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Arbitrability of Shareholder Disputes in Germany

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INTRODUCTION

Germany is considered as one of the most arbitration friendly jurisdictions in Europe if not world-wide, not least because the 1998 arbitration law is almost a *verbatim* translation of the UNCITRAL Model law. This arbitration-friendliness always encompassed also corporate disputes, safe for one minor, but important exception: arbitrations concerning the validity of shareholder resolutions. After many heated debates among scholars and courts, the German Federal Supreme Court ("**BGH**") has by now handed down three seminal decisions on this topic. These decisions show the gradual acceptance of arbitrability of shareholder disputes by the German judiciary, and will be briefly described.

On the back of this case law, foreign investors that purchase shares in a German company can be confident that possible disputes among shareholders in the target company can be comprehensively submitted to arbitration. This requires, however, that the arbitration agreement satisfies the criteria developed by the BGH. These drafting practicalities will therefore be addressed at the end.

ARBITRABILITY I

On 29 March 1996, the BGH handed down its first ruling on the arbitrability of shareholder disputes ("**Arbitrability I**").[1)] The BGH essentially denied that these disputes were amenable to arbitration.

In that case, the minority shareholder of a German limited liability company

("**GmbH**") sued the company before local courts challenging the validity of a shareholder resolution. The company objected to the court's jurisdiction on the ground that the articles of association of the company contained an arbitration clause which explicitly encompassed shareholder resolutions. The minority shareholder persuaded the local court that it had jurisdiction over the dispute. On appeal, the company prevailed with its assertion that state courts did not have jurisdiction over a shareholder claim in view of the arbitration clause. The BGH vacated the appellate court's decisions finding that shareholder disputes were not arbitrable under German law.

The BGH's Arbitrability I decision premised mainly on the fact that an award would necessarily be binding on all shareholders, irrespective of whether they participated in the arbitration or not. In ordinary court proceedings, this *erga omnes* effect is achieved through Sec. 248 German Stock Corporation Act ("**AktG**"). The BGH declined to apply this provision to arbitrations because it regarded it to be inconsistent with the arbitration law in force at that time according to which awards were only binding *inter partes*. In the BGH's view, the parties could not extend the reach of awards by agreement for three reasons:

1. There was risk that disputes concerning the validity of a shareholder resolution are not concentrated in one forum creating the risk of conflicting decisions;
2. In order to have an *erga omnes* effect, the decision needed to be completely objective and impartial, and to originate from a strictly formalized and transparent proceeding. The BGH hereby implicitly questioned to what extent arbitration satisfied these standards;
3. A shareholder who had not participated in the arbitration, but is bound by the decision because of its *erga omnes* effect, could be deprived of its right to appoint an arbitrator or influence the constitution of the tribunal.

The BGH stressed that it had no lawmaking powers and that, to the extent that arbitration in relation to the validity of shareholder resolutions was deemed to be desirable, the legislator had to provide a legal framework.

ARBITRABILITY II

In 1998, Germany amended its arbitration law, albeit without introducing a mechanism for disputes in relation to the validity of shareholder resolutions. Nevertheless, on 6 April 2009 the BGH reversed Arbitrability I through another ruling on the matter ("**Arbitrability II**").[2)]

As in Arbitrability I, the case concerned a dispute between a shareholder of a GmbH and the company. The majority of the shareholders passed a resolution according to which the claimant's shares were to be redeemed. The companies' articles of association contained an arbitration agreement that encompassed also disputes regarding the validity of shareholder resolutions. Moreover, the arbitration agreement spelled out that disputes should be tried by a three member tribunal. Further, the arbitration agreement set out that a party consisting of more than one individual or entity would be regarded as one single party and its decisions would be taken by majority vote.

The court of first instance declined jurisdiction in virtue of the arbitration agreement. On appeal, this decision was reversed because the arbitration agreement in question did not ensure that all claims concerning a specific shareholder resolution are concentrated in one forum and that all shareholders could participate in the constitution of the tribunal. Interestingly, the appellate court did not call into question the arbitrability of shareholder resolutions as such.

The BGH concurred with the appellate court that disputes concerning the validity of shareholder resolutions are, in principle, amenable to arbitration. Unlike in Arbitrability I, the BGH found that parties are free to agree on an *erga omnes* effect and that a specific legislative framework is unnecessary. This requires, however, that the arbitration lives up to the standard that the legislator had set out in Sec. 248 AktG for court decisions with *erga omnes* effect. Put differently, arbitral proceedings must to be functionally equivalent to court proceedings on the validity of shareholder resolutions. While the arbitration agreement in question did not satisfy this standard, the BGH articulated the criteria that need to be fulfilled:

1. all shareholders consented to arbitration either through an arbitration clause in the articles of association or by separate agreement;
2. all stakeholders, *i.e.*, all shareholders, managing directors, and members of the supervisory board, if any, must be notified of the institution of the arbitration and be constantly updated about the arbitration and be granted a fair opportunity to actively participate in the proceedings;
3. all stakeholder must have an equal opportunity to participate in the constitution of the tribunal;
4. all disputes regarding a specific shareholder resolution must be concentrated in one single arbitration to exclude conflicting decisions.

Finally, the BGH cautioned that an arbitration agreement that does not satisfy the above criteria is null and void.

Arbitrability III

On 6 April 2017, the BGH pronounced its most recent ruling on this matter ("**Arbitrability III**").[3] In Arbitrability III, the BGH did not alter the position under German law in substance, but extended the reach of its jurisprudence.

The facts underlying Arbitrability III are very similar to both previous cases. The major difference is that this decision related to a limited partnership under German law ("**KG**").

Both parties were shareholders of the KG. The claimant was a legal entity, namely a GmbH, whereas the respondent was a natural person. The claimants passed a resolution according to which the respondent was expelled as a shareholder. The 1968 articles of association of the KG contained an arbitration agreement. Moreover, in 1968 the shareholders had entered into a side agreement which also contained an arbitration agreement. In 2013, the shareholder replaced the 1968 articles of association, but the side agreement was left in place. Based on the arbitration clause in the 1968 side agreement, the respondent instituted arbitral proceedings challenging the validity of the shareholder resolution. While the claimant challenged the tribunal's jurisdiction, an interim award was handed down which confirmed the tribunal's jurisdiction. The claimant unsuccessfully sought to quash the interim award before local courts. This decision was vacated by the BGH.

The BGH held that Arbitrability II applied, in principle, also in relation to a KG. The ruling stressed the importance of granting all affected parties equal opportunities to influence the constitution of the tribunal, as well as a fair chance to participate in the proceedings from the beginning. The BGH advised, moreover, that these criteria may need to be adjusted if this is warranted by the different legal nature of the KG, but without providing any further guidance.

Conclusion

The above case law shows that the BGH accepts arbitration with regard to the validity of shareholder resolutions. At the same time, the BGH vigorously enforces each shareholder's right to participate in the arbitration and the constitution of the tribunal.

Foreign investors that wish to avoid litigating shareholder disputes in German courts must bear in mind the Arbitrability II jurisprudence. This does not only relate to GmbHs but also KGs, as Arbitrability III shows. In order to minimize the risks of unenforceable arbitration agreements, the German arbitration Institute ("**DIS**") has developed a model arbitration clause and Supplementary Rules for Corporate Law Disputes ("**DIS-SRCoLD**"), which incorporate the Arbitrability II criteria. Due to their complexity in relation to both the arbitration agreement and the subsequent arbitration proceedings, parties should try to agree on the DIS model arbitration clause and the DIS-SRCoLD to avoid unpleasant surprises once a dispute has arisen.[4)]

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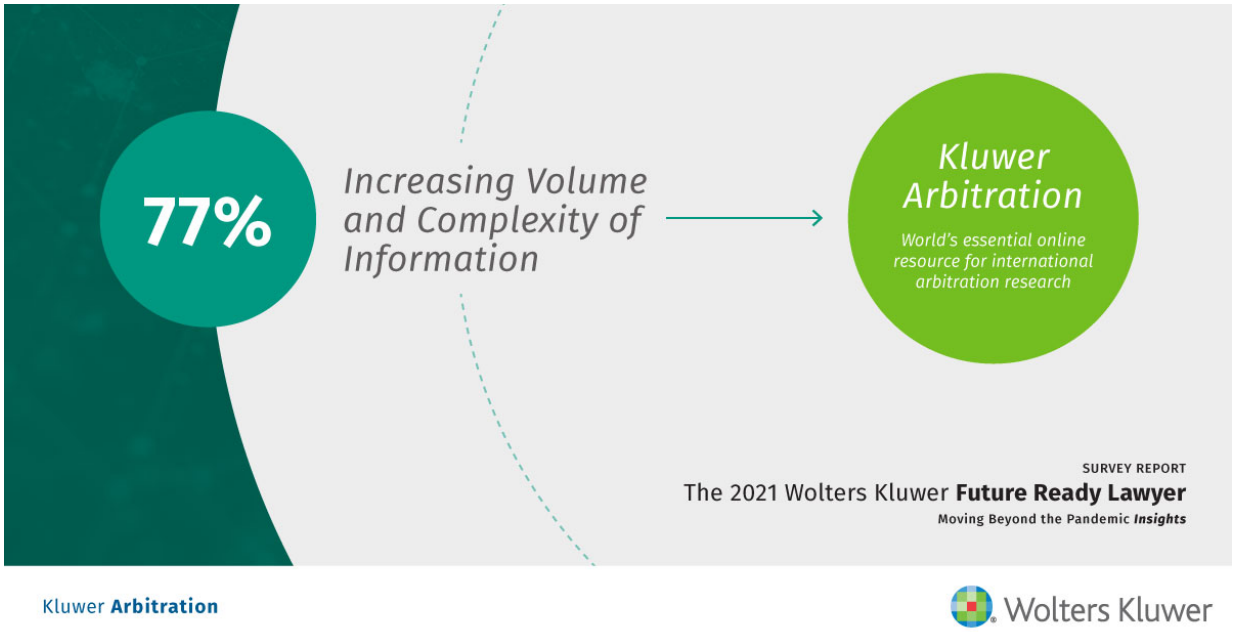

References

↑1 German Federal Supreme Court, decision, case no. II ZR 124/95 dated 29 March 1996.

↑2 German Federal Supreme Court, decision, case no. II ZR 255/08 dated 6 April 2009.

↑3 German Federal Supreme Court, resolution, case no. I ZB 23/16 dated 6 April 2017.

↑4 For an overview on the DIS-SRCoLD in English see Schmidt-Ahrendts/Covi, Arbitrability of Corporate Law Disputes: A German Perspective, International Commercial Arbitration Review, 2014 No. 1, pages 116 et seq., available on Kluwer Arbitration.

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