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Thank you. What, you might well ask, can an economist sandwiched between two eminent academic lawyers possibly contribute to this subject and you might, quite reasonably, answer nothing at all or if nothing at least two views and fortunately this is a subject on which there are two views.

According to the freedom of incorporation view, the country of incorporation does not necessarily have to coincide with the main activity or headquarters of a company whereas, according to the real seat doctrine it does.
The issues that this raises are to what extent does it make sense, is it desirable for incorporation to be separated from activities, will regulatory competition result in runs to the bottom, does it threaten the viability of some of the system wide issues that concern Europe, for example, the viability of some corporate systems as against another and it does it undermine potential attempts to pursue objectives other than those of investor returns and managerial interests, social objectives such as employment.

Now, the debate in the US about which we will hear much more this afternoon has argued that, in principle at least, freedom to move can give rise to efficiency in the design of law. On the other hand, there may be problems in terms of competition as a result of companies wishing to operate together from particular localities as a result of network exponalities and there may be dominant providers in certain states. There are also questions about the extent to which there is effective competition because of federal intervention. So, in a large part of the US the issue has boiled down to being an empirical one as to whether or not it is beneficial in terms of the effect on company evaluations and, for the most part, the evidence that has come out from that analysis is that it is efficient in terms of movement between states and in terms of share price reactions though there are some adverse consequences from introductions of anti-takeover rules in corporate charters and state legislation.

There are, though, important differences between the US and Europe. Essentially US is competition within a financial system or corporate system as against Europe which is competition between very different systems and this gives rise to our potential agency issues, agency conflicts and managerial incentives which are rather different from those in the US. It raises questions about the impact on other investors such as creditors as well as systems more generally and it gives rise to important social issues as well. The underlying observation is that there are significant differences between the structure of financial systems and corporate systems between the US and Europe – much more significant large holdings, block holdings in Europe than in the US, much more pervasive family ownership as against holdings by financial institutions, much more in the way of inter-corporate holdings of one company and another in particular in the form of pyramid structures, existence of dual class shares, voting right restrictions has, at least historically, been much more pervasive in Europe than in the United States and there is, in various circumstances, the use of staggered boards and self-electing boards to entrench management in one form or another.

Finally, there are important differences in the structure of financial markets with the role of banks as against stock markets being quite different and, as a consequence, differences in the capital structure of firms. Those differences give rise to different incentives on management

when one thinks about the freedom of incorporation issue. The greater diversity in terms of system gives rise to greater variation in the potential private benefits of control of management operating in different countries and that may give rise to still greater incentives on management to relocate to what one might term lower investor protection regimes and more opaque systems – more opaque, for example, in terms of executive remuneration about which disclosure varies considerably across different countries.

So, there's a first concern about the incentives that it gives rise to if this is dominated by managerial decision taking. The second issue is in relation to other investors. Given the variety that exists in terms of creditor protection across different European countries, it may be the case that companies seek to relocate as a way of, essentially, transferring value from one type of investor or creditor to other types of investors/shareholders. So, the first conflict that I described was between managers and shareholders. This is a conflict, if you like, between managers and shareholders together and other investors and it also raises broader issues about the extent to which it will be possible for different types of systems to persist. Some systems, as you'll be aware, in Europe rely very heavily on long term relationships between companies and financial institutions and it's questionable whether or not those long term relationships can persist if one essentially has freedom of exit. One area in which, as Eddie described, there are discussions about the merits of freedom exit relate to their tax implications as set out in the Daily Mail case.

There are conflicts between managers and shareholders, conflicts between different types of investors, there are also conflicts between investors as a whole and other stakeholders in the firm. So, the rights of employees differs appreciably across European countries, within some countries employees having representation on the boards of companies and management is perceived as performing a role of upholding these broader stakeholder interests in some countries as against others. There is a concern that there may be incentives for management and shareholders together to shift location in order to be able to take advantage of lower stakeholder protection regimes elsewhere.

The consequences or the concerns that are raised are that incorporation will be dominated by protection of private benefits, that investor protection will as a consequence be weakened, will move over to more opaque systems where financial integration will therefore be undermined, that there's a threat to other investor groups, in particular to creditors, there's a threat to financial systems which depend on long term relations and there's a threat to other stakeholder groups as companies seek to avoid their social obligations. That raises a question as to can anything be done to mitigate those problems and concerns but if one first of all thinks about the potential conflict between managers, on the one hand, and shareholders on the other then one can obviously to some extent mitigate issues by giving shareholders rights of veto on decisions to relocate so that if it's only with the agreement of shareholders – perhaps a supra majority as against a straight majority – to shift location then one might argue that protection, at least some protection, is provided against managerial self interest in seeking relocation. It's not clearly an entirely adequate solution in so far as decisions will still in a large part be initiated by management but at least it does provide a veto over decisions.

Secondly, in terms of the potential undermining of financial integration through moves to opaqueness what I think is a critical element in terms of the operation of freedom of movement is the role of disclosure. That is to say, giving investors the information about the regimes under which companies are operating the types of corporate governance protection that they are getting and that investor protection can play a large part in overcoming issues

associated with undermining financial integration. In terms of other investors, there are questions about the extent to which those can be provided in other forms through, for example, one might give creditors elements of consultation about relocation through corporate law or through private contracts. And, finally, in terms of social objectives, there is an issue as to whether or not these are in any event the proper subject of corporate law or whether or not they should be enshrined in other types of law, for example, in employment legislation instead. Now, these concerns are real concerns but I think that, set against them, one has to appreciate the real potential benefits associated with freedom of incorporation.

Essentially, as I described at the beginning, the real seat doctrine imposes a correspondence of law with location of activities whereas freedom of incorporation allows companies to match appropriate laws, legal regimes, with their activities. It, therefore, exploits the potential diversity of European systems and it allows for a greater diversity in terms of matching of laws with the diversity of activities that are going on in Europe. So, there is the potential for significant benefits associated with the process of freedom of incorporation and financial integration potentially can benefit from this process of freedom of movement through greater disclosure at the same time.

So, in summary, freedom of incorporation allows companies to undertake this matching of systems with corporate activities as well as, as described in the US context, encouraging efficiency in legal design and at least some of the potential adverse consequences may be mitigated through, for example, giving rights to shareholders and other stakeholders to impose vetoes on movement through greater disclosure, through corporate charters, contracts and potentially other legal requirements. So, perhaps rather unusually for a two handed economist, I come down quite firmly in favour of one view and that is the freedom of incorporation. Thank you.