Family Firms and Closed Companies in Germany and Spain

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and GERALD SPINDLER

Max-Planck-Institut
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Excessive Retention of Profits and Minority Protection

A German Perspective

Jennifer Trinks

I. Introduction

Decisions on profit distribution can easily become a tantalizing matter in family firms. Not only is it difficult to develop an adequate dividend policy – paying shareholders their proverbial due while retaining sufficient funds to develop the business – the matter is made more complicated by the fact that majority shareholders can deliberately turn a corporation's dividend policy into an oppression strategy against minority shareholders.[1]

In many jurisdictions, the decision to distribute or retain a corporation's profits stands or falls on the votes of the majority shareholders[2]; majority

[1] This contribution is based on a previous comparative analysis of German and Spanish Law by *H. Fleischer/J. Trinks*, Minderheitenschutz bei der Gewinnthesaurierung in der GmbH, Ein deutsch-spanischer Rechtsvergleich, NZG 2015, 289.

[2] Critically on the majority shareholders' powers in Germany *K.-P. Martens*, Grundlagen und Entwicklung des Minderheitenschutzes in der GmbH, in: Lutter/Ulmer/Zöllner (eds.), Festschrift 100 Jahre GmbH-Gesetz (Cologne 1992) 607, 619 et seq. For the US see

shareholders can even decide the full retention of profits against the will of the minority. The majority can thus cut off the minority from any source of income from their corporation, leaving financial profits dangling in sight, but out of the minority's reach. Especially in family firms, where the corporation's payments constitute the main source of income for their shareholders, the retention of profits can thus threaten the financial subsistence of the minority and put them under substantial pressure.[3] German scholars have even coined the term starvation dividends[4] (*Hungerdividende*) for this phenomenon. At the same time, majority shareholders remain largely unaffected as they can secure their liquidity through other ways of profit extraction from the corporate firm, e.g. by granting themselves a generous salary or substantial payments for services provided.[5] In consequence, the retention of profits has become a wide-spread method to oppress or even to force out minority shareholders of close corporations.[6]

Like other jurisdictions, German law is struggling to rein in such behavior and to protect minority shareholders. The statutory and contractual framework for the distribution of a corporation's profits in German Limited Liability Corporations (*Gesellschaft mit beschränkter Haftung* – GmbH) underlines the difficulty of drafting clear-cut rules to prevent the excessive retention of profits (II.). Scholars and courts draw on the shareholders' *Treuepflicht*, the shareholders' fiduciary duty towards the corporation and each other, to police shareholder resolutions on the application of profits (III.). However, even where a shareholder resolution to retain profits has been found to violate the law, providing an adequate remedy may prove difficult (IV.). While the flexible approach under fiduciary duty thus allows for a reasonable standard of review of shareholder resolutions, it might be worth reconsidering the general

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the majority's influence via the board of directors, *D. K. Moll*, Shareholder Oppression & Dividend Policy in the Close Corporation, Wash. & Lee L. Rev. 60 (2003) 841, 862 et seq.

[3] Cf. *P. Hommelhoff*, Auszahlungsanspruch und Ergebnisverwendungsbeschluß in der GmbH, in: Pfeiffer/Wiese/Zimmermann (eds.), Festschrift für Heinz Rowedder zum 75. Geburtstag (Munich 1994) 171 et seq.

[4] For all *G. Bachmann/H. Eidenmüller/A. Engert/H. Fleischer/W. Schön*, Regulating the Closed Corporation (Berlin/Boston 2014) 39.

[5] See e.g. *P. Hommelhoff*, Gesellschaftsrechtliche Fragen im Entwurf eines Bilanzrichtlinie-Gesetzes. Bemerkungen zur Umsetzung der 4. EG-(Bilanz)-Richtlinie, BB 1981, 944, 952.

[6] See e.g. *Moll, supra* note 2, 841; for oppression strategies involving the earlier stages of preparation and approval of the corporation's annual accounts *R. Bork/K. Oepen*, Schutz des GmbH-Minderheitsgesellschafters vor der Mehrheit bei der Gewinnverteilung, ZGR 2002, 241, 282 et seq.; see also *M. B. Gutbrod*, Vom Gewinnbezugsrecht zum Gewinnanspruch des GmbH-Gesellschafters, GmbHR 1995, 551 et seq.; *S. Mock*, in: Heidinger/Leible/Schmidt (eds.), Michalski Kommentar zum GmbHG (3rd ed., Munich 2017) § 29 marg. no. 22 et seq.

principles for the application and distribution of profits which form the backdrop to these resolutions (V.).

II. Statutory and Contractual Framework for Profit Distribution

The German Limited Liability Corporations Act (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung* – GmbHG)[7] provides shareholders with ample leeway when it comes to deciding how to apply the corporation's profits (1.). Shareholders of a GmbH can generally decide the distribution or retention of profits with a simple majority of votes[8] unless the corporation's articles of association provide otherwise, and indeed, shareholders seem to rarely contract for different or more specified rules on profit distribution (2.).

1. A Self-Effacing Legislative Compromise

Current German law leaves the decision on how to use a corporations' profits largely to its shareholders. While the right to participate in the corporation's gains constitutes one of the main shareholder rights[9], it requires a shareholder resolution to materialize. Only once the shareholder meeting has decided to distribute profits do shareholders have a valid and enforceable claim for payment of a dividend from the corporation.[10]

The GmbHG holds few limitations on the shareholders' decision-making power. It limits distributable profit to the amount of the annual surplus plus any profit carried forward and minus any losses carried forward, or respectively to the net earnings according to the corporation's balance sheet, and excludes sums required to be retained by statute or the corporation's articles of association.[11] Beyond these constraints, shareholders are free to decide the retention of profits or to carry them forward, as § 29 para. 2 GmbHG express-

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[7] *Gesetz betreffend die Gesellschaften mit beschränkter Haftung in der im Bundesgesetzblatt Teil III, Gliederungsnummer 4123-1, veröffentlichten bereinigten Fassung, das zuletzt durch Artikel 10 des Gesetzes vom 17. Juli 2017 (BGBl. I S. 2446) geändert worden ist.*

[8] For statutory limits on the distribution of dividends see e.g. §§ 30 para. 1 sent. 1, 58d GmbHG, §§ 253 para. 6 sent. 2, 268 para. 8 German Commercial Code (*Handelsgesetzbuch* – HGB), further *L. Leuschner*, in Habersack/Casper/Löbbe (eds.), Gesetz betreffend die Gesellschaften mit beschränkter Haftung. Großkommentar. Vol. II (3rd ed., Tübingen 2020) § 29 marg. no. 91 et seq.

[9] See also *W. Zöllner*, Die sogenannten Gesellschafterklagen im Kapitalgesellschaftsrecht, ZGR 1988, 393, 418.

[10] On the differentiation between an enforceable claim for payment of a dividend (*Gewinnanspruch*) and the general shareholder right to participate in the corporation's profits (*Gewinnstammrecht*) see e.g. *Leuschner, supra* note 8, § 29 marg. no. 5; *D. A. Verse*, Scholz Kommentar zum GmbH-Gesetz, Vol. I (12th ed., Cologne 2018) § 29 marg. no. 9.

[11] See § 29 para. 1 GmbHG.

ly states. Furthermore, in the absence of a specific majority requirement, the decision to retain or distribute the corporation's profits can be taken with a simple majority of the votes cast in accordance with general rules.[12]

However, this authority was only put into shareholders' hands in 1986.[13] In its original version, § 29 GmbHG contained an imperative to fully pass on the distributable profits to shareholders (so-called *Vollausschüttungsgebot*), which could only be derogated by a provision in the corporation's articles of association.[14] Early on, this rule has attracted reform proposals. Already the 1939 draft bill for a new GmbHG recommended allowing shareholders to retain profits and build reserves through a simple majority resolution.[15] The proposed reform bills of 1971[16] and 1973[17] included similar provisions. However, as both attempts at comprehensive reform of the GmbHG failed, the decision on profit distribution only became the prerogative of a simple majority of shareholders with the Accounting Directives Act of 1985 (*Bilanzrichtlinien-Gesetz* – BiRiLiG)[18] which entered into force on 1 January 1986. New and stricter rules on accounting had made it necessary to grant more flexibility in the application of profits to allow for the regular adjustment of the cor-

[12] See § 47 para. 1 and 2 GmbHG.

[13] For an overview of the norm's history see *V. Emmerich*, Fortschritt oder Rückschritt? Zur Änderung des § 29 GmbHG durch das Bilanzrichtlinien-Gesetz von 1985, in: Bärmann/Weitnauer (eds.), Festschrift für Hanns Seuss zum 60. Geburtstag (Munich 1987) 137, 138 et seq.; also *Verse, supra* note 10, § 29 marg. no. 3 ff. In detail on the previous legal situation *M. Winter*, Mitgliedschaftliche Treuebindungen im GmbH-Recht (Munich 1988) 276 et seq.

[14] Cf. § 29 sent. 1 GmbHG 1892: "Die Gesellschafter haben Anspruch auf den nach der jährlichen Bilanz sich ergebenden Reingewinn, soweit nicht im Gesellschaftsvertrage ein Anderes bestimmt ist." Pointing to the then available leeway used in establishing the financial statements *D. Joost*, Beständigkeit und Wandel im Recht der Gewinnverwendung, in: Lutter/Ulmer/Zöllner (eds.), Festschrift 100 Jahre GmbH-Gesetz (Cologne 1992) 289, 292 et seq.

[15] See §§ 87 para. 2, 89 paras. 6, 7 Draft of the Ministry of Justice of the Reich for a GmbHG 1939, reproduced at W. Schubert (ed.), Entwurf des Reichsjustizministeriums zu einem Gesetz über Gesellschaften mit beschränkter Haftung von 1939 (Heidelberg 1985) 118 et seq., 160 et seq.

[16] See § 45 Government draft for a reformed GmbHG 1971 (*Entwurf eines Gesetzes über Gesellschaften mit beschränkter Haftung [GmbHG]*), 31 January 1971, BT-Drs. VI/3088, 14.

[17] See § 45 Government draft for a reformed GmbHG 1973 (*Entwurf eines Gesetzes über Gesellschaften mit beschränkter Haftung [GmbHG]*), 26 February 1973, BT-Drs. 7/253, 14.

[18] *Gesetz zur Durchführung der Vierten, Siebenten und Achten Richtlinie des Rates der Europäischen Gemeinschaften zur Koordinierung des Gesellschaftsrechts (Bilanzrichtlinien-Gesetz* – BiRiLiG*)*, 19 December 1985, BGBl. I S. 2355.

poration's financing policy to evolving business needs.[19] In consequence, the principle of full distribution of profits was replaced by the (majority) shareholders' power to decide the full or partial retention of profits.

This decision-making authority was never intended to go unrestricted. All reform proposals up to the Government draft for the BiRiLiG counterbalanced the shift from full distribution of profits to a distribution according to the shareholder majority's decision with the possibility of pushing for a minimum dividend.[20] On the model of § 254 German Stock Corporation Act (*Aktiengesetz* – AktG)[21], shareholders were intended to be given the right to claim annulment of a shareholder resolution on the retention of profits when, firstly, from the perspective of a reasonable business person, this retention of profits was not necessary to secure the viability and resilience of the corporation for the foreseeable future given its economic and financial needs, and, secondly, the shareholder resolution does not arrange for the distribution of profits in the amount of at least 4% of the share capital minus shareholder contributions which have not been called.[22] As the annulment of a resolution requires proof of both conditions, this provision ultimately grants a *de facto* right to a minimum dividend. However, with 4% of the share capital, the amount of this minimum dividend probably would not satisfy the expectations and needs of shareholders. While this has already been criticized with regard to § 254 AktG[23], it holds even more true in close corporations, especially the GmbH, whose share capital typically lies far below the share capital

[19] See the justification given in the Government draft for the Accounting Directives Act (*Entwurf eines Gesetzes zur Durchführung der Vierten Richtlinie des Rates der Europäischen Gemeinschaften zur Koordinierung des Gesellschaftsrechts [Bilanzrichtlinie-Gesetz]*), 26 August 1983, BT-Drs. 10/317, 109.

[20] Cf. § 130 para. 3 Draft of the Ministry of Justice of the Reich for a GmbHG 1939, *supra* note 15, 131, 160 et seq.; § 205 GmbHG as proposed by the Government draft for a reformed GmbHG 1971, BT-Drs. VI/3088, 57; § 205 GmbHG as proposed by the Government draft for a reformed GmbHG 1973, BT-Drs. 7/253, 57.

[21] *Aktiengesetz vom 6. September 1965 (BGBl. I S. 1089), das zuletzt durch Artikel 1 des Gesetzes vom 12. Dezember 2019 (BGBl. I S. 2637) geändert worden ist.*

[22] See § 42h GmbHG as proposed by the Government draft for the BiRiLiG, BT-Drs. 10/317, 39: "Der Beschluß über die Verwendung des Ergebnisses kann unbeschadet anderer Anfechtungsgründe angefochten werden, wenn die Gesellschafter aus dem Jahresüberschuß Beträge in Gewinnrücklagen oder in einen Gewinnvortrag einstellen, die nicht nach Gesetz oder Gesellschaftsvertrag von der Verteilung unter die Gesellschafter ausgeschlossen sind, obwohl die Einstellung bei vernünftiger kaufmännischer Beurteilung nicht notwendig ist, um die Lebens- und Widerstandsfähigkeit der Gesellschaft für einen hinsichtlich der wirtschaftlichen und finanziellen Notwendigkeiten übersehbaren Zeitraum zu sichern, und dadurch unter die Gesellschafter kein Gewinn in Höhe von mindestens vier vom Hundert des um noch nicht eingeforderte Einlagen verminderten gezeichneten Kapitals verteilt werden kann."

[23] *E. Stilz*, in: Spindler/Stilz (eds.), Kommentar zum Aktiengesetz, Vol. 2 (4th ed., Munich 2019) § 254 marg. no. 2: "Effektivität der Vorschrift ist zweifelhaft".

of publicly traded corporations and whose shareholders largely rely on the stream of income from the corporation.[24] Promising little relief, this particular ground for annulment has consequently been left out of the GmbHG.[25]

The lack of a statutory limit to the shareholders' decision-making authority does however not mean that majority shareholders are completely free to decide the retention of profits. The legislative abstention from posing fixed thresholds is instead understood to delegate the matter to scholars and courts in order for them to develop a flexible solution.[26] This solution has been provided with the shareholders' *Treuepflicht*: Measuring a shareholder resolution to retain profits against the *Treuepflicht* indeed offers a soft standard which allows for the annulment of a resolution even where a dividend exceeding the 4% threshold is paid to shareholders.

In this vein, the legislative reticence to fix a uniform quantum for the distribution of profits might be interpreted as an acknowledgment that no single ratio between retention and distribution of profits can adequately satisfy the needs of all corporations, allowing them to flourish in the most diverse fields of operation and under all range of circumstances, not even as a mere default rule.[27] The lawmakers rejecting a one-size-fits-all-solution means there is also no room for the analogous application of § 254 AktG in a GmbH.[28] Further-

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[24] *Hommelhoff, supra* note 5, 952: "ridiküle 4%"; *L. Vollmer*, Mehrheitskompetenzen und Minderheitenschutz bei der Gewinnverwendung nach künftigem GmbH-Recht, DB 1983, 93, 94; specifically with regard to close corporations *C. Einhaus/W. Selter*, Die Treuepflicht des GmbH-Gesellschafters zwischen Ausschüttungs- und Thesaurierungsinteresse, GmbHR 2016, 1177, 1181; see further *Winter, supra* note 13, 291 et seq. on the constraints such a provision would have entailed.

[25] See Recommendation and report of the Legal Affairs Committee, BT-Drs. 10/4268, 131: "§ 42 h GmbHG-E wird aus ordnungspolitischen Gründen nicht übernommen. Ein bestimmter Gewinnanspruch der Minderheitsgesellschafter soll im Gesetz nicht ausdrücklich festgeschrieben werden."

[26] *P. Hommelhoff*, Die Ergebnisverwendung in der GmbH nach dem Bilanzrichtliniengesetz, ZGR 1986, 418, 424; *Verse, supra* note 10, § 29 marg. no. 7.

[27] *R. Liebs*, Die Anpassung des Gesellschaftsvertrags der GmbH an das Bilanzrichtlinien-Gesetz, DB 1986, 2421; generally on the difficulty of drafting a one-size-fits-all solution *Hommelhoff, supra* note 5, 953, proposing to adopt a statutory mandate for shareholders to agree upon a contractual rule on the matter of profit distribution.

[28] *M. Ehlke*, Ergebnisverwendungsregelungen in der GmbH nach dem BiRiLiG, DB 1987, 671, 677; *Einhaus/Selter, supra* note 24, 1181. For an analogous application of § 254 para. 1 AktG at least for non-personalistic GmbHs see *G. Hueck*, Minderheitsschutz bei der Ergebnisverwendung in der GmbH, Zur Neuregelung des § 29 GmbHG durch das Bilanzrichtlinien-Gesetz, in: Baur/Hopt/Mailänder (eds.), Festschrift für Ernst Steindorff zum 70. Geburtstag am 13. März 1990 (Berlin/New York 1990) 45, 56; also *C. Kersting*, in: Baumbach/Hueck Gesetz betreffend die Gesellschaften mit beschränkter Haftung (22nd ed., Munich 2019) § 29 marg. no. 31; critically *J. Ekkenga*, in: Fleischer/Goette (eds.), Münchener Kommentar zum GmbH-Gesetz, Vol. I (3rd ed., Munich 2018) § 29 marg. no. 166.

more, the legislative refusal to set a certain number as the minimum distribution requirement cautions against the application of other fixed thresholds. A proposal by an eminent author to allow for the retention of 60% of a corporation's profits up to the amount of its share capital, exempting resolutions within these boundaries from any material scrutiny would very well have improved the predictability and clarity of the law.[29] Nonetheless, it lies at odds with the legislative desire for a flexible and case-specific solution. Finding an adequate ratio poses additional difficulties, which would have been made even greater with the methodical justification of such a number which has no basis in the GmbHG or in established legal principles.[30] As long as the legislator does not step in[31], it thus seems measuring shareholder resolutions for the retention of profits against a clear-cut rule was impossible.

Of course, § 29 para. 1 sent. 1 GmbHG has opened the floor to shareholders themselves: in the articles of association, they can mandate the full or partial retention of profits by fixing a dividend policy and pre-forming the corporation's financial planning. Practice has shown, however, that only few shareholders have made use of this opportunity.

2. Lack of Contractual Specification

The shareholder meeting can only decide the retention or distribution of profits within the boundaries traced by statute, or by the articles of association. While the GmbHG generally allows for a full retention of profits, shareholders can dictate a different framework in the corporation's articles of association.[32]

Establishing a dividend policy in the articles of association allows the shaping of shareholders' expectations and can circumvent later disagreement. Particularly in light of the importance of profit distribution, commentaries and manuals regularly recommend including a provision in the founding document of a GmbH, to specify how the corporation's profits will be used.[33]

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[29] *Hommelhoff, supra* note 26, 427 et seq., with an additional absolute threshold for the retention of profits; also *P. Hommelhoff*, Lutter/Hommelhoff GmbH-Gesetz Kommentar (20th ed., Cologne 2020) § 29 marg. no. 25: "lediglich pauschalierende Richtwerte".

[30] *Ekkenga, supra* note 28, § 29 marg. no. 166; *Joost, supra* note 14, 302; *Kersting, supra* note 28, § 29 marg. no. 31; *K. Schmidt*, Scholz Kommentar zum GmbH-Gesetz, Vol. II (11th ed., Cologne 2014) § 46 marg. no. 31; also *Ehlke, supra* note 28, 678; *Liebs, supra* note 27, 2421; pointing further to the limited informational value of a GmbH's legal capital for predicting its actual financial needs *Leuschner, supra* note 8, § 29 marg. no. 131.

[31] Cautioning however against a uniform statutory distribution quota *H. Fleischer*, Excessive Retention of Profits and Minority Protection: Comparing German and French Law of Close Corporations, RTDF 3-2015, 56, 59.

[32] As to specific requirements for introducing such a provision see *Ekkenga, supra* note 28, § 29 marg. no. 175 et seq.; *Kersting, supra* note 28, § 29 marg. no. 37.

[33] *Ekkenga, supra* note 28, § 29 marg. no. 169; *Hommelhoff, supra* note 29, § 29 marg. no. 26; *Kersting, supra* note 28, § 29 marg. no. 34; *Verse, supra* note 10, § 29 marg. no. 7;

Even the Governance Code for Family Businesses, a collection of guidelines for the development of an adequate governance structure for family-owned enterprises put forward by a private initiative of associations of family firms and academics, advocates for "a reliable framework for all stakeholders" and recommends "that basic principles governing the allocation of earnings be incorporated within the articles of association".[34] More specifically, authors propose fixing a minimum retention or distribution quota, or establishing qualified majority requirements for shareholders decisions on the retention of profits, or delegating the decision-making authority to other bodies like a supervisory board or a shareholder committee. These various tools can of course be combined.[35]

However, such provisions appear to be used only rarely in practice.[36] A recent study has looked at the articles of association of 200 GmbHs with two or more shareholders and found that only four percent of these articles of association actually contained some form of distribution clause.[37] This reticence to contractually cover the question should not even be surprising: Usually, in the founding phase of the company, shareholders have little inclination to imagine future contention; with the typical dose of over-optimism, they might even think that the corporate project will continue running as smoothly as the founding process may have done. Additionally, shareholders might refrain from discussing the sensitive topic of profit distribution and financing policy with their fellow shareholders in an early phase when the problem seems abstract and far away. The anticipation of future conflict risks undermining

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further *M. Heusel/M. Goette*, Zum Gewinnausschüttungsanspruch bei Pattsituationen in der GmbH, GmbHR 2017, 385, 386 et seq.; *Hueck, supra* note 28, 47; *Ehlke, supra* note 28, 675 et seq.; even *Martens, supra* note 2, 621, holding the lack of a contractual provision to be a "kautelarjuristische[r] Kunstfehler"; comp. further *P. Hommelhoff/U. Hartmann/K. Hillers*, Satzungsklauseln zur Ergebnisverwendung in der GmbH, DNotZ 1986, 323, 326 et seq.

[34] P. May et al. (eds.), Governance Code for Family Businesses, 2015, 5.2.4. (p. 27), <http://www.kodex-fuer-familienunternehmen.de/images/Downloads/Kodex_englisch_2015.pdf>.

[35] For an overview *C. H. Seibt*, in: Römermann (ed.), Münchener Anwaltshandbuch GmbH-Recht (4th ed., Munich 2018) § 2 marg. no. 411; see already the examples of *Ehlke, supra* note 28, 676 et seq.; *Hommelhoff/Hartmann/Hillers, supra* note 33, 327 et seq.; *Liebs, supra* note 27, 2424 et seq.; also *Kersting, supra* note 28, § 29 marg. no. 35.

[36] Differently *Kersting, supra* note 28, § 29 marg. no. 35: "weit verbreitet"; also *H. Heckschen*, in: Heckschen/Heidinger (eds.), Die GmbH in der Gestaltungs- und Beratungspraxis (4th ed., Cologne 2018) Chapter 4 marg. no. 373.

[37] *F. Wedemann*, Gesellschafterkonflikte in geschlossenen Kapitalgesellschaften (Tübingen 2013) 212, 214, 215; cf. for the scarcity of contractual conflict-resolution mechanisms in the articles of association of close corporations with two shareholders with equal rights *J. Lieder/T. Hoffmann*, Die paritätische Zweipersonen-GmbH. Rechtstatsachen und Satzungsanalyse, GmbHR 2017, 1233, 1240 et seq.

confidence before the common project has even taken off and might endanger a frictionless conclusion of the founding process.[38] Finally, the reticence to negotiate a provision on the distribution of future profits might even be rational considering the difficulty of finding the perfect provision. Drafting a precise and clear-cut rule which is at the same time flexible enough to serve the company in different stages of its development and evolving economic contexts, is a herculean task.[39] This shows in the lack of a statutory specification; one might further see the impossibility of drafting the ideal rule reflected in corporate law manuals highlighting the need to tailor an adequate rule on the distribution and retention of profits to the particular corporation concerned[40] – thus delegating the task of finding the perfect custom-made rule to the individual lawyer when such a perfect rule might not even exist.

Finally, case law illustrates the difficulty of formulating a clause that effectively prevents disputes: A significant number of disputes over the distribution of profits brought before German courts make reference to a contractual provision in the corporation's articles of association.[41] In a case decided by the Higher Regional Court Hamm in 1991, the corporation's articles of association included a clause that ordered the distribution of at least 25% of the profits; it continued: "75% of the profits shall accrue to the shares of the shareholders if necessary. The decision is made by the shareholders' meeting."[42] Leaving the decision on the distribution of the remaining 75% of the profits to the shareholders' meeting left ample room for conflict. When the majority one year decided to distribute only 35% while retaining 65% of the profits, the minority challenged this decision and the parties ended up in court.

In view of these factors, it has to be considered that disputes over the fair application of profits can hardly be prevented *ex ante*. Hence, a fair and clear *ex post* solution becomes all the more important. German courts seek equitable solutions in the application of the flexible standard provided by the shareholders' *Treuepflicht*.

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[38] *Bachmann/Eidenmüller et al.*, *supra* note 4, 47 et seq. with further references.

[39] Cf. *Vollmer, supra* note 24, 95; on the difficulties of finding an adequate rule also *Fleischer/Trinks, supra* note 1, 296; see also *B. Grunewald*, in: K. Schmidt (ed.), Münchener Kommentar zum Handelsgesetzbuch, Vol. 3 (4th ed., Munich 2019) § 167 marg. no. 5 for the German Partly Limited Partnership (*Kommanditgesellschaft* – KG).

[40] See e.g. *T. Haasen*, Satzung einer kleineren, mehrgliedrigen GmbH, in: Lorz/Pfister/Gerber (eds.), Beck'sches Formularbuch GmbH-Recht (Munich 2010) C.I.2., § 8 para. 3; *Heckschen, supra* note 36, Chapter 4 marg. no. 373 et seq., Chapter 7 marg. no. 28 et seq.; for family firms *O. Habighorst*, A.V.21. Gesellschaftsvertrag einer Familiengesellschaft, in: Meyer-Landrut (ed.), Formular Kommentar GmbH-Recht (4th ed., Cologne 2019) § 24 and marg. no. 469 et seq.

[41] See e.g. OLG Koblenz, 1 February 2018, 6 U 442/17, GmbHR 2018, 1016.

[42] OLG Hamm, 3 July 1991, 8 U 11/91, GmbHR 1992, 458.

III. The Shareholders' *Treuepflicht* and Its Application

The *Treuepflicht* has become a well-established part of German corporation law.[43] It obliges directors to act in the sole interest of the corporation, and it binds shareholders to the interest of their corporation on the one hand, as well as to the interest of their fellow shareholders on the other. It thus also guides shareholders in their decision on how to use the corporation's profits.[44] Generally, the shareholders' *Treuepflicht* provides a flexible standard for policing shareholder behavior (1.). In the context of the decision to distribute or retain profits, it specifically requires shareholders to balance the corporation's self-financing interests against their and their fellow shareholders' interest in receiving payment of a dividend (2.). Scholars and courts however acknowledge that a corporation's financing strategy is a business decision, and they consequently make sure to respect the shareholders' business judgment (3.).

1. The Shareholders' Treuepflicht as a General Clause

Shareholders' rights in the corporation are generally self-interested rights, i.e. shareholders may exercise their rights in a way to foster primarily their own interests. However, when founding or entering a corporation, shareholders commit themselves to a common endeavor, and they may not counteract this commitment by hurting the corporation or their fellow shareholders. Scholars and courts thus see the shareholders under a specific duty of loyalty, a *Treuepflicht*, vis-à-vis the corporation on the one hand, and vis-à-vis their fellow shareholders on the other.[45]

The exact foundation of the shareholders' *Treuepflicht* is still subject to discussion. Some authors reference the statutory obligation to promote the achievement of a common purpose (see § 705 German Civil Code, *Bürgerli-*

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[43] See *M. Hippeli*, Treuepflichten in der GmbH. Aktuelle Entwicklungen in der Rechtsprechung, GmbHR 2016, 1257: "Die seit etwas über 100 Jahren angenommene gesellschaftsrechtliche Treuepflicht ist ein Chamäleon: Nur manchmal sichtbar, äußerst wendig und mit einer Vielzahl an Facetten."

[44] For an application of the *Treuepflicht* to the general partner of a KG who has been declared competent to decide the distribution or retention of profits by the partnership agreement see OLG Stuttgart, 13 June 2007, 14 U 19/06, DB 2007, 2587, 2589.

[45] BGH, 5 June 1975, II ZR 23/74, BGHZ 65, 15, 18 et seq. (*ITT*); BGH, 20 March 1995, II ZR 205/94, BGHZ 129, 136, 142 et seq.(*Girmes*); *W. Bayer*, Lutter/Hommelhoff GmbH-Gesetz Kommentar (20th ed., Cologne 2020) § 14 marg. no. 30; *L. Fastrich*, in: Baumbach/Hueck Gesetz betreffend die Gesellschaften mit beschränkter Haftung (22nd ed., Munich 2019) § 13 marg. no. 21; for a comprehensive summary in English see *J. Lieder*, The Duty of Loyalty in German Company Law, RTDF 3-2014, 33, 37 et seq.; in a comparative perspective *Bachmann/Eidenmüller et al.*, *supra* note 4, 53 et seq.

ches Gesetzbuch – BGB)[46],[47] others see the *Treuepflicht* implied in the position as a shareholder and the rights this position carries[48], or scholars simply point to the *bona fide* principle applicable to all private law relationships as laid down in § 242 BGB[49]. Almost consensually, though, it is admitted that the shareholders' *Treuepflicht*, in its consequences, goes beyond this mere general principle of good faith.[50]

The shareholders' *Treuepflicht* has come to apply to all forms of collective business organizations, from small partnerships to large corporations. In 1988, the German Federal Court (*Bundesgerichtshof* – BGH) explicitly confirmed the existence of a *Treuepflicht* between shareholders of a stock corporation.[51] The intensity of such a duty of loyalty does vary with the degree of confidence between shareholders, confidence on which the corporate firm is built. Where the personal ties between shareholders are strongest, e.g. in a partnership or a closely-knit, family-owned corporation, the standard to which shareholders are held is higher than in large stock corporations where the *intuitus personae* between shareholders is weak. The limitations and obligations drawn from the shareholders' *Treuepflicht* have thus to be adapted to the factual organizational structure of the corporation.[52] Specific manifestations of the *Treuepflicht* then result from a thorough balancing of interests between the parties concerned, which includes not only the shareholders of the corporation, but also the corporation as a business entity itself.[53]

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[46] *Bürgerliches Gesetzbuch in der Fassung der Bekanntmachung vom 2. Januar 2002 (BGBl. I S. 42, 2909; 2003 I S. 738), das zuletzt durch Artikel 1 des Gesetzes vom 12. Juni 2020 (BGBl. I S. 1245) geändert worden ist.*

[47] E.g. *M. Lutter*, Theorie der Mitgliedschaft. Prolegomena zu einem Allgemeinen Teil des Korporationsrechts, AcP 180 (1980), 84, 102 et seq.; also *H. C. Grigoleit*, in: Grigoleit (ed.), Aktiengesetz Kommentar (2nd ed., Munich 2020) § 1 marg. no. 51.

[48] Cf. *G. Bitter*, Scholz Kommentar zum GmbH-Gesetz, Vol. I (12th ed., Cologne 2018) § 13 marg. no. 54: "aus der vertraglichen Bindung der Gesellschafter"; *C. H. Seibt*, Scholz Kommentar zum GmbH-Gesetz, Vol. I (12th ed., Cologne 2018) § 14 marg. no. 71; limiting the *Treuepflicht*'s scope *H. Altmeppen*, in: Roth/Altmeppen Gesetz betreffend die Gesellschaften mit beschränkter Haftung (9th ed., Munich 2019) § 13 marg. no. 30.

[49] *J. Hennrichs*, Treupflichten im Aktienrecht. Zugleich Überlegungen zur Konkretisierung der Generalklausel des § 242 BGB sowie zur Eigenhaftung des Stimmrechtsvertreters, AcP 195 (1995), 221, 229 et seq. For an general overview see also *H. Fleischer*, in: Schmidt/Lutter (eds.), Aktiengesetz Kommentar (4th ed., Cologne 2020) § 53a marg. no. 45.

[50] *Fastrich, supra* note 45, § 13 marg. no. 20; *Seibt, supra* note 48, § 14 marg. no. 71; especially with regard to the shareholders' decision to distribute or retain profits see *Einhaus/Selter, supra* note 24, 1180.

[51] BGH, 1 February 1988, II ZR 75/87, BGHZ 103, 184, 194 et seq. (*Linotype*); see BGH, 20 March 1995, *supra* note 45, 143 on the minority shareholders' *Treuepflicht*.

[52] *Bitter, supra* note 48, § 13 marg. no. 51; *Fastrich, supra* note 45, § 13 marg. no. 22.

[53] *Altmeppen, supra* note 48, § 13 marg. no. 31; *Fastrich, supra* note, § 13 marg. no. 23; also *Lieder, supra* note 45, 38, see further 39: "a collective term and a blanket clause".

Case law and scholarship have tried to organize the different manifestations into categories of typical factual constellations such as the duty to not harm the corporation or its shareholders or to participate in certain essential corporate acts.[54] Prominent amongst these categories is the protection of minority shareholders against the excessive retention of profits.

2. Balancing the Corporation's Self-Financing Interest against the Shareholders' Dividend Interest

The shareholders' *Treuepflicht* allows for the material review of shareholder resolutions as to their actual content.[55] This review usually requires a balancing exercise: courts need to examine whether shareholders, in making their decisions, have adequately respected the interest of the corporation on the one hand, and the interest of their fellow shareholders on the other hand. With regard to protection against excessive profit retention, applying the shareholders' *Treuepflicht* thus asks us to weigh up the corporation's need to retain funds for business and financing purposes against the individual shareholders' interest of receiving payment of a dividend.[56]

While this standard has found wide-spread acceptance in scholarship and is commonly applied by the courts, some authors propose different solutions. Given the lack of a statutory foundation, only few scholars advocate for fixed limits to the shareholders' authority to decide the retention of profits.[57] Legal clarity and predictability are instead sought by rewriting the standard against which shareholder resolutions are measured and limiting judicial review to sanction only the abuse of shareholder rights.[58] This approach promises to also prevent courts from impinging on or overtaking the shareholders' decision-making prerogative when it comes to the distribution or retention of profits.[59] With regard to its outcomes, case law also points towards mainly sanctioning abusive shareholder resolutions; one court has even explicitly

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[54] See the different categories listed by *Seibt, supra* note 48, § 14 marg. no. 89 et seq.; also see also *Hippeli, supra* note 43, 1258; *Lieder, supra* note 45, 39 ff; across the board *Fastrich, supra* note 45, § 13 marg. no. 21: "nur beschreibend, nicht abschließend".

[55] *Ekkenga, supra* note 28, § 29 marg. no. 167: "Angemessenheitskontrolle".

[56] BGH, 29 March 1996, II ZR 263/94, BGHZ 132, 263, 276; see also OLG Koblenz, 1 February 2018, *supra* note 41, 1018; OLG Nuremberg, 9 July 2008, 12 U 690/07, DB 2008, 2415, 2417; OLG Hamm, 3 July 1991, *supra* note 42, 459; further *Ekkenga, supra* note 28, § 29 marg. no. 169; *Hueck, supra* note 28, 57; *Kersting, supra* note 28, § 29 marg. no. 32; also *J. Schulze-Osterloh*, Aufstellung und Feststellung des handelsrechtlichen Jahresabschlusses der Kommanditgesellschaft. Zuständigkeit und gerichtliche Durchsetzung, BB 1995, 2519, 2522; *Grunewald, supra* note 39, § 167 marg. no. 5 for the KG.

[57] Cf. already note 29.

[58] *Joost, supra* note 14, 303 et seq.; see also *Liebs, supra* note 27, 2422; *Vollmer, supra* note 24, 94; further *M. Henssler*, in: Lieb/Noack/Westermann (eds.), Festschrift für Wolfgang Zöllner zum 70. Geburtstag. Vol. I (Cologne *et al.* 1998) 203, 206.

announced that "a judicial review of the balancing of interests cannot lead to the result that only one possible decision would adequately respect all relevant interests"[60]. However, from a theoretical point of view, the shareholders' *Treuepflicht* seems to be the more adequate instrument.[61] First, this *Treuepflicht* has become a general principle in German partnership and corporation law, and guides shareholder behavior and the exercise of their rights; second, it allows the consideration of case-specific circumstances beyond the mere abuse of rights by majority shareholders[62].

The flexibility of the *Treuepflicht* standard thus is its boon and its bane. This shows particularly in the determination of which interests may be considered.

From the corporation's perspective, its interest in retaining profits in order to finance its business and future projects constitutes a serious concern. This was acknowledged expressly with the reform of 1986, and in the current wording of § 29 paras. 1 and 2 GmbHG. In order to specify the notion of relevant corporate interest, one can conclude from § 254 AktG, that specifically reasons relating to "the viability and resilience of the corporation" justify the retention of profits.[63] However, this statutory reference needs to be interpreted in the sense of a broad understanding.[64] While the retention of profits with no reason other than the accumulation of liquidity certainly cannot suffice to explain the refusal to pay any dividend,[65] it is also not necessary

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[59] Explicitly OLG Koblenz, 1 February 2018, *supra* note 41, 1018: "nur in eindeutigen Fällen".

[60] OLG Nuremberg, 9 July 2008, *supra* note 56, 2418; see also OLG Stuttgart, 13 June 2007, *supra* note 44, 2590 et seq.: "Die Thesaurierungsentscheidung darf jedenfalls nicht missbräuchlich erscheinen."

[61] *P. Hommelhoff*, Anmerkungen zum Ergebnisverwendungs-Entscheid der GmbH-Gesellschafter, GmbHR 2010, 1328, 1329.

[62] *Hueck, supra* note 28, 56; *K. Schmidt, supra* note 54, § 46 marg. no. 31; *Verse, supra* note 10, § 29 marg. no. 54; on this see also *Leuschner, supra* note 8, § 29 marg. no. 130; for partnerships further *H.-J. Priester*, Stille Reserven und offene Rücklagen bei Personengesellschaften, Zur Bedeutung von § 253 Abs. 4 HGB, in: Westermann/Rosener (eds.), Festschrift für Karlheinz Quack zum 65. Geburtstag am 3. Januar 1991 (Berlin/New York 1991) 373, 393.

[63] While the law-makers' abstention from including a similar provision in the GmbHG makes it difficult to apply § 254 AktG analogously to the GmbH (see already note 28), this is commonly understood to be due to the unwillingness to set a fixed threshold for profit distribution. It does not therefore preclude recourse to § 254 AktG in order to clarify which interests of the corporation are to be considered; see generally *Ekkenga, supra* note 28, § 29 marg. no. 170; *Kersting, supra* note 28, § 29 marg. no. 30; *L. Strohn*, in: Henssler/Strohn (eds.), Gesellschaftsrecht (4th ed., Munich 2019) § 29 GmbHG, marg. no. 44; cf. also *Winter, supra* note 13, 285. Critically, however, *Einhaus/Selter, supra* note 24, 1182.

[64] E.g. *Verse, supra* note 10, § 29 marg. no. 57.

[65] See also the insufficient justification through reference to "tough competition" (*harter Wettbewerb*) in OLG Brandenburg, 31 March 2009, 6 U 4/08, ZIP 2009, 1955, 1958.

to have an already initiated project or immediate need for liquidity. Instead, a plausible business plan for a foreseeable period of time suffices to illustrate the financing needs of the corporation.[66] That courts rather tend to err on the side of the corporation, generously accepting the reasons why the retention of profits would be necessary, is best shown in a decision handed down by the Higher Regional Court of Nuremberg in 2008: in order to determine the corporation's interest in self-financing, the court referred to the object of the corporation, the resources required to pursue this object, the financial situation of the corporation, the amount and availability of existing capital and revenue reserves, its creditworthiness, the amount and maturity of liabilities, the overall state of the economy, the market situation and the prognosis for the corporation's branch of business, the necessary precautions against potential liability claims, the necessity to engage in research activities, and so forth.[67] This list of relevant reasons could hardly be more extensive; it considers more or less any factor related to the corporation's business.[68]

In contrast, scholars and courts restrict the arguments a shareholder can add to the equation. It is evident that any shareholder has an interest in receiving a return on her investment, usually in the form of a dividend. However, this interest is easily outweighed by the abovementioned business reasons for retaining profits. Scholars are wondering whether an interest beyond the mere wish to participate in the corporation's profits can be taken into account.[69] The Higher Regional Court of Nuremberg pointed to the extent and the amount of previous dividends in order to specify the interest in profit distribution, and it further made reference to the shareholders' financial situation.[70] Some authors add that at the very least, tax liabilities arising from or in connection with the shareholding should generally be covered.[71] However,

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Also insufficient are private considerations of shareholders, e.g. tax reasons, see *Seibt, supra* note 35, § 2 marg. no. 415.

[66] *Priester, supra* note 62, 394 (for partnerships); similarly *Mock, supra* note 6, § 29 marg. no. 189; see also on the difficulty of justifying long-term retention policies without a contractual basis in the corporation's articles of association *Ekkenga, supra* note 28, § 29 marg. no. 171.

[67] OLG Nuremberg, 9 July 2008, *supra* note 56, 2418; see also OLG Brandenburg, 31 March 2009, *supra* note 65, 1958; "sämtliche Umstände der Vermögens-, Finanz- und Ertragslage".

[68] See in a similar vein *Kersting, supra* note 28, § 29 marg. no. 32.

[69] In view of the specific legal situation of limited partners see *Schulze-Osterloh, supra* note 56, 2523 et seq.

[70] OLG Nuremberg, 9 July 2008, *supra* note 56, 2418; agreeing to the former but objecting to the latter *Leuschner, supra* note 8, § 29 marg. no. 133; see also stressing the weight of the minority shareholders' expectations *Mock, supra* note 6, § 29 marg. no. 185.

[71] *Liebs, supra* note 27, 2422; further *Hommelhoff, supra* note 61, 1330; *Hommelhoff, supra* note 26, 432 pointing further to the cost of administrating one's shares; *Verse, supra* note 10, § 29 marg. no. 59; also restrictively BGH, 29 March 1996, *supra* note 56, 276 for

these approaches do not go undisputed in scholarship. There is a reticence to take the individual needs of particular shareholders which go beyond the corporate realm into account.[72] What is private, should not concern the corporation nor should it affect fellow shareholders.[73] It does indeed seem difficult to burden shareholders with their fellow shareholders' private problems over which they have neither knowledge nor influence. However, at least in corporations where the personal ties between shareholders are particularly strong, for example in family firms, the shareholders' *Treuepflicht* can gain specific weight.[74] In rare case constellations, it might thus become necessary to consider a shareholders' private situation if, to the knowledge and acceptance of all shareholders, there is a particular link with the corporate project.[75]

With its balancing requirement, the shareholders' *Treuepflicht* thus paves the way for a thorough judicial review of shareholders' resolutions to distribute or retain profits. While the statutory framework betrays no general preference for either decision, courts have proven reluctant to annul shareholder resolutions retaining all profits, largely relegating the decision to the shareholders' business judgment.

3. Respecting Shareholders' Business Judgment

In case law, the material review of shareholder resolutions to retain profits seems more lenient than the shareholders' *Treuepflicht* would suggest at first glance. However, the courts' prudence is well justified as it reflects their respect for the shareholders' business judgment and results from the corresponding burden of proof.

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a KG; pointing to § 110 HGB *W. Schön*, Bilanzkompetenzen und Ausschüttungsrechte in der Personengesellschaft, in: Budde/Moxter/Offerhaus (eds.), Handelsbilanzen und Steuerbilanzen. Festschrift zum 70. Geburtstag von Prof. Dr. h.c. Heinrich Beisse (Düsseldorf 1997) 471, 487 et seq.; further *Priester, supra* note 62, 394 (for partnerships). For a more general consideration of the shareholders' private interests see *Einhaus/Selter, supra* note 24, 1183: "Gemein ist diesen Ausnahmen, dass der Gesellschafter gerade aufgrund seines Geschäftsanteils eine Zahlung zu leisten hat."

[72] *Ekkenga, supra* note 28, § 29 marg. no. 169.

[73] Cf. § 122 para. 1 HGB for the commercial partnership; in detail *Schön, supra* note 71, 476 et seq.; also *Hommelhoff, supra* note 26, 426.

[74] See also OLG Frankfurt, 30 January 2002, 13 U 99/98, OLGR Frankfurt 2002, 154, 161 et seq.; further the similar reasoning specifically for family firms in OLG Frankfurt, 22 December 2004, 13 U 177/02, GmbHR 2005, 550, 556.

[75] *Verse, supra* note 10, § 29 marg. no. 59; see also *Kersting, supra* note 28, § 29 marg. no. 33: "Gewinnausschüttung auch ohne Anhalt in der Satzung generell derart zum Bestreiten des Lebensunterhalts der Gfter bestimmt sein, dass das ebenfalls Angemessenheit berührt, dann aber unabhängig vom konkreten privaten Ausgabeverhalten"; further for the KG *Grunewald, supra* note 39, § 167 marg. no. 5.

The countless considerations which can be brought forward to justify the retention of profits already provide some idea of the nature of such decisions as complex business decisions; one could even classify them as the archetype of a business decision.[76] Firstly, the financing of the business operation and its future development go to the very heart of a corporation's activity. The corporation's financial resources generally provide the basis for its business and mark the boundaries of its development. In this, financing issues are also linked to shareholders' expectations and plans for their business endeavor; depending on what they want to achieve, different options are viable. As one court put it: in deciding the retention or distribution of profits, there is no one single decision that would be correct; shareholders can choose from a range of distribution schemes which can all be considered reasonable.[77] Secondly, such forward-looking decisions are based on estimations of future developments and plans. Deciding about the need for a retention of profits requires a prognosis of the evolution of the market, the corporation's position in it and its potential for growth. Risks and opportunities have to be weighed against each other, and uncertainty lingers over all projected numbers.[78] Consequently and thirdly, these decisions are difficult to evaluate.[79] From the standpoint of the shareholders at the time they make their decision, various assumptions may seem plausible.[80] However, reviewers tend to assess such assumptions more strictly once they know the actual outcome of the matter. Courts need to avoid such a hindsight bias in the *ex post* evaluation of business decisions. They need to place themselves in the shareholders' shoes, not considering information and experiences which have only become available after the decision-making process was concluded.

In view of those pitfalls, courts try not to interfere with the concerned parties' business judgment, and they apply this prudence also with regard to the

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[76] *Hommelhoff, supra* note 29, § 29 marg. no. 21: "Im Ergebnisverwendungsentscheid der Gesellschafter prägt sich ihre unternehmerische Entscheidungsfreiheit (insbesondere in Finanzierungsfragen) in ihrem Kern aus."; see also *Fleischer/Trinks, supra* note 1, 292; *Vollmer, supra* note 24, 93: "integraler Bestandteil der unternehmenspolitischen Grundsatzentscheidungen", thereby confirming *P. Hommelhoff*, Vollausschüttungsgebot und Verbot stiller Reserven. Ein Plädoyer für die Novellierung des § 29 Abs. 1 GmbHG, GmbHR 1979, 102, 107.

[77] Cf. OLG Nuremberg, 9 July 2008, *supra* note 56, 2418; see also *Schön, supra* note 71, 484.

[78] Stressing this point *Joost, supra* note 14, 300; see also *Vollmer, supra* note 24, 94.

[79] See also *Einhaus/Selter, supra* note 24, 1182 et seq.

[80] Pointing to the prognostic elements of such decision and acknowledging that the shareholder resolution on the application of profits needs to be evaluated in view of the knowledge held at the time the decision was made OLG Nuremberg, 9 July 2008, *supra* note 56, 2417.

shareholders' decision to retain or to distribute profits.[81] The leeway thus given to shareholders in making business decisions is further complemented with the allocation of the burden of proof in those cases.

As a shareholder resolution to retain profits cannot stand where there is no need at all to save funds, a corporation is required to provide reasons for so doing. Initially, this gives rise to an obligation for the corporation to justify its shareholders' decision.[82] It has been shown, though, that this obligation can easily be fulfilled by naming some plausible business argument.[83] It thus falls to the shareholders challenging the decision to explain why the reasons given do not hold.[84] Considering the courts' deferral to the majority's business judgment, it is very rare for economic considerations and commercial arguments to leave a decision to retain profits untenable. In practice, minority shareholders have retention decisions successfully annulled especially when they provide additional evidence showing how the majority benefitted from cutting off the minority from all income from the corporation.[85]

Thus, in the case mentioned above decided by the Higher Regional Court of Nuremberg, the majority had decided to continue retaining profits for the fourth year in a row. The profits carried forward amounted to approximately 30 million euro while the corporation's share capital didn't even amount to one million euro.[86] Although the court considered the investments planned and the liabilities threatening the corporation wouldn't require retaining profits in the amount of 30 times the share capital, it finally concluded that the retention resolution was not arbitrary and therefore still within the discretionary power of the shareholders. At the same time, the court highlighted that in

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[81] OLG Nuremberg, 9 July 2008, *supra* note 56, 2418; OLG Stuttgart, 13 June 2007, *supra* note 44, 2590; see also *Kersting, supra* note 28, § 29 marg. no. 34; *Leuschner, supra* note 8, § 29 marg. no. 132: "auf eine Plausibilitätsprüfung beschränken", with regard to § 254 para. 1 AktG *Stilz, supra* note 23, § 254 marg. no. 10: "Einfallstor für die Heranziehung der Grundgedanken der sog. Business Judgement Rule".

[82] See OLG Brandenburg, 31 March 2009, *supra* note 65, 1958; *Ekkenga, supra* note 28, § 29 marg. no. 173; *Verse, supra* note 10, § 29 marg. no. 60.

[83] See also *Einhaus/Selter, supra* note 24, 1185; further *Leuschner, supra* note 8, § 29 marg. no. 135; *Verse, supra* note 10, § 29 marg. no. 58.

[84] *Ekkenga, supra* note 28, § 29 marg. no. 173; *Leuschner, supra* note 8, § 29 marg. no. 134 et seq.; *Verse, supra* note 10, § 29 marg. no. 60; slightly different, but with a similar result OLG Stuttgart, 13 June 2007, *supra* note 44, 2591: "Die Darlegungs- und Beweislast […] liegt […] beim Kommanditisten, der behauptet, die Entscheidung des Komplementärs sei missbräuchlich oder sonst treuwidrig und deshalb rechtswidrig." For repercussions of contractual provisions in the corporation's articles of association *Ehlke, supra* note 28, 677.

[85] See also Ekkenga*, supra* note 28, § 29 marg. no. 174, basing such claims to annulment on an abuse of rights as a sub-category of a breach of the shareholders' *Treuepflicht*; similarly *Kersting, supra* note 28, § 29 marg. no. 29.

[86] OLG Nuremberg, 9 July 2008, *supra* note 56, 2415 et seq.

recent years there had been profits distributed, and at five million euro in total, the sum was not insignificant.[87] It seems that the court found the shareholders' interest in receiving further dividends was reduced by the fact that they already had received payment of some dividends. In a similar case, the Higher Regional Court of Koblenz held both the arguments of the corporation and the arguments of the minority shareholder to be plausible. With regard to the majority's discretion regarding business decisions, the court did not annul the retention resolution.[88]

In contrast, facts beyond mere business reasons for the retention of profits led the Higher Regional Court of Brandenburg to find the continued retention of profits violated the majority shareholders' *Treuepflicht*. The corporation had retained all profits over seven years and the revenue reserves added up to more than twice the amount of the corporation's share capital. At the same time, the minority shareholder had lost his post as a director of the corporation and thus been cut-off from all sources of income from the corporation while the majority shareholders remained in place as directors, increased their remuneration and ordered luxury vehicles as company cars. Under these circumstances, the court held the continued retention of profits to constitute a breach of the shareholders' *Treuepflicht*.[89]

Private benefits taken by the majority and denied to the minority can thus show that the corporation's interest in retaining profits is not all that real.[90] This finding underlines that courts will only assume a violation of the shareholders' *Treuepflicht* in clear-cut cases. As long as the reasons given by the corporation to justify the retention of profits cannot be discarded straightaway, that means as long as there is some plausible explanation for the retention of profits, a shareholder resolution may stand. In the end, what is labeled a material review under the shareholders' *Treuepflicht* thus seems to come close to a mere check against the abuse of rights.[91]

On a last note, calling the shareholders' decision to distribute or to retain profits a business decision, might bring the business judgment rule to mind for corporate lawyers.[92] However, the business judgment rule has been designed to cover the behavior of directors, not of shareholders. As directors' duties and responsibilities are different from those of shareholders, the rule

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[87] OLG Nuremberg, 9 July 2008, *supra* note 56, 2418 et seq.

[88] OLG Koblenz, 1 February 2018, *supra* note 41, 1019.

[89] OLG Brandenburg, 31 March 2009, *supra* note 65, 1955 et seq., also 1959 specifically on hidden profit distributions to the majority shareholders.

[90] Cf. also OLG Frankfurt, 30 January 2002, *supra* note 74, 164.

[91] See also *Fleischer/Trinks, supra* note 1, 296 et seq.; *Verse, supra* note 10, § 29 marg. no. 7: "dass nach geltender Rechtslage das *Ausschüttungsinteresse* der Minderheit nur *schwach geschützt* ist"; similarly *Hommelhoff, supra* note 29, § 29 marg. no. 21.

[92] For the application of this rule see *Hommelhoff, supra* note 61, 1329; also *Hommelhoff, supra* note 29, § 29 marg. no. 21; *Leuschner, supra* note 8, § 29 marg. no. 134.

and its requirements cannot simply be transposed.[93] For instance, shareholders are by definition personally interested in the outcome of the decision to retain or to distribute profits; a disinterested decision can thus not be a precondition to granting the majority leeway in taking this decision. In addition, the information gathering requirement puts an extraordinarily high burden on shareholders as compared to directors. As shareholders are considered to be the residual owners of the corporation and the business entity, their decisions generally do not require a justification, and they therefore do not need to explain their vote or document the reasons which have led them to vote in a specific way. Interestingly enough, one author trying to transpose the business judgment rule to shareholders, imposed the obligation to collect the necessary information on the directors and not the shareholders themselves.[94] Still, it remains unclear to what extent the shareholders in this scenario would have to examine the reliability and integrity of the information given to them. Shareholders' exercise of their voting rights thus cannot be measured against the directorial business judgment rule.

However, the Higher Regional Court of Nuremberg has, in the abovementioned case, explicitly looked for proof that shareholders, in making their decision, have considered and balanced the corporation's interests as well as their fellow shareholders' interests.[95] In light of this decision, shareholders should probably prepare some kind of documentation of the needs and concerns they have taken into account when making the decision to retain profits, even though such documentation seems unwonted and out of place when it comes to shareholders' voting decisions.[96]

IV. A Difficult Choice of Remedies

If a minority shareholder manages to establish a breach of the majority shareholders' *Treuepflicht*, she can obtain an annulment of the resolution to retain profits (1.). However, this hardly ever provides full satisfaction. Quite the contrary, claiming payment of a dividend remains a difficult endeavor[97] (2.).

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[93] In more detail also *Einhaus/Selter, supra* note 24, 1183; acknowledging the differences also *Fleischer, supra* note 31, 60: "variant of the classical business judgment rule".

[94] *Hommelhoff, supra* note 61, 1329; putting the informational burden on the majority *Leuschner, supra* note 8, § 29 marg. no. 134.

[95] See OLG Nuremberg, 9 July 2008, *supra* note 56, 2417, 2420, albeit differentiating explicitly between the need to balance the relevant interests and its documentation; further OLG Jena, 10 August 2016, 2 U 500/14, ECLI:DE:OLGTH:2016:0810.2U500.14.0A, marg. no. 221; OLG Frankfurt, 30 January 2002, *supra* note 74, 163; in favor of such a documentation requirement also *Hommelhoff, supra* note 29, § 29 marg. no. 24.

[96] See also *Hommelhoff, supra* note 61, 1329.

[97] *Fleischer, supra* note 31, 58: "a long procedural obstacle chase".

In view of these challenges and the risk of continued disputes, exiting the corporation could afford the minority a clean break, but this is available only under strict preconditions (3.).

1. Annulment of the Retention Resolution

A breach of the majority shareholders' *Treuepflicht* in casting her vote constitutes grounds for the annulment of the resulting shareholder resolution, as that resolution is held to violate the law.[98] Shareholders can thus introduce an action for annulment according to general principles. The court's declaration of the resolution as null and void is retroactive in effect, thus removing the basis for the application of its distributable profits. The shareholder meeting must then decide anew.[99]

Of course, there is a strong risk that the majority shareholder will continue to vote for a retention of profits, in which case the minority shareholder would have to keep on challenging these retention resolutions.[100] The minority might thus try to have the court declare a shareholder resolution which allows for the distribution of profits.

The basis for such a shareholder resolution can be found in the votes of the minority. Some scholars conceptualize the breach of shareholder *Treuepflicht* rendering the votes concerned null and void.[101] Should the shareholders decide on a resolution to distribute profits and the majority votes down this proposal in breach of their *Treuepflicht*, the majority's votes are treated as inexistent. The only valid votes cast on the matter will then be the minority's votes in favor of the distribution of profits; courts could then hold a shareholder resolution to be taken with these minority votes alone.[102]

However, this kind of cherry-picking also raises doubts. It undermines the voting process, breaking the invalid shareholder resolution into its component parts and recycling the votes not affected by a breach of the shareholders'

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[98] See § 243 para. 1 AktG, applied analogously to GmbHs; generally on this *Fastrich, supra* note 45, § 13 marg. no. 30; *Mock, supra* note 6, § 29 marg. no. 201; *Verse, supra* note 10, § 29 marg. no. 66.

[99] In order to have a new decision on the application of profits made, the annulment of previous shareholder resolutions is a necessary prerequisite, see OLG Munich, 28 November 2007, 7 U 2282/07, GmbHR 2008, 362, 363.

[100] See further for the risk that the majority simply avoids taking any resolution *Bork/Oepen, supra* note 6, 243: "sozusagen ‚auf kaltem Wege' faktisch […] eine Voll-Thesaurierung".

[101] See BGH, 19 November 1990, II ZR 88/89, GmbHR 1991, 62; also *Einhaus/Selter, supra* note 24, 1177; *M. Geißler*, Die Kassation anfechtbarer Gesellschafterbeschlüsse im GmbH-Recht, GmbHR 2002, 520, 525.

[102] See BGH, 26 October 1983, II ZR 87/83, BGHZ 88, 320, 329 et seq.; *Bork/Oepen, supra* note 6, 245. For the difficulties of this approach in view of material grounds for annulment of a shareholder resolution, see *Geißler, supra* note 101, 528.

Treuepflicht.[103] Furthermore, where the articles of association require a quorum for shareholder resolutions, it must be ascertained whether the minority votes suffice to meet this quorum.[104] But first and foremost, practice has proven it difficult to have a shareholder vote on a distribution proposal put on the agenda of the shareholder meeting in the first place. After all, the majority has generally appointed the directors who prepare the shareholder meeting and its agenda.[105]

Shareholders might thus look for different ways to receive payment of a dividend.

2. *Payment of a Dividend*

As a general rule, a shareholder resolution deciding the distribution of profits is necessary to create an enforceable claim to payment of a dividend. This requirement does not result explicitly from § 29 GmbHG, but has been asserted by a majority of authors and confirmed by courts.[106] It explains the need to coalesce minority votes into a valid shareholder resolution for the distribution of profits. However, in view of the above-mentioned difficulties of this line of action, legal scholarship has envisaged alternatives.

A first step would be to have the court order shareholders to take any resolution on the (partial) distribution of profits.[107] In the absence of more specific guidelines, this solution admittedly risks seeing more retention resolutions and more challenges to shareholder resolutions: with each repetition of the

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[103] See also BGH, 12 April 2016, II ZR 275/14, MittBayNot 2016, 535, 537: "Die Unwirksamkeit der abweichend abgegebenen Stimmen ist eine Folge der Pflicht, in einem bestimmten Sinn abzustimmen."; generally further *J. Ekkenga*, Stimmrechtsbeschränkungen und positive Stimmpflichten des herrschenden Unternehmens im GmbH-Konzern. Das Urteil des OLG München in Sachen Media-Saturn, Der Konzern 2015, 409, 410: "trotz nachgewiesener Fehlerhaftigkeit der Ablehnung [verbleiben] regelmäßig diskretionäre Spielräume"; also *Winter, supra* note 13, 170: "letztlich darauf hinausläuft, im Prozeß gegen die Gesellschaft eine positive Stimmpflicht des Gesellschafters zu klären".

[104] *Bork/Oepen, supra* note 6, 249.

[105] On different avoidance strategies and possible remedies *Bork/Oepen, supra* note 6, 246 et seq.

[106] BGH, 14 September 1998, II ZR 172/97, BGHZ 139, 299, 302 et seq.; OLG Koblenz, 1 February 2018, *supra* note 41, 1019 et seq.; *Kersting, supra* note 28, § 29 marg. nos. 38, 42, 44; *Verse, supra* note 10, § 29 marg. no. 36; differently however *Hommelhoff, supra* note 29, § 29 marg. no. 4: "vorläufig gehemmter Auszahlungsanspruch"; in detail on this *Hommelhoff, supra* note 3, 184 et seq.: the claim becomes enforceable either with a shareholder resolution to distribute profits, or with the end of the shareholder meeting in which such a decision should have been made according to the meeting's agenda, or with the expiration of the time limits laid down in § 42a para. 2 GmbHG or § 267 para. 1 HGB.

[107] See *obiter* OLG Düsseldorf, 29 June 2001, 17 U 200/00, NZG 2001, 1085, 1086. On the shareholders' claim to have the corporation take the necessary steps to realize their right to payment of a dividend *Bork/Oepen, supra* note 6, 249 et seq.

shareholder vote, the majority could insist on retaining all profits, thus gaining time and requiring the minority to continue challenging these resolutions.[108] German law so far does not foresee judicial interference with the voting procedure; in particular, naming a third party to exercise the shareholders' voting right has not yet been tried or discussed further.

Instead, some scholars propose having the courts fix an adequate distribution-retention-ratio.[109] Once the court is allowed to determine what part of the profits is to be distributed, it is no longer necessary to have the shareholders take the resolution themselves, but a court order can replace such resolution. Of course, the issue arises whether a court is and should be allowed to decide on the distribution or retention of a private corporation's profits.

Arguments in favor of such an approach suggest that courts already enjoy similar authority in general contract law. Parties to a contract may leave the scope of their obligations to be determined by a third party; where the third party fails to do so in an equitable manner, courts may step in and specify the obligation owed in the third party's stead.[110] Similarly, courts could be allowed to determine the adequate amount of profits to be retained and decide the distribution of the remainder of the profits in a corporate context.[111] It has to be acknowledged, though, that the legal background is different. In this situation, shareholders usually have not left the decision on the retention or distribution of profits to a third party in the first place.[112] Further, the decision to retain or distribute profits is a complex commercial question which has repercussions on the whole business of the corporation. This consideration triggers the traditional hesitation held by scholarship and the courts when it comes to transferring a business decision which requires profound knowledge of the corporation's business and allows for entrepreneurial discretion into judges' hands.[113]

In order to make the judges' task easier, some authors advocate a principle of full distribution of profits. If shareholders do not decide otherwise, these authors want to allow judges to order the full distribution of profits; the court

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[108] For this argument OLG Zweibrücken, 28 May 2019, 5 U 89/18, ECLI:DE:POLGZWE:2019:0528.5U89.18.00, marg. no. 36; see also *Kersting, supra* note 28, § 29 marg. no. 41; pointing further to the risk that no resolution whatsoever will be taken *Hommelhoff, supra* note 3, 173.

[109] *Hueck, supra* note 28, 54 et seq., albeit with a tendency towards a full distribution of profits; further *Heusel/Goette, supra* note 33, 389; *Zöllner, supra* note 9, 417; for decisions regarding the process of establishing the financial statements see also *Schulze-Osterloh, supra* note 56, 2525.

[110] § 315 para. 3 sent. 2 BGB.

[111] *Zöllner, supra* note 9, 416 et seq.

[112] See also *Hommelhoff, supra* note 3, 174: "So nicht; das Prozeßgericht ist kein zur Rechtsgestaltung aufgerufenes Schiedsgericht."

[113] Cf. OLG Düsseldorf, 29 June 2001, *supra* note 107, 1086; on all this *Bork/Oepen, supra* note 6, 255 et seq.; *Gutbrod, supra* note 6, 557; *K. Schmidt, supra* note 54, § 46 marg. no. 33; critically *Leuschner, supra* note 8, § 29 marg. no. 121.

order would thus substitute for a shareholder resolution to distribute all profits.[114] While this principle might seem too rigid at first, its inflexibility would need to be attenuated by applying it cautiously: full distribution of profits might counteract long-term financial plans and could threaten to weaken the corporation's financial cushion. In addition, changes introduced by the BiRiLiG clearly express the legislature's intention to facilitate self-financing for GmbHs. Critics thus argue that the introduction of a principle of full distribution of profits is contrary to the law. However, the so-called principle would in fact remain the rare exception. Before a court would actually mandate the full distribution of profits, majority shareholders would be able to prevent this outcome at any time.[115] As shareholders can decide to retain profits with the sole votes of the majority, majority shareholders can always decide against the full distribution of profits when it comes to making this decision. A risk of full distribution of profits ordered by a court only arises where the majority acts in breach of its *Treuepflicht*. In such an event, however, scholarship allows the majority to take a new shareholder resolution at any point in time, up to the moment the court actually decides. That means that the majority can change its initial stance and arrange for the distribution of at least some part of the profits after it has been warned that there is a risk of its initial resolution being annulled by (i) first, the minority who filed suit and (ii) second, by the judges who might have shown some understanding for the minority's claim during the oral proceedings. Considering that the courts tend to accept virtually any plausible explanation, even for a continued retention of profits, and that they intervene only in extreme cases, the bar a corrected shareholder resolution on the distribution of profits has to pass is not very high. Yet, the threat of seeing the corporation's profits being distributed in full could induce the majority to compromise with the minority or, at least, to grant the minority its due.

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[114] *Bork/Oepen, supra* note 6, 270; *Kersting, supra* note 28, § 29 marg. no. 41; *Leuschner, supra* note 8, § 29 marg. no. 123; *Mock, supra* note 6, § 29 marg. no. 94; *Verse, supra* note 10, § 29 marg. no. 62; similarly *Strohn, supra* note 63, § 29 GmbHG, marg. no. 43; cf. BGH, 29 March 1996, *supra* note 56, 276 for a KG. See also for the automatic coming into existence of an enforceable claim to payment of a dividend once the statutory deadline established in § 42a para. 2 sent. 1 GmbHG is expired *Hommelhoff, supra* note 29, § 29 marg. no. 4; in detail *Hommelhoff, supra* note 3, 184 et seq. Recently ordering payment of a dividend in form of a claim for damages for breach of the *Treuepflicht* OLG Zweibrücken, 28 May 2019, *supra* note 108, marg. no. 36.

[115] *Bork/Oepen, supra* note 6, 269; *Hueck, supra* note 28, 55; *Kersting, supra* note 28, § 29 marg. no. 41; *Leuschner, supra* note 8, § 29 marg. no. 123; *Mock, supra* note 6, § 29 marg. no. 98; *Strohn, supra* note 63, § 29 GmbHG, marg. no. 43; *Zöllner, supra* note 9, 419; further *Verse, supra* note 10, § 29 marg. no. 62, also pointing to the self-restraint of the shareholder claiming profit distribution. Problems remain however where two shareholders or shareholder groups with equal voting rights block any decision, see *Heusel/Goette, supra* note 33, 389.

While scholarship has thus tried to show ways shareholders can achieve payment of a dividend even against the will of the majority, courts have not taken a stand on the issue so far. In order to escape this uncertainty, minority shareholders could be tempted to liquidate their interest by exiting the corporation, although, this continues to prove to be a difficult remedy to exercise.

3. Right to Exit the Corporation

Not only are shareholder conflicts over the distribution or retention of profits difficult to solve, but the decision to distribute or retain profits is a recurrent one. This means that as long as there are distributable profits, the question how to proceed with these profits arises every business year anew.[116] Where the majority follows its own agenda with no regard for the minority's needs, the conflict will resurge year after year, suits will be filed and court decisions appealed. One way to end this conflict could be for the minority to exit the corporation. However, this remedy is difficult to assert.

Modern corporations are built to persist. Shareholders' contributions, be they paid in cash or made in kind, are often vital for the corporation's business plans; repaying shareholders often threatens the basis on which a corporation operates. Corporation law recognizes this need for stability and restricts shareholders from one-sidedly withdrawing their contribution in order to safeguard the business.[117] However, especially in close corporations, the separation of shareholders might become necessary where personal cooperation is no longer possible. The German legislature has recognized this specific point, § 61 para. 1 GmbHG grants minority shareholders who (jointly) hold at least 10% of the corporation's share capital a right to claim dissolution of the corporation for good cause.[118] Similarly, German scholarship and courts also recognize good cause as grounds to allow shareholders to exit the corporation.

In 1930, the German Imperial Court (*Reichsgericht*) already developed a shareholders' right to exit from the GmbH for good cause.[119] While this right

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[116] See also *Joost, supra* note 14, 301.

[117] E.g. *E. B. Rock/M. L. Wachter*, Waiting for the Omelet to Set: Match-Specific Assets and Minority Oppression in Close Corporations, J. Corp. L. 24 (1999) 913, 919 et seq., 921 et seq.; on the considerations of the German legislator when drafting the GmbHG *V. Röhricht*, Zum Austritt des Gesellschafters aus der GmbH, in: Goerdeler/Hommelhoff *et al.* (eds.), Festschrift für Alfred Kellermann zum 70. Geburtstag am 29. November 1990 (Berlin/New York 1991) 361, 367 et seq.

[118] On this see *H. Fleischer/J. Trinks*, Gesellschafterstreitigkeiten als Auflösungsgrund in geschlossenen Kapitalgesellschaften. Die Auflösungsklage nach § 61 GmbHG im Vergleich zum französischen Recht, GmbHR 2019, 1209; in English also *H. Fleischer/J. Trinks*, Court-Ordered Dissolution of Closed Companies in Cases of Shareholder Disputes in Germany and France, RTDF 3-2019, 17.

[119] RG, 7 February 1930, II 247/29, RGZ 128, 1, 17; pointing to this decision's limited scope *Röhricht, supra* note 117, 365.

was first limited to specific cases where shareholders were obliged to provide continuous additional services, the court was already pointing out that dissolution of the corporation cannot suffice as a solution to certain issues. The BGH then based the right to exit for good cause on the general private law principle that a legal relationship which strongly interferes with the private life of the parties involved can be terminated prematurely if there is good cause.[120] Good cause is generally found where remaining a shareholder has become unacceptable for a person while, considering all circumstances, the interest of the corporation and her fellow shareholders in her retaining her shareholding must take a back seat.[121] Again, this requires a balancing act in light of the competing interests involved. One important factor which can tip the balance is the availability of a less invasive remedy; if a shareholder can, for instance, simply sell her shares, there is no scope for her to exercise an exit right instead.[122] The right to exit the corporation for good cause has thus become an important alternative to dissolving the corporation where shareholders can no longer be made to cooperate, but it has to remain an exceptional remedy, to be used only as a means of last resort.[123]

Generally, the shareholder's right to exit the corporation for good cause can be triggered where a majority continuously decides the retention of profits in breach of their *Treuepflicht*.[124] The courts have however highlighted that the mere retention of profits does not constitute good cause in and of itself.[125] Indeed, as has been said, retaining profits is most often justified as part of a

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[120] BGH, 1 April 1953, II ZR 235/52, BGHZ 9, 157, 161 et seq.; in detail on this decision's history *J. Thiessen*, § 3 – Sternbrauerei Regensburg – BGHZ 9, 157, in: Fleischer/Thiessen (eds.), Gesellschaftsrechts-Geschichten (Tübingen 2018) 99 et seq.; cf. further BGH, 16 December 1991, II ZR 58/91, BGHZ 116, 359, 369: "Dieses Recht gehört als Grundprinzip des Verbandsrechts zu den zwingenden, unverzichtbaren Mitgliedschaftsrechten. Es kann dann geltend gemacht werden, wenn Umstände vorliegen, die dem austrittswilligen Gesellschafter den weiteren Verbleib in der Gesellschaft unzumutbar machen."

[121] *Seibt, supra* note 48, Anhang § 34 marg. no. 10; *L. Strohn*, in: Fleischer/Goette (eds.), Münchener Kommentar zum GmbH-Gesetz, Vol. I (3rd ed., Munich 2018) § 34 marg. no. 180; also *Altmeppen, supra* note 48, § 60 marg. no. 105; *D. Kleindiek*, Lutter/Hommelhoff GmbH-Gesetz Kommentar (20th ed., Cologne 2020) § 34 marg. no. 148.

[122] *Kersting, supra* note 28, Anhang nach § 34 marg. no. 22; *Strohn, supra* note 121, § 34 marg. no. 189 et seq.; concisely also *Kleindiek, supra* note 121, § 34 marg. no. 144: "Notrecht (ultima ratio)"; in detail on the possibility to sell her shares *Röhricht, supra* note 117, 383 et seq.

[123] See already RG, 7 February 1930, *supra* note 119, 17.

[124] E.g. *Emmerich, supra* note 13, 148; *Verse, supra* note 10, § 29 marg. no. 60.

[125] OLG Munich, 9 June 1989, 23 U 6437/88, GmbHR 1990, 221, 222; see also *H. Eschenlohr*, Beschränkungen der Austritts- und Kündigungsmöglichkeiten des Gesellschafters einer Familien-GmbH, in: Hommelhoff/Schmidt-Diemitz/Sigle (eds.), Familiengesellschaften. Festschrift für Walter Sigle zum 70. Geburtstag (Cologne 2000) 131, 138; *Kersting, supra* note 28, § 29 marg. no. 34.

valid and desired self-financing policy of the corporation. Persistent minority oppression can however constitute a ground for exiting a corporation.[126] Where the retention of profits thus goes against the shareholders' *Treuepflicht* and comes as an expression of the majority abusing its power, such behavior can make it unacceptable for the minority to hold on to its shareholding. The continuous and excessive retention of profits in breach of the shareholders' *Treuepflicht* can then give rise to a right of the minority shareholder to exit the corporation for good cause. This is illustrated by a decision of the Higher Regional Court of Cologne[127]: the court granted a minority shareholder the right to exit the corporation where the majority had decided to retain profits, while also extracting private benefits on the basis of an over-priced consultancy agreement and handing out loans from the corporation to related parties at an overly modest interest rate and with no securities.

Especially where such obviously abusive behavior cannot be established, the *ultima ratio* requirement can however pose an obstacle to the minority's desire to exit the corporation. Shareholders can generally fight the excessive retention of profits as described above: they can have the shareholder resolution deciding the retention of profits annulled and try to claim payment of a dividend. Taking such steps can be required as a less invasive remedy than exiting the corporation.[128] This was the stance taken by the Higher Regional Court of Munich in an earlier decision.[129]

While a right to exit the corporation might thus be available for the oppressed minority, it is granted even more restrictively than the annulment of a shareholder resolution deciding the retention of profits.[130]

V. In Favor of a Clear-Cut Rule and Generous Exceptions

A corporation's decision on how to proceed with its profits, whether to distribute or to retain them, is complex. While this decision seems, first and foremost, to concern the corporation's (self-)financing policy, it also has to consider the interest of the shareholders in participating in the corporation's proceeds. Within this framework, however, deciding the retention or distribution of profits is an act of discretion, and various outcomes fall into the realm

[126] For a right to exit also in extreme cases of a continuous, but legitimate retention of profits see *Strohn, supra* note 63, § 29 marg. no. 44; also *Eschenlohr, supra* note 125, 139; further *Röhricht, supra* note 117, 363, 383.

[127] OLG Cologne, 26 March 1999, 19 U 108/96, NZG 1999, 1222, 1223.

[128] See *Röhricht, supra* note 117, 382 et seq.

[129] OLG Munich, 9 June 1989, *supra* note 125, 222, confirmed by BGH, 15 January 1999, II ZR 163/89, quoted at GmbHR 1990, 222.

[130] Cf. also *Vollmer, supra* note 24, 95 et seq. advocating for a general exit right; consenting *Emmerich, supra* note 13, 148.

of defensible decisions. Fixing clear thresholds for when this realm is overstepped has proven very difficult, to say the least. Numerous legislative and scholarly efforts to provide a general, but adequate rule illustrate this difficulty: set numbers can hardly capture the multifaceted reality of close corporations, their different organizational structures and business models, and their varying financing needs and economic challenges.

Under German Law, scholarship and courts therefore have recourse to the flexible concept of the shareholders' *Treuepflicht* in order to police shareholder resolutions on the retention of profits. The shareholders' interest to receive payment of a dividend has to be balanced against the corporation's interest in preserving liquidity and establishing an effective self-financing policy in view of the context and the specifics of the case at hand. In this balancing exercise, courts respect the shareholders' business judgment and avoid questioning the commercial and economic rationale behind the financial policy being pursued as long as the reasons given are plausible. Thus, a breach of the shareholders' *Treuepflicht* will only be assumed and the resolution on retaining profits will only be annulled in extreme and rather obvious cases. This is an outcome which reflects the extraordinary nature of interfering with a business decision attributed by law to the shareholders and is in tune with the judicial approach in other jurisdictions.

Merely annulling the shareholders resolution to retain profits only goes half-way when it comes to the minority's interest and potentially even their need for liquidity. Judicially, making a claim to payment of a dividend will proof difficult. Scholarship and courts are reluctant to have judges determine the amount to be distributed when a whole range of decisions would be legally permissible. In order to provide minority shareholders with a manageable way to receive payment of a dividend and take the burden of making business decisions from the courts, a clear-cut rule which might seem excessive at first sight, could look more attractive at a second glance: mandating the full distribution of profits where shareholders do not achieve a valid shareholder resolution on the (partial) retention of profits.

As has been said before, such a principle of full distribution could mainly stand because, in practice, the exception will probably be the rule. Up to the point a court decides, the majority can re-take a resolution allowing for the distribution of at least some profits. Considering that courts annul such resolutions only in extreme cases, it should be no problem for the majority to achieve a defensible solution with some goodwill, or even with mere caution. In practice, there is thus a strong chance that shareholder disputes over the retention of profits will regularly end with an autonomous shareholder decision.

The principle of full distribution would thus be a mere penalty default rule.[131] Unlike most so-called penalty defaults, this one would however not sanction a lack of initial contractual provision, but by leaving room for correction up until a judge's decision, the penalty would only sanction the ma-

jority's persistent use of their voting rights in breach of their shareholders' duty of loyalty. Shareholders indeed can prevent full distribution of profits at several steps along the road and after several warning signs have been passed. The threat a full distribution of profits might pose to the majority's plans and to the corporation's business at first sight, becomes a dimmer prospect on closer inspection.

Furthermore, current scholarship and case-law might not read § 29 para. 1 GmbHG to mandate full distribution of profits – unless at least part of the profits need to be retained according to law, the articles of association, or following a shareholder resolution. The wording of the rule would however allow for such an interpretation, the law granting shareholders a "claim to the annual surplus" minus statutory or individual retention provisions.[132] As long as shareholders do not decide otherwise, a judge might bring this claim into existence deciding to distribute all profits, overriding the shareholder meeting. Similarly, the fact that the 1986 amendment to § 29 GmbHG was intended to facilitate corporate self-financing does not preclude having recourse to the principle of full distribution of profits as a (comparatively weak penalty) default rule.[133] In any case, shareholders could at least introduce such a principle in the corporation's articles of association.[134]

Finally, the threat a principle of full distribution of profits could pose to the corporation's financial stability can be further attenuated through applying the shareholders' *Treuepflicht*. This *Treuepflicht* actually works both ways[135]: it requires shareholders to consider their fellow shareholders interest

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[131] On the concept of penalty defaults see *I. Ayres/R. Gertner*, Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules, Yale L. J. 99 (1989), 87; *I. Ayres*, Ya-Huh: There Are and Should Be Penalty Defaults, Fla. St. U. L. Rev. 33 (2006), 589.

[132] On the interpretation of § 29 para. 1 cf. *Hommelhoff, supra* note 29, § 29 marg. no. 4; similarly *Gutbrod, supra* note 6, 557; see further critically *Verse, supra* note 10, § 29 marg. no. 10.

[133] See the relatively general justification of the new rule, BT-Drs. 10/317, 109: "Für die Erhaltung und Fortentwicklung der Gesellschaft ist in aller Regel notwendig, den erwirtschafteten Gewinn zumindest zum Teil im Unternehmen zu belassen. Den Gesellschaftern soll daher die Möglichkeit eingeräumt werden, im Rahmen des Beschlusses über die Verwendung des Ergebnisses Beträge in Gewinnrücklagen einzustellen (Absatz 2)"; see also OLG Zweibrücken, 28 May 2019, *supra* note 108, marg. no. 36: "das Gesetz die Gewinnausschüttung als den Regelfall ansieht"; alternatively *Heusel/Goette, supra* note 33, 389.

[134] For potential options consider *Hommelhoff, supra* note 29, § 29 marg. no. 18; *Verse, supra* note 10, § 29 marg. no. 38.

[135] Generally on the obligation to consent BGH, 25 September 1986, II ZR 262/85, BGHZ 98, 276, 278 et seq.; also BGH, 12 April 2016, II ZR 275/14, MittBayNot 2016, 535, 537: "hohe[] Anforderungen"; further *I. Drescher*, in: Fleischer/Goette (eds.), Münchener Kommentar zum GmbH-Gesetz, Vol. II (3rd ed., Munich 2019) § 47 marg. no. 257 et seq.

in profit distribution, and, at the same time, it asks shareholders to accommodate the corporation's need to retain liquidity and profits. Shareholders might thus even be obliged to consent to a retention of profits.[136] In cases where a full distribution of profits would threaten the corporation's existence, judges could thus moderate the principle and, by cautiously applying the shareholders' *Treuepflicht*, mandate the partial – or even full – retention of profits and accordingly order all or only part of the profits to be distributed, or even reject the minority's claim to payment of a dividend.

While shareholder disputes over the distribution or retention of profits can hardly be avoided, scholarship and courts must work to provide consistent solutions and mitigate their negative effects. The shareholders' *Treuepflicht* has proven to be a powerful tool in this endeavor. Shareholders themselves should now step in and specify clear-cut guidelines in their corporation's articles of association.

[136] *Kersting, supra* note 28, § 29 marg. no. 35: "bei ganz unabweisbarem Bedürfnis im GesInteresse"; *K. Schmidt, supra* note 54, § 46 marg. no. 30; *Schulze-Osterloh, supra* note 56, 2522; *Verse, supra* note 10, § 29 marg. no. 61; in detail on § 29 GmbHG in its previous version *Winter, supra* note 13, 282 et seq.; see also the *obiter dictum* in OLG Stuttgart, 13 June 2007, *supra* note 44, 2590.