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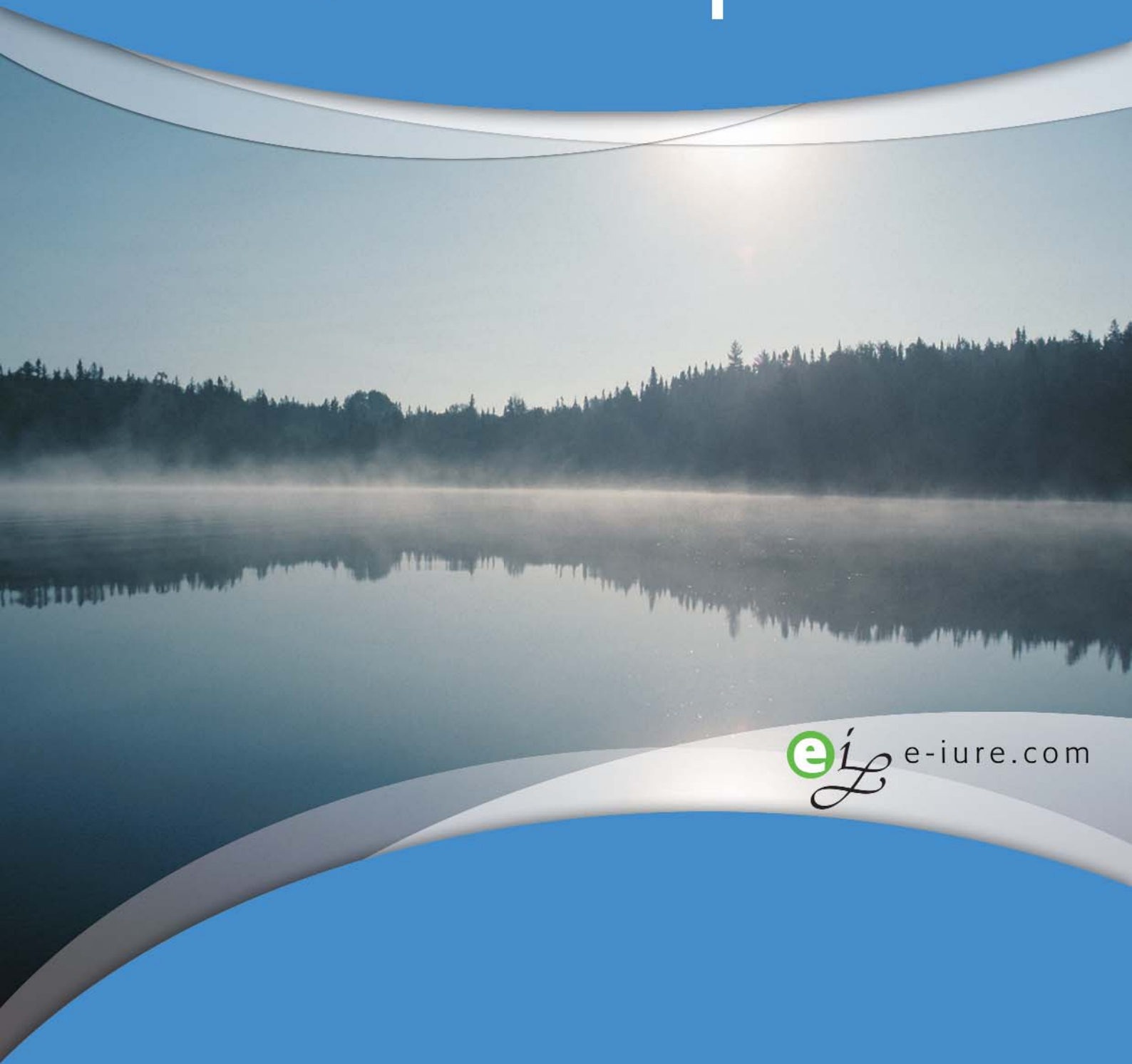

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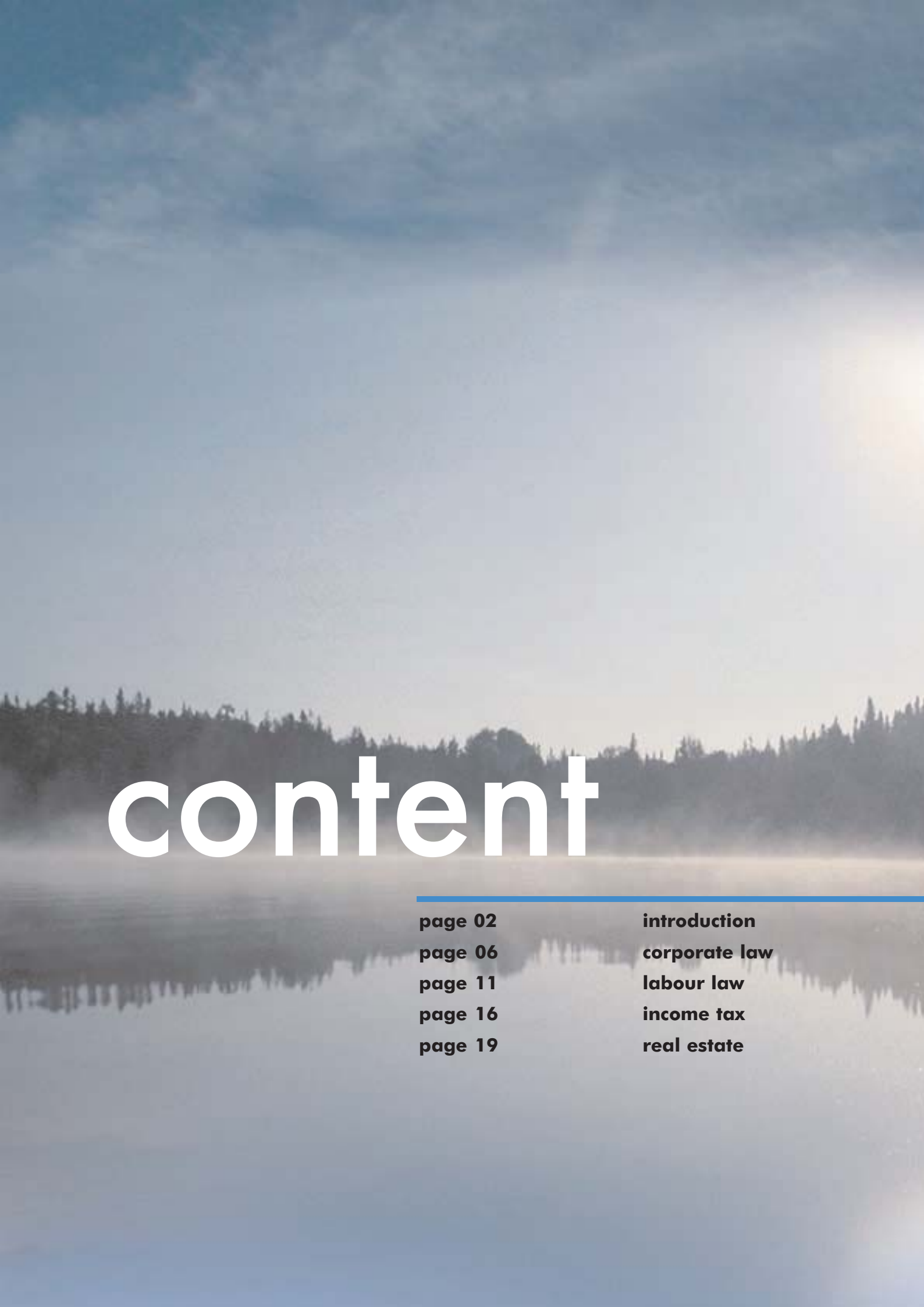

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Since its foundation some 25 years ago in Cologne, at the economic and geographical heart of Germany, JUNGE • SCHÜNGELER & PARTNER has been mainly focusing on advising enterprises and corporations and their respective operations on corporate, business, labor and trade law both in Germany and abroad. Over the years, these core competences have been consequently expanded to other fields like Bankruptcy and Creditors rights, M&A, Tax Consulting, Trademark & Patent Laws, Contracts, Family and Inheritance Law, Non-Profit Organizations, Real Estate and Construction Law.

Being strongly business-oriented from the outset, JUNGE • SCHÜNGELER & PARTNER has developed a philosophy of pragmatic "deal making" instead of "deal breaking." We consider the law to be just another tool to achieve and increase the economic success of our clients. In an increasingly complex and specialized economic environment, this approach requires profound knowledge about national and international tax systems and jurisdictions. In addition to the extensive know-how on this subject provided by the several tax advisors in our own ranks, a very close cooperation with the renowned ZWP ROTONDA GmbH auditors and tax consultants puts us in a position to offer tailor-made solutions to our clients' wide-ranging needs and requirements, from very specific legal advice to the elaboration of their financial statements.

Anticipating the far reaching impact of globalization and European integration, JUNGE • SCHÜNGELER & PARTNER readily responded to its clients' growing expectations of an international service by joining several international networks and developing close ties to a large number of individual correspondents worldwide and nationwide years ago. We therefore are well prepared to meet any challenge in our field, relying traditionally on cooperation on a non-exclusive basis, choosing German and international correspondents alike in response to the specific requirements of each case. Due to its international alignment and its strongly developed approach to international teamwork, JUNGE • SCHÜNGELER & PARTNER is able to provide truly international service for its clients both in Germany and abroad.

As a team of highly qualified and internationally trained lawyers, tax consultants, paralegals and professionals, we are fully committed to giving our clients outstanding care and advice and meeting their needs, expectations and objectives by providing them with the most effective, efficient and high standard of legal services.

The principal areas of the firm's practice are:

- Corporate including M&A
- Commercial and Trade Law
- Labor Law
- Trademark & Patents Law
- Tax Consulting
- Contracts
- Real Estate and Construction Law
- Non-profit organizations
- Family and Inheritance Law

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Regulations and Rules

German corporate law offers a wide range and broad variety of legal forms for conducting business, which reaches from the sole proprietorship via branches to various forms of corporations and partnerships. Unlike some other major Continental legal systems, the German corporate law is not integrated into one sole code as might be the case with the French Code de Commerce, but split into different codes.

The Civil Code (Bürgerliches Gesetzbuch - BGB) deals with company law in Articles 705 to 740, setting the legal framework for civil-law associations (Gesellschaft bürgerlichen Rechts – GbR). Regulations concerning partnerships are to be found in the Commercial Code (Handels Gesetzbuch - HGB). The two major types of corporations, the limited-liability company and the stock corporation, both have been regulated individually in their own Code, the Private Limited Company Act (Gesetz betreffend die Gesellschaften mit beschränkter Haftung - GmbHG) and the Stock Corporation Act (Aktiengesetz-AktG).

The German Reorganization of Companies Act (Umwandlungsgesetz – UmwG) furthermore provides a variety of ways to transform and merge existing business without generating the necessity to either liquidate the company or transfer single assets and liabilities. Recently a Corporate Governance Code has come into force, applicable to quoted companies.

Types of Companies and Liability of Shareholders

Investors willing to set up a business in Germany are necessarily restricted in their choice of entity to the legal forms provided by the above mentioned laws, which nevertheless provide a broad range of possibilities to conduct business. A foreign individual may wish to start business as a sole proprietor (Einzelkaufmann) or as a branch of a foreign entity (Zweigniederlassung). If he prefers to set up a legally independent entity in Germany, he may instead select between several forms of partnerships (Personengesellschaften) or corporations (Kapitalgesellschaften). The legal forms most commonly adopted by foreign investors and German businesses alike are the following:

1. Aktiengesellschaft (AG) (Stock Corporation): The AG is a separate legal entity with the liability of the shareholders restricted to the value of the corporation's assets including its share capital and outstanding contributions. The statutory minimum share capital is €50,000 and has to be fully subscribed. At least 25% of the share capital must be paid in by the date of application for registration in the commercial register.

This is the corporate form adopted by most of Germany's largest companies with the major advantage that its shares can be transferred rather easily and be listed on a stock exchange, making it relatively easy to raise capital from the public. Since the AG tends to enjoy a higher market reputation and its independent management is not bound by shareholder instructions, it has also been adopted by some smaller and privately owned businesses lately. On the other hand, the AG is subject to a large number of mandatory legislative regulations, which make its handling rather complex and sometimes might give little option to adapt the bylaws to specific shareholder requirements. Furthermore certain standards regarding the bylaws of listed AG's have come into practice and should be observed, at least if the AG considers being listed at the stock exchange.

2. Gesellschaft mit beschränkter Haftung (GmbH) (Private Limited Company or Limited-Liability Company): The second major form of corporation in German corporate law is the GmbH, which is the corporate entity most commonly used for enterprises in Germany. The minimum share capital of a GmbH is €25,000, divided into shares (Geschäftsanteile) which may have different nominal amounts and be in cash or in kind. With a clear and stable shareholder structure and

total liability protection for its shareholders – the liability is limited to the value of its assets including its share capital - the GmbH is designed to suit the necessities of private business. It is easier to establish and administer than the AG, and its bylaws (Gesellschaftsvertrag) may more easily be adapted to the requirements of the shareholders. Unlike the AG, Shareholders retain overall control over the appointed management. Being usually closely held, the GmbH is generally not subject to as many regulations as the AG might be. It must have a minimum of 1 shareholder and is not restricted to a maximum number. Domestic and foreign corporations and partnerships as well as individuals may become shareholders. A GmbH is established by executing a deed of formation and bylaws before a German notary. The bylaws need to include the registered domicile, the purpose and its share capital. The GmbH does not come into corporate life until it is registered at the local commercial register, where the bylaws become part of the public record. Should the GmbH commence business operations before, the shareholders may incur personal liability.

3. Offene Handelsgesellschaft (OHG) (General Partnership) and Kommanditgesellschaft (KG) (Limited Partnership): Besides AGs and GmbH's, Partnerships regulated by the German Commercial Code (HGB) continue to play an important role in German business life today. These partnerships are divided into general partnerships (OHG) and limited partnerships (KG), the main difference being the liability of the partners. All partners of an OHG are jointly and severally liable for all of the partnership's business debts. A limited partner of a KG, however, is only liable up to its subscribed and registered contribution of minimum €1 (Kommanditist), although the KG must have at least one general partner (Komplementär); the general partners are fully liable. This is reason enough for foreign investors to frequently set up a KG when choosing a partnership structure for their business.

Partnerships have quasi-legal status and can enter into contractual relationships, own assets and incur liabilities in their own name. To set up a partnership at least two partners are required, who can be either individuals, (foreign) corporations or other partnerships. The formation of a partnership requires the execution of a partnership agreement and has to be followed by registration at the relevant commercial register. To achieve the desired liability protection for the limited partners, the subscribed liability contribution must be properly registered to become legally effective.

In principle, the partners may freely agree on their rights and obligations in the partnership agreement, leading to a great flexibility in tailoring the internal affairs to the needs of the partners. Another advantage of partnerships compared to the AG and GmbH are the fewer publication requirements, the easier way to dissolve a partnership and to distribute its capital to the partners, direct management by the partners, and an advantageous gift and inheritance tax, making it especially attractive for smaller and family-owned businesses facing a generation shift. The transfer of any partnership requires an agreement between the transferee and the transferor, signed with the consent of all partners, unless the partnership agreement provides otherwise.

4. GmbH & Co KG (Corporation & Co KG): A quite common way in German corporate law of achieving the advantages of a partnership structure, without the frequent inconvenience, is to have a corporation with more or less no capital contribution as the sole general partner. The so called GmbH & Co KG grants all its partners to a certain extent security from unlimited liability, combining the advantages of a partnership with the liability limitations of a corporation. Small wonder a significant number of family-owned and medium-sized businesses in Germany have opted to do business under the legal form of a GmbH & Co KG.

5. Gesellschaft Bürgerlichen Rechts (GbR) (Civil-law association): A civil law association (GbR) is a partnership which has no registered business name and does not constitute a corporate entity separate from the partners. To set up a GbR, at least 2 partners are required to execute a partnership agreement. There is no registration needed. A GbR is usually used for non-commercial purposes (e.g. associations of professionals), or for individual contracts and transactions for a limited period (e.g. construction projects).

6. Sole proprietorship (Einzelkaufmann): The owner of a sole proprietorship is engaged in a typical commercial business and personally liable for all debts. His business must be registered at the commercial register (Handelsregister).

7. Branches (Zweigniederlassung): A foreign company not interested in doing business through a separate German legal entity may establish a branch in Germany. The branch has to be reg-

istered in the commercial register (Handelsregister) located at the local court of its registered office. Although contracts may be signed in its name, a branch is not a separate legal entity. For registration the court will request evidence of the existence of the foreign company such as copies of the articles of association, the amount of the share capital, the names of the managing directors etc. This information must be registered and kept up-to-date at the commercial register and in the German Federal Gazette (Bundesanzeiger).

Due to recent rulings of the European Court of Justice, German business is increasingly showing interest in the newly achieved possibility to establish its business in the form of a UK registered and seated Ltd or its different EU counterparts, which now is perfectly entitled to carry out business in Germany just by establishing a branch there without any form of discrimination, even if its business activities are carried out entirely in Germany. As this is a relatively new and untested approach, it remains to be seen whether the UK Ltd or similar EU corporations like the Spanish S.L. or French S.a.r.l are set to undermine or seriously replace in any way the GmbH and the AG as the two major legal forms of corporations in Germany.

Share Capital

As mentioned above, the statutory minimum share capital is €25,000 for the GmbH and €50,000 for the AG. It has to be subscribed in full. If it is contributed in cash, only € of the share capital of a GmbH, but at least a minimum contribution of €12,500, must be paid in by the date of the application for registration at the commercial register. In case of the AG, € of the share capital plus any premium must be paid in. Should either a GmbH or an AG be established by a single shareholder, either the full amount has to be paid in or security provided for the outstanding amount. Contribution in kind is possible, but must be fully effected in a way that assures that the assets are at the permanent disposal of the managing directors. German corporate law is strongly focused on ensuring that the share capital is duly paid in and maintained. A GmbH therefore is not allowed to make payments to shareholders that would reduce its net assets to a level below its stated share capital. The AG is subject to even stricter rules, which do not permit a company to repay share capital contributions to the shareholders regardless of whether such payments would reduce the AG's net assets to a level below its stated share capital or not.

The share capital of a GmbH is divided into shares (Geschäftsanteile) that can have different nominal amounts and which are not issued in the form of certificates. Each shareholder holds a share in the amount of the original contribution (Stammeinlage). The share must total at least €100. A share in a GmbH may be transferred by assignment or inheritance. The contractual transfer of shares has to be documented in notarial deeds and can be made conditional upon the consent of the GmbH, its articles or any other holder of shares.

The share capital of an AG is divided into shares that may be issued either with a par value (Nennbetragsaktien) of at least €1 per share or multiples thereof, or without par value (Stückaktien). Shares may not be divided and in general carry one vote each. They may be issued as bearer shares (Inhaberaktien), which are owned simply by the person who holds them, or registered shares (Namensaktien), in which case the name of the owner is registered in the company's share register. Additionally, shares can be issued as ordinary shares (Stammaktien) or preferred shares (Vorzugsaktien). Bearer shares enjoy free transferability. The corporation is not allowed to restrict in any way their transfer, whereas registered shares might be bound by stipulations of the articles providing that a transfer requires the consent of the company.

Corporate Governance

Shareholders meetings

Shareholders decisions are made through shareholder resolutions passed in general meetings (Hauptversammlung) in case of an AG and shareholders meetings (Gesellschafterversammlung) in case of an GmbH.

For an AG a general meeting is to be held each year within 8 months after the end of the financial year. It is convened by the management board. Additionally the management board, the advisory board or shareholders holding at least 20% of the share capital are entitled to call an extraordinary general meeting. Shareholders resolutions regularly require a simple majority of

more than 50%, unless mandatory law requires a greater majority (e.g. 75% as may be the case for amendments to the bylaws or increases or decreases in capital, transfer of all assets, or change of the corporate form) or the articles provide otherwise. The statutory rights of the general meeting include among others the appointment of members of the advisory board, the distribution of profits, the formal approval of the board members (management and advisory) with respect to their activities during the preceding financial year, the amendment of the articles as well as the liquidation and the reorganization of the AG.

For a GmbH, the managing director usually convenes general meetings of the shareholders. As is the case with the AG, at least one meeting is to be held each year within 8 months after the end of the financial year. Additionally the holders of 10% of the share capital are entitled to call a general meeting. Shareholders resolutions regularly require a simple majority of more than 50% of the votes cast, unless the bylaws of the GmbH require a greater majority. In some cases a majority of 75% is required by mandatory law as may be the case for amendments to the bylaws. The statutory rights of shareholders at the shareholders general meetings include, so long as the articles/bylaws do not provide otherwise, the appointment of managing directors, the review of their activities, the distribution of profits, the amendment of the bylaws and the approval of the financial statements.

Decision-making bodies

The AG is required to have a management board (Vorstand), which manages and represents the company in and out of court. The management board is appointed by the supervisory board for a term not to exceed 5 years and is independent both with regard to the shareholders and the supervisory board itself for the term of service. Neither the shareholders nor the supervisory board may issue instructions to the management board. During their term in office, the members of the management board can only be dismissed for cause. The shareholders and the supervisory board therefore lack any direct influence on the management of the AG. A limitation on the statutory authority of the management board is not effective against third parties, although internal rules may subject it to certain restrictions as might be the case with specific transactions which require approval of the supervisory board.

A GmbH is managed and legally represented by its managing director (Geschäftsführer). A GmbH must necessarily have one managing director but can have as many as desired. The principle of collective management and representation applies if the articles do not provide for something else. The managing director does not need to be a shareholder, a German citizen or even resident. However he must be an individual and hence not a corporate entity. The power to appoint and remove managing directors at any time belongs to the shareholders. The power of representation towards third parties cannot be restricted. Nevertheless the management authority (Geschäftsführungsbefugnis) can be restricted internally and shareholders may exercise their right to give managing directors instructions regarding any particular issue on which they wish to exercise their influence.

German law does not provide any specific rules limiting the fees of an AG's management board (Vorstand) or a GmbH's managing directors (Geschäftsführer). Nevertheless at least as far as the GmbH is concerned, the German Supreme Court (BGH) has ruled that if the fees exceed an appropriate proportion of the after-tax profit, the company is entitled to decrease the fees unilaterally.

Both the AG's management board and the GmbH's managing directors are bound to the company by a fiduciary duty and a duty of care and skill, leading to their far reaching liability for significant violations resulting in damage to the company.

An AG is obliged by law to have a supervisory board (Aufsichtsrat) in addition to the management board, the function of which basically consists in supervising and advising the management board, appointing its members, appointing the statutory auditor, reviewing and approving the annual financial statements, as well as representation of the AG in dealings with the management board. The supervisory board is not entitled to participate in the corporation's day to day management, but may nonetheless determine that certain categories of transactions have to be subjected to its approval. In case the approval is denied, the supervisory board may appeal the decision to the shareholders. Except for special provisions regarding the participation of employee representatives, the members of the supervisory board are elected by shareholder resolutions. The special rights of employees referred to federal laws, the "Drittelbeteiligungsgesetz" and the "Mitbestimmungsgesetz" (MitbG) or "Co-Determination Act," which give employees represen-

tation on the supervisory board. The "Drittelbeteiligungsgesetz" provides that all GmbHs with more than 500 employees as well as all AGs irrespective of their workforce, must allow employees to elect one third of the members of the supervisory board. The "Mitbestimmungsgesetz" or Co-determination Act requires that all companies with more than 2000 employees must grant their employees equal representation with shareholders on the supervisory board.

In case of a GmbH, a supervisory board is mandatory only if the GmbH has more than 500 employees. Should the company not reach that size, shareholders may nonetheless form a supervisory board or alternatively an advisory board ("Beirat") and to provide for their functions in the articles.

Accounting and Publication Requirements

All commercial businesses in Germany are subject to a bookkeeping requirement. In addition they have to prepare financial statements as of the end of each fiscal year in accordance with German GAAP. For corporations as well as commercial partnerships with no individual as general partner (GmbH & Co KG) the following special provisions also apply: Annual financial statements as well as profit and loss accounts regularly have to be established within 3 months, in special cases exceptionally within 6 months. There are special provisions regarding the format of the balance sheet and the evaluation of the assets and liabilities. Moreover, a management report is mandatory. Both management report and financial statement must be audited by a certified accountant (Wirtschaftsprüfer). There is an exception if the company does not exceed certain thresholds pertaining to its balance sheet total, turnover and number of employees (kleine Kapitalgesellschaft or "small company"). Corporations and partnerships with no individual as general partner are also required to file their financial statements at the commercial register and publish them in the Federal Gazette (Bundesanzeiger).

Quoted Companies

German corporate law does not in principle make any distinction between quoted and unquoted corporations or impose special rules on quoted corporations. Since 2002, however, quoted companies are subject to a mandatory corporate governance code.

Junge, Schüngeler & Partner
RA Michael Wirges

Employment contracts / Costs of wrongful dismissal

Generally there are two types of working contracts, such as temporary contracts and non-temporary contracts. A temporary contract needs to be fixed in written form. The limitation can be up to 24 month without reason. If an initial period is shorter then 24 month, the contract can be extended up to three times, not exceeding 24 month.
The costs of wrongful dismissal are not foreseen by german labour law. The actual costs depend upon the particular case but should be considered with about 50 % of the gross salary per month for each year of the duration of the working contract.

Collective Bargaining Agreements

Collective bargaining is carried out on a national or industry-wide level as on a regional or local level. Said agreements apply only to those employers and employees who are members of the respective employer organization respectively trade union unless the agreement is declared to be generally binding by the Federal Department for Labor and Social Affairs. Some 516 collective bargaining agreements of a total of 57,600 are currently declared to be generally binding.

Works Councils and Co-determination

Works councils can be formed in all companies with five or more employees. The members are elected for four years and need not be union members.

The rights of the works council, as set forth in the Works Constitution Act (Betriebsverfassungsgesetz, BetrVG), range form information rights to codetermination rights in organizational, social and other matters. In social matters, the employer is obligated to negotiate rules with the works council on the allocation of working hours, vacation schedules, grievances and matters of safety and welfare. The works council must be informed prior to the dismissal of any employee. The employer and the works council must under certain circumstances negotiate a reconciliation of interests and a social compensation plan in the case of mass redundancies in order to compensate employees for the actual and financial disadvantages suffered as a result of dismissal.

The most important co-determination laws are currently the so called “Drittelbeteiligungsgesetz” and the Co-determination Act 1976 (Mitbestimmungsgesetz, MitbG).

The so called “Drittelbeteiligungsgesetz” , provides that all GmbHs and AGs with more than 500 employees as well as all AGs irrespective of their workforce, if registered in the commercial register prior to August 10, 1994 and not family-owned must allow employees to elect one third of the members one the supervisory board.

The Co-determination Act 1976 requires that all companies with more than 2,000 employees must give employees equal representation with shareholders on the supervisory board. Employee representatives must include at least one management employee representative. The

chairman (usually a representative of the shareholders) has the deciding vote in the event of a tie.

Wages, Salaries, Bonuses, Working Hours, Holiday and Vacation

Law in Germany prescribes no minimum wage. Minimum wages are, however, often fixed by collective bargaining agreements in different industries. Equal pay legislation exists on a federal level providing equal pay for men and women. Although not a legal requirement, a thirteenth month salary/bonus is usually paid at Christmas,or split between Christmas and vacation time.

The general legal maximum is 40 hours per week (based on a five-day working-week), which can be extended up to 50 hours provided, however, within approximately six months the average will not exceed 8 hours per day. Trade unions are lobbying for a 35-hour week and collective bargaining agreements often provide for a shorter weekly working time (e.g. 38.5-hour week). Overtime is strongly opposed by unions.

All German states recognize the following public holidays:

New Year´s Day (January 1), Good Friday, Easter Monday, May Day (May 1), Ascension Day, White Monday, German Unity Day (October 3), Christmas Day (December 25), December 26.

Certain religious holidays exist in addition thereto which differ from state to state.

The minimum legal vacation is 20 working days annually after completing six months of employment. Collective bargaining agreements as well as individual employment contracts usually increase the number of vacation days (often up to 30 days or more per year) while state laws provide for leave for special purposes (i.e., educational leave). An employee is entitled to receive vacation pay equal to his or her current salary during vacation. Several collective bargaining agreements as well as business practice provide for an extra vacation bonus.

Employment Regulations

The Employment Protection Act provides that giving notice without an important reason to an employee who has worked in the same company for more than six months is only legally effective to the extent it is socially justified. The Employment Protection Act only applies, however, if the plant or shop regularly employs more than ten individuals based on full-time positions. Part-time positions are only counted proportionally (up to 20 hours per week = 0,5; up to 30 hours per week = 0,75).

Social justification within the meaning of the Employment Protection Act is limited to three principal areas. Firstly, the termination of employment may be due to the personal circumstances of the employee such as a series of short-term illnesses or a long-term illness. Secondly, the behavior of the employee may constitute social justification for termination, i.e. being absent from work without excuse despite repeated warning or refusal to work. Prior to issuing a notice of termination in such cases, the employer has to give a warning to the employee with regard to his or her shortcomings. Thirdly, a dismissal may be socially justified if based on operational reasons. In particular, this can be based on changes in the employer´s business organization resulting in redundancies of the relevant job due, for example, to a plant closing or reduction of the work force due to a shortage of orders. However, the employer has to apply the so called

"social factor method" considering the social data (age, seniority, maintenance obligation) in order principally to select those employees for dismissal first, who are the "least disadvantaged" by the redundancy. The employee has the right to challenge said notice and to file a cause of action for re-employment with the competent labor court within a three-week period after receiving the notice. A statutory severance payment does not exist.

The termination of an employment relationship under the Employment Protection Act is usually complicated and often results in paying off the employee through a settlement agreement. As a general and rough rule, an average severance payment amounts to about 50 % of the monthly gross salary for each year of service.

Additional employment protection exists for works council members, disabled employees, pregnant employees and employees on educational leave; said employees may not be terminated except for cause. Any termination, however, requires the prior consent of the competent authorities.

Social Security

Germany has a compulsory social security system that covers five principle areas: health and nursing care insurance, old-age-benefits, unemployment benefits and workers´ compensation. Contributions to the social security system are generally shared equally between the employer and employee.
The employer withholds the employee´ s share of the contribution to the Federal Insurance Agency.

Benefits from public health insurance include the payment of medical and hospital expenses and compensation for loss of salary. Contributions to the public health insurance system are only payable up to certain salary levels, which are usually increased annually. As of January 1, 2007 , only employees with a gross salary not exceeding € 42.750 annually or € 3.562,50 are obligated by law to make contributions to the public health insurance system. No compulsory health insurance exists beyond these salary thresholds; employees exceeding said thresholds might therefore opt to maintain a private health insurance, to continue the participation in the public health insurance system or to have no health insurance at all (which is rare). The exact rate of public health insurance depends on the individual insurance company but usually amounts to approximately 15,1% of gross salary (above caps apply). If the employee is not subject to compulsory health insurance, the employer must contribute up to € 236,91 per month (official average premium) to the employee´ s private health insurance.

Contributions to the nursing care insurance plan amount to 1,7% of gross salary capped again at € 42.750 annually or € 3.562,50 monthly. If the employee is not subject to compulsory health insurance, the employer must contribute up to € 33,46 per month (official average premium) to the employee´ s private nursing care insurance.

Old-age contributions are currently levied at a rate of 19,9% of gross salary capped at € 63.000 annually or € 5.250 monthly (Western part of Germany) and € 56.600 annually or € 4.550 monthly (Eastern part of Germany).

Unemployment insurance contributions amount to 4,2% of gross salary capped as well at € 63.000 annually or € 5.250 monthly (respectively € 56.600 annually/€ 4.550 monthly in the Eastern part of Germany).

Effects of § 613a BGB

In general the rule of § 613a BGB states, that in case of a so called "Betriebsübergang", which is the sale of a firm by legal transaction, the purchaser is stepping into the rights and obligations of the working contracts between the seller and his employees existing at the time of the transaction. This means, that all working contracts, which exist between the seller and his employees, automatically pass to the purchaser by law.

Some effects of the rule of § 613a BGB have to be considered even before the actual transaction has taken place.

For instance:

The employees, who will be effected by the transaction, have to be informed in detail either by the seller or the transferee about:

The date or the planned date of the transaction;
the reason for the transaction
the legal, economical and social effects of the transaction for the employees and
the planned measures (for instance further education) regarding the employees.

The time span between the information of the employees and the actual transaction depends upon the particular case, although it should be one month at least. The employees` right of protest, which is provided to the employees by law, against the transferration of their working contract onto the purchaser has to be considered thereby.

Due to the rule of § 613a paragraph 6 BGB the employees do have the right to protest against the transferration of their working contracts onto the purchaser. The protest has to be done in written form and within one month after the receipt of the above mentioned information.

The consequence of such a protest is, that the working contract of the protesting employee is not being transferred, but will furtherly exist between the seller and the protesting employee. Since the seller will not be leading the firm any more after the transaction has taken place, the purchaser is generally justified to terminate the working contract for operational reasons.

The above mentioned obligation of information must be followed in any case, because without a regular information of the employees, the time limit of the employees` right to protest will not even start to run. This leads to the fact, that the working relationship will remain between the seller and the employee until the employees have regularly been informed about the above mentioned points. Therefore, personal measures, such as the termination of a working contract, can only be done by the purchaser himself after the employees have been regularly informed.

Even if all information obligations have been fulfilled regularly and the transaction itself has taken place, it is forbidden by § 613a paragraph 4 BGB to use the transferration of the company itself as a reason for the termination of a working contract. However, a termination of a working contract, which is based upon the other reasons, which are admissible in German labour law, such as operational or personal reasons or the behaviour of the employees, is generally possible at any time and is not at all restricted by the transferration of the company.

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German income tax law is regulated mainly in the German Income Tax Act (" Einkommensteuergesetz ") for individuals and partnerships, the Corporate Income Tax Act (" Körperschaftsteuergesetz ") for corporations, and the Trade Tax Act (" Gewerbesteuergesetz ") for individuals, partnerships and corporations with respect to income generated from trade. The following information relates to applicable law of 2007.

Personal Income Tax

Income tax is based on an individual's worldwide income from all sources if the individual is subject to unlimited taxation (tax residence) in Germany. If an individual is not a resident for German tax purposes, limited taxation applies, on income from German sources.

German tax law has seven categories of taxable income, one of which is income from trading which is subject to the trade tax as well:

- Income from agriculture and forestry
- Income from trading
- Income from professional and other independent personal services
- Income from employment
- Income from investment
- Rental and royalty income

Other income

Taxable income allows several deductions from the gross income, especially income-related expenses and the trade tax.

The tax rates are calculated on a calendar year basis with separate tax tables for single and married taxpayers. After a tax-free allowance of €7,664 for singles and €15,329 for married couples, the tax rate starts with a minimum rate of 15% and continues progressively up to 42% plus a solidarity surcharge of 5.5% of the tax liability. The maximum tax rate of 42% is reached with a taxable income higher than €52,152 for singles and €104,304 for married couples. For 2007 only, the maximum tax rate is exceptionally increased to 45% for certain incomes higher than EUR 250,000 for singles or EUR 500,000 for married couples.

Corporate Income Tax

The most common German corporate entities are the limited-liability company (GmbH) and the stock corporation (AG). Corporate entities pay a flat rate of 25% tax plus a 5.5% solidarity surcharge from the income calculated on the base of the Corporate Income Tax Act, unless the Act provides otherwise. Corporate entities are subject to trade tax as well, regardless of the nature of the income.

A corporate entity which is a German resident for tax purposes is subject to corporate income tax on its worldwide income. Corporations whose seat and place of management are located outside of Germany are subject to taxation on their German source income only.

Branches and permanent establishments operating from Germany are subject to German corporate income tax and trade tax on their branch profits.

With the new "half-income" system starting in 2002, any dividends received by a German corporate entity from a corporate entity are generally exempt from corporate income tax and trade tax as well. However, 5% of the dividends are deemed to be a non-deductible expense, so that in fact only 95% of the dividends are tax-exempt.

Individuals who receive dividends from a corporate entity are tax exempt to the amount of 50%.

The corporate entity has to withheld 20% (plus 5.5 % solidarity surcharge on the withholding tax) of all dividends at source. The amount withheld in relation to German resident recipients is available as a tax refund or credit against their German income tax or corporate income tax liability.

When the thin capitalization rule applies, interest on shareholder loans is assumed to be a dividend and is not deductible from income. Under the thin capitalization rule, interest is classified as a dividend if:

- payments on behalf of loans will exempt the amount of € 250.000 and
- the shareholder has a substantial holding in the corporation (which means he directly or indirectly owns more than 25% of the corporation's shares), and
- the interest is not calculated as a proportion of capital, or
- the dept-equity ration exceeds 1.5:1 (safe haven), unless the corporation would have received the dept capital from a third party on the same conditions.

Trade Tax

Trade tax is a tax on the trading income of an individual, a partnership or a corporate entity payable to the local municipalities. Each municipality is entitled to determine its own effective tax rate by setting a multiplier which is applied to the basic rate.

The basis for trade tax is calculated on the basis of the German Income Tax Act or the Corporate Income Tax Act with a number of adjustments. The most important adjustment is the non-deductibility of 50% of interest paid on long-term loans.

Trade tax ranges from about 13% to 20% depending of the municipality tax rate.

Trade tax related income generated by individuals or partnerships is subject to a certain deduction for purposes of personal income tax.

Income Taxation of Partnerships

The most common German partnerships are the general commercial partnership (oHG) and the limited partnership (KG).

For purposes of German income taxation a partnership is transparent. As a first step the income of the partnership is calculated according to the German Income Tax Act and the German Trade Tax Act. After deduction of the trade tax, which is payable by the partnership after a tax-free allowance of €24,500, the remaining income will be allocated to the respective partners.

At the level of each partner, and only there, the allocated income is subject to income tax or corporate income tax depending on whether the partner is an individual or a corporate entity.

2008

Beginning with the year 2008 there most probably will be a flat tax rate for both corporate and trade tax together of about 30% for corporations. This rate will apply optionally as well for partnerships.

Treatment of Losses

Tax losses of individuals and corporate entities are allowed to be carried back one year, up to an amount of €511,500. If the losses exceed €511,500 or cannot be fully carried back into the previous year, losses will be carried forward up to an amount of €1,000,000. Higher losses can only be offset against profits, up to 60% of the taxable income. No limitations exist on the use of losses carried forward.

Tax losses will be cut off completely if the economic identity of the corporation changes. This is assumed if more than 50% of the shares of the corporation are transferred within a period of 5 years and the corporation continues its business with predominantly new assets.

For purposes of the trade tax, losses of individuals, partnerships or corporate entities will be carried forward. Within a partnership a change in partner will lead to a loss of proportionate trade tax loss carryforwards. Trade tax losses cannot be carried back.

Value Added Tax

All individuals and entities who independently carry out an income-generating trade, business or other profession are subject to VAT.

The German VAT system in general ensures that the end customer bears the VAT. VAT is charged at the rate of 19% of turnover. The reduced rate is 7%.

There are many exemptions from VAT, of which the most important are all transactions which are subject to real estate transfer tax, residential rental, all business carried out by banks and insurance companies, and export of goods.

Property Tax

Property tax is levied annually by all municipalities on land and buildings located in their region. The usual basic rate is 0.35% of the tax value of the property. The result is then multiplied by a percentage which is determined annually by each municipality.

Real Estate Transfer Tax

Real estate transfer tax is charged at a rate of 3.5 % of the tax value of real estate sales and other transactions which are considered to be a transfer of real estate, such as the transfer of at least 95% of a company owning real estate.

Inheritance and Gift Tax

Inheritance and gift tax is charged on the transfer of assets as a gift or by inheritance. Tax rates vary between 7% and 50%, depending on the degree of family relation and on the value of the property inherited or bestowed. Tax allowances are available for both spouses and children and also for the transfer of business assets and shares in domestic corporations.

Other Taxes

Other taxes that may be relevant are ecology tax (electricity tax, mineral oil tax), church tax, insurance tax and vehicle tax.

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The German law concerning real estate covers all matters connected to immovable property. The definition of real estate includes the following aspects:
in a factual sense, an indicated area on the earth's surface,
in a legal sense, an indicated area on the earth's surface registered on a separate page under a certain number in the German land register,
in the cadastral sense, a land parcel, and
in an economic sense, an indicated area on the earth's surface which forms an economic unit, but the unit includes not only the surface of the earth, but also the airspace above and earth below the surface.

Types of Ownership

A natural or legal person may be the sole owner of real estate.
In the case of joint property, all owners hold the real estate jointly. Each co-owner owns an ideal (not physical) part of the real estate. Under German real estate law, each ideal part of real estate is treated as if it were owned by a sole owner, so the co-owner can have his part to his own disposal and can, in particular, sell or encumber it unilaterally. There is an exception to this rule in the case of decisions that affect the real estate as a whole, which must be made jointly by all co-owners.

As there was a great need for residential space after World War II, it became necessary to let people take part in financing their housing and give them property equivalents for their invested money. Thus a law concerning "property in a freehold flat" ("Wohnungseigentum") was introduced, which offers the possibility of acquiring property in only a part of a residential structure. The real estate in such case includes the individually-held property of the flat or office (including constituent parts like balconies), plus an ideal part in the shared joint property in the whole building (all facilities and equipment belonging to the building and necessary to maintain it, or used by all co-owners jointly such as stairways or utility lines, laundry or storage rooms used by all proprietors) which is not part of any individually held property. The individually held property and the ideal co-ownership cannot be separated.

Another noteworthy feature of German real estate law is the "heritable building right" ("Erbbaurecht"). A basic principle of German real estate law is the unity of property of a building and the land of which the building is a permanent part. But the law authorizes an exception from that principle in case of the heritable building right, where the property of a building differs from the property of the land on which the building is built. Here the beneficiary has a property right in the building only for a limited time, and concerning the land the status is very similar to that of a full proprietor. The heritable building right is a charge on the land because it limits the rights and powers of the ultimate owner; as compensation, the beneficiary is obliged to pay ground rent to the owner. The heritable building right is a right equal to the rights to real estate, and so it is transferable and may be encumbered with a mortgage like real estate. For the beneficiary, the heritable building right provides the opportunity to put up a building without paying a great amount of money for land to build it on beforehand. For the owner, the benefit of the heritable building right lies in remaining the owner of the land (although another person has built a house on it) and obtaining

ground rent. It is common to agree upon a period of validity of 99 years. If the beneficiary fails to pay the ground rent, he is obliged (under certain conditions) to reconvey the heritable building right to the owner, who must pay compensation for the building to the former beneficiary. All these issues are regulated in the heritable building contract.

Land Register ("Grundbuch")

In order to protect legal relations, the land register ("Grundbuch") discloses all legal relationships concerning a piece of real estate. Every person who claims a legitimate interest is entitled to inspect the land register, which is kept at the land registry, a department of the relevant local court ("Amtsgericht"). The land register is divided into sections by region and each piece of real estate has its own page in the land register. With a few exceptions (such as public roads and waterways), all pieces of real estate must be entered in the register. A page of the land register is made up of three sections: The first section provides information about the owner, the third section provides information about liens on real property ("Grundpfandrechte") such as mortgages ("Hypothek") or land charges ("Grundschulden"), and the second section provides information about all other land charges (such as usufruct, "Nießbrauch"), restraints on disposition (e.g. because of insolvency) or interim measures (like a priority caution). Depending on the form of property, the page of the land register may also have the special form of a "housing register" ("Wohnungsgrundbuch") or "heritable building register" ("Erbbaugrundbuch"). An entry in the land register creates a presumption of a right, but the presumption may be rebutted.

Transfer Formalities

The legal conveyance of property rights in real estate requires an agreement of the parties to the contract ("Auflassung") and the registration of the transfer of property in the land register. The agreement on transfer must be in the form of a notarial deed. This rule is valid for all types of property mentioned above.

The deed of sale for real estate includes details about the contracting parties, the subject of the sale (especially the information drawn from the land register), conditions of payment, details on the building (whether already built or to be built), regulations and agreements on liability and avoidance of contract, and on the expenses of the contract, which are usually borne by the buyer. The costs usually include fees for the notary (approximately 0.3% to 0.4% of the purchase price) plus the fees for the land register (approximately 0.1% to 0.2% of the purchase price) plus the real estate acquisition tax (approximately about 3.5%). But this tax does not accrue if, for example, parents donate the real estate to their children.

Mortgages

Mortgages ("Hypothek") and land charges ("Grundschulden") are the most important liens on real property ("Grundpfandrechte"). Their purpose is to secure creditors. The creditor of a lien on real property (in most cases a bank) is entitled to two claims, one for payment, and if the debtor will not pay, then a claim for compulsory enforcement (in this case execution on the real estate).

It is common to issue a certificate for mortgages or land charges. These documents regarding liens on real property are issued by the land registry and provide information about the serial number of the charged real estate under which it is registered in the land register, plus the amount and the content of the lien on real property. A lien on real property is transferred if the certificate is handed over and the conveyance is declared. If a certificate does not exist, a lien on real property can only be transferred if the new creditor is registered in the land register. For that reason, chartered rights may be sold much more easily than non-chartered rights.

Liens on real property generally require a notarial deed. This is based on the fact that a credi-

tor with a lien on real property needs a title (the legal right to own something) to be able to proceed to compulsory execution against the real estate. An enforceable title includes, for example, a legally binding judgment, but to achieve such a judgment requires time and expense. A preferable solution is a title in the form of an enforceable notarial deed. The only prerequisite is that the debtor has already agreed in notarial form to immediate forced sale of the real estate.

Special Restrictions and Special Rights

In German law, there is no distinction between German and foreign buyers of real estate. Any legal or natural person, as well as a partnership, is entitled to buy real estate. But there are several legal provisions that limit this. These include, in particular, pre-emptive rights stipulated by law or contract. A pre-emptive right is the right to enter into an existing contract and take over the subject of the contract.

A municipality has pre-emptive rights in order to carry out urban building plans. In practice, municipalities only use their pre-emptive rights very restrictively.
Another application of pre-emptive rights is the right of lodgers living on real estate. If their house is supposed to become property in a freehold flat, they have a pre-emptive right to buy their own flat before it is sold to a third party.

Non-commercial housing estate companies ("gemeinnützige Siedlungsunternehmen") have a pre-emptive right concerning agricultural-use areas.

Furthermore, other charges may limit the acquisition of real estate in Germany, as in principle the conveyance of real estate must be free of encumbrances. But there may be several encumbrances, such as liens on real property, right to usufruct, heritable building right or right of abode. These encumbrances must be solved before the conveyancing, or else have to be assumed by the new owner (but then are reflected in the price for the real estate).

To ensure that no acts of disposal are conducted in the time between the conclusion of the contract and the entry in the land register, the buyer's interest is protected by a priority notice of conveyance ("Auflassungsvormerkung"). This notice, which is registered in the second section of the land register, assures the buyer's right to assignment of the real estate.

If the real estate is transcribed to the buyer before the purchase price is paid, the seller bears the risk of the buyer's insolvency. In that case, if the purchase price is not paid, the claim for payment could not be enforced. To avoid this risk, it is common to agree on deposit of the purchase price with the notary. In this case, as soon as the new owner of real estate is registered in the land register, the price can be paid to the seller, who is sure of receiving his money. If this way is not chosen, the seller can safeguard his right to payment, if both parties instruct the notary only to make the application to the land register when the purchase price has been paid or secured.

As mentioned above, provisions on rescission are made between the parties in the notarial deed of sale. As a rule, this will include the right of rescission for the seller if the buyer does not pay on time. On the other hand, the buyer has the legal right to rescind the contract if the seller is guilty of willful deceit, for example in regard to the nature or quality of the real estate.

Construction and Use Restrictions

Before land can be developed with buildings, permission by the relevant authority under the corresponding public law is required. The land must be designated for construction in the applicable local land-use plan.

Contracts of tenancy

German law distinguishes between contracts of tenancy for private housing accommodation and contracts of tenancy for business premises.

Unlike in some other major European countries, most people in Germany dwell as tenants. For that reason German law tends to provide special protection for tenants. Thus, appointments of the lease contract for tenements that differ from the provisions stipulated by law, concerning for example the tenant's right of abating the rent, the right to sublet the object or the right of due cancellation of the contract are declared void. Quite often the lessor uses standard forms to draw up the contract, which must conform to the requirements of the German law on "general terms and conditions". Furthermore, it is significant that a flat shall not be rededicated for different use, for example as accommodation for a shop, and shall not be left permanently vacant, it being the lessor's obligation to hire it out. Regarding the lease price, the lessor has to realign to the local amount of rent for comparison. It is not permissible for a lessor to demand an increased lease price of at least 20% above the average local amount of rent.

On the other hand, terms of lease contracts for business premises may differ from the provisions stipulated by law mentioned above (abating the rent, subletting, due cancellation). Furthermore, the lease price is not bound to the average local amount but only limited by the proscription of usury.

The German law of tenancy underwent far-reaching reform in September 2001, but is still subject to difficult interim arrangements applicable to contracts of tenancy that were concluded before that date.

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