Mandatory Corporate Law as an Obstacle to Venture Capital Contracting in Europe: Implications for Markets and Policymaking

Luca Enriques (*)
Casimiro A. Nigro (**)
Tobias H. Tröger (***)

Forthcoming in the *Elgar Research Handbook on the Structure of Private Equity and Venture Capital* (Brian Broughman & Elizabeth De Fontenay eds., 2025)

March 2025

(*) Bocconi University, Department of Legal Studies; ECGI; EBI (*luca.enriques@unibocconi.it*).

(**) Leeds University, School of Law; Goethe Universität, CAS on the Foundations of Law and Finance; LUISS "Guido Carli" (*c.a.nigro@leeds.ac.uk*).

(***) Goethe Universität, CAS on the Foundations of Law and Finance; the Leibniz Institute for Financial Research SAFE; ECGI; EBI (*troeger@jur.uni-frankfurt.de*).

We wish to thank Brian Broughman for the excellent comments to an earlier draft. We acknowledge our debt to the many people whose comments have greatly improved the output of this project in one of the companion papers. Casimiro Nigro and Tobias Tröger gratefully acknowledge research support from the Leibniz Institute for Financial Research SAFE and the Center for Advanced Studies Foundations of Law and Finance funded by the German Research Foundation (Deutsche Forschungsgemeinschaft, DFG) - project FOR 2774.

Abstract

Policymakers around the globe have sought to stimulate Venture Capital (VC) investments, and an extensive literature has inquired into the institutional determinants of a vibrant VC market, including corporate law.

We contribute to that literature by exploring the significance of corporate law for VC contracting and hence VC investments. Corporate law's relative rigidity or flexibility is key to the efficiency of the contractual technology governing VC deals. Importantly, it can hamper such transactions through a number of "constraints," which we have identified in a companion paper. To illustrate our point, in another companion paper, we take German and Italian corporate laws as two case studies and show how they are largely averse to VC contracting. In addition, we show that the regulatory constraints they impose stem from blackletter corporate law much less often than from scholarly constructs and courts' interpretations.

This chapter anticipates two objections that cast doubt over the importance of our findings as to the construction of vibrant VC markets in Germany and Italy. Specifically, the first of these objections is that VC funds and entrepreneurs planning to run their startups in Germany and Italy can circumvent the strictures of local corporate laws by incorporating abroad, and the other is that formal contracts are inconsequential in VC deals, meaning that the regulatory constraints we document are irrelevant. Meanwhile, the chapter also shows that the detailed understanding of regulatory constraints unveiled by our research can inform more effective policymaking. Ultimately, we make two policy recommendations: first, we propose the adoption of a statutory provision that would explicitly insulate the arrangements that typically shape U.S. VC deals from undue interventions; and, second, we argue in favor of a standard charter aligned with U.S. VC transactional practice that the law itself should declare entirely enforceable.

Keywords: Comparative Corporate Law; Comparative Corporate Governance; Entrepreneurship; Financial Contracting; Private Ordering; Startups; Venture Capital; Entrepreneurial Finance.

Classification: G38; K22; L26.

Summary

INTRODUCTION

Policymakers across the globe have attempted to spur venture capital (VC) investments and an extensive literature has inquired into the institutional determinants of a vibrant VC market, which is considered an important driver of innovation and growth.

We contribute two pieces to that literature. In Enriques, Nigro, and Tröger (2025a), we have explored the significance of corporate law for VC contracting and investments. In particular, we have revisited the argument that corporate law affects VC contracting because of its flexibility or lack thereof, and isolated the channels through which corporate law's rigidity affects the adoption of the presumptively efficient contractual technology governing VC deals in the U.S. and/or the exercise of the ensuing rights.

Meanwhile, in Enriques, Nigro, and Tröger (2025b) we have shown: that the corporate law regimes "in action" in two key European jurisdictions, namely Germany and Italy, impose myriad constraints on VC funds (VCFs) and entrepreneurs attempting to transplant the U.S. VC contractual technology into their home jurisdictions; that, rather than from blackletter law itself, these constraints stem much more often from normatively charged implicit rules and standards that scholars derive from blackletter law and that practitioners and courts in their different capacities apply; and that the corporate law directives and regulations passed by the European Union (E.U.) play a very limited role in this process.

In this chapter, we address some critical questions raised by our findings. In particular, does it matter that the corporate law regimes in force in Germany and Italy stand in the way of using the contractual framework governing VC deals in the U.S.? Are our findings relevant to the purpose of engineering vibrant VC markets in Germany and Italy and, insofar as these two countries' corporate law frameworks are representative of a broader phenomenon, elsewhere? If better (i.e. more flexible) corporate law is a possible driver of VC investments, what are the implications of our findings for the design of corporate law reforms?

In Part I, we motivate our research by briefly taking stock of the initiatives that policymakers in the E.U. and its member states—including those in Berlin and Rome—have undertaken to stimulate the development of local VC markets, and then accounting for their limited growth relative to the U.S. market. Thereafter, we place our research in the context of the law and finance literature examining the institutional determinants of VC investments. In Part II, we address two essential objections to the real-world relevance of corporate law rigidity for VC contracting. The first such objection is that German and Italian corporate laws do not matter because German and Italian startups can bypass the strictures of domestic corporate law by resorting to foreign corporate vehicles. We counter this objection by arguing that such a move would seldom be cost-effective for VCFs and entrepreneurs, especially for early-stage VC-backed firms. The other objection is that corporate law's impact on contractual arrangements is of no significance because formal contracting itself does not really matter, including in a VC-backed firm context. On the one hand, due to reputational concerns, VCFs and entrepreneurs solve their disputes without resorting to formal enforcement of their contractual rights. If litigation in the VC ecosystem is scarce even in the litigious U.S., it would seem implausible for it to be more frequent in Germany and Italy. On the other hand, VCFs and entrepreneurs, like many other market players, may view formal contracting predominantly as an exercise aimed at outlining their mutual expectations to guide behavior and project exposures, as opposed to defining specified rights that can be enforced before a court. Hence, according to this objection, most of the time it would make no difference whether the formal contractual arrangements shaping VC deals are enforceable. We counter this objection by showing that, first, a mere guiding function of VC contracts is insufficient to resolve typical conflicts between VCFs and entrepreneurs in critical scenarios, and, second, formal contracts' enforceability has a bearing on the financial returns of parties (and especially VCFs), particularly in a downturn.

In Part III, we discuss the implications of our findings for corporate law reform. Policymakers at both the E.U. and member state levels have occasionally acknowledged the importance of corporate law in supporting the development of a dynamic VC market. Yet, at the E.U. level, they have done nothing more than generically encourage member states to make their corporate laws more flexible, while at the member state level, they have passed reforms that have at best tackled only the most patent obstacles raised by the rigidity of corporate laws on the books to the adoption and use of the contractual technology governing VC deals in the U.S. As our research unveils that the vast majority of such obstacles come from corporate law in action, we offer novel insights into how to enact more effective legal reforms in this area. In Part IV, we wrap up and conclude.

I. CORPORATE LAW AND VC

In this part, we motivate our research by accounting for the initiatives undertaken by the E.U. and its member states to support VC investments and the VC investing patterns in the U.S. and the E.U., with a focus on the German and the Italian markets (Section I.A). Then, we briefly place our research in the context of the law and finance literature discussing the determinants of VC investments (Section I.B). Finally, we report our companion papers' findings. First, we revisit the theory that corporate law, depending on whether it is enabling or mandatory, matters as a determinant of VC investments, and offer a primer of the channels through which rigid corporate laws can impair the ability of VCFs and entrepreneurs to achieve their goals through private ordering. Second, we illustrate the significance of our theoretical framework by showing how real-world corporate law in Germany and Italy impedes VC contracting that mimics the contractual technology governing VC deals in the U.S. Third, we stress that the regulatory constraints we document stem almost entirely from implicit requirements that scholars devise mostly by leveraging on domestic corporate law (as opposed to E.U. directives and regulations), and that these requirements then penetrate into transactional practice through the intervention of practitioners assisting parties in VC deals and courts and arbitrators judging on the validity of the arrangements stipulated in VC contracts or the exercise of the ensuing rights (Section I.C).

A. *VC Markets' Development*

VC as we know it started growing exponentially in the 1980s (Nicholas 2019, 143-182). Since then, VC has been associated with increases in innovation, employment, and growth (Kortum and Lerner 2000; Manigart and Sapienza 2000; Samila and Sorenson 2009; Gornall and Strebulaev 2021). The development of a thriving VC market has been a crucial component of the infrastructure facilitating the financing of innovation in the U.S. (Kenney 2011), dubbed as one of the "crown jewels" of the U.S. economy (Gilson 2003, 1068).

It is therefore unsurprising that, over the last 50 years, policymakers around the world have made strenuous efforts to build vibrant local VC markets by initiating public programs or stimulating private initiatives (see, e.g., Gilson 2003, 1093-1101). In the E.U., policymakers—at both the central and national levels—have made repeated attempts at fostering VC investments (Da Rin, Nicodano, and Sembenelli 2011). For more than three decades now, policymakers in Brussels have sought to support the growth of the European VC market by, *inter alia*, expanding capital supply and encouraging capital raising through a variety of policy and regulatory measures (Nigro and Gözlügöl 2022). For example, the Capital Markets Union project initiated in 2014 identified VC as one of the pillars of E.U. capital markets (European Commission 2015 and 2020). Along similar lines, in 2020, E.U. institutions expressed their ambition to transform Europe into "a new startup continent" (European Commission 2021a), and in pursuit of this very aim they recently created a mega VC fund to nurture the next generation of "European Tech Champions" (European Investment Bank 2023).

At the same time, in the last decade, member states' governments, including those in Berlin and Rome, have passed a variety of measures to support the development of national VC markets.[1]

In the same period, the E.U. VC market has grown at an unprecedented rate (Demertzis and Guetta-Jeanrenaud 2022; Bertoni, Colombo, Quas, and Tenca 2019). Yet, some analysts believe that this boom may be primarily due to the favorable economic cycle and market environment (Caselli and Zava 2023), and doubt whether such levels of VC activity can be maintained (Demertzis and Guetta-Jeanrenaud 2022). Moreover, despite the recent massive upswing, overall VC investments in the E.U. pale—just like they did in the past (Kräussl, Krause, and Manigart 2012)—in comparison to the size of the U.S. VC market, which continues to grow at a far higher rate (Figure 1). At the end of 2021, investments by E.U. VC firms totaled less than 50 billion USD, which is less than one-fifth of the 260 billion USD that U.S. VC investors injected into startups in the same year. The German and Italian VC markets were no exception from the E.U. trend.

[1] For instance, in late 2020, the German Ministry for Economic Affairs announced the creation of an investment vehicle with an initial endowment of 10 billion euro. See Bundesministerium für Wirtschaft und Klimaschutz 2020. The fund started its operations in 2023. Similarly, starting in 2012, the Italian government has undertaken initiatives to support private investments in VC and public VC investments, chiefly by recalibrating the applicable tax regime. See Migliocco and Ricotti 2013. In 2022, it expanded existing public VC funds' endowments. See Ministero dello Sviluppo Economico 2022.

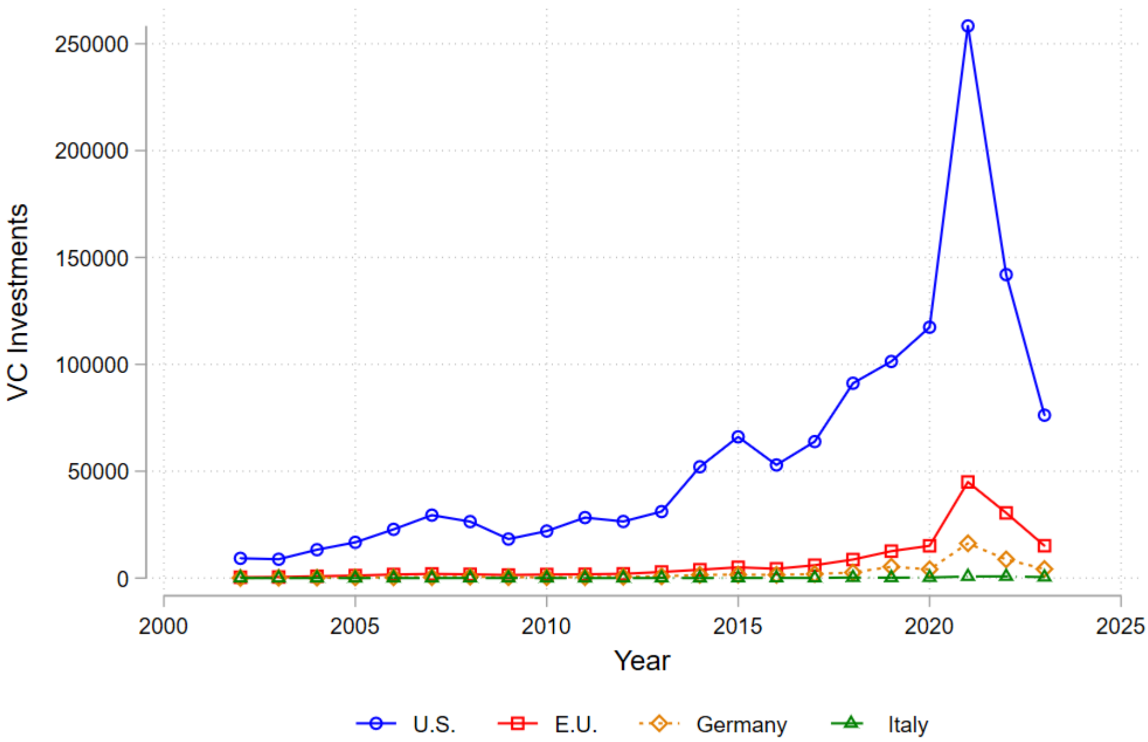

FIGURE 1. VC investments (seed up to L-Series) in the U.S., E.U., Germany, and Italy over the period 2002-2023 (in USD million). Data source: *Preqin*, 2024.

The data on regional and national VC market development in the E.U. look even less benign once VC investments are scaled to GDP (Figure 2). The U.S. VC market attracts funds equivalent to up to more than one-hundredth of the national GDP, while E.U. markets raise far lower fractions of GDP. The German and Italian economies generate significantly less capital for VC investments than the U.S. economy.

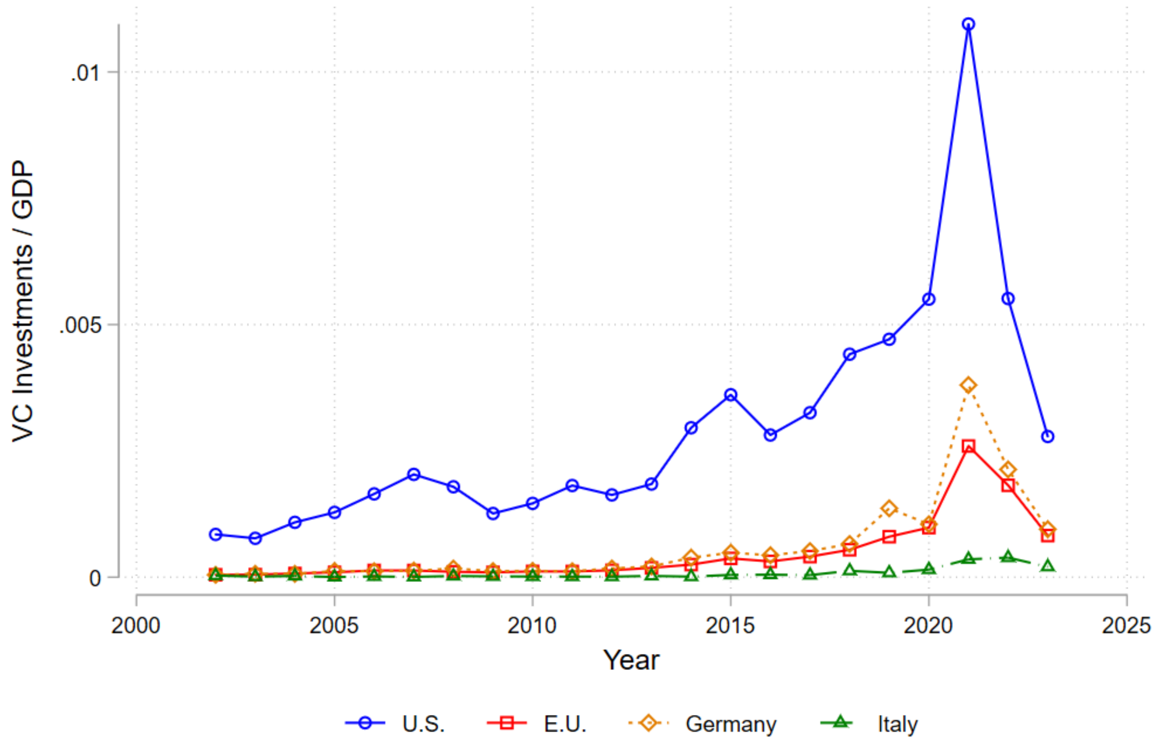

FIGURE 2. VC investments (seed up to L-Series) in the U.S., E.U., Germany, and Italy over the period 2002-2023 scaled to GDP (in USD million). Data sources: *Preqin*, 2024*; World Bank*, 2024.

Available data about the median size of VC deals in the U.S., the E.U., Germany, and Italy also help to gauge the significance of the existing transatlantic gap in VC investments (Figure 3). The median size of VC deals in the E.U. has consistently been smaller than the U.S. VC equivalent. However, for some years in the sample period, the median size of VC deals in Germany and/or Italy was larger than that of U.S. deals. These data points represent outliers, driven by a few exceptionally large deals in otherwise thin markets with a handful of (to be fair: self-reported) transactions. The more stable trend observable in recent years is that the gap has not only become persistent but has widened. In 2006, U.S. (E.U.) VC deals had a median size of 6 (4) million USD. After descending from the exceptional peak in 2021, U.S. (E.U.) VC deals had a median size of 9 (5) million USD in 2023. Even in the bullish market during the record year of 2021, with U.S. (E.U.) median deal sizes of 13 (6) million USD, the gap was wider than in 2006. At the national level, the picture is similar. In 2006, German and Italian VC deals had a median size of 3 and 2 million USD, respectively; in 2023, those figures stood at 6 and 5 million USD, respectively, indicating a persistent and significant delta for individual funding rounds. Only at the 2021 peak did the funding gap narrow for Germany (median VC deal size of 10 million USD), although this was not the case for Italy (median VC deal size of 4 million USD).

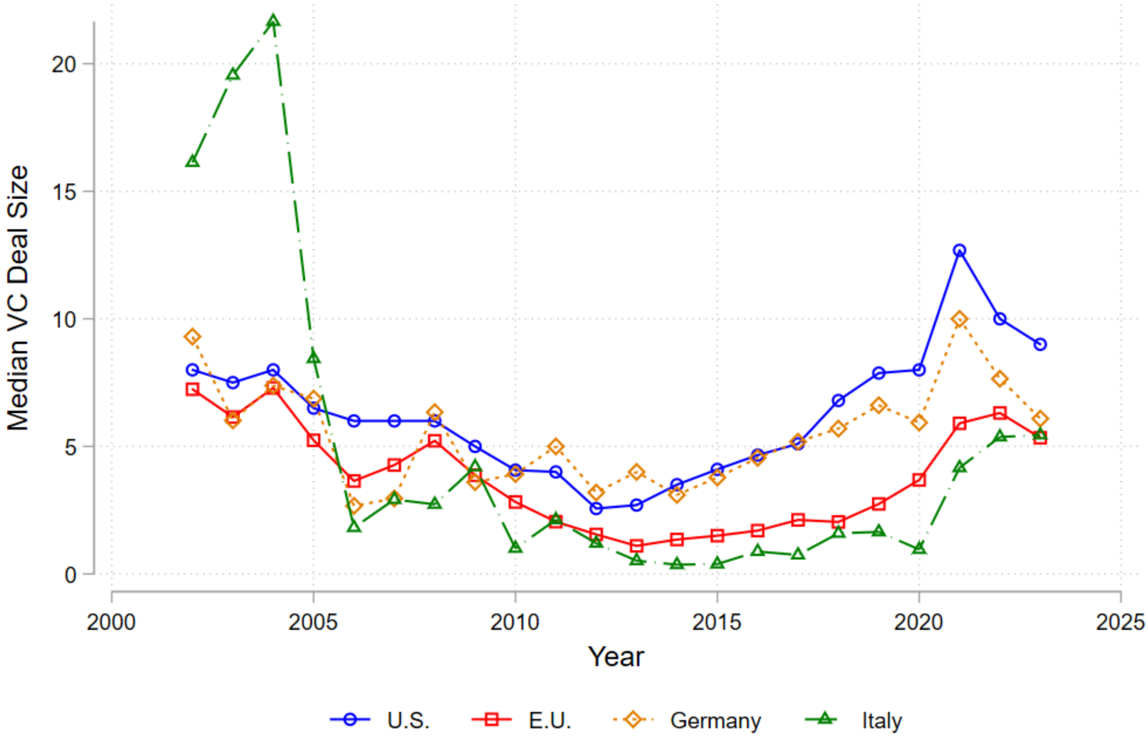

FIGURE 3. Median size of VC deals (seed up to L-Series) in the U.S., E.U., Germany, and Italy, over the period 2002-2023 (in USD million). Data source: *Preqin*, 2024.

B. *Corporate Law as a Determinant of VC Investments: The Law & Finance Perspective*

An abundant law and finance literature has focused on the institutional determinants of VC investments (Grilli 2024), including corporate law. A strand of this literature has drawn from the framework of La Porta et al. (1998) to test the hypothesis that better investor protection correlates with higher volumes of VC investments, but failed to yield consistent results. Three of these studies are relevant to this chapter. First, Bonini and Alkan (2012) found that common law jurisdictions enjoy a competitive advantage thanks to superior investor protection. Second, Lerner and Schoar (2005) reached the same finding but linked it to the greater reliability of contractual enforcement in those jurisdictions, which in their view facilitates the adoption of complex and state-contingent private ordering solutions that are instrumental to the separate allocation of control and cash-flow rights. That, in turn, allows VCFs to lower the monitoring costs associated with investing in different jurisdictions. Third, Kaplan, Martel, and Strömberg (2007) analyzed the impact of legal regimes on VC contracts more granularly and concluded that, among other factors, corporate law's quality does not play a major role. They found "no substantive differences across low and high minority [shareholder] protection countries," because "there appear to be few institutional impediments to implementing U.S.-style [contract] terms," particularly for more experienced venture capitalists (*Id.*, 308).

This last finding stands, however, in stark contrast with anecdotal evidence reported in similar literature about the viability of transplanting U.S. VC contracts into jurisdictions outside the U.S. (Lerner and Schoar 2005). Above all, it contradicts various legal studies that have shown that the corporate law regimes of many jurisdictions—from Europe to Latin America to Asia—often obstruct the transplant of the individual components of U.S. VC contracts (for Germany, Baums, and Möller 1999, and Kuntz 2016; for Italy, Giudici and Agstner 2019, Agstner, Capizzi, and Giudici 2020, and Nigro and Enriques 2021; for China, Lin 2020; and for various other jurisdictions, Pereira 2023).

These studies align with two fundamental intuitions about the corporate law-VC nexus, namely that: (a) private ordering is key to building a VC market (Klausner and Litvak 2001; Gilson 2003); and (b) corporate law's flexibility is key to allowing VCFs and entrepreneurs to allocate cash-flow and control rights as they see appropriate in order to mitigate the frictions associated with the financing of highly innovative and risky projects (Armour 2003; McCahery and Vermeulen 2003).

C. *Our Findings*

Building on those intuitions and findings, we develop a more articulate and nuanced theoretical framework to explain how corporate law's flexibility affects VC contracting and investments, and illustrate our hypothesis by using Germany and Italy as case studies serving as a contrast to the U.S. paradigm. In one of our companion papers, we revisit the idea that corporate law's flexibility (or lack thereof) matters by identifying the channels through which rigid corporate law affects VC contracting and, possibly, discourages investments (Enriques, Nigro, and Tröger 2025a). In the other companion paper, we look into how the German and Italian corporate law regimes in action hinder the transplant of the contractual framework governing VC deals in the U.S. into these jurisdictions (Enriques, Nigro, and Tröger 2025b). This section summarizes the results of our research.

In Enriques, Nigro, and Tröger (2025a) we build on the premise that sophisticated market participants, especially when aided by specialized legal counsel, can protect their own interests, to define corporate law as optimally flexible for VC contracting if it (a) adopts a hands-off approach regarding the enforceability of private ordering solutions that shape VC transactions, (b) refrains from employing ex post gap-filling mechanisms that might restrict the exercise of parties' rights in ways inconsistent with the economic rationale of their agreements, and (c) punishes the abusive exercise of such rights, where abuse is defined as self-serving behavior that violates the economic rationale of the VC deal. The expansion of private ordering enhances contracting parties' ability to delineate their rights and obligations with certainty, thereby confining legal uncertainty to isolated instances.

Delaware corporate law in action aligns almost perfectly with that model. The interaction of several elements within the local institutional environment—including an enabling statute and meta-rules favorable to private ordering—has resulted in a corporate law regime characterized by three principal features.

First, Delaware corporate law has a long-standing tradition of adopting a largely deferential approach to private ordering, regarding arrangements contained both in a firm's constitutional documents and in shareholder agreements,[2] even in the context of startups,[3] with only rare deviations from this norm.[4]

Second, Delaware courts have generally interpreted VC contracts in a manner that aligns closely with the underlying functional logic of the given contracts. Consequently, they have refrained from imposing fiduciary standards in ways that might undermine the exercise of contractual rights arising from the VC agreement.[5] In a more recent development, potentially aimed at mitigating the distorting effects of the well-known *Trados* doctrine,[6] contracting parties have been authorized to utilize private ordering to delineate the prescriptive content of

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[2] Cf., e.g., *Jones Apparel Group v. Maxwell Shoe Co.*, 883 A.2d 837 (Del. Ch. 2004), at 845 (affirming the validity of a charter provision that establishes that the record date for any consent solicitation of stockholders shall be the date on which the first consent is delivered to the company). See also *Manti Holdings, LLC v. Authentix Acquisition Co., Inc.*, 2021 WL 4165159 (Del. Sept. 13, 2021), at 48 (confirming the enforceability of waivers of appraisal rights, contingent upon passing a reasonableness test. Specifically, the waiver must (i) be clearly articulated, (ii) be part of a written contract entered into with actual consent, (iii) involve sophisticated stockholders who fully understand the provision's implications, (iv) provide the opportunity to reject the provision, and (v) be agreed upon for bargained-for consideration, as reflected in other contractual terms).

[3] For examples of private ordering solutions that are typical in VC deals that Delaware courts have upheld thus far, see—in addition to the case law cited in the previous foonotes and *infra*, note 7—*In re Appraisal of Ford Holdings, Inc. Preferred Stock*, 698 A.2d 973 (Del. Ch. 1997) (confirming the validity of an arrangement in the firm's constitutional documents imposing a cap on the price that preferred shareholder would receive by exercising their appraisal rights).

[4] One such rare instance was when the Delaware courts ruled on reportedly "extreme" private ordering solutions that in the aggregate would have had the practical effect of depriving the board of its core function. See *West Palm Beach Firefighters' Pension Fund v. Moelis & Co.*, No. 2023-0309-JTL (Del. Ch. Feb. 23, 2024) (invalidating various provisions in an unusual shareholder agreement assigning extremely broad veto rights to a shareholder). The Delaware legislature "reversed" Moelis by amending the Delaware General Corporation Law. *See, e.g.,* Mark Lebovitch, *The Drama Around Moelis and New DGCL Section 122(18) Just Got Hotter*, CLS BLUE SKY BLOG, Nov. 18, 2024, at https://clsbluesky.law.columbia.edu/2024/11/18/the-drama-around-moelis-and-new-dgcl-section-12218-just-got-hotter/.

[5] The best example in this respect comes from the judicial endorsement of the "control-contingent approach," as it can be gauged from the joint reading of two notable cases—*Orban v. Field*, No. 12820, 1997 Del. Ch. LEXIS 48 (Apr. 1, 1997), and *Equity-Linked Investors, L.P. v. Adams*, 705 A.2d 1040 (Del. Ch. 1997). In brief, the control-contingent approach implies that, if the interests of the VCF *qua* preferred shareholder and the entrepreneur *qua* common shareholder conflict, the party who is in control of the board can take decisions that are inimical to the other party, provided that such decisions are held to be in the best interest of the firm. For details see Jesse M. Fried and Mira Ganor (2005).

[6] *In re Trados, Inc.*, 73 A.3d 17, at 40-41 (Del. Ch. 2013).

the duty of loyalty according to their preferences.[7] This approach modulates the use of ex post gap-filling tools in a manner consistent with VC contracts.[8]

Third, Delaware courts do not shy away from addressing the abusive exercise of rights arising from the contractual arrangements that structure VC deals.[9]

The consistent application of Delaware corporate law to ensure the enforcement of promises made through private ordering allows contracting parties to define their rights and obligations with greater certainty.[10] As a result, legal uncertainty is largely confined to isolated instances.[11]

VCFs and entrepreneurs have levered the properties of Delaware corporate law to engineer a complex contractual framework that pursues two fundamental goals. First, VC contractual arrangements address the severe problems of uncertainty, information asymmetries, and moral hazard that characterize the funding of highly innovative projects. Contracting can mitigate the inefficiencies looming under corporate law's default rules by improving incentives to share information promptly and accurately, encouraging optimal effort, and reducing the risk of opportunism through various powerful "carrot-and-stick" mechanisms.

Second, private ordering solutions are instrumental to aligning VC-backed firms' lifecycles with the organizational and operational features of VCFs. As strategic investors, VCFs have strong incentives to support inter-firm information flows and facilitate the creation of synergies that may increase overall portfolio returns. To this end, they value information and resource exchanges among portfolio companies to facilitate inter-firm alliances, as well as having discretion in allocating funds and business opportunities across those firms. In addition, because the entrepreneur is key to the venture's success and the VCFs invest with a view to cashing out (at the latest) before the VC fund is wound down, VCFs need arrangements that

[7] In one recent decision, the Delaware judiciary has in fact held a shareholder-specific contractual waiver of the duty of loyalty as valid, so long as it is explicit and narrowly tailored to apply to a specific transaction, and subject to the reasonableness review envisioned and deployed in *Manti* (see *supra*, fn. 3). Yet, it has also stated that in no event can a party contractually waive claims arising from an intentional tort. See *New Enterprises Associates 14, L.P., et al. v. George S. Rich, Sr., et al.*, A.3d, 2023 WL 3195927 (Del. Ch. May 2, 2023), at 129.

[8] The case law cited to in the previous footnote appears to have restored contracting parties' ability to shape fiduciary duties in a way that is consistent with VC contracts' functional logic. The National Venture Capital Association has therefore included these waivers in the Model Legal Documents. See National Venture Capital Association 2024.

[9] See *Basho Technologies Holdco B LLC v. Georgetown Basho Investors LLC*, C.A. No. 11802-VCL (Del. Ch. July 6, 2018).

[10] Cf., e.g., *Ascension Ins. Hldgs., LLC v. Underwood*, 2015 WL 356002 (Del. Ch. Jan. 28, 2015), at 4 ("[Delaware corporate law] respects the right of parties to freely contract and to be able to rely on the enforceability of their agreements; where Delaware's law applies, with very limited exceptions, our courts will enforce the contractual scheme that the parties have arrived at through their own self-ordering, both in recognition of a right to self-order and to *promote certainty of obligations and benefits*.") (emphasis added).

[11] As evidenced by the emergence of the *Trados* doctrine, legal disruptions are not unprecedented. However, such disruptions are not only infrequent but also transient. The conditions allowing contracting parties to rely on private ordering to define their business relationships with certainty are swiftly reinstated through subsequent case law (*New Enterprises*, *supra*, note 7), thereby mitigating legal uncertainty once again.

both lock-in their partnership with entrepreneurs at the initial stage of the joint endeavor *and* give them control over exit decisions.

Through decades of iterations, the contractual framework governing VC deals in the U.S. has reached high levels of standardization and complexity. In addition to being the closest to the predictions of financial contracting theory that transactional practice has thus far engineered, the framework has remained largely unchanged over investment cycles and across VC-backed firms' sectors. Moreover, it has more recently become the contractual underpinning of startup-financing relationships outside the VC industry as well. These observations suggest that U.S. VC contracts are, if not optimal, at least the best real-world arrangement available to the parties in VC investment relations. Consistent with this hypothesis, economic theory predicts that U.S.-style VC contracts should gain popularity across jurisdictions over time, serving as a model for value-enhancing private ordering. To date, transactional practice across the globe has in fact been consistent with those predictions.

Corporate law, however, can limit the ability of VCFs and entrepreneurs to transplant VC contract clauses developed in U.S. transactional practice. The more prescriptive a given corporate law is, the harder it is for contracting parties to transpose such clauses into their contracts. Thus, contracting parties need to resort to alternative arrangements. Yet, corporate law often hinders functionally equivalent arrangements as well—that is, arrangements that enable contracting parties to achieve (1) the *same practical result* as the model solution (2) *without incurring higher costs*. Thus, contracting parties have to content themselves with arrangements lacking either or both of these features and are therefore inferior (hereinafter referred to as alternative arrangements).

Rigid corporate law can prevent contracting parties from resorting to private ordering to allocate control and cash-flow rights as they see fit through a number of constraints. In Enriques, Nigro, and Tröger (2025a), we describe these constraints, explaining that they can be qualified as either "absolute" or "relative" prohibitions.

Absolute prohibitions rule out not only the relevant U.S. clause itself, but also, possibly via general anti-evasion principles, any meaningful alternative arrangements. For example, under neither German nor Italian corporate laws can private ordering provide for automatic and cumulative dividends or any alternative arrangement, which are used to grant downside protection in U.S. VC deals.

Relative prohibitions rule out the viability of a specific U.S.-style private ordering solution and functionally equivalent solutions but nevertheless allow contracting parties to resort to alternative arrangements. Bad leaver provisions provide an illustration of how rigid corporate law can mandate the integration of the original U.S. clause with additional provisos that reduce their effectiveness. They are in fact legal only if the price paid to the misbehaving entrepreneur for their shares is above a fairness threshold, because both German and Italian corporate laws are interpreted as including the rule that divestments can only be forced at a "fair" price—which ultimately reduces the disciplining effect of these arrangements.

In addition, we show that corporate law rigidity can be enhanced if rules of interpretation grant scholars and courts wide discretion in "finding" implicit mandatory rules that go well beyond what statutory law may state, and argue that this reduces the value to the parties of any private ordering solution.

Where constraints of this kind limit market participants' freedom to determine the terms of their contracts, they can only enter into VC deals under a suboptimal contractual framework, which implies an increase in VC-backed firms' cost of capital and, at the margin, should reduce the number of VC deals and lead to a thinner VC market with negative ramifications for innovation and economic growth.

In Enriques, Nigro, and Tröger 2025b, we comprehensively analyze German and Italian corporate laws to ascertain the extent to which they stand in the way of the adoption and use of the private ordering solutions shaping U.S. VC deals and contracting parties' ability to exercise the ensuing right in a way that is consistent with the economic logic motivating their deal. To do so, we look at corporate law in action, which we define as the set of corporate law rules that are either spelled out in the blackletter law or result from the interpretations made by German and Italian legal scholars, practitioners, courts, and arbitrators on the basis of their doctrinal analyses. The consideration of the law in action here is key to gaining a reliable understanding of the institutional environment that shapes transactional practice.

In both jurisdictions, rules of interpretation enable gatekeeping practitioners and courts to hold contractual provisions null and void well beyond what, on the face of it, blackletter law would warrant. Ultimately, legal scholars and courts are driven by a deeply ingrained distrust in market-based, uncoordinated, and bottom-up solutions. Their interpretations affect VC contracting via either (i) legal gatekeepers—such as lawyers and notaries—who shape transactional practice or (ii) rulings of enforcers—namely, courts and arbitrators—that strike down contractual clauses inconsistent with such interpretations. Importantly, we find that the constraints limiting contracting parties' ability to design agency cost-minimizing governance structures predominantly stem from domestic corporate law requirements rather than from E.U. corporate law directives and regulations and the interpretations thereof.

The corporate law regimes in force in Germany and Italy manifestly depart from our conceptual model of VC-friendly corporate law. In fact, German and Italian corporate laws, as we document in our companion papers (Enriques, Nigro, and Tröger 2025a and 2025b):

(a) are averse to the transplant of the private ordering solutions shaping VC deals in the U.S. and do not allow for functionally equivalent arrangements;

(b) marshal rules and standards that courts can leverage to second-guess the exercise of the rights ensuing from the VCF-entrepreneur contract with no questions asked as to whether their review is any way consistent with the parties' ex ante mutual expectations of accepted behavior; and

(c) define abuse as behavior in contrast with broad, abstract standards that are often not adapted to the peculiar economic rationale of individual corporate contracts.

As an outcome, the largely unpredictable ways in which corporate law will make it into the VCF-entrepreneur contract imply a significant degree of legal uncertainty, which in turn means that contracting parties cannot fully rely on contracts as a tool to define their expected behavior.

The ultimate result is that German and Italian corporate laws have an adverse impact on the adoption and use of the contractual technology governing VC deals in the U.S. in Germany and Italy. Our companion paper shows that German corporate law only allows for waivers of the corporate opportunity doctrine and tag-along rights provisions, and that Italian corporate law only allows for tag-along provisions. All the other arrangements that typically comprise U.S. VC deals are unviable, whether as such or as functionally equivalent solutions, under both German and Italian corporate laws. Accordingly, VCFs and entrepreneurs in Germany and Italy have no other option than to seek to replace them, to the extent possible, with alternative arrangements.[12].

Convertible preferred shares—the backbone of U.S. VC deals—are perhaps the most significant example here. Due to implicit corporate law requirements that, according to predominant German and Italian doctrinal scholarship, define the key features of a share in a corporation, such securities are inconsistent with the two countries' corporate law regimes. To mention just one of the many hurdles to convertible preferred shares, conversion rights are illegal chiefly because: (a) under German corporate law, they create uncertainty as to the actual position of an investor in the firm and thus clash with the "informative function" of the firm's constitutional documents; and (b) under Italian corporate law, they are, *inter alia*, incompatible with the idea that a share must always, from its very inception and throughout its entire existence, incorporate the right to share in the firm's upside. VCFs and entrepreneurs bargaining under German and Italian corporate laws have therefore envisioned arrangements that, in spite of some scholars' views, are not functionally equivalent.

To conclude, market players bargaining in the shadow of German and Italian corporate laws face regulatory constraints that strongly curb their ability to avail themselves of U.S. arrangements (and of functionally equivalent solutions), and compel them to settle for alternative arrangements.

Although we cannot quantify the efficiency losses stemming from the impact that corporate law's rigidity has on VC contracting, we provide systematic and tangible evidence that the functional gap we document is large and thus has plausibly significant consequences for contract functionality.

[12] Seeking such alternative arrangements is the only option available when the costs forming a corporation in a friendlier jurisdictions, such as Delaware, are higher than the benefits from the relevant arrangements. Judging from the absence of migration patterns among VC-backed companies in Europe (see *infra*, Part II.A), this appears to be the case in Germany and Italy. These arbitrage costs in fact can be thought of as the upper bound on the costs (in terms of lower functionality) of alternative arrangements. The fact that scaling-up VC-backed firms sometimes do reincorporate abroad (see *infra*, Part II.B) is consistent with this intuition.

II. DOES RIGID CORPORATE LAW MATTER FOR GERMAN AND ITALIAN VC MARKETS?

Two objections may cast doubt on the relevance of our findings. First, one may argue that our findings have no real-world significance because German and Italian market players could simply sidestep the constraints stemming from the rigidity of the domestic corporate law regimes by incorporating the VC-backed firm or its holding company in a foreign jurisdiction. The second objection is that the constraints that corporate law imposes on contracting parties are of no real-world importance because formal contracting does not have any bearing on the VCF-entrepreneur relationship. In this part, we show that German and Italian VCFs and entrepreneurs have limited incentives to opt out of domestic corporate law (Section A), and that formal contracting *does* matter (Section B).

A. *Domestic Corporate Law as the Sole Legal Product Available*

The VC-backed firm's domestic corporate law is only significant for VC investments if VCFs and entrepreneurs cannot select an alternative legal product to directly or indirectly circumvent the strictures of local corporate law by incorporating the firm or its holding company in another jurisdiction more hospitable to private ordering. We argue that, at least for early-stage ventures, choosing another jurisdiction's corporate law, whether directly or indirectly and whether within or outside the E.U., is not cost-effective.

1. Incorporating Abroad

After *Centros* and its progeny of case law,[13] VCFs and entrepreneurs in Germany and Italy can indeed use any E.U. (or European Economic Area) corporate laws. Taking advantage of German and Italian private international laws,[14] VCFs and entrepreneurs could therefore incorporate in any E.U. member state that does not adhere to the real seat doctrine, such as the Netherlands or Ireland, and then run their firms in Germany or Italy. In addition, both Germany and Italy have concluded international bilateral treaties regulating, *inter alia*, the mutual

[13] ECJ, *Centros Ltd v Erhvervsog Selskabsstyrelsen* (C-212/97), 9 March 1999.

[14] Germany has no codified private international corporate law, but courts apply the law of the registered seat for entities incorporated in an E.U. member state. See *Bundesgerichtshof* 13 March 2003, 154 ENTSCHEIDUNGEN DES BUNDESGERICHTSHOFS IN ZIVILSACHEN [BGHZ] 185; *Bundesgerichtshof*, 19 September 2005, 164 BGHZ 148; *Bundesgerichtshof,* 14 March 2005, 26 ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT 805 (2005). As to Italy, see Legge 31 May 1995, No. 218.

recognition of companies with several countries including the U.S.[15] (but not the U.K.[16]). As a result, incorporating, for instance, in Delaware could be an alternative solution for VCFs and entrepreneurs seeking to arrange their business relationships under a more malleable corporate law.

Yet, for most VC-backed firms, foreign incorporation is in practice unlikely to be cost-effective.[17] Even leaving aside double taxation issues and the increase in compliance costs and risks that incorporating abroad would entail (Ribes 2012), incorporating a German or Italian VC-backed firm in a different jurisdiction cannot entirely avoid the firm and its shareholders' relationship also falling, at least in part, under German or Italian corporate laws. This is due to the regulatory treatment of "pseudo-foreign corporations" (i.e. corporations incorporated in a foreign jurisdiction with which they have minimal business connections) running their business in Germany or Italy.

First, the recognition of foreign firms incorporated outside the E.U. is subject to the requirement that their charters contain no clauses contrary to "public policy."[18] This term of art is broad enough to justify the imposition of domestic corporate law rules, regardless of whether such rules are explicitly spelled out in the blackletter law or result from the interpretations of scholars and courts.

Second, even within the E.U., recognition of a foreign corporation does not guarantee that the corporate law of the incorporation state will govern the company's organization and internal affairs *exclusively*. Some host state mandatory rules also apply to foreign corporations, although

[15] See "'*Freundschafts-, Handels- und Schiffahrts-vertrag zwischen der Bundesrepublik Deutschland und den Vereinigten Staaten von Amerika' vom 29. Oktober 1954*"; and "*Trattato di Amicizia, Commercio e Navigazione tra la Repubblica Italiana e gli Stati Uniti d'America' del 2 febbraio 1948*".

[16] As of July 2024, neither the E.U. nor its member states have thus far signed an agreement with the United Kingdom to grant the mutual recognition of companies after Brexit.

[17] In many cases, private VCFs co-invest with state-owned VCFs in Germany and Italy. From multiple conversations with VC players, we learned that as a condition for co-investment, the latter require that the startup company is domestically incorporated, hence giving private parties no choice to incorporate abroad.

[18] According to several judgments by the Corte di Cassazione—the Italian Supreme Court—,foreign corporations registered in countries with which a bilateral treaty exists can only be recognized if their structural and functional features do not violate public policy—also terms "*ordre public*." For details, see Dagnino 2008, 333. German international private law also explicitly refuses to recognize foreign law if it is against public policy or "*ordre public"*. See § 6, *Einführungsgesetz zum Bürgerlichen Gesetzbuche*. However, the Bundesgerichtshof—that is, the German Supreme Civil Court—has ruled that the *ordre public* does not hinder the recognition of U.S. corporations even if they have their real seat in Germany. See, e.g, *Bundesgerichtshof*, 29 January 2003, in 57 ZEITSCHRIFT FÜR WIRTSCHAFTS- UND BANKRECHT 699 (2003); and *Bundesgerichtshof*, 5 July 2004, in 50 RECHTS DER INTERNATIONALEN WIRTSCHAFT 787 (2004). Generally, German courts reject the recognition of foreign corporations based on the *ordre public* only in extreme cases. See, e.g., Oberlandesgericht Düsseldorf, 3 April 2010, in 20 INTERNATIONALES STEUERRECHT 475, 479-80 (2011) (not recognizing a foundation with the main purpose of tax evasion). However, some scholars advocate applying specific domestic corporate law rules (e.g. corporate veil piercing doctrine) to foreign corporations. See, e.g., Kindler 2021.

the E.U. freedom of establishment limits the extent to which such overriding mandatory provisions are legitimate under E.U. law.[19]

Third, mutual recognition of foreign corporations is limited to corporate law. Other areas of the host state's legal regime, such as insolvency law, still apply to the foreign corporation, arguably regardless of whether they can be qualified as part of corporate law from a functional perspective.[20] In fact, the choice of a foreign corporate law may lead to negative synergies between the foreign corporate law and other areas of the host jurisdiction's legal regime, which may increase the cost of incorporating abroad, potentially to a prohibitive extent (Gerner-Beuerle, Mucciarelli, Schuster, and Siems 2019).

Because determining which specific regime governs foreign corporations is not straightforward (Gerner-Beurle and Siems 2019), VC deals dependent on the choice of a more flexible corporate law are fraught with a high degree of legal uncertainty. As this can, in turn, result in potentially large costs for VC-backed firms (Drouven and Mödl 2007), VCFs and entrepreneurs planning to run the firm in Germany or Italy may therefore rationally accept national corporate laws. In short, opting in to a foreign corporate law regime while running a business in a different jurisdiction can resemble buying a pig in a poke.

To be sure, whether the foreign incorporation of a domestic venture in Germany or Italy is attractive ultimately hinges on a cost-benefit analysis. If the contracting inefficiencies under domestic corporate law are large enough, they will outweigh the costs of uncertainty and the higher out-of-pocket expenses of being a foreign (and especially a Delaware) corporation when it comes to obtaining legal advice (Drouven and Mödl 2007). Hence, beyond an equilibrium point, choosing foreign law will be the better option. Although we cannot provide conclusive evidence to that end, the observed incorporation patterns suggest that German and Italian VCFs and entrepreneurs reach this equilibrium point only in a limited number of instances: startup firms are mostly organized under national law, at least until they scale-up (Weik, Achleitner, and Braun *in print*).

2. Using Dual Structure Companies

German and Italian VCFs and entrepreneurs planning to run their firms in Germany and Italy could circumvent the strictures of local corporate laws also by resorting to more complex

[19] Mandatory provisions protecting public policy would still apply even for intra-E.U. incorporated firms within the limits of the so-called "*Gebhard Test*." See Gerner-Beurle and Siems (2019). In short, the "*Gebhard test*" makes the applicability of local laws and regulations contingent upon four circumstances. First, they have to apply in a non-discriminatory manner. Secondly, they have to be justified by imperative requirements that are in the general interest. Third, they have to be suitable for the attainment of the objective pursued. Fourth, they must not go beyond what is necessary to obtain the objective (proportionality).

[20] For instance, since 2008, the duty of directors of German companies to file for insolvency is formally part of insolvency law. It thus falls outside the *lex societatis* and therefore, intentionally, applies to foreign corporations whose centre of main interest is in Germany, which is the case at foreign corporations that mainly conduct their business in Germany. See, e.g., Gerner-Beuerle and Siems 2019.

organizational solutions, such as so-called “dual companies,” two-tier cross-border structures that use a foreign entity—predominantly, a U.S. corporation—as a holding company for the domestic subsidiary that operates in the jurisdiction where the business is located (Fenwick 2021).

This solution entails a significant increase in out-of-pocket costs (Orrick 2021; Glazer 2021). While its adoption is reportedly not so rare in some jurisdictions (for China: Li 2012; for Latin America: Andrade and Pereira 2023), to the best of our knowledge, dual companies are seldom used for early-stage startups in Germany and Italy and when this happens it is generally because the VCF is based in the U.S. In Italy, for instance, the data available shows that 16 out of 64 VC-backed firms *with a U.S. investor* have resorted to this kind of organizational structure (Giudici and Agstner 2019). These figures, however, look less impressive if one considers that in Italy there are at least 183 VC-backed firms (Giudici, Agstner, and Capizzi 2022), and the data appear downright negligible if considered against the entire universe of innovative firms, which includes more than 11,000 corporations (Giudici and Agstner 2019).

While unattractive for early-stage VC-backed firms, dual companies are more credibly emerging instead as a relatively popular option for more mature firms seeking scale-up capital abroad (whether in the U.S. or the U.K.), even though significant variation exists across countries (Mind the Bridge 2017).

B. *Formal Contracts Matter to the Governance of VC Relationships*

A second objection to the relevance of our findings draws on the observation that VC contracting may serve purposes other than underpinning the formal enforcement of contractual terms in litigation. VCFs and entrepreneurs generally abstain from resolving their disagreements through litigation because doing so would taint the reputations of VCFs and (serial) entrepreneurs. Against this background, it would not be a problem if the contractual arrangements shaping VC deals were invalid and thus unenforceable, because the contracting parties would never end up before a court anyway. Yet, nevertheless, formal contracts may matter in relation to contracting parties, not as a specification of discrete rights and duties but rather as a set of guidelines on which parties can draw to identify breaches in a highly incomplete contract, with formal enforcement being a nuclear option parties will seldom, if ever, consider. Again, if contracts would serve such a mere indicative function of outlining contracting parties’ mutual expectations, the inclusion of null and void clauses would not meaningfully affect this function.

1. The Remote Risk of Litigation

VCFs and entrepreneurs seldom engage in litigation, because such practice would taint the reputations of VCFs and (serial) entrepreneurs (Atanasov, Ivanov, and Litvak 2012). If VCFs and entrepreneurs rarely litigate their disputes due to reputational concerns even in the U.S., where litigation is a key determinant of shareholder protection (Spamann 2022), similar patterns can be expected *a fortiori* in jurisdictions such as Germany and Italy where private enforcement in the corporate context is generally rarer (Verse 2019; Ferrarini and Giudici 2019).

Even in a jurisdiction where courts and arbitrators, with the support of scholars, generally hold certain charter and contract provisions null and void and therefore refuse to enforce them, including such provisions in formal contracts would still be valuable especially if they are self-enforcing, as many VC contract clauses are designed to be (Enriques, Nigro, and Tröger 2025a). If there is no need for formal enforcement of the contractual rights and the risk that the other party will resort to a court or an arbitrator to have the clauses that grant those rights declared null and void is remote, one can simply rely on such clauses and ignore the law.

Yet, practitioners advising the parties may refuse to include specific clauses in contracts if any such provision is clearly contrary to statutory or case law, or unanimous interpretations of the law (Enriques, Nigro, and Tröger 2025a). Clear illegality is not necessarily limited to cases where contract clauses are irreconcilable with the apparent meaning of blackletter law. Even an interpretation widely shared by legal scholars and, *a fortiori*, by courts and arbitrators, may be sufficient to induce legal gatekeepers—such as lawyers and notaries—to leave a given clause out of the contract (Enriques, Nigro, and Tröger 2025b).

Indeed, both in Germany and Italy, it is not just a matter of advice. Notaries may simply veto the insertion of contractual arrangements that are in contrast with corporate law in the firm's constitutional documents (which have to be notarized) (Arruñada 1996). In Germany, notaries are under the legal obligation not to provide their services to support evidently illegal ends.[21] Despite some variations, professional ethics and the precautionary principle will generally prompt notaries to adopt a conservative approach that curtails private ordering.[22] In Italy, the firm's constitutional documents have also to be drawn up with the assistance of a public notary, who has a duty to refuse assistance for charters containing provisions that are against the law,[23] which leads notaries to take a similarly cautious approach (Enriques, Nigro, and Tröger 2025b). To be sure, for clauses that are not patently invalid but are of dubious legality, it may well be that parties will give no weight to the related uncertainty and that

[21] See § 14(2), *Bundesnotarordnung* of 24 February 1961. In the literature, see generally Wolf 2008, 351.

[22] The majority view permits notaries to refuse their services even if they only doubt the legality of the transaction before them, which indicates the cautious stance that German notaries are supposed to observe. See Sandner 2023.

[23] See Article 28, Legge 16 February 1913, No. 89. In the literature, see generally Casu and Sicchiero, 2010.

lawyers will attempt to use the available U.S. model without searching for alternative solutions or raising any objections. Under such circumstances, assuming that the contracting parties manage to find a public notary who does not raise any objection, even illegal clauses may eventually end up in VC contracts.

However, such contractual arrangements in German and Italian VC deals arguably do not have the same value for the parties as they have in the U.S. Every single clause is part of a complex deal in which economic terms and governance and exit rights combine and influence the price the entrepreneur has to pay for the VCF's contribution. The uncertain legality, let alone the blunt illegality, of a clause implies that contracting parties will attach a lower value to it (Hermalin, Katz, and Craswell 2007). The greater the uncertainty of a clause's legality, the higher the probability that litigation will ensue (Priest and Klein 1984). In turn, the more significant the risk of litigation, the thicker the wedge between that clause's value in an interventionist jurisdiction compared to a deferential one. Ultimately, a higher probability that a contracting party will be unable to exercise the rights and prerogatives stipulated in the clause will result in a higher cost of capital.

It is possible that during VC investment booms the risk of litigation will be so low that the wedge becomes negligible. However, it may become significant in a downturn. The recent fall in VC investment following interest rate hikes could lead VC firms to ration subsequent capital injections and therefore terminate a higher number of funded projects, which would have the effect of antagonizing entrepreneurs. If VCFs use their exit rights to liquidate their investments and thereby cause the VC-backed firm to stop trading, the entrepreneur has strong incentives to prevent or react to that move to retain some of the venture's value (Bartlett, 2015; Bratton and Wachter, 2013). Threatening litigation, especially in the context of an uncertain legal framework that makes it harder for parties to agree on a settlement, may be an effective weapon in the arsenals of entrepreneurs. For instance, following the recent dramatic change in the VC market in 2022, in the U.S. as much as in Europe, many VC-backed firms have undergone down-rounds (Temkin 2022; Nowshin 2022) that, by virtue of anti-dilution provisions, have often shifted value from entrepreneurs to VCFs. A rigid corporate law environment that imperils the smooth execution of these transactions creates strong incentives and levers for entrepreneurs to seek value redistribution via litigation that remain unavailable under a flexible corporate law (Enriques, Nigro, and Tröger 2025a).

Furthermore, when innovation is more incremental and/or products face greater competition and more elastic demand, the road to success for the VC-backed firm may be longer, and the decision to persevere in the venture or "pull the plug" becomes correspondingly harder. Under these conditions, the contractual arrangements defining the financial structure and the governance model of the VC-backed firm are more likely to impact the relevant course of action as they influence incentives and allocate risks.

For instance, the unenforceability of the strong governance rights that VCFs typically receive may prove especially burdensome if the entrepreneur is reluctant to go down the bargained-for path. Similarly, when the VCF imposes liquidation or a bad sale of the company, the uncertainty afflicting the judicial recognition of the specific allocation of cash-flow rights may lead to suboptimal outcomes and costly litigation. Moreover, the entrepreneur may see redistributive potential in fighting rather than just accepting failure and, possibly, moving on to the next venture (Nigro, Enriques, and Tröger 2025b; Agstner, Capizzi, and Giudici 2020). Empirical evidence confirms the significance of this risk (Broughman and Fried 2010). Non-legal constraints on such hold-out strategies, for instance in the form of negative reputational effects, matter less where serial entrepreneurship is uncommon (which is the case even in the U.S., see Bengtsson 2013). Also, given the undiversifiable nature of the risk associated with entrepreneurship (Hall and Woodward 2009), founders can be expected to defend their once-in-a-lifetime engagement doggedly (Broughman and Fried 2013).

Consistent with this narrative, law and economics scholars have stressed that the value of the contractual technology deployed in U.S. VC deals is greatest exactly when VC-backed firms perform poorly (Bratton and Wachter 2013; Riethmueller 2021). VCFs can exercise their right to terminate such ventures to recoup any value left in the firm without court interference (Baird and Henderson 2008) and save on the additional costs associated with continuation (Cable 2015). Anecdotal evidence corroborates this narrative, showing that VCFs realize the full potential of their private ordering solutions when investments go south: for instance, Kaplan, Martel, and Strömberg (2007, 309) reported that an interviewed VC investor understood the importance of the arrangements governing VC-backed firms only after unsuccessful attempts to sell a portfolio company during the downturn that followed the bursting of the Dot.com bubble.

It is thus at least plausible that VCFs, who are sophisticated repeat players, will not totally ignore the risks associated with the unenforceability of contractual rights or the uncertainty thereof and, ultimately, factor these risks in when pricing the terms of the deal. Alternatively, they may settle for less effective alternatives that will have the same implications on the financials of the VC deal. At the margin, this would mean a higher cost of capital for startups.

2. Scaffolding

A similar argument against the real-world relevance of our findings can be based on the scholarship of Hadfield and Bozovic on the scaffolding function of formal contracts (Hadfield and Bozovic 2016). Their research found that companies extensively use formal contracts to plan and manage innovation-oriented relationships. The function of these contracts is not to secure the benefits of a credible threat of formal contract enforcement. Rather, they largely rely on termination and reputation to induce compliance. Formal contracts serve "to coordinate beliefs about what constitutes a *breach* of a highly ambiguous set of obligations" (Hadfield and Bozovic 2016, 981, emphasis added).

One may argue that formal contracting between VCFs and entrepreneurs similarly serves the function of identifying ex ante what parties are expected (not) to do, with no real concern for whether those contracts will be enforceable in a court of law.

Yet, the type of relational contract where the scaffolding theory has been shown to have explanatory value is only superficially similar to the one between VCFs and entrepreneurs. Hadfield and Bozovic tested their theory by interviewing general counsels or managers at innovative firms about external relationships with suppliers or customers that were inherently long-term and required heavy relationship-specific investment on both sides, typically to develop new products jointly (Hadfield and Bozovic 2016, 995). In those circumstances, parties share a common interest in preserving their relationship and, therefore, in amicably resolving disputes on what constitutes a contractual breach. There is no way of knowing whether the study's findings rely on answers specifically relating to VC relationships, as the authors do not indicate what kind of relationship each response refers to, and mention VC nowhere else in their article (Hadfield and Bozovic 2016, 1019-32).

The relationship between VCFs and entrepreneurs is different. In many cases (that is, for all but the few successful ventures allowing VCFs to obtain the returns expected by their investors, and the ventures that are a total failure) there comes a point where parties are in a clear conflict about the merits of carrying the relationship forward (Bartlett, 2015; Pollman, 2019), as empirical evidence confirms (Bian, Li, and Nigro, 2021). The VCF may want to terminate the venture, while the entrepreneur may want to keep going—or vice versa (Wansley 2019). Using formal contracting as mere "guidelines" here would not be very effective. In addition, in the VC setting, the matter is less frequently about whether either party has breached their obligations (that is clearly the case in some instances, such as bad leaver provisions) than about whether the VC-backed firm should be liquidated or sold to third parties. The scaffolding function has, at best, a limited role in these endgame situations where parties' interests can hardly be reconciled.

Finally, the fact that formal contracts may play a scaffolding role in VC relationships does not exclude them from performing their traditional function in the admittedly rare scenario, in which parties decide to take advantage of its clauses. In line with this reasoning, even scaffolding advocates do not rule out this traditional function of contracts being served (Hadfield and Bozovic 2016, 1014).

III. Some Policymaking Implications

Our work shows that German and Italian corporate laws prevent VCFs and entrepreneurs from adopting nearly all the private ordering solutions shaping VC deals in the U.S. and also rule out functionally equivalent solutions. With some exceptions, they are instead compelled to use alternative arrangements that are less functional than those available in the U.S. This, however, is seldom the result of lawmakers' explicit choices. Rather, it is primarily the byproduct of scholars' doctrinal interpretations endorsed by practitioners and/or courts and, at a deeper level, of the predominant legal culture (see *supra*, Part I.C.).

This part builds on these findings to discuss the actions policymakers could take to tackle the adverse impact of corporate law in action on VC contracting in Germany and Italy.

A. *Reforms to Expand the Private Ordering Space*

The source of the strictures preventing VCFs and entrepreneurs from shapeshifting German and Italian VC-backed firms in a way that mirrors the U.S. example is much less often blackletter law than the interpretations of scholars and, in their different capacities, practitioners and courts and arbitrators. To be sure, German and, far more so, Italian corporate laws have recently undergone significant reforms that were expressly aimed at making them more flexible and thus friendlier to VC contracting (for Germany: Noack and Beurskens 2008, and Schmolke 2023; for Italy: Ferrarini, Giudici, and Stella Richter 2006, 661-663 and 683-689, and Giudici and Agstner 2019, 616-617). Yet, scholars and courts still tend to look at VC contractual arrangements through their traditional cognitive lenses (Enriques and Nigro, 2025). Therefore, they continue to superimpose a web of implicit mandatory rules on the blackletter regime, pervasively constraining private ordering (Nigro and Enriques, 2021; Enriques, Nigro, and Tröger, 2025b; Enriques and Nigro, 2025).

It is therefore difficult for national policymakers to overcome the root causes of the problem: reforming blackletter law, which is the approach thus far prevailing in Germany and Italy (as well as in other member states, see Neville and Sørensen 2014, 550-554), in the direction of getting rid of its explicit mandatory provisions is likely to leave the implicit requirements that curtail private ordering unaffected.

Nor do E.U. policymakers appear to be in a good position to take a more effective approach. Their focus remains narrowly confined to reforms of statutory corporate law. In 2021, the European Commission introduced the "Startup Nation Standards," a set of best practices designed to foster entrepreneurship and accelerate startup growth in the E.U. The Standards recommend, *inter alia*, that national corporate laws be simplified to better align with startup culture (European Commission 2021b). However, these recommendations are vague and unlikely to drive systematic amendments to national regimes. Even if implemented, local scholars and courts would continue interpreting new legal frameworks through traditional lenses, leaving the underlying approach—and the resulting rigidities and uncertainties—largely unchanged.

In 2024, following the release of a Startup Manifesto by various stakeholders (European Startup Network 2023), the "Draghi Report" advocated for the creation of a "European startup regime" (E.U. Commission 2024, 29-30). While this proposal quickly gained support from VC firms, startups, and unicorns, which launched a petition to speed the process up (Browne 2024), it is unlikely to succeed or prove effective. The proposal is not a priority for E.U. policymakers. Moreover, such initiatives typically face strong resistance throughout the legislative process and are prone to derailment. Incumbent advisors (attorneys, notaries, and accountants) fear that special regimes, even though initially limited in scope, will be expanded over time and therefore are a trojan horse that ultimately imperils the quasi-monopoly rents they enjoy from providing their services under a purely domestic legal framework. The ill-fated history of the *Societas Privata Europea (SPE)* (Hirte and Teichmann 2013) provides evidence for this pattern: the SPE was narrowly conceived as an organizational form for cross-border subsidiaries but stirred fears among advisors that it would displace domestic legal forms for closed corporations over time. Even if the current pro-startup momentum and the influence of key proponents were sufficient to make this a priority and overcome political resistance, the regime would still fall short. It would inevitably feature gaps that would need to be filled, creating the preconditions for national corporate laws and the underlying legal culture to reintroduce rigidities and uncertainties in key areas.

While these initiatives would likely yield no appreciable results, some other measures would still help. As far as Italy is concerned, the introduction of a new legal rule stipulating that, unless otherwise explicitly stated, all corporate law provisions are mere default would be useful (Giudici and Agstner 2019, 626). In Germany, a clear rule to this effect exists for the private limited company (GmbH),[24] while the corporate law regime for stock corporations (AGs) is informed by the principle that any provision is mandatory unless explicitly stated otherwise.[25] Such an explicit stipulation of the non-imperative character of corporate law rules reduces the uncertainty surrounding the mandatory or default nature of blackletter law provisions and, if the choice was taken to make most rules default (unlikely as that is), it could also affect legal scholars' and courts' ability to infer implicit standards from statutory provisions.

However, legislators may still find some difficulty in countering the "erosion" of the space for private ordering due to the creative expansion of the mandatory law that we document as a result of the activities of scholars, practitioners, and courts (Nigro and Enriques 2021; Enriques, Nigro, and Tröger 2025b). Here, scholars, practitioners, and courts can argue that the implicit rule or standard they invoke to trump contractual freedom is rooted in constitutional guarantees with which ordinary laws have to be consistent. For instance, the German Constitutional Court has in the past invoked constitutional guarantees to allow courts to review the fairness of corporate transactions, in particular to check if the price that a divesting shareholder receives in a transaction subject to an appraisal remedy (e.g. mergers or squeeze-outs) reflects the fair value of their equity interest.[26] Similarly, the Italian Constitutional Court

[24] § 45(1), GmbHG.

[25] § 23(5), AktG.

[26] See Bundesverfassunggericht, 27 April 1999, in 100 ENTSCHEIDUNGEN DES BUNDSVERFASSUNGSGERICHTS 289 (asserting that the constitutional guarantee of private property encompasses

has demonstrated its readiness to apply reasonableness, which they derive from the supreme principle of equality before the law, to strike down statutory rules.[27] Such constitutional principles can also be used by scholars and courts to interpret existing laws in a way that constrains contractual freedom beyond the wording of statutory provisions.[28] For instance, a court may consider a contractual clause as valid, but subject the exercise of the rights it confers to scrutiny based on the good faith standard applying to contracts generally, with outcomes which may well be inconsistent with the contract's economic rationale.[29]

Short of the make-believe scenario of a change in domestic legal culture, the inclination to expand the turf of mandatory corporate law and correspondingly restrict the domain of private ordering is bound to curtail most statutory interventions attempting to facilitate the use of U.S.-style contractual arrangements for VC deals. Scholars have highlighted the functional deficiencies of relying solely on amendments to statutory texts as a means to change legal culture (Pistor 2002), particularly regarding its impact on private ordering (Nigro and Enriques 2021, 191; Enriques and Nigro 2025).

B. *Two Policy Proposals*

Two further policy proposals are worth sketching out, though. On the one hand, the private ordering solutions that typically shape U.S. VC deals could be insulated from restrictive interpretations with no clear basis in blackletter law by enacting a statutory provision explicitly tackling this phenomenon. It could do so by stating that the corporate law regime for the relevant corporate forms cannot be interpreted (a) in such a way as to rule out the validity of the contractual arrangements that are typically used in VC deals (and that the provision itself should duly describe), or (b) as conditioning their validity on their consistency with any implicit corporate law requirements, including general standards, that are incompatible with the common interests of the parties as can be derived from their arrangements.

On the other hand, a statutory model could be devised for corporations' constitutional documents and shareholder agreements for VC-backed firms similar to the U.K.'s Table A of

the substance and the value of share ownership); and Bundesverfassungsgericht, 23 August 2000, in 53 NEUE JURISTICHE WOCHENSCHRIFT 279 (2001) (confirming the prior judgement).

[27] "Reasonableness" is a concept stemming from the "principle of equality" enshrined in the Italian Constitution. The Italian Constitutional Court deploys such concept to assess the legitimacy or illegitimacy of any statutory rule that may have been brought before it to constrain the discretion of the legislator. Reasonableness in this context implies an assessment of any such statutory rule against the "common sense." See Corte Costituzionale, 31 May 1996, No. 172. For details, see Servizio Studi della Corte Costituzionale 2013.

[28] See, e.g., Corte Costituzionale, 5 February 1999.

[29] In Italy the general good faith clause that can be used to identify additional implicit obligations for contractual parties has been considered an application of the fundamental duty of solidarity as expressed in Article 2 of the Italian Constitution. See, e.g., Corte di Cassazione, 18 September 2009, No. 20106.

the Companies Act for companies limited by shares.[30] Table A provides a standard charter enshrined by an Act of Parliament. Because its provisions are statutory in nature, scholars, practitioners, and courts have no leeway to come up with interpretations considering or declaring them null and void. Parties are free to opt-in to Table A or, at the price of losing its protection, deviate from it.

Germany has tinkered with a similar approach for the private limited company.[31] The initiative, however, has not succeeded, arguably because the one-size-fits-all standard charter was inadequate for most companies founded by more than one person (Heckschen 2009). Italy has more recently followed a similar path. One prominent initiative consisted in the adoption of a standard charter that prospective shareholders of an "innovative startup" could use to incorporate a private company *online* on a freely accessible platform and, importantly, without any notarial intervention.[32] This reform proved to be short-lived: notaries promptly leveraged on minor imperfections in the lawmaking process (Stella Richter Jr. 2021) to have the relevant regulation struck down by administrative courts.[33] Since then, lawmakers have approved a law that allows prospective shareholders to incorporate online by using a new standard charter that is partly modifiable with the assistance of a notary.[34] Yet, neither of the standard charters was specifically tailored to the needs of VC-backed firms.

The model contractual form (i.e. a model charter and one or more model shareholder agreements) for VC-backed firms that we advocate would include all the private ordering solutions that shape VC deals in the U.S., duly amended, where necessary, to adapt to the strictures of explicit mandatory provisions deriving from E.U. harmonization measures, from which member states cannot deviate (which, according to our analysis, are very few: Enriques, Nigro, and Tröger 2025b). Of course, there would be no requirements for contracting parties to take the whole package or none of it: they would be free to adapt its contents to their preferences, with the obvious caveat that any deviating arrangement would be at a high risk, and possibly a higher risk than is currently the case, of being declared null and void. Ideally, rules granting public notaries vetting power over deviations from the model statute would be repealed to allow for experimentation and evolution in VC contracting. Moreover, it should be clarified that no implicit duties can be imposed on contracting parties based on other provisions of the Table A-style model form or, *a fortiori*, on general corporate law.

One critical puzzle that lawmakers would have to solve in devising an effective model form for VC-backed firms is how to make sure, possibly building on the inputs of scholars, that

[30] Government of the United Kingdom 2017.

[31] See § 2(1a), GmbHG and Annex 1, GmbHG (stipulating that shareholders can incorporate a private company by using a standard charter and providing such statutory standard charter).

[32] See Article 4(10-bis), Decreto Legge 24 January 2015, No. 3 (converted into Legge 24 March 2015, No. 33). See also Decreto del Ministero dello Sviluppo Economico 17 February 2016, No. 3.

[33] See Consiglio di Stato, 29 September 2021, No. 2643.

[34] See Article 29(1), Legge 22 April 2021, No. 53; and Article 2, Decreto Legislativo 8 November 2021, No. 183. See also Decreto del Ministero dello Sviluppo Economico 26 July 2022, No. 155.

courts do not take advantage of the discretion inherent in the use of the contractual gap-filling tools at their disposal to alter the functional logic of the rights and powers stemming from the model form. Long-term relational contracts, like the arrangements governing VC-backed firms, are inevitably incomplete. Therefore, gap-filling plays a crucial role in implementing contracts governing VC deals (Broughman, Pollman, and Smith 2020). German and Italian corporate laws deploy gap-filling techniques that, similar to those available under U.S. corporate law (Pargendler 2008), enable courts to review the exercise of rights stemming from a contract. Good faith is the most commonly used standard for this purpose (for Germany: Hennrichs 1995; for Italy: Preite 1992 and Nuzzo 2003). Our findings show that, under German and Italian corporate laws, some of the arrangements typically found in U.S. VC deals are legal, but the exercise of the ensuing rights is subject to a good faith review aimed at testing their "fairness" (which is broadly construed). Incidentally, the outcome is a distortion of those arrangements' economic functions (Enriques, Nigro, and Tröger 2025b). Unfortunately, there is no reason to think that, supported by scholars, courts would take a less intrusive approach to the matter if they had to rule on how VCFs and entrepreneurs ought to make use of the rights stemming from the model contractual form.

IV. CONCLUSION

In this chapter, we have presented the findings of two companion papers that identify German and Italian corporate laws as a hindrance to VC contracting, due to their rigid structure and, to a far larger extent, the inclination of scholars, practitioners, and courts to interpret them in private-ordering-averse manner. In addition, we have validated the relevance of our findings in terms of building a vibrant VC market by responding to two objections. The first of these objections is that such rigidity poses no obstacles to private parties, because they can escape them by incorporating the VC-backed firm abroad or, similarly, by using dual companies. We have shown why these escape routes are imperfect, costly, and ultimately unattractive, at least for early-stage companies. Thus, we conclude that our findings are significant for transactional practice. Meanwhile, the second objection is that the enforceability of formal contracts does not matter, because litigation is rare in the VC space and/or because the function served by formal contracts is independent of their enforceability. Here, first, we have argued that it may be impossible for parties to use U.S.-style contractual arrangements even if they knew that they are not valid. Second, especially in a downturn, formal contracts' enforceability may actually matter for the financial returns of parties (and especially VCFs).

Finally, we have discussed the policy implications of our work. In this regard, one important finding of our work is that most regulatory constraints in German and Italian corporate laws come from implicit requirements that narrow the scope of private ordering, well beyond blackletter law constraints. Building on that, we have sketched out some initiatives that policymakers could undertake to change course and support VC investments. Notably, the simple suppression of blackletter law mandatory provisions would have a limited effect, and thus we have proposed two alternative solutions. One comprises a rule of interpretation explicitly carving out commonly used contractual terms from private-ordering-averse interpretations of existing corporate laws. The other entails a model contractual form adopted as part of a statute, and transplanting the contractual arrangements of VC contracts in the U.S. Ultimately, though, the main hindrance to efficient VC contracting comes from legal culture, which even parliaments can do little, if anything at all, to change.

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