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GERMANY IMPLEMENTS EU SHAREHOLDERS' RIGHTS DIRECTIVE; COMPREHENSIVE REFORM TO STOCK CORPORATIONS ACT PASSED

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EU SHAREHOLDERS' RIGHTS DIRECTIVE IMPLEMENTED INTO NATIONAL LAW

On 4 August 2009 Germany passed comprehensive amendments to the German Stock Corporations Act (*Aktiengesetz* - the "Act"), implementing the European Shareholders' Rights Directive ⁽¹⁾ and effecting critical changes to numerous key sections of the Act. The changes largely relate to procedural matters connected with the convening and holding of general meetings of shareholders, and enhance shareholder communication and shareholder participatory rights – in particular for shareholders

who are unable to attend such meetings in person. In addition, the reforms address abusive shareholder suits and modify capital contribution rules.

The amended Act provisions will generally take effect in September and November 2009. The amendments will have immediate significance for the management of stock corporations, management's advisors and – of course – for shareholders of German stock corporations. The following article provides a very brief summary of the amendments.

INCREASING SHAREHOLDER PARTICIPATION AND TRANSPARENCY: NEW RULES FOR SHAREHOLDER COMMUNICATION, MEETING AND VOTING

A major goal of the new legislation is to further empower shareholders to effectively participate in shareholders' meetings and to otherwise contribute to decision-making. In particular, the amendments provide for the following:

- The corporation's articles may now permit shareholders to participate in meetings of shareholders via electronic means, including voting on resolutions via text, letter or elec-

tronically. This major amendment replaces the rule to date that in order to vote in a meeting of shareholders, a shareholder must be physically present at the meeting, either in person or through a proxy;

- The corporation's homepage is now designed to be the central medium for shareholder communications. In particular, listed corporations will be required to make large numbers of docu-

ments and information accessible to shareholders via the corporation's homepage immediately after calling a shareholders' meeting. The provision of documents and information by electronic means correspondingly reduces the corporation's duties to mail written documents to shareholders or to make these available in written form on request.

- As elsewhere, in Germany it is extremely common for financial institutions and shareholder associations to hold shares on behalf of individual investors and to exercise these shareholders' rights at shareholder meetings in accordance with shareholders' instructions. Frequently the nominee holders craft recommendations to shareholders; where agreed to, these recommendations serve as the basis for the nominee to take an active role in representing a diverse array of shareholders (bloc voting). The amendments streamline this process, relaxing certain obligations for nominee holders to forward shareholder information to the sharehold-

ers and permitting shareholders to grant the nominee holder broader authority to act on the basis of management's recommendations.

- Powers of attorney permitting a proxy to act on behalf of a shareholder need no longer be granted in writing; simple text form (e.g. via email or by way of an online form) will now be sufficient.
- Amendments to the Act have now clarified the definitions of notice periods for the publication of invitations to shareholders' meetings and deadline dates for establishing entitlement to participate as a shareholder. In particular, notice periods will be calculated on the basis of calendar days, disregarding holidays. This amendment will be of special help for non-German shareholders who may not be familiar with Federal and Federal State statutory holidays.

ENHANCED REGULATIONS TO PREVENT ABUSIVE SHAREHOLDER SUITS

In 2005, Germany passed legislation ⁽²⁾ to limit the ability of shareholders to file abusive shareholder suits to set aside resolutions passed by shareholders governing corporate actions, in particular, on the basis that procedural technicalities had not been complied with. Such shareholder suits – commonly filed by a small number of well-known activists – are designed to disrupt the corporation's actions by preventing corporate matters from being registered with the corporation's commercial register and therefore becoming legally effective. ⁽³⁾

In 2005, an accelerated approvals proceeding (*Freigabeverfahren*) was created to permit courts to quickly dispense with spurious shareholder suits. In addition, several courts awarded damages settlements to corporations which had been affected by abusive shareholder litigation. Nonetheless, abusive litigation continued, not least as a result of different treatment of approvals proceedings by a variety of courts.

The 2009 amendments now provide that the Higher Regional Court (*Oberlandesgericht*) shall have sole jurisdiction over approval proceedings, namely, the approval of the registration of corporate changes which are still subject to suits to set these aside. Further procedural reforms have been made to prevent the shareholder plaintiff from unnecessarily delaying court proceedings, e.g. by insisting on separate service of process in relation to the approvals proceeding.

Additionally, the amendments contain a revised statutory test to be applied by the court in determining whether to permit registration to take place in light of a shareholder's (often questionable) objections. Under this test, the court must weigh the detriment to be suffered by the petitioning shareholder against the corresponding detriment to the corporation and the other shareholders. Previously, this test required the court to assess relative disadvantage to be suffered by the corporation as against the disad-

vantage to all of the shareholders, proceeding on the assumption that the disaffected plaintiff represented a broad array of shareholders. The new narrower test is likely to present a far higher barrier to activist shareholders seeking to block registrations.

Finally, a shareholder will be prevented from contesting an approvals procedure where the share-

AMENDMENTS TO CAPITAL CONTRIBUTION RULES

Deemed capital contributions in kind (*verdeckte Sacheinlagen*) occur where a shareholder contributes cash funds to a corporation, triggering an increase in the corporation's nominal capital (and issuance of shares), and then immediately causes the corporation to purchase assets from the shareholder or a related party. In effect, a capital contribution in kind is achieved without the purchased assets having been properly valued and registered as such for German corporate law purposes.

Recent legislation amended the German corporate statutes for the GmbH limited liability company.⁽⁴⁾ Originally, 'double liability' attached to the shareholder's obligation to make the contribution: an

COMMENT

Although affecting quite different aspects of the Act, in their sum total, these amendments generally empower the shareholders of a stock corporation. In particular, the ability of shareholders located elsewhere to participate in corporate decision-making is considerably enhanced - the requirement to physically attend shareholder meetings or arrange for a personal proxy is a powerful disincentive for minority shareholders. Amendments permitting electronic form communication and shareholder participation are also encouraging and timely.

The management of a stock corporation will not have long to become accustomed to and comply with these amendments. Annual general meetings of shareholders scheduled as of 1 November 2009 must be held in compliance with the amended Act.

holder holds shares with nominal share capital of less than EUR 1,000. Of all of the above measures, this measure will likely be the most effective; those corporations trading at many times nominal value are also the corporations most likely to be targeted by activist shareholders, who often only hold one share in the corporation.

agreement founding the obligation to contribute the non-cash assets was deemed invalid and the material fulfilment of the agreement was also deemed invalid. This double liability was dispensed with in amendments to the German Limited Liability Companies Act in 2008. Generally in keeping with the legislation governing the GmbH company treatment of deemed capital contributions in kind, the amendments to the Act now provide that a subsequent (lower) valuation of the non-cash assets will trigger an obligation on the part of the shareholder to contribute any difference in value, ensuring a complete capital contribution, and the ineffectiveness of the original contribution can be cured.

Please contact us for further information on these developments and with any questions you may have.

¹ Directive 2007/36/EC of 11 July 2007, OJ L 184/17

² *Gesetz zur Unternehmensintegrität und Modernisierung des Anfechtungsrechts (UMAG)*, BGBl. 2005, I, 2802

³ As a general rule, corporate matters which are subject to a claim to set these matters aside (*Anfechtungsklage*) are unable to be registered with the commercial register, rendering these ineffective at law until registration.

⁴ Act to Modernise the Law Governing Limited Liability Companies ("MoMiG"), which took effect in November 2008

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