

# THE 5<sup>th</sup> FREEDOM: CORPORATE MOBILITY WITHIN THE EU



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2023 marked 30 years since the establishment of the European Single Market and the introduction of the four fundamental freedoms of movement it embodies: freedom of goods, capital, services, and people. These freedoms have revolutionised our understanding of borders in the Western world, enhancing European values of unification and harmonization in our daily lives.

Keeping to the theme, Directive (EU) 2017/1132 consolidated a significant portion of European Union (EU) company law rules into a single directive that covers issues like the formation of companies, capital and disclosure requirements, and their operational procedures.



As economic progress continued unabated, the need for healthy and flourishing companies that could promote economic growth and attract further investments into the EU increased. In response, Directive (EU) 2019/2121 of the European Parliament and of the Council of 27 November 2019, amends Directive (EU) 2017/1132 to address cross-border conversions, mergers and divisions (the "Directive"). This Directive, as an extension or facilitator of the freedom of establishment and considered the 'fifth freedom', enhances the mobility of companies within the internal market. It enables them to reorganize their operations across borders more easily while maintaining their legal identity and perhaps include a functional aspect of corporate freedom of movement alongside the existing four freedoms.

According to the explanatory memorandum of the European Commission:

*'...companies need to operate in a legal and administrative environment which is both conducive to growth and adapted to face the new economic and social challenges of a globalised and digital world.'*

## **The Directive outlines several key provisions:**

**1. Cross-border Conversions:** It sets out rules and procedures for companies within the EU to convert their legal structure while preserving their corporate identity. This includes converting a company from one member state to another without the need for winding up the company and establishing a new one. The Directive also implements safeguards to protect the interests of shareholders, employees, and creditors throughout this process.

**2. Cross-border Mergers:** The Directive streamlines the merger process for companies operating in different member states, allowing them to consolidate their operations and resources across borders. It provides clear guidelines on necessary steps, including shareholder approval, creditor protection, and compliance with relevant regulatory requirements.

**3. Cross-border Divisions:** Companies are granted the ability to split into two or more separate entities across different member states, with provisions to ensure transparency, fairness, and legal certainty throughout the process. This allows companies to restructure their operations more efficiently and adapt to changing market conditions while maintaining compliance with EU laws and regulations.

**4. Protections for Stakeholders:** The directive prioritises the protection of stakeholders, including shareholders, employees, and creditors, by requiring companies to adhere to strict transparency and disclosure requirements. It emphasises the need for companies to provide adequate information and consultation to affected parties during cross-border operations.

The Directive represents a significant step towards facilitating cross-border business activities within the EU while ensuring robust legal frameworks and protections for all stakeholders involved. By harmonising rules and procedures across member states, the Directive aims to promote economic growth, competitiveness, and stability within the European single market.

The implementation of the Directive in Cyprus is likely to have several notable impacts on the country's business environment, corporate governance landscape, and legal framework:

**1. Increased Cross-Border Business Activity:** With streamlined procedures for cross-border conversions, mergers, and divisions, Cypriot companies will have greater flexibility to expand their operations beyond national borders. This could lead to an increase in cross-border business activity, as companies seek to capitalise on opportunities in other EU member states.

**2. Enhanced Competitiveness:** The ability to undertake cross-border operations more efficiently could enhance the competitiveness of Cypriot companies in the European single market. By facilitating mergers, divisions, and conversions, the Directive may enable Cypriot companies to consolidate resources, access new markets, and achieve economies of scale more effectively.

**3. Improved Legal Certainty:** The Directive provides clear guidelines and procedures for cross-border transactions, offering greater legal certainty for companies operating in Cyprus. This clarity can help mitigate risks associated with cross-border operations and enhance investor confidence in the Cypriot market.

**4. Stakeholder Protections:** The Directive includes provisions to safeguard the interests of stakeholders, including shareholders, employees, and creditors, during cross-border transactions. Companies registered in Cyprus will be required to adhere to these protections, ensuring transparency, fairness, and accountability throughout the process.

**5. Challenges and Adaptation:** Despite the potential benefits, implementation of the Directive may also present challenges for Cypriot companies, particularly in terms of understanding and complying with new regulatory requirements. Companies may need to invest in staff training, legal advice, and administrative resources to ensure smooth adaptation to the new rules.

Under the existing Companies Law, CAP 113, the matter of cross-border mergers is properly regulated in line with the provisions of Directive (EU) 2017/1132 in sections 201Θ to 201KZ of the Companies Law. The issue of transfer of seat/migration of a company from or to Cyprus is regulated in sections 354A to 354IH of the Companies Law provided that the laws of the other country (incorporation or hosting jurisdiction) permit it.

The cross-border division provisions, as introduced by the Directive, represent a significant breakthrough for the Cyprus legal corporate system seeing as the Companies Law only addresses local divisions/demergers in the context of 'reorganisations', which lacks the cross-border element necessary for international restructurings and flexibility for corporations.

Overall, the implementation of the Directive in Cyprus is expected to bring both opportunities and challenges for the country's business community. Upon transposition of the Directive into local legislation, Cypriot companies can better position themselves to capitalise on the benefits of increased cross-border integration within the European single market.