LEGAL UPDATE
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Transition of the Brexit's "Corporate Victims" into German corporate law – particularly through the Fourth Amendment Act on the German Act on Corporate Reorganisations (*Umwandlungsgesetz* – "UmwG")

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The withdrawal of the United Kingdom from the European Union was decided in the course of the 2016 referendum. The British House of Commons just rejected the withdrawal agreement negotiated with the EU. Theresa May stated that "*a vote against this deal is a vote for uncertainty, division, and the very real threat of a no deal"*.

An unregulated "hard" Brexit has far-reaching consequences affecting all legal areas, particularly corporate law aspects.

Legal uncertainties for British companies located in Germany

Companies of an EU member state can invoke the European freedom of establishment. Thereunder, the so-called "foundation theory" applies in the context of international corporate law. A company incorporated under English law must therefore also be recognised as such if it carries out its activities predominantly or exclusively in another member state. In the case of a hard Brexit, this legal status ends on 29 March 2019.

The end of the freedom of establishment affects an estimate of around 8,000 to 10,000 companies incorporated under English law with their administrative seat being in Germany. The majority is incoporated as Private Company Limited by Shares (Limited or Ltd.) or Limited Liability Partnerships (LLP).

Under German international corporate law, these companies would in future be subject to the "domicile theory", according to which a company is subject to the corporate law of the state in which it has its (administrative) seat. As a result, companies once incorporated as legal entities under English law would then be qualified as a partnership (*Gesellschaft bürgerlichen Rechts*), a general partnership (*offene Handelsgesellschaft*) or, in the case of single shareholder, as a sole trader (*Einzelkaufmann*), due to the lack of valid foundation acts and a not existing registration with the commercial register. This would ultimately lead to an unrestricted personal liability of the shareholders for the liabilities incurred by the company (including former liabilities).

"Exit" from the English corporate law

The aforementioned downsides could be avoided if the respective company is converted into a legal entity under German law. In order to achieve this, different instruments are available under German law, such as

- a cross-border change of the legal form,
- a cross-border collapse merger (*Anwachsung*), and
- a cross-border (regular merger).

Additionally, another possibility (apart from a relocation of the administrative seat back to the United Kingdom) would be the transfer of the assets of the company by way of an asset deal. This, however, regularly brings along several other disadvantages.

From a first glance, the most attractive way would be a **cross-border change of the legal form**. The legal uncertainties that were considered for quite some time have been gradually reduced due to respective rulings of the European Court of Justice as well as national courts, so that cross-border changes of the legal form between certain EU member states nowadays occur quite frequently. As regards the United Kingdom, it has to be considered that the Companies Act 2006 only allows companies incorporated as private company, public company, private limited company and unlimited private company to undertake a change of the legal form. If a change of legal form has not yet been initiated, the clock is ticking, as a cautious approach on a cross-border change of legal form requires a two-month waiting period.

The **cross-border collapse merger** also seems to be appealing, particularly due to the limited formal requirements. Nevertheless, this possibility bears considerable uncertainties. For example, it is some-

times difficult to provide sufficient evidence on the universal legal succession (*Gesamtrechtsnachfolge*) and undesirable tax consequences can also arise.

A further possibility to "exit" the English corporate law would be a **cross-border merger**, which finds its unquestionable legal basis in Articles 118 et seq. of the Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 on certain aspects of company law and was implemented by the German legislation in Sec. 122a et seq. of the UmwG.

Fourth Amendment Act on the UmwG

Against the background of the impending Brexit, the provisions on cross-border mergers were recently changed by the German legislator. The Fourth Amendment Act on the German Act on Corporate Reorganisations from 19 December 2018 (Federal Law Gazette 2018 Part I, No. 49 p. 2694) shall primarily facilitate the process of a transition for companies in certain English legal forms, which have their administrative seat in Germany, into German (corporate) law.

For this purpose, a new Sec. 122m of the UmwG was added, according to which it is now sufficient for the companies involved to (only) have the merger plan notarised in due time before the Brexit becomes effective. A registration in the commercial register before the Brexit is not necessary. However, the filing for registration must occur immediately, but no later than within two years.

Anyhow, a fairly prompt implementation is required in terms of time considering a possible hard Brexit on 29 March 2019, as the merger plan and merger report must generally be published one month before the notarisation occurs.

A further novelty under the Fourth Amendment Act on the UmwG is that under German law it is now possible to merge into commercial partnerships (*Personenhandelsgesellschaften*) (Sec. 122b para. 1 no. 2 of the UmwG). For example, a British Limited could now merge into a limited partnership (*Kommanditgesellschaft*). Therefore, even "capital-weak" companies can go through a cross-border merger (e.g. into a UG & Co. KG) without having to raise the share capital of a German limited liability company (*Gesellschaft mit beschränkter Haftung*).

A further benefit of a merger into a commercial partnership is that, pursuant to Sec. 8 para. 3 of the UmwG, the requirement for a merger report can now be waived (Sec. 122e sentence 3 UmwG) and it is predominantly considered that at least the one month waiting period regarding the merger plan set forth in Sec. 122d sentence 1 UmwG can be reduced. In terms of time, this means somewhat a little more room for the necessary actions.

Note

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