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The Implementation of a Statute for a European Company (SE) and basic information on its usage

The basic framework of the legal framework for a European Company (= *societas europaea* “SE”), was agreed in principle at a EU summit held in December 2000, and later approved at a labor ministers’ meeting held in the same month. This framework consists of the “EU regulations for SE legislation” and the “EU Directive with regard to employee involvement for SE legislation”. The SE legislation, effective since October 8, 2004 enables the establishment of a company under EU Law (SE), separate from domestic law, and is an advanced form of EU integration for company law purposes. While each member state must adopt the SE legislation in its domestic law, not all member states have completed this procedure at the present stage.

This article will introduce the basic concepts and information with regard to the SE. What we would like to confirm is that neither the SE nor its legislation aim to abolish the domestic company laws of EU member countries. The SE is an alternative company form which is an “option” adopted in cases of merger where two or more companies located in several EU member states have merged (through a merger or by establishing a new company), or in the case of the establishment of a joint venture or a holding company. By using the domestic rules, of each member state, leaving out and adopting them into their company laws, the SE and its legislation aim to simplify corporate reorganization at EU Community level. As a result, SE legislation does not provide detailed rules. Rather, it provides a basic legal frame. Specifically, SE legislation assumes companies will establish SEs and does not assume that an individual contributor will establish the SE.

1. Registration: Minimum capital and preparation of statements of account

SE registration is carried out through an existing registration body in each member state as other companies to be established under its domestic law would and status as a legal entity is guaranteed from the date when the registration procedure has been completed. Registered place (the location registered or the country of registration) must be the place where the corporate decision-making is carried out, that is the place which carries out head office functions, enabling the overall effective supervision of the SE and to prevent the abuse of the SE structure for tax avoidance or money laundering. The way to supervise functional discrepancy at the registered place and head office

location has not yet been clarified at the present stage. However, the Netherlands and Belgium insisted that this matter of functional discrepancy should be dealt with over the course of discussions at Nice. As a result, a report with regard to this subject will be issued within five (5) years of the implementation of SE legislation.

As stated above, SE legislation does not provide detailed rules and in principle, the domestic law in a country where the SE is registered and located will apply. Therefore, the registered country of the SE will be a very important point. A registered SE will be announced publicly in accordance with regulations of domestic law in the registered country, and at the same time will be disclosed in the EU Official Journal. The title of the SE must be affixed before or after the company title to identify its legal form.

If, once established, the SE wishes to change its registered country, such a change would be admitted without additional legal procedures, such as liquidation of the exiting SE and establishment of a new SE, provided that protection of claimers and right to participate the joint decision system for employees are ensured and legal procedure therefore is provided. However, tax rules to prevent any tax demerits for the SE are not included in the SE legislation agreed to in Nice, so an early agreement to cope with tax demerits is anticipated.

The minimum capital amount of an SE is 120,000 Euro and if the registered country provides a higher amount of capital for the specific line of business, the SE would be subject to such a rule. Regarding the maintenance of the capital, measures regarding capital increase or reduction and other issues, the SE will follow any company rules provided by the registered country. The preparation of statements of accounts, disclosure and auditing will also be subject to the company rules of the registered country. For example, an SE registered in non-EU member state may prepare, audit and disclose its statements of accounts in both Euro currency and local currency.

2. Establishing principal and establishment method

The establishing principal of an SE must be a corporate body located in an EU member state (more precisely, its registered place and head office function should be located in an EU member state). Specific information regarding the kind of legal entity which may become an establishing principal is listed in an Appendix of "EU regulation for SE".

An SE can be established under either of the following methods:

- (1) Two (2) or more companies already existing in EU member states merge into each other (=stock company merger SE);
- (2) Two (2) or more different companies or limited liability companies in EU member states establish a new holding company as its parent companies, or two (2) or more companies or limited liability companies with subsidiaries or branches in other EU member states for two (2) years or more newly establish a holding company as its parent companies (= holding company SE);
- (3) Two (2) or more companies in different EU member states (including companies provided under public laws) establish a new common subsidiary, or two (2) or more companies or limited liability companies with subsidiaries or branches in other EU member states for two (2) years or more newly establish a common subsidiary (= joint venture SE); and
- (4) A company with a subsidiary in another EU member state for two (2) years or more reorganizes its company as an SE (=reorganized company SE).

For an SE to change its registered place to another EU member state, liquidation and new establishment are not required for “reorganized company SE”. However, the SE would not be admitted to change its registered place to another EU member state at the same time as at the establishment of a “reorganized company SE”. In the case of a “stock company merger SE”, a “merger proposal” must be prepared. In the cases of a “holding company SE”, “establishment proposal” and a “reorganized company SE”, a “reorganization proposal” must be prepared. In order to protect the rights of claimers and employees, these documents must be disclosed within a certain period and should be approved at a general shareholders’ meeting.

3. Organization of an SE

As it is well known, EU member states have the two-layer structure and the single-layer structure as the basic structures for companies with legal entities (particularly stock companies). The “two-layer structure” has two different organizations, i.e., “board of directors” conducting management business and an “auditors committee” supervising the board of directors, like an Aktiengesellschaft (AG) in Germany. As well as a general shareholders’ meeting, there are three organizations consisting the stock company in this case. The “single-layer” company is conducted by a board of directors conducting management and supervising the management. The typical example is an Anglo-Saxon type company in the UK. In this type, the stock company consists of two organizations, a general shareholders’ meeting and the board of directors.

These different types of organization for stock companies are still effective under the SE legislation.

Under the “two-layer structure”, the minimum and maximum numbers of the auditing committee members are provided under an article of incorporation complying with the domestic laws of the EU member state. Under the “single-layer structure”, the number of board of directors members is provided under the articles of incorporation, although this should be comply with the domestic laws of the EU member states. If the SE is subject to a joint decision system based on “EU Directive with regard to employees’ involvement for SE legislation”, the minimum number of members of the board of directors is three (3). Under the “two-layer structure”, members of the board of directors are elected by the auditing committee separate from the general shareholders’ meeting (in Germany). However, if the domestic laws of the EU member states provide that the general shareholders’ meeting should elect members directly, the SE would be subject to such a law.

Among the rules of a “two-layer structure” and the “single-layer structure”, the most important are those regarding the office term of the board of directors and auditing committee members, as well as those regarding corporate member acceptance by such organization. Specifically, the maximum office term under the article of incorporation would be six (6) years and if the domestic law of the registered country allows, a corporation may become a member of the board of directors or auditing committee, provided that a person (natural?? person) is sent as a representative of the said corporation.

4. Employee involvement of an SE and the joint decision system

Similar to the issue of the organization structure of a stock company, there are a variety of rules regarding employee involvement, participation structure and scope thereof. While this may be resolved by ensuring options such as the “two-layer structure” or the “single-layer structure”, Germany has insisted on its own method, fearing that the German joint decision system might lose its substance. This is why the idea of an SE has been abandoned many times and it has taken almost 30 years to reach the Nice agreement.

The basic policy of this issue is:

- (1) In the case of a newly-established SE, mutual agreement is required between the employer and the union; and
 - (2) If there is no agreement, a “standard rule” will apply, except for special cases.
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- (1) Conference with special negotiating body

According to “EU Directive with regard to employee under SE legislation”, in cases where the establishment of a new SE is determined regardless of the establishment method stated above (more specifically, promptly after the disclosure of the merger proposal and the like), the management side must commence in discussions regarding the form and scope of employee participation under the joint decision system with the Special negotiation body (SNB”). The members of the SNB are elected equally from EU member states according to a ratio of personnel of affiliated companies in a multiple number of countries. This conference will continue for a basic length of six (6) months (one year at maximum) and a definite agreement must be reached regarding (i) scope of the agreement, (ii) number of employees and allocations thereof, (iii) procedures to provide information and conference procedures for employees, (iv) the frequency of employee organization meeting, (v) financial and physical support there to, and (vi) dispatching representative employees to the board of directors or the audit committee. Costs incurred from the mutual conference should be born by SE and the decision is effective by majority vote.

(a) Application of “standard rule”

If within a certain period of time an agreement cannot be reached between the labor?? and the employer, via the special negotiation body of the SE, regarding the “form and scope of employee participation for joint decision system” or both the employees and the employer have committed to the adaptation of the above Directive, the “standard rule” provided under the above Directive shall apply (assuming that the content of EU Directive must be adopted under domestic laws).

The “standard rule” is classified into “participation of employees to labor conference via employee representative organization” and “participation of employee representative to board of directors and auditing committee”. The standard rule of the former case is an obligation of (i) presenting a list of discussion themes at the board of directors’ meeting and the auditing committee, and (ii) regular reporting from the employer to the employee representative organization about the general shareholders’ meeting. This report should include corporate management policy and future trends, change of production volume, productivity and management policy, merger and discharge. Also, if there are any important issues, such as relocation or the liquidation of the company, information may be requested from the employee representative organization in the form of a special report. Consequently, a wide range of employees’ rights are protected under the SE legislation.

The standard rule of “participation of employee representative to board of directors and auditing committee” contains the ensured right to reserve the adoption of the rule to the domestic laws (which may not be adopted under the domestic laws), and restriction of compulsory application.

Specifically, in the case of a “reorganized company SE”, the participation rights of employees to the board of directors or the auditing committee should be continuously applied, and in case of “stock company merger SE”, the right of an employee representative to participate on the board of directors and the auditing committee should be continuously ensured if the number of employees is 25% or more of the total number of SE employees. In case of a “joint venture SE” and “holding company SE”, the ratio is 50%.

5. SE and taxation issue

SE aims for the reduction of administrative costs of legal procedures, promotion of reorganization within the EU and ultimately, the deeper economic integration of the EU by ensuring a continued and uniformed legal substance under prescribed conditions for cross-over group companies within EU. However, from a tax perspective, such intentions are totally disregarded under the EU company system which became effective on and after October 8, 2004, although the tax implications of the SE structure were partially provided under the draft proposal of SE rules. This means that although SE legislation has been provided, there is no favorable tax treatment with regard to the SE legislation. Consequently, the concept of an “SE with no favorable tax treatment” is derived from the concern that tax treatment focusing only the SE would provide a distorting tax system within the EU which would disturb the development of the EU market, so that there would be no tax treatment only focusing on SE’s in future.

Tax implications for SE’s should be considered from various perspectives; what kind of measures should be adopted during the process of “EU tax harmonization” and what kind of merit will be given to the SE. Direct guidance of the “EU tax harmonization” is a report by EU Committee entitled “For EU market with no tax barrier” issued in October 2001, whereby two-way approaches, i.e., an inclusive approach in the harmonization of a corporate tax base and an individual approach, such as the amendment of the EU Directive such as “Directive on merger taxation EU” and “Directive on dividend between parent and subsidiary”, establishment of joint forum of transfer pricing legislation, commencement of conference to provide uniformed use of carried forward tax loss, are adopted, based on the recognition that there are 15 different tax systems (countries) and 30% or more discrepancy in effective tax rates within EU. On December 7, 2004, an agreement was reached at the EU finance ministers’ board with regard to an amendment of the “EU Directive on merger taxation”. Although this “EU Directive on merger taxation” originally became effective in 1990, a draft proposal was announced in 2003 to clarify the application rule so that an agreement at EU level was anticipated along with the enforcement of SE. Although it will take some time until taxpayers may enjoy the merits, the relocation of an SE or in the case of a stock company merger

SE, transfer of assets may be conducted without incurring taxation on the deemed profit, provided that certain conditions are met.

In conclusion, the adoption of an SE is a matter of an issue of “tax harmonization within EU” that is a central issue in the deepening of the economical integration of the EU. Therefore, tax related issues for the SE structure should be considered from the perspective of “tax harmonization within EU”.

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