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New German Legislation Designed to Curb Suits by Predatory Stockholders

Avocado Law

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Klaus Zapf founded his moving company in the 1970's and made fortune on it. Then he decided to become a Robin Hood and launched a series of lawsuits against German publicly traded companies which earned him a place on the list of German stockholders which was compiled in a recent study by the Institute of Law and Finance in Frankfurt.

Mr. Zapf and his brothers in arms are the prime targets of new legislation enacted by the German parliament recently incentives for predatory stockholders. At the same time, the new law which also transforms an EU directive into national law makes it easier for foreign stockholders to exercise their rights in the general assembly by allowing, inter alia, internet voting.

1 Overview

The new Act, the *Gesetz zur Umsetzung der Aktionärsrichtlinie* (ARUG), implements the EU Stockholders' Rights Directive. Most of the new regulations have become effective as of September 2009.

The ARUG substantially modifies the German Stock Corporation Act (AktG) and addresses two major areas: First, the law aims to prevent or at least to impede the possibility of predatory stockholders filing legal challenges against resolutions adopted at the general assembly (*Hauptversammlung*). Second, the ARUG substantially modifies the rules governing the general assembly of stock corporations to facilitate the participation of stockholders.

2 The end of abusive stockholder suits - difficult times for professional plaintiffs

Since 1980, suits by stockholders involving allegedly illegal stockholder resolutions have increased by approximately 100%. In these cases are filed by a small group of about 40 professional plaintiffs.

If a resolution of the general assembly is challenged, it can normally not be registered in the commercial register, which prevents it from becoming legally effective. This applies in particular to stockholder resolutions regarding capital increases, mergers and profit and loss absorption agreements. Thus, restructuring measures or capital increases would have to be suspended until a final court decision with regard to the underlying stockholder resolution. As in other jurisdictions, professional plaintiffs have often forced companies into financial settlements. Until a few years ago, companies did not have a choice but to agree to such settlements.

The first attempt to curb such vexatious litigation was made in 2005 when a procedural tool – the so-called clearance procedure (*Freigabeverfahren*) was introduced. The clearance procedure allows the company – under certain circumstances – to register a stockholder resolution that has been challenged can nevertheless be registered on the condition that the challenge is, most likely unfounded; or if the need for the resolution to become effective prevails when balancing the potential disadvantages to the company and its stockholders which would result from a delay. Even though these measures were in the right direction, the fix was not complete.

Thus, the ARUG now introduces additional hurdles for professional plaintiffs by modifying the clearance procedure:

Since the main potential for exerting pressure is the delay caused by the court proceedings, these had to be accelerated. Challenging the validity of stockholder resolutions are henceforth rendered by the Higher Regional Court (*Oberlandesgericht*). The Higher Regional Court is final and binding, so that no appeals can be filed. Thus, companies obtain clarity already which in practice means a period of three to four months at most.

A common strategy used by predatory stockholders to buy time is a residence in a foreign country, e.g., in China or Russia. The complicated and time-consuming service of process procedures. Under the new rules, a German lawyer representing a stockholder in an action for avoidance of a resolution is deemed to have authority to represent the stockholder not only in this action

procedure. This eliminates the need for lengthy service of process procedures in foreign countries.

The ARUG also provides courts with more precise guidance for determining whether the interest of the company in a interest of the stockholder to have the resolution declared void by refining the conditions under which the court can i: the registration to go ahead. The court must issue such an order if (i) the action is inadmissible or obviously unfound does not prove that his aggregated shareholding amounts to a face value of at least EUR 1,000, or (iii) the company's i of the resolution due to the foreseeable disadvantages for the company and its stockholders outweigh the disadvantag plaintiff.

3 Deregulation of the general assembly

Furthermore, the ARUG also aims to simplify the rules regarding the general assembly of the company by, inter alia, f information about the general assembly via the Web and making it possible for investors to also attend the general as

Convocation of a general assembly

The ARUG provides for new regulations regarding the convening of a general assembly of the stock corporation. The c assembly must now include specific further information, for instance regarding the rights of the stockholders to put a agenda of the general assembly.

Furthermore, the website of the company now becomes the focal point for the exchange of information between the c stockholders. The way in which information can be provided to the stockholders prior to and during the general assen example, documents which are relevant to the general assembly must no longer be provided in printed form at the cor may be published documents on their website.

Voting made easier

Furthermore, the ARUG simplifies the participation of stockholders in the general assembly. Stock corporations can r much greater extent when preparing and holding general assemblies.

In the past an active participation of stockholders in the general assembly was only possible by personal attendance o proxy. Such personal attendance is no longer required. Now a stock corporation also has the option to permit its stock the general assembly online or via the internet.

An online attendance can be organized in various ways. Stockholders may be allowed to ask questions in real time via general assembly or to vote via the internet. It would also be possible to allow stockholders to speak to the general ass conference. This makes it possible for international stockholders to take part in the corporation's general assembly wi Germany.

However, it must be noted that in case of online participation in the general assembly any disruptions of the internet s shareholder the right to challenge a resolution of the general assembly.

Stock corporations may also allow their stockholders to vote by absentee ballot if they cannot attend the general asser company may determine the details with regard to how such vote must be conducted. For instance, the company may forms to be used by the voting stockholders. However, voting by email would probably not be practical because the se identified.

Voting by proxies

In particular smaller stockholders authorize their bank to vote in the general assembly of the company on their behal was highly complicated. The ARUG makes it much easier for stockholders to appoint a bank as their proxy. The gener: depository bank must vote as stipulated by the stockholder. If no directions are given by the stockholder, the bank ma proposal with respect to the agenda items and may cast the vote accordingly unless the stockholder gives specific inst The bank may, however, also ask the stockholder for a general (revocable) instruction to vote in accordance with the p supervisory board of the corporation. The new regulations regarding proxy voting will most likely enhance the represe stockholders in the general assembly of the corporation.

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