ALLEN & OVERY

The Financing for the Future Act: Reforms for German ECM transactions

The Financing for the Future Act came into force on 15 December 2023. The significant reforms to stock corporation and capital market law increase flexibility in German ECM transactions.

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Overview of the key changes

The key parts of the Financing for the Future Act (*Zukunftsfinanzierungsgesetz*) (**ZuFinG**) came into force on 15 December 2023. The new law is intended to strengthen the performance of Germany's capital markets and to enhance the attractiveness of Germany as a financial centre and part of a strong European financial centre. In particular, the access to the capital market and equity raises for start-ups, high-growth companies and small and medium-sized enterprises (**SMEs**) shall be eased.

In addition to facilitating capital increases, a number of current trends in the capital market such as advancing digitalisation and the previous obstacles of German stock corporation law for SPAC IPOs are addressed. The main changes introduced by the ZuFinG for German ECM transactions concern the following areas:

- Changes for capital increases;
- Introduction of multiple voting shares (*Mehrstimmrechtsaktien*);
- Creation of a Listed Shell Stock Corporation (*Börsenmantelaktiengesellschaft*) as German SPAC;
- Introduction of electronic shares.

Changes for capital increases

Higher volume of cash capital increases with simplified exclusions of subscription rights

The ZuFinG increases the volume limit for the implementation of cash capital increases with a simplified exclusion of subscription rights from the previous limit of 10% to 20% of the share capital (Sec. 186 Para. 3 Sent. 4 Stock Corporation Act (*Aktiengesetz* – **AktG** new version). Since capital increases excluding the subscription rights of existing shareholders can be implemented much faster and more cost-effectively than subscription rights issues – in particular, in the case of private placements to qualified institutional investors in line with market-standards, no prospectus is required – increasing the volume limit is a significant extension and simplification of the procedure for raising equity capital with a substantial impact on transaction practice. Such volume increase also applies to the sale of treasury shares (*eigene Aktien*) (Sec. 71 Para. 1 No. 8 AktG), the issuance of convertible bonds (*Wandelschuldverschreibungen*), income bonds (*Gewinnschuldverschreibungen*) and participatory rights (*Genussrechte*) (Sec. 221 Para. 4 Sent. 2 AktG) and the issuance of shares out of authorised capital (Sec. 203 Para. 1 AktG).

In order to be able to use the expanded volume flexibly depending on market conditions, issuers should seek shareholder approvals for the exclusion of subscription rights in the expanded volume within the framework of authorised capital as well as authorisations for the issuance of convertible and warrant bonds or have existing authorisations adjusted accordingly.

Increasing the threshold for implementing capital increases without subscription rights will ensure harmonisation with the threshold provided for in the EU Prospectus Regulation[1] for the admission of new shares without a prospectus (Article 1 Para. 5(a) EU Prospectus Regulation). Prior to the enactment of the ZuFinG, German issuers have not been able to fully utilise the 20% threshold provided for in the EU Prospectus Regulation because a subscription rights offer required a prospectus once the 10% threshold was reached due to the limitation under German stock corporation law pursuant to Section 186 Paragraph 3 Sentence 4 AktG old version.

However, according to the draft of the proposed EU Listing Act currently being discussed at the European level, the threshold for the admission of shares without a prospectus contained in Article 1 Para. 5 Letter a) of the EU Prospectus Regulation is to be increased from 20% to 40%. If this increase will be implemented as planned, the German Stock Corporation Act will again remain behind the framework established at the European level.

Changes to conditional capital

The ZuFinG also increases the volume limits for the creation of conditional capital (Sec. 192 Para. 3 Sent. 1 AktG new version):

a) For company combinations (*Unternehmenszusammenschlüsse*) (Sec. 192 Para. 2 No. 2 AktG), the maximum limit of conditional capital is raised from 50% to 60%. The ZuFinG is intended to offer greater flexibility in company combinations which use shares as consideration or for the servicing of subscription and severance payment rights and is a response to criticism of the previous limit as a barrier compared to the more flexible laws in the United States.

b) For employee share schemes (*Mitarbeiterbeteiligungsprogramme*) (Sec. 192 Para. 2 No. 3 AktG), the limit for conditional capital for granting subscription rights is increased from 10% to 20%. This is intended to give companies, especially high-growth companies, greater scope when it comes to incentivising and remunerating highly qualified employees with minimal impact on a company´s liquidity.

[1] Regulation (EU) 2017/1129 of the European Parliament and of the Council of 14 June 2017 on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Directive 2003/71/EC., in its current version.

However, the creation of conditional capital to grant exchange or subscription rights based on convertible bonds remains limited to half of the share capital (Sec. 192 Para. 3 Sent. 1 No. 1 AktG new version).

New system of legal protection when implementing capital increases without subscription rights

The ZuFinG introduces a new system of legal protection for situations where shareholders challenge the implementation of a capital increase without subscription rights on the grounds that the value of the contribution per share is unreasonably low or special benefits (*Sondervorteile*) are being granted (Sec. 243 Para. 2 AktG). While shareholders in this case were previously able to file a legal action for avoidance (*Anfechtungsklage*) in accordance with Secs. 243 et seq. AktG against the general shareholders' meeting resolution (Sec. 255 Para. 2 AktG old version), this is no longer permitted (Sec. 255 Para. 2 AktG new version).

a) If a capital increase without subscription rights is resolved at a company's general shareholders' meeting and the subscription rights are excluded in a way other than in accordance with Section 186 Paragraph 3 Sentence 4 AktG, the shareholders are instead entitled to a cash compensation claim (*Barausgleichsanspruch*) against the company (Sec. 255 Para. 4 AktG new version), if the value of the contribution per share is unreasonably low.

    (i) After the implementation of the capital increase, the adequacy of the compensation payment can be reviewed during judicial valuation proceedings (*Spruchverfahren*) (Sec. 255 Para. 7 AktG new version). In justifying, the legislature reasons that valuation questions, which are usually more complicated with capital increases, cannot be determined in the short term as part of an approval procedure (*Freigabeverfahren*) as an expedited procedure (*Eilverfahren*). At the same time, the company and investors' interests in the timely completion of a capital increase take precedence. Taking all interests into account, it is therefore reasonable to carry out the judicial valuation proceedings only after the capital increase has taken effect.

    (ii) In order to mitigate possible cash compensation obligations, the company can also provide for the granting of additional shares in the resolution approving the capital increase as an alternative to a cash compensation payment (Sec 255a, 255b AktG new version). These shares are created by a capital increase, whereby the shareholders entitled to compensation contribute the compensation claim awarded to them by the court against the issue of new shares (Sec. 255b AktG new version).

    (iii) In order to clarify the question of whether the issue price of the new shares is too low, a comparison of the volume-weighted stock market price of the company's shares must generally be made for listed companies during the last three months before the day preceding the decision to implement the capital increase (Sec. 255 Para. 5 Sent. 1, 4 AktG new version, Sec. 5 Para. 1 German Securities Acquisition and Takeover Act Offer Regulation (*Wertpapiererwerbs- und Übernahmegesetz-Angebotsverordnung* – **WpÜGAngebV**). Only if the stock exchange price on that day is lower than the determined reference price, such stock exchange price will be relevant (Sec. 255 Para. 5 Sent. 5 AktG new version).

    (iv) There is no entitlement to compensation if the issue price is not significantly lower than the stock market price (Sec. 255 Para. 5 Sent. 2 AktG, new version). During the legislative process, the German Finance Committee clarified that the fundamental valuation of a capital increase remains at the discretion of the Company's Management Board and that the value of the contribution may also include the agreement of a discount. Such a discount may go beyond the principles developed under Section 186 Paragraph 2 Sentence 4 AktG and the issue price of the shares may therefore be more than three to five percent below the stock market price.

b) If a capital increase with a simplified exclusion of subscription rights in accordance with Section 186 Paragraph 3 Sentence 4 AktG is resolved by the company's general shareholders' meeting, the aforementioned compensation payments do not exist. Even though the wording of Section 255 Paragraph 2 AktG new version is not clear in this respect, the action for avoidance under Sections 243 et seq. AktG due to non-fulfillment of the requirements of Section 186 Paragraph 3 Sentence 4 AktG - in particular the granting of an excessive discount on the stock market price – should remain permissible.

c) In the particularly relevant case for ECM transaction practice, that the Executive Board and Supervisory Board resolve the capital increase by using existing authorised capital, the aforementioned new regulations will not apply. The previously applicable limited options for legal protection remain.

Introduction of multiple voting shares (*Mehrstimmrechtsaktien*)

The ZuFinG provides for the introduction of multiple voting shares into German stock corporation law, removing the basic principle previously set out in Section 12 Paragraph 2 AktG old version, according to which multiple voting rights were inadmissible. In particular, this is intended to ease the access to the capital market for owner-managed companies and to increase their willingness for capital market financing.

Particularly for family- or founder-managed (*familien- oder gründergeführte*) medium-sized or high-growth companies, the fear of a loss of control can represent an obstacle to an IPO. Multiple voting rights enable founders and owners of family-managed companies to maintain extensive control over "their" company even after an IPO. Under the previous legal position, this was only possible via the detour of a partnership limited by shares (*Kommanditgesellschaft auf Aktien*) structure or the issue of preferred non-voting shares.

Registered shares can be designed as multiple voting shares in the form of a separate class of shares through a corresponding provision in a company's articles of association, both when a company is founded and later as part of a capital increase. The issuance or provision of shares with multiple voting rights requires the consent of all shareholders (Sec. 135a Para. 1 Sent. 3 AktG new version). Therefore, issuing these shares is only practical up until the time of an IPO because post-IPO an unanimous vote at a shareholders' general meeting is likely unachievable. In addition, the issue of multiple voting shares from authorised capital is not possible (Sec. 202 Para. 1 Sent. 2 AktG new version).

In order to protect minority investors, the design and operation of shares with multiple voting shares is subject to restrictions, namely:

a) The potential voting rights weight of multiple voting shares is limited to a maximum of ten times the simple voting rights per share (i.e. 1:10) (Sec. 135a Para. 1 Sent. 2 AktG new version);

b) the multiple voting right does not affect the majority of capital, as it only provides a higher number of votes, but not additional capital underlying the shares; in this respect, multiple voting shares only have a veto position in resolutions with an additional capital majority requirement, e.g. when convening a general shareholders' meeting, approving resolutions to increase and reduce capital or the approval of a company agreement;

c) within the scope of the appointment of an auditor or special auditor, multiple voting shares only entitle one vote (Sec. 135a Para. 4 AktG new version);

d) in the case of listed companies and companies whose shares are included on the open market, the multiple voting rights expire when the respective multiple voting shares are transferred (Sec. 135a Para. 2 Sent. 1 AktG new version). In addition, the multiple voting rights expire no later than ten years after listing or the inclusion of the shares on the open market, although this period can be shortened by a provision in a company's articles of association (Sec. 135a Para. 2 Sent. 2 AktG new version). The aforementioned period can, at the earliest one year before expiry, be extended for up to a further ten years through an

amendment to the company's articles of association if they are passed by a three-quarters capital majority (*Dreiviertel-Kapitalmehrheit*) (Sec. 135a Para. 2 Sent. 3, 4 AktG new version).

In the case of non-listed companies, the statutory grounds for extinguishing the multiple voting rights upon transfer do not apply, nor are multiple voting shares limited in time. Nevertheless, the company is free to set restrictions in accordance with its articles of association (Sec. 135a Para. 3 AktG new version).

If multiple voting rights expire, the total number of voting rights in the company is reduced. The voting weight of shareholders also changes accordingly. This can lead to a shareholder exceeding the control threshold in accordance with Section 29 Paragraph 2 German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz* – **WpÜG**) who would therefore generally be obliged to publish a mandatory offer (*Pflichtangebot*) within the meaning of Section 35 WpÜG. However, in the ZuFinG's explanatory notes, reference is made to the possibility of an exemption from the mandatory offer obligation due to a reduction in the total number of voting rights in the target company in accordance with Section 37 WpÜG in conjunction with Section 9 Sentence 1 No. 5 WpÜGAngebV.

The ZuFinG partly contains more stringent restrictions with regards to multiple voting shares than the corresponding provisions in the draft of the proposed EU Listing Act currently being discussed at the European level. For example, the EU Listing Act does not provide for an express limitation of shares with multiple voting rights to ten times the voting rights, but only generally calls for protective measures in favour of shareholders with single voting rights. On the other hand, the scope of application of the provisions of the EU Listing Act regarding multiple voting shares is limited to non-listed stock corporations that are seeking admission to an SME growth market, whereas the ZuFinG regulations are generally accessible to all companies within the scope of application of the German Stock Corporation Act – regardless of their stock exchange listing.

Creation of a Listed Shell Stock Corporation (*Börsenmantelaktiengesellschaft*) as German SPAC

Due to existing restrictions in German stock corporation law, particularly in the areas of raising and maintaining capital (*Kapitalaufbringung und -erhaltung*), German SPAC transactions have so far only been carried out using foreign legal forms, in particular the Societas Europaea (**SE**) under Luxembourg law. Therefore, the prospectus was approved by the foreign supervisory authority and then notified to Germany by means of so- called EU- passporting (Article 24 EU Prospectus Regulation). The ZuFinG is now creating a new legal variant of the stock corporation, the Listed Shell Stock Corporation (*Börsenmantelaktiengesellschaft* – **BMAG**), whose legal purpose is to achieve its own listing on the stock exchange (Sec. 44 Para. 1 Sent. 1 of the German Stock Exchange Act (*Börsengesetz* – **BörsG**) new version), and thereby ought to enable original German SPAC transactions.

The special provisions for the BMAG created in the newly inserted Chapter 4a of the German Stock Exchange Act are, in addition to the German stock corporation law (Sec. 44 Para. 7 BörsG new version), only applicable to German stock corporations or Societas Europaea (SE) under German law (Sec. 44 Para. 4 BörsG new version):

a) whose articles of association contain the following provisions:

   (i) The object of the company is the management of its own assets, the preparation and implementation of its own stock exchange listing as well as the preparation and completion of the takeover transaction, which corresponds to the criteria described in the listing prospectus and relates to a company that is not listed on a stock exchange (**Target Transaction**);

   (ii) the existence of the company is dependent on the execution of the Target Transaction within the period specified in the company's articles of association between 24 and 36 months from the admission of the company's shares to trading on the regulated market;

(iii) the option of holding a virtual shareholders' general meeting is provided; and

b) whose securities have been admitted to a regulated market in accordance with Section 32 BörsG.

In principle, the BMAG must be constituted as a stock corporation and have "Börsenmantelaktiengesellschaft" or a generally understandable abbreviation in its name (Sec. 44 Para. 5 BörsG new version). The special form of the BMAG is also accessible to Societas Europaea (SE) under German law (Sec. 44 Para. 8 BörsG new version) because of the corresponding applicability of German laws on stock corporations to the Societas Europaea (SE), in accordance with Article 10 of the EU European Company Regulation[2].

The key condition for the continued existence of a BMAG is the Target Transaction, the implementation of which is decided by a general shareholders' meeting with a three-quarters capital majority (Sec. 46 Para. 1 Sent. 1, Para. 3 Sent. 1 BörsG new version) and in which the voting rights of the initiators, i.e. the founders and board members who hold shares or other subscription rights, are excluded (Sec. 46 Para. 3 Sent. 2 BörsG new version).

If the deadline for the existence of the BMAG specified in the company's articles of association threatens to expire without a Target Transaction being carried out, the deadline can be extended by 12 month periods up to a total of 48 months by means of a resolution amending the articles of association (Sec. 44 Para. 3 Sent. 4 BörsG new version). If the deadline expires, this represents a reason for dissolution of the BMAG as well as a reason for a possible revocation of the admission to the stock exchange by the management of the stock exchange in accordance with Section 39 BörsG (Sec. 47b Para. 1 Sent. 1 BörsG new version). However, if the acquisition of assets worth at least 80% of the contributions made to the BMAG are carried out in full prior to the deadline, the company will continue to exist but without the BMAG status in accordance with the provisions of the German Stock Corporation Act (Sec. 47b Para. 1 Sent. 2 BörsG).

The ZuFinG also overcomes the existing obstacles of German stock corporation law with regard to SPAC transactions:

a) As an exception to the general capital raising principle (*Kapitalaufbringungsgrundsatz*), the contribution made must be held by a suitable trustee in an escrow account and is therefore largely withdrawn from access by the board of directors (Sec. 45 Paras. 1-2 BörsG new version).

b) In addition, the ZuFinG provides for a special provision for shareholders who have objected to the resolution to carry out the Target Transaction and who want to assert their contractually granted right to have their investment returned and withdraw from the BMAG. Previously, such a return of deposits (*Einlagenrückgewähr*) would only have been possible if the company was dissolved, however objecting BMAG shareholders now have the opportunity to have their shares transferred to the company in return for repayment of the contribution and premium within two months of the adoption of the general shareholders' meeting's resolution (redemption right), which is declared to be compatible with the principle of capital preservation (*Kapitalerhaltungsgrundsatz*) (Sec. 47 Para. 1, Para. 3 Sent. 1 BörsG new version). In addition, the limit of Section 71 Paragraph 1 No. 3, Paragraph 2 Sentence 1 AktG for the purposes of the acquisition of own shares by the BMAG in order to fulfill the shareholders' claims from the redemption right will be increased from 10% to 30% of the share capital (Sec. 47 Para. 2 AktG new version).

c) The permissibility of issuing independent warrants (naked warrants) on additional shares of the company, which are issued independently of a warrant bond (Sec. 221 Para. 1 Sent. 1 AktG), is generally considered to be controversial, particularly against the background of the prohibition on issuing subscription rights that are decoupled from shareholder status (Sec. 187 Para. 2 AktG). The BMAG provisions, however, expressly permit the issuance of naked warrants, provided that these are serviced from conditional capital in accordance with Section 192 AktG (Sec. 47a Para. 1 AktG new version). The minimum holding period

[2] Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), in its current version.

for such warrants in accordance with Section 193 Para. 2 No. 4 AktG is declared inapplicable (Sec. 47a Para. 2 BörsG new version).

Introduction of electronic shares

With the introduction of electronic shares, the legislature has not created a new class of shares, but has amended the German Stock Corporation Act and the Electronic Securities Act (*Gesetz über elektronische Wertpapiere* – **eWpG**) (newly introduced two years ago), to allow for the electronic issuance of shares through entry in an electronic securities register. This option has already existed for bearer bonds (*Inhaberschuldverschreibungen*) since June 2021.

The registration of the issued shares in the electronic securities register replaces the previously required issue of a securities certificate (Sec. 2 Para. 1 eWpG). The eWpG differentiates between two types of electronic securities registers: the central register and the crypto securities register. While in a central register the registrar (*registerführende Stelle*) has its own authority to change the register and exercises this centrally, it is a characteristic of crypto securities registers that they are decentralized as well as largely algorithm-based and automated. Central registers may only be maintained by securities depository banks and central custodians (in Germany: Clearstream Banking AG), whereas crypto securities registers, can in principle, be maintained by any company if they have the appropriate permission to provide financial services. In addition, the registrar can also be granted responsibility for maintaining the share register as a separate register for registered shares (instead of being maintained by the issuer itself) (Sec. 30a eWpG new version).

Registered shares can be issued via registration in a central register and by registration in a crypto securities register using blockchain technology. For bearer shares only the central register is available; therefore, the ZuFinG does not provide for bearer crypto shares (*Inhaberkryptoaktien*) (Sec. 1 No. 2, 3 eWpG new version). This is essentially due to the legislature's concerns regarding money laundering, as it would make it considerably more difficult to determine the beneficial owner (*wirtschaftlich Berechtigter*) of a bearer share, which can in principle be registered or rebooked using blockchain technology without intermediaries. In addition, there are challenges under corporate law, such as identifying the shareholder, which do not arise with registered shares maintained on a share register. Potential financial benefits (in particular in relation to transaction and administration costs) through the issuance of crypto shares and the associated comprehensive avoidance of intermediaries are therefore reserved exclusively for issuers of registered shares.

If a company wants to have its shares entered as electronic shares in an electronic securities register, it must exclude physical securitisation in its articles of association (Sec. 10 Para. 6 Sent. 1 AktG new version). Companies which want to issue registered shares in the form of crypto shares must explicitly permit this in their articles of association (Sec. 10 Para. 6 Sent. 2 AktG new version). There is no need for an explicit provision in a company's articles of association regarding the admissibility to issue and register electronic shares in a central register (Sec. 10 Para. 1 Sent. 2 No. 3, Para. 6 AktG new version).

Finally, the ZuFinG clarifies that it is possible that shares which are already issued and registered through share certificates can be replaced by electronic registered shares (Sec. 6 Para. 3, 4 eWpG).

Further changes

In addition to these significant changes for German stock corporation and capital market law introduced by the ZuFinG, there are also numerous less significant changes to other laws, such as the following:

a) For stock exchange listings, the minimum amount of shares to be admitted is reduced from €1.25 million to €1 million (Sec. 2 Para. 1 Sent. 1 BörsZulV new version).

b) While a stock exchange admission generally had previously to be applied for together with a credit institution, financial services institution, a securities institution or a company operating in accordance with

Section 53 Paragraph 1 Sentence 1 or Section 53b Paragraph 1 Sentence 1 of the Banking Act (*Kreditwesengesetz*) (Sec. 32 Para. 2 Sent. 1 BörsG), stock exchange regulations may in future provide that issuers can submit an application on their own (Sec. 32 Para. 2a BörsG new version). However, this only applies to admissions outside of parts of the regulated market with further obligations, i.e. on the Frankfurt Stock Exchange only for the General Standard and not for the Prime Standard.

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