FOREIGN INVESTMENTS: ON THE EDGE OF PUBLIC AND PRIVATE LAW*

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Investing into a foreign country always requires risk management and preliminary research in order to identify a favorable legal and economic environment for the prospected activity. This presumption enacts various duties to the host state in case it wants to accept foreign investors. It is, however, a very complex and sensitive question and presumes a coordinated cooperation among multiple areas of legislation. Many think that taxation is the exclusive method to lure foreign investors in and to show them how open the country is to foreign investments. In practice, foreign investors examine a lot more than just taxation and they often pay attention to the company law regimes and protective measures or guarantees the state is willing to provide in case of unfavorable events (eg. insolvency, creditor arguments).

The purpose of modern company law is to provide an effective framework for conducting business activities in a legally regulated and transparent form, and also to provide protection to several interest groups, such as the shareholders against the company's management, minority shareholders against the decisions of the majority, and creditors/business partners against the company and its assets in general. A foreign investor may most likely take these factors into consideration when deciding on establishment in one country or the other. Modern day company laws in Europe seem to follow different paths. Some believe in a very flexible form of company regime, while others still tend to keep mandatory rules and guarantees alive even in the 21st century. The purpose of this study is not a deep analysis on the advantages or disadvantages of the two different regimes but a short introduction on what the potential foreign investors may see in one system or the other.

The European Union continuously puts the member states under pressure and try to make them accept a more standardized or harmonized system of company law. So far, there has not been a major breakthrough in this respect as the already adopted directives only deal with basic questions, leaving an almost unlimited freedom to the member states to develop their company laws the way they wish. A foreign investor is most likely looking for a predictable and secure legal environment, where maneuvering in the market has clear boundaries while the law still provides the option of reasonable flexibility. Before we jump into a conclusion that flexible company laws that are considered less secure to creditors hit the jackpot here, we should get back to square one: the question of establishment. Establishing a company always requires some core capital that is typically coming from the founders, the first shareholders of the company. This core capital may seem to be a simple legislative decision from the angle of private law, however, it truly has deep connection with policy considerations.

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Classic company law in the 19^{th} and the early 20^{th} centuries treated capital requirements as safeguards to the creditors and bails in exchange for the limited liability of the shareholders. Today, it is more of a political decision than a legal one, therefore, the public nature of the capital requirements is more eminent than the private considerations behind their regulation. Foreign investors are willing to invest a certain capital that they determine based on the prospected starting expenses of the activity. Their mind is not set to look for the legal limbo on that issue, they rather make economic analysis on the problem and then see a system that fits in. For the first look, laws with symbolic or no core capital requirements may seem to be the ones that completely abolished this once very important factor of the establishment problem and creditor protection. In fact, they solely rely on the market and they let the market determine the amount of money certain activities require for a start. These systems treat the investors and their future business partners – the future creditors – as adults and true professionals. While the law provides endless freedom to the investors and founders, their bad choices may result in serious economic consequences. If the desired activity bears a huge risk and calls for a decent deposit in the market, pennies would not be sufficient to enter into the market. Other factors like the crowded nature of the given market full of competitors and potentially rival companies may also come to consideration when deciding over the capital. In these systems, the legal type of the prospected company has very little to do with the amount company law requires for a start. It is more determined by the activity and market conditions. Even in such regimes, the law imposes strict minimums for activities that bear high risks to a significant group in the society (eg. insurance, financing). These barriers are, however, independent from the company type and the general considerations of shareholder liability or creditor protection, they are more dependent on public policy. This method is also present in those systems where a general minimum of core capital is regulated for each company type. The selected activities and the individualized core capital regulations merit from the same ground: to protect public interests in the given sectors.

Another important angle to foreign investors is the security of their investment under the selected company type. The limited liability company types are the most popular forms for foreign investments as they guarantee a loss-minimization right at the beginning. The foreign investors only risk what they were willing to invest as a contribution to the venture. Future debts do not impose burdens on their private assets. It seems to be an understandable need as very few investors are willing to take major risks, especially in an unknown territory. One of the new phenomenon of company laws in Europe in the 21^{st} century is the continuously increasing number of liability norms that seem to threaten or – in some cases – undermine this assumption. After inventing the corporate veil concept, we had to find tools to penetrate it for the greater good: to protect creditors against fraudulent company and shareholder activities. The recent financial crisis generated an increased number of insolvency procedures and liquidations. We could not treat limited liability companies as absolutely independent legal entities, independent from their shareholders. In insolvency law and in company law, we can identify plenty of clauses that may shift the otherwise protected status of the shareholders in cases when they fraudulently caused the insolvency of the company they own. As life is more colorful then words, these shifter clauses are rarely exact.

Open clauses and general rules govern this area of company law providing a fair discretional power to the courts even in civil law legal systems. We experience that in certain cases, judges tend to follow policy considerations (eg. an increased need for accountability instead of leaving obligations unsatisfied; general assumptions that foreign investors or the foreign parent companies can survive the loss) when interpreting these clauses rather than the classic governing principles (creditor protection, bona fide – male fide) of private law.

While scholars of international business law tend to emphasize that foreign investments should be protected against political turmoil, hostile governments, unstable political regimes or the unlawful and extensive practices of eminent domain, we believe that foreign investors also have to take a deeper look at the policy considerations behind the rules of company law. This can prove an attitude how business activities are treated in the host country and how open and welcoming the prospected territory of the venture toward foreign investors. It certainly gives a better and clearer picture for risk assessment too. The European idea on the dichotomy of private and public law is somewhat blurry these days, and company law is a great example to back up this statement.

Where does Hungary stand in this debate? The new Civil Code (Act V of 2013) certainly made the problem multi layered and complex. In Europe, the Hungarian Civil Code seems to be the most flexible code on company law in terms of providing an almost unlimited option for derogation (Article 3:4). If we take a closer look, the flexible and open clauses can easily become traps to foreign investors as they adumbrate an unpredictable attitude of the courts upon registering a company and even on the questions of shifting shareholders' liability in litigation. It does not pamper investors with a secure and predictable company law environment, rather, it places a great deal of trust in the hands of judges who may be open for serving public policy agendas instead of deliberating in individual cases. If a foreign investor is looking for a regime where the structure and the operation of the company can be largely customized by his needs, Hungary is definitely a good place. If the foreigner wants to secure a no-risk policy for his venture, he may be better off waiting a bit more to see how the courts will use the suddenly earned trust of the legislator. The ongoing projects for the revision of the company law rules in the Civil Code also do not encourage foreign investors and these may also easily deliver a bad message to the courts: company law is purely dependent on the policy considerations of the legislator and does not follow private law principles and theories, therefore, it can be changed whenever the legislator wishes to enforce its will in a specific question. The manifestations of such policy changes can only be wise and cautious if they do not happen too often, and they step beside the already existing rules instead of knocking them out, resulting in a coherent regime.