Trends in European Corporate Group Law Systems and the Future of Japan’s Corporate Law System*

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Abstract

Balancing the interests of the parent company (the corporate group as a whole) and those of its subsidiaries when managing a corporate group is a challenge in corporate law. To address this challenge, legislative proposals based on the understanding that protecting the interests of subsidiaries should be the top priority have been repeatedly presented in Japan and Europe. However, in Europe, rules that appear to place priority on the activities of parent companies and corporate groups as a whole have recently been presented due to the practice of conducting corporate activities on a group basis and the effects of globalisation.

This paper closely examines recent debates concerning this matter in Europe and identifies the factors that have brought changes in the basic thinking behind the debates. By doing so, the paper reviews existing views concerning corporate group law system in Japan (particularly in relation to the management of groups) and presents points of attention concerning how to proceed with future debates.

Keywords: corporate group law system, protection of minority shareholders of subsidiaries

I. Introduction

Balancing the interests of the parent company (the corporate group as a whole) and those of its subsidiaries when managing a corporate group is a challenge in corporate law. To address this challenge, legislative proposals based on the understanding that protecting the interests of subsidiaries should be the top priority have been repeatedly presented in Japan and Europe.¹

In Japan, the Working Group on the Corporate Law System of the Legislative Council of the Ministry of Justice (henceforward ‘CLS Working Group’), which was constituted in 2010, discussed almost all the issues related to corporate groups. However, it did not reach a consensus on the final proposal for reforming the Companies Act regarding the material provision for the protection of minority shareholders in subsidiaries in the management of a corporate group.²

Discussions about the protection of minority shareholders in subsidiaries in Japan have

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been strongly influenced by German law, especially the German Stock Corporation Act (*Aktiengesetz: AktG*), which was enacted in 1965. However, the debates on this issue in recent years in Germany are different from earlier debates because of the impact of harmonisation in the European Union. Further, a legislative proposition that aims to improve the efficiency of a corporate group as a whole was submitted by The Reflection Group on the Future of EU Company Law (henceforward ‘The Reflection Group’) to the European Commission in 2011.\(^3\) This proposal is under discussion in the Informal Company Law Expert Group of the European Commission.

This study reviews prior studies on corporate group law in Japan and aims to discuss this subject by identifying the elements that affect the basic objectives of the corporate group law system in Europe.

The rest of this paper proceeds as follows. First, the German corporate law for the protection of minority shareholders in subsidiaries, which had a strong impact on the European legislative action on corporate group law, will be briefly discussed (Section II). Subsequently, the French case law and its acceptance in the discussion of the European Union (EU) will be shown (III), and the Italian corporate group law will be introduced in Section IV. These European systems will be analysed in Section V. Finally, suggestions for future research on the Japanese legal system will be presented in Section VI.

In this article, a company that is in a controlling position in a corporate group is referred to as the ‘parent company’, and a company that is in a controlled position in a corporate group is referred to as the ‘subsidiary’.

II. The German Law System

The German law related to corporate groups is of interest to Japanese law scholars, and it is often included in discussions on legal interpretations and law-making.\(^4\)

One of the most important rules of the German legal system that the Japanese legal system uses as a reference point is related to *de facto* corporate groups, where a parent company exercises controlling power over its subsidiaries not by contractual arrangement but by the voting rights of the shares in the possession of the former.

The essence of this rule is that the parent company should not exercise controlling power in such a way that would involve any disadvantageous legal or factual acts against the subsidiaries unless the disadvantage is suitably compensated (paragraph 311 of German Stock Corporation Act [*AktG*]).

According to the most popular interpretation,\(^5\) this rule does not prohibit the parent company from initiating any disadvantageous measures against its subsidiaries; the parent com-

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\(^2\) The proposal related to the protection of minority shareholders in subsidiaries (See, The Counsellor’s office for Civil Affairs Bureau of the Ministry of Justice (2011), Part 2, Section 2, Subsection 1, Plan A) was extinguished in the final proposal (See, Legislative Council of the Ministry of Justice (2013), Part 2).


\(^4\) See Takahashi (2008), for example.

\(^5\) For example, see Schmidt (2002), p.960.
pany is permitted to do so provided there is adequate compensation. This seems very convenient for the parent company. However, this rule is meant to be implemented very strictly: every legal and factual act must be verified to determine whether it is disadvantageous.\(^6\)

Therefore, the German system is criticised for its inefficiency to manage corporate groups.\(^7\)

III. European Commission’s recent legislative move

In an effort to harmonise corporate regulations in the 1970s, the 9\(^{th}\) company law directive on corporate groups, which was modelled on the German system, was drafted. However, it was abandoned\(^8\) following the negative evaluation of the German system.

Subsequently, the dominant theory on corporate group discipline in the context of the EU was modelled on French case law.

III-1. The Rozenblum Doctrine

In France, there is a firmly established case law where the director of a subsidiary cannot be charged with the criminal offence of misusing his/her company’s assets \((\textit{abus de biens sociaux})\)\(^9\) for receiving financing from the parent company if the following four conditions are met: firstly, the group structure must be firmly established; secondly, a coherent policy for the entire group must be in place; thirdly, the advantages and disadvantages for each company must be properly distributed within the group so that balance is maintained\(^10\); finally, the financial assistance for the subsidiary must not exceed the capacity of the company that bears the financial burden. This case law is called the Rozenblum Doctrine (Rozenblum is the surname of the defendant in the most important case).\(^11\)

III-2. Forum Europaeum Konzernrecht

According to the report of the ‘Forum Europaeum Konzernrecht’ published in 1998,\(^12\) the Rozenblum Doctrine gained attention in the European discussions. In the report, in order to ‘legitimise in all Member States groups which are organised on a EU market-wide basis and thereby ensure that such groups as a whole and their subsidiaries (parent, subsidiary, sub-subsidiary) operate on a firm legal basis’,\(^13\) a civil rule is proposed: ‘If the management of a group subsidiary operates its commercial policy in the interests of the group and conse-

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\(^6\) Emmerich and Habersack (2013), §311 Rn.54.


\(^10\) This summary of the French case law is quoted from Forum Europaeum Corporate Group Law (2000), p.198.


sequently acts in a manner which is not in the commercial interests of its own subsidiary, it is not thereby in breach of its duty if: the group has a balanced and firmly established structure and the subsidiary is incorporated into a long-term and coherent group policy and the management may reasonably assume that the loss, damage or disadvantage (in particular, the loss of business opportunities) following from their actions will, within a reasonable period, be balanced by benefit, gain and advantage’.  


After the publication of this report, there was no further discussion about this subject for several years. Recently, it regained attention in Europe following the publication of the Reflection Group’s report in 2011.

The Reflection Group’s report proposed the introduction of a set of EU-wide rules. The concept of ‘interest of the group’ is recognised: the parent company can manage its subsidiaries in the ‘interest of the group’, and the director of subsidiaries can consider the ‘interest of the group’. However, details about the rules are not clear, especially regarding whether and under what conditions the director of a subsidiary with minority shareholders can pursue the interest of the group.

Notably, this report mentioned that ‘member States which have adopted the German approach but wish to have an opportunity to change to a more flexible approach might have the impetus for such a change’, and that ‘[b]y recognizing the “interest of the group”, the EU could therefore lead the German and German oriented system to move towards the alternative model, which is the one towards which, after decades of application, they seem to be moving in practice anyway’. This shows that the report intended to change the ‘notorious’ German-oriented system by recognising the interest of the group.

This proposal from the Reflection Group’s report was included in the Action Plan of the European Commission in 2012 in the form of a declaration that ‘the Commission will, in 2014, come with an initiative to improve both the information available on groups and recognition of the concept of “group interest”; this initiative is under development.

IV Recent legislative movement of the Member States: Italian law system as an example

Recently, some of the EU Member States expressed interest in making an individual national legislation of the corporate group law, although it would be subject to the influence of

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19 The “Informal Expert Group on Company Law” was organised to assist the Commission in the preparation of new initiatives in company law, especially to improve the mechanism of cross-border mergers and to develop initiatives for cross-border divisions and ‘groups of companies’.
the EU legislative action. The Italian Civil Code (codice civile), which deals with corporate matters, has provisions\textsuperscript{20} to deal with parent companies that acted in their own entrepreneurial interest or in the interest of others in violation of the principles of correct corporate management of the companies (subsidiaries) while carrying out direction and coordination activities for its subsidiaries; these parent companies are held to be directly responsible to the shareholders of the companies (subsidiaries) for which they carry out direction and coordination activities for the damage caused to the profitability and the value of the shareholding. Further, the parent company has had no liability ‘when no damage is caused in light of the total result of the direction and coordination activities or when the damage is eliminated also as a consequence of specific operation carried out to this purpose’\textsuperscript{21} since the Civil Code reform in 2003. The second half of this provision is said to be the manifestation of the case law rule before the Civil Code reform in 2003.\textsuperscript{22} Analogous to the case law rule,\textsuperscript{23} the advantage that sets off the liability of the parent company—the so-called compensative advantage (vantaggi compensativi) in Italy—is also understood under the Civil Code provision: it cannot be hypothetical, and the existence of such advantage must be proved by the person who will avert the liability.\textsuperscript{24} Whether the current Italian law, which is deemed to approve of the concept of ‘group interest’,\textsuperscript{25} is different from the general civil principle of the evaluation of damage or compensatio lucri cum damno remains a topic of debate.

V Analysis of the European discussion

V-1. Evaluation of the change in the basic concept of corporate group law

As was discussed earlier, in Europe, the corporate group regulation mainly involved the protection of the minority shareholder initially. However, in the 2000s, the emphasis of the legislation moved towards the discharge of the directors of subsidiaries who subject their own company to disadvantageous instructions from its parent company (and the discharge of the director of such parent companies). This change in trend indicates a transformation from a ‘protective law’ to an ‘enabling law’\textsuperscript{26}.

However, this transformation seems to be affected by some political elements of the EU sui generis.

One element relates to the raison d’être of the EU. There are two alternatives that the EU can follow in the legislative action in order to harmonise the laws of the Member States. One is the convergence on a rule that aims to protect the stakeholders (including minority shareholders) of subsidiaries rather than to promote business activities; i.e. the convergence

\textsuperscript{20} Paragraph 2497 Italian Civil Code
\textsuperscript{21} Using Piacentini (2014) as a reference for English translation.
\textsuperscript{22} Patti (2003), p. 253.
\textsuperscript{23} For example, Cass. 24. 8. 2004, n.16707, in Giur. it., 2005, 69.
\textsuperscript{24} Cariello (2006), p.333.
\textsuperscript{25} See, Enriques, Hertig and Kanda (2009), p.177.
\textsuperscript{26} Teichmann (2013).
on ‘protective law’. The other is the convergence on a rule that aims to promote business activities rather than to protect stakeholders; i.e. the convergence on an ‘enabling law’. It seems easy for the EU to take the second alternative for the ‘promotion of the cross-border activity of corporate group’ because the EU must comply with the principle that it can interfere with legislative action only when a problem cannot be solved by the relevant Member State on its own.

The other element is the preference of the EU leaders during the discussion. If the person in charge negatively evaluates the German system, it is likely that he/she seeks to fulfil his/her own (hidden) intention of changing the German system or the analogous system by using the EU’s legislative action as external pressure (from outside the relevant Member State).\(^{27}\)

That is, the theoretically prominent rule was not necessarily chosen in the recent legislative movement in the EU. This point is relevant for the discussion of Japan’s legal system.

\(V-2.\) The optimal balance between ‘protective law’ and ‘enabling law’

First, it is necessary to understand the European debate not as a dichotomy between ‘protective law’ and ‘enabling law’ but as a matter of degree, where an equilibrium of the interests of both the parent company and its subsidiary needs to be established. Thus, the corporate group law, which is an ‘enabling law’ by nature, has the characteristics of ‘protective law’ intrinsically.

One example of such coordination is the German compensatory system in the \textit{de facto} group. The German system works on a one-to-one basis, where each individual transaction is examined in terms of the arms-length rule. Such a one-to-one approach is meant to ensure that the notional advantage, such as that caused by mere affiliation with a group, should not be recognised as a reason for being awarded compensation for the disadvantage caused by the unified direction of the parent company.

In contrast, the Rozenblum Doctrine seems to have no interest in individual compensation as long as the management of a subsidiary operates its commercial policy in the interests of the group.

Theoretically, however, it is not necessary to examine whether or not each individual transaction is disadvantageous in order to avoid notional compensation caused by mere affiliation with a group.

For instance, a Nordic corporate law scholar pointed out the similarity of this concept to the general principle in the Nordic corporate law: if on balance the transactions among the group companies are fair and part of doing business, it should not matter that a particular transaction is contrary to the interest of a company when viewed in isolation, as long as there is a reasonable expectation that the company on average will be compensated by other transactions within the group.\(^{28}\) Another example is a case law in UK that rules out the lia-

bility of the directors of a subsidiary in the absence of an actual separate consideration as to 
whether an intelligent and honest person in the position of the company could have reason-
ably believed that the transactions were for the benefit of the company.29 Each of these ap-
proaches shows the possibility of a rule for regulating corporate groups by paying attention 
to the interests of the group as a whole while remaining as a rule that works on an individual 
company basis.

VI Suggestion for future discussions in Japan

VI-1. What is the main purpose of corporate group law?

Taking a hint from the European discussion, it is necessary to first clarify the main pur-
pose of corporate group law.

In Japan, the leading theories were usually discussed in terms of the ‘protective law’. It 
is interesting that the discussion in the CLS Working Group was based on the theory of ‘en-
abling law’ as well. However, the Interim Proposal of the Companies Act Reform planned 
by the CLS Working Group is so ambiguous that its norm could be understood not only as 
protective but also as enabling.30 For a clearly stated rule, it is crucial to first clarify the main 
purpose of the provision.

VI-2. Standard of the ‘should-be’ transaction

According to Prof. Kenjiro Egashira, who constructed the leading theory on this subject 
in Japan, it is a globally valid principle that the ‘fair’ transactions between the parent com-
pany and subsidiaries follow an ‘arms-length’ rule.31 Although his interpretation of the arms-
length rule is not clear, his proposal seems to be based on the belief that a subsidiary should 
be managed in the same way as an independent company.32 Since such a belief, anticipation, 
or request could affect the concept of ‘fairness’, the arms-length rule would be asserted to 
account for this fairness.

On the other hand, as shown by the recent European discussion, it is possible that the 
standard to determine whether or not the transaction is fair differs across jurisdictions. It 
seems that fairness in Germany means maintaining the individual equilibrium between each 
performance and counter-performance, while in France, it means equal commitment in a 
broad sense, as long as a firmly-established group structure and group policy exist.

This difference in the standard of ‘fairness’ across jurisdictions might be caused by the 
difference in the anticipation or request (primarily of minority shareholders) regarding what

30 Funatsu (2012).
32 See also Ito (2009), p.60.
kind of transaction should be made. Thus, in Japan as well, fairness depends on the social anticipation or requests at different times; therefore, the standard could be similar to the Rozenblum Doctrine.

For the interpretation of the current law, it is important to specify such anticipation or requests at the moment. However, the discussion in the CLS Working Group indicated that there is no consensus about this point.

If the existing rule must be specified despite this situation, it is better to use the general civil principle as a hint (for example, the rule governing estimation of damage or compensatio lucri cum damno) instead of using the fiction that the subsidiary would have been managed in the same way as an independent company.\(^\text{33}\)

On the other hand, if the ambiguous concept of ‘fairness’ is not favourable, a legislative action can be considered such that the anticipation or request could be clarified and fixed; further, whether it is favourable to set a single standard that follows the one-size-fits-all principle should be considered.

References


<http://www.moj.go.jp/content/000084699.pdf>
