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SHAREHOLDER AGREEMENTS IN AUSTRIA: NEW REGULATIONS WON'T OFFER FULL PROTECTION

ASSUME NOTHING. NEW REGULATIONS FOR CIVIL LAW PARTNERSHIPS WON'T PREVENT A CONTRACTING PARTY FROM TERMINATING A SHAREHOLDER AGREEMENT. PROTECT YOURSELF AND CONSULT AN EXPERT.

The 2015 Amendment of the Austrian Civil Code rules governing civil law partnerships has the potential of affecting the status of existing shareholder agreements in unexpected ways. Thus, as a part of new 2016 omnibus corporate bill, the Austrian legislator attempts to repair the potentially problematic provisions of the 2015 statute. Nevertheless, for old and new shareholder agreements, particular caution is advisable.

As of 1 January 2015, the law governing Austrian civil law partnership has been overhauled in its entirety. Why does this matter for shareholder agreements? Because the majority-view held by courts and scholars is that shareholder agreements are to be treated as civil law partnerships.

The problem at hand is that the 2015 amendment of the Austrian Civil Code provides for the mandatory right of members of civil law partnerships to terminate such arrangements which makes it harder to include a valid provision for longer contractual terms. The contracting parties of a shareholder agreement usually want the shareholder agreement to last as long as the enterprise exists (i.e., the company governed by the shareholder agreement) or as long as a party to the shareholder agreement is a shareholder of the company.

The relevant provisions introduced as part of the 2015 Amendment of the Austrian Civil Code foresee that:

a) civil law partnerships concluded for an indefinite period of time (this is often the case with shareholder agreements) may be terminated at the end of each business year with six month notice (Section 1209 para 1 Austrian Civil Code);
b) a waiver of said termination right is unlawful; only a reasonable extension of the six month notice period is permitted (Section 1209 para 2 Austrian Civil Code);
c) civil law partnerships which have been concluded for the lifetime of a shareholder are deemed concluded for an indefinite period of time; the same applies if they are tacitly renewed after the expiry of a definite term (Section 1211 Austrian Civil Code) – and, therefore, they may be terminated nevertheless in accordance with Section 1209 Austrian Civil Code mentioned sub a).

The above mentioned rules governing the duration and termination of civil law partnerships (and, by inclusion, shareholder agreements) are going to enter into legal

effect on 1 July 2016. The unusual long gap between the law's promulgation and its entry into force can be viewed as a grace period allowing companies and their shareholders to adjust to the new law and amend their existing arrangements. Moreover, civil law partnerships which already existed prior to January 1, 2015 may postpone the taking effect of the new termination provisions until 1 January 2022 (opting-out). However, this right will need to be exercised by 30 June 2016 at the latest. (http://diepresse.com/home/recht/rechtwirtschaft/4966801/Syndikatsvertraege_Frist-bis-Ende-Juni-nicht-versaeumen?from=simarchiv).

In spite of the possibility of opting-out of the new regime for already existing agreements, the new regulations are severely criticized for restricting the contractual freedom in relation to shareholder agreements. (Cf., *Kalss/Probst*, GesRZ 2015, 154; *Artmann*, RdW 2015, 371; and *Hoenig/Buxbaum*, ecolex 2015, 671. http://wolftheiss.com/fileadmin/content/6_news/clientAlerts/2016/2016_Q2/160520_ecolex_2015_671.pdf

Perhaps in response to this criticism, the Austrian legislator reacted by means of a supplement to Section 1209 Austrian Civil Code. As of July 1, 2016, the following wording is added to its para 2: 'this does not apply to *Innengesellschaften* (a term that is commonly translated as "undisclosed civil law partnerships", as arrangements, as those that are typical among shareholders bound by a shareholder agreement, do not manifest themselves operationally towards the public)' (http://derstandard.at/2000023191908/Neues-Scheidungsrecht-fuer-Syndikate) (http://diepresse.com/home/wirtschaft/recht/4971923/Syndikatsvertraege_Gesetz-soll-repariert-werden). Due to this reaction of the Austrian legislator, as regards shareholder agreements, a waiver of termination rights is permissible and, basically, parties may also agree on extended notice periods. And yet, even though the majority of shareholder agreements may qualify as undisclosed partnerships – as foreseen by the legislator – this is not always necessarily the case. One may reasonably argue that, in case a shareholder agreement triggers any external effects (e.g., in case of financial commitments upon which bank loans are granted), no undisclosed partnership is established. Exactly, under what circumstances a shareholder agreement meets the criteria to be considered an undisclosed civil law partnership is not entirely clear. It will be for the Austrian courts, in particular, the Austrian Supreme Court, to provide clarity in future rulings.

The restrictions governing the permissible duration of civil law partnerships and shareholder agreements resulting from the provisions of Section 1211 Austrian Civil Code still remain in force. In this context, one needs to distinguish between two different scenarios: On the one hand, there may be (in our opinion, this would be the minority of cases) shareholder agreements concluded for the lifetime of a shareholder which are tacitly extended following the shareholder's death. This is a scenario most frequently encountered in connection with family businesses. On the other hand, there will be shareholder agreements which have been originally concluded for a definite term and are tacitly renewed. In our view, this would be the scenario in the majority of cases. In both instances, there is the danger of an unexpected (and unintended) termination. At

any rate, as regards the conclusion of new shareholder agreements, parties and counsel should take adequate precautions to mitigate this risk.

However, based on the provisions of the 2015 Amendment of the Civil Code which exactly mirror Section 134 Austrian Commercial Code (former Trade Act), one may conclude that an excessively long contractual term would not be enforceable and – in case a provision to that effect is nevertheless included in a shareholder agreement – the civil law partnership/shareholder agreement would in all likelihood be terminated upon the expiry of such a term as the parties might have been able to agree upon without violating Section 1209 para 1 Austrian Civil Code. The problem, however, is that nobody really knows what is the maximum duration for a long-term contract permitted by Austrian law. As regards Section 134 Austrian Commercial Code, a term of 30 to 40 years is considered as permissible, which – in the light of the same wording of Section 1211 – may also apply to civil law partnerships and shareholder agreements. This means that, by the mere passing of time, relatively old shareholder agreements are already at risk of being subject to termination and that "younger" or more recently concluded agreements may gradually "grow" into the risk associated with excessively long contractual terms. However, in light of the new provisions entering into legal effect as of July 1, 2016, according to which the prohibition of the waiver of termination rights of does not apply to undisclosed civil law partnerships (and therefore typically not for shareholder agreements) one could argue that the legislator has made it sufficiently clear that contractual terms lasting for a considerable period of time are lawful. It cannot make any difference whether an agreement has originally been concluded for e.g., 50 years or whether the right to termination has been waived for 50 years. In case the latter is permissible, this must also apply to the former. However, does this also hold true for a term of 99 years or more? Result: In case of old agreements concluded for a definite period of time, there is a risk of such agreements being subject to termination, also in cases where no right of termination is contractually stipulated for, provided that these agreements already existed for 30 or 40 years. As regards newly concluded agreements, one may assume that this problem will arise in a few decades.

Old agreements, which have expressly been concluded for an indefinite period of time (unfortunately, this is sometimes the case) remain problematic also after the enactment of the 2016 amendment which removes undisclosed civil law partnerships from the rules governing termination rights codified in Section 1209 para 2 of the Austrian Civil Code. Such agreements may be terminated under Section 1209 para 1. Therefore, also in case of new shareholder agreements such provisions should be avoided by all means.

Shareholder agreements without any provision in relation to their respective term or termination are therefore deemed to be concluded for an indefinite term and may therefore be terminated in accordance with Section 1209 para 1 Austrian Civil Code. In case of the conclusion of a new shareholder agreement such "contractual silence" should of course be avoided. Regarding old shareholder agreements, one may try to argue that the parties have tacitly agreed on the agreement's temporal limitation, namely that the agreement's term shall be limited by the existence of the principal company or shall apply for each party as long as such party is a shareholder of the principal company.

There is at least one decision by the Austrian Supreme Court in support of this view, although the facts underlying this case are somewhat atypical.

Lastly, there are shareholder agreements which are expressly concluded for the duration of the principal company (respectively for each individual party for the duration of their position as shareholder in the principal company), thus, removing the possibility for an ordinary early termination. With certain exceptions, this is also typically the contracting parties' intention. (The reason that – as indicated – shareholder agreements very often do not contain such provision may be that the termination provisions are not sufficiently taken into consideration by the parties drawing-up such agreements; it may also very well be that the parties do not reach an agreement on the rights to terminate the agreement and that the agreement therefore does not expressly address this point.) In our view, such a provision is permissible. However, there is a certain risk that one may successfully argue that a shareholder agreement containing such limitation has in fact been concluded for an indefinite period of time and, as the exact term of the principal company remains unclear, such agreement may therefore be terminated at the end of each business year under observation of the six months' notice period.

RECOMMENDATIONS:

Existing shareholder agreements should be checked for the potential risk of being terminated unexpectedly by a contracting party. Since the issues in relation to the termination respectively the term of shareholder agreements are not only subject to discussion among professionals but have also been covered in the media, one or the other shareholder might think about asserting a claim against the other shareholders by threatening or actually declaring an agreement's termination.

In this respect, one should consider using the possibility of "opting-out" of the new regime until January 1, 2022. Due to the 2016 Amendment entering into legal effect on July 1, 2016 which carves out undisclosed civil law partnerships from the scope of Section 1209 para 2 of the Austrian Civil Code, however, the exercise of this option might be dispensable in most cases. (Beware: Apart from the termination provisions there are also other regulations of the new law on civil law partnerships the applicability of which one may want to postpone).

Upon the conclusion of new shareholder agreements one should particularly consider the agreement's term and the respective provisions on the agreement's termination. As indicated above, in case of doubt the linkage of the agreement's term to the existence of the principal company or for single shareholders to the term of their position as shareholder is advisable. Remaining uncertainties may be avoided by concluding the agreement subject to a foreign (non-Austrian) law or to draft the agreement in such a way making it quite difficult to qualify as a civil law partnership.

WOLF THEISS
Christian Hoenig and Doris Buxbaum

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For more information about our services, please contact:

Christian Hoenig
Partner
christian.hoenig@wolftheiss.com
T: +43 1 51510 5040

Doris Buxbaum
Senior Associate
doris.buxbaum@wolftheiss.com
T: +43 1 51510 5046

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Wolf Theiss
Schubertring 6
AT – 1010 Vienna

www.wolftheiss.com