

10 pitfalls when hiring and firing a Managing Director in Germany



The Managing Director is a key role in any German limited liability company. The person – who regularly holds no (or at least no majority) shares in the company – is not only the legal representative of the German GmbH (equivalent to the US LLC) but also part of the (local) management. German employment law foresees a different legal framework for Managing Directors than for employees. Given the special role, also corporate aspects must be considered and kept in mind. The following 10 pitfalls should help to navigate through the relevant areas.

1 Service Agreement vs. Employment Agreement

Managing Directors (*Geschäftsführer:in*) are no regular employees. They are seen to be part of the management of the company and different rules and regulations apply. Hence, Managing Directors will sign a Service Agreement (*Dienstvertrag*) instead of an Employment Agreement (*Arbeitsvertrag*). The documents are structured in a similar way but differ in detail which take the different roles and legal framework into account. The conclusion of the Service Agreement with the Managing Director is a transaction separate and distinct from the act of appointment. This means, e.g., that the removal of a Managing Director from his corporate position has no effect on the existence of his Service Agreement which follows its own rules.

2 Role of Managing Director

The Managing Director is a corporate body of the GmbH (besides the company's shareholder meeting) and each GmbH must have one or more Managing Directors who manage and represent the company. Any distinction between executive and non-executive directors is unknown to German law. All Managing Directors are subject to, and must abide by, identical duties and obligations. Even if several Managing Directors are appointed and if each of them has been assigned a distinct field of primary responsibility, such division of competencies has internal effect only. Limitations on the statutory

authority of the Managing Directors to bind the company contractually have no effect with respect to third parties. Only internal rules of procedure for the Managing Directors can hold them liability vis-à-vis the company or the shareholders of the company if breached.

3 D&O Insurance

Directors and officers liability insurance (D&O) is common in Germany and it is, as a practical matter, certainly easier for a company to retain experienced management personnel if D&O is offered as part of the remuneration package. It may also enhance the company's credit-worthiness if it can show to its banks that D&O is in place. The D&O is usually taken out by the company and covers potential liability of the Managing Directors, vis-à-vis both the company and third parties. Premiums are normally paid for by the company.

4 Post-Contractual Non-Compete

The provisions of sections 74 et seqq. German Commercial Code (*Handelsgesetzbuch*) which regulate post-contractual non-competes and compensation for employees do not apply directly or analogously to Managing Directors. There is thus greater flexibility for tailoring the provisions for Managing Directors than for employees. However, restrictions arise to the extent that post-contractual non-competes may not unreasonably disadvantage the

Managing Director and must serve the legitimate business interests of the company. Companies can therefore not use post-contractual non-compete templates associated for employees.

5 Appointment and Revocation of the Managing Director

The Managing Directors are appointed and removed by company's shareholder resolution. The appointment and revocation must be entered in the German commercial register, although such entering has declaratory effect only. The appointment and revocation are valid with immediate effect upon the shareholder resolution. Managing Directors may, generally speaking, be removed from their corporate position at any time for any or no reason, notwithstanding the fact that their Service Agreements remain in force and will therefore have to be honored.

6 Tax Risk

If a GmbH only has a foreign Managing Director, this may result in the place of management of the GmbH being (transferred) abroad. This can have unexpected tax consequences since it may establish a tax liability for the company in that foreign country. This might not be the case in all countries, but the details depend on the applicable double taxation treaty between Germany and the foreign country.

Even if this might not necessarily make a big difference in tax burden, it can still lead to high administrative costs or the incorrect payment of taxes, which can also have personal consequences for the Managing Director under German criminal law.

7 Protection Against Dismissals

Managing Directors of a GmbH do not enjoy protection against dismissal under the Act Against Unfair Dismissal (*Kündigungsschutzgesetz* – "KSchG"), as they are considered to be a corporate body of the company and not an employee. Given that, longer notice periods and sometimes even contractual agreed severance payments in case the company ends

the relationship with the Managing Director for operational reasons are common.

8 Managing Director and Wet-Ink Signature

In Germany certain documents must be signed with a wet-ink signature by the legal representative of the company, i.e. Managing Director, unless a proper power of attorney is in place. Especially if such documents are time-critical (e.g. wet-ink notice letter must be served to employees within the current calendar month), it is essential to make sure that there is always one acting and current Managing Director in place who is depicted in the German commercial register and in a position to wet-ink sign such documents on short notice and to provide the original document. Otherwise, the employee may reject the termination letter. This is especially important if there is a change in the Managing Director position as it takes some time to update the commercial register.

9 Keep any eye on existing Employment Agreement

It happens regularly that an employee is being promoted to become a Managing Director. When then agreeing on the Service Agreement, the existing Employment Agreement must be terminated by mutual consent. Otherwise, the employment relationship is only put dormant and may revive when the Managing Director's Service Agreement ends. Diligent drafting of the Service Agreement ensures compliance and protection for the company.

10 Transfer of IP

The German Employee Invention Act (*Gesetz über Arbeitnehmererfindungen*) does not apply to Managing Directors and thus the assignment of IP rights to the company requires a contractual agreement which can be included in the Service Agreement. Proper contract drafting and/or side agreements are highly recommended, especially if the Managing Director is part of the engineering team.

Taylor Wessing's Employment & Pensions Team

The Employment & Pensions practice area of Taylor Wessing comprises about 100 lawyers. Some 30 recognised specialists work at our German offices. What makes our consultancy different is our in-depth familiarity with the challenges and concerns of the industries of tomorrow:

- Technology, Media & Communications
- Life Sciences & Healthcare
- Financial Institutions & Insurance
- Energy & Infrastructure
- Logistics & Transport

In addition, we are of course fully up-to-date on the particularities of many other industries and offer the full range of advice on all employment-related issues there as well.

Flexible, reliable project management is one of our key strengths. Based on our partner-led approach we will build a team of experts tailored to your individual requirements and managed by a responsible partner who will be available to you at all times.

Employment Team



Dr. Christian Maron
Partner, Munich
+49 89 21038-257
c.maron@taylorwessing.com



Dr. Benedikt Groh
Salary Partner, Munich
+49 89 21038-414
b.groh@taylorwessing.com



Dr. Larissa Burger, M.A.
Associate, Munich
+49 89 21038-323
l.burger@taylorwessing.com



Carolin Wagner
Associate, Munich
+49 89 21038-313
c.wagner@taylorwessing.com

Corporate Team



Dr. Daniel Schrembs, LL.M.
Salary Partner, Munich
+49 89 21038-466
d.schrembs@taylorwessing.com



Fritz Krings
Senior Associate, Munich
+49 89 21038-280
f.krings@taylorwessing.com



We're a global law firm that serves the world's most innovative people and businesses. Deeply embedded within our clients' sectors, we seek to challenge expectation and create extraordinary results. We work closely together with our clients to crack complex problems, enabling ideas and aspirations to be successful.

By shaping the conversation in our sectors, we enable our clients to unlock growth, protect innovation and accelerate ambition.

[taylorwessing.com](https://www.taylorwessing.com)