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German Tax and Legal News

German Federal Court of Justice: Liability of a Director of UK-Limited for payments resulting in a reduction of insolvency assets pursuant to German law

The director of a UK Limited can also be liable for payments made after insolvency pursuant to Sec. 64 German Limited Liability Companies Act.

A foreign legal form does not protect the legal representatives from being held personally liable under German Insolvency law

By judgment of 15 March 2016, the Federal Court of Justice (BGH) has ruled that, even a director of a UK Limited, which is subject to insolvency proceedings in Germany can be held liable for payments made after insolvency according to Sec. 64 German Limited Liability Companies Act.

Factual Circumstances

The debtor company was incorporated in the UK, under UK laws as a private company limited by shares (Limited) however operated mainly in Germany via its German registered branch. After the opening of insolvency proceedings over the assets of the company in Germany, the insolvency administrator sought reimbursement from the director of the Limited for payments made after the debtor company became insolvent. The BGH suspended the legal proceedings and requested the ECJ first to decide on the question of whether legal action seeking reimbursement for payments made after insolvency pursuant to Sec. 64 German Limited Liabilities Company Act (GmbHG) is governed by insolvency law or by company law. This question is of major relevance as affairs of foreign EU/EEA companies are generally governed by the company law of the state of incorporation whereas insolvency proceedings and their effects are subject to the applicable laws of the Member State in which the insolvency proceedings are opened. As such in the first case, the director of the UK company would not run the risk to be held liable under German corporate law, like the GmbHG, whilst in the latter case he could be affected irrespective of where the company has been established.

Decision of the BGH

Based on the ECJ ruling of 10 December 2015 according to which legal action for reimbursement of prohibited payments after insolvency according to Sec. 64 GmbHG falls within the scope of insolvency law, the BGH has decided (II ZR 119/14, 15 March 2016) that Sec. 64 GmbHG also applies to a director of a UK Limited. In the Court's view, the purpose of this provision is to avoid payments resulting in a loss or reduction of assets before the opening of insolvency proceedings. In the event that the director fails to comply with his obligation to secure the company assets, it is necessary to restore the company assets to ensure equal payment to all insolvency creditors. Losses of future insolvency creditors shall be covered but not losses of the company. This ratio legis applies to both types of companies as their shareholders in general cannot be held personally liable with their assets for any company liabilities. Both types of companies are managed by a responsible person not necessarily being the shareholder of the company. Since there is a risk in both cases that the director makes payments to the detriment of the insolvency creditors and thereby reduces the insolvency assets, it is justified that both the director of the German GmbH and the director of the UK Limited are treated equally with regard to the liability for such prohibited payments.

Conclusion

This landmark decision opens the way for liability claims of German insolvency administrators against directors of companies established outside Germany but having a German branch and/or mainly operating in Germany in case of insolvency proceedings over the assets in Germany. Moreover, it can be assumed that other legal instruments such as the liability for delaying insolvency proceedings or for causing insolvency and the liability for repayments of shareholder loans will also be subject to insolvency law. As a result, the

directors of foreign companies can also be held liable on the basis of these provisions.

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