Mutual Recognition of Companies as an Agency Problem

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> *'Can it be believed that the democracy which has overthrown the feudal system and vanquished kings will retreat before tradesmen and capitalists?'*[1]

1. Introduction

Much is made in popular and academic discourse of the sacrifices which EU membership requires of sovereignty and democracy. It is said that the EU system requires states to transfer decision-making from the national level to supranational institutions, thereby creating vertical distance between citizens and the locus of prescriptive power.[2] It is not surprising, therefore, that debates about the vertical distribution of power between citizens, the Member States, and the Union have led to the gradual, albeit incomplete, empowerment of a representative European Parliament. The European Parliament, the argument goes, reduces the distance between lawmakers and subjects of the law.[3]

In tandem with the democratisation of the institutions of the Union, however, the establishment and consolidation of an internal market which is founded in great part on mutual recognition creates a horizontal separation between law-maker and law-taker. In this context, the deepening democracy deficit has been quite readily justified in the literature, to the extent that it has been noted at all.[4] This chapter situates the question of democratic legitimacy at the heart of the discussion of legal pluralism in the European Union. It does so, in part, by theorising mutual recognition and the attendant redistribution of prescriptive sovereignty as agency problems between the Member States.

Taking corporate mobility as an illustrative example of mutual recognition as it operates in politically contentious aspects of internal market regulation, it is argued that mutual recognition renders states regulatory agents of one another. Corporate mobility in the EU has come to be understood as the ability of companies to self-select the law by which they are governed. It is, principally, *de jure* mobility, as opposed to the *de facto* ability of a company to access markets of different Member States as a consequence of freedom of establishment narrowly construed. This has the effect of enabling Member States to legislate extraterritorially insofar as companies, and by extension corporate stakeholders, with which they have no factual connection may be governed by their law. Hence a principal-agent relationship between the Member State of the chosen law, and the Member State which is

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[1] Alexis de Tocqueville, *Democracy in America* (Wordsworth Classics 1998) 8

[2] See P Craig, 'Integration, Democracy and Legitimacy' in P Craig and G de Búrca (eds) *The Evolution of EU Law* (2nd edn Oxford University Press 2011) 28-31, and the references therein.

[3] A Moravcsik, 'In Defence of the "Democratic Deficit": Reassessing Legitimacy in the European Union' (2002) 40(4) *JCMS: Journal of Common Market Studies* 603, 605-606

[4] See, for example, M Poiares Maduro, 'So close and yet so far: the paradoxes of mutual recognition' (2007) 14(5) *Journal of European Public Policy* 814, 815

required to recognise the law and the administrative acts resulting in the existence of the company, including the system of governance prescribed by the chosen law. Worryingly, there are few mechanisms to align the interests of principal and agent. Quite the contrary, in fact. In a market for laws, a regulatory agent may be motivated to seek to maximise self-utility by undercutting the principal with a view to rendering its legal product more attractive to consumers of that product.[5] The situation is exacerbated as a consequence of a lack of robust *ex post* and *ex ante* mechanisms which would enable the principal to limit the effects of the agent's behaviour.

In political terms, mutual recognition of companies raises two distinct questions concerning corporate decision-making. The first requires an inquiry into the nature of companies; the other related question concerns the distribution of power in the market as between European *demoi*. The question of the nature and purpose of companies is unresolved as a matter of EU law. Throughout the process of integration conflicting theoretical approaches to the corporate form have coexisted, but, latterly, pressures have been brought to bear on models which account for a broader spectrum of corporate stakeholders.[6] Consequently, decisional power is displaced from the democratic processes which are, usually, most relevant to the stakeholders who are most intimately connected thereto. This in turn raises several concerns about the legitimacy of liberalised decision-making, whether from a corporate policy or democratic perspective. It is argued in conclusion that, while agency theory provides the tools to diagnose governance problems, remedies to the systemic disconnect between the law and its subjects are to found in other, more traditional analytical frameworks of democracy in the EU integration process.

2. The nature of companies in EU law

The constitutionalisation of corporate law provides ample evidence in support of Miguel Maduro's observation that the European Union has built a constitutional body with little regard for its constitutional soul.[7] Harmonisation of substantive corporate law has been somewhat sporadic, and limited in scope;[8] positive regulation of the private international law of companies has been characterised more by its failures than the fulfilment of its transformative potential.[9] There is little, therefore, in the way of joined-up legislative intervention which would articulate a clear vision of the nature and function of companies for the purposes of EU law.[10] Instead, through constitutional norms enshrined in the TFEU, a

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[5] M Becht, C Mayer and H Wagner, 'Where do firms incorporate? Deregulation and the cost of entry' (2008) *Journal of Corporate Finance* 241, 252

[6] See for example K Balez and T Baldwin, 'The End of the Real Seat Theory (*Sitztheorie*): the European Court of Justice decision in *Ueberseering* of 5 November 2002 and its Impact on German and European Company Law' (2002) 3(12) *German Law Journal* <DOI: https://doi.org/10.1017/S2071832200015674> accessed 21 October 2019

[7] M Poiares Maduro, 'Europe and the constitution: what if this is as good as it gets?' in JHH Weiler and M Wind (eds) *European Constitutionalism Beyond the State* (Cambridge University Press 2003) 77

[8] See generally L Enriques, 'EC Company Law Directives and Regulations: How Trivial Are They?' (2006) *University of Pennsylvania Journal of International Economic Law* 1

[9] See G-J Vossestein, 'Transfer of the registered office: The European Commission's decision not to submit a proposal for a Directive' (2008) 4(1) *Utrecht Law Review* 53, 59-60

[10] See J Borg-Barthet, 'Company law in the Single European Market: Trends and Challenges' in JM Beneyto and J Maíllo (eds) *Fostering growth in Europe: Reinforcing the Internal Market* (CEU Ediciones 2014) 143

process of market-driven liberalisation has fundamentally changed the manner of decision-making concerning the governance of economic activity.[11] In view of the dialectic of judicial development of the law, this has occurred with very little in the way of sustained engagement with the policy questions which are central to the development of corporate law.[12]

This is not to say, however, that constitutional ideas about the nature of companies are altogether absent from the treaties themselves. Indeed, the Treaty of Rome was drafted with a view to enabling Member States to guard against the incursion of more permissive models of corporate law. France, in particular, insisted on the inclusion of what is now Article 50(2)(g) TFEU as a legal basis for harmonisation of corporate law in order to counter possible advantages which would otherwise accrue to the Netherlands' more permissive corporate law regime.[13] As is so often the case, however, legislative intentions were flanked by a market eager for liberalisation, and a sympathetic judiciary.[14]

The lack of sustained legislative engagement with corporate policy concerns is problematic, of course, because the nature of companies is far from settled in corporate legal theory,[15] or indeed in the practice of states.[16] At one end of the theoretical spectrum, companies are viewed primarily as creatures of contract; they are the product of a private agreement which is merely endorsed or facilitated by the state.[17] At the opposing end, companies are established by state law with a view to attaining public goods.[18] While the reality is usually somewhere between these extremes, the normative influence of divergent theories remains significant in states' regulatory behaviour.[19] These divergences are especially important in a

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[11] Becht, Mayer and Wagner, 'Where do firms incorporate? (n 5) 241

[12] A rare example of analysis of the diversity of corporate law is to be found in the Advocate General's Opinion in *Powell Duffryn*, a case concerning prorogation of jurisdiction. However, here too, the Advocate General was eager to dismiss the doctrinal controversy in company law in order to resolve the matter with reference to the aims of the Brussels Convention. See AG Tesauro in Case C-214/89 *Powell Duffryn plc v Petereit* ECLI:EU:C:1991:431

[13] S Grundmann, 'The Structure of European Company Law: From Crisis to Boom' (2004) 5(4) *European Business Organisation Law Review* 601, 605; CWA Timmermans, 'Company Law as Ius Commune?' (2002) Walter van Gerven Lecture, Leuven Centre for a Common Law of Europe <http://www.iuscommune.eu/html/pdf/wvg/wvg1.pdf> accessed 21 October 2019, 5

[14] See, for example, J Borg-Barthet, *The Governing Law of Companies in EU Law* (Hart 2012) 104-141

[15] J Paterson, 'The Company Law Review in the UK and the Question of Scope: Theoretical Concerns, Practical Constraints and Possible New Directions' in R Cobbaut and J Lenoble (eds), *Corporate Governance. An Institutional Approach* (Kluwer Law International 2003) 141; J Dine, *The Governance of Corporate Groups* (Cambridge University Press 2000) 1; A Belcher, 'The Boundaries of the Firm: The Theories of Coase, Knight and Weitzman' (1997) 17(1) *Legal Studies* 22

[16] See M Andenas and F Wooldridge, *European Comparative Company Law* (Cambridge University Press 2009) 417; A Winkler, 'Corporate Law or the Law of Business? Stakeholders and Corporate Governance at the End of History' (2004) 67 *Law and Contemporary Problems* 109, 123

[17] See, for example, Dine, *The Governance of Corporate Groups* (n 15) 22-39

[18] Ibid

[19] Ibid

legal order such as that of the European Union, which presupposes the co-existence of multiple legal systems in the same interlinked juridical space. The result, essentially, is that different policy choices co-exist notwithstanding the fact that some of those choices might be fundamentally opposed to the political consensus pertaining in the relevant territory.

Understanding the extent to which divergent policy choices can co-exist harmoniously necessitates engagement with the spectrum of policy implications of corporate legal theory. The development of corporate legal theory began with an enquiry into the reasons for the deployment of the corporate form in preference to reliance on market mechanisms.[20] It was not an exercise in the establishment of the broader goals which corporate law should set out to attain, but intended instead to identify economic explanations for what was.[21] Coase asked why, if it was assumed that the open market produced efficient outcomes, would an entrepreneur choose instead to bring factors of production within the firm, thereby foregoing the efficiencies of the price mechanism. His answer itself is hardly controversial; the firm does away with the cost of repeated negotiation, replacing this with long-term agreements.[22] Coase's focus on efficiencies which benefit the entrepreneur has, however, shaped much of the critical work in corporate law and theory, including transnational iterations of the disciplines.[23] Indeed, the position of the entrepreneur remained the central focus of economic analyses of the firm for some time following Coase's work. Alchian and Demsetz, however, moved discussion towards analysis of team production, and the need, as they saw it, for centralised oversight with benefits attached thereto by way of compensation for onerous management tasks.[24] This, in turn, enabled others to theorise the firm as a nexus of contracts; essentially, a repository for private agreements.[25] Crucially, the view was taken that those private agreements were designed to attain the private ends of shareholders, as opposed to broader public goods.[26] It follows, on these accounts, that it is for the shareholders to determine the content and governing law of the corporate contract.

The identification of team production as a central problem in economic analysis of firms enabled more progressive theorists to develop analyses which recognised the stake of different inputs in the firm, however. Rather than a nexus of contracts, Rajan and Zingales

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[20] RH Coase, 'The Nature of the Firm' (1937) *Economica* 386, 386
[21] Paterson, 'The Company Law Review in the UK and the Question of Scope' (n 15) 145
[22] Coase, 'The Nature of the Firm' (n 20) 386-405
[23] See S Lombardo, 'Conflict of Law Rules in Company Law after *Überseering*: An Economic and Comparative Analysis of the Allocation of Policy Competence in the European Union' (2003) 4(2) *European Business Organization Law Review* 301, 314-322; MJ Whincop, 'Conflicts in the Cathedral: Towards a Theory of Property Rights in Private International Law' (2000) 50(1) *University of Toronto Law Journal* 41, 52-54; EM Iacobucci, 'Toward a Signaling Explanation of the Private Choice of Corporate Law' (2004) 6(2) *American Law and Economics Review* 319, 319-320; FJ Garcimartín Alférez, 'Cross-Border Listed Companies' (2007) 328 *Recueil des Cours de l'Académie de Droit International* 13, 47
[24] AA Alchian and H Demsetz, 'Production, Information Costs and Economic Organization' (1972) 62(5) *American Economic Review* 777, 779-781
[25] MC Jensen and WH Meckling, 'Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure' (1976) 3(4) *Journal of Financial Economics* 305, 310
[26] Ibid

characterised the firm as a nexus of specific investments.[27] Essentially, it is not only those who invest capital who make an investment in the firm. Indeed, whereas capital is fungible and readily capable of being transferred, investors of skills often incur a greater opportunity costs in that theirs may be a firm-specific investment which is not readily transferrable elsewhere.[28] Here too, however, there is no agreement as to the governance consequences of recognition of stakeholder interests. Some theorists simply acknowledge the existence of multiple interests, but reason that shareholder-appointed directors remain best placed to achieve positive outcomes for the company and, by extension, its stakeholders; other stakeholders are able to secure their stake in a firm through means other than corporate governance.[29] Others advocate a sort of benevolent shareholder dictatorship in the form of the imposition of stakeholder-regarding obligations on directors who remain appointed by and (primarily) for shareholders,[30] a position not unlike that adopted in the UK's Companies Act 2006.[31] Others still argue that all contributors to the firm should have a role in its governance, favouring an approach which focuses on just processes as much as outcomes, and the importance of just *ex ante* processes to secure just outcomes.[32] On the latter view, choice of corporate law would fall to be constrained by territorial connections to stakeholders, as opposed to being a private matter to be determined freely by the shareholders.

As noted above, these theoretical differences of opinion are not merely abstract ideas about the organisation of companies. They reflect the vast swathe of approaches to company law and corporate mobility in state practice. Indeed, the differences in states' views of the nature and purpose of companies represented an insuperable barrier to the articulation of an EU-wide construct of companies, and the mechanisms which would govern their transnational mobility, as is elucidated further in the next part of this chapter.

2.1 Corporate Law and Mobility in the EU

Notwithstanding the significant distance between Member States' overarching corporate philosophies, EU law has evolved in a manner which facilitates the application of one state's policy choices within the territory of another. The principle of mutual recognition, first applied to companies in *Centros*, requires Member States to recognise the existence of a company established under the laws of another Member State notwithstanding the fact that it might be more closely connected to another legal system.[33] Essentially, the law takes a

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[27] RG Rajan and L Zingales, 'Power in a Theory of the Firm' (1998) 113(2) *Quarterly Journal of Economics* 387, 388

[28] RE Freeman, 'A Stakeholder Theory of the Modern Corporation' in TL Beauchamp and Norman E Bowie (eds) *Ethical Theory and Business* (5th edn, Prentice Hall 1997) 67; E Fama, 'Agency problems and the theory of the firm' (1980) 88(2) *Journal of Political Economy* 288, 290

[29] OE Williamson, *The Economic Institutions of Capitalism* (Free Press 1985) 313-314; H Hansmann and R Kraakman, 'The End of History for Corporate Law' (2001) 89 *Georgetown Law Journal* 439, 450-451

[30] Freeman, 'A Stakeholder Theory of the Modern Corporation' (n 28) 67

[31] Companies Act 2006, s.172

[32] M Blair, 'Firm-Specific Human Capital and Theories of the Firm' in M Blair and MJ Roe (eds) *Employees and Corporate Governance* (Brookings Institute 1999) 70; AF Alkhafaji, *A Stakeholder Approach to Corporate Governance* (Quorum Books 1989) 111; NE Bowie, *Business Ethics: A Kantian Perspective* (Blackwell 1999) 112-113

[33] Case C-212/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* ECLI:EU:C:1999:126

contractual view of the corporation, reflecting the narrower theoretical constructs of the limits of corporate governance.

This was not always so. The different approaches to the substance of corporate law are reflected in divergence as regards the openness of the national choice of corporate law rules.[34] States which viewed companies primarily as vehicles for private enterprise tended to adopt a contractual approach to choice of corporate law; if national corporate law was a vehicle for the furtherance of private agreements, there should be no reason to prevent the extension of private ordering beyond the confines of one legal system.[35] This approach, known as the incorporation theory, was adopted in states such as the United Kingdom, and (principally) other common law jurisdictions.[36] In contrast, most continental Member States, which generally had a more stakeholder-oriented view of corporate law intended to prevent concentrations of power, preferred recognition theories which constrained the ability to choose, and thereby to import, a foreign company law model.[37] Hence the application of the real seat theory in the majority of the Member States. The real seat theory requires companies to be established under the law of the state in which they 'live', which is to say the place in which their operational headquarters are situated.[38]

The differences between choice of law rules were left undisturbed by EU law for the better part of the twentieth century. This is not to say that efforts to harmonise choice of law were altogether absent. The founding Member States concluded a Convention on the Mutual Recognition of Companies and Bodies Corporate in 1968, but this failed to achieve ratification in the Netherlands and so never came into force.[39] The Convention would have created a presumption of mutual recognition which would have, on the face it, appeared to move EU law towards a system which embraced contractual freedom of shareholders in corporate law.[40] Nevertheless, the Convention included so much room for states to apply protective exceptions that it may have simply entrenched the status quo, which is to say the

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[34] Dine, *The Governance of Corporate Groups* (n 15) 67; WF Ebke 'The "Real Seat" Doctrine in the Conflict of Laws' (2002) 36 *The International Lawyer* 1015, 1027-1029.
[35] Lombardo, 'Conflict of Law Rules in Company Law after *Überseering* (n 23) 314-322; Whincop, 'Conflicts in the Cathedral' (n 23) 52-54; Iacobucci, 'Toward a Signaling Explanation of the Private Choice of Corporate Law' (n 23) 319-320; Garcimartín Alférez, 'Cross-Border Listed Companies' (n 23) 47
[36] E Rabel, *The Conflict of Laws: A Comparative Study. Volume 2* (2nd edn, University of Michigan Press 1960) 31-46
[37] Ibid
[38] Ibid; see also B Angelette, 'The Revolution that Never Came and the Revolution Coming – *De Lasteyrie du Salliant, Marks & Spencer, Sevic Systems* and the Changing Corporate Law in Europe' (2006) *Virginia Law Review* 1189, 1193-1194
[39] EC Convention on the Mutual Recognition of Companies and Bodies Corporate of 29 February 1968, Bulletin of the European Communities, Supplement 2/69, 7-18 (hereafter 'EC Convention 1968'). For academic commentary, see RR Drury, 'The Regulation and Recognition of Foreign Corporations: Responses to the Delaware Syndrome' (1998) 57(1) *Cambridge Law Journal* 165, 181-182. T Ballarino, 'Sulla mobilità delle società nella Comunità Europea. Da *Daily Mail* a *Überseering*: norme imperative, norme di conflitto e libertà comunitarie' (2003) 48(4) *Rivista delle società* 669, 670; E Stein, 'Conflict-of-Laws Rules by Treaty: Recognition of Companies in a Regional Market' (1970) 68(7) *Michigan Law Review* 1327, 1337; A Santa Maria, *European Economic Law* (Kluwer 2009) 10
[40] EC Convention 1968, Art 1

preponderance of the real seat approach.[41] The Netherlands, which had recently adopted the incorporation theory, took the view that the entrenchment of the real seat theory was incompatible with its corporate law outlook.[42] Essentially, therefore, the experience of the drafting and (lack of) ratification of the 1968 Convention merely served to emphasise the salience of national corporate legal philosophies, and the marked differences as between those philosophies.[43]

In view of the rejection of mutual recognition as an instrument for market integration, the furtherance of the internal market was to rely entirely on other methods which would facilitate the cross-border activities of companies. Article 50(2)(g)TFEU provided the legal basis to achieve this. The purpose of the legislation adopted under the authority of Article 50 is twofold. In the first place, harmonisation provides the means to render the legal persons established under the laws of the Member States more understandable to potential contracting parties in other states.[44] By way of example, the harmonisation of publicity requirements and accounting standards enables providers of credit to evaluate the credit-worthiness of counterparties regardless of the legal system under which they are established.[45] Secondary legislation therefore acts as an instrument for the integration of markets.[46]

More broadly, however, harmonisation could serve as an instrument of corporate policy. In this respect, Article 50 TFEU reflects a policy decision to establish a level playing field by developing common standards through legislative intervention, as opposed to a system which transferred decision-making to the whims of dominant market actors.[47] Indeed, Article 50 TFEU recognises the interests of stakeholders other than shareholders as possible beneficiaries of the harmonisation of corporate law. The harmonisation of core corporate law policy has, however, been far more modest than the promise of the Treaty might suggest. Indeed, the failure of the Fifth and Tenth Company Law Directive, which would have harmonised corporate governance with reference to the German stakeholder-oriented model, further emphasises the fact of significant distance between the Member States' views of the

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[41] Ibid, Art 3

[42] Drury, 'The Regulation and Recognition of Foreign Corporations' (n 39) 181-182; Ballarino, 'Sulla mobilità delle società nella Comunità Europea' (n 39) 670; Stein, 'Conflict-of-Laws Rules by Treaty' (n 39) 1337

[43] M Goldman, 'La nationalité des sociétés dans la Communauté économique européenne' (1969) *Travaux du Comité français de droit internationale privé* 215, 219-226; Stein, 'Conflict-of-Laws Rules by Treaty' (n 39) 1329-1331; see also C Timmermans, 'Impact of EU Law on International Company Law' (2010) 18(3) *European Review of Private Law* 549, 554

[44] B Pasa and G Antonio Benacchio *The Harmonization of Civil and Commercial Law in Europe* (Central European University Press 2005) 264-272; J Wouters, 'European Company Law: Quo Vadis?' (2000) 37(2) *Common Market Law Review* 257, 289-290

[45] See Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law (codification), ch II-III

[46] Pasa and Antonio Benacchio *The Harmonization of Civil and Commercial Law in Europe* (n 44) 264-272; Wouters, 'European Company Law: Quo Vadis? (n 44) 289-290

[47] Goldman, 'La nationalité des sociétés dans la Communauté économique européenne' (n 43) 554. See, for example, Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement

manner in which, and the extent to which, the corporate form is to regulate the competing interests of corporate stakeholders.[48]

2.2 Negative Harmonisation

The failure of the legislative process to resolve choice of law problems, or to articulate a pan-European corporate law policy, provided room for the development of a familiar story in European integration. As was the case in respect of other fundamental freedoms, market actors took note of the promise of the economic freedoms established in the treaties, and sought to rely on their direct effect to further economic liberties. In other words, the development of corporate policy was dislodged from slow-moving political processes, and placed instead in a judicial sphere which proved to be less sensitive to divergence in corporate policy.

Initially, the Court was reluctant to intervene where the legislator had failed to express a view. In *Daily Mail*, the Court found that the private international law rules applicable to companies were to be addressed in future legislation.[49] In the absence of positive harmonisation, it was for the Member States to determine the rules which would apply to companies established under their laws. This demonstrated an admirable, and somewhat uncharacteristic, degree of judicial restraint. The Court, it seems, was acutely aware of the policy implications of the matters upon which it had been asked to adjudicate, and was equally conscious of the Member States' failure to achieve consensus on the underlying policy concerns.[50]

Judicial restraint abated, however, with the *Centros* line of judgments in which the CJEU decided that the establishment of a company under the laws of one Member State was to be recognised throughout the Union.[51] It did not matter, in the Court's view, that the establishment of a company under the laws of the United Kingdom in this case, was specifically designed to avoid the capitalisation obligations which would arise from incorporation in Denmark, where the company was to operate.[52] In keeping with AG La Pergola's Opinion, the Court effectively developed an EU choice of law rule which confers decision-making powers in companies on shareholders. La Pergola took the view that the purpose of freedom of establishment 'is to guarantee to all Community citizens alike the

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[48] See Pasa and Antonio Benacchio *The Harmonization of Civil and Commercial Law in Europe* (n 44) 364-368

[49] Case C-81/87 *The Queen v H. M. Treasury and Commissioners of Inland Revenue, ex parte Daily Mail and General Trust plc* ECLI:EU:C:1988:456. For academic commentary, see Drury, 'The Regulation and Recognition of Foreign Corporations' (n 39) 181-182; Ballarino, 'Sulla mobilità delle società nella Comunità Europea' (n 39) 670; Stein, 'Conflict-of-Laws Rules by Treaty' (n 39) 1337; Santa Maria (n 39) 10

[50] Santa Maria, *European Economic Law* (n 39) 11; S Rammeloo, *Corporations in Private International Law: A European Perspective* (Oxford University Press 2001) 36-37; Stein, 'Conflict-of-Laws Rules by Treaty' (n 39) 1330; T Ballarino, 'From *Centros* to *Überseering*: EC Right of Establishment and the Conflict of Laws' (2002) *Yearbook of Private International Law* 203, 208

[51] Case C-212/97 *Centros Ltd* (n 33); Case C-208/00 *Überseering BV v Nordic Construction Company Baumanagement GmbH* (NCC) ECLI:EU:C:2002:632; Case C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd* ECLI:EU:C:2003:512

[52] Case C-212/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* (n 33)

freedom to engage in business activities through the instruments provided by national law.'[53] This is a somewhat surprising reading. The history of the provisions of the TFEU concerning freedom of establishment suggests precisely the opposite interpretation is true. Far from being a system designed to confer free choice of corporate law to promoters of companies, the Treaty of Rome conferred powers on the Community to adopt legislation to safeguard the interests of a broad array of stakeholders, while reserving the question of choice of law itself to future legislation.[54] To the extent that the Treaty reveals any corporate law philosophy it suggests a rejection of a model which is driven by the choices of shareholders;[55] there was no suggestion that promoters of companies were to be empowered to apply the corporate policy choices of one Member State in the territory of another.

Nevertheless, *Centros* opened the floodgates insofar as the liberalisation of choice of law was concerned. Mutual recognition of companies was followed by the ability of companies to change their governing law, whether through a cross-border merger,[56] or in a single step by way of a cross-border transfer.[57] Not only were promoters of companies free to choose the corporate law which would apply to the entity, therefore, but dominant decision-makers could change that choice from time to time.

The judgments of the CJEU are, of course, articulated in the usual terms deployed in internal market law. The focus is primarily on questions of discrimination and access to markets, notions which are familiar across the spectrum of fundamental freedoms.[58] Beneath the rather mundane surface, however, is a vibrant encounter between different views concerning authority in the European economic constitution. The legal decisions entrusted to the Court carried with them policy outcomes which could be momentous for the organisation of economic production. The net result of the decisions is the liberation of corporate decision-makers from the confines of corporate policy choices of the state in which they are headquartered.[59] The corollary of this, however, is that stakeholders who do not exercise

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[53] AG La Pergola in Case C-212/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* ECLI:EU:C:1998:380 para 20. See also TH Tröger, 'Choice of Jurisdiction in European Corporate Law - Perspectives of European Corporate Governance' (2005) 6(1) *European Business Organization Law Review* 3, 57

[54] Timmermans, 'Impact of EU Law on International Company Law' (n 43) 554

[55] Borg-Barthet, *The Governing Law of Companies in EU Law* (n 14) 74-85

[56] Case C-411/03 *SEVIC Systems AG* ECLI:EU:C:2005:762. See MM Siems, '*SEVIC:* Beyond Cross-Border Mergers' (2007) 8(2) *European Business Organization Law Review* 307, 312-313; MM Siems, 'The European Directive on Cross-Border Mergers: An International Model?' (2005) 11 *Columbia Journal of European Law* 167, 179-181; LL Hansen, 'Merger, Moving and Division Across National Borders: When Case Law Breaks through Barriers and Overtakes Directives' (2007) 18(1) *European Business Law Review* 181, 196-198; FM Mucciarelli, 'Company 'Emigration' and EC Freedom of Establishment: *Daily Mail* Revisited' (2008) 9(2) *European Business Organization Law Review* 267, 276-277

[57] Case C-378/10 *VALE Épitési kft* ECLI:EU:C:2012:440; Case C-106/16 *Polbud - Wykonawstwo sp. z o.o.* ECLI:EU:C:2017:804. See Gitte Soegaard, 'Cross-Border Transfer and Change of Lex Soceitatis After Polbud, C-106/16: Old Companies Do Not Die…They Simply Fade Away to Another Country' (2018) *European Company Law* 21, 21-24

[58] See, for example, Case C-411/03 *SEVIC Systems AG* (n 56) paras 22-23

[59] A Looijestijn-Clearie, 'Centros Ltd – A Complete U-Turn in the Right of Establishment for Companies?' (2000) 49(3) *International and Comparative Law Quarterly* 621, 621-642

control over a company by way of corporate law – in some cases, as a consequence of the choice of law – may also lose the ability to exercise extraneous policy influence by way of the political processes of the state in which the company 'lives'. This creates two closely associated problems, one of horizontal transfers of sovereignty resulting in an unchecked agency problem between states, and one of democratic legitimacy. These are addressed in turn in the following parts of this chapter.

3. Theorising mutual recognition as an agency problem

At its most basic level, mutual recognition operates as a private international law rule which resolves questions concerning which legal system's substantive law should apply to a given case. Essentially, the rule requires states to recognise as lawful that which is lawful in another legal order; states commit to uphold one another's laws within their territories. Ordinarily, the effect of mutual recognition is merely to apply somewhat different technical solutions to the same problem. By way of example, the core principles of the laws of contract are not, generally, especially different from one state to another notwithstanding their diverse origins and evolutionary systems.[60] They are united by overarching principles such as the privity of contract and the principle of *pacta sunt servanda*.[61] The extension of private ordering to the transnational sphere is, therefore, not especially controversial.[62] Crucially, however, it is possible that relevant policy decisions reflected in the substantive law of the recognising state might not accord fully with those taken in the legal system which is given extraterritorial effect by way of the mutual recognition rule. This is especially accentuated in situations, such as the mutual recognition of companies, in which states may have fundamentally different views concerning the nature of the relevant rights and obligations, and the purpose of the relevant body of law.[63]

More broadly, mutual recognition is to be understood firstly with reference to party autonomy. This, in principle, serves the purpose of upholding the dignity of individuals as reflected in their ability to order their own affairs.[64] Furthermore, it is argued that private ordering produces efficient outcomes for the parties since contracting parties will invariably prefer a legal order which reduces transaction costs.[65]

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[60] M Sarfatti, *Le obbligazioni nel diritto inglese in rapport al diritto italiano* (Casa Editrice Francesco Vallardi 1924) 66

[61] See, for example, B Nicholas *The French Law of Contract* (Oxford University Press 1992) 4

[62] M Reimann, 'Savigny's Triumph? Choice of Law in Contracts Cases at the Close of the Twentieth Century' (2008) 39 *Virginia Journal of International Law* 571, 575-578; G Rühl, 'Party Autonomy in the Private International Law of Contracts: Transatlantic Convergence and Economic Efficiency' in G Eckart, M Ralf, G Rühl and J Von Hein (eds), *Conflict of Laws in Globalized World* (Cambridge University Press 2007) 155-158; P Nygh, *Autonomy in International Contracts* (Oxford University Press 1999) 13

[63] Dine, *The Governance of Corporate Groups* (n 15) 67; Drury, 'The Regulation and Recognition of Foreign Corporations' (n 39) 182-183; Ebke 'The "Real Seat" Doctrine in the Conflict of Laws' (n 34) 1027-1029

[64] PS Atiyah, *The Rise and Fall of Freedom of Contract* (Clarendon 1979) 292-321; Nygh, *Autonomy in International Contracts* (n 62) 7-8

[65] Hansmann and R Kraakman, 'The End of History for Corporate Law' (n 29) 446

The application of these principles in the context of company law is, however, fraught with difficulty. As noted in Part 2 above, the crucial disagreements in corporate legal theory and state practice concern the characterisation and delimitation of the firm. Whereas some view the company as an expression of the will of shareholders, and therefore enable shareholders to determine the personal scope of the corporate contract, others are of the view that a broader spectrum of stakeholders is to be included in the core of corporate law.[66] In a multi-jurisdictional context, this means that a choice of law would be viewed as an expression of the will of all relevant parties in some legal systems, whereas others would take the view that parties to the social contract constituting the company have been excluded from crucial decisions concerning the legal contract.[67] In this latter construct, far from constituting an expression of the autonomy and dignity of the parties, certain parties are excluded altogether and subjugated to the will of dominant actors. Furthermore, as elaborated hereunder, the parties who are excluded from the choice of law process are denied the ability to influence the content of the relevant law by way of participation in democratic life; the relevant democratic decisions occur in a jurisdiction over which they have no clear means of exerting influence.

The democratic disconnect created by formal cross-border mobility of companies could equally be expressed as an interstate concern. When viewed from the perspective of private international law as an interstate system, mutual recognition is often characterised as an expression of comity.[68] Sovereign equals recognise one another's acts and give effect to those acts as a consequence of a presumption of equivalence. The principle has evolved, however, transcending traditional iterations to now occupy a central role in EU governance as a constitutional principle underpinning economic liberties.[69] It enables economic actors to choose the polity or polities by which certain of their activities are governed. Democratic choice is allocated to market forces, as opposed to harmonisation, where supranational deliberative processes determine political outcomes.[70]

Democratic concerns arising from mutual recognition are especially accentuated in corporate law as a consequence of the fact of privileged access to decision-making processes for some stakeholders. There is no question of the legitimacy of the subjection to the chosen law of those who made the choice, of course.[71] Equally, it is plainly legitimate that members of the relevant democratic system and residents in the relevant territory should be subject to the law of the land. The application of the law to other stakeholders, however, benefits from no obvious source of legitimacy based on consent or other connections. While it is arguable that voluntary interactions such as, for example, through employment contracts or the extension of credit, could signal consent to be bound by the law applicable to a company,[72] this would represent a somewhat generous account of the power dynamics of employment and other

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[66] Dine, *The Governance of Corporate Groups* (n 15) 1-36
[67] See S Deakin 'Legal Diversity and Regulatory Competition: Which Model for Europe?' (2006) 12(4) *European Law Journal* 440, 441
[68] See R Drury, 'The "Delaware Syndrome": European Fears and Reactions' (2005) 6 *Journal of Business Law* 709, 709
[69] Poiares Maduro, 'So close and yet so far: the paradoxes of mutual recognition' (n 4) 815
[70] Ibid, 815-816
[71] See, by analogy, Case C-214/89 *Powell Duffryn plc v Petereit* (n 12)
[72] See, for example, Coase, 'The Nature of the Firm' (n 20) 390-391 in which the author analyses the rewards of voluntary subjugation to authority in employment relationships.

markets in which incentives and bargaining power are not distributed equally among the parties.[73] Moreover, it would be to superimpose a model of corporate law which includes a broader array of stakeholders on one which does not; it would not survive the scrutiny of the system the choice of which it sought to legitimate.

4.1 3.1 Theoretical Characterisation

Nicolaïdis characterises the recognition by a state of the laws of another state as a 'horizontal transfer of sovereignty'.[74] The term 'horizontal transfer' is deployed in recognition of the fact that the EU legal system is not merely made of up vertical transfers of prescriptive authority from sovereign states to shared supranational institutions, as in the classical account of European integration.[75] This is especially noteworthy in that mutual recognition might otherwise be viewed merely as a tool for the fulfilment of the economic goals of the Union; an instrument for the fulfilment of a supranational constitutional framework. Nicolaïdis' characterisation brings a functional aspect of EU law firmly within the scope of discussion concerning constitutional order. It highlights the fact that the Union is not built only on vertical interactions between states and supranational institutions, but also on the interactions between states and their respective legal systems.[76] Thus, the notion of shared sovereignty is to be reconstrued. It is not merely the pooling of sovereignty in international institutions, not merely the surrender of prescriptive rights to an institution that occupies a higher space in a hierarchy, but the sharing of sovereignty between states on a horizontal plane.

It is submitted, however, that the notion of horizontal transfers is somewhat problematic insofar as it fails fully to capture the complexity of the relationship between states which commit to recognising one another's acts as equal to their own. The term 'transfer' suggests a degree of finality which is not evident in the politics of mutual recognition. A rather more fluid relationship is discernible in which one party enables the other to act on its behalf, and consents to be bound by those acts. Crucially, however, there is no alienation of the right to legislate. There is merely an acknowledgement that the acts of others are of equivalent force to one's own.

Agency theory, therefore, provides a more accurate theoretical prism through which to analyse mutual recognition. Mutual recognition results in the incorporation of a company by one state as though it were an incorporation of a company 'for' another state.[77] Accordingly,

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[73] Blair, 'Firm-Specific Human Capital and Theories of the Firm' (n 32) 63

[74] K Nicolaïdis, 'Trusting the Poles? Constructing Europe through mutual recognition' (2007) 14(5) *Journal of European Public Policy* 682, 685; see also SK Schmidt, 'Mutual recognition as a new mode of governance' (2007) 14(5) *Journal of European Public Policy* 667, 672; Poiares Maduro, 'So close and yet so far: the paradoxes of mutual recognition' (n 4) 819

[75] See, for example, Schmidt, 'Mutual recognition as a new mode of governance' (n 74) 672

[76] Ibid

[77] See BM Mitnick, 'The Theory of Agency: A Framework' (1976) *Annual Meeting of the American Sociological Association* 8 <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1021642> accessed 21 October 2019

it creates interdependencies whereby the prescriptive and administrative acts of one party bind the other party. Admittedly, mutual recognition does not fit perfectly comfortably the typical notion of agency wherein one party, the principal, contracts the other party, the agent, directly to act on its behalf, retaining only an instructing or monitoring role.[78] The peculiarity of mutual recognition is that the agent is in fact, at least apparently, acting on its own behalf, but its actions are recognised as binding upon the principal too. In other words, the agency relationship is incidental to the ordinary functions of territorial legislation. Nevertheless, there is an irresistible truth in the fact of extraterritoriality of legislative choices and administrative acts. While the legislation of one state might not be specifically intended to operate within another territory, the fact of the matter is that it does as a consequence of what is otherwise defined as a 'horizontal transfer of sovereignty'.

Nor does mutual recognition fit comfortably the traditional analyses of agency wherein there is an immediately recognisable, direct relationship between principal and agent from which fiduciary duties would flow. It is not immediately obvious that a Member State owes duties to states which are obliged to recognise its legislation. Still less are duties owed by public authorities to voters in unconnected *demoi*. Indeed, to suggest an agency relationship between states or *demoi* muddies the agency relationship between legislators and voters within states.[79] It is fundamentally unsound to suggest an incidental agency relationship should supersede the primary obligation to legislate in accordance with the instructions of the polity of the agent's territory. Nevertheless, it is submitted that this too does nothing to alter the fact of an agency relationship. While obligations might flow from a finding that an agency relationship exists, it does not follow that that the existence of an agency relationship is contingent on consequential obligations. Indeed, the absence of clear rights and obligations arising from interstate (or inter-polity) agency relationships merely serves to highlight the extent of the agency problem arising from systems-separation between governor and governed, to which the next section turns.

4.2 3.2 Strategies for the limitation of agency costs

In situations in which the law recognises the existence of an agency relationship, legal strategies are deployed to compel agents to act in the interests of the principal. This is in recognition of the fact that, if unchecked, rational agents will often act opportunistically with a view to maximising utility for themselves in preference to the interests of the principal.[80] Indeed, even in the absence of greed on the part of the agent, behaviour which is not to the satisfaction of the principal cannot be excluded.[81]

Agency costs arise particularly, however, where the interests of principal and agent are not aligned. This is especially difficult in the context of transfers of sovereignty because the agent-state is not expected to act in the interests of the principal-state, as in a regulated

[78] See, for example, SA Ross, 'The Economic Theory of Agency: The Principal's Problem' (1973) 63(2) *The American Economic Review* 134, 134

[79] For a critical account of agency theory as it applies to democracy, see CT Borowiak, *Accountability and Democracy: The Pitfalls and Promise of Popular Control* (Oxford University Press 2011) 53-78

[80] Jensen and Meckling, 'Theory of the Firm' (n 25) 308

[81] Alchian and Demsetz, 'Production, Information Costs and Economic Organization' (n 24) 783-784

agency relationship.[82] European Union law does not establish any duties which are owed by the agent to the principal, save to the extent that – conceptually – the principle of sincere cooperation may preclude behaviour which could have the effect of jeopardising the operation of the single market.[83] In the specific context of mutual recognition of companies, the Court did provide one avenue for the non-recognition in *Centros*. In the event that a choice of corporate law was motivated by fraud, the Court found that the existence of the company so established need not be recognised.[84] This, however, could not properly be classed as a mechanism to reduce agency costs as much as one to prevent outright illegality. The underlying inter-state agency problem remains undisturbed insofar as corporate policy is concerned; non-recognition merely operates as a partial law enforcement remedy; it does not constrain the agent to act in a manner which conforms to the principal's policy choices.

To further compound matters, in most circumstances the agent is unaware of, or indifferent to, the fact of the agency relationship and the effects of legislative action on the principal. In other words, the prescriptive behaviour of agents may occur entirely independently of the agency relationship, having regard only to domestic concerns and political developments.[85] By way of example, the United Kingdom is the leading exporter of corporate law because UK corporate law is among the most accommodating to promoters of companies (and thus among the least accommodating to other stakeholders).[86] Yet there is little to suggest that the UK legislation is anything other than the product of domestic juridical development that was intended to respond to domestic corporate law and policy needs. Indeed, contrary to what one might expect of an opportunistic agent, the UK's 2006 reforms to the Companies Act include relatively progressive developments such as greater minority shareholder protection and stakeholder-regarding governance.[87] There is no suggestion of opportunistic behaviour in response to the *Centros* judgment, but merely an incidental-agent acting only with reference to domestic concerns.

On the other hand, Member States may be fully aware of the implications of their legislation for other states, but may knowingly adopt or retain legislation which conflicts with the political consensus elsewhere. By way of example, there can be little doubt of the reality of social dumping in the online gaming market. States such as Malta are keen to create a business environment which is attractive to companies that intend to export gambling services, while the legislation concerning the domestic gambling market is far less accommodating.[88] It is in these circumstances that agency problems are most accentuated. The agent is keen to maximise its own revenues, and has no interest in mitigating the implications of its laws for other Member States. Indeed, not only does the relevant state adopt legislation (or refrain to do so, as is the case may be) entirely in its own interest, but

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[82] Jensen and Meckling, 'Theory of the Firm' (n 25) 308-310

[83] See S Carrera, 'The Price of EU Citizenship: The Maltese Citizenship-for-Sale Affair and the Principle of Sincere Cooperation in Nationality Matters' (2014) 21(3) *Maastricht Journal of European and Comparative Law* 406, 419-420

[84] Case C-212/97 *Centros Ltd v Erhvervs-og Selskabsstyrelsen* (n 33) para 25

[85] See generally, Paterson, 'The Company Law Review in the UK and the Question of Scope' (n 15)

[86] See generally Becht, Mayer and Wagner, 'Where do firms incorporate? (n 5)

[87] Companies Act 2006, s.172

[88] J Borg-Barthet, 'Online Gambling and the Further Displacement of State Regulation: A Note on *PMU v Zeturf*' (2008) 57(2) *International and Comparative Law Quarterly* 417, 418

that such legislative choices are intended specifically to circumvent the declared interests of other states.[89]

Typically, an agency relationship would impose fiduciary obligations on the agent which would compensate in some measure for the opportunistic or self-regarding behaviours noted in the two immediately foregoing paragraphs. The principal would be empowered to monitor the behaviour of the agent, and to provide incentives which would induce the agent to act in the principal's interests.[90] In the event that these inducements do not suffice, the principal is at liberty to deploy the ultimate penalty of severing an agency relationship, which itself operates as a Damoclean sword which the agent would not wish to disturb. In EU law of mutual recognition of companies, none of these tools is available, however. The principal is required to accept the regulatory-agent's policy choices in preference to their own, and no opportunity is afforded which would enable those choices to be adjusted.[91]

It could be argued, of course, that the co-existence of numerous norms in a single polity might cause the principal to reconsider historical choices through 'a new deliberative moment' prompted by the importation of foreign choices.[92] From an agency perspective, this is deeply problematic insofar as it suggests an adjustment of the principal's behaviour in response to the agent's actions, as opposed to the principal instructing the agent to act according to their instructions. Taken on its own merits, however, the suggestion is that the adjustment occurs with a view to reflecting the will of the principal as presently articulated. In the context of corporate law, this argument is not entirely persuasive. Evidence from both the EU and the United States indicates that, when mutual recognition prompts changes in corporate law, this is a consequence of a supply and demand calculus in which the demand side is dictated by dominant corporate stakeholders to the exclusion of others.[93] In other words, corporate laws are tailored to the stakeholders who are in a position to choose the state in which to incorporate, to the exclusion of other stakeholders.[94] More broadly, however, within the European Union there has not been a frantic 'race to the bottom', but toleration of the co-existence of significantly different corporate law standards with no systemic democratic deliberation to accompany the importation of norms determined by regulatory agents operating in a horizontally separate order. This poses significant questions of democratic legitimacy, to which agency theory provides few obvious answers in the context of systemically separate national democratic orders. The concluding section of this chapter considers the manner in which democratic means could be identified to connect the principal and agent in a broader deliberative moment to address the manner in which corporate laws could co-exist in the EU order.

4. Conclusion: Future prospects for democratic legitimation

Discussion concerning theories of governance tends towards disregarding mutual recognition as a system of governance, focusing instead on more traditional concerns regarding the

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[89] Ibid
[90] Jensen and Meckling, 'Theory of the Firm' (n 25) -310.
[91] Case C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v Inspire Art Ltd* (n 51)
[92] Poiares Maduro, 'So close and yet so far: the paradoxes of mutual recognition' (n 4) 820
[93] See Becht, Mayer and Wagner, 'Where do firms incorporate? (n 5) 252
[94] Ibid

allocation of decisional power as between vertically distributed public actors. The focus on a vertical democratic deficit neglects to engage with a far more acute disconnect between polities and the political choices by which they are governed. Whereas some democratic means of influence are invariably available as regards the adoption of EU primary and secondary legislation, mutual recognition results in decisions being taken by a polity and political system over which subjects of the law have no influence. Ordinarily, this could be justified with reference to individual liberty,[95] which is to say the principle that individuals should be free to determine their own preferences without reference to state interests.[96] That justification fails, however, in circumstances in which the choice of law is an expression of the will of only some actors to the exclusion of others.[97]

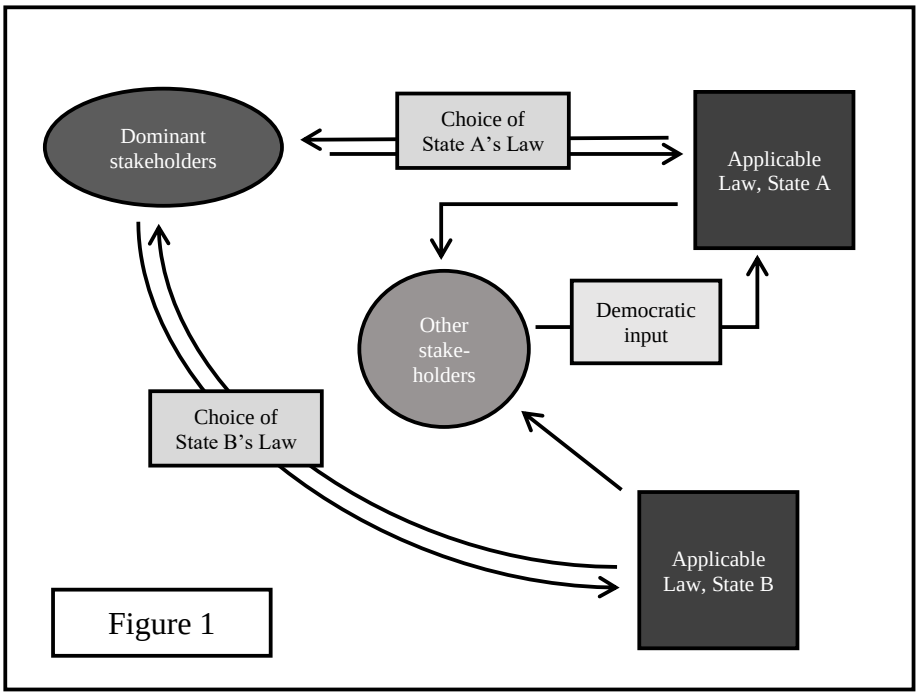

Figure 1 above illustrates how the relationship between all relevant actors is synallagmatic in the event that stakeholders are situated in State A, and the law of State A is chosen. In these circumstances, the applicability of the law of State A to stakeholders who are not party to the choice of law is justified with reference to ordinary democratic consent; stakeholders are able to influence the law by which they are governed, and their consent to be so governed is presumed as a consequence of a broader social contract. Dominant stakeholders are unique, however, in that they also enjoy a synallagmatic relationship with the law of State B in the event that they elect to subject the company to its laws. Theirs is a contractual arrangement among themselves whereby they determine that the law governing their relationships should be that of a Member State other than that in which the company is situated. The difficulty here is that the contractual covenant concerning the governing law also has effects on parties who are deemed extraneous to that contract. Those other stakeholders have no means to

[95] Nygh, *Autonomy in International Contracts* (n 62) 7-8
[96] M Lehmann, 'Liberating the Individual from Battles between States: Justifying Party Autonomy in Conflict of Laws' (2008) 41 *Vanderbilt Journal of Transnational Law* 381, 416
[97] See Part 2 above.

influence the governing law of the company, whether through corporate or democratic governance.

Private international law could offer the means to better align democratic governance through the introduction of mechanisms which would blunt the sharper edges of the incorporation theory. By way of example, the principal could be empowered to instruct the agent to require the upholding of selected norms which reflect a 'vigorous legislative intention' on the part of the principal,[98] or could elect to impose those norms as a condition of recognition.[99] This would offer a compromise which would retain the stated efficiencies of freedom of choice in the internal market, while mitigating potential market failures and horizontal democratic deficits. In particular, where a polity expresses a particular view concerning the beneficiaries of corporate governance and the participants in its management, this could not be bypassed through the application of norms determined by another polity. Crucially, however, this would require legislative intervention by the Union, both because it would otherwise be at odds with judgments concerning unilateral Member State intervention,[100] and because legal certainty could not be achieved in the absence of clear delimitation.[101]

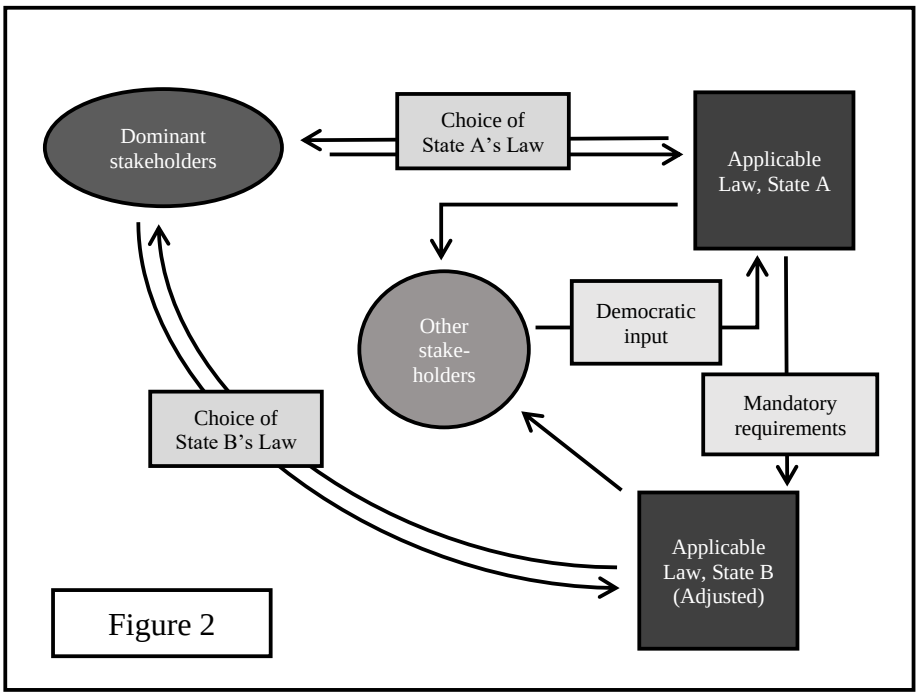

Figure 2 illustrates the operation of the inclusion of the mandatory requirements of the law of State A among the norms applicable to a company otherwise governed by the law of State B. This schema reconnects the democratic input of stakeholders in State A with the law governing the company, thereby limiting the agency problem as between Member States and polities. Importantly for the purposes of the obligations of the agent to its electoral principal,

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[98] See Borg-Barthet, *The Governing Law of Companies in EU Law* (n 14) 149-170
[99] ER Latty, 'Pseudo-Foreign Corporations' (1955) 65 *Yale Law Journal* 137, 159-160; see also Rammeloo, *Corporations in Private International Law* (n 50) 22-23
[100] Case C-167/01 *Kamer van Koophandel en Fabrieken voor Amsterdam v. Inspire Art Ltd* (n 51)
[101] Borg-Barthet, *The Governing Law of Companies in EU Law* (n 14) 155-158

this is achieved without imposing a particular view of corporate governance on the law of the agent as it applies generally.

Equally, whether as a complementary or alternative strategy, further harmonisation of corporate law offers the possibility to articulate an EU-wide view of the corporate form. Rather than legislating for one another, the Union's institutions could legislate the core features of company law collectively, thereby setting aside the inter-state agency problem insofar as the law is harmonised to reflect a shared view. This, of course, requires the articulation of a common view, not merely as a consequence of crisis management as has been the norm of late,[102] but with the reference to a broader view of the nature and purpose of the corporate form.

Whichever path is adopted by the Union, the displacement of democratic decision-making, and the attendant agency problem between states (and, therefore, between democratic polities), merit further attention with a view to reconnecting systems of decision-making with the territories in which those decisions take effect. This necessitates reconsideration of the manner in which the private governance of the internal market operates with a view to re-establishing a link with the subjects of that governance. In the present state of EU law, it is perfectly possible for there to be no systemic connection between the political processes through which corporate law is shaped, and the subjects of corporate decision-making. Accordingly, the most powerful party to the bargains among stakeholders is further empowered to determine the parameters of future bargaining by prescribing the legal framework in which this occurs.

The resolution of inter-state agency problems in corporate law, however, encounters the difficulty of legitimising democratic decision-making in the absence of a deliberative pan-EU demos, as discussed in other chapters of this book.[103] The history of harmonisation of both private international law and the substantive law of companies provides few positive signals in this respect, demonstrating instead the flaws of an integration process in which geographically distinct and entrenched views of corporate governance have resulted in counter-productive legislative abdication.[104] Agency analysis provides lawmakers with the means to identify the extent of the democratic disconnect in the Union's present regulatory landscape. The resolution of that disconnect, however, will require sustained and systematic engagement with corporate law and theory with a view to replacing wholesale market-driven judicial reordering with deliberative adjustment of the choice of law and substantive rules governing European corporations.

[102] See J Armour and W-G Ringe, 'European Company Law 1999-2010: renaissance and Crisis' (2011) 48(1) *Common Market Law Review*, 125, 149-157
[103] See the contributions by Cardwell, Everson, Saurugger and Terpan in this volume.
[104] See Part 2 above.