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Seminar für Handels-, Schifffahrts-
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Seminar

The two-tier system in Germany and Italy

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The responsibility of the supervisory board and the manager

b) The responsibility of the manager

– Executive Summery –

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von

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Executive Summery

A. Introduction

This paper discusses the responsibilities of a manager of a German Private Limited Company (PLC) (GmbH). The work comprehends the responsibility of managers in respect to “their” company, the shareholders and the counterparty of the company according to the civil law.

B. The manager of a German Private Limited Company

§ 46 no. 5 GmbHG states that the shareholders of a PLC must designate at least one manager for their company; a PLC without a manager cannot be registered in the Commercial Register. § 6 II GmbHG states various reasons that exclude a person from being appointed as a manager; often they are linked to insolvency crimes.

According to § 35 II 2 GmbHG the manager represents the company both in juridical proceedings and any other matters. Following this there are the two main assignments: The manager has to administrate the business of the company (intern accountability) and represent the company towards the counterparties (extern accountability).

The designation of a manager according to § 38 I GmbHG can be rescinded at any time and without any specific reason by the shareholders. On the contrary, the right of the manager to resign from his charge cannot be limited by the shareholders.

C. Responsibility of the manager

The responsibility and liability of the manager are explained in four chapters according to the subject that the individual duty protects.

I. Principal article on the responsibility – § 43 I, II GmbHG

The principle article for the responsibility of the manager of a German PLC is § 43 I, II GmbHG: "Managers of a PLC shall employ the diligence of a prudent businessman in the matters of the company. Managers who violate their obligation are jointly and severally liable against the company for the resulting damage."

The primary duties of the manager resulting from § 43 I, II GmbHG can be outlined in the following four groups:

1. The manager must adhere to the rules and restrictions that are established in the *law, articles of incorporation and bylaws*.

2. He must work together with his colleagues on a *co-operative basis*. He has to inform whenever necessary his colleagues on important changes of strategy, decisions and developments. He is also responsible for the execution of decisions of the shareholders' meeting.

3. He is incumbent by the *obligation of confidentially*. He is bound to secrecy on any confidential information and strategy planning, business secrets and in any other confidential matters.

4. The most important duty is the obligation of *professional and diligent management of the business* of the company. The manager has to comply with the objective of the company set out in the articles of incorporation. He must take into consideration the underlying principles of economy and has to avoid taking significant risks for the company.

II. Special duties that primarily protect the company including its shareholders

This chapter contains those special duties that are established primarily to protect the company against defaults by the manager.

Infringement of shareholders' directives: According to § 37 I GmbHG the manager is obliged to follow and to execute the directions of the shareholders' meeting, as long as they are in accordance with the law, the articles of incorporation and the *bonus mores.* If the manager infringes upon a legally valid directive of the shareholders' meeting, he will be liable for the damages caused pursuant to § 43 II GmbHG.

Non-competition: The GmbHG does not include a special non-competition clause for the manager. But the duty of non-competition originates from the duty to loyalty and applies even in the case that it is not mentioned expressively in the articles of incorporation, the bylaws or the employment contract. The duty of non-competition prohibits commercial operations of the manager for personal account and third party accounts. The substantial range of the duty to non-competition is determined by both the objective of the company set out in the articles of incorporation and the area where the company effectively executes business.

Contracts between the manager and the company: According to § 181 BGB basically the manager is prohibited to enter into any contracts between himself and the administrated company. But there are three exceptions to this rule: The manager is allowed to fulfil a legally and correctly established obligation of the company (§ 181 BGB), he may sign contracts between himself and the company if the company is entirely legally benefiting from the contract and finally in case of the companies' permission (§ 181 BGB).

III. Special duties that focus on the protection of both the company and its counterparties

This chapter explains those duties that are established in order to protect both the company and the counterparties of the company. The protection is put into effect often by the means of protecting the registered share capital of the company. With this the legislator intends to prevent the insolvency of the company as this secures both the share value for the shareholders and the companies' liquidity to pay the demands of the counterparties.

Convocation of the shareholders' meeting: According to § 49 GmbHG the manager must convene the shareholders' meeting if this is expressively required by the law or by the articles of incorporation, in the interest of the company as and when it is necessary and especially if half of the registered capital of the company is lost.

Exceeding the power: Pursuant to § 37 II GmbHG basically the manager has unlimited power to act on behalf of the company. The (external) power to enter into contracts cannot be restricted, neither by the articles of incorporation nor by a decision of the shareholders' meeting. This means that internal restrictions do not affect the external power of the manager. But the *doctrine of the abuse of power* provides an exception to this rule: a contract is not binding for the company in the case that the manager exceeds internal restrictions and maliciously works together with the counterparty of the company (so-called collusion) or if the manager consciously exceeds internal restrictions and the counterparty either knows about it or at least that the transgression of the restriction was notorious for the counterparty (so-called evidence).

Duty to file for insolvency: § 64 I GmbHG states that the manager must file for insolvency without undue delay but latest within three weeks if the company is unable to pay its debts or is over-indebted. Otherwise he incurs liability to the counterparties of the company pursuant to § 64 I GmbHG, § 823 II BGB. The Creditors that already became creditors of the company *before* the date that the duty to file for insolvency came into existence, these creditors can claim as damage the difference between the amount they in fact received from the remaining assets of the company and the amount that they would have had received if the manger had filed for insolvency on time. According to recent jurisprudence those creditors that became creditors *after* the filing for insolvency, they can claim all the money they lost due to the insolvency of the company.

Payments after inability to pay or over-indebtedness: According to § 64 II GmbHG the manager is liable to the company for restitution of payments made after the inability to pay has occurred or after the over-indebtedness has been ascertained. Payment in terms of § 64 II GmbHG not only means the transfer of money but also any benefit to a creditor which reduces the companies' assets, like e.g. the delivery of goods, the transfer of rights and provision of services. The prevailing opinion holds, if the company receives an equivalent value in exchange for the payment, then the manager can reduce his liability by the received amount, because of this compensation the company did not suffer any loss in the sum of its assets.

Payments to the shareholders: According to § 43 III 1 GmbHG the manager is liable for damages if, contrary to the provision of § 30 GmbHG, payments were made out of the assets of the company which are required for the preservation of the registered share capital.

Initially, if a prohibited payment occurs, the manager is responsible to demand from the receiving shareholder that the latter should return the obtained money or benefit to the company. Further the manager is liable against the company and has to compensate the company until the amount that the registered share capital is covered again.

Credits that substitute equity capital: If a shareholder grants a loan to the company in a situation when an diligent businessman would instead have contributed capital to it (crisis of the company), then such a loan must not be repaid to the shareholder, as far as the loan is necessary to cover the registered share capital (§§ 32 a and b GmbHG analogous). The same applies if the loan was conceded before the company entered into a crisis and the shareholder did not demand its return within two or three weeks after the company entered into the crisis.

IV. Special duties that focus primarily on the protection of the counterparty of the company

Acquisition of own shares: According to § 43 III 1 GmbHG the manager is liable to pay damages if the company acquires its own shares under violation of § 33 GmbHG. Shares are allowed to be acquired only if the share capital contribution has been *fully paid* (§ 33 I GmbHG) and the acquisition costs can be paid out of *assets exceeding the registered share capital* and that the reserve required by § 272 IV HGB can be set up without reducing the share capital or a reserve to be set up is in accordance with the articles of incorporation which may not be used for payments to shareholders (§ 33 II GmbHG). If a prohibited purchase occurs, then the manager has to claim restitution of the purchase price paid by the company from the (former) shareholder pursuant to § 31 I GmbHG or § 812 BGB. If the purchase price cannot be obtained then the manager has to compensate the company for this amount.

Absence of the GmbH-addition: § 4 GmbHG contains the provision that the company's name has to include the addition "Gesellschaft mit beschränkter Haftung" (Private Limited Company) or a common abbreviation of this. If the manager does not use the addition and fails to inform the counterparty on the limitation of liability although this is required, then he is liable to the counterparty with his personal assets jointly and severally together with the company.