Germany

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GENERAL

1. Is it common for employees to be offered participation in an employee share plan?

Employee share plans, in particular, share option plans, are becoming increasingly common in German companies. Legislation does not specifically set out any employee incentives, but a considerable body of regulations exists to encourage employee shareholdings through participation in employee share plans.

2. Is it lawful to offer participation in an employee share plan where the shares to be acquired are shares in a foreign parent company?

Employees in Germany can generally participate in the share plan of a parent company that is located in a different jurisdiction. However, certain employment law principles, such as that of equal treatment, only apply to the German company and not to the corporate group.

It is disputed as to whether share options granted by a foreign parent company can be considered remuneration. If they are, they are subject to certain protective provisions, such as section 613a of the German Civil Code (*Bürgerliches Gesetzbuch*) which specifies that if a business or a part of a business is transferred to another owner, the new employer enters into the rights and obligations of the old employer, so must carry on paying the same remuneration. The Federal Labour Court (*Bundesarbeitsgericht*) has not yet ruled on this issue. However the High Courts of Düsseldorf, Hessen and Munich have held that share options granted by a foreign parent company are not remuneration.

SHARE OPTION PLANS

3. Please list each type of share option plan operated in your jurisdiction (if more than one).

No specific types of share option plan exist.

4. In relation to the share option plan:

- **What are the plan's main characteristics?**
- **Which types of company can offer the plan?**
- **Is this type of plan popular? If so, among which types of company is this plan particularly popular?**

Share option plan

Main characteristics. A company grants a specific number of shares at a defined exercise price within a defined time period to its employees or managers, or those of its affiliated company. Employees exercise options to make a profit if the shares' market value (that is, the price at which they are traded on the market) is higher than the exercise price.

If an employee exercises an option, the employer has two ways of providing the shares. It can either:

- Purchase its own shares on the market. This is governed by paragraph 71, sub-paragraph 1(8) of the Stock Corporation Act (*Aktiengesetz*).
- Increase its share capital. This is governed by paragraph 192, sub-paragraph 1(3) of the Stock Corporation Act.

The share option plan's terms and conditions must be adopted by a resolution of the company's shareholders' meeting (*paragraph 193, sub-paragraph 2, Stock Corporation Act*). The resolution must specify the:

- Distribution of options.
- Individual vesting conditions.
- Fixed date at which the employee can first exercise the option.
- Period of time during which the employee can exercise the option.

Types of company. The only companies that can offer share options plans are:

- Public limited companies (*Aktiengesellschaften*).
- Companies with elements of a limited partnership (*Kommanditgesellschaften*).

Popularity. Share option plans are becoming increasingly popular to remunerate managers who directly influence the company's share price through their performance. In the IT and software industries it is becoming popular to grant share options plans to other employees as well.

5. In relation to the grant of share options under the plan:

- **Can options be granted on a discretionary basis or must they be offered to all employees on the same terms?**
- **Is there a maximum value of shares over which options can be granted, either on a per-company or per-employee basis?**
- **Must the options have an exercise price equivalent to market value at the date of grant?**
- **What are the tax and social security obligations arising from the grant of the option?**

Share option plan

Discretionary/non-discretionary. The employer can grant share option awards to employees and managers, but not to members of its supervisory board. The employer must observe the principle of equal treatment when awarding share options. According to decisions of the Federal Labour Court, this principle is not breached if there is a reasonable justification for offering the same terms only to individual groups of employees (for example, executive staff). However, the employer must offer the same terms to employees with comparable skills and positions.

Maximum value of shares. The value of shares that a company offers under share option plans cannot exceed 10% of its share capital (*paragraph 71 and paragraph 192, sub-paragraph 3, Stock Corporation Act*).

Market value. The exercise price can be above market value, but must not be below it.

Tax/social security. No tax or social security is payable on grant.

6. In relation to the vesting of share options:

- **Can the company specify that the options are only exercisable if certain performance or time-based vesting conditions are met?**
- **Is any tax or social security contributions payable when these performance or time-based vesting conditions are met?**

Share option plan

Exercisable only on conditions being met. The law requires that the option cannot be exercised any earlier than two years after grant. It can also specify performance conditions. The shareholders must agree to the terms (*see Question 4, Share option plan: Main characteristics*).

Tax/social security. Tax and social security contributions are not payable on vesting.

7. Do any tax or social security implications arise when the:

- **Option is exercised?**
- **Shares are sold?**

Share option plan

Tax/social security on exercise. Income tax is charged on exercise. The taxable benefit is the difference between the shares' fair market value on exercise and the exercise price. Income tax is charged at progressive rates, ranging from 15% to 42% in 2007.

Social security contributions are also payable. Employees and employers share social security contributions equally between them.

Tax/social security on sale. Capital gains tax is charged on the profit made if the shares are sold within 12 months after exercise. The employee must pay the tax.

SHARE ACQUISITION OR PURCHASE PLANS

8. Please list each type of share acquisition or purchase plan operated in your jurisdiction (if more than one).

No specific types of share purchase plan exist. They are regulated by paragraph 186, sub-paragraph 29, and paragraph 71, sub-paragraph 23 of the Stock Corporation Act.

9. In relation to the share acquisition or purchase plan:

- **What are the plan's main characteristics?**
- **Which types of company can offer the plan?**
- **Is this type of plan popular? If so, among which types of company is this plan particularly popular?**

Share purchase plan

Main characteristics. The company offers employees the right to buy a certain number of shares at a discounted price, or to buy some shares and receive additional shares free of charge.

Types of company. Only public limited companies can offer a share purchase plan, irrespective of whether they are listed or under another company's control.

Popularity. Companies have offered share purchase plans for several years. They are currently the most common employee incentive.

10. In relation to the initial acquisition or purchase of shares:

- **Can entitlement to acquire shares be awarded on a discretionary basis or must it be offered to all employees on the same terms?**
- **Is there a maximum value of shares that can be awarded under the plan, either on a per-company or per-employee basis?**
- **Must employees pay for the shares and, if so, are there any rules governing the price?**
- **Is any tax or social security contributions payable when the shares are awarded?**

Share purchase plan

Discretionary/non-discretionary. The employer must comply with the equal treatment principle when awarding an entitlement to acquire shares (*see Question 5, Share option plan: Discretionary/non-discretionary*).

Maximum value of shares. The shareholders' meeting can only authorise up to 10% of the company's share capital as shares offered under a share purchase plan (*paragraph 71, Stock Corporation Act*)

Payment of shares and price. The company can sell shares to the employee for a price that is below their market value. However, the price cannot be inappropriately low (*paragraph 255, sub-paragraph 2, Stock Corporation Act*).

Tax/social security. If employees purchase shares below market value, they pay income tax and social security contributions on the difference between the purchase price and market value.

11. In relation to the vesting of share acquisition or purchase awards:

- **Can the company award the shares subject to restrictions that are only removed when performance or time-based vesting conditions are met?**
- **Is any tax or social security contributions payable when these performance or time-based vesting conditions are met?**

Share purchase plan

Restrictions removed only on conditions being met. The company can place performance or time-based vesting conditions on the award. It is particularly common to impose time-based conditions, to commit the employee to the company. However, any vesting period cannot exceed five years.

Tax/social security. No tax or social security contributions are payable when vesting conditions are met.

12. What are the tax and social security implications when the shares are sold?

Share purchase plan

On sale, employees pay capital gains tax on the profit, that is, the difference between the shares' sale price and purchase price.

PHANTOM OR CASH-SETTLED SHARE PLANS

13. Please list each type of phantom or cash-settled share plan operated in your jurisdiction (if more than one).

There are two types of phantom share plan:

- Phantom share plans.
- Share appreciation rights.

14. In relation to the phantom or cash-settled share plan:

- **What are the plan's main characteristics?**
- **Which types of company can offer the plan?**
- **Is this type of plan popular? If so, among which types of company is this plan particularly popular?**

Phantom share plan

Main characteristics. The employee owns equity units that mirror the company's shares and receives a cash award that amounts to the difference between the employer's shares' market value and a specified price that the employer and employee agree on. The employee may also receive cash dividends, for a certain period of time, that relate to the underlying shares. This amount is often paid as part of the employee's regular salary.

Types of company. Only public limited companies can offer a phantom share plan.

Popularity. Phantom share plans are not very common.

Share appreciation right

Main characteristics. The employee receives the same economic reward that he would have received if a share option had been granted. The employee can exercise the award and benefits from any increase in the share value without actually receiving any shares.

Types of company. Only public limited companies can offer share appreciation rights.

Popularity. Share appreciation rights are not very common, but they are useful for employers that wish to reward members of their supervisory board, who cannot receive share options (*see Question 5, Share option plan: Discretionary/non-discretionary*).

15. In relation to the grant of phantom or cash-settled awards:

- **Can the awards be granted on a discretionary basis or must they be offered to all employees on the same terms?**
- **Is there a maximum award value that can be granted under the plan, either on a per-company or per-employee basis?**
- **Is any tax or social security contributions payable when the award is made?**

Phantom share plan

Discretionary/non-discretionary. The employer can offer phantom share plans to any employee. It must comply with the equal treatment principle (*see Question 5, Share option plan: Discretionary/non-discretionary*).

Maximum value of awards. There is no limit to the maximum value of awards that can be made.

Tax/social security. No income tax or social security contributions are charged on grant.

Share appreciation right

Discretionary/non-discretionary. The employer can offer share appreciation rights to any employee. It must comply with the equal treatment principle (*see Question 5, Share option plan: Discretionary/non-discretionary*).

Maximum value of awards. See above, *Phantom share plan: Maximum value of awards.*

Tax/social security. See above, *Phantom share plan: Tax/social security.*

16. In relation to the vesting of phantom or cash-settled awards:

- **Can the awards be made to vest only where performance or time-based vesting conditions are met?**
- **Is any tax or social security contributions payable when these performance or time-based vesting conditions are met?**

Phantom share plan

Award vested only on conditions being met. The award can be structured to vest only if performance or time-based conditions are met.

Tax/social security. No tax or social security contributions are charged on vesting.

Share appreciation right

Award vested only on conditions being met. See above, *Phantom share plan: Award vested only on conditions being met.*

Tax/social security. See above, *Phantom share plan: Tax/social security.*

17. What are the tax and social security implications when the award is paid out?

Phantom share plan

The award is treated as part of the employee's income, so is charged to income tax. If the share plan was awarded to an employee, both the employer and employee pay social security contributions on the award. However, no social security contributions are payable for managers. No capital gains tax arises.

Share appreciation right

See above, *Phantom share plan.*

GUIDELINES

18. Are there any institutional, shareholder, market or other non-statutory guidelines that apply to any of the above plans, and which types of companies are subject to them? What are their principal terms?

The Corporate Governance Code (*Deutscher Corporate Governance Kodex*) applies to public limited companies listed on the German stock exchange. It is updated every year by the government commission (*Regierungskommission Deutscher Corporate Governance Kodex*) and contains several basic mandatory principles. Managers and the supervisory board must report each year as to whether they fully comply with the code. The report must always be accessible to shareholders (*paragraph 161, Stock Corporation Act*).

The Corporate Governance Code requires disclosure of dealings and ownership of shares in a company if they exceed 10% of the company's issued share capital (*section 6.6*).

EMPLOYEE REPRESENTATIVES

19. Is consultation or agreement with, or notification to, employee representative bodies required before an employee share plan can be launched?

If the company has a works council and the employees entitled to receive share options are not managers (as defined in paragraph 3, section 5 of the Works Council Constitution Act (*Betriebsverfassungsgesetz*)), the works council may have a co-determination right (*paragraph 1, No. 10, section 87, Works Constitution Act*). This means that although the works council's consent is not required to launch the plan, the employer must consult it when planning how the options are distributed, and all other details.

If a foreign parent company implements an employee share plan, consultation with the works council is not required.

EXCHANGE CONTROL

20. Do exchange control regulations prevent employees sending money from your jurisdiction to another to purchase shares under an employee share plan?

There are no exchange control regulations in Germany. However, an employee who transfers more than EUR12,500 (about US$16,802), must inform the German Central Bank (*Bundesbank*).

21. Do exchange control regulations permit employees to repatriate proceeds derived from selling shares in another jurisdiction?

There are no exchange control regulations in Germany.

INTERNATIONALLY MOBILE EMPLOYEES

22. What is the tax position when:

- **An employee who is ordinarily resident in your jurisdiction at the time of grant of a share plan leaves your jurisdiction before exercising the option?**
- **An employee who is not ordinarily resident in your jurisdiction is sent to your jurisdiction holding share awards already granted in another jurisdiction?**

Resident employee

If an employee exercises an option granted in Germany when no longer resident in the country, German tax is charged on the gain in proportion to the time during which the employee was resident in Germany after grant. If the employee exercises the option abroad but is still officially tax resident in Germany, tax is charged on the whole gain. Tax relief may be granted if a double taxation treaty applies between Germany and the other jurisdiction.

Non-resident employee

If a non-resident employee exercises in Germany an option granted in another jurisdiction, German tax is charged on the gain in proportion to the time during which he has been in Germany since grant. If the employee becomes resident in Germany before exercising the option, tax is charged on the whole gain. Tax relief may be granted if a double taxation treaty applies between Germany and the other jurisdiction.

PROSPECTUS REQUIREMENTS AND OTHER CONSENTS OR FILINGS

23. For the offer of and participation in an employee share plan:

- **What prospectus requirements (if any) must be completed and by when? What exemptions (if any) are available?**
- **What other regulatory consents or filings (if any) must be completed and by when? What exemptions (if any) are available?**

Prospectus requirements

The Securities Prospectus Act (*Wertpapierprospektgesetz*) implements Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading (Prospectus Directive).

The Prospectus Directive requires companies to publish a prospectus for offers of securities to the public. An offer of securities to the public is defined as a communication that sets out sufficient details to enable investors to decide whether to purchase or subscribe for the securities. A prospectus is even required if the shares are listed on an EU stock exchange. However, for securities that are already listed on a regulated market and offered to employees, the employer can present a document instead of a prospectus. This document must contain information on both the:

- Amount and form of the securities.
- Reason for making the offer.

Most share options do not fall under the Prospectus Directive, because they are generally non-transferable and non-negotiable on the capital market. In addition, there are exemptions that significantly limit the number of share plans that require a prospectus (*paragraph 2, section 1, Securities Prospectus Act*). The most important exemption is if securities are offered to the public in the EU for a value of less than EUR2.5 million (about US$3.37 million). This threshold refers to the amount payable by employees, and not to the value of shares offered. Another important exemption is an offer that is made to less than 100 employees.

Other regulatory consents or filings

Government approval is not generally required when launching an employee share plan. However, the Securities Trading Act (*Wertpapierhandelsgesetz*) sets out certain rules, in particular the prohibition of insider trading. In addition, any capital share increase must be registered in the commercial register (*Handelsregister*).

DEVELOPMENTS AND REFORM

24. Please briefly summarise:

- **The main trends and developments relating to employee share plans over the last year.**
- **Any official proposals for reform of the law on employee share plans.**

Trends and developments

There have been no recent trends or developments relating to employee share plans.

Reform proposals

There are no proposals for reform of the law relating to employee share plans.