
Comparative Corporate Law



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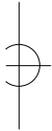
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Comparative Corporate Law

United States, European Union, China and Japan

Cases and Materials



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Preface

It is true enough that the world is becoming a smaller place. Business enterprises today contemplate venturing into places they would not have considered even thirty years ago. This venturing has been made infinitely easier since the mid 1990s with the advent of the Internet as a tool of commerce. Electronic commerce is revolutionizing the nature of retail as well as wholesale commerce. The legal and economic ramifications of this change in commercial practice will be worked out in this century. The pace of the harmonization of commercial practice has accelerated in response to these rapid changes. The recent work of the United Nations Commission on International Trade Law in creating a Model Law on Electronic Commerce is a case in point. *See, e.g.*, <<http://www.un.or.at/unicitral/english/texts/electcom/>>.

At the same time, the world is becoming a more consolidating place. Changes in commercial practice are inducing change in the organization and strategies of commercial enterprises. The most significant of these changes have resulted from the challenges faced by enterprises increasingly pulled from within the borders of their places of formation. Political transformation has mirrored changes in commercial practice. Groups of countries are increasingly uniting for diverse purposes. These political and trade groupings are meant to take advantage of the greater flexibility and power that unity brings. That has been the case in the area of trade in the United States has taken advantage of this flexibility through its participation in the North American Free Trade Association composed of the United States, Mexico and Canada, as well as in the World Trade Organization.

The tendency to consolidate has not been reserved to the arena of mutually advantageous foreign relations. Increasingly, nation-states have begun to surrender a portion of their sovereignty to effect more intimate unions with other nations. Sometimes the process has been extraordinarily successful—consider the union of the states which has become known as the United States of America. Sometimes they have been unsuccessful—consider the fates of the former Union of Soviet Socialist Republics, Yugoslavia and Czechoslovakia. Latin America has seen the emergence of a number of economic unions patterned, to some extent on the European Community. The largest of the South American regional trade associations, MERCOSUR, for example, unites Brazil, Argentina, Uruguay and Paraguay. It is still too early to gauge the success of these new economic combinations. However, the pattern emerging at the end of the twentieth century is clear enough: the nation-state has increasingly become a hindrance, rather than a help for expanding trade and economic development. Law and political organization is slowly shifting to recognize the economic realities of patterns of world wide commerce.

Europe is of particular interest in this regard. Since the end of the Second World War, the nations of Western Europe have been attempting to create of a new form of a union

of sorts—a community of nations producing a “Europe without borders” while retaining the separate national characters of the member states. This process started in the early 1950s when six nations, France, West Germany, Italy, Belgium, Luxembourg, and the Netherlands, created three distinct, but related, functional “communities”—the European Economic Community (“EEC” now the “EC”), the European Coal and Steel Community (“ECSC”) and the European Atomic Energy Community (EURATOM”). This union of six nations had grown to twelve by 1991: Portugal, Spain, The United Kingdom, France, Germany, Belgium, the Netherlands, Luxembourg, Denmark, Ireland, Greece, and Italy. In 1994 three additional Member States were admitted: Sweden, Austria and Finland (Norway chose not to join but to remain associated with the Communities). Today, the three Communities have expanded their scope and become the nucleus of a European Union (“EU”). The impetus within the EU is for even greater union among the Member States.

The aim of the EU is to create, as between its members, a unified geographic and political area characterized by free trade and free circulation of goods, services, capital and persons. To aid in this effort, the members of the Communities created a number of central governing institutions with supra-national authority to effect the necessary integration. The goal of creating a unified market has resulted in a significant effort to harmonize the laws of the EU’s Member States. The result, it is hoped, will be a union with the economic advantages of the US, but without the loss of the political authority which the states of the US have suffered since 1789.

In contrast to the coming together of the nations of the European continent stands Japan. Since the Second World War, Japan, like Europe, has risen to become among the most powerful of the industrialized nations of the world. However, Japan has not chosen to seek economic or political union with its neighbors. Yet Japan has managed to extend its markets worldwide to a remarkable degree. It has, perhaps deliberately, avoided creation of a political system mimicking that of the United States. Japan is an important source for the comparative study of systems of corporate governance because, unlike most other nations in the world, Japan has had to successfully absorb not one but two distinct systems of law into its own governance traditions, and all within the space of a century. The first was the absorption of European governance principles during the second half of the nineteenth century. The second was the absorption of American principles during the forced democratization of social, political and economic organizations during the military occupation of Japan after 1945. To that extent alone Japan provides fertile ground for studying the ability of a socially and culturally distinct community to absorb the norms of another, and the conditions under which such absorption is possible. The lessons are important for the emerging economies of Asia as well as the nations which emerged from under the influence of the Soviet Union after 1991.

Increasingly important to the United States, the European Union, and Japan is the People’s Republic of China (“PRC” or China). A political union with significant restive ethnic and political communities, the PRC has successfully reconstituted itself in the eyes of the outside world as a unified nation. The PRC is expected to dominate trade, if only because of its population and size. Yet the PRC remains unwilling to freely participate in the rush toward convergence. China has begun to transform itself from a backwater militaristic totalitarian dictatorship state organized as a blend of traditional Chinese norms and Eastern European Marxist-Socialist totalitarian practices into a control economy participating in the emerging worldwide market economy. It is accomplishing this transformation by aping, for benefit of the market, the forms of market organiza-

tion, while retaining, at the same time, its core normative organization as an anti-capitalist state. As such, China provides evidence of the power of the emerging world market to induce convergence in even the most hostile state. On the other hand, to the extent that China is able to devise a viable non-capitalist alternative to enterprise organization, it will provide an important point of divergence for a host of states which have yet to participate in this world-wide market. It will also exert a strong pull for convergence to proceed along the lines pioneered by China. The ability of the Chinese leadership to overcome the contradictions of the position it has staked out will make China among the most interesting places to observe in this new century. The PRC is thus an important subject of study for any person interested in issues in comparative enterprise governance.

But comparisons with the United States raise very real questions about the extent to which harmonization and uniformity is necessary to achieve the free circulation of people, goods, services and capital between nation-states. This is especially so in the area of the regulation of business enterprises, particularly enterprises operating in corporate form. For example, the EU has been working toward internal harmonization of its Company (Corporate) Law and its securities' markets, while the United States has achieved a fairly uniform internal market with a substantially decentralized regulation of corporations, but with a highly centralized regulation of its securities markets. Japan, on the other hand, has remained aloof from regimes for regional or supra-national integration. Japan, however, has made serious efforts to conform its practices to at least outward conformity with emerging global norms. The PRC, even more than Japan, offers an example of resistance to wholesale absorption of global norms which do not have a "Chinese face." Each, in its own very different way, avoids succumbing wholesale to the norms of cross border harmonization, except to the extent necessary to preserve their respective overseas markets and to participate in international markets for capital.

Moreover, consolidation and harmonization remain partial accomplishments. Political borders remain real and significant barriers for enterprises seeking to trade across borders. Enterprises organized as companies, like merchants in an earlier age, can still be stopped at a political border. And like those merchants, modern enterprise organizations can still be required to conform to the trading and organizational rules of the political community in which they seek to profit. Consequently, and especially with respect to larger market areas, it becomes important to understand the rules by which "insiders" can organize and "outsiders" can penetrate these borders.¹

The European and Japanese approaches to the organization and regulation of economic enterprises has become of increasing importance to the American business lawyer. As the harmonization of European Company Law becomes more of a reality, as the governing institutions of the EU become more important in the regulation of corporations, and as Americans become more involved in business activities in the EU, an understanding of the approaches of the European Communities to the regulation of its most significant form of business enterprise becomes important. The same, of course, applies to Japan. In both cases divergence and convergence of business practices as well as regulation will have a singular impact on American enterprises venturing abroad. Moreover, in the emerging world order, Japan becomes singularly important because of

1. A more concentrated study of these rules is usually reserved for the standard course in international business transactions, and will not be the focus of the materials in this book.

its proximity to China. As China emerges from its self-imposed economic isolation to join the world economic community, it is likely that the PRC will look to Japan for acceptable models of corporate governance. Moreover, the experience of the EU and Japan may provide valuable lessons for American businesses and legislatures as they grapple with the periodic calls for formal change in the regulatory structure of American business. For example, Japan may provide lessons for isolationists, but especially for those in the US who mean to resist the regularizing regimes of international, commercial and enterprise organizational norms. Europe provides a model of the benefits and travails of the sort of federalization of corporate law that has been advocated in the United States from time to time. *See, e.g., Cary, Federalism and Corporate Law, Reflections Upon Delaware*, 83 *YALE L.J.* 663 (1974).

The purpose of these materials is to introduce readers to the comparative analysis of American, European, Chinese and Japanese approaches to the regulation of business enterprises operating in corporate form. The goal is to provide the student with a basic understanding of the fundamental, and perhaps fundamentally different, approaches taken by governments in the US, the EU, China, and Japan to the regulation of the corporation. The focus will be on giving a basic flavor of difference to the beginning student in a number of significant areas of corporate governance. As such, the materials concentrate on the formal sources of law and thereafter highlight some ways in which the difference in approach is manifested in actual regulation. While an understanding of the approaches of the systems for the regulation of corporations of other nations might also be useful, the sole emphasis of these materials is on the laws and approaches of the nations comprising the US, the EU, Japan, and China.² The ultimate aim of this focus is to understand the ways in which systems adjust to the existence of other, and sometimes competitive systems of corporate governance, in an era of global trade. The power of harmonization, emulation, penetration, convergence, and separation is inseparably linked to the comparative study of governance systems. The perhaps problematic notion of technological determinism, that different systems reach similar results when confronted by the same problem, provides a sub-text of this study.

These materials are intended for a basic course in comparative corporate law. It also may be appropriate for use in courses taught overseas in short or semester long programs of study. These materials may be used either for a "lecture" course or as the basic readings of a seminar. Depending on the time available and the interest of the students and faculty, the course instructor can utilize all of the materials, or she may limit the scope of the course to a review of the materials which cover the United States and some, but not all of the other systems included in the materials. In past years, when teaching from these materials in Europe, I have concentrated on the US and the EU and limited the discussion of issues of Chinese and Japanese law. Conversely, the course can emphasize the comparative study of US and Asian systems, minimizing the considerations of issues of European law.

2. Other systems of corporate governance are also worthy of study. The governance systems of Latin America, the Indian subcontinent and Africa merit discussion in their own right. India and the States of Latin America evidence the effects of the colonial experience on systems of law, but in two different contexts. India, like Japan, grafted western, and in India's case English, systems of corporate governance onto a strong and vibrant indigenous culture. Latin America's experience was different. There, as in the United States, the indigenous population was marginalized, and Spanish, and then French systems of law, introduced wholesale. Considerations of space, the similar experiences of some of the nations covered, and the focus on primary systems of corporate governance in the emerging world economy militated against an in depth treatment of the systems of these states.

The course is best utilized by students who have taken a basic course in enterprise organization or are taking concurrently with it. However, there are enough materials provided so that even students who have not taken the basic course may profit from a study of these materials. The course materials are meant to provide a sound grounding for courses in international business transactions and international or cross border dispute resolution courses as well as provide a close study of materials usually treated lightly in Conflicts of Laws courses. The materials assume no familiarity with Japanese, Chinese, European national or EU law, but do assume some familiarity with basic US law. For classes in which students have already taken a basic enterprise organization law course, the materials can be explored at a deeper level.

The materials are divided into eleven chapters. Chapters One and Two introduce the basic concepts which will be useful throughout the rest of the study. Chapter One introduces the student to the basic parameters of comparative law, and particularly, comparative law focused on issues of corporate governance. The materials provided introduce students to the basic themes and tensions in comparative study, with a focus on issues of enterprise governance. Chapter Two provides a very basic introduction to the political regimes of the governments that constitute the objects of study. In particular, there is a substantial amount of introductory material on the organization of the European Union, and the political and social organization of Japan and the People's Republic of China. Because the assumption is that students know very little about the political or social organization of at least some for the countries or supra-national organizations studied, the materials cover much basic ground. To the extent that students are better grounded in this introductory material, teachers may choose to skip this material, referring back to it from time to time as needed, rather than teaching through it.

Chapter Three introduces the student to the regulatory context of enterprise organization. The first part of the chapter introduces the student to the patterns of formal organization of corporations in the U.S., some of the Member States of the EU, Japan and China. The second considers the way a state determines which pattern of enterprise regulation is best for them. Particular emphasis is placed on a consideration of legal, economic and sociological characterizations of the corporation as a form of enterprise organization, and raises issues about the efficient regulation of these enterprises based on these characterizations. Introduced here also are issues of legal personality and their effects on regulatory regimes. Thus, these Chapters cover both the formal characteristics of corporate form, what makes a corporation different from other forms of business organization, and the problems of corporate reification. The concentration on reification is used as the introduction to the comparative analysis of American, European and Japanese approaches to the regulation of the corporation.

Chapter Four draws on the discussions in prior chapters, particularly in the last parts of Chapter Three, to consider the way in which conceptions of legal personality affect the form and substance of corporate regulation. The first part of the Chapter considers external regulation, and in particular the availability of constitutional or fundamental rights for corporations. The second part of the Chapter turns to the effect of different conceptions of legal personality on internal regulation of corporations. Chapter Four provides the basis for much of the discussion in the rest of the materials. Moreover, this chapter provides materials which illuminate the sharp differences possible among the various systems reviewed. Most importantly, it shows the way in which different views of corporate personality *within* a system can have a significant effect on the way in which corporations are regulated.

Chapters Five and Six introduce students to issues peculiar to corporate governance within multi-level federal or supra-national systems. As such, these chapters concentrate on the regulatory systems of the U.S. and EU. Japan and the PRC, as integrated unitary systems, do not encounter the formal problems of regulation considered in these chapters. Both chapters, however, point to patterns of regulation which might form a basis for worldwide harmonization in the future. Chapter Five concentrates on an area of fundamental difference between the corporate law of the U.S. and EU—how most efficiently to harmonize the corporate law of an integrated political union. In the United States such harmonization has occurred from the bottom up, by way of the so-called incorporation or “internal affairs” doctrine. Under this doctrine, the laws of the state of incorporation of a corporation determine its validity and the extent of the rights and obligations of the participants in the corporate enterprise. Once determined to be valid in the state of incorporation, such an enterprise must be recognized as valid and permitted to operate as such in all other states in the U.S. In contrast, most European states have embraced the “siège social” doctrine, under which a corporation, to be validly established, must be registered in compliance with all of the company laws of the state in which its primary operations are located. The Chapters also introduce students to the means certain states, notably, California and New York, have sought, with limited success to import the concept of “siège social” into the American corporate jurisprudence, as well as the ways in which the European Court of Justice may be incorporating the English model of corporate organization into the constitutional law of the European Union.

Chapter Six continues the study of the problems of corporate governance in integrated federal unions by considering the potential for and effects of the federalization of corporate law in the U.S. and EU. The first part of the chapter considers arguments for the federalization of American corporate law. The latter part of the chapter is taken up with a consideration of the sources of Community Law affecting company law. Particular focus is directed to the characteristics and effects of EC directives and regulations to harmonize corporate law within the Member States.

Chapters Seven through Eleven provide four distinct and separable areas of comparative study of corporate governance. Chapter Seven introduces the student to issues of liability for the pre-incorporation obligations of the enterprise, and the liability of the corporation for ultra vires actions. The chapter considers the imposition of this liability under two circumstances—when the incorporators or promoters enter into agreement prior to the filing of the requisite documents which establish the existence, in law, of the corporation, and when people enter into contract or incur other obligations on behalf of an invalidly formed corporation. On the American side, the emphasis will be on general common law, with some consideration of the approach suggested under the Revised Model Business Corporation Act. On the European side, the chapter considers how the First and Second Council directives on company law harmonization treat these issues in the European Community. The nuance of Chinese and Japanese law round out the study.

Chapter Eight considers issues touching on state regulation of capital and capital requirements for companies. In the US, the emphasis will be on the approach taken by Delaware, a representative of the traditional approach to the maintenance of capital requirements. Consideration will also be given to the “modern” approach of the Revised Model Business Corporation Act, and the approach taken by California. Capital requirements form a far more important part of European and Japanese company law than they do in the US, and for reasons largely rejected as irrelevant in the US—the

protection of creditors and other strangers to the corporate enterprise. The chapter examines the attempts to harmonize capital maintenance requirements set forth in the Second Company Law Directive and the Japanese system of minimum capital requirements. China's distinctive approach is also considered.

Chapter Nine takes up a study of a core value of enterprise organization in corporate form—limited liability for investors. Much of the law in this area in the United States remains a matter of state law. The same can, to some extent, be said of the law in the Member States of the EU. Japanese law provides a nice example of the way in which reception of foreign law that is not culturally compatible can be reworked to achieve a harmonious result. The Chinese approach to limited liability, based on the appointment of a natural person to stand in the place of the corporate legal person, is unique and ties the study of this area more closely to earlier considerations of the effect of conceptions of legal personality on corporate governance. The Chapter highlights the different approaches to the application of the doctrines of disregard of corporate personality in cases of multi-corporate enterprises, that is, of enterprises operating through a series of related corporations.

Chapters Ten and Eleven take up another core area of corporate governance—the supervision and disciplining of a corporation's managers and dominant shareholders. Chapter Ten explores judicial and legislative approaches to the regulation of managers. It starts with a review of the American common law and statutory rules defining the nature of a manager's duties to the enterprise. It then contrasts these rules of fiduciary duty with the more formal, but also more narrowly tailored approaches in Europe. The European approach is contrasted with the Japanese hybrid of American and European approaches. Chinese construction of a system of monitoring managers will then be considered. The principal focus will be on what are known in the United States as the duties of care and loyalty.

Chapter Eleven considers the special case of shareholder duty to the enterprise. It considers the circumstances under which shareholder discretion with respect to her holdings are properly the subject of regulation or control by the state. The American fiduciary duty approach, adopted by some, but by no means all, of the states, is contrasted with the approaches of continental Europe and Japan. Particular attention is paid to the problems of shareholder regulation in states where the state has or had a dominant position in the economy. In this connection, the focus is on Russia as a transitional economy and the People's Republic of China as a nation still wed to the concept of state ownership of the means of production.

My hope is that the study of some or all of the issues raised in these materials will provide students with a broader perspective for understanding the benefits and limitations of American systems of governance, and an appreciation for differences in governance in other economically important parts of the world. I also hope that the study of these materials provide the basis for understanding the limited number of patterns existing or used for the regulation of enterprise organizations, and the ways in which these patterns manifest themselves in the context of different political systems.

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