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## Lowering the Corporate Veil in Germany: a case note on BGH 16 July 2007 (Trihotel)

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*In the recent Trihotel case, the German Federal Court of Justice has substantially modified its previous position on lifting the corporate veil, by which shareholders can become liable towards company creditors. The present case note argues that the tort-based new approach will not only afford company creditors with adequate protection but also direct German company law jurisprudence towards a greater regard for fundamental principles of company and insolvency law.*

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### Introduction

How the interests of company creditors are best protected when the company becomes insolvent because of the misfeasance of the company controllers is an issue which courts in all jurisdictions are facing. In Germany, this issue is particularly relevant where the company in question is a limited liability company (a *Gesellschaft mit beschränkter Haftung* or GmbH for short), which is roughly equivalent to what is in common law jurisdictions called a private (limited) company.<sup>1</sup> Until recently, the Federal Court of Justice of Germany (*Bundesgerichtshof*, BGH) had resolved the issue through two different approaches, both of which entailed, to a different extent, something that can be viewed as lifting of the corporate veil. The first of these is the 'qualified *de facto* group' approach. The second, which was adopted in the beginning of the 21<sup>st</sup> century after the BGH abandoned this notion of a 'qualified *de facto* group', was termed as the 'liability for destroying the company's existence' approach. In its decision of a recent case, *Trihotel*, the BGH developed a third approach which does not involve veil-lifting, through reconceptualizing the notion of company destruction liability.<sup>2</sup> The purpose of this article is to assess the means of protection provided for company creditors under the new approach through a close examination of the *Trihotel* case, and to place this in the comparative context of common law notions of company creditor protection. As the new approach has been developed through rejection or reconceptualization of the two previously used concepts, the following will provide a brief introduction to these two superseded approaches.

### Liability within 'qualified *de facto* groups'

Liability within qualified *de facto* groups is a concept that the BGH has developed in considering the liability of the controlling shareholder of a GmbH for the company's debt through an analogous application of the provisions governing enterprise groups in Germany's Stock Corporations Act (*Aktiengesetz*, AktG). We will therefore first have to take a look at how the AktG deals with such enterprise groups for stock

corporations, which are similar to public (limited) companies in common law jurisdictions.

The so-called '*de facto*' or 'non-contractual' groups are one of two different types of enterprise groups that are regulated under the enterprise group provisions in the AktG, the other being the so-called 'contractual groups'. Contractual groups are formed through controlling agreements and profit-and-loss transfer agreements among different companies that intend to form company groups. The purpose of forming this type of enterprise groups is to maximize tax advantages.<sup>3</sup> A non-contractual or '*de facto*' enterprise group is formed where dependent enterprises are joined together under the uniform management of a controlling enterprise.<sup>4</sup> Such an arrangement becomes a 'qualified *de facto* group' where the controlling enterprise abuses its controlling position when seen from an objective point of view.<sup>5</sup>

The relationships among enterprises within contractual groups are governed by §§ 300ff AktG, whereas *de facto* groups are regulated under §§ 311ff. There are, on the other hand, no statutory provisions on GmbH groups. The law on GmbH groups has therefore been developed by case law and literature, largely through analogous application of provisions governing enterprise groups in the AktG.<sup>6</sup> Of the above-mentioned provisions, the most relevant are §§ 302, 311 and 317. § 302 requires the controlling enterprise to settle an annual deficit of its subordinate enterprises. § 311 prohibits the controlling enterprise from using its influence to induce a subordinate enterprise to enter into a transaction that is disadvantageous to the subordinate enterprise without being given compensation. Where no such compensation is provided, § 317 grants to the aggrieved subordinate enterprise a claim for damages against the controlling enterprise.

In a number of earlier cases, the BGH held a controlling person of a GmbH group liable for the debt of a company within the group, based on the notion of 'liability within a qualified *de facto* group' through an analogous application of the above-mentioned AktG provisions. Examples include the *Video* case<sup>7</sup> and the *TBB* case<sup>8</sup>, where the Court upheld the claim of the creditor of a subordinate company against the controlling person of the GmbH group. In both cases, the defendants were natural persons who controlled the group as shareholders and directors, and the Court treated them as the 'controlling enterprise' for the purpose of an analogous application of § 302 AktG.

This concept of 'liability within a qualified *de facto* group' was severely criticized for lack of any precise definition<sup>9</sup> and for the uncertainty which it created as to whether a party would be liable under § 302 AktG. A more perturbing problem of the 'liability within a qualified *de facto* group' approach, however, is that it is rather questionable whether an analogy should be drawn from a contractual stock corporation group to a *de facto* limited liability company (GmbH) group. The problem of the analogy is that it leads to an application of provisions governing contractual groups of stock corporations to situations where relationships among companies in a company group are not at issue. In both the *Video* and *TBB* cases, the so-called 'controlling enterprise' was not really an enterprise but a natural person who had controlling influence in a company within the group, which was not really a stock corporation group.<sup>10</sup> The qualified *de facto* group approach leads to a lifting of the corporate veil by making the controlling person liable for a 'subordinate' company's debt.

### Liability for destroying the company

It was probably in reaction to this criticism that the BGH abandoned the 'qualified *de facto* group' approach in favour of the concept of "liability for destroying the company's existence" at the beginning of the 21<sup>st</sup> century.<sup>11</sup> The BGH's change of mind was indicated first in an *obiter dictum* that the Court made in the *Bremer Vulkan* case.<sup>12</sup> In that case, Bremer Vulkan Verlag AG was both the sole shareholder of MTW GmbH and the controlling company of a corporate group. MTW had received a sum of money from the State. Rather than keeping this money within the assets of MTW, Bremer Vulkan stashed this sum into the central treasury of the company group under its control. Both the company group and MTW then became insolvent. The

claimant, a state agency, then sued the members of the management board of Bremer Vulkan.

The Court observed *obiter dictum* that MTW should be protected neither through an analogous application of §§ 291-310 AktG (on contractual stock corporation groups) nor of §§ 311-317 (on *de facto* groups). Such protection should rather be based on the doctrine of capital maintenance and the company's right to continuing existence.

The capital system under the GmbHG is constituted by, broadly, three elements. The first is the requirement of a fixed minimum share capital.<sup>13</sup> The minimum amount of share capital required under GmbHG, is € 25,000.<sup>14</sup> The second is the obligation on the part of the incorporators to pay their capital contribution in full.<sup>15</sup> The third is the prohibition against repayment of capital contributions to shareholders.<sup>16</sup> The main anti capital withdrawal provisions are §§ 30, 31 GmbHG. § 30 prohibits the withdrawal of capital contributions, whereas § 31 requires a defaulting shareholder to repay to the company the capital contribution that he has wrongfully withdrawn.

The company's right to continuance requires that the controlling shareholder should pay due consideration to the company's interests when interfering with the company's assets or business opportunities. Such due consideration would be lacking if the company becomes unable to meet its obligations because of the shareholder's interference with its assets.<sup>17</sup> This is the concept of liability for company destruction.<sup>18</sup> Having caused the company's destruction would, however, render the defaulting shareholder liable for the company's debt only if the company's ability to discharge its debt towards the creditor cannot be restored by enforcing claims against the shareholder under § 30, 31 GmbHG. 'Company destruction', being a judicially developed basis of liability, therefore was subsidiary to §§ 30, 31 GmbHG.<sup>19</sup>

This company destruction liability approach to the defaulting shareholders' liability for the company's debt received its first application in the *KBV* case.<sup>20</sup> In that case, the claimant had entered into a contract to provide services to KBV GmbH (KBV). After the claimant had performed its part of the contract, KBV entered into a transaction with a third party, L GmbH (L), which had the effect of depriving KBV of part of its assets. This transaction was entered into by A, who was one of KBV's two shareholders, with the consent of B, the other shareholder in KBV, who was also this company's Managing Director. No insolvency proceedings were initiated against KBV because of its lack of assets. The unavailability of KBV's assets was caused by that company's transaction with L, which was procured by A and B.

The claimant brought an action against, *inter alia*, A and B. The Court held that the two shareholders were obliged to compensate the claimant for the loss that it had suffered because of its inability to recover from KBV. The Court's ruling was based on two concurrent doctrinal bases. The first is liability for company destruction, and the second is the delict of intentional infliction of loss in violation of good morals (*contra bonos mores*) under § 826 BGB, the German Civil Code.

On the first ground, the Court ruled that the privilege of limited liability granted to the shareholders of a private company under §13 para. (2) GmbHG was subject to the precondition that the company's assets must be committed to the preferential satisfaction of company creditors for as long as the company exists.<sup>21</sup> Shareholders had access only to the surplus in the company coffers, i.e. assets which were not required for fulfilling the company's obligations.<sup>22</sup> An act on the part of a shareholder to siphon off the company's assets without taking into account the company's ability to discharge its debt obligations amounted to an abuse of the legal form of the company. The consequence of this abuse is the loss of the shareholder's privilege of limited liability, but only to the extent that the loss suffered by the company in consequence of this interference with the company's assets is not made good by remedies under §§ 30, 31 GmbHG, the effect of which has been discussed above.<sup>23</sup> As concerns delictual liability for violation of good morals, the Court held that A and B had deliberately and *contra bonos mores* harmed the interest of the claimant, who was a creditor of the company. The harmful action of the shareholders was *contra bonos mores* because it constituted an abuse of the legal form of a company.<sup>24</sup>

The *contra bonos mores* rule in § 826 BGB establishes liability for damages if a person wilfully causes damage to another in a manner contrary to good morals. § 826 is one of the general tort provisions in the BGB. It was intended from the outset to be an 'all-purpose residual provision'.<sup>25</sup> The types of situations that have been litigated under this provision include misstatements, obtaining court decisions by fraud, inducing breach of contracts, malicious falsehood, abuse of rights, passing off, wrongful use of monopoly power, and other underhand activities.<sup>26</sup>

In order to establish this liability under § 826 BGB, the claimant must plead and if necessary prove four elements. These are:

- (1) the claimant has suffered damage;
- (2) this damage was caused by the conduct of the defendant;
- (3) that conduct was *contra bonos mores*; and
- (4) the defendant intended to cause the damage.<sup>27</sup>

In our situation the claimant is a creditor of the insolvent company. It is quite easy to prove the first three elements. The creditor suffers a loss because the insolvent company cannot pay. The shareholders caused this loss through their interference with the company's assets. For the reasons explained above when establishing 'company destruction' liability, the abuse of the corporate form also amounted to conduct *contra bonos mores*.

The fourth element, intention, is normally the one which is most difficult to establish under § 826 BGB. This is, however, not the case in the present context. It is sufficient that the defendant shareholder was aware that the act which gives rise to liability would render the remaining company capital inadequate, which in turn was likely to injure the interest of the claimant company creditor.<sup>28</sup>

### Liability for company destruction no longer a self-contained cause of action

In the *Trihotel* case, which came only five years after its decision in KBV, the BGH changed its mind once again on shareholders' liability for the company's debts where the company is insolvent.<sup>29</sup> In essence, where the company is insolvent and the insolvency administrator has decided not to proceed with the insolvency process for lack of company assets, an aggrieved company creditor no longer has a direct cause of action against a defaulting shareholder.<sup>30</sup> In *Trihotel*, the defendant was the managing director of three companies, namely, A-GmbH, J-GmbH, and W-Hotel-GmbH. He did not hold shares in any of the three companies. The shares in A-GmbH were rather held by the defendant's wife (48%) and J-GmbH (52%) respectively. The defendant's mother was the sole shareholder of J-GmbH, which also held 90% of the issued shares in W-Hotel-GmbH. The remaining shares in W-Hotel-GmbH were held by the defendant's mother.

A-GmbH had run a hotel business within premises that were leased from the defendant. The defendant terminated the lease agreement five months before it would have expired. The property was subsequently leased to W-Hotel-GmbH. Thereafter, A-GmbH continued to manage the hotel business on behalf of W-Hotel-GmbH, for 40% of the latter's turnover. The turnover payable by W-Hotel-GmbH to A-GmbH was subsequently reduced to 28%. In the meantime, in order to meet the financial needs of A-GmbH, the defendant's mother had given a loan to that company. The same company agreed to transfer its inventory to the defendant's mother as security.

The financial situation of A-GmbH deteriorated and insolvency proceedings followed. The Appeal Court of Rostock held the defendant liable for the bad debts of the company towards its creditors on the ground that he had destroyed the debtor company (A-GmbH). The court believed that the defendant had done so through interference with A-GmbH's assets on at least two occasions. First, the security assignment of A-GmbH's inventory to the lender (the defendant's mother), was excessive when compared to the value of the loan. Second, the premature termination of his lease contract with A-GmbH was financially unjustifiable.<sup>31</sup>

The BGH, however, decided that the Appeal Court had erred in its judgment when

holding that these two transactions amounted to abusive interference with A-GmbH's assets. The BGH pointed out that the Appeal Court's conclusions were based on assumptions that were not supported by available evidence, and that the effect which these transactions might have had on the subsequent insolvency of A-GmbH could only be determined with the help of expert opinions.<sup>32</sup> The BGH therefore referred the case to the Appeal Court and requested it to reconsider the case after having obtained such expert evidence, and by giving regard to the new notion of company destruction liability which the BGH outlined in the same case.<sup>33</sup> The following sections will show how this new notion differs from the previous concept of company destruction liability (A), why the old approach had to be abandoned (B), and the wider significance of the changed notion of company destruction liability when seen in a comparative context (C).

### **A. The new notion of company destruction liability**

Although the BGH decided to abandon its previous company destruction liability approach, it has not given up this capital maintenance based approach to the liability of defaulting shareholders. On the contrary, the Court decided that company destruction liability should continue in both name and content.<sup>34</sup> The Court, however, shifted the basis of this liability and developed a concept which differs from its predecessor on both doctrinal and practical levels. On a doctrinal level, company destruction liability is no longer treated as an independent basis of liability which is subsidiary to liability for wrongful withdrawal of capital under §§ 30 and 31 GmbHG. It is now seen as a special category within the delict of intentional infliction of loss *contra bonos mores* under § 826 BGB.<sup>35</sup> One practical difference is that claims under § 826 BGB and under §§ 30-31 GmbHG are concurrent. This means - as opposed to the previous concept - even if a claim under §§ 30-31 GmbHG can be established, § 826 BGB is applicable.<sup>36</sup>

The other important practical effect is that a disappointed creditor of the company cannot invoke § 826 BGB, because the tort is committed against the company, not the creditor, as it is the company's (and not the creditor's) assets which have been tampered with. The primary victim of the tort is the company. Although it may be possible to establish that a company creditor is a secondary victim of the tort,<sup>37</sup> allowing direct actions by company creditors would contravene the separate entity doctrine enshrined in § 13 GmbHG.<sup>38</sup>

The most important practical difference is therefore that a disappointed creditor of the company can no longer sue directly an abusive shareholder under company destruction liability. No longer will such abusive interference with the company's assets lift the corporate veil in the sense that a shareholder becomes directly liable for the company's debt.<sup>39</sup> Under the new approach, the creditor can only sue the company itself. The only recourse which the disappointed creditor of an insolvent company has against the abusive shareholder is indirect. The creditor must first establish the claim against the company and then enforce it by a motion of attachment to have the company's claim against the abusive shareholder transferred to the creditor.<sup>40</sup>

### **B. The new approach: why the change?**

Four interrelated reasons for the shift to a new concept of company destruction liability can be gleaned from the judgment of the BGH. First, the old company destruction approach is internally inconsistent and conceptually fuzzy.<sup>41</sup> Company destruction liability was intended to fill the gaps left in the provisions on statutory capital maintenance, §§ 30 and 31 GmbHG. § 30, it will be recalled, prohibits shareholders from receiving payments out of their capital contribution. § 31 provides that the company has a claim for restitution of the payments received against a shareholder who has contravened § 30. These two provisions, however, will not always restore the company to the position which it held prior to the contravention of Art 30. The contravention may have caused collateral damage, or the extent of the damage may in other ways not be reflected sufficiently in the company's balance

sheet. Company destruction liability was created to fill these gaps.

Abusive shareholders were to lose their privilege of limited liability under § 13 GmbHG. They were, at least in theory, to become fully liable to the company's creditors. This could produce injustice in certain situations. For example, if the company was already in deficit or already over-indebted before the defendant shareholder's interference took place, the shareholder would be liable for losses not resulting from the interference, and the creditors would be better off than if the interference had not taken place.<sup>43</sup> The BGH had responded to this flaw by allowing the shareholder to prove that the company would have become insolvent even without the interference, in which event the shareholder would be liable only to the extent that the actual loss suffered by the creditors exceeded the loss they would have suffered if the shareholder had acted lawfully throughout.<sup>44</sup>

However, while this limitation avoided some injustice, it was inconsistent with the main doctrinal basis which the BGH had initially identified for company destruction liability, namely that the shareholder should lose the privilege of limited liability because of the abuse.<sup>45</sup> This inconsistency may well have been a main reason for the BGH's rejection of its old approach.

Second, the notion of company destruction liability was developed in order to extend the application of the statutory capital maintenance regime.<sup>46</sup> It was meant to fill gaps in the protection of company assets under §§ 30 and 31 GmbHG. Such an enlarged capital maintenance regime was, however, difficult to reconcile with the previous rule which allowed company creditors (and not just the company) to sue an abusive shareholder. As it is only the company itself which has a cause of action against the defaulting shareholder under §§ 30 and 31, that company should also be the only party who has standing under the enlarged capital maintenance regime.

Third, the Court also clarified in its judgment in *Trihotel* that an abusive interference with the company's assets by a shareholder is neither conceptually nor functionally an abuse of corporate form.<sup>47</sup> However, the Court, did not expand on why interference with the company's assets did not amount to an abuse of corporate form, and rather referred to an article written by Zöllner in support of this view.<sup>48</sup> Zöllner has stated that a case of abuse of legal form can be made out only if the legal form is used to conceal certain facts.<sup>49</sup> If this test is applied, a deprivation of a company's assets which has affected the company's state of solvency can hardly be understood as an abuse of the legal form. Corporate form in this situation is not used to conceal anything or deceive anybody.

It can be inferred from Zöllner's view, which the BGH has cited with approval, that the corporate veil should be lifted only where corporate form is abused and the corporate form is not abused if it is not used to conceal anything. This appears to be consistent with the views that common law courts have expressed in more recent cases that involved an issue on veil-lifting. One of the tests that commonwealth courts have employed in considering whether the corporate veil should be lifted was whether corporate personality had been used as a 'mere facade concealing the true facts'.<sup>50</sup> If abusive interference with the company's assets does not amount to an abuse of corporate form, then the corporate veil should not be lifted. Where the corporate veil is not lifted, it is doctrinally impossible to hold a shareholder directly liable to a company creditor.

Fourth and finally, the old company destruction liability concept is inconsistent with the principle that a company possesses a separate legal personality, a fundamental company law principle enshrined in the GmbHG.<sup>51</sup> Subjecting a shareholder who has committed a wrong against the company to a direct action by a company creditor who has allegedly suffered a consequential loss contravenes the company law principle that protection of company creditors must be mediated through the company.<sup>52</sup> Where there is no reason to disregard the company's personality, there is no ground to deviate from the separate personality principle enshrined in § 13 GmbHG. The creditor's debtor is the company, not the shareholders of that company.

### C. Implications of the new approach

The level of doctrinal integrity of the new approach is much higher than that of the previous notion of company destruction liability. The new approach does not suffer from the internal inconsistency and conceptual fuzziness that the old approach was fraught with.<sup>53</sup> Treating company destruction as a category under § 826 BGB enables the courts to protect company creditors' interests from shareholders' abusive meddling of company assets without having to agonize over the doctrinal dilemma between the need for stripping the delinquent shareholder of his privilege of limited liability and the absurd consequence that may follow.<sup>54</sup>

One noticeable feature of the BGH's decision on the delictual aspect is that company destruction is treated as a delict which is actionable by the company only. This is a conscious choice of the BGH, not a natural consequence of the fact that liability is placed under § 826 BGB. As this provision makes a party liable for intentionally inflicting loss on another *contra bonos mores*, it could also cover directly the loss which an abusive shareholder intentionally inflicts on the company's creditors. And as § 826 BGB is generally thought to be capable of protecting both the interests of the company and that of the company creditors,<sup>55</sup> one could argue that company creditors should also be allowed to sue the shareholders directly under this provision.

The BGH's decision that a claim for company destruction liability under § 826 BGB can be brought only by the company itself must therefore be attributed to a different doctrinal basis. This is found in the fundamental principle of company law, enshrined in the GmbHG, under which a company has a legal personality which is separate from that of its shareholders, with the consequence that shareholders are not subject to direct actions by creditors. The constitutionality of courts disregarding such a principle which parliament has set out in a statute has been called into question even in common law jurisdictions when discussing the courts' power to disregard a company's own legal personality.<sup>56</sup> Apart from this 'matter of principle', there are practical legal reasons why creditors should not have standing to sue shareholders when the company is in the state or on the verge of insolvency. Heydon has expressed the view, endorsed by the Australian High Court in a recent Australian case, *Spies v R*,<sup>57</sup> that (in the common law context):

there is a duty of imperfect obligation owed to creditors: the directors<sup>58</sup> must bear their interest in mind, and breaches of the duty cannot be forgiven without their consent, but they cannot enforce that duty save to the extent that the company acts, on its own motion or through a liquidator.<sup>59</sup>

Heydon did not explain why the obligation was imperfect. One of the reasons, however, must be that "any claim brought by a liquidator should be for the benefit of the liquidation assets generally, to be distributed among the creditors and members in accordance with their statutory ranking and entitlement."<sup>60</sup> Giving remedial advantages to a given creditor or to particular categories of creditors may adversely affect the interests of other creditors who, under insolvency law and policy considerations, deserve equal protection.<sup>61</sup> The BGH's indication in *Trihotel* that they may still be willing to consider stripping shareholders of their privilege of limited liability in cases where the remaining assets of the company were 'stashed away' for the purpose of injuring the interest of a single remaining creditor<sup>62</sup> supports this view. Lifting of the corporate veil in those circumstances would obviously not affect company creditors' right to *pari passu* participation.

On a practical level, the BGH's new approach to the notion of company destruction liability is not likely to compromise the interest of an individual creditor to any significant extent. It is even arguable that the new approach is beneficial to company creditors. Normally, an insolvency administrator will proceed with an action against any allegedly abusive shareholder where such an action is promising according to the administrator's professional judgment. An insolvency administrator will normally decide not to proceed only if such a claim does not have a reasonable likelihood of success and is therefore unlikely to increase the assets of the company.<sup>63</sup> At least where this professional judgment of the administrator is sound, a direct action by a creditor will not be of much assistance.

## Conclusion

Perhaps what is most commendable about the BGH's decision in *Trihotel* is the Court's appreciation how important it is to avoiding lifting the corporate veil for more than is strictly necessary. Any veil-lifting encroaches on the basic company law principle that a company has a legal personality which is separate from that of its shareholders and the possibility of finding a theory on the constitution of exceptions to this principle probably does not exist.<sup>64</sup> Lifting the corporate veil should therefore be treated as the last resort when all other avenues have been exhausted.<sup>65</sup> *Trihotel* exemplifies how a type of cases that had previously been decided by lifting the corporate veil to a certain degree can instead be disposed of by application and creative development of other private law and company law rules. With this judgment from Germany's highest court in civil matters, it is highly likely that *Trihotel* will reorient company law jurisprudence to a new direction where fundamental company law principles such as the doctrine of the separate legal personality are not disregarded unless it is absolutely impossible find a solution on the basis, or through a legitimate extension, of other rules.

## Endnotes

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<sup>1</sup> One of the reasons is that the creditors of a limited liability company, i.e., *Gesellschaft mit beschränkter Haftung* (GmbH), are not as well protected as those of a stock corporation which is roughly equivalent to what in common law jurisdictions is called a 'public company'. The latter are regulated under the Stock Corporations Act (*Aktiengesetz*, AktG), where by company creditors who are unable to obtain their claims against the company are given standing to sue shareholders who are in breach of capital maintenance provisions: Art 62 (2) AktG. No similar standing is provided under the Limited Liability Companies Act (GmbHG). For the meaning of private and public companies, see P Davies, *Gower and Davies' Principles of Modern Company Law* (7th edn, Thomson Sweet & Maxwell, London 2003) 12ff and P Redmond, *Companies and Securities Law: Commentary and Materials* (4th edn, LBC, Sydney 2005) 113ff.

<sup>2</sup> BGH, judgment of 16 July 2007, II ZR 3/04, available at: <http://www.bundesgerichtshof.de>; for a discussion of the case see: H Altmeppen, 'Abschied vom 'Durchgriff' im Kapitalgesellschaftsrecht' (2007) *Neue Juristische Wochenschrift* 2657-2660; E Schanze, 'Gesellschafterhaftung für unlautere Einflussnahme nach § 826 BGB: Die Trihotel-Doktrin des BGH' (2007) *Neue Zeitschrift für Gesellschaftsrecht* 681-686.

<sup>3</sup> R Volhard and A Stengel, *German Limited Liability Company* (John Wiley & Sons, NY 1997) 255.

<sup>4</sup> Volhard and Stengel (n 3) 261.

<sup>5</sup> Volhard and Stengel (n 3) 264.

<sup>6</sup> Volhard and Stengel (n 3) 253.

<sup>7</sup> BGH judgment of 23 September 1991, BGHZ 115, 187.

<sup>8</sup> BGH judgment of 29 March 1993, BGHZ 122, 123. See S M Bartman and J Roest 'Piercing the Corporate Veil in the Netherlands and Germany: A Convergent Legal Development' in K Boele-Woelki, et al (eds) *Comparability and Evaluation: Essays on Comparative Law, Private International Law and International Commercial Arbitration* (Martinus Nijhoff, Dordrecht, The Hague 1994) 3, 6.

<sup>9</sup> F Wooldridge, 'Controlling Shareholders' Liability in German Private Companies' (2005) 26(9) *Comp Law* 286, 286.

<sup>10</sup> Wooldridge (n 9) 286; Hänisch (n 10) 19.

<sup>11</sup> Wooldridge (n 9) 286.

<sup>12</sup> BGH judgment of 17 September 2001, BGH *Neue Juristische Wochenschrift* 2001 3622.

<sup>13</sup> § 5 GmbHG.

<sup>14</sup> § 5 GmbHG. Note, however, that the recent reform of the GmbHG introduced the so-called *Unternehmergesellschaft (haftungsbeschränkt)* (UG) (entrepreneur company (limited liability)) - with a minimum capital of only € 1. The UG must save 25% of its annual profits, which are not distributable

but must be accumulated. As soon as the shareholders increase the stated capital to € 10, 000, the UG (*haftungsbeschränkt*) will convert into a fully fledged GmbH, which is not obliged to comply with the profit accumulation requirement. For further information on the above-mentioned company law reform, see M Beurskens and U Noack, 'The Reform of German Private Limited Company: Is the GmbH Ready for 21st Century?' (2008) 9(9) *Germany Law Journal*, available at <http://www.germanlawjournal.com/article.php?id=989>.

[15](#) § 9 GmbHG.

[16](#) §§ 30, 31 GmbHG.

[17](#) M Shilling, 'The Development of a New Concept of Creditor Protection for German GmbHs' (2006) 27(11) *Comp Law* 348.

[18](#) The term of 'liability for company destruction' (in literal translation: liability for existence destruction), however, has been criticized by German commentators as misleading. The argument goes that the characteristic attribute of this concept is not destruction of the existence of a company but the causing of the company's insolvency. The notion of insolvency and that of company destruction have to be kept separate, as the destruction of a company is caused by the official act of deleting the company from the company register. This may happen several years after the realization of the liability. Often insolvency does not lead to a destruction of the existence but to the maintenance of the existence by way of restructuring the company or by setting up an insolvency plan etc. This means that the destruction of the company's existence is not a condition of this kind of liability: W Zöllner, 'Gläubigerschutz durch Gesellschafterhaftung bei der GmbH', in: B Dauner-Lieb et al (eds), *Festschrift für Horst Konzen zum siebzigsten Geburtstag* (Mohr Siebeck, Tübingen 2006) 999, 1003.

[19](#) BGH, *GmbHRundschau* 2007, 930, para 17.

[20](#) BGH judgment 24 June, 2002, *Neue Juristische Wochenschrift* 2002, 3024.

[21](#) BGH *Neue Juristische Wochenschrift* 2002, 3024.

[22](#) BGH *Neue Juristische Wochenschrift* 2002, 3025.

[23](#) Text to n 17.

[24](#) BGH *Neue Juristische Wochenschrift* 2002, 3024, 2005; Hänisch (n 10) 21; Shilling (n 18) 348.

[25](#) B S Markesinis and H Unberath, *The German Law of Obligations, Vol II, The Law of Torts, A Comparative Introduction* (3rd edn, OUP, Oxford 1994) 894.

[26](#) Markesinis and Unberath (n 27) 896-898.

[27](#) K Rebmann, et al, (ed), *Münchener Kommentar zum Bürgerlichen Gesetzbuch, Band 5* (4th edn Verlag C H Beck, München 2004), § 826 BGB, Rn 5; Hänisch (n 10) 17.

[28](#) *Münchener Kommentar* (n 29) §826 BGB, Rn 5.

[29](#) BGH, judgment of 16 July 2007, *GmbHRundschau* 2007, 930.

[30](#) For circumstances in which an aggrieved creditor may be allowed to pursue the errant shareholder direct, see text to ns (65, 66).

[31](#) BGH, judgment of 16 July 2007, *GmbHRundschau* 2007, 930, para. 12.

[32](#) BGH, *GmbHRundschau* 2007, 930, para. 47-54.

[33](#) BGH, *GmbHRundschau* 2007, 930, para 52.

[34](#) BGH, *GmbHRundschau* 2007, 930, para 16. The word 'content' here means the notion of company destruction as conceived of in BGH's previous decisions and the criteria for the establishment of the liability, see BGH, *GmbHRundschau* 2007, 930, para 16.

[35](#) BGH, *GmbHRundschau* 2007, 930, Preamble (b), para 31; See text to n 28.

[36](#) Under the old approach company destruction liability was subsidiary to §§ 30, 31 GmbHG, meaning that a the claim by an aggrieved *creditor* against the defaulting shareholder on the basis of 'company destruction' was activated only where §§ 30, 31 GmbHG were not applicable or where a successful claim by the *company* against the defaulting shareholder under §§ 30, 31 GmbHG did not restore the company's ability to discharge its liability.

[37](#) BGH, *GmbHRundschau* 2007, 930, para 26.

[38](#) BGH, *GmbHRundschau* 2007, 930, para 36. Allowing direct actions by company creditors will also upset the insolvency rule in relation to *pari passu* participation by all company creditors. See text to n 63.

[39](#) Text to n 25.

[40](#) BGH, GmbHRundschau 2007, 930, para 36. See also M Goetz, 'The Federal Court of Justice's concept for piercing the corporate veil due to destruction of a German limited liability company', Client Newsletter 9/2007, Rechtsanwaltskanzlei Goertz, available at [www.goertz.net](http://www.goertz.net).

[41](#) BGH, GmbHRundschau 2007, 930, para. 20.

[42](#) BGH, GmbHRundschau 2007, 930, para. [24]

[43](#) B Dauner-Lieb, 'Die Existenzvernichtungshaftung-Schluss der Debatte?' (2006) Deutsches Steuerrecht 2034, 2041.

[44](#) Shilling (n 18) 350.

[45](#) Text to n 25.

[46](#) BGH, judgment of 16 July 2007, GmbHRundschau 2007, 930, para. 33.

[47](#) BGH, GmbHRundschau 2007, 930, para 28.

[48](#) Zoellner (n 19).

[49](#) Zoellner (n 19) 1008.

[50](#) *Woolfson v Strathclyde Regional Council* [1978] SLT 159 at 161 per Lord Keith of Kinkel; *Re Polly Peck International plc (in admin)* [1996] 2 All ER 433 at 447 per Robert Walker J; *Trustor AB v Smallbone (No 2)* [2001] 1 WLR 1177 at 1185-1186 per Sir Andrew Morritt V-C. See also *Lee Sow Keng v Kelly McKenzi Ltd* [2004] 3 HKLRD 517. Note, however, that it is almost impossible to reconcile the decided common law cases on the prerequisite for a lifting of the corporate veil: see text to n 69.

[51](#) BGH, judgment of 16 July 2007, GmbHRundschau 2007, 930, para 33.

[52](#) BGH, GmbHRundschau 2007, 930, para 33.

[53](#) Text to n 43.

[54](#) Text to n 45.

[55](#) E Schanze, 'Gesellschafterhaftung für unlautere Einflussnahme nach § 826 BGB' (2007) Neue Zeitschrift für Gesellschaftsrecht 685.

[56](#) R Tomasic and S Bottomley, *Corporations Law in Australia* (Federation Press, Sydney 1995) 62.

[57](#) 35 ACSR 500 at 526. The full court did that indirectly through endorsing the opinion that Gummow J expressed in *Re New World Alliance Pty Ltd; Sycotext Pty Ltd v Baseler* (1994) 122 ALR 513 at 550. Gummow J cited Heydon (see n 62 below) in formulating His Honour's view in the above-mentioned case.

[58](#) The focus of similar common law cases is the duty of directors, who, in equity, owe various heads of duties to the company.

[59](#) J D Heydon, 'Directors' duties and the company interests' in P Finn (ed) *Equity and Commercial Relationships* (Law Book, Sydney 1987) 120, 131. Cf R Grantham, 'The judicial extension of directors' duties to creditors' (1991) JBL 1.

[60](#) L S Sealy, 'Directors' weird' responsibilities - problems conceptual, practical and procedural' (1987) 13 Monash U L Rev 165, 185. Cf R Grantham, 'The judicial extension of directors' duties to creditors' (1991) JBL 1. However, Sealy's view seems to have gained the support in recent common law cases: *Spies v R* (2000) 35 ACSR 500; *Geneva Finance Ltd (Receiver and Manager Appointed) v Resource & Industry Ltd* (2002) 20 ACLC 1, 427.

[61](#) On creditors' right to *pari passu* participation, see the comments by Gaudron, McHugh, Gummow and Hayne JJ in *Spies v R* (2000) 35 ACSR 500 at 526 and Em Heenan J's view in *Geneva Finance Ltd (Receiver and Manager Appointed) v Resource & Industry Ltd* (2002) 20 ACLC 1, 427 at 1, 438.

[62](#) BGH, judgment of 16 July 2007, GmbHRundschau 2007, 930, para 33.

[63](#) BGH, GmbHRundschau 2007, 930, para 37.

[64](#) D French, S Mayson and C Ryan, *Mayson, French & Ryan on Company Law* (24th edn, OUP, Oxford 2007) 139; R Baxt, K Fletcher and S Fridman, *Corporations and Associations: Cases and Materials* (9th edn, Butterworths 2003) 194.

[65](#) This is the attitude of the common law courts: Austin and I M Ramsay, *Ford's Principles of Corporations Law* (13th edn, Butterworths, Sydney 2007) 131.