

ECONOMIC STABILITY FUND FOR THE GERMAN ECONOMY

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With its Economic Stabilisation Fund, the German federal government has created a further opportunity to support companies in the real economy impacted by the coronavirus crisis.

"The legislation used the legal and organisational framework previously devised for the Special Fund for Financial Market Stabilisation created during the 2008 financial crisis."

INTRODUCTION

In response to the coronavirus pandemic, the German Parliament (Bundestag), with the approval of the Federal Council (Bundesrat), decided on 27 March 2020 to establish an Economic Stabilisation Fund (Wirtschaftsstabilisierungsfonds – “WSF”). The WSF is intended to provide unbureaucratic financial support on short notice to German companies that have run into economic difficulties and liquidity shortages as a result of the pandemic. To aid the establishment of the WSF at such short notice, the legislation used the legal and organisational framework previously devised for the Special Fund for Financial Market Stabilisation (Sonderfonds Finanzmarktstabilisierung – “SoFFin”) created during the 2008 financial crisis. The WSF has a capitalisation of €600bn.

While the SoFFin was established to support financial services companies during the 2008 financial crisis (prominent examples include Commerzbank, HSH Nordbank and Hypo Real Estate), the new WSF addresses the real economy. Its focus is on companies with a particular importance for Germany as a business location due to their size, the number of their employees or their strategic importance. It complements the programmes of the Kreditanstalt für Wiederaufbau (“KfW”), which has also been set up to deal with the current crisis.

Its broad scope makes the new WSF an important support for companies in all sectors. In addition to sectors particularly affected by the crisis (especially tourism and retail), the WSF should also be of particular interest to operators of critical infrastructure and companies in the transport and energy sectors. The new rules considerably facilitate corporate financing transactions through loans and capital increases with the participation of the WSF. Companies wishing to take advantage of WSF measures should therefore familiarise themselves with the legal framework and possible measures early on, including the requirements and consequences of their use.

The WSF is not available to companies in the financial sector.

LEGAL FRAMEWORK

The legal basis of the WSF is the Economic Stabilisation Fund Act (Wirtschaftsstabilisierungsfondsgesetz – “WStFG”) (Federal Law Gazette – BGBl. 2020 I, p. 543). The WStFG essentially amends and extends the previously mentioned Financial Market Stabilisation Fund Act and consists of two parts: the Stabilisation Fund Act (Stabilisierungsfondsgesetz – “StFG”) and the Economic Stabilisation Acceleration Act (Wirtschaftsstabilisierungsbeschleunigungsgesetz – “WStBG”). These laws partly modify the current regulatory framework for corporate financings in order to enable the swift implementation of stabilisation measures in the WSF.

"The WSF is a special fund without legal capacity that may, however, act in its own name, sue and be sued in legal transactions."

The Federal Ministry of Finance (Bundesministerium der Finanzen – “BMF”) is authorised, together with the Federal Ministry of Economics and Energy (Bundesministerium für Wirtschaft und Energie – “BMWi”), to issue a regulation (“Framework Regulation”) specifying the requirements and legal consequences of the WSF measures.

STABILISATION MEASURES

Overview

The WSF is a special fund without legal capacity (nichtrechtsfähiges Sondervermögen) that may, however, act in its own name, sue and be sued in legal transactions. It is intended to contribute to the stabilisation of the real economy by strengthening the liquidity and capital base of affected companies.

The main instruments that the WSF can use for this purpose are:

- guarantees;
- participation in companies; and
- loans to KfW to refinance special programmes.

There is, explicitly, no legal entitlement to benefit from the WSF. However, when deciding on whether to grant stabilisation measures, the authorities are obliged to exercise their discretion in a legally appropriate manner.

Requirements of Stabilisation Measures

The WSF’s stabilisation measures are granted to a company in the real economy upon application. The application must be submitted to the BMWi, which will then decide on the application together with the BMF. An inter-ministerial committee (“WSF Committee”) decides on fundamental questions, matters of particular importance and on material measures and conditions.

A company in the real economy applying for stabilisation measures must fulfil two of the following three criteria in the last two financial years before 1 January 2020 (based on the definition for SMEs pursuant to Art. 1 of Recommendation 2003/361/EC of the EU Commission):

- balance sheet total exceeding €43m;
- annual turnover exceeding €50m; and
- more than 249 employees (annual average).

These basic requirements are in principle exclusionary, i.e. if a company does not fulfill two of the above-mentioned criteria it is not eligible for funding from the WSF. However, the WSF Committee can exempt individual companies operating in a sector pursuant to Sec. 55 of the German Foreign Trade Regulation (Außenwirtschaftsverordnung – AWV) from these requirements. These are in particular operators of critical infrastructure, software developers to the critical infrastructure sector, telecommunications providers as well as broadcasting and press companies. An exemption requires that the relevant company's significance to the security or economy of the Federal Republic of Germany is comparable to companies meeting the above criteria. In addition, the WSF Committee can decide on state participation in companies that have been valued at a minimum of €50m in a financing round since 1 January 2017 – thus, start-up companies are also eligible.

If the above-mentioned criteria are met, or suspended pursuant to the paragraph before, further requirements must be fulfilled in order to qualify for a stabilisation measure including:

- The company does not have access to any other form of financing. No further guidance in relation to this requirement is provided in the StFG or the materials from the legislative process. One cannot expect a company in difficulty to spend the time and resources required to assess all conceivable possibilities for a bank or capital markets financing before a stabilisation measure can be granted. Whether this requirement will be deemed fulfilled will likely depend on whether, from an objective point of view, there is a realistic chance of a successful financing at reasonable conditions from another source;
- The stabilisation measure must give the company the prospect of being able to continue independently once the pandemic has been overcome (going concern perspective) (Fortführungsprognose);
- The company must not already have qualified as an “undertaking in difficulty” by 31 December 2019. According to 20 of Communication from the Commission 2014/C 249/01, an undertaking is in difficulty when, without intervention by the State, it will almost certainly be condemned to going out of business in the short or medium term. This requirement ensures that only companies that have run into economic difficulties as a result of the coronavirus pandemic will be eligible for a stabilisation measure; and
- The company must have a sound and prudent business policy. Dividend policy and board remuneration can be expected to be among the relevant factors in this respect. The company should also contribute to stabilising supply/production chains and protecting jobs. Specific conditions are likely to be imposed upon companies to ensure compliance with these requirements (in particular by means of the so-called self-commitment declaration – see below).

"Shareholder resolutions violating the self-commitment declaration can be legally challenged."

Via the Framework Regulation, the BMF and BMWi can also establish requirements and conditions for companies receiving support. These additional requirements may *inter alia* relate to the use of funds, further borrowing, board remuneration, dividend policy, the timeline for the fulfilment of these requirements and to measures preventing a distortion of competition. The Framework Regulation may also provide for a self-commitment to these requirements by the management of the relevant company. Any action contrary to this so-called self-commitment declaration is likely to constitute a breach of managerial duties. In return, however, the management is also entitled to implement the contents of the declaration of commitment. Shareholder resolutions violating the self-commitment declaration can be legally challenged. The Framework Regulation may provide for further legal consequences.

In addition to the above-mentioned requirements, the BMWi and BMF should take the following criteria into account in their discretionary decision:

- the importance of the company for the German economy: The main focus here is likely to be on preventing a collapse of supply chains for important consumers and “domino effects”;
- the urgency, i.e. how quickly the relevant company needs liquidity assistance before insolvency becomes imminent;
- the impact on the labour market (i.e. how many employees would be affected by an insolvency of the company) and competition; and
- the principle of efficiency, i.e. the basic principle of public administration, according to which certain objectives are to be achieved with as few resources as possible.



€400BN FROM THE TOTAL VOLUME OF THE WSF IS AVAILABLE TO SECURE THE EXTERNAL DEBT FINANCING OF COMPANIES VIA ITS GUARANTEES.

The StFG also stipulates that stabilisation measures are subject to compatibility with EU state aid law (Art. 107, 108 TFEU). The temporary framework for state aid to support the economy in view of the current outbreak of COVID-19 (Communication of the Commission 2020/C 91 I/01) does, however, *inter alia*, not provide for a recapitalisation (see below). Therefore, recapitalisation measures in particular are likely to come under review by the Commission for compliance with state aid law.

WSF stabilisation measures are only possible until 31 December 2021.

The Individual Stabilisation Measures

a) Guarantees

€400bn from the total volume of the WSF is available to secure the external debt financing of companies via its guarantees. These WSF guarantees are intended to enable affected companies to use the capital and credit markets to obtain the urgently needed liquidity, which they would otherwise not be able to obtain due to their economic situation.

WSF guarantees are to be remunerated appropriately and have a maximum duration of 60 months. Liabilities for which the WSF provides a guarantee cannot be claimed or terminated prematurely by the creditors.

b) Recapitalisation

A WSF recapitalisation can be executed in the form of subordinated debt, hybrid bonds, profit participation rights, silent participations, convertible bonds or an acquisition of shares in companies ("recapitalisation"). €100bn is available for recapitalisations. The debt instruments available for recapitalisation are subordinated and therefore do not have to be accounted for in the over-indebtedness accounts (Sec. 19 para. 2 sentence 2 of the German Insolvency Act (Insolvenzordnung – InsO).

"Any general meeting to decide on a recapitalisation can be convened within the shorter 14-day notice period pursuant to 16 para. 4 of the German Takeover Act."

In contrast to a guarantee granted by the WSF, a recapitalisation by the WSF requires an important interest on parts of the state in stabilising the company and that stabilisation cannot be achieved in any other way. Above all, WSF recapitalisation measures are likely to be relevant for companies which are of particular importance for Germany as a business location. These companies can be expected to include system-relevant companies in the infrastructure, transport and energy supply sectors.

Recapitalisation measures must also be adequately remunerated. The duration of a recapitalisation is not limited.

c) Refinancing of KfW Programs

For completeness, it should also be mentioned that the WSF can grant loans to the KfW to refinance special KfW programmes.

IMPACT ON COMPANY LAW

The WStBG is intended to enable the swift implementation of stabilisation measures under the StFG – in particular, recapitalisations. To achieve this purpose, key provisions of corporate law are modified or even completely suspended. The WStBG replaces the Financial Market Stabilisation Acceleration Act (Finanzmarktstabilisierungsbeschleunigungsgesetz – "FMStBG") and thus also applies to companies from the financial sector to the extent that they have received funds from SoFFin.

In the following we explain the modifications that are particularly important in practice:

AG, KGaA and SE

One important feature of the WStBG for accelerating stabilisation measures is a simplified framework for voting procedures. For stock corporations (AG), partnerships limited by shares (KGaA) and European companies (SE), the adoption of shareholder resolutions in connection with stabilisation measures is facilitated. Majority requirements are reduced, and minority rights are cut back considerably:

- Any general meeting to decide on a recapitalisation can be convened within the shorter 14-day notice period pursuant to 16 para. 4 of the German Takeover Act (Wertpapiererwerbs- und Übernahmegesetz – WpÜG); restrictions on voting proxies under the articles of association are invalid. The shorter notice period, explicitly, also applies if the agenda includes further items (i.e. in addition to the recapitalisation);
- If the recapitalisation is structured as a capital increase, the resolution on the capital increase can be adopted with a simple majority. The regular three-quarter majority is suspended and any deviating provisions of the articles of association are irrelevant;
- The quick acquisition of shares by the WSF via a capital increase regularly requires that the subscription rights of shareholders are excluded. In order to facilitate this complex process under stock corporation law, the majority requirement for the resolution on the exclusion of subscription rights is reduced to two-thirds in deviation from Sec. 186 para. 3 of the German Stock Corporation Act (Aktiengesetz – AktG) (three-quarters majority). If half of the share capital is represented, the exclusion of subscription rights can even be resolved by a simple majority, analogous to the resolution on a capital increase. Due to the quorum presence majorities (Präsenzmehrheiten) of the major shareholders generally existing at German stock corporations, these will usually set the direction. The same majority requirements also apply to a capital reduction, which may be used to cover losses, especially in times of crisis. In addition, the exclusion of subscription rights is always considered permissible and appropriate;
- The issue of new shares at the stock exchange price is also considered appropriate, even if this is lower than the issue price. With the approval of the supervisory board, the management board may even order an issue below the stock exchange price; an issue below par is excluded;
- Resolutions of the general meeting in connection with the measures described above shall become effective upon publication of the resolution on the Company's website or upon publication in the Federal Gazette (Bundesanzeiger). Entries in the commercial register should be made without delay but are not a prerequisite for effectiveness. The action for rescission (Anfechtungsklage) (Sec. 246 AktG) and the associated ban on registration (Registersperre) is therefore not an obstacle to the validity of the resolution. If the action is well founded, the plaintiff has a claim for damages pursuant to Sec. 246 para. 4 AktG, which, however, will not lead to a removal of the resolution of the general meeting. As a result, minority shareholders have no means of preventing a resolution; and
- The exclusion of minority shareholders by the WSF (so-called squeeze-out under stock corporation law according to Sec. 327a para. 1 AktG) is already possible if the WSF holds 90% of the share capital.



**AUTHORISED CAPITAL
(GENEHMIGTES KAPITAL) FOR
RECAPITALISATION CAN BE CREATED
IN UNLIMITED AMOUNTS.**

In particular, shares with preferential rights to profits (Gewinnvorzug), shares with priority in the distribution of the Company's assets or non-voting preferred shares (stimmrechtslose Vorzugsaktien) may be issued as new shares.

In addition, several other measures will facilitate or accelerate the participation of the WSF and the injection of liquidity:

- Authorised capital (genehmigtes Kapital) for recapitalisation can be created in unlimited amounts (cf. in contrast, Sec. 202 para. 3 AktG: 50% of the existing capital). This again requires only a simple majority in the general meeting;
- The WSF can make an advance payment even before the capital increase resolution, which is then assigned to its obligation to make a contribution. This ensures a rapid inflow of liquidity; and
- Shares issued to the WSF with preferential rights to profits automatically lose these rights when the shares are transferred to a third party. The WSF may determine that preference shares are converted into (voting) ordinary shares upon transfer.

Until 31 December 2021, the management board can also decide, with the approval of the supervisory board, on the issue of profit participation rights and subordinated bonds to the WSF (without subscription rights of shareholders). The approval of the general meeting is only required if the instrument in question provides for a right of the WSF to (subsequently) convert the instrument into shares. In this case, the simplifications already mentioned in connection with the capital increase apply to any necessary resolutions of the general meeting. The issue of profit participation rights and bonds to third parties is also possible under the simplified conditions if the WSF provides a guarantee for this.

"For the first time, the WStBG also allows a squeeze-out for the GmbH against compensation if this is necessary for the success of the stabilisation measure."

GmbH

In limited liability companies (GmbH) too, measures under company law are considerably simplified insofar as they are connected with stabilisation measures:

- The decision on a capital increase, a capital reduction or the creation of authorised capital (if necessary including the exclusion of subscription rights) in the context of a recapitalisation only requires a simple majority of the votes present at the shareholders' meeting, whereby deviating provisions in the articles of association are irrelevant;
- In deviation from Sec. 48 para. 2 of the Limited Liability Companies Act (Gesetz betreffend die Gesellschaften mit beschränkter Haftung – GmbHG), voting in the shareholders' meeting is also possible in writing or in text form even if not all shareholders agree to this form of voting;
- For the resolution to become effective, what has been said about the AG applies accordingly. In particular, no entry in the commercial register is required, but only a notification on the company website; and
- For the first time, the WStBG also allows a squeeze-out for the GmbH against compensation if this is necessary for the success of the stabilisation measure. The squeeze-out requires a three-quarters majority of the votes present.

In accordance with the rules for the AG, the management may also issue profit participation rights and subordinated bonds without the approval of the shareholders' meeting.

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The decision on whether to accept the WSF as a limited partner of a (GmbH & Co.) KG requires only a simple majority in the partners' meeting. Conflicting provisions in partnership agreements and other shareholder agreements are irrelevant.

Silent Participation

The WStBG also facilitates participation in companies as a silent partner:

- If the WSF (or a third party) participates in the struggling company as a silent partner on a recapitalisation, the agreement on the asset contribution does not give rise to an inter-company agreement within the meaning of Secs. 291, 292 AktG. Consequently, no approval by the general meeting or entry in the Commercial Register is required;
- The agreement can also grant a subscription or exchange right for/to shares – excluding the subscription right of shareholders. This requires the approval of the general meeting with the reduced majority requirements described above for the exclusion of subscription rights; and
- In order that the subscription or conversion rights of the silent partner can be satisfied, conditional capital (bedingtes Kapital) can be created specifically for this purpose.

IMPACT ON OTHER AREAS OF LAW

The company law simplifications described above for the rapid implementation of stabilisation measures are flanked by numerous other amendments to the law. These essentially include:

- **Insolvency law:** Legal acts in connection with stabilisation measures cannot be challenged at the expense of the WSF and provisions of the InsO regarding shareholder loans do not apply at the expense of the WSF;
- **Competition law:** The WSF is largely exempted from the competition law provisions of the German Act against Restraints of Competition (GWB). Regulations regarding agreements restricting competition and market dominance are not applicable. There is no German merger control with regard to the acquisition of shares by the WSF;
- **Law of obligations:** Regulations which provide for a special right of termination of the contractual partner of a company in case of a change of shareholders or the automatic termination of the contractual relationship (so-called change-of-control clauses) are ineffective if the WSF is the new or selling shareholder. The same applies to contractual compensation or indemnification claims in employment or other contracts of board members; and
- **Capital market law:** For shares to be issued to the WSF, no stock exchange listing must be applied for. The WStBG exempts companies extensively from notification and publication obligations in connection with an acquisition of shares by the WSF. The WSF is also not required to make a takeover offer pursuant to Sec. 35 para. 2 sentence 1 WpÜG. In the event of a sale, the company is the responsible party, initiator of the prospectus (Sec. 9 German Securities Prospectus Act (WpPG)) and cost bearer.

SUMMARY AND OUTLOOK

With the new WStFG, the legislation essentially relies on instruments which are believed to have proven their worth in the 2008 financial crisis while targeting companies in the real economy. This will provide important ways out of liquidity bottlenecks for both “big players” and SMEs of all legal forms that get into difficulties due to the current lockdown. Board members and managing directors are well advised to examine the measures available as part of crisis management.

Due to the far-reaching suppression of minority rights under company law, it is also to be expected that shareholders and investors in particular who hold a stake in affected companies, will be confronted with previously unknown legal challenges. In order to best protect their rights, an early examination of the legal framework of the WSF is strongly recommended for this group of investors as well.

Jan Winzen, a former managing associate in our Frankfurt office, also contributed to this article.

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