

Germany's new hammer to glass ceilings

Published: 15 April 2015

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On March 6, 2015, the German Federal Parliament (Bundestag) passed the Act on Equal Participation of Women and Men in Executive Positions in the Private Economy and the Public Sector (the "Gender Quota Act").

Going forward, the provisions of the Gender Quota Act will have to be complied with when private equity advisers plan the future composition of the governing bodies and senior management of their German portfolio companies. The requirements of the law that are relevant for the private sector are said to affect directly a total of 3,500 companies in different respects although the indirect knock-on effect will likely be much more significant.

As of January 2016, approximately 108 German companies will be subject to a fixed mandatory quota pursuant to which their supervisory boards have to consist of at least 30 persons of persons of the underrepresented gender. This feature of the quota law applies to publicly-listed stock corporations (Aktiengesellschaft, AG) or limited joint stock partnerships (Kommanditgesellschaft auf Aktien, KGaA) and the Societas Europaea (SE) which in addition have a mandatory supervisory board with an equal number of shareholder representatives and employee representatives.

Each of the groups of the shareholder representatives and the employee representatives in the supervisory board is called a "camp". Essentially, those are the companies that employ 2,000 or more employees in Germany. From January 2016 onwards, supervisory board members appointed prior to such time may remain in office for the remainder of their respective term, even if the applicable quota is not met. But whenever a seat on the supervisory board becomes vacant, a member of the underrepresented gender must then be appointed. In case of failure to do so, the relevant seat remains vacant.

Avoiding pitfalls

The Gender Quota Act contains a number of pitfalls which can, however, be avoided by planning the basic operation and

composition of a supervisory board under the quota regime in a timely and thorough manner.

To start with, the mechanics of the quota calculation in various scenarios – particularly in light of the two camps within a supervisory board – should be kept in mind.

In a supervisory board consisting of 12 or 20 members in the aggregate, the overall minimum number of members from the underrepresented gender is identical irrespective of a joint or separate calculation of the members from the shareholder and/or employee side. If the supervisory board has, however, 16 members, the aggregate number of the members from the underrepresented gender can increase or decrease in case of separate calculations or joint calculation, depending on the numbers in question. This deviation is due to rounding differences, but may encourage tactical decisions on the separate calculation of shareholder and employee representatives and thus might contravene the spirit of the gender quota which ultimately aims at equal representation of women and men.

As a general rule under the Gender Quota Act, the shareholder representatives and the employee representatives are looked at jointly in order to determine whether the quota is satisfied. However, each camp may –before a new election or court appointment of supervisory board members – object to a joint counting.

An open seat

A vacant seat can have tremendous effects on the balance of power in the supervisory board, particularly with regard to strategic decisions. In case of a tied vote, the chairperson – who as a rule is a shareholder representative – has a casting vote in a second round of voting. Naturally, this can only apply in case of a deadlock. If, however, due to a vacant seat on the shareholder side, the employee side already achieves a majority in the first vote, the casting vote will not kick in.

Target thresholds at the top

Another aspect of the Gender Quota Act has not been in the public focus as much as the fixed quota, but will affect a far larger number of companies in the private sector already as early as of September 30, 2015.

About 3,500 German companies which are either publicly listed or subject to employee representation on the supervisory board have to fix target thresholds for female representation in the management board, the two levels below the management board and the supervisory board (unless the fixed 30 percent quota applies). The companies affected include in addition to the aforementioned companies also unlisted stock corporations, joint stock partnerships and limited liability companies (GmbH), provided such (unlisted) company has 500 or more employees in Germany and is thus subject to an employee co-determination regime under which at least one third of the members of the supervisory board must be employee representatives. Any Societas Europaea (SE) meeting these criteria is also affected.

The supervisory board is in charge of setting the target number for the supervisory board itself and for the management board. The management board is responsible for setting the targets for the two management levels below the management board. The target quota is chosen separately for each group.

The Gender Quota Act does not provide for immediate sanctions in case of non-compliance with the selfdetermined quotas. However, the companies are subject to reporting obligations and such reporting must also include an explanation of the reasons why a company fails to meet the envisaged targets.

Outlook

Looking at the near future, the fixed 30 percent gender quota may cause some companies to move supervisory board re-elections forward into the year 2015 to delay the application of the Gender Quota Act in practice by creating additional protected seats. But even in such a case, any member who resigns unexpectedly and with only short notice must, after January 1, 2016, be promptly replaced by a member from the underrepresented gender. Thus, prudent planning and determining suitable candidates in a timely manner should not be postponed in either case.

As regards the flexible quota, the absence of a rigid sanctions regime should not be overestimated. The reporting required in case of targets not being met may not only be burdensome but also negatively impact a company's public perception. Also, at this stage it cannot be ruled out that the failure to meet set targets might lead to refusals of the annual discharge (Entlastung) of the management; and a failure to set such targets at all likely amounts to a breach of fiduciary obligations which may result in personal liability of the members of the relevant corporate body.

Overall, the Gender Quota Act provides an opportunity for females to break through the glass ceiling in typically male dominated sectors of the economy. While the challenges regarding the application of the law may still require further clarification in detail by the courts, the Gender Quota Act aims to provide a practical and effective tool to promote and foster equal opportunities for females which will likely result in a larger number of female professionals in the private equity sector and its portfolio companies.

Gibson Dunn M&A lawyers Markus Nauheim and Birgit Friedl are based in Munich.