

Establishing a GmbH in Germany

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1. Introduction

A 'Gesellschaft mit beschränkter Haftung' is a limited liability company – abbreviated 'GmbH' – defined as a legal entity under German civil law. In contrast to a partnership ('Personengesellschaft'), the GmbH is a company limited by shares centered not around the association of its members, but around the share capital contributed to the company.

A GmbH has many benefits for the founders of a new business: On the one hand, it reduces personal risks to a minimum as the external liability of the founders is limited to their initial contribution of at least € 25,000.00 (made in cash or as a non-cash capital contribution), while their personal assets remain untouched; on the other hand, this legal form offers great flexibility and scope for action, as most of the provisions of the GmbHG ["Gesetz betreffend die Gesellschaften mit beschränkter Haftung": German Limited Liability Companies Act] are non-binding. A carefully thought-out company agreement may accommodate the individual needs of the company, whether it be a family-run business or a large enterprise. For this reason, according to the German Federal Statistical Office, about 39.3% of all new registered companies in 2014 were GmbHs, making this the most popular legal form by far.

2. Concluding a company agreement / articles of incorporation

The company agreement ('Gesellschaftsvertrag'), also known as the articles of incorporation ('Satzung'), sets the cornerstones of the company and regulates the relationships between the shareholders. If a GmbH is incorporated, the agreement or articles of incorporation are to be officially recorded by a notary public and it determines, among other things, the name, registered offices and objective of the company; it also contains the regulations concerning the organs of the company, the management, and the shareholder meeting. In practice, the agreement mostly has optional provisions, for example the options available to settle arguments and disputes.

According to Sec.2 (1a) GmbHG, there is a model protocol; in practice, however, if the GmbH is formed by a maximum of three shareholders and one managing direc-

tor, it is not recommended to use the model protocol for the GmbH. The provisions of the sample articles of incorporation cannot be changed, but rather have to be adopted as they are, even though they are only suitable for a small percentage of the prospective companies. The disadvantage of the statutory sample articles of incorporation in the simplified procedure mainly is that shareholder membership cannot be controlled, as the shares can be freely ceded and sold to third parties. A sample or template with universal validity is impracticable as there is a great variety of different companies in real economic life; the GmbHG only provides a few selected binding corner points. Instead, the articles of incorporation shall be tailored to the individual needs as best as possible. At the latest when a conflict arises between the shareholders, it will have been worth while to elaborate a well-conceived company agreement that prevents lengthy and costly legal disputes.

3. Appointment and duties of a managing director

The managing director ('Geschäftsführer') is the organ that legally represents the GmbH. A company is not capable of acting if it does not have a managing director. The managing director manages the business operations and represents the company to the outside. If several people are appointed as managing directors, they represent the company jointly. Nevertheless, it is possible to grant sole power of representation ('Einzelvertretungsbefugnis'). This must be registered in the commercial register.

The right to represent of a managing director cannot be limited to the outside. That means that all business transactions that the managing director concludes for the company with third parties shall be effective, even if they are not covered by his internal powers of representation. However, the company is entitled to an internal compensatory claim against the managing director.

Any natural person having unlimited legal capacity can be appointed managing director. The managing director shall not necessarily have to be a shareholder – appointing outside managers is not an uncommon practice. To become a managing director in Germany, it is not necessary for the appointee to have a legal residence in Germany or to be a German citizen. However, it must be ensured that there is a person entitled to represent within the country, who will serve as a point of contact

for the authorities and official agencies. As a managing director of a German GmbH, non-EU citizens can apply for a business travel visa at any time, allowing the managing director to stay in the Federal Republic of Germany for 90 days per half year.

Basically, there are no special requirements regarding the qualifications of a managing director. There are exceptions for businesses that need special permissions or authorizations, for example, transport or passenger service companies. Handicraft or craftsman's businesses require that either the managing director or a contracted works manager have the necessary craft or trade qualifications (usually a master craftsman's certificate or 'Meisterbrief').

Individuals who were sentenced due to a delay in filing petition in insolvency or any other insolvency offense or offenses against property (e.g. credit fraud or breach of trust) are barred from taking office as managing director for five years from the date of final judgment.

The shareholder meeting appoints the managing director. The appointment as well as any change regarding the managing director are to be registered in the commercial register. In principle, the managing director may be removed from office at any time and without cause.

The managing director is responsible for taking all measures necessary to attain the objective of the company and that are not reserved to the shareholder meeting by law or the company agreement. The powers of the managing director can be limited by the articles of incorporation. As a consequence of the fiduciary duty the managing director owes the company, the managing director may under no circumstances exploit its organ status for motives of self-interest to the detriment of the company. This results in a prohibition of competition that forbids the managing director to compete with the company either in person or with another company during the term of the mandate. The responsibilities of the managing director further include the convocation of and participation in the meeting of shareholders. The managing director must always keep an eye on the financial situation of the company. If the company becomes materially or factually insolvent, the managing director must file a petition to open insolvency proceedings within three weeks. If the managing director fails to do so, liability will extend to the personal assets by way of exception.

4. Managing director employment agreement

Besides the status of an organ within the GmbH, a managing director employment agreement regulates the contractual relationship of the managing director with the company. As the organ status and contractual relationship must always be treated separately, the main function of the agreement, from the point of view of the managing director, is to provide protection against the company, which could remove the managing director, being an organ of the company, from office at any time and without cause. The design and content of the agreement is not subject to any strict guidelines. The relationship between the managing director and the company can either be regulated by a service, employment or consultancy agreement. Which of these options is the most beneficial depends on the remaining circumstances of the company. An employment agreement can be concluded informally. However, for the sake of clarity and as a means of proof, it is strongly recommended to conclude an agreement in writing.

As the official language in German courts is German (Sec.184 GVG [“Gerichtsverfassungsgesetz”: German Judicature Act]), it is further recommended to draft the binding version of the employment agreement in German, even if the corporate policy has banned this language from being used for its daily operations. This avoids the costly certified translation of the agreement in the event of legal proceedings. Managing directors who do not speak German can be given a bilingual synopsis as a reference.

5. Raising capital stock and opening an account

The company agreement determines the capital stock of the company. It is subdivided in initial contributions with which each of the shareholders participates in the company. According to Sec.5 GmbHG, the capital stock must be at least € 25,000.00. The GmbH can only be registered in the commercial register if each of the shareholders has remitted at least 25% of the subscribed capital contribution to the account of the GmbH in formation ('Vor-GmbH') and all contributions amount to at least € 12,500 (Section 7 subsection 2 GmbHG). The stock capital must be freely available to the GmbH either as a cash deposit or as a non-capital cash contribu-

tion. After being registered in the commercial register, the GmbH shall be entitled to use the full amount of the stock capital for business purposes, for example to purchase fixtures and furniture.

The nominal stock capital made available to the GmbH must be maintained during the entire duration of business operations, meaning that it may not fall below the nominal amount. In the event of a loss of stock capital of 50%, a meeting of shareholders has to be convened immediately (Sec. 49 (3) GmbHG). If the stock capital is used up completely, the shareholders must file for insolvency (Section 64 GmbHG).

In the case of corporations, a bank account must be opened for the company. This account does not necessarily have to be held at a German financial institution; it can also be opened at a financial institution from a country within the EEA as long as there is a German subsidiary or the financial institution fulfills the requirements in Sec. 53b (1) Sentence 1 or (7) KWG [“Kreditwesengesetz”: German Banking Act]. The company shall not be permitted to use a private account. The account can and must be opened as early as the foundation stage so the contributions can be paid. However, as long as the company has not been registered in the commercial register, the account remains dormant. Once the company has been registered in the commercial register, the bank enables the account, provided the excerpt from the commercial register and the tax identification number of the company have been submitted.

6. Notarization and registry

In order to establish a GmbH, it is necessary to notarize the resolution of incorporation and the company agreement, as well as the appointment of the managing director. It is furthermore necessary to draw up a list of shareholders. Once proof has been presented to the notary public that the minimum amount has been remitted to the corporate account (see number VI.4), the notary files a petition for registry of a new GmbH in the commercial register at the competent local court. Once the petition has been reviewed, the local court confirms the registration of the GmbH in writing. During the time between the notarization and the actual registry, the GmbH may already become active on the market, however, under the legal form 'GmbH i.G.'.

7. Excursus: The 'GmbH & Co. KG'

Beside the legal form 'GmbH' explained above, another legal form that has been highly popular in Germany these past decades is 'GmbH & Co. KG'. A GmbH & Co. KG basically is a 'Kommanditgesellschaft' (similar to a limited partnership, abbreviated 'KG'), and therefore is made up of a general partner with full liability ('Komplementär') and one limited partner ('Kommanditist') who is only liable with the sum of the contribution. In a GmbH & Co. KG, the GmbH is the general partner, meaning that the otherwise unlimited liability is limited to the stock capital of the GmbH. This legal form is very popular among family-run businesses as it allows them to keep the structure of a partnership whilst avoiding the unlimited personal liability of the general partner. Compared to the GmbH, a GmbH & Co. KG also has fiscal advantages. Especially regarding the trade tax and the possibility of passing losses to account, the GmbH & Co. KG can be the best choice for many.

8. Summary

Choosing the right legal form is essential to run a business in Germany. Depending on the choice, there are important differences regarding the formalities, liability and fiscal effects. For this reason, it is recommended that you clarify which legal form is right for you before you enter the market. We are happy to advise you, gauge the risk and demonstrate the practical effects of the different possibilities with clear examples.

If you've decided to establish a GmbH, we will also be happy to help you draft a suitable company agreement. We attach great importance to precise and understandable wording and thanks to our experience with corporate law, we know what issues could cause disputes and show you how to prevent them with suitable provisions in your agreement. We also organize and coordinate the notarizing process and contact all the necessary public agencies and banks.

9. Check list

This is a chronological check list of all things that need to be done when establishing a GmbH:

1. Find and determine a name for your company
2. Determine and raise the stock capital (in the case of a GmbH, at least € 25,000.00; you can choose between a cash subscription or non-cash capital contributions, in which case the economic value of the contributed goods would have to be determined)
3. Check with the Chamber of Industry and Commerce to ensure that the company name and objective of the company (purpose) are unique and cannot be mistaken for another company. The electronic commercial register provides information on all companies registered in Germany.
4. Draft the company agreement
5. Prepare a list of shareholders
6. Make an appointment with the notary to establish the GmbH and bring all founding documents for banks, the internal revenue office, etc.
7. Open a bank account for the business, remit the stock capital
8. Present proof of the deposit to the notary
9. Register the GmbH with the municipal trade office ('Gewerbeamt')
10. Request a tax identification number from the tax office/authorities ('Finanzamt')
11. Have the notary register the company
12. Pay notary and commercial register fees at the local court
13. Receive the written confirmation of the local court that the company has been registered in the commercial register
14. Prepare an opening balance sheet for the internal revenue office
15. Prepare the business papers containing at least the following information: Name, legal form, registered offices, registry court, commercial register number, first name and surname of the managing director
16. If you have a company website, it must include a legal disclaimer ('Impressum') with further information such as address, value added tax identification number, etc