



German M&A and Corporate Law

## Telephone Briefing

### How to Deal with International Employee Share and Incentive Plans in M&A Transactions under German Law

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# International Employee Share and Incentive Plans in M&A Transactions under German Law

## *A common situation*

- Z-GmbH is the German subsidiary of General Inc., a corporation listed in the US
- The General Inc. group operates an employee share plan, under which certain employees can opt to convert a defined portion of their net salary into shares in General Inc. („the Plan“)
- Z-GmbH tops up the converted salary portion by 50%, i.e. for each EUR converted into shares, participants receive shares in General, Inc. with a market value of 1.5 EUR
- The Plan has been implemented at Z-GmbH by means of an agreement with the competent works council

# International Employee Share and Incentive Plans in M&A Transactions under German Law

## *Scenario 1*

- Z-GmbH sells all assets of a business line to B GmbH, B GmbH continues to operate the business line and the acquired business in an unchanged way
- Under Sec. 613a of the German Civil Code the employment relationships of all employees who are attributable to the transferred business line transfer to B GmbH. B GmbH takes over all rights and obligations under the transferred employment relationships. Works council agreements remain in force.
- Employee X transfers to B GmbH. He wants to convert parts of his salary into shares of General Inc.

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## *Scenario 1*

- The right to participate in the Plan is a benefit under the respective agreement with the works council and hence part of the employment relationship.
- However, while it may be factually possible for B GmbH to grant the benefit, the benefit does no longer serve its purpose, i.e. to increase identification with and loyalty towards the employer and its economic success.
- Does B GmbH have to grant future participation in the Plan?

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## *Scenario 1*

- Language of the Plan's rules
  - Do the Plan's rules contain provisions that apply in a transfer of business scenario?
- Interpretation of the Plan's rules
  - What did the parties intend when the Plan was introduced into the employment relationship?
  - Rules on Leavers may contain indications for the parties' intentions
- Doctrine of Frustration (*Wegfall der Geschäftsgrundlage*)
  - Is the application of the Plan still acceptable?

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## *Scenario 1*

- Replacing the Plan
  - Past-Service entitlements remain unaffected
  - Employee has a right to receive a benefit of equivalent value
    - Examples: Cash compensation, shares in B GmbH's mother company, phantom shares, pension entitlements, contributions to long-term time account schemes
  - Works Council co-determination rights must be observed when the plan is replaced

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## *Scenario 2*

- The Plan has been implemented by means of individual agreements or grant letters
  - Plan rules must be tested against strict T&C rules
  - Constructive Dismissal may be considered
    - Mutual solutions preferable
    - Equal treatment

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## *Scenario 3*

- Participation in the Plan is not agreed between Z-GmbH and Employee X, but instead directly between General Inc. and Employee X
  - Right to participate is not part of the employment relationship
  - Obligations under the Plan do not transfer to B GmbH
  - Check whether situation is covered in Plan's rules



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## *Scenario 4*

- General Inc. sells all shares in Z-GmbH to B Limited
  - Z-GmbH remains the employer, but is no longer part of General Inc.'s group of companies
    - Language of the Plan's rules
    - Interpretation of the Plan's rules
    - Doctrine of Frustration (*Wegfall der Geschäftsgrundlage*) or Constructive Dismissal
      - Is the application of the Plan still acceptable for Z-GmbH?

# Thank you for your participation!



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