TWO PAGER

Key facts about a specific employment law topic

Pusch Wahlig Workplace Law

Removal and dismissal of limited liability company managing directors

German law distinguishes between the corporate law status and the employment law status of a managing director (Geschäftsführer) of a German Limited Liability Company (GmbH). The removal from the corporate law office and the termination of employment will be subject to different rules as set out below.

1. **When can a managing director be removed?** The removal of a managing director from their corporate function as legal representative of the company is in principle possible at any time without a reason. In companies that are subject to the German Co-determination Act or the Montan Co-determination Act however, the removal of the managing director requires an important reason within the meaning of Section 84 (3) Stock Corporation Code. In addition, the articles of association may restrict the possibility to remove the managing director from their office at any time.

2. **What are the formal requirements for the removal of a managing director?** In principle, the shareholders' meeting is responsible for the removal of a managing director. Exceptions exist for the co-determined limited company (supervisory board) or to the extent the articles of association provide for the responsibility of a different body (advisory board or supervisory board). When inviting to the shareholders' meeting formalities will need to be complied with which result from the articles of association (agenda, invitation deadlines, required majority). The removal of the managing director is usually possible by a simple majority vote.

There is no specific time limit to comply with. However, if removal is only possible where an important reason must be ascertained, the removal has to be implemented as soon as practicable after knowledge of such reason has been gained. Otherwise there is a risk of forfeiture. While § 626 para. 2 BGB would ordinarily impose a two-week period to be met for dismissals, a corporate law removal in this instance does not need to abide by this requirement.

The removal is to be announced to the managing director, insofar as he/she was not present at the shareholders' meeting. The removal of the managing director is subject to registration in the Commercial Register. In order to register in the Commercial Register, the formal resolution by the relevant corporate body must be enclosed in its original version or in a certified copy. Although the registration is only of a declaratory nature, it is necessary in order to avoid that third parties could still validly assume that the managing director is still in office and able to act on behalf of the GmbH.

3. **What are the consequences of the removal for the managing director's employment?** As set out above there exists a principle of separation between the corporate law position and the employment of the managing director. Therefore the removal does not have any direct effect on the employment. So-called „linking clauses" in the service contracts of managing directors are customary, according to which, the removal of a managing director is also regarded as a termination of the service contract of the managing director. According to case law, these clauses are only effective if the removal is deemed to be ordinary termination with observance of the applicable period of notice. In addition, the possibility of ordinary termination must have been expressly reserved in the case of fixed-term management service contracts. A termination of the managing director's service contract without notice is only possible if there is a good cause for such termination, even in the case of a linking clause. Furthermore, the clause must be made transparent against the background of the case law on general terms and conditions.

In the case of doubt as to the effectiveness of the linking cause, as a precaution an explicit termination of the managing director's employment should be issued.

4. **When can a managing director's employment be terminated with notice?** A fixed-term managing director's service contract is not ordinarily terminable unless it allows for an ordinary termination during the fixed term. Thus, at best, extraordinary dismissal may be considered. A fixed-term managing director's employment with the possibility of ordinary termination or an unlimited managing director's employment can be terminated by observing the period of notice. There is no need for a dismissal reason. The Dismissal Protection Act does not apply.

5. **When can a managing director be given extraordinary notice of termination?** All managing director service contracts are subject to the possibility of extraordinary termination irrespective of whether the managing director's service contract is limited in time or for an unlimited period. The requirements are governed by sec. 626 German Civil Code. Serious breaches of contractual obligations in particular are a good cause for termination, such as competitive activity, violation of confidentiality obligations or criminal offences against the company, such as embezzlement, theft or fraud.

6. **What are the formal requirements for termination of the managing director's employment?** In principle, the shareholders' meeting (or, in exceptional cases, the supervisory board or advisory board) is responsible for the termination. When convening the shareholders' meeting and passing resolutions, the aforementioned formalities must be observed. A deadline for giving notice of termination is only to be observed in the case of extraordinary termination.

This is governed by sec. 626 para. 2 German Civil Code. Within two weeks after knowledge of the person entitled to terminate the contract is ascertained, the extraordinary termination has to be served upon the managing director. The statutory period of notice differs according to whether the managing director is a so-called external managing director or a managing shareholder. Longer periods of notice agreed in the service contract shall take precedence over the statutory periods. Although there is no statutory written form requirement for the notice of termination, written form is recommended for purposes of proof. In addition the service contract will usually require written form so that a termination letter with wet ink signatures of authorised persons is required. If the resolution of the shareholders' meeting instructs a representative to give notice of termination, original minutes of the resolution should be presented to the managing director when the notice of termination is handed over in order to prove the power of authority granted. Otherwise, the managing director would have the option of immediately rejecting the termination due to the absence of the power of attorney. Consequence of a valid rejection is the ineffectiveness of the dismissal.

7. **Is there an obligation to continue to employ the managing director after a corporate law removal during the period of notice? If so, does this affect the remuneration of the managing director?** The managing director may not demand any further employment as managing director during the period of notice. However, even in the event of garden leave, the managing director is entitled to continued payment in accordance with the contractual remuneration. Case law states that the managing director is obliged to accept an offer for reasonable activity below the managing director level. Otherwise, the remuneration may be reduced due to intentional failure to make other earnings. However, in principle it is not recommendable to continue employing the managing director in a different role as this may result in an implicit conclusion of a separate employment contract as an employee which may then in turn result in dismissal protection.

8. **What issues are to be considered, if an employee is promoted to managing director?** When an employee is promoted to managing director, the fate of the previous employment contract should be regulated (termination or suspension). Reason for this is that managing directors have a different legal status in relation to employee protection as they are generally not considered employees under German law. Case law assume that the conclusion of a written managing director employment contract will terminate the previous employment contract. However, the prerequisite is that the contracting parties to the employment contract and the managing director's service contract should be the same – due to different corporate law competencies for the conclusion of contracts (managing director for employees vs. shareholders' meeting for managing director) this will often not be the case. If a dormant employment relationship for the managing director is agreed upon, then a termination of such an employment will usually only be possible where there is a reason for dismissal under the Dismissal Protection Act.

9. **What legal protection is available against the termination of the managing director's service contract? What legal action can be taken?** The managing director has the right of appeal to the civil courts. The disadvantage of taking the matter to the civil courts as opposed to the labour courts include considerably longer durations of proceedings and risk of higher costs. According to the case law of the Federal Labour Court, the decisive factor for the opening of legal recourse to the labour courts is whether the removal as managing director has already taken place or will take place before a final decision on the competent jurisdiction. The Regional Courts have jurisdiction before the removal of the Managing Director. After that, the question of the competent court depends on whether claims from a managing director's service contract or an (alleged) employment contract are asserted.

10. **How can the managing director end his term of office?** The resignation of office as a managing director must be made The resignation of office as a managing director must be made to the appointing body, i.e. the shareholders' meeting. For evidence purposes, a written resignation is strongly recommended. Resignation may be effected regularly without notice. In the event of unfaithful resignation or resignation that is ill-timed, claims for damages may be asserted. As a result of the separation principle, the resignation of office will not at the same time be a resignation of the managing director's employment. If a regular termination is possible, then the managing director must also adhere to the notice period. For an extraordinary termination they must also meet the requirements of § 626 BGB (good cause and the two-week deadline for giving notice). If the resignation is done without cause, this may entitle the company to give extraordinary notice of termination of the managing director service contract.