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THE EPC VERSUS THE UK PRIVATE LIMITED COMPANY

I have been asked to examine the issue of why an EPC statute could be useful even though the UK private Limited company is around as a competitor. The decisions of the European Court of Justice in *Centros* (registration of branch of a foreign company) and *Überseering* (recognition of a foreign registered company) have opened many doors to free movement of companies and hence to competition between national company law regimes within the EU. They are beneficial because they have focussed the attention of legislators on the needs of business in a way that pleas from employers federations like the BDI in Germany, MEDEF in France or the CBI in England, and the recommendations of Government committees, the legal professions or academic commentators have never been able to achieve. Overt competition from the UK's private limited company has prompted reforms, for example, in France (2002/2003 abolition of minimum capital for the S.A.R.L.), The Netherlands (bill of 08-11-2006 proposing the abolition of the €18,000 minimum capital and simplification of procedures), Italy (2003 reform increasing flexibility) and Germany (proposal to reduce minimum capital to €10,000 or less).

To get some idea of the scale of the competition in Germany we can look at an estimate given privately and unofficially by the Inland Revenue office Hanover-North/ Finanzamt Hannover-Nord, which deals with all English private limited companies tax registered in Germany that there are at least 20,000 Limiteds registered in Germany at the end of 2006. These are only the tax registered and hence actively trading Limiteds. There are quite a few establishments in Germany offering to form Limiteds for clients at bargain prices. A search on the internet reveals pages of such offers. One of these, Go Ahead Limited, claims to be the market leader with more than 28,000 incorporations of Limiteds to its credit.

We therefore need to examine the reasons why a German business might want to operate through a UK private limited company. Several reasons spring to mind immediately:-

- i) no minimum capital
- ii) rapid incorporation
- iii) flexible structure
- iv) usable for wide range of objects that do not have to be commercial or profit-making

How would the proposal for the EPC compare with this:-

- i) its minimum capital of €10,000 does not have to be paid up initially. If an English Limited is required for a commercial purpose, in practice the bank or other financial supporter will require either a substantial capital commitment by the founders or require personal guarantees from them and probably both. Either way a considerable sum of money will be at stake in the running of the business, with the personal guarantee resulting in the effective loss of limited liability. In the EPC a known sum of €10,000 will be at risk in the business, although the banks may require more. It is effectively a guarantee, but no capital needs to be tied up

- from the outset, if that is desired. The EPC in many situations could, from this point of view, be equally attractive to the Limited.
- ii) In terms of rapid incorporation, much depends upon how the EPC Regulation is drafted. Because there should be no necessary link to national law, in direct contrast to the *Societas Europea*, the formation procedure can be made fairly slick and quick, and there will be no need to subject the incorporation, for example, to the lengthy Government checks on the founders, that have motivated Dutch businessmen to use the Limited. See the case of *Segers*. Also, if desired, the expensive and time consuming Notarisation and Commercial Court procedures that currently form an important part of the German system, would not have to be adopted across Europe. Precedents exist in the UK and Ireland, for rapid incorporation procedures that could be adopted. Prohibition of reference to national law means that a single European system will have to be devised, although the registration itself will take place in national registries or commercial courts.
 - iii) Although the limited has a flexible structure the EPC, with its potentially minimalist approach to compulsion in the Regulation, is even more flexible and scores very heavily in this department.
 - iv) No restrictions are currently placed on use of the EPC in the CREDA/MEDEF proposal or the Teichmann update. Hence it compares very favourably with the Limited on this front also at the moment. However, the UK Companies Act 2006 will remove the necessity for the Limited to state any objects at all in its constitution and if felt desirable the EPC Regulation could do the same. Much could be made to depend on the wishes of the founders.

If the Limited still looks more attractive after this preliminary analysis, it could be on grounds of cost, of certainty or of reputation. So let us look at these factors from a German perspective.

Cost

In terms of initial cost, Go Ahead in Germany is offering a Limited for €260. In the UK one company is offering to form a Limited, for domestic use admittedly, for as little as £24.99 (€37). Another offers to form a Limited with a Bank Account, VAT Registration, Domain & Website in 3hrs. for £99 (€147). However this only tells part of the story. A more realistic figure for those who do not want to have to deal with the formalities of running a company in the UK is that from the reputable company Jordans who offer a full 1 year service including Annual reports etc. for £340 + VAT = £399 (€591).

It is one thing to own a Limited, but quite another to use it for commercial purposes in Germany. To do this it will require a German bank account. To obtain this it will be necessary to register a branch (*Neiderlassung*) of the Limited on the Handelsregister. For this you will need notarised copies of the constitution of the Limited (presently memorandum and articles of association, but soon only the articles) costing some €70 each. This must have an official translation by a Court appointed translator who charges some €10 per line of translation. We could end up with a Limited with say £100 capital, costing some €1500. Even if you are going to comply with the English formalities yourself, and not pay someone like Jordans to do it for you at some £400 a year, you will still need to prepare two sets of accounts, one set for the German tax authorities and another set, on a different basis, for submission to Companies House in the UK. The list goes on. One of my students has calculated that over a period of 8-10 years it will be more expensive to run a Limited than to

have formed a G.m.b.H. in the first place. For the EPC the process may well be like the introduction of any new product. Lawyers skilled in the formation process will initially be hard to find and no doubt expensive. Drafting of a constitution from the beginning to reflect the needs of clients could be complex. However, as the years go by lawyers will have ready drafted precedents to rely on, and increasing experience of the operational requirements of the EPC will bring the price down. The inclusion of model sets of *Satzung* in the Regulation will ease the way for the formation of relatively simple EPCs, and over time the costs will reduce as they do for computers, basic mobile phones etc.

Certainty

English company law may not be always very easy (as my students will tell you) but for ordinary transactions it is at the moment fairly well established, certain and predictable. Certainty and predictability are factors that have contributed strongly to the current pre-eminence of Delaware in the competitive environment of the United States. However, the new Companies Act 2006 will be introduced in the UK this year or next, and this contains much new wording which will have to be assimilated by lawyers and company secretaries alike. For example, duties of directors are now to be governed by formal wording in the Act instead of depending on a close study of the case law. This could eventually lead to greater certainty, but for several years the exact meaning of the words of the Companies Act will be a source of contention and possibly confusion in the UK. This may not be anything like as great as the problems of interpreting a new EU Regulation on the EPC, but it is worth considering in the short term.

Reputation

At the moment, the Limited seems to enjoy a high reputation with German customers. However, it may well be that over time it becomes associated with fraud or malpractice. For example, the Finanzamt Hannover-Nord have indicated that of the 20,000 or so Limiteds on the tax register about 70-80% were founded out of some insolvency problems of GmbHs in order to carry on with the business until a 22 month period is over, perhaps until a new GmbH could be formed. Many of these seem to be ill advised with fatal consequences. Lack of official communication between Companies House in the UK and the German tax authorities means that German bound Limiteds have to do the VAT registration themselves, and this can open the door to fraud. The activities of people like Jürgen Reiger using a London Briefkastenfirma for one of his projects could reduce the reputation of Limiteds still further. The emphasis on economic credibility that forms an essential part of the EPC proposal could result in a high reputation and is certainly intended to do so.