MAYER·BROWN

The legal form of a **European Stock Corporation** is an interesting alternative for mid-sized partnerships and also for large corporations.

Formation of a European Stock Corporation

Organizational Possibilities and Advantages

A European Stock Corporation ("Societas Europaea", abbreviated "SE") is a type of corporation which can be established in any European Union member state pursuant to European Law. In June 2013 there were 1832 SEs throughout the EU, of which 252 were established in Germany. Many companies are currently considering their possible transformation into the legal form of an SE. The spectrum of companies that have either already transformed into an SE or are considering transforming varies from large, listed companies to mid-sized partnerships.

Friedrich Merz
Partner, Düsseldorf
T +49 211 86224 110
fmerz@mayerbrown.com

Dr. Ulrike Binder
Partner, Frankfurt
T +49 69 7941 1297
ubinder@mayerbrown.com

Dr. Hendrik Otto
Partner, Düsseldorf
T +49 211 86224 110
hotto@mayerbrown.com

Legal framework

As of October 2004, it is possible to establish and enter an SE into the commercial register of any member state of the European Union ("EU") and the European Economic Area ("EEA"). The establishment of an SE is governed by the Regulation regarding the Statute for the European Company ("SE Regulation"), valid in all EU and EEA member states as uniform and directly enforceable law. In addition to regulating the establishment of an SE, the SE Regulation also contains regulations regarding the minimum capital, internal constitution, shareholder meetings, accounting and liquidation of an SE as well as governing the transfer of an SE's registered office to another EU or EEA member state. However, it does not contain any concluding regulations. An SE is treated as a stock corporation of the respective member state in which the company has its registered office and is subject to:

- the SE Regulation,
- the SE's articles of association (which must be in accordance with the SE Regulation or national corporation law, as the case may be),
- as well as in regards to areas, which are not or only partially regulated in the SE Decree
  - the national legal provisions that have been specifically enacted for the regulation of SEs (for example, in Germany this is the Act to Establish the European Company (*Gesetz zur Einführung der Europäischen Gesellschaft*, SEEG) and
  - the legal provisions that are applicable to stock corporations in the member state in which the company has its seat (for example, in Germany such legal provisions would include the Stock Corporation Act (*Aktiengesetz*), the Law Regulating the Transformation of Companies (*Umwandlungsgesetz*) and the Commercial Code (*Handelsgesetzbuch*).

Employees' participation in SEs is regulated by an EU directive which was implemented in Germany by the Law regarding the Employees' Participation in a European Company (*Gesetz über die Beteiligung der Arbeitnehmer in einer Europäischen Gesellschaft*, SEBG).

SEs are established in accordance with the SE Regulation (irrespective of member state in which it has its registered office). However, their legal organizational form will differ depending on the national laws under which the SE is registered, just as is the case for stock corporations.

Advantages

Over the last few years SEs have gained in popularity, particularly in Germany. An SE offers advantages that other company forms do not, in particular:

- Corporate governance structures in SEs can be organized more flexibly and efficiently. An SE can choose between the two-tier system of governance (with a board of directors and a supervisory board) and the one-tier system of governance (with just an administrative board).

- SEs facilitate dealing with cross-border issues. For example, structures in internationally operating groups of companies can be organized uniformly and an SE's registered office can simply be relocated from one member state to another without the need for liquidation and formation of a new company.

- The employee involvement model is negotiated and agreed upon on the establishment of the SE. An increase in the number of employees does not lead to a corresponding increase in the number of employees serving on the supervisory board or executive board. Therefore, the employee involvement agreement can be "frozen" by the establishment of an SE.

- The establishment of an SE emphasizes the company's international orientation to the public and supports the construction of a European image and European market appearance.

The establishment of an SE

An SE can only be established in accordance with the forms of establishment (or *numerus clausus)* as set out in the SE Regulation. The SE Regulation provides four primary forms of establishing an SE:

- the merger of a national stock corporation with an SE,

- the transformation of a national stock corporation into an SE,

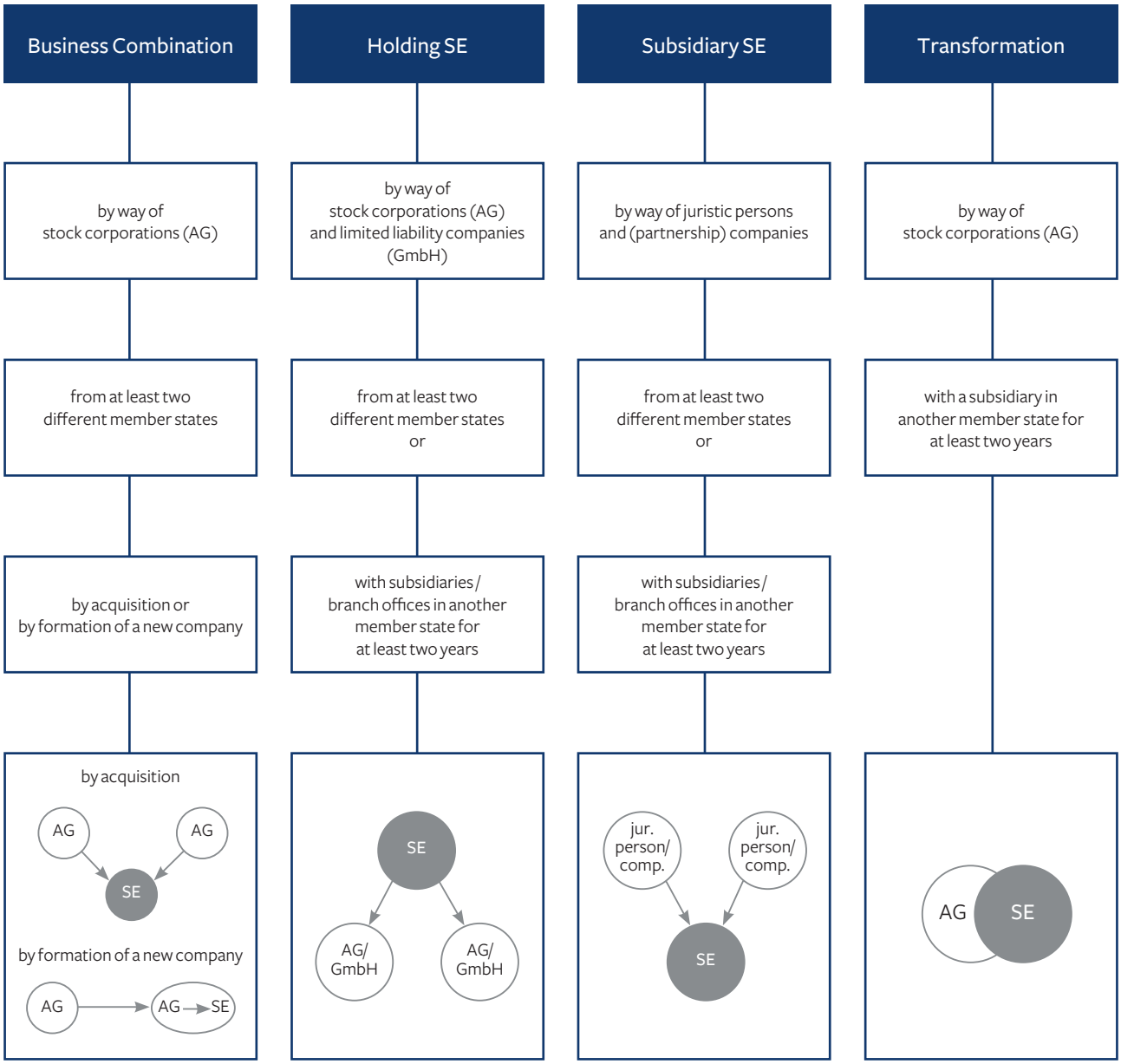
- the establishment of a joint holding SE, and

- the establishment of a joint subsidiary SE.

An existing SE can also establish a subsidiary SE.

The establishment of an SE inevitably raises cross-border issues. Only certain legal entities are permitted to establish the different forms of an SE, as set out in the SE Regulation. For instance, private persons can be the founders of an SE via their interest in the holding entity of the SE and participate in the establishment of an SE. However, it is not possible to establish an SE via a hive-off or spin-off in accordance with the Transformation Act (*Umwandlungsgesetz*). Therefore, certain preparatory measures may be necessary prior to the establishment of an SE. The use of shelf SEs, which are combined into an existing company or companies is becoming increasingly common.

The primary forms of establishment, as set out in the SE Regulation, are as follows:



Corporate Governance

The law governing SEs permits corporate governance models, which neither the German stock corporation nor the limited liability companies laws permit. The law governing SEs allows a choice between the two-tier management system (consisting of a board of directors and a supervisory board), and the one-tier management system (consisting of an administrative board which combines the functions of the board of directors and the supervisory board).

TWO-TIER MANAGEMENT SYSTEM

An SE can, like a German stock corporation, have a two-tier management system. The SE is managed by a board of directors which is supervised by a supervisory board. The supervisory board's size is not dependent upon the number of employees in the SE (as is the case for a German stock corporation). This makes it possible for companies with equal representation of employees and representatives of the employer on the supervisory board to reduce the supervisory board's size by changing the legal form of the entity into an SE and thereby increasing the efficiency with which decisions are made in the organization. Additionally, it is possible to include a provision in the SE's articles of association that the board of directors' chairperson has a veto right. In this case the board of directors' chairperson has a particularly strong position.

ONE-TIER MANAGEMENT SYSTEM

An SE with a one-tier management system has an administrative board which manages the company, determines and supervises the implementation of its guiding principles. If the SE has a share capital of EUR 3 million, the administrative board must consist of at least three people. Under certain circumstances a veto right can also be incorporated in the articles of association of the SE for the administrative board‘s chairperson.

The administrative board appoints one or more managing directors. Administrative board members can also be managing directors if the majority of the administrative board consists of non-managing directors. The managing directors manage and represent the company (both in court and out of court). They can be removed from office by the administrative board at any time, except to the extent that the articles of association provide otherwise. It should be noted that a legal representative of an SE dependent company cannot also be an administrative board member. However, the legal representative of a dependent company can be a managing director for the controlling SE.

The one-tier management system creates a concentration of power which is not possible to achieve with a stock corporation. This system is therefore particularly interesting to small and family-operated companies. The one-tier management system is also advantageous to companies with Anglo-American stockholders, as their stockholders are more familiar with the one-tier board governance system from their native legal system, rather than with the German stock corporation's two-tier management system. Finally, the one-tier management system makes it possible for groups of companies operational throughout Europe to implement subsidiaries with a uniform management system.

Labor law aspects of an SE

A company's employee involvement is established differently in an SE than is applicable in the German employee involvement laws. The SEBG provides that employees and employers must generally negotiate how the employees' involvement will be organized in the SE prior to its establishment. This statutory requirement includes negotiations regarding the implementation of instruments to secure the employees' rights to be informed and heard, as well as negotiations regarding the organization of the company's employee involvement in the SE's supervisory bodies.

Generally, there is a timeframe of six months, up to a maximum of one year, in which the employees and employer have to agree a solution on employee involvement. If within the statutory prescribed timeframe no agreement has been reached, the existing statutory minimum requirements for employee involvement will be effective. In relation to an SE, the employee involvement of the participating legal entity will then be applicable, which provides for the highest quota of employees in the company's supervisory or executive boards. If a stock corporation transforms into an SE, and the employee involvement negotiations are unsuccessful in the prescribed timeframe, the employee involvement statute which was in place in the transformed company shall remain in force, and any negotiations will be frozen permanently. Therefore, the negotiations, which are led on the employees' side by a special negotiating body established for this particular purpose, do not enable a unilateral "escape" from the German company employee involvement law. The employee involvement regulations in SEs are independent of the number of employees employed by the SE. Therefore, an increase in employee numbers does not lead to a higher employee quota in the SE's supervisory or executive board, i.e. employees' influence is not increased by an increase in employee numbers.

Tax aspects

No independent tax law was created for SEs, the tax laws generally applicable to corporations apply. However, the tax laws were slightly modified in relation to SEs in the SE Regulation's implementation in 2006. Furthermore, the implementation of the SE as a legal form was a catalyst for changes to the German transformation tax law, bringing German tax law more in line with the rest of Europe and making the transfer of a company's registered office easier.

Tax issues should be considered during the SE's planning phase and before its establishment. As noted previously, it is possible to establish an SE in more than one member state of the EU or EEA. The following should be considered when deciding on the appropriate member state registered office: the effective tax burden, the net of double tax treaties, existing group tax regimes, the regulation regarding the taxation of dividends, the tax deductibility for financing expenditures and possible substance requirements for cross-border activities. When choosing one of the forms of establishment of an SE, one should bear in mind the taxation effects of such form, for example, an imminent disclosure and taxation of secret reserves or demise of existing losses carried forward upon establishment of all participating legal entities and their shareholders.

The SE's ongoing taxation is no different to the taxation of other corporations, for example, a stock corporation (AG) or a limited liability company (GmbH). The "general" tax limits become particularly important regarding cross-border activity. As the SE and its shareholders, or, as the case may be, subsidiaries, are always domiciled in at least two EU member states, the applicability of different taxation systems can lead to a double taxation, as the tax authorities in different countries want to tax the SE on the same basis. If the SE is active within the EU predominantly via permanent establishments, the profit limitation between the parent company and permanent establishments and the assignation of the economic assets are of great relevance. Questions regarding transfer prices are the centre of attention for foreign subsidiaries.

The cross-border transfer of an SE's registered office from Germany to another member state in the EU or EEA only initiates a taxable disclosure of the secret reserves insofar as the economic assets are "detangled", i.e. access to German taxation is withdrawn and the assets do not remain in a domestic permanent establishment of the SE. It is advisable to pursue in-depth tax advice as well as to regularly co-ordinate with the tax authorities in advance of establishing an SE.

About Mayer Brown

Mayer Brown is a global legal services organization advising clients across the Americas, Asia and Europe. Our presence in the world's leading markets enables us to offer clients access to local market knowledge combined with global reach.

We are noted for our commitment to client service and our ability to assist clients with their most complex and demanding legal and business challenges worldwide. We serve many of the world's largest companies, including a significant proportion of the Fortune 100, FTSE 100, DAX and Hang Seng Index companies and more than half of the world's largest banks. We provide legal services in areas such as banking and finance; corporate and securities; litigation and dispute resolution; antitrust and competition; US Supreme Court and appellate matters; employment and benefits; environmental; financial services regulatory & enforcement; government and global trade; intellectual property; real estate; tax; restructuring, bankruptcy and insolvency; and wealth management.

OFFICE LOCATIONS

AMERICAS
- Charlotte
- Chicago
- Houston
- Los Angeles
- New York
- Palo Alto
- Washington DC

ASIA
- Bangkok
- Beijing
- Guangzhou
- Hanoi
- Ho Chi Minh City
- Hong Kong
- Shanghai
- Singapore

EUROPE
- Brussels
- Düsseldorf
- Frankfurt
- London
- Paris

TAUIL & CHEQUER ADVOGADOS
in association with Mayer Brown LLP
- São Paulo
- Rio de Janeiro

Please visit www.mayerbrown.com for comprehensive contact information for all Mayer Brown offices.

0613