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Assessing Regulatory Impact on Family Businesses

A Family Business Test for Germany and the EU

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Summary of main results

1. Up to now, the practice of impact assessment has not taken account of the distinctive characteristics of family businesses either at national or European level. This is hardly surprising given the fact that the actors involved in the legislative process are likely to have a limited level of awareness of the distinctive features of family businesses and of the specific relevance of much of the legislation for such companies.

2. A family business test would help to close the awareness gap on the part of legislators. Such a test is intended to supplement the tool box of German and European legislators with an instrument that is tailored to the specific circumstances of family companies and will improve the awareness of legislators of the consequences of their actions, in particular in the context of family businesses. In turn, the family businesses concerned, and consequently the economy, should be protected from any unintended negative impact.

3. The family business test could and should supplement the SME test at national level and be included in the tool box at European level.

4. The backdrop for the test is the fact that family companies have features that clearly set them apart from other company types.

    a. One characteristic is the desire of family members involved in the business to ensure their (direct or indirect) material influence over company management permanently – and therefore across generations – and so to prevent the transfer of corporate influence to non-family members; this endeavour places the family company, from a functional perspective, on a par with a family foundation, and lends the share held by a family shareholder a quasi-fiduciary character.

    b. Endeavours on the part of family shareholders to secure the influence of the family and defend it against non-family members more or less inevitably involve doing without inflows of equity from external third parties, resulting in the need for self-financing.

    In its design, the family business test should be aligned with these structural features of a family company.

5. German law does not provide for a specific legal form in the case of a family company and its definition does not depend either on the size of the company or the legal form of the legal entity. As a result, virtually all provisions of company law, – and with these large parts of civil law – along with the fiscal framework conditions, become especially relevant to family companies, in that family shareholders are dependent upon finding a legal form that is suitable for their own specific purposes.

6. The family business test should ask the concrete question as to whether family companies are particularly affected or vulnerable in terms of the legislative environment when it comes to (i) corporate governance of the company, (ii) succession, (iii) possible third-party administration of the shareholding, (iv) disclosure of company data and other information, (v) financing the company or (vi) the mobility of the company and its shareholders, given the cross-generational character of the company, the distinctive characteristics of corporate financing and the quasi-fiduciary character of the shareholding.

A. Basic principles

I. Preface

Up to now, the practice of impact assessment[1] has not taken account of the distinctive characteristics of family businesses. This is hardly surprising given the fact that the actors involved in the legislative process are likely to have a limited awareness of these characteristics and of the specific relevance of much of the legislation for such companies. Against this backdrop, a special family business test is intended to enrich the current practice of impact assessment and, as part of the legislative procedure, to allow for the assessment of the impact of proposed legislation on both the civil and fiscal circumstances of family companies and on the family members themselves. In addition, the test aims to enable the detection of inconsistencies with other legislation (which arise from the fact that shareholders belong to one family) and of practical problems in implementing the law in family businesses. In other words, the aim is to determine the specific impact of legislation on family businesses, and not to establish the general cost of regulation as associated with compliance and new legislation; this is the subject of Section 1 (3) of the German Act on the Establishment of a National Regulatory Control Council (Gesetz zur Einsetzung eines Nationalen Normenkontrollrates – NKRG).[2]

The final report submitted in 2009 by the expert group set up by the European Commission "Overview of Family-Business-Relevant Issues: Research, Networks, Policy Measures and Existing Studies" rightly refers to the

> "limited awareness of policy makers of the specificities of family businesses and the contribution they make to society."[3]

The family business test is intended to help close this awareness gap on the part of legislators at national and European levels.

II. The need for a family business test

The need for a test specifically for family businesses arises not least in view of the distinctive characteristics[4] of the family business in general and the family company specifically, which will be treated later

1 See also II.

2 In addition III.1.

3 European Commission, Final Report, p. 12.

4 At B.

in this study[5]– namely, the dominant influence of family members over management, the cross-generational nature of the enterprise and its inherent limitations on corporate financing and the typically keen interest in sustainable management. On the other hand, the specific public interest in taking these characteristics into account as part of the legislative process is due not only to the general desire of the legislator for judicious and tailor-made legislation, but also and primarily to the considerable economic importance of family businesses.[6] A special family business test could therefore add an extra instrument tailored to the specific circumstances of family companies to the legislator's toolbox. In this way, it will improve the awareness of legislators of the consequences of their acts for family companies, while at the same time protecting the family companies concerned, and with them the economy, against any unintended negative impact. In other words: At issue is closing the awareness gap mentioned at the start and ensuring the transparency of regulatory impact, not a privileged status for certain companies.

III. Family business test in the context of existing instruments for impact assessment – the insufficiency of the SME test

1. The national level

Impact assessment has long been an established part of modern legislation. At the national level, the National Regulatory Control Council established by the Federal Chancellery under Section 1 (2) of the NKRG has the task of supporting the Federal Government in the areas of bureaucracy reduction and improved regulation. Under Section 1 (3) of the NKRG, the National Regulatory Control Council is required to examine, in particular, the presentation of the cost of compliance with new legislation to citizens, business and public administration in terms of its transparency and suitability of methodology, and the presentation of other costs to businesses, in particular to medium-sized enterprises.[7] Under Section 2 (1) of the NKRG, compliance costs include the entire measurable expenditure of time, in addition to costs that are incurred for compliance with federal legislation by citizens, businesses and public administration. Against the backdrop of the requirements of the NKRG, Section 43 (1) no. 5 of the Joint Rules of Procedure of the Federal Ministries (Gemeinsame Geschäftsordnung der Bundesministerien – GGO) provides that the explanatory memorandum of a bill should include the regulatory impact, specifically in accordance with Section 44 of the GGO. According to its paragraph 1, regulatory impact

> "is understood to mean the material effect of legislation. It includes both the intended effect and the unintended side effects."

Section 44 (5) p. 1 no. 1 of the GGO requires the presentation of

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5 On terminology, see also at B.I.

6 In addition, *ZEW/ifm*, Die volkswirtschaftliche Bedeutung der Familienunternehmen, 5th edition 2019; *Woywode/Keese/Tänzler* ZGR 2012, 418, 420 et seq. with further references.

7 Not, in contrast, the intended aims and purposes of legislation, see Section 1 (4) NKRG.

> "other costs to business, in particular to medium-sized companies, and the impact of the legislation on individual prices and the price level" [our translations],

among other things.

One example that is relevant to the present context and should be mentioned is the "Leitfaden zur Berücksichtigung der Belange mittelständischer Unternehmen in der Gesetzesfolgenabschätzung (KMU-Test)", a set of guidelines for considering the interests of SME companies in impact assessment known as the "SME test", developed by the Federal Government, the National Regulatory Control Council and the Federal Statistical Office. In view of the fact that many national and international studies have shown "that small and medium-sized enterprises (SMEs) are often disproportionately affected by the implementation of statutory legislation", the test is intended to introduce

> "a systematic approach for taking into consideration the interests of small and medium-sized enterprises when drafting Federal laws." [our translations]

However, the guidelines are aimed at companies with four employees (including the proprietor) and annual sales of 600,000 euros and are for this very reason not suitable for reflecting the distinctive features of family companies – which, as will be explained in greater detail later in this study,[8] can also include large companies.

Even to the degree that the group of family companies overlaps with the group of SMEs and some family companies are small or medium-sized family enterprises, the term SME does not mirror the specific circumstances of a family company; the German SME test, therefore, falls short even with respect to small and medium-sized family enterprises. The test is aimed primarily at establishing the particular compliance costs of SMEs that could arise from a lack of electronic preparation for regulatory compliance, a lack of routine or from the need for investment or external costs, for example, tax consultancy costs, related to compliance. In contrast, the family business test to be developed is justified on the basis of the distinctive features of family businesses that are size-independent, namely the family connection of the shareholders and the associated company law and economic circumstances.

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8 At B.

2. The European level

There is a complex system of impact assessment at European level as well.[9] In addition to guidelines,[10] this consists in particular of a toolbox which in turn contains an SME test.[11] This SME test goes in the same direction as the national SME test mentioned above and should be considered against the backdrop of the European Commission pursuing a special SME policy,[12] as seen for example in the EU Accounting Directive[13] with its system of size-specific accounting and the many associated reliefs for micro-enterprises and for small and medium-sized enterprises.[14] The SME test also refers back to the SME policy of the Commission:

> *"SMEs are the backbone of the EU economy, creating more than 85% of new jobs in Europe. Due to their size and limited resources, SMEs can be affected by the costs of regulation proportionately more than their bigger competitors. … SMEs' interests should be taken into account at the very early stages of policymaking in order to make legislation more SME friendly. In addition, it is Commission policy to exempt micro-enterprises from EU legislation wherever possible or introduce special regimes so as to minimise the regulatory burden on them."*[15]

However, it is also the case that the SME test is not capable of recognising the specific circumstances of family companies and, for this reason, it should be supplemented with the family business test. This family business test would be intended for inclusion in the toolbox mentioned above in addition to the SME test and – as is the case at national level – would be for use with ongoing legislation proposals.

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9 Referred to as "Impact Assessments", s. https://ec.europa.eu/info/law/law-making-process/planning-and-proposing-law/impact-assessments_en.

10 https://ec.europa.eu/info/law/law-making-process/planning-and-proposing-law/better-regulation-why-and-how/better-regulation-guidelines-and-toolbox_en.

11 https://ec.europa.eu/info/better-regulation-toolbox_en.

12 See in particular Recommendation of the Commission of 6 May 2003 regarding the definition of micro-enterprises and small and medium-sized enterprises(2003/361/EC), OJ no. L 124/36 of 20 May 2003.

13 Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC (OJ. EU L 182/19 of 29 June 2013).

14 See for German law the description of the size categories in Sections 267, 267a HGB; for more details *see Habersack/ Verse*, Europäisches Gesellschaftsrecht, 5th edition 2019, Section 9 m.n. 22 et seq.

15 https://ec.europa.eu/info/sites/info/files/better-regulation-toolbox-22.pdf.

IV. Addressees of the family business test

In line with the above findings[16] relating to the practice of impact assessment, the family business test to be developed here is intended both for national and the international legislators. The family business test could and should supplement the SME test at national level and be included in the "toolbox" at European level.

16 At III.

B. The family company as a connecting element

I. Family business and family company

Even though some distinctive features of a family business – for example, the cross-generational character and the marked sustainability mentality – may be present in relation to businesses that are operated by sole traders, the following considerations focus on family companies, that is to say, on companies that are under the dominant influence of shareholders who have a family connection with the company.[17] The sole trader company is generally operated by a natural person who is typically a member of a family. However, the special features of a family business run by a company – that is, a family company – stem precisely from the prerequisite of a family member as shareholder, and the family typically makes preparations for securing its cross-generational influence over the company and its management.[18]

The cross-generational character of the family business and a pronounced sense of sustainability in family companies are therefore the result of agreements made under the articles of association and those made apart from the articles under the law of obligations and are institutionalised. Questions relating to tax and inheritance issues may arise with sole proprietor businesses. However, in addition to regulation under company law, which by its nature does not apply to sole proprietorships, provisions that are especially relevant to companies as legal entities, for example, relating to accounting law or capital markets law, also distinguish the particularly pronounced, specific impact of family companies and suggest focusing the following considerations on such companies. The name "family business test" for the test to be developed need not of course be an obstacle.

II. Irrelevance of Section 1 (1) no. 1 sentence 3 of the DrittelbG

If it is to be an appropriate instrument for impact assessment, a family business test must be based on as precise a definition as possible of its connecting factor and therefore of the actual elements of the family company. It would appear that after Section 157 (4) no. 2 of the German Stock Corporation Act (Aktiengesetz - AktG) was replaced by Article 2 no. 24 of the EU Accounting Directive of 19 December 1985,[19] the term family company only appears in Section 1 (1) no. 1 sentences 2, 3 of the German Act on One-Third Participation of Employees in Supervisory Boards (Gesetz über die Drittelbeteiligung der Arbeitnehmer im Aufsichtsrat - DrittelbG). The provision should be understood in the context that stock corporations registered prior to 10 August 1994 are still subject to self-determination provided

17 For more details see III.

18 For more details see III.

19 BGBl I p. 2355 (2391).

for in the DrittelbG if they have fewer than 500 employees.[20] Under Section 1 (1) no. 1 sentence 2 of the DrittelbG, only "family companies" are excluded here. The following are deemed to be such under Section 1 (1) no. 1 sentence 3 of the DrittelbG:

> *"Stock corporations whose shareholder is a single natural person or whose shareholders are related directly or by marriage within the meaning of Section 15 (1) nos. 2 to 8, par. 2 of the German Fiscal Code (Abgabenordnung)." [our translation]*

This definition meanwhile is entirely tailored to the purpose of co-determination and is not suitable as a general definition.[21] This follows alone from the fact that the term family company, even though we encounter such companies frequently enough in the legal form of a stock corporation (AG),[22] is conceived as being independent of legal form for the purposes of impact assessment and for this reason must include businesses that are constituted as companies with limited liability (GmbH) or as business partnerships.[23] It also reflects the fact that German company law does not recognise any special legal form for a family company; the family affiliation of the shareholders is entirely indifferent to the choice of legal form and therefore does not restrict the freedom of choice of those involved. In this respect, the term family company may only be developed independently of a legal form and taking into consideration the characteristics that are inherent in the family affiliation of the company.

III. The term family company and its characteristics

The characteristics of the family company,[24] which will be explored below, do not necessarily have to feed into the term family company to be used within the framework of impact assessment. However, not only do they indicate how a family company differs from a non-family company and why a family company deserves special consideration as part of impact assessment, but they actually enable the development of precise test criteria.

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20 The prevailing opinion suggests, however, that the company must have at least five employees, s. BGH ZIP 2012, 669 m.n. 14 et seq.; for details see Habersack/Henssler/*Habersack*, Section 1 DrittelbG m.n. 17 et seq.

21 Previously *Habersack*, in: Tröger/Wilhelmi, Rechtsfragen, pp. 19, 20; also *Foerster* BB 2019, 1411, 1414.

22 For details, see MünchKommAktG/*Habersack*, Intro. m.n. 9.

23 Generally in this sense *Fleischer* NZG 2017, 1201, 1202; *Foerster* BB 2019, 1411, 1414; *Kalss/Probst*, Familienunternehmen, m.n. 2/23; *Hueck*, Family constitution, p. 15.

24 See also contributions of *Brink* and *Prütting*, in: Lange/Windthorst, Sicherung des Familieneinflusses and contributions by *Kalss* and *Lieder*, in: Vogt/Fleischer/Kalss, Recht der Familiengesellschaften; further *Kalss/Probst*, Familienunternehmen, m.n. 2/1 et seq.; *Fleischer* NZG 2017, 1201, 1202 et seq; *Fleischer* BB 2019, 2819 et seq.; *Foerster* BB 2019, 1411, 1414 et seq.; *Habersack*, in: Tröger/Wilhelmi, Rechtsfragen, p. 19 et seq.; *Lange* BB 2005, 2585 et seq.; *Woywode/Keese/Tänzler* ZGR 2012, 418, 420 et seq.; generally on corporate governance and SMEs *Weller* ZGR 2012, 386 et seq.; *Wicke* ZGR 2012, 450 et seq.; on the aspect of conflict avoidance and conflict solution *Wedemann*, shareholder conflict, p. 85 et seq., 451 et seq.

1. Term

There is agreement on the term family business in principle, but not in relation to all details. In agreement with a relevant proposal at European level[25] the Stiftung Familienunternehmen defines a "family business" as follows:[26]

> *"A company of any size is a family business if:*
>
> 1. *The majority of decision-making rights is in the possession of the natural person(s) who established the company, or in the possession of the natural person(s) who has/have acquired the share capital of the company, or in the possession of their spouses, parents, child or children's direct heirs.*
> 2. *The majority of these decision-making rights are indirect or direct.*
> 3. *At least one representative of the family or kin is formally involved in the governance of the company.*
>
> *Listed companies meet the definition of a family business if the person(s) who established or acquired the company (share capital) or their families or descendants hold at least 25 per cent of the decision-making rights mandated by their share capital.*
>
> *This definition includes family companies which have not yet gone through the first generational transfer. It also covers sole proprietors and the self-employed (provided there is a legal entity which can be transferred)." [our translation]*

First of all, the definition does not depend on the size of the company or the legal form of the legal entity. Rather, in addition to small and medium-sized enterprises of a personalised style (typically with the legal form of a general partnership (OHG), limited partnership (KG) or a limited liability company (GmbH), it includes large stock corporations and large limited partnerships, even if they are listed.[27] The definition only requires that the family members have sufficient influence over the management of the company. In addition to the founders, the term family also includes their spouses, parents and direct or indirect issue; according to this, a number of branches still comprise a family.

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25 European Commission, Final Report, p. 9 et seq.

26 https://www.familienunternehmen.de/en/definition-family-businesses.

27 Previously *Habersack*, in: Tröger/Wilhelmi, Rechtsfragen, p. 20 et seq., also *Foerster* BB 2019, 1411, 1414 et seq.; *Kalss/Probst*, Familienunternehmen, m.n. 7/1 et seq., 7/123 et seq.; *Lange* BB 2005, 2585 et seq.; *Woywode/Keese/Tänzler* ZGR 2012, 418, 421 et seq.; especially on capital market compliance of listed family companies *Oppitz*, in: Vogt/Fleischer/Kalss, Familiengesellschaften, p. 133 et seq.

The influence of the family is demonstrated typically in the voting rights allocated to family members: In closed companies it requires the family members to hold a majority shareholding, while in open companies that make use of the organised capital market[28] and ensure that typically 40 to 60 percent of the voting rights are represented at the general meeting, a shareholding of 20 to 30 percent is aimed at.[29]

It also appears appropriate to include the indirect co-decision rights in addition to the direct co-decision rights of the family, and therefore also the case in which the shareholding rights of family members are placed in an intermediate holding company. On the other hand, the question may be academic as to whether the official participation of at least one representative of the family or the relatives in the management or control of the company is an actual element of a family business or instead a phenomenon that is typically associated with the substantive shareholding of the family. In any case, it would not suffice if the intention were, as demanded at times in the literature,[30] to focus on the participation of the family in management; rather a family company is undoubtedly also assumed where the family places the management of the company in third party hands and simply monitors this – for example, by way of representation on a supervisory or advisory[31] board.[32]

It also stands to reason that even companies that have not yet completed the first generational transfer and – what is frequently the same – companies that are only held by one natural person, are to be regarded as family businesses even in cases where the characteristics of a family business may not be fully developed. In any case, the definition of the term family business should not depend upon the intention of transferring the business to the next generation.[33] The crucial factor is rather that the company is under the major influence of one family; this alone justifies, as a rule, – and this is to be assumed when defining the term – the assumption that the participatory rights will typically pass to the next generation.

After all, the existence of a family company does not assume the predominance in the business of a corporate culture shaped by the family.[34] A certain type of corporate culture may well be present in

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28 This refers to the use of the organised capital market for placing shares; whether the regulated market or the open market is used should be irrelevant.

29 See also in this connection Section 29 (2) of the German Securities Acquisition and Takeover Act (Wertpapiererwerbs- und Übernahmegesetz – WpÜG), which defines "controlling" as holding at least 30 percent of the voting rights in the target company.

30 *Kalss/Probst*, Familienunternehmen, m.n. 2/4; *Lange* BB 2005, 2585, 2586.

31 With respect to the advisory board of the family company, see *Woywode/Keese/Tänzler* ZGR 2012, 418, 431 et seq.

32 In opposition to the requirement for the active participation of the family in management see also *Foerster* BB 2019, 1411, 1415; *Lange* BB 2005, 2585, 2587.

33 However, see *Kalss/Probst*, Familienunternehmen, m.n. 2/27; see also (yet misleading) MünchKommAktG/*Habersack*, Intro. m.n. 9; see also (in justifiable contrast) *Foerster* BB 2019, 1411, 1415.

34 However, see *Woywode/Keese/Tänzler* ZGR 2012, 418, 421 et seq.

companies dominated by one family and sometimes even be set out in a "family constitution".[35] Apart from the fact that the existence of a specific corporate culture is hardly suitable as a legally manageable element of a family business test, it is – as is generally the case with management oriented towards sustainability and caution – a consequence of the characteristics of the family company that the following section describes in detail.[36]

2. Characteristics

For the purposes of a family business test, at issue is not the facts of the family company as outlined above or its individual characteristics. Rather, the considerations behind these facts are important and therefore the circumstances and consequences of a legal and economic nature that are typically associated with them.

a) Ensuring the influence of the family and the quasi-fiduciary nature of the participation

Of paramount importance is the effort undertaken by the family shareholders to ensure their substantial (direct or indirect) influence on the management of the company permanently – and accordingly cross-generationally – and by doing so to prevent the transfer of corporate influence to non-family members.[37] One particular instrument that is used widely for securing influence is the protective association agreement. Such an agreement generally contains far-reaching voting agreements that are intended to ensure the uniform proxy voting of members or a branch of the family, and reciprocal purchase rights and rights of first refusal in addition to put options that are intended to permanently keep the ownership rights in the protective association and therefore in the family or branch of the family.[38] Two landmark decisions of the Second Civil Panel of the Federal Court of Justice (Bundesgerichtshof - BGH) included

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35 For details see *Brink*, in: Lange/Windthorst, Sicherung des Familieneinflusses, p. 9 et seq.; *Fleischer* NZG 2017, 1201 et seq.; *Foerster* BB 2019, 1411 et seq.; *Kalss/Probst*, Familienunternehmen, m.n. 3/21 et seq.; *Prütting*, in: Lange/Windthorst, Sicherung des Familieneinflusses, p. 35 et seq.; *Uffmann* ZIP 2015, 2441 et seq.; *Hueck*, Familienverfassung, passim, in particular p. 59 et seq., 129 et seq.; generally on the special features of the contract between members of the (entrepreneur) family *Röthel*, in: Röthel, Verträge, p. 9, 16 et seq., 37 et seq.

36 See also B.III.2.c).

37 *Artmann*, in: Vogt/Fleischer/Kalss, Familiengesellschaften, p. 195 et seq.; *Bühler*, in: Vogt/Fleischer/Kalss, p. 221 et seq.; MünchKommAktG/*Habersack*, Preface Intro. m.n. 9; *Habersack*, in: Tröger/Wilhelmi, Rechtsfragen, p. 21 et seq.; *Kalss/Probst*, Familienunternehmen, m.n. 4/13 et seq.; *Lange*, in: Lange/Windthorst, Sicherung des Familieneinflusses, p. 95 et seq.; *Lange* NZG 2015, 1249 et seq.; *Prütting*, in: Lange/Windthorst, Sicherung des Familieneinflusses, p. 35 et seq.; *K. Schmidt*, in: Tröger/Wilhelmi, Familiengesellschaften, p. 37 et seq.; *Ulmer* ZIP 2010, 549, 550 f.; *Westermann*, Festschrift Bezzenberger, p. 449 et seq.; on the economic implications of cross-generational "altruism" see *Woywode/Keese/Tänzler* ZGR 2012, 418, 424 et seq. with further references.

38 For details see *Habersack* ZHR 164 (2000), 1 et seq.; *Hoffmann-Becking* ZGR 1994, 442 et seq.; *Westermann*, Festschrift Bezzenberger, p. 449 et seq.; *Zöllner*, Festschrift Ulmer, 2003, p. 725 et seq.

in the Official Collection (Decisions of the Federal Court of Justice in Civil Matters) in particular have made the content of such agreements accessible to the professional world.[39]

The functional comparability of the family company to the family foundation is demonstrated especially in the – quite typical – case where one shareholder who is willing to sell must first give the other members (be it members of his/her own family company or members of the protective association) a put option for the share, and these members are consequently entitled to acquire the share at a price that is below market value.[40] It is generally also evident in the restrictions on the claim to compensation of a shareholder willing to resign;[41] the share takes on the character of a trust property or a fief instead of a fungible economic asset. It should be viewed in the context of shares generally acquired through family membership and by virtue of the law of succession; that is, due to family inheritance and not as the result of deliberate investment decisions and the use of capital.[42] This should naturally not preclude the legitimacy of such agreements.[43] In its "Freudenberg" decision in relation to the recognition of contract amendments agreed by the majority, the BGH recognised the cross-generational interest in the preservation of the family business and ruled that the individual interest of individual shareholders was subordinate to this.[44]

b) Dominant position of self-financing

The effort of family shareholders to secure family influence and to defend it against the exercise of influence by non-family members involves not only the use of protective association agreements but – more or less inevitably – an extensive forfeiture of the inflow of equity through external third parties.[45] This is the case regardless of the legal form of the family company.

Stock corporations may issue preferential shares without voting rights in accordance with Section 139 et seq. of the AktG, thereby increasing their equity without relinquishing the influence of existing

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39 BGHZ 126, 226 – Schutzgemeinschafsvertrag I; BGHZ 179, 13 – Schutzgemeinschaftsvertrag II; in addition MünchKommBGB/*Schäfer*, before Section 705 m.n. 68 et seq.

40 On this subject as well as on the barriers, see BGHZ 126, 226, 230 et seq. – Schutzgemeinschaftsvertrag I.

41 For in-depth details see *Ulmer* ZIP 2010, 805 et seq.; especially on questions about the compulsory portion see *Schauer*, in: Vogt/Fleischer/Kalss, Familiengesellschaften, p. 241 et seq.

42 For in-depth details see *Reuter*, Privatrechtliche Schranken, p. 87 et seq.

43 For details see *Ulmer* ZIP 2010, 549, 556 et seq.; *K. Schmidt*, Gesellschaftsrecht, p. 81 et seq., 116 et seq.; see also BGHZ 126, 226, 230 et seq. – Schutzgemeinschaftsvertrag I, where the admissibility of valuation discounts is limited but fundamental admissibility is not questioned; for a dissenting view, see *Reuter*, Privatrechtliche Schranken, p. 87 et seq.

44 BGHZ 85, 350, 357 et seq.; see also *Ulmer* ZIP 2010, 549, 554; then BGH NJW-RR 1989, 1259, 1260 – Röchling; see also OLG Karlsruhe NZG 2007, 423.

45 *Ulmer* ZIP 2010, 549, 550 et seq.

shareholders. Thus it is anything but coincidental that Porsche Automobilholding SE, Volkswagen AG, BMW AG and Henkel AG & Co. KGaA have issued such shares. However, new issues of preferential shares are rarely found in practice now that investors have learned to appreciate the value of the voting rights inherent in the share and are unwilling to become involved in risk capital without influence. For this reason, the former Fresenius SE assumed the legal form of SE & Co. KGaA in 2011, in connection with the changeover from preferential to ordinary shares. This change ensures the influence of the foundation Else-Kröner-Fresenius-Stiftung required by the foundation's business – even though, owing to capital measures, the foundation only holds 25.1 percent of the capital.

Companies that have different legal forms also have the option of issuing shares without a voting right.[46] Apart from foundation constellations – such as Robert Bosch GmbH, where the foundation Robert Bosch Stiftung holds 92 percent of the capital, but without voting rights – it is more likely to be the exception that investors become involved in an investment in a limited liability company (GmbH) or partnership with virtually no influence.

The lack of acceptance of shares without a voting right combined with the lack of willingness to issue shares with voting rights to external third parties leaves family shareholders to cover the equity needs of the company by subscribing themselves to new shares that have been created by increasing capital or rigorously retaining profits to strengthen the reserves of the company.[47] At the same time, family shareholders must take precautions against an excessive outflow of capital when shareholders leave the company, for instance by introducing restrictions on compensation. Therefore, it is primarily the applicable requirements under company law that are of greater relevance for family companies;[48] as regards the retention of profits specifically, the general conditions relating to income taxes are significant.[49]

Apart from that, even raising external capital is possible only to a limited extent.[50] For instance, the family company will only agree to financing through loans if the creditor waives the co-determination

46 See regarding GmbHs *Schäfer*, GmbH-Geschäftsanteil, passim; regarding partnerships see Habersack/Schäfer/*Schäfer*, OHG, Section 119 m.n. 40 et seq., 66 et seq.

47 On the practical need to retain a substantial portion of the annual profits for the purpose of self-financing see also *Sigle*, Festschrift Rowedder, p. 459, 468 et seq.; for in-depth treatment, see *Claussen* in: Tröger/Wilhelmi, Familiengesellschaften, p. 79 et seq.; see *Hommelhoff* in: Tröger/Wilhelmi, Familiengesellschaften, p. 65, 71 et seq.; for an economic assessment of the distribution of profits in family companies, see *Woywode/Keese/Tänzler* ZGR 2012, 418, 426 et seq.

48 See above at B.II.3.a).

49 See also at C.II.5.

50 European Commission, Final Report, p. 14: "Reinvestment of profits plays an important role in the capitalisation of family firms. The debt-equity ratio of family companies is often lower than non-family firms."

rights that are customary within the framework of a[51] covenant. The issuing of convertible bonds – which has been very popular for a long time now – is not an option for family businesses because they would give convertible bond creditors the right to convert their claims into company shares and in so doing to become company shareholders.

Ultimately, family shareholders pay a high price for striving to ensure their influence over the company across generations: Financing is primarily their responsibility and is carried out in particular through the inflow of new equity capital and where applicable by retaining profits;[52] the purchase rights of the co-shareholders and restrictions on compensation claims serve to avoid an excessive outflow of capital in the event of a shareholder resigning, which justifies the above-mentioned quasi-fiduciary nature of the share – generally acquired through family inheritance and without any investment – and which must be understood as a contribution on the part of the shareholders to the self-financing of the company.

c) Conclusions

Family companies are rightly said to have a strong sense of sustainability, management that is focused on the principle of prudence, extensive identification of the shareholders with the corporate goals, a strong connection between the company and its location and the existence of a corporate culture shaped by the family.[53] However, these phenomena are ultimately more or less inevitable consequences of the cross-generational character of the entrepreneurship and the associated focus on self-financing. In particular, restrictions on disposals and compensation that disadvantage shareholders wanting to leave the company are the downside of a situation in which shares are acquired on the basis of family inheritance and without investment expenditure, and are therefore an expression of the quasi-fiduciary nature of the shareholding. The "Three-Circle Model" of *Tagiuri/Davis*[54] expresses the close connections between family, shareholder position and company that shape family companies, and it goes without saying that a family business test also draws its legitimacy from the consequences described above. In terms of design, however, such a test has to be aligned first and foremost with the structural features upstream of the effects – the cross-generational nature of the business, the special features of company financing and the quasi-fiduciary nature of the share.

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51 Also BGH ZIP 2009, 1273 m.n. 16; *Habersack* ZGR 2000, 389, 395 et seq.; for in-depth treatment, see *Servatius*, Gläubigerschutz, passim.

52 See also at C.II.5.

53 Austrian Institute for SME-Research, Overview of Family Business Relevant Issues, p. 2 et seq.; *Habersack*, in: Tröger/Wilhelmi, Rechtsfragen, p. 21 et seq.; *Woywode/Keese/Tänzler* ZGR 2012, 418, 421 et seq.; on "family constitutions" see III.1 with references in footnote 35.

54 *Tagiuri/Davis*, Family Business Review 1992, 43, 49; see also *Uffmann* ZIP 2015, 2441, 2444; *and Foerster* BB 2019, 1411, 1414 with further references.

C. Key regulatory areas in a family business test

I. Overview

German law does not provide for a specific legal form for the family company, not does the definition of a family company depend either on the size of the business or on the legal form of the legal entity.[55] Against this backdrop, virtually all provisions in company law – and, with them, areas of civil law – and general tax conditions are of particular relevance for family companies because family shareholders rely on finding a legal form that is appropriate for their specific needs. In general the legislator – and the same applies to decisions of the BGH[56] – does not refer explicitly to the concerns and special characteristics of family companies, but assumes that companies will find a suitable framework for themselves within the general rules. This assumption does not apply across the board, of course. A number of examples of statutory provisions are set out below that are more or less successful from the point of view of family companies, and they offer a basis for developing criteria[57] that are relevant to a family business test (with recourse to the characteristics of family companies) and thus a type of guideline for the legislator.

II. Selected legislation and decisions that are relevant to family companies

1. Corporate governance relating to the listed company

a) Period of restriction for listed companies (Section 100 (2) sentence 1 no. 4 of the AktG.

Section 100 (2) sentence 1 no. 4 of the AktG is one of the provisions that takes into consideration the interests of family companies with the legal form of a listed stock corporation[58] or limited partnership. According to this, a person may not become a member of the supervisory board if s/he was a member of the management board of the same listed company in the course of the past two years unless s/he is elected through nomination by stockholders holding more than 25 percent of the voting rights in the company. The purpose of the provision is to take account of the – not unfounded – fear

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55 See at B.III.1.

56 One exception is, for example, the "Freudenberg" decision of the BGH (BGHZ 85, 350), in which the Second Civil Panel in connection with the recognition of majority clauses, including those concerning contractual amendments in general and company conversion in particular, referred to the circumstance that the shareholders "wish to take into consideration in particular the fact that in the case of far more than 100 (in the meantime 145) shareholders domiciled abroad – even if they do belong to the same family – one cannot rely upon overcoming differences of opinion about whether and how articles of association may be amended, or upon ultimately reaching an acceptable contractual compromise" (BGHZ 85, 350, 358) [our translation]. In addition, the Civil Panel considered the "character of the family company" to be majority-proof (BGHZ 85, 350, 360); for further details see *Ulmer* ZIP 2010, 549, 553 et seq. The problem of a special law tailored to large family partnerships has been largely resolved, in any case, with regard to the recognition of majority clauses, see BGHZ 203, 77 and also MünchKommBGB/*Schäfer*, Section 709 m.n. 81 et seq. (90 et seq.).

57 At D.

58 The SE is on a par with the AG.

> "that the former member of the board could hinder the new board and prevent the correction of strategic errors or the elimination of irregularities arising from his/her own time on the board."[59]

We will leave aside the question, which is of no consequence in the above context, as to whether the provision, insofar as it refers to all members of the supervisory board and not only to its chair and where applicable also to members of the audit committee, sufficiently solves the conflict of objectives between the demand for independent supervisory board members and efforts to professionalise the supervisory board and the need to improve advisory and monitoring quality.[60] Even so, it is worth noting that the legislator quite rightly considered it unreasonable to prohibit the appointment of a former member of the board as a member of the supervisory board, if

> *"the main shareholders (e.g. family shareholders, foundation) are of the opinion [. . .] that they do not wish to do without the knowledge and ability of a deserving member of the board."*[61]

It cannot be assumed from these legislative considerations that the possibility of overcoming the appointment obstacle by means of a proposal from shareholders whose shareholdings account for more than 25 percent of the voting rights would be limited to family companies and other comparable companies.[62] However, the legislator evidently allowed itself to be guided by the circumstances of the family company. In actual fact it would then be entirely inappropriate for a family company to ignore such a shareholder proposal (which would then be followed by a resolution of the general meeting, the exercise of the right of appointment or appointment by judicial order, if the former member of the board were to become a member of the supervisory board). This applies not only where a family shareholder him/herself was a member of the board and now wishes to retire to the supervisory board but also in cases where the candidate is an external third party who had managed the business of the company to the satisfaction of the family shareholders and whom the family shareholders have now selected as the professional overseer of the new management at the company.

b) Gender quota (Section 96 (2) AktG)

Since the start of 2016, the gender quota rule provided for in Section 96 (2) of the AktG has applied to stock corporations and partnerships limited by shares that are listed and are at the same time subject to parity co-determination as provided for by the Act on the Co-Determination of Employees, the Act on the Co-Determination of Employees on the Supervisory Boards and Management Boards of Companies

59 Grounds for the proposed resolution of the Bundestag Legal Affairs Committee, BT-Drs. 16/13433, p. 11; see also OLG Stuttgart ZIP 2017, 671, 675 [our translation].

60 For more details on this discussion and further references see MünchKommAktG/*Habersack*, Section 100 m.n. 40.

61 Grounds for proposed resolution of the Bundestag Legal Affairs Committee, BT-Drs. 16/13433, p. 11 [our translation].

62 MünchKommAktG/*Habersack*, Section 100 m.n. 45 with further references.

in the Mining and Iron and Steel Producing Industries (Gesetz über die Mitbestimmung der Arbeitnehmer in den Aufsichtsräten und Vorständen der Unternehmen des Bergbaus und der Eisen und Stahl erzeugenden Industrie - Montan-MitbestG) or the Act to supplement the Act on the Co-Determination of Employees on the Supervisory Boards and Management Boards of Companies in the Mining and Iron and Steel Producing Industries (Gesetz zur Ergänzung des Gesetzes über die Mitbestimmung der Arbeitnehmer in den Aufsichtsräten und Vorständen der Unternehmen des Bergbaus und der Eisen und Stahl erzeugenden Industrie - MontanMitbestErgG). Accordingly, the supervisory boards of such companies have to consist of at least 30 percent women and at least 30 percent men.[63] Pursuant to Section 96 (2) sentence 6 of the AktG, any election of members to the supervisory board and any appointment to the supervisory board that is in violation of the requirements of gender quota is null and void;[64] the place reserved for the under-represented gender therefore remains vacant.[65]

In Germany, approximately 100 companies are subject to the above-mentioned legislation on gender quotas, and they include family companies. Both genders have always held positions of corporate responsibility in family companies. It is primarily the members of the owner families who are active in management and supervisory boards, regardless of their gender. Not least for this reason, a statutory gender quota (whose constitutional compliance is incidentally entirely in doubt[66]) can lead to considerable internal disruption in such companies, as it intervenes extensively in the independence of the shareholders. This can occur where one or more places on the supervisory board has to be filled from the group of shareholders but there is no suitable candidate of the under-represented gender in the family. In addition, if the management board is controlled by non-family members and the supervisory board has parity of co-determination, surprising majorities can arise against the owners. It can be just as problematic where, due to the gender quota, the designation rights in a business managed by a number of family branches is in dispute because the family branch to be designated does not have a qualified member of the under-represented gender. This situation threatens the very carefully balanced parity of the family branches in the board. Ultimately, shareholders will be prevented from being represented on the supervisory board, at their own request, by a person of the opposite sex.

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63 Pursuant to Section 96 (3) of the AktG, the same applies to listed companies formed from a cross-border merger that are subject to the Act on the Co-Determination of Employees in Cross-Border Mergers (Gesetz über die Mitbestimmung der Arbeitnehmer bei einer grenzüberschreitenden Verschmelzung - MgVG). Sections 17 (2) and 24 (3) of the German SE Implementation Act (SE Ausführungsgesetz) provide for a similar gender quota in the case of listed companies that have the legal form of an SE and whose supervisory and administrative boards comprise the same number of shareholder and employee representatives.

64 For companies that are subject to the MgVG, the legal consequence referred to in the text arises from Section 96 (3) sentence 2 AktG in conjunction with Section 96 (2) sentence 6 AktG; in the case of companies with the legal form of an SE, Section 96 (2) sentence 6 AktG applies on the basis of the reference provision of Article 9 (1) lit. c ii SE Regulation.

65 Referred to as the “empty chair”.

66 For details see *Habersack/Kersten* BB 2014, 2819 et seq.

2. Shareholder succession

a) Succession of the partnership share

One of the most outstanding landmark decisions of the Second Civil Panel of the BGH on the law of partnerships is the judgment of 10 February 1977.[67] In its decision, the Panel had a practical and interesting response[68] to the question – only regulated to a limited degree in Sections 131 (3) sentence 1 no. 1 and 139 of the German Commercial Code (Handelsgesetzbuch HGB) and Section 727 of the German Civil Code (Bürgerliches Gesetzbuch BGB), and of great significance precisely for family companies – of the inheritance of the shares of a personally liable shareholder in a partnership.[69] The details are not important in the present context. Nonetheless, it is important to point out that in the event of the death of a shareholder, the interests of the company (family company or other) are not served either by dissolving the company or by not replacing the deceased; while the dissolution of the company would result in liquidation, the failure to replace the deceased shareholder would burden the company in terms of the compensation obligation vis-à-vis the heirs. Rather, the BGH's solution is fair to the parties involved – and not just from the company's viewpoint[70]. At its core, it consists of (i) interpreting the succession clause in the articles of association such that the share is hereditary and that it transfers to the successor mentioned in the clause provided the successor is also an heir, and (ii) in the case of a qualified succession clause, accepting the direct acquisition of the share in its entirety by the successor named in the clause (once again, inheritance assumed) and in this way ensuring a smooth succession that will spare the company the burden of compensation.

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67 BGHZ 68, 225, 235 et seq; for further details see MünchKommBGB/*Schäfer*, Section 727 m.n. 28 et seq. with further references. See also öOHG NZG 2019, 904 m.n. 63 et seq.: Violation of moral principles of a succession clause in the articles of association that discriminates against the gender of a potential successor.

68 The privileged treatment under inheritance law of company assets and shares in stock corporations as provided for in Section 13a et seq. of the German Inheritance and Gift Tax Act (Erbschaftsteuer- und Schenkungsgesetz – ErbStG) is well intentioned. However, it is problematic that Section 13a (3) and (6) ErbStG makes an exemption under Section 13a (1) ErbStG dependent on the maintenance of payroll levels and on the non-disposal of the share, and in so doing cements the relationships of the company concerned for years to come. The matter pursued here is clear. Indeed, if one considers that the problem of inheritance tax relates to company assets and share ownership primarily at the level of the tax rates to which taxpayers in tax category I are subject, it appears more efficient – and preferable in terms of the bottom line for family companies – to forego inheritance tax privileges and exemptions entirely and, in opposition to the associated widening of the assessment basis, to lower the tax rates to a level that is reasonable from a company assets perspective.

69 The decision of the BGH is indeed significant for the limited partner's share. Section 177 HGB provides for the succession of the heirs in the absence of a provision in the articles of association, meaning that there is no threat of a dissolution or the emergence of a compensation obligation; however, the succession of a majority of heirs can only be countered by means of a qualified succession clause within the meaning of BGHZ 68, 225, 235 et seq.

70 One should not ignore the fact that the solution developed by the BGH obligates the successor to undertake value equalisation towards his/her co-heirs, insofar as the share value exceeds the share of the value of the estate; see BGHZ, 68, 225, 238 et seq.

b) Succession of the GmbH share

While the legal situation in the event of the death of a GmbH shareholder differs initially from that of a shareholder in a partnership, Section 15 (1) of the German act on limited liability companies (Gesetz betreffend die Gesellschaften mit beschränkter Haftung – GmbHG) provides that the business shares may be disposed of and inherited. The interests, however, are identical to those of a partnership: typically, the GmbH shareholders wish to avoid both compensation from the company for the heirs of the deceased shareholder and the uncontrolled interference of one or more of the heirs in the company. This interest cannot be met by a qualified succession clause, but is met through transfer clauses in the articles of association that obligate the heirs to transfer the share to a specified successor; the point of the transfer obligation in the event of the death of the shareholder is honoured, according to the prevailing opinion, by recognising clauses that exclude compensation or remuneration.[71]

3. Third-party administration of the share

The third-party administration of the share throws up some difficult questions. While the substantive issues raised by the appointment of an executor or administrator of the estate can largely be considered clarified,[72] in practice, questions arise again and again relating to the appointment of a legal guardian for a shareholder who is a minor as well as to the appointment of a custodian; for example, the circumstances under which the exercise of shareholder rights requires the involvement of a counterpart custodian or counter legal guardian or the approval of the family court.[73] Also associated with legal uncertainty is the granting of an enduring power of attorney preventing the appointment of a custodian within the meaning of Section 1896 (2) sentence 2 of the BGB; in this case, the question of whether an extensive enduring power of attorney is compatible with principles under company law is joined by the question of the extent of the powers of the authorised representative and sanctions in the event of misconduct.[74] Such legal uncertainty is all the more significant as the final stage of appeal – subject to appeal in accordance with Section 77 of the German Act on Proceedings in Family Matters and in Matters of Non-contentious Jurisdiction (Gesetz über das Verfahren in Familiensachen und in den Angelegenheiten der freiwilligen

71 For further details on the matter see Habersack/Casper/Löbbe/*Löbbe*, GmbHG, Section 15 m.n. 13 et seq., 18 et seq. See in this context also OLG Karlsruhe NZG 2007, 423: Effectiveness of a provision in the articles of association according to which the shareholder by marriage, in the event of divorce, is required to transfer the business share received from the spouse without consideration, at his or her choice and free of charge, to the latter or the children in that branch of the family.

72 See regarding partnership share Habersack/Schäfer/*Schäfer*, OHG, Section 139 m.n. 37, 57 et seq.; regarding the GmbH share Habersack/Casper/Löbbe/*Löbbe*, GmbHG, Section 15 m.n. 31 et seq.

73 For more details on the custodianship of standing shareholders see *Schäfer* ZHR 175 (2011), 557, 560 et seq.

74 For more details on the enduring power of attorney see *Schäfer* ZHR 175 (2011), 557, 560 et seq.

Gerichtsbarkeit - FamFG)[75] – is the OLG[76], so that uniform, country-wide interpretation is not guaranteed. Without having to describe and treat these questions here in detail, the above-mentioned institutions highlight the considerable relevance of what are presumed to be peripheral areas of law for companies in general and family companies in particular. The legislators should bear this relevance in mind if they are considering revising the law on custodianship in particular.

4. Disclosure

a) Financial reporting

It was noted in the introduction[77] that European accounting law provides for many forms of relief for micro-enterprises and for small and medium-sized enterprises. However, they do not take account of the special features of family companies; they are simply characteristic of general SME policy. Given the obligation regulated in Article 14 lit. f of the Directive on certain aspects of company law[78] in conjunction with Article 30 et seq. of the EU Accounting Directive[79] on the disclosure of single-entity and consolidated financial statements (consisting of the balance sheet, the income statement and the notes), the management report and the group management report, European law – and consequently German law under Section 325 et seq. of the HGB – indeed requires large stock corporations and large atypical partnerships[80] and, with certain restrictions, medium-sized stock corporations and medium-sized atypical partnerships to meet disclosure obligations. These obligations go much further than the corresponding obligations under US law[81] for instance. Ultimately they rigorously dissolve the tension between competition and an interest in information on one side and, on the other, the interests that companies subject to disclosure obligations have in protecting their business secrets – and do so to the detriment of the protection of confidential information.[82] This is particularly true given that, according to the case law of the CJEU,[83] the application to enforce disclosure required under the German law at the time could

75 The BGH is responsible in this case; see Section 133 of the German Courts Constitution Act (Gerichtsverfassungsgesetz – GVG).

76 See Sections 72 (1), 119 (1) GVG.

77 At A.III.2.

78 Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017, OJ EU, 30 June 2017, No L 169/46.

79 See footnote 13.

80 Within the meaning of Section 264a of the HGB.

81 Rightly emphasised by *Schön*, Festschrift K. Schmidt, 2019, p. 391, 397 et seq.

82 On this issue see the contributions of *Wartenburger, Cordewener, Eßbauer* and *Schön* in: Schön, Rechnungslegung und Wettbewerbsschutz, p. 49 et seq., 105 et seq., 287 et seq., 563 et seq.

83 CJEU decision from 23/09/2004 – C-435/02, C-103/03, Slg. 2004, I-8663 – Axel Springer; previously CJEU, decision from 04/12/1997 – C-97/96, Slg. 1997, I-6843 – Daihatsu.

also be made by the competitors of a company subject to disclosure obligations, thus recognising the legitimate interest of private persons in published information.

It is evident that family companies are especially impacted by this far-reaching disclosure regime, since the documents to be disclosed allow conclusions to be drawn about shareholding structures and profit shares of family shareholders that are typical for companies subject to disclosure obligations.

b) Transparency register

In addition to the obligation to publish annual financial statements and a management report, companies are also obliged to disclose a substantial amount of other trade, corporate, capital market and fiscal information. This is not the appropriate place to present these obligations in detail or to examine their specific relevance for family companies.[84] However, the most recently adopted implementation of the Fifth EU Anti-Money Laundering Directive (AMLD) of 30 May 2018 must be mentioned.[85] With the implementation act of 12 December 2019,[86] the German legislator has complied with the obligation arising from Article 30 (5) lit. c) of the AMLD, at any rate[87] with regard to making "the name, month and year of birth, the country of residence and the nationality of the beneficial owner and the type and extent of the economic interest" available for "all members of the public."[88] With this, the previous requirement of a legitimate interest in the inspection no longer applies and private third parties may now inspect the notifiable data without the notifier becoming aware of the inspection.[89] In conjunction with the financial reporting that requires disclosure[90] and subject to a blocking order pursuant to Section 23 (2) sentence 2 no. 1 of the German Act on Tracing Profits from Serious Criminal Offences (Gesetz über

84 Commendable inventory at *Schenke/Teichmann*, Publizitätspflichten von Familienunternehmen, 2018, p. 19 et seq.; see also *Windthorst*, in: Aspekte der Unternehmenstransparenz, 2019, p. 61 et seq.; especially on "shame sanctions" *Nettesheim*, Öffentlichkeit als Unternehmenssanktion, 2019, p. 13 et seq.

85 Directive (EU) 2019/843 of the European Parliament and of the Council of 30/05/2018 to amend Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing and to amend Directives 2009/138/EC and 2013/36/EU, OJ no. L 153/43 of 19 June 2018.

86 Act on the Implementation of the Amending Directive to the Fourth EU Anti-Money Laundering Directive of 12 December 2019, I p. 2602.

87 Article 30 (5) AMLD permits the Member States to provide for access to additional information that allows for the identification of the economic owner and, in compliance with data protection legislation, includes at least the date of birth or the contact data.

88 For details see *Assmann/Hütten* AG 2017, 449, 453 et seq.

89 For details see *Schenke/Teichmann*, Publizitätspflichten von Familienunternehmen, 2018, p. 45.

90 In addition at C.II.4.a).

das Aufspüren von Gewinnen aus schweren Straftaten - GwG), the transparency register will in future allow for any private third party to determine the income and asset situation of notifiable shareholders.[91]

Even if one assumes that the new legislation is compatible with union and constitutional law,[92] the justified confidentiality interests of those concerned remain largely unconsidered. It is clear that the shareholders in family companies are particularly impacted by the new legislation, especially considering the fact that "Exercising control in other ways" within the meaning of Sections 3 (2) sentence 1 no. 3, 19 (3) no. 1 lit. b) of the GwG is interpreted as broadly as possible and, in the case of family companies, covers common agreements under the law of obligations, such as agreements between shareholders and family members who do not hold the formal position of shareholder.[93]

5. Financing

The characteristics of a family company include, as set out here in detail, the reliance of the company on self-financing by the company, be it through the retention of profits or through the inflow of new capital from the family shareholders. Furthermore, German company law provides for companies of any legal form to issue shares without voting rights and therefore to accept equity from external third parties without diluting the influence of the family.[94] The restriction of the volume of preferential stock equity under the AktG to half of the share capital (Section 139 (2) of the AktG) is likely to be acceptable to family companies too, particularly since non-voting shares are no longer as easily placed on the market for risk capital as in the past. Nonetheless, it is to be welcomed that the amendment to the AktG introduced in 2016[95] – even though it was primarily intended to comply with bank supervisory requirements relating to the recognition of regulatory core capital – made the mandatory subsequent payment of an advance or additional dividend subject to the articles of association[96] and consequently rendered the equity financing of the stock corporation more flexible.

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91 *Schenke/Teichmann*, Publizitätspflichten von Familienunternehmen, 2018, p. 100 et seq.; see also *Windthorst*, in: Aspekte der Unternehmenstransparenz, 2019, p. 68.

92 Negating constitution and union law compliance, specifically regarding the comprehensive right of inspection with substantial considerations, see *Schenke/Teichmann*, Publizitätspflichten von Familienunternehmen, 2018, p. 73 et seq. (100 et seq.); *see also Windthorst*, in: Aspekte der Unternehmenstransparenz, 2019, p. 68 et seq.

93 For this reason, *Kinzl/Reuter* BB 2019, Heft 49, p. I, call for the exercise of control to be specified in some other way; for more details on this matter see *Assmann/Hütten* AG 2017, 449, 456 et seq.

94 Details at B.III.2.b).

95 Act to Amend the German Stock Corporation Act (Amendment to Stock Corporation Act 2016) of 22 December 2015, BGBl. I p. 2565.

96 See Sections 139 (1) sentence 3, 140 (2) AktG and in addition Hüffer/*Koch*, AktG, Section 139 m.n. 12 et seq.

From the point of view of family companies, it is indeed a disadvantage that the cost of external capital and therefore the cost of interest in particular are basically operating costs:[97] Insofar as family companies – as part of the desire to secure the influence of the family – finance the company through the inflow of new equity and the retention of profits, they do not reap the tax benefits of external capital, which in turn is a competitive disadvantage vis-à-vis non-family companies. Through Section 34a of the German Income Tax Act (Einkommensteuergesetz - EStG) created within the framework of the German Corporate Tax Reform Act 2008 (Unternehmensteuerreformgesetz 2008), the legislator attempted to give privileged treatment, for income tax purposes, to profits that are not withdrawn, and in this way to grant a reduction to the taxable person "who continues to make the generated capital available to the business by foregoing the private use of the capital and in so doing strengthens the equity basis of the business", and in addition to improve investment options "without the need for the use of external capital".[98] However, this measure was less than successful. The legislator assumed that the reduction would contribute to a permanent decrease in the external equity ratio of the companies, but this has not proven to be the case; in actual fact, the reduction has not been used as expected[99] by 90,000 companies, but by substantially fewer companies.[100]

This lack of acceptance should of course not be misinterpreted: in particular from the point of view of family companies relying on self-financing, there is still a considerable structural interest in the income tax-related reduction of retained profits. The legislator should take the real findings as an opportunity to improve the preferential treatment of the retention of profits.[101]

6. Mobility of the company and the shareholders

Despite the fact that family companies generally demonstrate a firm attachment to their registered locations,[102] they too are interested in and reliant upon using the options made available by general company law and the German Transformation Act (Umwandlungsgesetz - UmwG) for reorganisation and relocation of the registered office, even if only with reference to group companies.

Large family businesses in particular are in international competition and operate globally, and family shareholders require mobility as well. Brexit has drawn attention to a situation that is apparently not

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97 For further details see Habersack/Mülbert/Schlitt/*Breuninger/Frey*, Unternehmensfinanzierung, Section 19 m.n. 8 et seq.

98 Explanatory memorandum to government draft, BT-Drs. 220/07, p. 101 [our translation].

99 Explanatory memorandum to government draft, BT-Drs. 220/07, p. 62.

100 See response from the Federal Government, BT-Drs. 19/6308, p. 7 (2012: 6,762 companies; 2013: 6,431 companies; 2014: 6,271 companies).

101 For in-depth treatment see *Hey*, Belastung thesaurierender Personenunternehmen, 2020.

102 See above at B.III.2.c).

seldom of concern for family companies, namely relocation tax pursuant to Section 6 of the German Foreign Tax Act (Gesetz über die Besteuerung bei Auslandsbeziehungen - AStG) that will be imminent on expiry of the transition period. The starting point is the deferral provided for in Section 6 (5) of the AStG, the scope of which is limited to EU and EEA matters, and which, once Brexit has been implemented, will no longer apply to relocation situations; in the case of relocation that has already been executed it is possible that a previously approved deferral may be withdrawn.[103] The issues surrounding relocation taxation generally, the consequences associated with it in the event of Brexit and the need in any case to reform the entire system need not be developed in detail here[104] in order to demonstrate the serious consequences for the liquidity of family shareholders and perhaps even family companies themselves of the legislator imprudently abolishing a scheme that is beneficial to the taxable person.

103 *Kudert/Hagemann/Kahlenberg*, Die Internationalisierung der Unternehmerfamilie, 2017, p. 95 et seq.

104 For in-depth treatment see *Kudert/Hagemann/Kahlenberg*, Die Internationalisierung der Unternehmerfamilie, 2017, p. 9 et seq., 27 et seq.

D. The family business test in detail

I. Starting point of the design

Given the term family company as developed here and the legal and economic characteristics that lie behind that term, the foundations have been laid for developing criteria for the family business test which may be used as an instrument for impact assessment both at national and European levels. The test criteria thus have their origin in both the cross-generational nature of the enterprise and the associated focus on self-financing itself and in the limitations on disposal and compensation to the detriment of shareholders willing to resign. These limitations represent the downside of a situation in which the share is typically acquired through family-related inheritance and without investment expenditure, and are therefore an expression of the quasi-fiduciary nature of the share.

The test must aim to identify the burden on family companies arising from proposed legislation – and therefore the specific impact on family companies – and in this way to enable the legislator, based on reasonable information, in this case the full knowledge of any possible burden on family companies, to adjudicate on the implementation of the proposed legislation.

II. Key issues

1. Corporate governance factors

Are family companies particularly impacted by legislative proposals relating to corporate governance at the company?

One example – in addition to the gender quota provided for in Section 96 (2) of the AktG – is Section 100 (2) sentence 1 no. 4 of the AktG, which is inappropriate for family companies simply because it provides for the possibility of the requirement of a qualifying period being rescinded on the proposal of shareholders holding over 25 percent of voting rights.

2. Succession

Are family companies particularly impacted in terms of succession?

Beyond the considerable legal uncertainty that exists in connection with custodianship and the enduring power of attorney preventing custodianship, the sparse ruling on the inheritance of OHG and KG shares may serve as an example. It is inappropriate for family companies merely due to the fact that in the case law of the BGH, principles were developed which, in practice, allow for the embedding of specified successors (assuming they are heirs) in the company, while avoiding both the dissolution of the company and the burden of compensation obligations.

3. Third-party administration of the share

Are family companies particularly impacted in terms of the regulatory situation for third-party administration of the company share?

The execution of wills, the administration of estates, legal guardianship, custodianship and enduring powers of attorney that prevent custodianship are all integral parts of daily life in family companies. Legislators should consider the substantial relevance of these and other supposedly peripheral legal issues for family companies if they intend to tackle reforms, for example, in custodianship law.

4. Disclosure obligations

Are family companies particularly disadvantaged by disclosure and transparency obligations and the associated relativising of the interests of companies subject to disclosure requirements in the protection of their business secrets?

In this case, reference is made to the implementation of Article 30 (5) lit. c) AMLD, which removed the previously applicable requirement of a legitimate interest for the inspection of the transparency register. In conjunction with the financial reporting that has to be disclosed and subject to a blocking order pursuant to Section 23 (2) sentence 2 no. 1 of the GwG, the transparency register will in future allow for any private third party to determine the income and asset situation of company shareholders required to disclose this information.

5. Financing

Are family companies particularly affected when it comes to financing their businesses?

The cross-generational character of the family company and the more or less inevitable inherent endeavour to secure the family influence require – *de lege lata* guaranteed across all legal forms – that such companies be able to accept equity without granting influence. Furthermore, it is important to consider that family companies are dependent on self-financing by the shareholders. Consequently, the tax deductibility of the costs of financing the company through external capital have less of an impact than is the case with non-family companies; this should be taken into consideration through amendments within the framework of Section 34a of the EStG.

6. Mobility of the company and of the shareholders

Are family companies particularly impacted in terms of their own mobility and that of their shareholders?

As an example, reference is made to relocation taxation under Section 6 of the AStG and its possible revival in the course of Brexit.

III. Embedding in existing instruments for impact assessment

1. The national level

At national level, the still-to-be-written "Guidelines for the Consideration of the Interests of Family Businesses in Impact Assessment (Family Business Test)" should be in line with the SME test in terms of their design. The test should therefore pose the question of whether a review of the interests of family companies should be carried out in the context of the specific legislative proposal. However, while the SME test makes such a review dependent on the financial cost of performing it, it should be carried out for a family business test if family companies are particularly impacted by specific legislative proposals. The specific impact on family companies in turn should be examined on the basis of the specific nature of a family company (that is to say, the cross-generational character of the business, the special features of company financing and the quasi-fiduciary character of the shareholding) first and foremost as regards the legal framework conditions in relation to (i) the corporate governance of the company, (ii) succession, (iii) possible third-party administration of the share, (iv) the disclosure of corporate data and other information, (v) financing the business or (vi) the mobility of the company and its shareholders, and therefore, in the context of the key issues outlined above (at II.).

If it is established that there is a specific impact resulting from a concrete regulatory proposal, then the family business test should ensure that the Federal Ministry for Economic Affairs and Energy and the Federal Ministry for Justice and Consumer Protection are made aware of this within the framework of inter-departmental cooperation. This will enable a joint search for measures leading to the structural equal treatment of family companies and non-family companies (e.g. exceptions, transition periods and exemptions).

2. The European level

At European level, the family business test should be incorporated into the toolbox. From a design point of view it can be positioned with the SME test that is already anchored in the toolbox but which does not reflect the specific characteristics of family companies. As is the case with the SME test, the family business test is intended to have four stages:

In terms of identifying the potential effects of legislative proposals on family companies, which is the first stage of the test, the special characteristics of the family company and the key issues outlined above (at II.) are assumed, as is the case at national level.

If there is at least the possibility of a specific impact on family companies, as a second stage the consultation phase should be initiated – which, in addition to the usual mechanisms for consultation provided for in the toolbox[105] and in harmony with the SME test, can include targeted consultations as part of roundtables and discussion events.

The third stage involves the assessment of legislative alternatives that may be considered in terms of their specific impact on family companies. At issue (in deviation from the SME test) is not merely the cost of regulatory compliance, but generally relevance and impact with regard to family companies – and in each case in comparison with non-family companies.

Finally, the fourth stage considers alternatives and seeks measures that might reduce the specific impact on family companies and allow for a level playing field. Such measures could include (total or partial) exceptions from the scope of application of a legislative act,[106] but also transition periods and exemptions.

105 Tools #53, #54, #55 in the toolbox, accessible at https://ec.europa.eu/info/better-regulation-toolbox_en.

106 At national level for example Section 1 (1) no. 1 sentence 3 DrittelbG; see also at B.II.

E. Conclusions

A family business test is needed – this is the key finding of the considerations presented here. It is not least due to the efforts of family shareholders to secure the influence of the family across generations that these companies have characteristics that clearly set them apart from other companies and can prove to be a disadvantage in competition, and up to now these characteristics have not been included in impact assessment either at German national level or at European level. For this reason, a family business test should be created both at the level of the Member State and at EU level in order to ensure that legislators are aware of any possible specific impact on family businesses (which could involve competitive disadvantages for these companies and an erosion of the family company culture).

In this country, the test is intended to exist alongside the SME test and to be guided conceptually by it. However, what should be investigated is not the financial cost of regulation but, starting with the key issues discussed at D.II, the specific impact on family companies so as to provide for the structural equal treatment of family and non-family companies.

At European level, the test should be included in the toolbox and be aligned with the SME test anchored there, which does not reflect the specific characteristics of family companies. As is the case with the SME test, the family business test should have four stages, namely (i) identification of the potential impact of legislative proposals on family companies (again, on the basis of the key issues outlined at D.II), (ii) if specific impact is identified, introduction of a consultation phase, (iii) assessment of legislative alternatives and (iv) consideration of alternative options and measures with which the specific impact on family companies could be lessened, thereby ensuring a level playing field.

List of abbreviations

AG	Aktiengesellschaft (German Stock Corporation Act)
AktG	Aktiengesetz (German Stock Corporation Act)
AMLD	Anti-Money Laundering Directive
AStG	Außensteuergesetz (German Act on Foreign Taxation)
BB	Betriebs-Berater (management consultancy journal)
BGB	Bürgerliches Gesetzbuch (German Civil Code)
BGH	Bundesgerichtshof (Federal Court of Justice)
BGHZ	Entscheidungen des Bundesgerichtshofs in Zivilsachen (decisions of the German Supreme Court in civil matters)
BT-Drs.	Bundestags-Drucksache (Parliamentary papers from the Bundestag)
Coll.	Collection (collection of decisions of the European Court of Justice)
DrittelbG	Gesetz über die Drittelbeteiligung der Arbeitnehmer im Aufsichtsrat (German Act on One-Third Participation of Employees in Supervisory Boards)
ErbStG	Erbschaftsteuer- und Schenkungsteuergesetz (German Inheritance and Gift Tax Act)
GGO	Gemeinsame Geschäftsordnung der Bundesministerien (Joint Rules of Procedure of the Federal Ministries)
GmbH	Gesellschaft mit beschränkter Haftung (German limited liability company)
GmbHG	Gesetz betreffend die Gesellschaften mit beschränkter Haftung (German act relating to limited liability company)
GKFU	Governance Kodex für Familienunternehmen (governance code for family businesses)
GvG	Gerichtsverfassungsgesetz (German Courts Constitution Act)
GwG	Geldwäschegesetz (German Anti-Money Laundering Act)
lit.	littera
MyVG	Gesetz über die Mitbestimmung der Arbeitnehmer bei einer grenzüberschreitenden Verschmelzung (Act on the Co-Determination of Employees in Cross-Border Mergers)
NKRG	Gesetz zur Einsetzung eines Nationalen Normenkontrollrates (Act on the Establishment of a National Regulatory Control Council)
NJW	Neue Juristische Wochenschrift (weekly legal journal)

NZG	Neue Zeitschrift für Gesellschaftsrecht (journal on company law)
öOGH	Österreichischer Oberster Gerichtshof (Austrian Supreme Court)
OLG	German Higher Regional Court
m.n.	marginal number
SE	Societas Europaea (European Company)
SMEs	Small and medium-sized enterprises
WpÜG	Wertpapiererwerbs- und Übernahmegesetz (German Securities Acquisition and Takeover Act)
ZIP	Zeitschrift für Wirtschaftsrecht (journal for business law)

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