# Corporate Reorganisations 2019

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*Latham & Watkins*

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Getting The Deal Through

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Lexology Getting The Deal Through is delighted to publish the second edition of *Corporate Reorganisations*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Belgium and Turkey.

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Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editors, Nick Cline, Robbie McLaren and Frederick Brodie of Latham & Watkins, for their continued assistance with this volume.

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# Introduction

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'Corporate reorganisation' is something of an umbrella term, and is used in many different contexts to mean a multitude of different things. At one extreme, a reorganisation may refer to 'paper' changes to a corporate group's funding and capital structure that, ultimately, have little or no impact on customers, suppliers or employees of the companies concerned. At the other extreme, a full 'operational' reorganisation can involve fundamental changes to the way a business operates, affecting day-to-day trading arrangements with customers and suppliers, having a major impact on employees and affecting regulatory status. It is important to draw a distinction at the outset between the solvent corporate reorganisations that are the focus of this guide, and insolvent or financially distressed restructurings, the latter of which is addressed separately in *Lexology Getting The Deal Through – Restructuring & Insolvency*.

Reorganisations broadly fall into two categories: internally driven and externally driven. Internally driven reorganisations are those caused by factors relating specifically to the group itself, such as trading performance and corporate acquisitions, disposals and mergers. Externally driven reorganisations include factors such as the economic environment, changes in laws, or tax regimes and geopolitical pressures, all of which can be incentives for company managers to undertake business reviews and seek to optimise their company's performance and prospects. Consequently, the objectives of a reorganisation are hugely diverse and typically multifaceted. In practice, this means that many businesses, and particularly very large businesses, will experience at least some drivers for reorganising frequently or even constantly. Recent years have seen tax-driven inversions and re-domiciliations by high-profile multinationals. Operationally, the relatively low growth environment in Western economies since 2007–2008 has seen corporate groups focus on increasing bottom line profits through cost-cutting and efficiency measures. Analysis by McKinsey in 2016 indicated that approximately 60 per cent of companies in the S&P 500 had undertaken significant cost-reduction or reorganisation activities in the preceding five years.

Unlike many of the areas dealt with in Lexology Getting The Deal Through's series of guides, corporate reorganisations are typically quasi-internal transactions with no real counterparties to the group undertaking the reorganisation. The lack of an adverse party or parties can make reorganisations easier to implement than other transactions in certain respects, as there is often no need to negotiate terms. That is not to say, however, that third parties are not involved, or that there are no challenging issues – on the contrary, corporate reorganisations nearly always involve a number of external and internal stakeholders, so giving due consideration to these parties' interests is essential. The involvement of multiple third parties means planning, engagement and communication are critical to the successful implementation of a reorganisation. Depending on the nature and purpose of a reorganisation, a company may need to draw on the expertise of legal, financial, tax, accountancy, regulatory, PR, employment and benefits, or other professionals. The mechanisms for – and challenges to – implementing reorganisations are equally varied, with some jurisdictions recognising corporate mergers (such as the cross-border merger regulations applicable in the EU) or providing mechanisms for transferring businesses comprising assets and liabilities relatively easily, while others do not. Large, multi-jurisdictional reorganisations are nearly always complex and time-consuming, making careful coordination, timing and project management between jurisdictions important considerations. Some legal systems have procedures that allow reorganisations to be undertaken privately, whereas others are more public in nature, owing to matters such as creditor notification obligations, or the necessity of involving courts to effect or approve reorganisation steps.

In all but the most straightforward 'paper' reorganisations, it will be necessary to identify and communicate with key stakeholders. To employees, regulators and contractual counterparties, simply hearing that a company is undergoing a reorganisation can cause concerns about potential job losses, compliance with regulatory requirements or reductions in creditworthiness and reliability. These concerns can often be addressed by communicating early and clearly with stakeholders and consulting them where appropriate. Employees in particular are afforded extensive rights and protections in some countries and may have an automatic entitlement to be consulted, even where no redundancies or changes to working conditions are anticipated. Consultation obligations can be complicated by the presence of collective bargaining or representation arrangements, and this is a particularly important issue in industries and jurisdictions where work forces are unionised or represented by works councils. Where such formal structures exist, the level of engagement may be prescribed; although, even in jurisdictions where that is not the case, the need to preserve industrial relations may dictate a certain level of employee involvement in the reorganisation process. Straightforward 'paper' reorganisations involving an intragroup transfer of shares in a wholly owned subsidiary may seem unlikely to present material issues, but may nonetheless inadvertently trigger change-of-control provisions in contracts with customers and suppliers, or result in a breach of the terms of a regulatory licence or finance and security documents. The examples outlined here are just a sample of the issues that may arise in the context of reorganisations. Groups should, therefore, consider the available options in the context of the relevant circumstances, and select the most appropriate mechanisms in each jurisdiction to minimise the risk of unexpected challenges arising at or after implementation of the reorganisation.

**Brexit**

We must also mention the United Kingdom's decision to leave the European Union. The decision was described by Jean-Claude Juncker, the president of the European Commission, as posing an 'existential threat' to the European integration project that has progressed across much of Europe for decades. While the full terms and implications of the UK's exit remain unclear even one month from 29 March 2019, the scheduled date for Brexit, many large multinational businesses – and particularly those in industries that rely heavily on pan-European



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regulatory frameworks – have been reorganising their operations in preparation for Brexit. A number of organisations have formally announced plans to redomicile in the Netherlands and other European jurisdictions, and to move operations and supply chains out of the UK – citing Brexit as one of the key motivations.

This has mirrored the steps taken by the EU in relation to those European agencies and institutions that have been based in the UK, with the EU27 ministers voting on 20 November 2017 to relocate the European Medicines Agency to Amsterdam and the European Banking Authority to Paris.

Since such announcement, there has been extensive speculation regarding whether businesses in the pharmaceutical and banking industries are likely to follow the agencies by setting up new operations in Amsterdam and Paris. Even before the recent relocation announcements, many businesses, particularly those in the financial services sector (many of which rely on 'passporting' rights between the UK and the rest of the EU allowing them to operate across the EU market), had publicly announced plans to migrate operations. The fear of losing rights to access the EU market has already caused banks, insurers, asset managers and other financial services providers to start relocating employees and operations from London to major European financial centres to ensure business continuity in the event that the Brexit terms do not include ongoing passporting rights.



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# England & Wales

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## LEGAL AND REGULATORY FRAMEWORK

### Types of transaction

**1 What types of transactions are classified as 'corporate reorganisations' in your jurisdiction?**

The term 'corporate reorganisation' can be used to mean a wide variety of transactions, but is most typically used to refer to transactions involving the transfer of assets, whole businesses or shares between entities forming part of the same corporate group on a solvent basis. Certain related company law matters also commonly arise in the context of corporate reorganisations, such as adjustments to the funding and capitalisation of companies, returns of profits or capital to shareholders, and intra-group services and loans. Reorganisations may be operational, where the manner in which an underlying business operates changes, or financial, where the funding and capital structure changes but the underlying business continues to operate in the same way.

Corporate reorganisations may be driven by a number of factors, the most common of which are: (i) to prepare for a sale of part of a corporate group or business; (ii) to integrate an acquired business or group into the corporate structure of the acquirer (or to prepare for the integration of a prospective target); (iii) to improve the efficiency of operations or capital structure; and (iv) to facilitate a refinancing or the granting of security. Transactions such as shareholder distributions and intra-group loans often arise in reorganisations but may also occur in the ordinary course of business as part of the day-to-day means of managing cash within a corporate group, so are not necessarily indicative of a reorganisation.

### Rate of reorganisations

**2 Has the number of corporate reorganisations in your jurisdiction increased or decreased this year compared with previous years? If so, why?**

Given the wide variety of drivers for undertaking corporate reorganisations, demand tends to be relatively steady, regardless of economic conditions. Some of the drivers for corporate reorganisations are linked to M&A activity, so high M&A activity tends to result in more M&A-related corporate reorganisations, such as reorganisations in contemplation of a disposal or for integration purposes following an acquisition. Larger M&A transactions in particular often lead to substantial post-transaction integration work, and also potentially sale preparation work, where the acquirer wishes to divest any non-core assets acquired as part of the transaction or needs to comply with a requirement from a competition regulator in relation to the original acquisition.

Conversely, in periods of lower M&A activity, there are countercyclical drivers for reorganisations. Where market uncertainty, financial conditions or other factors reduce M&A activity, businesses often choose to focus on internal opportunities, such as improving operational efficiency or the capital structure and funding of the business. The demand for corporate reorganisations, therefore, exists through the economic cycle. Occasionally, one-off factors, such as changes in law or regulation, may trigger short-term increases or decreases in the number of reorganisations as new rules open up new opportunities or close down previously available options.

### Jurisdiction-specific drivers

**3 Are there any jurisdiction-specific drivers for undertaking a corporate reorganisation?**

One recent example of a one-off driver causing an increase in reorganisations is the result of Brexit, the United Kingdom's vote to leave the European Union. While the implications of Brexit still remain unclear, the UK's departure from the EU could have a dramatic impact on companies in sectors that are heavily influenced by EU regulation, such as financial services or pharmaceuticals. Many financial services groups have either started making contingency plans or actively taking measures to mitigate the potential effects of Brexit, which may include the loss of passporting rights between the UK and the rest of the EU, which many UK financial services businesses rely on to operate across the EU market (and vice versa). A number of multinational organisations have also announced plans to redomicile their European headquarters from the UK to the Netherlands and other jurisdictions in continental Europe.

### Structure

**4 How are corporate reorganisations typically structured in your jurisdiction?**

The structuring of a reorganisation will depend on its particular circumstances, but there are a number of overarching concepts that it is useful to keep in mind as general guiding principles:

- transactions between group companies should typically be entered into at arm's length (eg, charging reasonable interest on loans, not transferring assets at an undervalue, and charging a market rate for services);
- distributions may only be made where distributable profits are available for the purpose (see below);
- companies must maintain their share capital and may only return share capital to shareholders through limited routes permitted under company law (eg, share buy-backs, reduction of capital procedures or through a winding up);
- directors' duties are owed to each corporate entity to which a director is appointed, and may override the interests of the corporate group as a whole (even if the directors also happen to serve as directors of other group companies); directors must consider their duties in the context of a reorganisation just as they do for third-party transactions, including assessing the corporate benefit of a particular course of action for the company in question, taking into account the circumstances in the round;


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- the articles of association of each of the companies involved (as well as any applicable shareholders' agreement) should be reviewed to check whether they provide for any peculiar restrictions or procedural requirements in relation to the step proposed (for example, the requirement for shareholder approval in respect of an acquisition or disposal even between group companies); and
- any relevant finance documents or other material contracts should be checked for restrictions, particularly for change-of-control provisions.

When considering a reorganisation plan, it is also important to consider whether any transactions could be challenged by a liquidator or administrator in the event of a subsequent insolvency, such as transactions at an undervalue or preference at a time when the company is unable to pay its debts, or where such transactions cause the company to become unable to pay its debts.

In respect of acquisitions of shares of public companies (or private companies with a public company subsidiary), financial assistance is generally prohibited, though this is not the case in relation to acquisitions of shares of private companies generally. See below for further details on financial assistance.

**Laws and regulations**

5 | What are the key laws and regulations to consider when undertaking a corporate reorganisation?

The Companies Act 2006 (CA 2006) sets out the primary legal framework in relation to distributions and maintenance of share capital requirements, as well as codifying the duties owed by directors to their appointing companies. However, old common-law rules continue to apply and remain a key part of the analysis of whether a distribution is lawful or not. Other relevant areas of law that generally apply include tax, employment, pensions, data protection and others, though additional areas may apply depending on a company's industry and regulatory status. See below for further details on regulation.

**National authorities**

6 | What are the key national authorities to be conscious of when undertaking a corporate reorganisation?

There are no national authorities that are automatically involved in corporate reorganisations. However, a wide variety of authorities may be involved, depending on: the nature of the group undertaking the reorganisation; whether the companies affected by the reorganisation are regulated; and the reorganisation steps themselves. Regardless of the nature of the group or its regulatory status, if it operates a UK defined benefit pension plan (DB Plan), the UK Pensions Regulator will need to be considered (see further below).

Reorganisations of businesses that are regulated (eg, financial services, pharmaceuticals or defence) or dependent on specific licences to operate will usually require additional planning and a longer implementation period. In such cases, it is likely that advice will need to be obtained and regulators consulted prior to undertaking any reorganisation. While exemptions for intra-group transactions may be available in some situations, this is not always the case; even seemingly innocuous matters, such as small adjustments to shareholdings as between members of the same corporate group, changing personnel in particular roles or inserting a new indirect intermediate holding company into an ownership chain, may require regulatory consent. The implications of failing to obtain mandatory consent can be severe, with potential criminal penalties for both legal entities and individuals.

## KEY ISSUES

**Preparation**

7 | What measures should be taken to best prepare for a corporate reorganisation?

Planning the reorganisation prior to its commencement is key. Where the optimisation of the capital structure (including funding and tax) is a significant driver for a reorganisation, accounting and tax leads will typically design an outline of the reorganisation with its objectives in mind, sometimes setting out proposed steps for achieving those results. Where the steps are specified, legal advisers will need to analyse the proposed steps to establish their feasibility from a legal perspective. Where detailed steps are not specified, legal advisers will need to assess and advise on the available options. In either case, tax and legal advisers typically need to work together to create a plan that implements the group's reorganisation objectives.

Although corporate reorganisations are primarily intra-group transactions, they must nonetheless be considered and planned carefully, as a number of internal and external stakeholders are likely to be interested in their objectives and implementation. Communication with key stakeholders is therefore important and should be considered early in the planning stage. Employees in particular may be very sensitive to the implications of a reorganisation and worry about their job security. Auditors will need to review and assess the transactions undertaken and the way they have been accounted for during the course of their annual audit, and tax authorities may do the same from a tax perspective. Prospective buyers will normally undertake due diligence where a pre-sale corporate reorganisation has been undertaken and will want comfort that the transactions were properly undertaken, that the correct assets and liabilities are held in the target group, and that the reorganisation has not resulted in the target group inadvertently incurring liabilities. Commercially, customers and suppliers may be concerned about their trading partners' financial stability and reliability, and contracts or assets may not be capable of transfer without a consent or waiver from contractual counterparties, particularly where prohibitions on assignment or subcontracting do not contain a carve-out for intra-group transactions. Lenders (particularly those holding security over affected companies or assets) may need to be consulted and their approval sought under the terms of finance or security documents. In these circumstances, the lenders will need to be satisfied that their risk exposure or security position is not adversely impacted by a proposed reorganisation.

In order to plan with all the above in mind, a preparatory due diligence or information gathering exercise is helpful in ensuring the re-organisation is structured and implemented optimally. The number of issues to consider means that larger reorganisations require extensive coordination and project management.

**Employment issues**

8 | What are the main issues relating to employees and employment contracts to consider in a corporate reorganisation?

The impact of a reorganisation on employees depends on how it is structured. If a reorganisation is effected through transfers of shares and employees remain with their existing employers, the reorganisation should have a limited impact on those individuals, and their terms and conditions of employment. However, if a reorganisation will result in employees transferring between group companies, this is likely to constitute an employee transfer under the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE). TUPE requires a prescribed informational process (and, in certain circumstances, a


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consultation process) to be carried out with employee representatives prior to the transfer, and generally restricts changes to employee terms and conditions, and redundancies in connection with the transfer.

Aside from any TUPE transfer, another possible outcome of a reorganisation might be employee redundancies. If so, a pre-redundancy consultation process would need to be undertaken with, or on behalf of, the relevant employees in accordance with UK law and redundancy payments would be payable (either on a statutory minimum or company-specific enhanced basis). If 20 or more employees are being made redundant, a consultation period of a minimum of 30 days will apply prior to the redundancies being implemented.

9 | What are the main issues relating to pensions and other benefits to consider in a corporate reorganisation?

The key issue to consider is whether the group operates, has operated, or is a participant in a DB Plan, and whether the reorganisation is being undertaken in connection with an M&A transaction. In any case, the impact of the reorganisation on the DB Plan should be assessed and, where necessary, addressed. If a company that participates in a group pension plan is to be sold to a third-party purchaser (with the pension plan staying behind with the retained seller group), in practice, the departing company will need to cease participation in the pension plan. If so, its pension liabilities can be apportioned on a contingent basis to one or more group companies that will continue to participate in the pension plan. The UK Pensions Regulator (the Regulator) and the pension plan trustees are likely to play an important role in this process. Appropriate legal, financial and actuarial advice may need to be obtained by the group before implementing a reorganisation, particularly where a DB Plan is involved.

No formal consent is needed from the Regulator in relation to re-organisations. However, if the Regulator considers that a reorganisation is materially detrimental to a DB Plan, it has statutory 'moral hazard' powers, which it can seek to exercise against the group (and any other connected parties, wherever located in the world) to require additional funding or other financial support to be put in place to support the DB Plan. This can be up to the level of the DB Plan's buyout deficit (ie, the cost of securing liabilities in full with an insurance company). The Regulator has been increasingly interventionist in its approach in recent times, particularly in relation to M&A transactions, so reorganisations undertaken in contemplation of M&A transactions may come under increased scrutiny and should be planned with the M&A process in mind. The Regulator operates a voluntary 'clearance' process, which allows groups to seek confirmation that the Regulator will not exercise its moral hazard powers in connection with a reorganisation.

The consent of the trustees of the DB Plan is likely to be required if the reorganisation will result in any group company ceasing to participate in the DB Plan (for example, if that company is being substituted for another group company as a participating DB Plan employer). The trustees' consent should generally not be required for any reorganisation steps as such. However, the trustees will need to be informed of any material corporate activity within one month of this taking place and, if they are concerned about the impact of the reorganisation on a DB Plan, they may seek to exercise any powers available to them (such as to demand additional employer contributions to the DB Plan) or involve the Regulator.

In relation to other employee benefits (including defined contribution pension arrangements), the impact of the reorganisation is unlikely to have a material impact from a legal perspective, although it may still need to be addressed. For example, if employees are transferring under TUPE from one group company to another, the receiving employer will need to ensure it has suitable benefit arrangements in place for provide the transferring employees. The impact of the reorganisation on any share incentive arrangements will also need to be evaluated (eg, whether the reorganisation will result in the accelerated vesting of any employee share options).

**Financial assistance**

10 | Is financial assistance prohibited or restricted in your jurisdiction?

The historic prohibition on the giving of financial assistance by a company in connection with the acquisition of its shares by a third party was repealed in respect of private companies on 1 October 2008. Therefore, the current position under English law is that private companies that are not part of group involving a public company may give financial assistance to fund a third party's acquisition of its or its parent company's shares.

The position is different in relation to public companies, which are prohibited from giving financial assistance for the purpose of the acquisition of their shares or shares in a parent company. This prohibition also prevents private company subsidiaries from financially assisting such acquisition of shares in a public company that is its parent company. The term 'financial assistance' is broadly defined and can include (without limitation) cash payments, gifts, loans, transfers above or below fair market value, asset transfers, incurring liabilities, releasing debts and providing security.

Where a reorganisation involves the acquisition of shares in a public company or its parent, it is essential to ensure that the parties involved comply with the relevant provisions of the CA 2006. A breach of the financial assistance prohibition may result in fines, and directors may face fines or prison terms of up to two years, or both. In 2017, four former executives at a major listed UK bank were charged with criminal offences in relation to the giving of unlawful financial assistance during the financial crisis in 2008.

**Common problems**

11 | What are the most commonly overlooked issues or frequently asked questions in a corporate reorganisation?

One common area of difficulty is in relation to 'capital contributions' (ie, contributions to the capital of a company without the issuance of shares). Capital contributions are common in some jurisdictions, but are a source of uncertainty and confusion in England owing to a lack of statutory framework (the CA 2006 makes no reference to capital contributions) and conflicting guidance regarding their treatment from tax and accounting authorities, and in case law.

HM Revenue & Customs' (HMRC's) guidance manual states that capital contributions are 'occasionally' made and proposes that they should be treated as either 'distributable reserves . . . as a gift or a donation' or, where such payment may be repayable in any circumstances, as a loan. The Privy Council case of *Kellar v Williams* states that 'if the shareholders of a company agree to increase its capital without a formal allocation of shares, that capital will become, like share premium, part of the owner's equity, and there is nothing in the company law of . . . England to render their argument ineffective', indicating that a capital contribution should go to a non-distributable reserve. Finally, the guidance in the technical release on realised and distributable profits issued by the Institute of Chartered Accountants in England and Wales in April 2017 states that a capital contribution will be treated as a realised profit (thereby increasing distributable reserves) where it is received in the form of 'qualifying consideration'. The question of whether consideration is qualifying is not always straightforward, as the definition of 'qualifying consideration' includes cash, assets readily convertible into cash, the release, settlement or assumption of liabilities by a third party and various other forms of consideration that are essentially 'cash-like'



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by nature, but these may need to be set off against any liabilities contributed.

As a result of the uncertainty surrounding capital contributions, tax, accounting and legal advice should always be sought where capital contributions are proposed, and the terms on which a capital contribution is given and received should be clearly documented and recorded.

Other common issues include, in relation to employment and pensions, the need to consider the powers of the UK Pensions Regulator and pension plan trustees in any reorganisation involving a DB Plan and the application of TUPE. The internal flow of services and licences, and the changes that arise as a result of a reorganisation, are also commonly overlooked. Developments in recent years in relation to data protection also need to be considered to ensure changes in the flows of personal data resulting from the reorganisation are compliant and accurately reflected in policies and consents.

## ACCOUNTING AND TAX

### Accounting and valuation

**12** How will the corporate reorganisation be treated from an accounting perspective? How are target assets and businesses valued?

The accounting treatment will depend on the precise steps carried out as part of the reorganisation. As seen above in relation to capital contributions, the accounting treatment may not be straightforward, so it is important to obtain accounting advice before undertaking a re-organisation to ensure the desired accounting outcomes are achieved. In addition, where distributions are contemplated, it may be necessary or desirable to obtain assistance from accountants in verifying both whether the relevant companies have sufficient distributable profits, and whether distributions received from subsidiaries may be treated as realised profits (and whether an impairment in the book value of the subsidiary making the distribution should be made as a result of the distribution).

### Tax issues

**13** What tax issues need to be considered? What are the tax implications of carrying out a corporate reorganisation?

Specific tax advice should always be obtained in good time during the planning phase of the reorganisation, and the documents implementing a reorganisation should be reviewed from a tax perspective to ensure the desired tax treatment is achieved. This is important because reorganisations can impact taxation at both the corporate group level (in terms of the reorganisation steps and also in terms of the tax profile of the group going forwards) and shareholder level. Depending on where the relevant group companies and shareholders are based, consideration may need to be given to non-UK as well as UK tax systems.

In principle, some of the key aims of any tax structuring will be to avoid the incurrence of any 'dry' tax charges caused by the reorganisation (ie, the triggering of a tax charge where the liable entity has not received any corresponding income or gain that would enable it to pay the tax charge), and also to minimise or eliminate any transfer taxes or stamp duty that may be incurred as a result of the reorganisation steps. These aims can often be achieved through relying on various reorganisation exemptions provided for in tax legislation, but care is typically required to ensure that such exemptions are available. It is, therefore, important for tax advisers to work closely with the legal advisers drafting the documentation for implementing the reorganisation steps and review its terms to ensure the desired tax treatment is achieved.

It is usually permissible for companies forming a group for capital gains purposes to transfer assets on a tax-neutral basis. The intention of this is to treat companies in the same group as one taxable entity. It should be noted that when an intra-group transfer is on a no-gain, no-loss capital gains basis, there may be a de-grouping charge if one of the companies in the group exits within six years of the transfer.

While usually not mandatory, consideration should be given to whether any tax authority filings or clearances are desirable in connection with a proposed reorganisation, particularly where the application of exemptions or relief is essential to avoid a dry tax charge.

In addition, in July 2013 the Organisation for Economic Co-operation and Development (OECD) published an Action Plan on 'Base Erosion and Profit Shifting' (BEPS). Its 15 'actions' are aimed at providing an international framework to address and combat international tax avoidance. Over recent years OECD and G20 countries have introduced a number of tax measures aimed at implementing the BEPS project. For example, in response to Action 4, the UK introduced new rules with effect from 1 April 2017 that limit the amount of interest that may be deductible for corporation tax purposes for large UK groups. There is now a greater focus on BEPS when structuring new transactions, and it is likely that larger corporate groups will continue to review their internal funding structures and react accordingly in light of recent and future developments.

## CONSENT AND APPROVALS

### External consent and approvals

**14** What external consents and approvals will be required for the corporate reorganisation?

As noted above, various third parties will usually have an interest in a reorganisation. Whether the third-party consent is required or not will depend on the specific facts of the reorganisation (eg, whether a company has third-party financing arrangements in place, whether contracts or land will be transferred, whether a business is subject to regulatory oversight, whether contracts contain change-of-control provisions and whether shareholder rights are engaged). In some cases, advance consent may not be necessary, but a company may be obliged to give notice before or after the reorganisation is implemented.

For regulated groups, mandatory consent or notifications may be required. Such consent and notifications are usually required before a reorganisation can be implemented, and it is especially important to undertake a detailed analysis of any regulatory requirements where the group is involved in a heavily regulated sector, such as energy and power, telecommunications or financial services. Failure to obtain a mandatory consent could give rise to criminal liability for a company or its directors.

See questions 6 and 9 in relation to pensions approvals and tax notifications.

### Internal consent and approvals

**15** What internal corporate consents and approvals will be required for the corporate reorganisation?

As with most considerations in relation to reorganisations, the internal corporate consents and approvals required for the corporate re-organisation will depend on the steps being taken and the extent of the reorganisation. As a matter of good corporate governance, directors should act formally in relation to significant decisions and record their decisions in board minutes, even if their decision is to delegate responsibility for oversight and implementation of the reorganisation to an individual or committee.

Reorganisations will usually involve the boards of multiple companies making decisions. Each company's board (even if boards comprise the same individual members) must independently consider significant transactions relevant to that company in terms of the corporate benefit



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of the transactions proposed. The directors of a company owe statutory duties under the CA 2006 to that company, even if that company forms part of a larger group. They must act in the best interests of that company, and should consider any potential conflicts of interest they may have in relation to proposed transactions. If it is not clear whether a matter is in the best interests of the company or presents a conflict, directors should consider whether to seek shareholder approval of the relevant matters.

Shareholder approvals or resolutions may be mandatory under constitutional documents, shareholder agreements or company law for certain actions. Since some constitutional documents and shareholders' agreements prevent directors from making significant disposals or acquisitions in the absence of shareholder approval (or approval of a certain class of shareholder), constitutional documents and shareholders' agreements (if any) should always be checked. They may contain exemptions from shareholder approval requirements for intragroup transactions, but this should be verified. Shareholder approval may also be required where a director of the selling company in a group is a shareholder in the buyer. In this instance, the disposal may constitute a substantial property transaction under section 190 of the CA 2006, though transactions between a holding company and wholly owned subsidiaries are exempt from this requirement.

## ASSETS

### Shared assets and services

**16 | How are shared assets and services used by the target company or business typically treated?**

Assets and services that are shared by a party to the reorganisation should be identified in the planning stage of a reorganisation so that an assessment can be made as to the impact of the reorganisation steps on them. Where assets are owned by the group and services are internally provided, a reorganisation is less likely to cause significant challenges. However, where an entity holds contracts with third parties on behalf of the group and services are provided to a company involved in a reorganisation on a pass-through basis, the terms of the underlying third-party contract will need to be checked to ensure that the services may continue to be provided following the implementation of the reorganisation. Where the terms are such that the services could not continue to be provided following a proposed reorganisation, it may be necessary to seek the third party's consent to continue providing the services following the reorganisation or, failing that, make alternative arrangements.

It may also be necessary to license back intellectual property or information technology contributed to a company by its parent, or to grant new licences to newly incorporated group members to allow them the use of shared assets, such as intellectual property or information technology. Consideration should be given to the terms and documentation of shared assets and services, particularly as regards transfer pricing arrangements within a group. Particular care should be taken where a reorganisation is undertaken in preparation for a sale, especially where the proposed target requires licences and services provided by the selling group to operate.

### Transferring assets

**17 | Are there any restrictions on transferring assets to related companies?**

Transferring assets between related companies is generally permitted and is common in practice. If the transfer is on arm's-length terms (ie, for fair market value), then there are no issues or restrictions, since there is no extraction of value from one company in favour of the other. Issues and restrictions may arise where a company proposes to transfer assets for less than fair market value (see question 18) or pay more than fair market value for assets (which may be treated as a deemed distribution if the payor is a subsidiary or sister company of the transferor).

Where a company has given a charge over its assets, the consent of one or more lenders under the terms of the applicable finance or security documents will likely be required. Assets that are subject to a fixed charge will need to be released and a non-crystallisation certificate may need to be obtained for those assets that are subject to a floating charge before they can be transferred as part of a reorganisation.

Some classes of assets are subject to additional requirements in connection with their transfer. For example, if assets relate to accreditation marks, their transfer will require special permission to ensure the transferee has the ability to uphold and enforce the accreditation system. Intellectual property rights will be transferred subject to any licences of which the transferee has notice.

Before transferring personal data between companies, the terms on which the data is held should be checked to ensure that the transfer and post-transfer use of the data will be permitted and in accordance with applicable data protection laws (eg, by way of binding corporate rules or data transfer agreements). This issue has gained greater significance following the General Data Protection Regulation, which came into force across the EU on 25 May 2018 and can involve material penalties if breached.

**18 | Can assets be transferred for less than their market value?**

Where a transfer of an asset is made to a parent or sister company for consideration that is less than the fair market value of the asset, or where payment in excess of fair market value of an asset is made to a parent or sister company, the maintenance of capital rules are engaged and must be considered. Such a transfer will generally be considered a distribution and must therefore comply with detailed requirements to ensure it does not constitute an unlawful distribution. In order to determine whether a transfer at less than fair market value or payment in excess of fair market value is permitted, the company must first establish the value of the distribution and assess whether it has sufficient distributable profits to justify the proposed transfer. A distribution that does not comply with the relevant rules will be unlawful, and the consequences of unlawful distributions may include: (i) a shareholder who knew or had reasonable grounds to believe that a distribution (or part thereof) was unlawful may be liable to repay the unlawful amount; (ii) a director who authorised the payment of an unlawful distribution may have breached statutory or common-law duties and may therefore be personally liable to repay the company; and (iii) distributions constituting an unlawful return of capital may trigger a default under third-party finance arrangements.

Where a company has distributable profits, a transfer of an asset for consideration that is equal to or greater than the asset's net book value will be permitted, even where the consideration is less than fair market value. In those circumstances, a transfer at net book value is deemed to be a distribution of zero, whereas a distribution for more than net book value will increase the company's distributable profits. However, where the consideration is less than net book value, the transferring company may only make the transfer if it has distributable profits of at least the amount of the difference between the price paid and the net book value of the asset (ie, the deficit); and the transfer does not entirely extinguish the company's distributable profits, even if the transaction leaves the company with only a nominal amount of distributable profits following the transfer. If a company does not satisfy these criteria, the transfer will constitute an unlawful distribution.

Even if an asset is deemed to be lawfully distributed for the purposes of the CA 2006, a transfer may still result in a breach of the common law



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maintenance of capital rules or the Insolvency Act 1986 prohibition on transactions at an undervalue (if the company subsequently goes into administration or liquidation within a statutory 'hardening period').

Finally, a director's statutory duties must always be considered, as noted above. A transfer may constitute a lawful distribution, but not be in the best interests of the transferor and therefore result in a breach of duty being committed by the company's directors.

## FORMALITIES

### Date of reorganisation

**19 Can a corporate reorganisation be backdated or deemed to have already taken place, for example from the start of the financial year?**

Where a group wants to give effect to a step from a given date in the past, it is possible to state in the contract that parties agree that the step is to take effect from an earlier date. This will only be an effective agreement between the relevant parties, and will not alter obligations to third parties, in particular to HMRC. A company's auditor may question attempts to give retroactive effect to a reorganisation, so it is prudent to consult the auditor before undertaking reorganisation transactions.

If steps or a reorganisation has occurred historically without formalisation, then steps can be taken to ratify and document the transactions that were undertaken. If this is the case, there will usually be evidence in the form of accounts and bank statements. Where reorganisation steps are documented retrospectively, the documents may state that the steps took place on an earlier date, notwithstanding that the document recording it is dated with a later date, though actions that require certain formalities to be complied with, or registrations or notifications to be made, will only take effect when the relevant formalities, registrations or notifications have taken place.

The above situations are not the same as backdating documents (ie, dating a document with an earlier date than that on which it is actually executed). Backdating documents can result in a number of criminal offences being committed, including under the Theft Act 1968, the Fraud Act 2006 and the Forgery and Counterfeiting Act 1981, and may additionally constitute a misrepresentation, which could give rise to civil liability.

### Documentation

**20 What documentation is required in a corporate reorganisation?**

It is not usually necessary to include extensive protections in documents between members of the same group, so the documents implementing a reorganisation are generally shorter and less detailed in their content. However, it is nevertheless important that the transactions undertaken and their terms are properly recorded, authorised and executed. In some instances, a more arm's-length approach may be appropriate, such as where the solvency of one of the parties is an issue or where one of the parties may be sold following the reorganisation.

Reorganisations involving a transfer of shares or a business typically involve the following documentation:

- an asset or share purchase agreement;
- formal transfer documentation (eg, stock transfer forms for shares, property transfers or assignments, assignments or licences of intellectual property rights, assignments, or novations of contracts, including licences);
- ancillary documents, including board or shareholder minutes or resolutions, notices to employees, HMRC notifications, clearances or applications for relief, loan agreements (if consideration for the transaction will be left outstanding as an intra-group loan), releases from charges, new banking security documentation; and
- other documents for separation purposes (eg, transitional services agreements, service agreements and additional intellectual property licences).

### Representations, warranties and indemnities

**21 Should representations, warranties or indemnities be given by the parties in a corporate reorganisation?**

It is not common practice for the parties to a reorganisation to include extensive protective provisions in the documentation implementing a reorganisation. Transfers are often made with either no warranties or very limited warranties covering, for example, a few key matters, such as the transferring party's title to the relevant assets or shares. A warranty on title is advisable for the purposes of satisfying the directors' duties for the directors in the buyer. The transferee's directors may also want the documentation to confirm that all major known liabilities are disclosed; although, where the parties have common directors this may not be considered necessary. It is not common to include representations, indemnities or provisions relating to confidentiality, price adjustments or post-transfer conduct in intra-group documentation; however, as noted above, a more arm's-length approach may be appropriate where one party may be sold following the reorganisation. Regardless of the terms of the documentation, purchasers may consider it necessary to seek indemnification or warranty protection from sellers in relation to pre-sale reorganisations affecting a target company.

### Assets versus going concern

**22 Does it make any difference whether assets or a business as a going concern are transferred?**

From a tax perspective, a transfer of a business as a going concern is outside the scope of VAT. The VAT treatment of a transfer of assets that do not comprise a going concern will need to be considered individually, but it is likely that VAT will be payable where assets are transferred other than as part of a going concern.

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**Type of entities**

23 | Explain any differences between public, private, government or non-profit entities to consider when undertaking a corporate reorganisation.

As noted above, additional restrictions, such as the prohibition on financial assistance, apply to public companies, potentially making reorganisations of public companies and their groups more challenging. In addition to company law issues, public companies listed on a stock exchange will need to comply with the rules and requirements of the exchange, which may include additional requirements, restrictions and disclosure obligations, such as in relation to transactions with related parties.

Governmental and public bodies are often created by statute, so the relevant statute that created them will need to be considered and reviewed for any specific rules and restrictions applicable to them.

**Post-reorganisation steps**

24 | Do any filings or other post-reorganisation steps need to be taken after the corporate reorganisation takes place?

Post-reorganisation steps and filings often include:

- announcements (particularly relevant if one of the companies in the group is a listed company, subject to Listing Rules and DTRs);
- applications to HMRC for stamp duty relief or stamp duty land tax relief;
- registrations of the new proprietorship details in respect of Intellectual property assignments;
- notifications to landlords as required under lease terms;
- execution of novations and relevant notices of assignment to customers and suppliers;
- administrative matters, including documentation for insurance, PAYE, payroll, pensions and VAT;
- Companies House filings (eg, registration of security and notifications of changes to persons with significant control of an entity); and
- updating company books (in particular, the target).



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# Germany

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## LEGAL AND REGULATORY FRAMEWORK

### Types of transaction

1 What types of transactions are classified as 'corporate reorganisations' in your jurisdiction?

In general, the term 'corporate reorganisation' describes legal or economic measures to maintain or improve the organisation, financial status and situation of a corporate group, as well as the stability and economic efficiency of the corporate group's overall structure. Such measures include, in particular, the transfer of shares, individual assets or whole businesses between relevant group companies by way of, for example, internal transfers of shares or individual assets, or changes of the legal form, mergers or spin-offs within the corporate group.

Further reorganisational measures constituting a corporate reorganisation could be, for instance, changes to the funding or capitalisation of group companies, capital repayments to shareholders, as well as amendments of intra-group service or loan agreements.

### Rate of reorganisations

2 Has the number of corporate reorganisations in your jurisdiction increased or decreased this year compared with previous years? If so, why?

Demand for reorganisation-related legal advice in Germany appears to be relatively constant. Owing to a wide range of drivers for corporate reorganisations, the demand is to a certain extent independent from economic fluctuations. However, in recent years Germany has experienced high M&A activity that has been an important catalyst for corporate reorganisations. The main M&A-related factors for reorganisations are the preparation of a sale of certain group companies (or part of a company) or a business (unit) (ie, spin-off or carve-out transactions), and the integration of an acquired business into existing corporate structures. Other common drivers are:

- separation of liability risks;
- internal transfer of profits or losses (including for purposes of tax optimisation);
- disentanglement of large corporate groups in order to promote efficiency in relevant markets;
- prevention/limitation of employee co-determination in corporate group structures;
- improved efficiency of business operations or capital structure; and
- enablement of a refinancing or granting of securities.

While the aforementioned aspects may be relevant in the context of M&A transactions they may also apply independently as standalone drivers, in particular when it comes to regulatory arbitrage, improvements from an operational perspective or the disentanglement of overly complex corporate structures. Corporate reorganisation may also be considered somewhat countercyclical. In the event of low M&A activity or economic downturn corporate groups often decide to focus on internal structuring possibilities to improve operational efficiency or the overall capital structure.

Apart from these factors demand for corporate reorganisations may be driven by external one-off effects. A recent example of such external factor is the United Kingdom's vote to leave the European Union. The Brexit decision appears to have prompted an increase of corporate reorganisations in certain industries, in particular, financial services related reorganisational plans often consider Germany or other jurisdictions outside the UK as potential new locations for corporate groups' European headquarters.

### Jurisdiction-specific drivers

3 Are there any jurisdiction-specific drivers for undertaking a corporate reorganisation?

German corporate law provides for a limited number of corporate legal forms each having specific but sometimes limited possibilities for customisation. Therefore, specific advantages of certain legal forms may drive demand for corporate reorganisations. For example, limitations of German stock corporation law regarding corporate governance structure and, in particular, mandatory employee co-determination appear to be critical factors for German stock corporations to change their legal form into Societas Europaea (SE). The legal form of an SE provides for more leeway not only regarding the governance structure but also in terms of cross-border activities. In case of a cross-border merger in the process of the formation of the SE more lenient corporate governance rules can be transferred from one member state to the other. Further, in recent years the legal form of GmbH & Co. KGaA (essentially a partnership limited by shares), which allows single shareholders to keep control of the company without owning the majority stake, attracted family-owned businesses seeking access to capital markets.

### Structure

4 How are corporate reorganisations typically structured in your jurisdiction?

The specific structure of a corporate reorganisation depends on the circumstances of each individual case. Nevertheless, the following guidelines typically apply in relation to a corporate reorganisation. In general, the related proceedings can be divided into three stages: a planning and preparation phase, a negotiation phase and an implementation phase. For details on the planning and preparation phase, see question 7. In the course of the negotiation phase, in particular, the interests of the stakeholders need to be aligned. For example, employee-related issues may arise under certain circumstances, demanding mandatory involvement of employee representatives (see question 10). In the context of



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the implementation phase, reorganisational measures are implemented and, therefore, specific structural changes come into effect.

In this regard, several basic principles of German law need to be taken into consideration in connection with a corporate reorganisation. Transactions between group entities should generally be conducted at arm's length. Thus, services rendered should, in principle, be charged at the market rate and assets should generally not be transferred for less than their fair market value. Moreover, statutory and fiduciary duties are generally owed to every single group entity to which an individual has been appointed as representative; so the acting individuals cannot, in general, act to the sole detriment of one group entity. Exemptions can exist when limited liability companies (GmbHs) are involved, where the respective shareholders can issue comprehensive instructions to a GmbH's management, even if such instructions have negative consequences for that GmbH. It should be noted that if a domination agreement or profit and loss transfer agreement exists between the relevant group entities, the relevant controlling entity is entitled to issue instructions, even to the detriment of the controlled entity, and is, in case of profit and loss transfer agreements, entitled to direct a profit transfer, even when statutory capital maintenance rules are no longer complied with. In the absence of a domination agreement where a company can, however, still factually control a subsidiary (eg, because it holds the majority of voting rights in such entity), the relevant controlling entity generally cannot exert its influence to the detriment of the controlled entity without compensation. Whether a measure is detrimental mainly depends on whether a reasonable and diligent representative would have approved or conducted such measure.

Further, the articles of association (or similar) of the relevant group entities should be reviewed together with other material contracts and documentation with a view to potential restrictions or procedural requirements that could have an impact on the contemplated corporate reorganisation.

**Laws and regulations**

5 | What are the key laws and regulations to consider when undertaking a corporate reorganisation?

German law provides for a variety of different laws that are potentially relevant in relation to corporate reorganisations. For example, the primary legal framework relating to the organisation of partnerships is set out by the Commercial Code (HGB). The German Limited Liability Companies Act (GmbHG) contains relevant provisions in relation to GmbHs, whereas the Stock Corporation Act (AktG) sets the legal framework for stock corporations. The latter also comprises provisions on the organisation of holding structures that are typically of particular interest in the context of corporate reorganisations. The key regulatory framework in the event of transformations within corporate reorganisations is the Transformation Act (UmwG). The German Takeover Act (WpÜG) determines further regulations, and the European Market Abuse Regulation determines ad hoc disclosure requirements for public companies regarding inside information. Additionally, in particular, tax, labour and intellectual property law, as well as other pertinent fields of law, may apply on an individual basis.

**National authorities**

6 | What are the key national authorities to be conscious of when undertaking a corporate reorganisation?

Corporate reorganisations do not per se require any specific involvement of national authorities. Whether national authorities need to be involved mainly depends on the individual corporate reorganisation measure, the nature of the corporate group concerned and the business affected.

However, internal reorganisations typically have significant tax implications. Hence, in certain cases the involvement of tax authorities may be advisable. In addition, changes to the legal status may need to be registered with the competent commercial register in order to become effective, such as in the case of an intra-group merger that results in the transferring group company being dissolved and consequently de-registered from the commercial register. Further, transfers of real property between group companies need to be registered with the competent land register.

Other authorities may need to be involved if the corporate reorganisation relates to regulated industries. This, in particular, concerns companies that operate in the fields of financial services, pharmaceuticals, defence, infrastructure and energy. In this context, consultation with the relevant national authority at an early stage frequently plays an important role, in particular where a national authority's consent is required for the consummation of the contemplated corporate reorganisational measure or where misconduct could lead to substantial fines.

Corporate reorganisations involving companies listed on a regulated market in Germany may require filings with the Federal Financial Supervisory Authority (BaFin). In this regard, requirements set out in the German Takeover Act (WpÜG) may also be relevant.

## KEY ISSUES

**Preparation**

7 | What measures should be taken to best prepare for a corporate reorganisation?

Since an individual corporate reorganisation can have wide-ranging impacts, its implementation should be carefully considered and precisely planned. In addition to the indispensable legal analysis of the contemplated measure, tax experts, auditors or (national) authorities, if applicable (see question 6), need to be involved at an early stage in order to review the contemplated measures and provide advice thereto, where applicable. To best prepare a corporate reorganisation, it is recommended to clearly outline and determine its objective from the very beginning.

To secure the maximum support of the stakeholders affected, communication is one of the key factors for a successful corporate reorganisation. In particular, in relation to employees and a potential transfer of undertakings, resulting in the relevant employees ending up with another employing entity (see question 8), it is important to keep in mind that employees tend to react rather cautiously to structural changes due to concerns about job security. Therefore, it is often advisable to inform and involve affected employees at an early stage of the contemplated corporate reorganisation measure. The early involvement and information of business partners and other third parties may also help to avoid concerns about a potential deterioration of financial credibility or requests for provision of additional security, etc.

**Employment issues**

8 | What are the main issues relating to employees and employment contracts to consider in a corporate reorganisation?

Whether a corporate reorganisation has a significant impact from an employment law perspective mainly depends on whether the relevant measure shall be conducted by way of a sale of stock or an asset deal. No material issues occur in the case of share deals, as the employing entity remains the same. However, particular rules apply if a business or its parts are transferred to another entity by way of an asset deal. In the latter case, a transfer of undertakings may simultaneously occur.


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The rules on transfers of undertakings are governed by the Civil Code (BGB), which, in turn, resulted from the implementation of the former European Union Acquired Rights Directive (now the European Union Transfers of Undertakings Directive). In general, these rules apply where a business is being transferred to and continued by an acquirer. In this case, the employment relationships of respective employees are automatically transferred to the acquirer, which cannot refuse to take on transferring employees and related employee obligations. Employees who are assigned to the business will generally be entitled to transfer to the acquirer under the same terms and conditions of employment as those that previously existed with the previous employing entity. Changes to those employment conditions are legally restricted. A transfer of undertakings, furthermore, requires a notification of the employees who are entitled to object to the transfer of their employment relationship. In this case, the employment relationship of the objecting employee will not transfer to the acquirer but will continue with the previous employing entity (however, it would then likely be subject to termination for operational reasons by the previous employing entity due to the transfer of the relevant business). Although the acquirer enters into the employment relationships with all rights and duties, the previous employing entity is, together with the acquirer, generally jointly and severally liable with regard to those obligations that arise prior to the transfer date.

With regard to certain corporate reorganisations, the German Works Constitution Act (BetrVG) requires the involvement of employees by way of a co-determination process in the event a works council exists and certain operational changes, such as the closure of an entire plant or parts thereof, shall be undertaken. A works council is entitled to negotiate particular agreements like a reconciliation of interests or social plan.

### 9 What are the main issues relating to pensions and other benefits to consider in a corporate reorganisation?

Corporate reorganisations typically have no material impact on pensions or other benefits from a legal perspective. Nonetheless, any such benefits should be assessed with a view to the legal nature of the particular agreement they are based on (eg, collective bargaining agreements, works agreements or individual employment agreements, as well as the respective scope of application).

In the case of a transfer of undertakings, the employment relationships of the employees automatically transfer to the acquirer under the same terms and conditions of employment as those that previously existed (see question 8). This includes accrued benefits (eg, company pension, bonuses and anniversary bonuses). The acquirer has to establish provisions or otherwise sponsor such benefits (eg, by way of contribution to insurance contracts).

**Financial assistance**

### 10 Is financial assistance prohibited or restricted in your jurisdiction?

Under German law, the acquisition of own shares by a public or private company is generally restricted. Therefore, the provision of financial assistance to fund an acquisition of a company's own shares by a third party or a group company is restricted as well and, with regard to stock corporations, generally prohibited. The categories of legal acts that fall under the term 'financial assistance' is wide-ranging and rather broadly interpreted by German courts. It includes, for example, cash payments, the granting of loans or advances by a company and, in particular, the granting of security interests over the company's assets as collateral by way of, for example, share pledges over the shares of its subsidiaries and the pledging of its bank accounts or simple upstream guarantees.

German law only provides for explicit strict rules regarding financial assistance for stock corporations, whereas no explicit rules exist for GmbHs (other than in relation to capital contributions and maintenance). With regard to stock corporations, German law does not, in general, allow the provision of financial assistance to third parties for the acquisition of its own shares. However, there are certain exceptions for a limited number of purposes and circumstances (eg, in order to offer a stock corporation's shares to employees under bonus or incentive programmes). Further, intra-group transactions in relation to corporate reorganisations can be excluded from the prohibition to provide financial assistance in the case of existing controlling or profit and loss transfer agreements. Every transaction that violates the prohibition of financial assistance by a stock corporation is void, with the relevant stock corporation being entitled to claim restitution for the benefits provided to the relevant beneficiary; the persons involved, in particular executive board members, can potentially be personally liable or even face criminal liability.

With regard to GmbHs, financial assistance in the acquisition of own shares is generally permissible, but certain restrictions apply in connection with the rules on capital contributions and maintenance, the relevant provisions of which comprise extensive limitations. Financial assistance to fund the acquisition of shares of a company other than the assisting company itself is generally permitted but also subject to the aforementioned rules on capital contributions and maintenance.

**Common problems**

### 11 What are the most commonly overlooked issues or frequently asked questions in a corporate reorganisation?

The scope of frequently asked questions depends, in particular, on the nature of the relevant corporate reorganisation measure, the structure and size of the affected corporate group and its companies, the geographical location of the group companies and the overall purpose of the contemplated corporate reorganisation. For example, there are typically various questions in relation to employees in case of a contemplated asset transfer (see question 8) but also in relation to tax matters (see question 13).

Another difficult subject in the context of intra-group corporate reorganisations is that the underlying transactions should generally be conducted at arm's length. Hence, the valuation of assets or shares that are within the scope of the contemplated corporate reorganisation is a frequently asked question. If the main purpose of an intra-group transaction is the optimisation or even prevention of taxes, it is, for example, questionable whether assets or shares can be transferred within the relevant corporate group for less than their fair market value (see question 18).

Other frequently asked questions concern the involvement of national authorities and, in particular, the question of which authorities need to be involved – and if so, how such authorities should best be approached (see question 6). Also, it needs to be analysed whether relevant public permits exist and, if so, whether these automatically transfer or may need to be re-applied for. Further, it is often crucial to analyse whether a corporate reorganisation affects third-party agreements and whether third-party consent is required. It is, therefore, advisable to involve legal and other advisers at an early stage and to conduct comprehensive due diligence in relation to, for example, all relevant third-party arrangements.


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## ACCOUNTING AND TAX

### Accounting and valuation

**12 How will the corporate reorganisation be treated from an accounting perspective? How are target assets and businesses valued?**

Pursuant to the Commercial Code, with regard to a corporate group's consolidated annual accounts, the parent company and its subsidiaries are considered as one economic unit (principle of economic unity). Following this principle, corporate reorganisations can, in general, be structured as neutral from an accounting perspective.

However, under certain circumstances, an intra-group transfer of assets or shares may not be consummated at the actual net book value thereof, with the consequence that, due to a reappraisal, significant formerly hidden profits or losses could be released (acquisition cost method). In order to identify any hidden assets and choose wisely between different accounting methods, it is important to obtain accounting advice in relation to matters concerning the German Commercial Code or the International Financial Reporting Standards – which are applicable in case the parent company is listed – prior to implementing a corporate reorganisation.

### Tax issues

**13 What tax issues need to be considered? What are the tax implications of carrying out a corporate reorganisation?**

Potential tax implications should be carefully analysed prior to the implementation of any corporate reorganisation. In general, corporate reorganisations bear the risk that transfer taxes are triggered or hidden reserves are disclosed. Adverse tax effects cannot only be caused at the level of the group companies directly involved in the corporate re-organisation, but also at the shareholder level or at the level of another group company.

While there is no stamp duty in Germany, transfer taxes in the form of real estate transfer tax and value added tax (VAT) can be a cost factor. Corporate reorganisations can trigger real estate transfer taxes, in a worst-case scenario even more than once in one transaction. Depending on where the real property is located in Germany, the tax rate ranges from 3.5 per cent to 6.5 per cent of the value of the real property. It should be noted that corporate reorganisations outside of Germany might have adverse real estate transfer tax effects if German real property is held by the corporate group. Inter-group exemptions might be available in case the respective requirements are met. VAT in Germany (ie, German turnover tax) is levied on all payments for goods delivered and services rendered. Where corporate reorganisations include transfers subject to VAT, it might be recoverable as input VAT in some cases but might have to be accounted for as transaction costs in other cases, where the person or entity receiving goods or services does not qualify for the VAT deduction.

Profits or capital gains tax may potentially be triggered by certain measures in the course of a corporate reorganisation in the event no exemption applies. The possibility of a tax-neutral roll-over of book values is generally available under the Reorganisations Tax Act. If the respective requirements are met, the parties of a corporate reorganisation generally have the right to opt for a tax-neutral treatment (roll-over of book values) or a step-up in basis, which is generally subject to tax, but individual exemptions (eg, loss carry forwards) might be taken into consideration when making the decision. In order to ensure the economic success of corporate reorganisations in Germany, an overall assessment of potential tax consequences (German tax and non-German tax) is indispensable.

## CONSENT AND APPROVALS

### External consent and approvals

**14 What external consents and approvals will be required for the corporate reorganisation?**

Various third parties can have an interest in a corporate reorganisation, depending on, for example: the corporate group structure; the nature of the corporate reorganisation; the business type; and the existence of third-party rights in relation to certain assets of the involved group companies. For example, if public permits have to be reapplied for, the relevant authorities must be involved. Also, if the corporate reorganisation includes the (individual) assignment of contracts with third parties, the respective consent of the affected third parties has to be obtained.

Further, third-party consent and approval could, for example, be necessary where: (i) the involved group companies have third-party financing arrangements in place; (ii) contractual third-party approval rights, such as in relation to change-of-control scenarios, are part of the relevant contracts; or (iii) real property shall be transferred. In the event of transformations within corporate reorganisations, pursuant to the Transformation Act, third-party consent is typically not required, as the acquiring group company in this case becomes the universal legal successor of the transferring group company and, hence, the transfer does not qualify as transfer of individual assets, which would result in third parties being entitled to the aforementioned consent rights.

In other instances, however, no express consent may be required for a corporate reorganisation to become fully effective, but the group companies involved may, under certain circumstances, nevertheless be obliged to give notice to third parties before or after the respective measure is implemented.

With regard to corporate groups operating in regulated industries, certain consent or at least notification requirements may exist in relation to the relevant national authorities. In particular, in case a corporate group is active in a heavily regulated sector related to, for example, energy, telecommunications or financial services, it is advisable to analyse regulatory requirements in detail at an early stage, as a failure to comply with existing requirements could result in fines or even criminal liability of the persons involved.

### Internal consent and approvals

**15 What internal corporate consents and approvals will be required for the corporate reorganisation?**

As with many aspects of an individual corporate reorganisation, whether internal corporate consent and approvals are required depends on the individual nature of the specific corporate reorganisation.

For example, under certain circumstances, intra-group transactions concerning corporate reorganisations require approving shareholders' resolutions or even the approval of a (mandatory or optional) supervisory board or other supervising bodies. Each group company's management must independently consider differing facts and interests, and act with good intent in terms of the individual corporate benefit of the transactions proposed and the benefit of the corporate group as a whole. Exemptions can, in particular, exist in the case of GmbHs involved where the respective shareholders can issue comprehensive instructions to a GmbH's management, even if such instructions have negative consequences for that GmbH.



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## ASSETS

### Shared assets and services

**16 | How are shared assets and services used by the target company or business typically treated?**

In the planning phase, it is recommended to identify assets and services that are being shared by any group company affected by the relevant corporate reorganisation in order to assess any possible effects on the corporate reorganisation process.

Assets exclusively owned, as well as services exclusively rendered within a corporate group, typically do not result in specific challenges in light of a corporate reorganisation, unless the relevant measure serves the purpose of preparing for a future disposal of involved group companies.

However, business relationships between a group company and third parties can require a more complex legal analysis. For example, the underlying contractual relationship between said group company and a third party should be diligently reviewed in order to ensure that any affected services or assets can also be used by the relevant group company after consummation of the relevant corporate reorganisation. Should the relevant agreements at hand not comply with the existing legal framework of the corporate group, it may become necessary to negotiate a respective amendment of the agreement with the relevant third party beforehand.

### Transferring assets

**17 | Are there any restrictions on transferring assets to related companies?**

Transferring assets between related group companies is generally permitted and does not have any particular legal implications, in particular as long as the asset transfer within the corporate group is conducted at arm's length. Any such transfers do not result in any value added from one group company in favour of another group company. Restrictions may apply if group companies intend to transfer certain assets for less than the relevant fair market value (see question 18) and such transfers may therefore be treated as a profit distribution.

Other legal restrictions in the context of an intra-group asset transfer can apply in case the transferring group company violates capital maintenance provisions or does not comply with formal statutory requirements. This can be the case if, for example, real property or all of the assets of a group company are being transferred intra-group. Further, the relevant assets may, due to their use as collateral, be subject to pledges, etc, that may require the obtainment of the respective security holder's consent under the terms of the applicable finance or security documents prior to consummation of the relevant corporate reorganisation.

Another restriction can occur in the event of a data transfer between group companies. This, in particular, applies to cases where personal data shall be transferred. German data privacy law is very strict and can therefore limit or even prohibit the transfer of such data. Since the General Data Protection Regulation (GDPR) came into effect across the EU on 25 May 2018, the legal landscape for transferring and processing personal data has changed drastically. As a result, data protection standards have significantly increased in all member states. Such standards, in general, also apply to transferring data between related companies. However, the EU legislator identified the administrative necessity and practical relevance of transferring data between related companies – explicitly indicating in Recital 48 of the GDPR that related companies may have a legitimate interest in transmitting personal data within the group of companies which could simplify data proceedings within related companies. Data protection issues, therefore, must be carefully examined in the preparation of a corporate reorganisation.

**18 | Can assets be transferred for less than their market value?**

Assets can generally be transferred for less than their market value. However, restrictions may apply in the event that assets are transferred by a German stock corporation (Aktiengesellschaft). In general, an asset transfer without fair consideration is permitted if and to the extent the relevant group company has sufficient distributable profits. Should assets be transferred at a lower value than their net book value, the intended asset transfer is only admissible if the transferring group company has sufficient distributable profits in an amount constituting at least the delta between the actual consideration that shall be paid for the relevant assets and their net book value. The aforementioned scenario could otherwise result in a violation of statutory capital maintenance provisions, resulting in potential liability of the persons involved and repayment obligations. It should be noted that any such (indirect) distributions may potentially also result in a violation of third-party finance arrangements, particularly when the relevant assets are used as collateral. The transfer of assets for less than their market value can also have adverse tax effects, particularly when the actual transfer value is less than the net book value of the assets and, hence, the transaction could be deemed a constructive dividend.

## FORMALITIES

### Date of reorganisation

**19 | Can a corporate reorganisation be backdated or deemed to have already taken place, for example from the start of the financial year?**

As regards the effectiveness of a corporate reorganisation from a corporate law perspective, it is generally possible for the involved group companies to agree in the relevant documentation that the relevant measure shall have economic effect from an earlier date than the actual execution date. This, of course, only applies to the internal relationship between the involved group companies. Any relationships with third parties, consent requirements, etc, will not be affected thereby. Should a corporate reorganisation be given retroactive effect, it is necessary to consult with the relevant auditor to discuss any restrictions and limitations prior to the consummation of the corporate reorganisation.

The aforementioned should not be confused with the actual backdating of documents (ie, signing documents with an earlier date than the date on which the documents were executed). Under German law, the backdating of agreements may lead to invalidity of such agreements, liability of the involved group companies and individuals, and can even constitute criminal offences.

### Documentation

**20 | What documentation is required in a corporate reorganisation?**

The content of the required transaction documentation mainly depends on the scope and structure of the individual corporate reorganisation. For example, purely internal measures between already existing group companies usually require less documentation compared to measures with the purpose to, for example, integrate formerly external (ie, newly acquired) companies into an existing corporate group. Having comprehensive transaction documentation available may, of course, always be helpful to avoid legal disputes regarding the exact content and objective of the relevant corporate reorganisation. Also, by diligently executing comprehensive transaction documentation, the relevant group companies, as well as the respective individuals acting on their behalf, will be able to show that the concerned measure was implemented (eg, in compliance with the arm's-length principle).



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Typically, the transaction documentation in relation to a corporate reorganisation should comprise:

- an asset or share purchase agreement, or in the case of, for example, transformations pursuant to the Transformation Act (UmwG), the relevant inter-company agreement (eg, merger agreement);
- any relevant transfer documentation, of which its scope mainly depends on the assets transferred (eg, shares, real property, intellectual property);
- authorising documents, such as minutes of shareholders' resolutions, notices by national authorities, if applicable; and
- further documentation in relation to transitional services, intellectual property licences or employees, etc.

**Representations, warranties and indemnities**

21 | Should representations, warranties or indemnities be given by the parties in a corporate reorganisation?

Transaction documentation on corporate reorganisations typically does not provide for comprehensive contractual protection in this respect. In many instances, title warranties may be, more or less, the sole warranties provided. This may, under specific circumstances, be different in scenarios where the relevant corporate reorganisation measure is implemented as part of a pre-sale structuring process. The acquiring group company may be provided with more comprehensive contractual protection in relation to the transferring group company. This could be helpful if the acquiring group company has to seek recourse internally at a later stage after a consummated sale of the relevant assets to a third party that asserts certain claims in relation thereto. However, the aforementioned does not, in our experience, have any practical significance.

**Assets versus going concern**

22 | Does it make any difference whether assets or a business as a going concern are transferred?

The transfer of assets or a business as a going concern is, under certain conditions, outside the scope of VAT. Any other transfer of assets or a business not qualifying as a going concern would, in turn, be either subject to VAT or VAT-exempt. While the qualification of a transfer as a going concern provides for a simplification in the first place as the group of assets does not have to be individually classified as VAT-exempt or subject to VAT (including the assessment of tax base, tax rate, tax liability, etc), it should be noted that the qualification of a transfer of assets as a going concern generally triggers a secondary liability of the transferee for business taxes of the transferor. While certain limitations with respect to the kind of taxes, periods for which the secondary liability applies and time limitations for the assessment of taxes by competent tax authorities are to be considered, the underlying transaction documentation should generally address such secondary liability and how the parties intend to secure it.

**Type of entities**

23 | Explain any differences between public, private, government or non-profit entities to consider when undertaking a corporate reorganisation.

Corporate reorganisations involving public (ie, publicly listed) companies are typically subject to a more restrictive legal framework. One example in this respect is the prohibition of provision of financial assistance (see question 10). Further, in particular, the acquisition of shares in public companies is subject to the compliance with certain restrictive statutory requirements under the Securities Acquisition and Takeover Act and the Securities Trading Act. Another example in this regard is the mandatory compliance with the European Market Abuse Regulation, which, for example, stipulates ad hoc disclosure requirements for public companies in relation to inside information. Overall, a corporate reorganisation involving public companies is, in general, more complex, cost-intensive and challenging for the parties involved. The same will, in principle, apply to governmental and public companies as well, mainly due to specific regulations and restrictions applicable to such entities that, if applicable, have to be complied with in the course of a corporate reorganisation.

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**Post-reorganisation steps**

24 | Do any filings or other post-reorganisation steps need to be taken after the corporate reorganisation takes place?

The answer to this question depends, again, on the nature of the individual corporate reorganisation measure. For example, in the case of public companies, certain announcements to the Federal Financial Supervisory Authority may become necessary. Also, certain changes need to be registered with the competent commercial register in order to become effective (eg, a merger between group companies). In the case of a transfer of real property, respective filings will have to be made with the competent land register. Should a transfer of intellectual property have occurred, respective filings with the competent patent or trademark office may have to be made. Also relevant in this context may be the notification of affected business partners, such as customers, suppliers or other relevant third parties. Finally, all relevant company books and records may have to be updated accordingly to reflect the consummation of the corporate reorganisation.

## UPDATE AND TRENDS

**Current developments**

25 | What are your predictions for next year and how will these impact corporate reorganisations in your jurisdiction?

The UK's departure from the EU will likely have a particular impact on corporate groups and industries that are heavily influenced by EU regulation; for example, financial services businesses that may lose their passporting rights between the UK and the rest of the EU, which are vital to operate across the EU financial services market. However, as Brexit negotiations are ongoing the outcome is still uncertain.



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In order to absorb uncertainties regarding the legal status of private limited companies having their registered seat in the UK and business address in Germany, the German government has announced its forthcoming proposal for amendments to the German Transformation Act. This will allow companies affected by Brexit an orderly change to a German domestic legal form.



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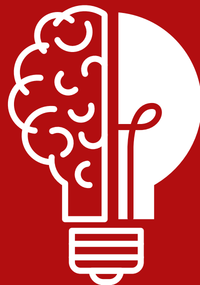

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