidiary can be exercised for the benefit of the group, and, if yes, if there is a need for compensation.The problem is described with the term *group interest*, which denotes an interest apart from the individual company's interest. The interest of the group equals, at least according to the predominant view, the interest of the holding parent company [7, p. 257; 8, mn. 92, mn. 156]. It is yet in the parent company's interest that the share in their affiliate is performing well, as it constitutes an asset of the holding company [8, mn. 156]. The subsidiaries interests are thereby considered indirectly and form part in the holdings' interests.The academic discussion revolves around whether the interest of the group can supersede the interest of the single company.

Even if the prevailing view in Austria refrains from acknowledging a group interest, because it – in simplified terms – is deemed to contradict the independence of a company, other European Member States approach the issue very differently.Their regimes stretch from not acknowledging the group at all to a far-reaching integration of the subsidiary into the parents undertaking. How European groups struggle with this system will become apparent immediately.

B. Three Regulatory Models of the Interest of the Group in Europe

I. Non-Consideration of the Group

One way of regulating groups is not recognising the group structure at all in terms of law. Besides Austria, this system prevails in the United Kingdom and other smaller Member States.A corporate group enjoys no legal privileges and each company has to be treated individually, despite the economic ties. Business has to be done according to the interest of the single undertaking.

If a company hence forms part of a group and is expected to adjust to a group policy, the management has to evaluate every action on an individual

basis regarding whether or not it respects the subsidiaries interest to an appropriate extent. Such assessment on a case-by-case basis requires time, as well as it disregards the benefits that typically result from the formation of a group. Apart from deterring group formation, the model therefore is perceived to be slow and labour-intensive [9, mn. 7.58].

In addition to this, the obligations of the managing directors are defined rigorously [3, p. 17].If managers consider the interest of the group disproportionally and fail to exercise the necessary diligence for the subsidiaries interest, they expose themselves to liability claims [4, p. 200] as well as criminal sanctions.They must not run the company in a manner that is "unfairly prejudicial" to its members [3, p. 17] and should refuse parent's instructions if they prove detrimental to the subsidiary (the detriment has to be judged within a certain timeframe) [3, p. 14]. Law-abidance hence is secured by a personal liability of the board [4, p. 200].

II. Compensation for Disadvantages

The second model is the system prevalent in Germany, which has had wide effects on other (Member) States: Portugal, Hungary, Croatia, Slovenia, Czech Republic, Albania, and even Brazil and Turkey have introduced similar policies, yet to a variable extent [4, pp. 199 et seq.].

According to the German *Aktiengesetz*, a transaction made for the benefit of the group is legitimate, if the financial prejudice suffered by the subsidiary company is justified by other advantages or a compensation [10, p. 13].The parent company enjoys the right to instruct its subsidiaries on detrimental business transactions, but has the duty to compensate the subsidiary's losses and detriments originating from this direction on a yearly basis. It is therefore liable to compensate for any disadvantage that the subsidiary entailed during a business year.

As long as they are balanced, all kinds of negative transactions may be executed by the subsidiary [9, mn. 7.53].No individual assessment of the transactions is required as to whether it respects the subsidiaries interest, which offers the management a great flexibility in business transactions [9, mn. 7.58].As regards the exact nature of the offset and the time as well as the procedure of the compensation, this is subject to different determinations in the Member States [10, p. 13].

III. Precedence of the Interest of the Group

The third and last model originates from French law. It became famous under the name "*Rozenblum*-doctrine", which stems from a ruling of the French *Cour de Cassation* in 1985 [11].In his ruling the court defined the interest of the group as a guideline for entrepreneurial behaviour in a group.

Subsidiaries do not have to consider the advantages and disadvantages for their company when taking managerial decisions, but are allowed to act solely in the interest of the group. This may result in transactions that are to the detriment of the subsidiary. In contrast to the German model, compensation of the subsidiaries is not necessary[12, mn. 1.34]. Adequate protection of the subsidiary is automatically established when the necessary criteria are fulfilled, which are(1) a stable structure of the group, (2) an ex-ante defined, coherent group policy instituted by the parent, as well as (3) a fair distribution of benefits and costs among the group members. The last criterion implies that the group in total pursues a profitable purpose [1, p. 19;cf. also 4, pp. 200 et seq.;9, mn. 7.56;13, p. 14; 14, pp. 92 et seqq.].

This system proves to be the most flexible for the parent as well as the subsidiaries. It provides a safe harbour for the managing board as they do not have to fear to face liability or even committing a penal offence when acting for the benefit of the group [12, mn. 1.34].Due to those reasons, the *Rozenblum*-doctrine has spread to other Member States. The Netherlands for example have implemented the same concept under a different name (so-called *Nimox*-doctrine [15]). Italy follows a similar concept too [cf. 16, pp. 175 et seqq.].

C. Cross-border Transactions

The fact that the European Member States handle the issue differently creates extensive legal uncertainty for cross-border groups and their managers. Whether or not a legislation acknowledges the group interest defines which rules for business conduct the management has to respect in each country.

The management has to evaluate if it can introduce a uniform corporate group policy for the entire group, given the diverging and maybe even contradicting legal frameworks. In the case of cross-border groups with subsidiaries in many different countries, the large number of legal concepts can lead to precarious situations for the management, both of the parent and the subsidiary companies. First, the management board of the holding needs profound legal knowledge as to which extent - or whether at all - they are allowed to govern the group according to uniform guidelines and whether they have a right to make use of instruction rights. The directors of subsidiaries face liability or even penal sanctions if they take forward a measure that is not in line with the national law. If they do not align with the group policy, on the other hand, they risk their dismissal [10, p. 13; 17, pp. 90 – 91; 18, p. 313].

D. European Efforts and Developments

Pierre van Ommeslaghe identified the problem already 50 years ago and wrote about the conceptual problem that there is no (European) law on groups

[19, cf. p. 153]. His apprehension has not lost its validity over the years. The key to a harmonised law of groups of companies and therefore to legal security is the recognition of the interest of the group on a union-wide basis [17, p. 91; 20, p. 22].

On an overall European basis, no explicit body of law was agreed upon that shapes the legal relationships regarding groups.Despite the significant relevance of company groups in the European Union [cf. 1, p. 2], only little harmonising measures have been implemented Europe-wide [21, p. 337]. There are a few regulations in place that indirectly affect groups, at least in certain aspects. Examples are the SE-Regulation, which tries to remove obstacles to the creation of groups by offering a European company [22, cf. Recital 4] or the Accounting Directive [23], which obliges groups to draw up consolidated financial statements [24, m.nos. 6.5 et seq.].

The European Commission has made a number of efforts trying to harmonise the group interest. Dating back to 1974 and 1975 [25], first attempts for a union-wide harmonisation of the law of company groups were made. The topic was on the agenda a few more times [cf. for example 26;27; 28], however, a consensus was never reached [cf. 29, pp. 266 et seq.].

Since then, legal academia has not abandoned the topic. Expert groups, consisting of academics as well as practitioners, have kept the topic high on the European agenda. The *High Level Group of Company Law Experts*, the *Reflection Group on the Future of EU Company Law*, the *Informal Group of Company Law Experts*, the *Forum Europaeum on Company Groups* as well as the *European Company Law Experts* have basically recommended following and further developing the acknowledging of the group interest [1, p. 19; 20, p. 15].

The *Rozenblum*-concept is the go-to strategy for the various expert groups researching on harmonising the group interest on the European level [cf. for example 18; 30]. Yet, no consensus was found on any of their proposals. Concerns expressed range from the interest of the company's creditors not being protected effectively to a lack of a fair balance of burdens and advantages over time for the company's shareholders [10, p.13].

Due to lacking European legislation, however, it is still upon the Member States to implement adequate provisions. But just like Austria, many European Member States only rely on general principles of corporate law to regulate groups or have narrow rules for specific aspects of groups of companies [13, p. 10]. Only few dispose of explicit rules governing the legal relationships of groups of companies (e.g. Germany, Italy, Croatia, Portugal, Slovenia, Czech

Republic, Hungary) [13, pp. 9 et seq.] and the content of the norms is even more diverging.

E. Future Prospects

The introduction of the group interest is yet a desirable harmonisation in terms of enabling European groups to do business transnationally. Cross-border trade can be enhanced with a European framework that allows managers to adopt a uniform group policy [10, p.13]. It can also reduce the cost for such transactions since groups have to invest less in analysing the technicalities of each national law [31, p. 61]. This has the potential to disburden especially smaller groups (SMEs), due to facilitation of the management [4, p. 210].

The latest developments in this respect focus on wholly owned subsidiaries. The proposals suggest that if all the shares of a subsidiary (a so-called *Service Company*) are held by the parent,it may take account of the parents interests in its business decisions as there are no endangered minority shareholders [18, pp. 299 et seqq.; 30, pp. 40 et seqq.; 32, pp. 447 et seqq.].

Even if this might constitute a first step, it is still a long way from a business-friendly, enabling group law. While there is some convergence on other aspects of group regulation [1, p. 19], acknowledging the group interest Europe-wide will continue to be discussed.

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Keywords: groups of companies, interest of the group, European Union, Austria, group law, company groups, harmonisation