JEAN GUYÉNOT*
CHARLES P. D'EVEGNÉE†

The French Legal and Tax Aspects of the Formation of Subsidiaries in a European Context

I. The Choice of the Subsidiary's Form

French substantive law—but not tax law—ignores the notion of "group of companies," in the sense that this terminology does not appear in the basic Law of July, 1966 "relative to commercial companies."[1] Groups of companies are, however, taken into consideration by the legislature, not as entities, but as a fact which asserts itself by its obviousness: no more than men do companies live and act in isolation. To progress, they group themselves. By strategy, they swarm, retaining control over the companies which gravitate around them. Whatever the means—joint-venture agreements, creation of subsidiaries, take-over through purchase on the stock market or a tender offer,[2]—the group formed under the direction and impetus of one of them acts freely subject to the requirements of the economic legislation regarding competition.[3]

From a practical point of view, the advantage is considerable. Within the freedom which the Law of July 24, 1966 provides, companies can unite as they see fit, in the forms which appeal to them. No one can complain.

The subsidiaries—the outside stockholders of which are minorities in the group—have their share of the prosperity brought about by the existance of the group. As a matter of strategy, the companies do not want to stir up protest and thereby incite the legislature to enact as law the attractive "proposition" of M.

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*Professor of Law, University of Paris (France); Graduate of the University of Grenoble, the University of Lyons, and the University of Paris; Editor-in-chief of the Revue des Sociétés, Dalloz, Paris; Author; Member of the French Bar.

†Consultant, Frank B. Hall & Co., Inc., New York City. B.A. (1966), Brigham Young University; M.A. (1969), University of Connecticut; J.D. (1974), Law School, University of Connecticut; Student member, American Bar Association.

[1]See, generally, 1 J. HÉMARD, F. TERRÉ & P. MABILAT, SOCIÉTÉS COMMERCIALES (1972); see also, 1 J. GUYENOT & P. MOREAU, TRAITÉ PRATIQUE DES SOCIÉTÉS COMMERCIALES (1973).

[2]Regulated by Decrees of January 21, 1970, [1970] J.O. 844, [1970] D.S.L. 844, and of February 17, 1972, [1972] J.O. 932, [1972] D.S.L. 932. Exchange tender offers and purchase tender offers receive the same treatment under the regulations.

[3]See generally J. GUYÉNOT, DROIT DES ENTENTES INDUSTRIELLES (1972); see also J. GUYÉNOT, DROIT ANTITRUST EUROPÉEN (1973).

Pierre—Bernard Couste[4] or to accelerate the work pending at the chancellery relative to a "bill" on company groups.[5] From an economic point of view, the freedom being beneficial to all, French law practices a "wait and see" policy with a marked preference for overall regulation at the European level.

This freedom engenders a multiplicity of groups of enterprises of the most varied types, tailor-made, adapted to need, interchangeable at any time.[6] Under the impetus which impels enterprises to group in order to prosper together, the legislature offers them new forms such as "groupements d'intérêt économique" ("G.I.E.," *i.e.*, economic interest associations), half-way between companies and economic cartels.[7]

While ignoring the "groups" concept, the legislature does not ignore the effect of their creation and operation on the legal status of the companies composing them. A section (arts. 354 to 359) of the Law of July 24, 1966 is devoted to "subsidiaries and affiliates," defining them and assigning a limit on freedom by forbidding reciprocal shareholding affiliations for fear of impairing the capital which is regarded as the creditors' security.[8]

Thus, on the one hand, article 354 defines "subsidiary" by stating that "when one company owns more than half of the shares of another one, the second company is considered a subsidiary of the first." On the other hand, article 355 recognizes that when the investment is less than 50 percent, there is only an affiliate relationship. The law states it in these terms: "When one company owns a fraction ranging from 10 and 50 percent of the shares on another one, the first company is considered as having an interest in the second one." When the interest is less than 10 percent, the law being silent, it is considered that it is merely an investment made by a company which adds to its portfolio securities issued by another company.

In other words, the legislature fixes a percentage threshold beyond which a company becomes the subsidiary of another, which implies that the subsidiary as well as the parent company are share companies.[9] Consequently, ordinary

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[4]For a discussion of Couste's "proposition," see Bachvogel, Die Gesetzesvorlage Couste für ein Konzernrecht in Frankreich, Zeitschrift für Unternehmens und Gesellschatsrecht [Z.G.R.] 76 (1972); Rodière, La protection des minorités dans les groupes de sociétés: sur la proposition de loi dite Couste, no. 1055 du 9 avril 1970, 1970 Revue des Sociétés [Rev. Soc.] 243.

[5]Under study since the beginning of 1971.

[6]See, generally, J. GUYÉNOT, LES CONTRATS DE CONCESSION COMMERCIALE (1968); see also, J. GUYÉNOT, CONCESSION COMMERCIALE ET FRANCHISING (1973).

[7]See generally J. GUYÉNOT, LES CONTRATS DE GROUPEMENTS D'INTÉRÊT ÉCONOMIQUE (1970); see also, J. Guyénot, Les G. I. E. (1971).

[8]A reciprocal affiliation arises when a company owns more than 10 percent of another company's capital and, in turn, the latter company owns more than 10 percent of the capital of the first. Articles 356 to 359 are directed against reciprocal affiliation and establish a procedure calculated to put an end to the practice.

[9]In French company law, companies are classified in two broad classes: "sociétés de capitaux" or share companies, and "sociétés de personnes" or ordinary partnerships. For a comparison between these two classes, see 2 Dictionnaire de Droit § 13, at 624 (2nd ed. Librairie Dalloz 1966).

partnerships are excluded in principle from the subsidiary concept since they have no shares or capital stock but a "fund" common to all the partners, who are personally liable for their debts. A "G.I.E." formed without capital stock, like a partnership, is identified with the latter. If a "G.I.E." should have capital stock, the point is debatable, but, in our opinion, it should still be treated like a partnership because of the personal and unlimited liability of its members.[10]

Therefore, the choice of a subsidiary's form is limited in practice to share companies, with a predilection for the form of "sociétés anonymes" ("S.A.," *i.e.*, limited companies or business corporations).[11] The "sociétés à responsabilité limitée" ("S.A.R.L.," limited-liability companies, incorporated partnerships or close corporations) can also be used as a legal form for the subsidiaries, but in practice, they are somewhat neglected,[12] even though the Law of July 24, 1966 has indisputably aligned them with share companies.[13]

II. Resemblances and Differences Between "Société Anonymes" and "Société à Responsabilité Limitée" to be Taken into Account in Deciding on the Subsidiary's Form

Like the shareholders of an "S.A.," those of an "S.A.R.L." do not have the status of "commerçant"[14] and are liable only to the extent of their assets brought into the business. This dual advantage is responsible for the success of the "S.A.R.L.," instituted by the Law of March 27, 1925 and similar to the "GmbH" created in Germany in 1892. However, the prohibition against representing shares by negotiable certificates, as well as their non-transferability between shareholders or to third parties, gave the S.A.R.L. a structure close to that of a partnership, while the omnipotence of the manager conferred upon it a particular style, suitable only to small family undertakings or to persons united by close ties of interest.

The reforms effected by the Law of July 24, 1966 have patterned the law of the "S.A.R.L." on the more perfected legal mechanisms of the "S.A." This pattern has been accentuated by the changes made in the Law of July 24, 1966 by the Ordinance of September 20, 1969 aimed at insuring the application of

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[10]J. GUYÉNOT & P. MOREAU, *supra* note 1. See generally the above-mentioned works.

[11]The new types of share companies can also be assimilated; see generally J. GUYÉNOT, LES SOCIÉTÉS CIVILES IMMOBILIÈRES DE CAPITAUX (1972).

[12]As a matter of strategy, branches and agencies are sometimes created under the form of "S.A.R.L." subsidiaries, the shares of which belongs almost entirely to the parent company of a distribution or service network.

[13]Derrupé, *Le nouveau visage de la société à responsabilité limitée dans la loi du 24 juillet 1966*, in MÉLANGES BRETHE DE LA GRESSAYE 177 (Bière ed. 1967).

[14]In France, the status of "commerçant" subjects one to numerous obligations. For an enumeration of these obligations, see 1 Dictionnaire de Droit § 23, at 338 (2d ed. Librairie Dalloz 1966).

the EEC council's directive of March 9, 1968.[15]

In the application of current legislation, the resemblances are clear on the following points:

1. The rules of incorporation of the "S.A.R.L." are very close to the regulations provided for an "S.A." which does not make a public offering.[16]

2. The name rules are henceforth identical; even if the company name includes the names of the incorporations, they are not personally liable for its commitments. Third parties are on notice of the company's form since, from now on, as with the "S.A.," the name must be immediately preceded or followed by the words "société à responsabilité limitée" or by the initials "S.A.R.L." and by a statement of the amount of the capital stock.[17]

3. Regulation of agreements between the company and the manager or a shareholder draws its inspiration from the same principles as those of the "S.A.," while being appreciably simpler.[18]

4. The holding of shareholders meetings and providing information to the shareholders are also patterned on rules which are characteristic of the "S.A."

5. Some rules, patterned after those of the "S.A.," govern both the sanctions for irregularities in incorporation and the duties of the decision-making bodies.

6. The status of the auditors is defined in the Law of July 24, 1966 by a simple reference to the law governing " sociétés anonymes."[19]

7. Some rules, almost identical to those of the "S.A.," require a legal reserve and provide for a procedure comparable to the one established in case of loss of three-quarters of the capital.[20]

8. A minimum capital is required as with the "S.A." It is 20,000 F., whereas in the case of an "S.A." not making a public offering, the minimum is 100,000 F. If, in the course of the company's existence, the capital should fall

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[15]Directive 68-151 of the EEC Council (J.O.C.E., L. 65, March 14, 1968) which harmonizes among the member states the various guarantees required of companies in order to protect the shareholders as well as third parties.

[16]A public offering is made whenever a company has recourse to banks, financial institutions and brokers, or other means of publicity for marketing its shares; see sections IV and V-A, infra.

[17]Law of July 24, 1966, art. 34, para. 2, [1966] J.O. 6.402, [1966] D.S.L. 6.404.

[18]Law of July 24, 1966, art. 50, [1966] J.O. 6.402, [1966] D.S.L. 6408; Decree of March 23, 1967, arts. 34 & 35, [1967] J.O. 2.843, [1967] D.S.L. 2847.

[19]French corporate law requires, under penal sanctions, that the incorporators appoint one or more auditors to assist the shareholders in supervising the management of corporations the capital of which exceeds 300,000 F. The auditors are chosen from among those registered on the list of approved auditors or among the experts registered on one of the lists established by the courts and tribunals (in France, tribunals are distinguished from courts in the sense that they are inferior courts of limited jurisdiction), Law of July 24, 1966, arts. 64, 430 & 455, [1966] J.O. 6402, [1966] D.S.L. 6409; Decree of March 23, 1967, art. 43, [1967] J.O. 2843, [1967] D.S.L. 2848.

[20]Since enactment of Act No. 69-12 of January 6, 1969, amending the Law of July 24, 1966 (art. 68 § 241), the duty to decide within four months following the approval of the accounts whether the company should be dissolved is no longer tied in with loss of three-quarters of the capital but with the fact the net book assets of the company are less than one-fourth of the capital; see generally Hémard, Terré & Mabilat, *Les dixième et onzième réformes du droit des sociétés commerciales,* 1969 REV. SOC. 9.

below 20,000 F., the "S.A.R.L." has an option which it must exercise within a year: either it must increase the capital to at least 20,000 F. or it must be converted into a company of another type. In the latter case, the "S.A.R.L." can be converted only into a partnership, for which unanimous consent of the shareholders is required.[21]

This possibility notwithstanding, the closeness of the system of management of the two types of companies, "S.A.R.L." and "S.A.," is of such a nature as to facilitate, in case of need, the change from one form to the other. Such conversion, moreover, is considered in law as a normal operation when the number of shareholders goes beyond fifty,[22] for example, as a result of inheritance. But the resemblances do not exclude some sharp differences.

The differences between the "S.A." and the "S.A.R.L." are great because of the ties that the latter retains with partnerships.

1. The prohibition against representing the shares by negotiable certificates is absolute, without exception. The shareholder must prove the existence of his right by producing the articles of incorporation.

2. An "S.A.R.L." may not issue transferable securities on its or any other company's behalf, on pain of nullity of the issue. Disregard of this prohibition is criminally punishable.

3. The shares must be entirely subscribed for by the incorporators and be fully paid-up when issued—whether they are paid for in cash or in kind, while only one-fourth of the price of the shares need be paid-up upon issuance in the case of an "S.A." The requirement that shares issued for cash be fully paid-up, a requirement which does not exist in Germany, can sometimes hinder the raising of any sizable capital and thus jeopardize the company's credit. On the other hand, it has the great advantage of obviating subsequent calls for payment addressed in vain to the shareholders and also of precluding, to a certain extent, the creation of fictitious companies.

4. The shareholders are jointly liable to third parties for any shortfall in the value assigned to the contributions in kind in the articles of incorporation.[23] The nature of this liability is very much disputed and the legal provision (Law of July 24, 1966, art. 40) which imposes this liability has aroused strong protests from practitioners, even though the Law of July 24, 1966 (art. 40) provides that the shareholders are guarantors only of the value of the contributions *at the time* of the incorporation of the company. They thus do not guarantee the preservation of this value. The depreciation of contributions is a risk to which the creditors of any company are exposed.

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[21]Law of July 24, 1966, art. 69, para. 1, [1966] J.O. 6402, [1966] D.S.L. 6409.

[22]Law of July 24, 1966, art. 36, [1966] J.O. 6402, [1966] D.S.L. 6405.

[23]The value of the contribution in kind is decided on by the incorporators upon presentation of a report prepared by an expert appraiser and annexed to the articles of incorporation. The appraiser is unanimously appointed by the future shareholders.

5. The shares of an "S.A.R.L." are not freely transferable even though shareholders, in principle, can freely negotiate the shares which represent their contributions. But since enactment of the Law of July 24, 1966 (art. 45), the shareholder of an "S.A.R.L." is assured of being able to withdraw from the company by sale of his shares,[24] even against the wishes of the other shareholders; in this regard, his position is similar to that of the shareholder of a "société anonyme," the articles of which contain a clause restricting share transfers.

6. An "S.A.R.L." cannot have more than fifty shareholders (Law of July 24, 1966, art. 36). This rule is a reminder of the concern with persons characteristic of the "S.A.R.L."[25] but not of the "S.A."

7. The admission of new shareholders requires the consent of a specified majority in interest of the existing shareholders. The majority rule characteristic of share companies clearly differentiates the "S.A.R.L." from a partnership, in which all decisions are made by unanimity, unless otherwise provided for in the articles. But if, in this regard, the legal entity escapes contractual law to a large extent, the legal mechanisms of the "S.A.R.L." are dependent upon a procedure appropriate to companies whose shareholders are linked by family ties or close material ties. The latter make the "S.A.R.L." a close company, dominated by the manager who, until adoption of the Law of 1966, was practically irremovable and absolute master of the company. This sovereignty, redoubtable for the shareholders as well as for third parties, has been deminished by the Law of 1966 which has introduced rules establishing real responsibility of the manager and effective supervision of his management by the shareholders assisted by an auditor.[26]

III. Special Rules for the Incorporation of Companies by Non-Nationals

The incorporation of a company in a country other than one's own involves the transfer of its head office into that country. Because of the difficulties encountered in the transfer of its head office, a company usually extends its business operations to another country by creating a secondary establishment, subsidiary or branch.[27]

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[24]He does not forfeit his investment but, on the contrary, the value of the shares must be paid to him. For a short explanation of the mechanics involved here, see Dictionnaire de Droit § 83, at 116 (2d ed. 1966, Supp. 1971).

[25]See *supra*, note 9.

[26]See, generally, J. GUYÉNOT, COURS DE DROIT COMMERCIAL (1969).

[27]The creation or extension of a branch must be reported to the minister of finances as a foreign investment made in France (Decree of January 27, 1967, art. 2). Before the opening of a branch or an agency in France, the foreign company must file with the clerk's office of the Commercial Court having jurisdiction over the branch or agency, two copies of the company's articles of incorporation and any amendments translated into French if need be (Decree No. 67-237 of March 23, 1967, art. 63). Moreover the foreign company must be registered in the commercial registry in the name of the

In the European Economic Community, the general directive drafted by the Council on December 18, 1961 concerning the rendition of services and the right of establishment provides for the elimination of all restrictions on the creation of agencies, branches and subsidiaries. These measures have been partly implemented; they are applied for the benefit of:

1. The nationals of the member states and associated overseas countries and territories, on the condition that they be established in the territory of a member state or associated overseas country or territory;

2. Companies organized under the laws of a member state or associated overseas country or territory and having in one of such states or territories their real head office, their general management or their principal place of business, provided that—if they only have their registered office there—their activity present an actual and permanent tie with the economy of a member state or overseas territory. This proviso is calculated to preclude enjoyment by an enterprise foreign to the Common Market by virtue of the creation of a fictitious head office, of the benefits of preferential treatment reserved for the companies of the member states;[28]

3. In respect of the activities freed, or "emancipated," from restrictions, the foreign trader's card[29] is not required of the managers of the subsidiaries, branches and agencies established in French territory. The Ordinance of August 28, 1969, supplementing the Decree of November 12, 1938 relative to the trader's card, dispenses with it in regard to the carrying on of emancipated activities by nationals of the member states of the EEC, which activities are alluded to in the appendix to the above-mentioned ordinance as supplemented by the Ordinance of December 29, 1972. Moreover, the Decree of January 5, 1970 has made domestically applicable the provision of Directives 64-220 and 64-221 of February 25, 1964, which have removed the restrictions on most business activities.[30]

A foreign company not a national of a member state can create a subsidiary in France which will function according to the rules of French corporate law, harmonized with the directives of the council by the Ordinance of December 20, 1969.[31] Possession of the trader's card is required of the partners if they are

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branch or the agency. Finally, the manager of the branch or the agency must hold a foreign trader's card (Decree of February 2, 1939, art. 5, para. 2); see section III-A, 3., *infra*.

[28]The tie required may not in any way relate to the nationality of the shareholders or of the members of the subsidiary's decision-making bodies.

[29]This card, issued by the ministry of industry and commerce, indicates the business occupation(s) authorized as well as the district(s) in which they can be carried on; see section III-B, *infra*.

[30]Directive 64-220 of February 25, 1964 deals with the elimination in principle, of the restrictions on travel and residence of the nationals of a member state who wish to settle in another member state with a view to engaging in business there for their own account. Directive 64-221 of the same date harmonizes the measures of the member states concerning the travel and residence of "European" nationals.

[31]Ordinance No. 69-1176 of December 20, 1969 modifying Law No. 66-537 of July 24, 1966 (relative to commercial companies), [1969] J.O. 12679, 1970 Rev. Soc. 125.

unlimitedly and jointly liable for the debts, of the manager of an "S.A.R.L.," and, in the case of an "S.A.," either of the chairman of the board of directors and of the directors, or of the chairman of the directorate and of the members of the supervisory board. Case-law extends this requirement to foreigners who in fact exercise the management control under cover of nominal executives of French nationality.[32]

IV. Special Rules for Public Offerings in France by Companies Organized by Non-Nationals

In the European Economic Community, certain directives and draft directives tend to facilitate the issue and sale of stock by companies belonging to the member states. The measures under study would allow them to issue transferable securities, as if they belonged to the state in which the public offering is made.

Companies not belonging to the community, as well as the companies belonging to it, can issue stock in France only after obtaining a ministerial authorization.[33]

This rule excepted, the issuing companies, whether belonging to the community or otherwise are subject to the laws which govern the issue of transferable securities. These laws intended for the protection of investors express public policy. In particular, the issuing company must fulfill the following conditions:

1. Obtain the authorization[34] of the Stock Exchange Transactions Commission ("C.O.B.," *i.e.*, Commission des Opération de Bourse, established by Ordinance No. 67-883 of September 28, 1967[35]) before it can publish a prospectus[36] intended for prospective subscribers.

2. Prior to any issue—and prior to admission to trading on a stock exchange, jointly decided on by the "C.O.B." and the Stockbrokers' Association—the issuing company must, if it does not have a branch or agency in France, file with the clerk's office of the Commercial Court in Paris, two certified copies of its articles and amendments, translated into French if need be.[37]

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[32]*Zielinsky and Petitjean,* [1956] D. Jur. 720 (Cass. crim.); *Uzan and Sultan,* [1967] J.C.P. II 15525 (Cour d'appel, Paris).

[33]Decree of January 27, 1967, art. 5, [1967] J.O. 1672, [1967] D.S.L. 1672; Ministerial Order of January 27, 1967, arts. 5&6.

[34]The issuing company must submit to the commission a statement which discloses its financial status and organization and the trend of its business. The authorization to proceed with the issue is given once the commission has verified the accuracy of the information submitted by the company.

[35]See generally our commentary on the ordinance in Les ordonnances de septembre 1967 et le droit commecial (1968); see also our study, La commission des opérations de bourse et l'information des porteurs de valeurs mobilières sur l'activité et lés resultats des sociétiés, in Gazette du Palais, March 19, 20, 21 &22 (1973).

[36]See section IV-B, 3., *infra.*

[37]Decree of March 23, 1967, art. 64, [1967] J.O. 2843, [1967] D.S.L. 2849, modified by the Decree of January 2, 1968, [1968] J.O. 124, [1968] D.S.L. 124.

3. The issuing company must, finally, publish in the *Bulletin d' Annonces Légales Obligatoires* ("B.A.L.O.," annexes of the *Journal Officiel*) a notice indicating the principal characteristics of its legal status (name, objects and purposes, registered office, etc.) and of its operational procedures (conditions of admission of shareholders, voting rules, distribution of profits). The prospectuses, circulars and advertisements intended to publicize the issue, must reproduce the statements of the notice with reference to the issue of the "B.A.L.O." and to the authorization of the "C.O.B."[38]

V. The Articles of Incorporation of an "S.A." and of an "S.A.R.L."

The société à responsabilité limitée is formed by articles of incorporation signed by the shareholders. They must know each other and, in this respect, the company is similar to a partnership. The prohibition of the issuance of transferable certificates generally obliges the promoters to seek shareholders within their circle of business relations, friends, or family connections. This accounts for the fact that the rules concerning the incorporation of the société a responsabilité limitée are almost the same as those relative to sociétés anonymes which do not make public offerings. In the Law of July 24, 1966, the legislature modeled on the rules of incorporation of the "S.A.R.L." the incorporation of the "S.A." not making a public offering.[39]

1. The validity of the articles of incorporation depends on the agreement of at least two incorporators on a lawful business purpose.

2. The collected contributions constitute the capital. These can only be made in cash or in kind.[40] After the valuation of the contributions in kind upon presentation of a report of an expert appraiser,[41] the minimum amount of the capital must be 20,000 F. (Law of July 24, 1966, art. 35). The capital is divided into shares of equal par value. The Decree of March 23, 1967 has set the minimum par value of each share at 100 F.[42]

3. Within eight days of receipt thereof, the funds representing cash contributions must be deposited with the Deposit and Consignment Office, or a notary or a bank for account of the company in process of organization (Decree of March 23, 1967, art. 22). The deposit is mentioned in the articles, under penal sanctions (Law of July 24, 1966, art. 423). Withdrawal of the funds can be

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[38]See La commission des operations de bourse et l'information des porteurs de valeurs mobilières sur l'activité et les résultats des sociétés, *supra* note 35.

[39]See section IV, *supra.*

[40]Contributions in the form of personal services are not allowed: the capital being in principle the only guarantee of the shareholders, the services of a shareholder cannot be considered as a part of the capital.

[41]The report is prepared on the responsibility of the appraisers.

[42]This amount may be lower for companies incorporated before the effective date of the Law of July 24, 1966; see art. 301.

made by the authorized agent of the company only upon presentation of a certificate of the clerk of the Commercial Court attesting to the registration of the company in the commercial registry.

4. The articles can be drawn up by a notary or by the parties themselves; if they are drawn up by the parties, as many originals as are necessary should be prepared in order to have a copy for the head office, for fulfillment of the formalities required by the clerk of court's office, and for filing of the articles with the tax authorities.[43] Moreover, a copy on unstamped paper must be given to each shareholder (Decree of March 23, 1957, art. 20).

5. Assumption of the promoters' contracts is dealt with in article 26 of the March 23, 1967 Decree, which specifies the terms on which the company can assume contracts made for its account during the pre-incorporation period. A report on such transactions stating, as to each, the obligations resulting therefrom for the company, is presented to the shareholders before the signing of the articles. This report is annexed to the articles, the signing of which will constitute assumption of the contracts by the company once it has been registered in the commercial registry.

6. According to the ordinary law of commercial companies, a notice of incorporation must be published in a newspaper carrying legal advertising in the district ("département") of the head office.[44] This notice recites the company's basic characteristics.[45]

This newspaper advertising is the last step before the company acquires legal entity status by registration in the commercial registry.

7. Registration of the company with the clerk of the Commercial Court having jurisdiction over the company's head office is required. The application is accompanied by a certain number of documents: two copies of the articles, a declaration by the incorporators attesting that the company has been incorporated according to the laws and regulations in force and, if need be, the instruments appointing the managers and the auditors,[46] and the report of the expert appraiser on the valuation of the contributions in kind.

In application of the EEC Council's directive of March 9, 1968, the Decree of December 24, 1969, supplementing the Decree of March 23, 1967 relative to the

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[43]See section VII, *infra.*

[44]The newspapers carrying legal advertising have services specializing in the accomplishment of all the formalities of publicity including those of the office of the clerk of the Commercial Court. In practice, companies rely on these newspapers for the formalities. "Les Petites Affiches," 2 Rue Montesquieu, Paris 2, founded in 1612 by Théophraste Renaudot, and the "Gazette du Palais," 3 Blvd. du Palais, Paris 4, are the principal such newspapers.

[45]The same requirement of publication is imposed as to any subsequent amendment which changes any of the basic characteristics of the company. The sanction for failing to advertise is the imposition of liability on the incorporators and on the initial managers, nullity of the incorporation excepted.

[46]Appointment of auditors is compulsory, as has been indicated, for companies whose capital exceeds 300,000 F.

commercial registry, charges the clerk of court, who up to then had a passive role, with making sure that the formalities provided by the law and regulation relative to commercial companies have been accomplished.[47]

After this check, the clerk of court sends copies of the instruments filed to the National Institute of Property which keeps the central commercial registry.[48] Moreover, he is required to see to it that a notice is published summarizing the basic characteristics of the company in the official bulletin of commercial notices ("B.O.D.A.C.," *i.e.*, Bulletin Officiel des Annonces Commerciales), annexes of the *Journal Officiel.*[49]

With respect to sociétés anonymes, the Law of July 24, 1966 regulates their incorporation by distinguishing between two types: companies which make public offerings and those which do not (Law of July 24, 1966, art. 72).

Incorporation without a public offering is relatively simple, as it is patterned on that of the "S.A.R.L."[50] Without repeating the description already given of the steps for formation of an "S.A.R.L.," we merely point out the differences:

1. The minimum amount of capital is 100,000 F., an intermediate figure between that of the "S.A.R.L." and the "S.A." making a public offering.

2. The number of shareholders is not limited by law; in practice, it is small.

3. The amount of cash paid in by the shareholders is certified by a statement by one or more shareholders—usually the incorporators—made in the presence of a notary and transcribed in a notarial instrument. The notary must be given in advance the list of stockholders, showing the sums paid by each, as well as a certificate of the trustee of the funds—Deposit and Consignment Office of bank, if the notary is not the trustee—attesting the payment of the funds.

4. The shares issued for cash must be paid up to the extent of at least 25 percent when issued.[51]

5. The valuation of the contributions in kind upon presentation of the report of the expert appraiser—and stated in the articles—is approved by the shareholders by their signing of the articles, in the same way as for an "S.A.R.L." But contrary to the "S.A.R.L." rule, the shareholders do not assume any liability to third parties for this valuation.

6. The articles must name the first directors or the first members of the supervisory board, as well as the first auditors.[52]

There is no incorporators' meeting. All the shareholders sign the articles as for an "S.A.R.L." They are published in the same way as those of an

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[47]With this reform, the French system is deemed to have satisfied the requirements of the directive.

[48]As to the set-up of the commercial registry, see J. GUYÉNOT, *supra* note 26, at 202.

[49]On the sanctions for defective incorporation, see J. GUYÉNOT, *supra* note 26, at 397; see also G. RIPERT & R. ROBLOT, TRAITÉ DE DROIT COMMERCIAL 539 (1972).

[50]See section V-A, *supra.*

[51]Different rule for an "S.A.R.L." already noted above.

[52]Law of July 24, 1966, art. 88, [1966] J.O. 6402, [1966] D.S.L. 6409.

"S.A.R.L." and the company acquires legal entity status by registering in the commercial registry.

Because of the simplicity of this type of incorporation for the "S.A.," it is rare in practice for the incorporators to turn to the more complex formalities of incorporation of an "S.A." making a public offering. First they incorporate the "S.A." as has just been indicated. Then they wait for two years, after which time the Law of July 24, 1966 permits a public offering, provided that the initially-issued shares are fully paid. The public offering is made as described above.[53]

The incorporation with public offering being exceptional in practice, we will only describe the step of incorporation of the "S.A."

As a preliminary, let us recall that there is a public offering when a company has recourse to banks, financial institutions and brokers, or other means of publicity for marketing its shares.[54]

A public offering is made upon incorporation when the company must obtain in the shortest possible time a large number of shareholders and a sizable amount of capital to realize its objective.

The steps of the incorporation are then as follows: the incorporators decide to organize the company and carry out the first legal transactions necessary for its creation—purchase of lands and buildings, printing of publicity documents, hiring of personnel—which the company will take over in its name upon incorporation; they seek shareholders by appropriate means[55] and those who agree to join the company so signify by subscribing for shares; the shareholders then hold a general organizational meeting which votes on the articles, approves the pre-incorporation transactions, elects the directors or the members of the supervisory board and the auditors; the articles are published and the company is registered in the commercial registry. It is then that the corporate existence begins.

VI. The Choice Between Two Forms of Administration of the Sociétés Anonymes

The Law of July 24, 1966 offers to existing or future companies[56] an unrestricted choice of two forms of administration.

The traditional form: board of directors and president. This form derives from the old Law of July 24, 1867—partially repealed by the Law of July 24, 1966 (strange way of celebrating the centennial jubilee)—based on English law,

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[53]See section IV, *supra.*

[54]On the concept of public offering and its extension by the "C.O.B.," see the work mentioned in note 11, *supra.*

[55]Authorization must have been previously obtained from the "C.O.B."

[56]Companies incorporated before the effective date of the 1966 Law can adopt the new system by amending their articles in the usual way.

but substantially amended by the Laws of November 16, 1940 and March 4, 1943. Revamped by the 1966 Law, the management is entrusted to a board composed of three to twelve members who must be stockholders, elected by the shareholders.[57] The board has broad powers, being vested with "the most extensive powers to act in the name of the company in all circumstances" (Law of July 24, 1966, art. 98).[58]

At the head of the board is placed a president elected by the directors. He retains the role defined by the Law of 1940, assuming "on his responsibility, the management of the company" (Law of July 24, 1966, art. 113). Elected by the board, he does not derive his powers from the latter, but from the law.

The new form: directorate and supervisory board. This new form was born of the criticisms made of the traditional form, with a view to doing away with the managing powers of a board which limits itself to supervising the president's management while the latter presides over the meetings of the body charged with supervising his acts. To resolve this ambiguity, the 1966 Law creates a second form comprising a more rigorous separation of functions between two bodies, each of which is to discharge its duties with increased efficiency.

The directorate, composed of a maximum of five persons[59] who need not be shareholders and are elected by the supervisory board, possesses full powers to act in the name of the company. The supervisory board can confer on one of the members of the directorate the title of president with power to represent the company in its relationships with third parties.

The supervisory board, consisting of not less than three nor more than twelve members, is elected by the shareholders.[60] In addition to various powers, among which is the power of recommending to the shareholders the removal of members of the directorate, the supervisory board exercises standing supervision of the directorate's management of the company.

This form, derived from German law, is the closest to the one that European law intends to create for the "S.A.E."[61]

In both forms, the auditors retain their responsibility for auditing the accounts while being subject themselves to supervision by the "C.O.B." in the care of an "S.A." making a public offering.[62]

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[57]This term of office is fixed by the articles: it cannot exceed six years in case of election by the shareholders and three years in case of nomination in the articles. The directors are eligible for re-election unless otherwise provided in the articles. An age limit has been set by Law No. 70-1284 of December 31, 1970, [1970] J.O. 12281, [1970] D.S.L. 12281, 1971 Rev. Soc. 137; see Guyénot, La limite d'âge des administrateurs de sociétés par actions, Journaux Judiciares Associes de Paris (Les Petites Affiches), January 26, 1973, at 8, col. 1.

[58]Two representatives of the works council, representing the personnel, attend board meetings but have no vote.

[59]There may be a one-man directorate in an "S.A." the capital of which is less than 250,000 F., Law of July 24, 1966, art. 119, para. 2, [1966] J.O. 6402, [1966] D.S.L. 6412.

[60]*Id.*, Article 134.

[61]See Gleichmann & Cathala, *Le statut des societes anonymes europeennes*, 1972 REV. SOC. 1.

[62]J. GUYENOT, *supra* note 11.

VII. Registration Fees and Taxation of Contributions

The registration fees are collected upon the incorporation of companies just as they are with respect to certain legal instruments, for example, sales, donations and leases. These taxes are collected by the "tax offices," formerly called "registration offices."

Until enactment of the Law of December 26, 1969, a distinction was made between the registration fees, properly so-called, collected by the "tax offices," and the "land registration tax" (0.60 percent in general) collected at "the mortgage office upon the filing of instruments involving land registration, such as sale of real estate and assimilated transactions (including contributions of real estate to companies), and the registration of mortgages."

Since adoption of the Law of December 26, 1969, the "registration fees" and the "land registration tax" have been merged into a single formality. Consequently, the incorporation of companies which comprise contributions of chattels (including cash) and of real estate gives rise to the collection of taxes only at the time of registration with the "tax office," without an additional collection upon the registration of the deeds of conveyance in the mortgage office.

The registration formality has a primarily tax objective: to calculate the amount of "taxes" to be collected by the revenue service with regard to a legal instrument. The "taxes" can be fixed (20 F., 50 F., 80 F., 150 F.) or proportional to the value of the assets to which a transaction relates.

Upon incorporation, the taxes are proportional in principle, being calculated on the value of the contributions made to the company by the shareholders.

The taxation of the contributions or "taxes applicable to the contributions" vary according to whether "pure and simple contributions" or contributions said to be "for valuable consideration" are involved.

1. The pure and simple contributions are those the consideration for which is the shares issued in exchange and which are exposed to the risks of the enterprise. In exchange for his contributions, which may be in cash or in kind (going business, equipment, real estate, etc.), the contributor receives shares according to the form of the company, either negotiable stock (in an "S.A.") or not-transferable shares (in an "S.A.R.L."). These are pure and simple contributions.

These contributions are subject to a one percent tax.

But this principle has one exception: contributions of real estate, going businesses, leases or options to lease real estate, are treated like contributions for valuable consideration when they are made to a corporate body subject to corporate income tax,[63] *i.e.*, to an "S.A.," and "S.A.R.L." or a "société en

[63]The income tax rate is 50 percent.

nom collectif" (*i.e.*, a partnership) which has opted for corporate income tax treatment.

2. The contributions for valuable consideration are those the consideration for which is an equivalent protected from risks, for example, contributions in cash not in exchange for shares or the assumption by the company of a contributor's liability.

In these instances the taxes applicable to these contributions are "the transfer taxes" corresponding to the nature of the assets. As an example, the transfer tax is:

- 20 percent for a going business, with the exception of the merchandise which is subject to the V.A.T. (*i.e.*, value-added tax);
- 16.6 percent for a building, with certain exceptions (notably residential buildings, 4.80 percent);
- 20 percent for an option on a building lease;
- 50 F. for a patent whether exploited or not.

In the case of mixed contributions, the tax on pure and simple contributions is applicable to the fraction of the assets the consideration for which is shares, while the transfer tax is payable on the fraction contributed for valuable consideration.

The articles of incorporation must be filed within a month of their execution and the taxes must be paid at the time of filing, subject to the right of payment in installments.

However, in view of the blocking of the funds contributed to an "S.A." or an "S.A.R.L." until the filing of the articles in the commercial registry, the Law of July 12, 1967 (art. 37) provides that the incorporation documents of commercial companies are provisionally registered at the fixed tax of 50 F. The contributions "taxes" normally due to the revenue service are payable only at the end of three months from the date of the documents. Finally, late recording gives rise to a penalty of three percent for the first month and an additional one percent for each subsequent month or fraction of a month or arrears.

VIII. Special Tax Treatment of Company Groups

With a view to encouraging companies to group, the tax law provides two special tax programs, one called "special rules for parent companies," the other "tax consolidation."

The special tax rules for "parent companies" derive from the concept that a parent company and its subsidiaries should not, under the corporate income tax, be more heavily taxed on the profits derived from subsidiaries than on those which are directly generated by the parent company because, together, these companies constitute a single business unit. Therefore, the income of the subsidiaries, when distributed to the parent company, is exempt from further

corporate income tax, having already been taxed. If this exemption were not granted to the parent company, double taxation of the same profits would result for the group.

To have the benefit of this treatment, the following conditions must be met: the parent company must be an "S.A." or an "S.A.R.L."; the holding in the subsidiary must be ten percent at least; finally, the parent company must have French nationality—a debatable condition which is explicable on the ground that this special treatment is established to encourage companies to group in the interests of the national economy. But, in regard to subsidiaries, this condition is neutralized, since they may have either French or any other nationality.

The special "tax consolidation" treatment is allowed to parent companies which own 95 percent of their subsidiaries' stock. Because of the resultant confusion in assets, rights and obligations, the Law of December 24, 1971 permits parent companies to determine their taxable income as if the subsidiaries were merely divisions without legal entity status.

The legislature being empowered to allow the benefits of this treatment in the interests of the national economy only, the parent company as well as its subsidiaries must have French nationality. Moreover the "fiscal consolidation" treatment can only be accorded by order of the minister of the economy and finances when a concentration of enterprises or a reorganization of a group of companies takes place. This condition requires that such a concentration or reorganization present some benefit for the national economy which must especially adapt itself to the requirements of a market enlarged to the size of the European economy.