

**The German “special representative” and Corporate Governance**

Corporate Governance for crisis situations in financial institutions

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By: Bernhard Thor Eric Fiedler

Student No: FDLBER001

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Signed by candidate

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## C. The German “special representative” and Corporate Governance

Corporate Governance for crisis situations in financial institutions

### I. Introduction

In Germany, banks and insurance companies are regulated and supervised by the financial supervisor, the *Bundesanstalt für Finanzdienstleistungsaufsicht* [BaFin]. The Banking Supervision Act *Kreditwirtschaftsgesetz* [KWG] and the Insurance Supervision Act *Versicherungsaufsichtsgesetz* [VAG] provide the financial supervisor with a broad range of powers regarding the enforcement of the law. One of these powers is the ability to appoint a special representative. Under certain circumstances, according to s 83a (1) VAG, the financial supervisor is allowed to suspend parts or even whole organs of a supervised company and to replace them with a special representative. In general these circumstances are:

- Insufficient knowledge and abilities of the managing directors (s 83a (1) (1) VAG)
- Breach or infringement of the supervision law and every related law (s 83a (1) (2) VAG)
- Possibility of insolvency of the supervised company (s 83a (1) (3) VAG).

S 36 (1a) KWG includes the same provision for the banking supervision, however for reasons of a general view only the provisions of s 83a (1) VAG will be subject of the following elaborations. The special representative acts like the organ he suspends. However he does not become an organ himself nor is he bound by instructions of the financial supervisor. In theory, it is also possible to replace all of the company’s organs with only one special representative. Yet, this leads to serious interferences in the company’s legal and corporate governance framework. It is, so to say, an instrument ultima ratio. That means where the supervising authority has no other means of intervening in the supervised company in such a crisis situation as described in s 83a (1) VAG itself the appointment of a special representative offers a final solution for the crisis situation.

Within this thesis, I am going to elaborate on the special representative in the corporate governance framework. On the one hand most common law countries like the United Kingdom, Australia and South Africa acknowledge the disqualification of board members by their financial supervisor but apparently there is no equal instrument to the special representative. On the other hand in Germany the special representative turned out to be a powerful instrument to guarantee a fast and effective reaction to a crisis situation in a bank or insurance company. The thesis strives to examine what would happen if the special representative would be introduced to a common law system, what kind of different rules he would have to obey, and what kind of problems could arise. The relation of the special representative to the fiduciary duties will be specially stressed in the thesis.

The words “corporate governance” are a short form for the legal and factual regulation framework for the management and control of the company<sup>1</sup>. The appointment of a special representative regularly can be seen as an intervention in the management of the company. If a special representative is appointed for the whole supervisory board or the whole management board, he enters into the function of one of the highest organs of the insurance stock corporation. In this case the particular roles, competences and functionalities as well as the interaction of the company’s organs is affected. Subsequent to this the special representatives’ primary effect results in an intervention with the inside perspective<sup>2</sup> of corporate governance. Subsequent to this, the question of the relation of the special representative in, or as the case may be, to the corporate governance arises, especially to what extent corporate governance principles are infringed upon and, as the case may be, what corporate governance principles the special representative has to comply with.

The most important principles of corporate governance are the principles of separation of power, transparency, reduction of conflicts of interest and the motivation for value orientated performance<sup>3</sup>. As a matter of particular interest in regard to the appointment of a special representative, firstly there should be a closer look at the principle of separation of powers. Through separation of powers, monopolies of force, which otherwise would be subject to an individual arbitrariness, can be avoided<sup>4</sup>. As an example of this, the German company laws’ necessary division between management board and supervi-

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<sup>1</sup> Von Werder, *Corporate Governance Code*, p 2.

<sup>2</sup> Compare to Hommelhoff/Hopt/von Werder, *Handbuch CG*, p 4.

<sup>3</sup> Hommelhoff/Hopt/von Werder, *Handbuch CG*, p 14.

<sup>4</sup> Hommelhoff/Hopt/von Werder, *Handbuch CG*, p 14.

sory board can be mentioned. In the monistic board system the same is achieved through the distinction between executive and non-executive directors. If a special representative is appointed for the management board as well as for the supervisory board, the problem arises that he cannot effectively control himself in regard to his management position. Subsequent to this a level of control in the company, which is seen as a fundamental cornerstone of supervision by the legislator, does not apply<sup>5</sup>.

## II. Insurance supervision in Germany

As mentioned above the insurance supervision in Germany is governed by the VAG. The supervising authority currently is the BaFin, which calls itself an “all finance” supervisor (The BaFin is the legal successor of the former BAV (federal authority for insurance supervision), BAKred (federal authority for banking supervision), and BAWe (federal authority for securities supervision)).

The insurance supervision law forms part of the public law sector, specifically the administrative law sector in Germany. Therefore the insurance supervision law is a special variation of the trade supervisory centre. This becomes apparent, because until now one of the main objectives of the insurance supervision is preventing threats and deficiencies; a common goal for the broader principle of trade supervision<sup>6</sup>. Another main objective of the insurance supervision is the protection of the insured. This is also referred to as the central goal of insurance supervision<sup>7</sup>.

The supervising authority has a broad range of instruments to intervene in insurance companies if it suspects or becomes aware of deficiencies which usually are also a threat to the insured. Because the supervising authority forms part of the public law it has to comply with several public law principles. The supervising authority first is bound to the law and secondly may not interfere into private rights without the exculpation of a law; a so called basis of authorisation for the intervention. In addition all actions of the supervising authority have to be proportional. Finally some of the instruments are connected to the discretion of the supervising authority. The supervising authority by all means has to exercise its discretion in a lawful and reasonable way. If the

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<sup>5</sup> Regierungsentwurf eines *Gesetzes zur Kontrolle und Transparenz im Unternehmensbereich* (KonTraG) dated 28. January 1998, BT-Drucks 13/9712, p 11.

<sup>6</sup> Winter, *Zielsetzung der Versicherungsaufsicht*, ZVersWiss 2005, p 105, 109

<sup>7</sup> Winter, ZVersWiss 2005, p 105, 111.

supervising authority violates any of those principles with its actions these actions are unlawful and become voidable.

### **III. Different systems of corporate governance**

The different worldwide systems of company constitutions are constructions, which have been grown in different structures for the last hundred years. One of the major differences can be seen in the German dualistic system and in the Anglo-American monistic board approach. How difficult it is to make changes in such an existing corporate governance system can be seen in the contrary trends in Germany on the one hand, and the Anglo American system on the other hand. While in Germany people are discussing and postulating the privileges of the Anglo-American board system, people in the United States and the UK at the same time are watching the dualistic system with great interest. Despite these global players, elaborations about corporate governance are made in many economically developed countries of the world and also in the so-called emerging markets.

#### **1. Dual system of the German corporate governance**

As mentioned above, the German stock corporation has three necessary organs: the management board, the supervisory board and the general meeting, whose responsibilities are tightly delimited from each other. The dual management/supervisory board system leads to a straight distinction between a management organ and a control/supervisory organ. The managing board, as the managing organ, represents the stock company in its own discretion to the inside as to the outside. In addition, the managing board is obliged to perform actions that are lawfully decided by the general meeting as long as it is concerned<sup>8</sup>. The general meeting is the deciding organ. The stock owners perform their rights by voting. Tasks of the day to day business are only decided by the general meeting if it is explicitly asked to do so by the management board. The supervisory board appoints the management board and controls and consults the management board, which runs the company. As a basic principle the general meeting elects the members of the supervisory board. One big exception is that as far as the Co-

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<sup>8</sup> The general meeting does not have the power to instruct the management board with regard to questions of the day -to-day business. The general meeting only has powers with regard to principle decisions of the company and participates in the management of the company only to the extent it is asked to do so by the management board.



determination Act *Mitbestimmungsgesetz* [MitBestG] is applicable, some of the members of the supervisory board have to be representatives of the employees, who have to be elected by the employees themselves. The number of employees in the supervisory board depends on the size of the company. However the supervisory board in a company where the MitBestG is applicable has to be staffed equally with representatives of the stockowners and representatives of the employees<sup>9</sup>. The participation of the employees in the supervisory in stock corporations with a wide spread stock ownership make the German corporate governance a special case. This system is also known as an “Insider-system”. This is because the supervisory institutions and strategic investors have a major role in the external stewardship of the company.

## 2. Anglo-American corporate governance system

Compared to the German dualistic approach, the American and the British stock corporations only have two organs, the general meeting of the stockowners and the board of directors. In the Anglo-American monistic board approach, the management and control functions are basically united in one institution. The stockowners elect the board of directors as a central administration organ, whose business at the same time is the management of the company on the one hand, and the control of the management on the other. The officers appointed for a regular occupation are called “Inside Directors” whereas the directors appointed only for a part time occupation are called “Outside Directors”<sup>10</sup>. On the one hand the board of directors shall supervise the management in the stockowners interest. On the other hand the board of directors points out the business’s development and is part of strategic planning and management of the company. For the fulfilment of all the different issues, the board normally constitutes different committees. Specifically, the audit committee, which is mostly staffed with “Outside Directors”, is in charge of a control function in the company. Another major difference to the German dualistic system is that in the Anglo-American monistic board approach normally no workers or trade union members are represented<sup>11</sup>. In the US and the UK the “outsider-system” plays a crucial role; in other words, the stockownership is widely spread and banks and workers do not normally participate in the corporate governance of the company. Especially institutional investors are in charge of the control by using

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<sup>9</sup> E.g. according to s 7 (1) No. 1 MitBestG the supervisory board of a company with more than 10,000 employees has to be staffed with six representatives of the stockowners and six representatives of the employees

<sup>10</sup> Potthoff, *Board-System versus duales System*, BFuP 1996, p 253 f.

<sup>11</sup> Langenbucher/Blaum, *Audit Committee – ein Weg zur Überwindung der Überwachungskrise*, DB 1994, p 2197, 2198 f.

the capital market whose target, is, of course, the maximisation of the company value. As a consequence the intern control mechanisms are merely less developed. A reason for this is that they do not affect the functioning of the external controls, which are related to the capital market.

#### **IV. Corporate Governance in Insurance Companies**

It seems to be reasonable first to elaborate on the types of companies that perform in the insurance business. After this the German Corporate Governance Codex, which only is applicable to those companies that are listed at the stock exchange, will be subject to this discussion.

##### 1. Types of companies

In the Federal Republic of Germany because of s 7 VAG only two types of Companies are allowed to undertake insurance business. The one type is the stock corporation (*Aktiengesellschaft*) and the other, the mutual insurance company (*Versicherungsverein auf Gegenseitigkeit-VVaG*). Regarding the governance of the company, the VVaG is mostly similar to the stock corporation. However there are some differences between the two types of insurance companies.

##### (a) Insurance stock corporation

The management board is the organ with the highest responsibility within the stock corporation and therefore has the function of the highest internal leadership<sup>12</sup>.

Basically the management board is governed by the principle of collective responsibility (*Kollegialprinzip*)<sup>13</sup>. However, s 84 (2) AktG points out, that in the case where more than one member is appointed to the management board, the supervisory board has the power to appoint one member of the management board as the chairperson of the management board. S 77 (2) AktG provides that single tasks of the management of the company can be arranged through by-laws. These by-laws can be enacted either by the management board itself or they can be enacted by the supervisory board within the limits of

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<sup>12</sup> Hahn/Hungenberg, *Wertorientierte Controllingkonzepte*, p 29.

<sup>13</sup> Compare to Hüffer, § 77 AktG, at 6.

the articles<sup>14</sup>. The chairperson of the management board can be put in an emphasised role insofar as he is acknowledged to possess certain competences<sup>15</sup>.

The introduction of the Corporate Sector Supervision and Transparency Act *Gesetz zur Kontrolle und Transparenz im Unternehmensbereich* [KonTraG] also led to an extension of the duties of the management board. According to s 90 (1) (1) AktG the management board now has to report to the supervisory board over the proposed business policy and other principle questions with regard to the business development. Especially, the financial-, investing- and human resources planning are part of the aforementioned. However, the list given by the legislator shall not be exclusive<sup>16</sup>. The supervisory board, which shall supervise the management board by this type of reporting duties, obtains the duty to control the management board not only in retrospect but also to control the management board in an ex ante oriented way<sup>17</sup>.

In the stock corporation the supervisory board is in charge of some kind of a special position. It is a control and supervision organ. Its main purpose is the supervision of the management board. According to the AktG the supervisory board has certain rights and duties from which the content of its supervision duty can be determined<sup>18</sup>. Besides the provisions of the company act, the articles of association and the by-laws lead to a concretisation of the functioning of the supervisory board.

The supervisory board of the stock corporation has the rights and duties to decide about the composition of the management of the company (ss 84, 105, 77 and 78 AktG), to represent the company against the members of the management board (ss 84, 86, 87, 89 and 93 AktG), to gain its own information (ss 90, 111, 170, 337 and 171 AktG), to influence the management (ss 111 and 171 AktG) and to participate in principle decisions (ss 111 and 172 AktG). Out of the area of rights and duties of the supervisory board, four different functions can be determined. These functions are the appointment and withdrawal of the members of the management board as well as the agreement of the employment contracts of the members of the management board; the consultation with the management board with regard to the management of the company; the participation

<sup>14</sup> Compare to Hüffer, § 77 AktG, at 9f.

<sup>15</sup> Schewe, *Unternehmensverfassung*, p 123; Catchwords in this regard are competence of lead management (*Federführungskompetenz*), competence of coordination (*Koordinationskompetenz*), right of passive information (*Passives Informationsrecht*), competence for guidelines (*Richtlinienkompetenz*), competence of disposition (*Dispositionskompetenz*) and competence of order (*Ordnungskompetenz*)

<sup>16</sup> Regierungsentwurf eines *Gesetzes zur Kontrolle und Transparenz im Unternehmensbereich* (KonTraG) dated 28. January 1998, Bt-Drucks. 13/9712, p 15.

<sup>17</sup> Bt-Drucks. 13/9712, p 15.

<sup>18</sup> Albers, *Corporate Governance in AGs*, p 29.

in important business decisions such as the approval of the annual balance sheet; and the active supervision of the management by the management board<sup>19</sup>.

The KonTraG also introduced some alterations for the supervisory board. Influenced by these alterations is, amongst others, the composition of the supervisory board and their meeting frequency. In addition now according to s 100 (2) AktG, the board of directors seats for one person are limited. Since the amendment of s 111 (2) sentence 3 AktG, now the supervisory board appoints the auditor and not the management board of the company according to s 290 Commercial Code *Handelsgesetzbuch* [HGB].

The main organ of representation for the shareholders is the general meeting. The competence of supervision of the general meeting develops more in an indirect way, hence it is basically limited to the competence of appointment (*Bestellungskompetenz*) and the competence of discharge (*Entlastungskompetenz*). A competence of supervision similar to the one of the supervisory board however is not existent<sup>20</sup>.

The KonTraG is also tangential to the rights of the general meeting. Majority votes (*Mehrheitsstimmrechte*) and supreme votes (*Höchststimmrechte*) have been abolished in the case of listed companies. According to this, the principle of “one share one vote” should have been accommodated.

(b) Mutual insurance company

At first the insurance supervision act distinguishes between small and larger VVaG. Ss 15 to 52 of the VAG imply regulations for larger VVaG where s 53 VAG only defines some of the rules of the VAG for application. The distinction between a large and a small VVaG is made by the financial supervisor. The line between a large and a small VVaG can be drawn where the circumstances of the business do not legitimate the privileges of the small VVaG<sup>21</sup>, e.g. often staff pension funds of larger German corporations are organised in the form of an VVaG<sup>22</sup>. These privileges are mostly dependent on the right of association (*Vereinsrecht*) and not on the stricter companies law.

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<sup>19</sup> Albers, *Corporate Governance in AGs*, p 31.

<sup>20</sup> Schewe, *Unternehmensverfassung*, p 170.

<sup>21</sup> Müller, *Der Versicherungsverein auf Gegenseitigkeit / Chancen und Risiken aus der Sicht eines Versicherungsaufsehers*, Frankf. Votr., p 8.b

<sup>22</sup> Those VVaG are not open to the general public and therefore usually are treated as small VVaG.

S 15 VAG includes a pretty comprehensive definition of this type of company, which is limited to insurance business<sup>23</sup>. The VVaG is, according to s 22 of the German civil code *Bürgerliches Gesetzbuch* [BGB], an economic association. Unlike the stock corporation, the VVaG does not acquire its legal capacity until it acquires the approval for business seen as a concession (ss 5, 6 VAG). The VVaG has members that shall be insured on the principles of mutuality. The VVaG is a personal association based on membership<sup>24</sup>. At least in principle the VVaG just strives, instead of the stock corporation, which strives for profit, to provide balance of risks between its members<sup>25</sup>. There is no principal (*Grundkapital*) or corpus (*Stammkapital*).

The VVaG as an association is a legal person (*juristische Person*). The club funds belong to the association such that it is only liable for its debts. The VVaG can act as a party in legal proceedings and also in insolvency proceedings. As long as it does not provide insurance for non-members, by common sense, it cannot be seen as a merchant according to the HGB. The structural similarity between the VVaG and the stock corporation becomes apparent with s 29 VAG. This section asserts that the articles of association (*Satzung*) have to specify how the three necessary association organs, the managing board (*Vorstand*, s 34 VAG), the supervisory board (*Aufsichtsrat*, s 35 VAG) and the supreme representation (*oberste Vertretung*, s 36 VAG) are constituted. Even on closer inspection the similarities to the stock corporation are immanent. Besides the VVaG specific rules contained in ss 34, 35 and 36 VAG, the legislator also used several cross-references to the AktG.

For the managing board of the VVaG s 34 sentence 2 VAG refers nearly completely to the companies acts rules for the stock corporations managing board. Under s 76 (2) sentence 1 AktG, only the postulated circumference of the minimum occupancy is modified by s 34 sentence 1 VAG in that not only one, but two persons are necessary. In addition, the managing board's duties in the case of loss, excessive indebtedness or illiquidity arising out of s 92 AktG are not included in the cross reference<sup>26</sup>. Also, the liability of the managing board to pay damages is not determined by s 93 (3) AktG, but by s 34

<sup>23</sup> “An association which wants to provide insurance for its members on the principles of mutuality, acquires its legal capacity by the approval of the supervising authority to operate business as an mutual insurance company”.

<sup>24</sup> Müller-Wiedenhorn, *VVaG im Unternehmensverbund*, p 12 f.; Goldberg/Müller, Vor § 15 VAG, at 2.

<sup>25</sup> Farny, *Der Beitrag des Versicherungsvereins auf Gegenseitigkeit zur Versicherung in Vergangenheit und Zukunft*, ZfV 1975, p 10, 14.

<sup>26</sup> S 92 AKTG imposes a duty to the management board to file for an insolvency procedure the case of loss, excessive indebtedness or illiquidity. However according to s 88 (1) VAG only the financial supervisor is entitled to file for an insolvency procedure for a supervised company. Because VVaG only perform insurance businesses a reference to s 92 AktG is not necessary.

sentence 4 VAG. Subsequent to this, the managing board members are liable in the case that the effective initial fund (*Gründungstock*) is unlawfully charged with interest or amortised, or in the case that the association funds are allocated, or in the case that a payment is made, or a debt is granted after illiquidity. The VVaG managing board is the managing organ and the representation organ of the association<sup>27</sup>. The managing board manages the company in its own stewardship.

The provisions concerning the supervisory board of the VVaG in s 35 (1) VAG are nearly identical with the ones of s 95 AktG. The supervisory board of a VVaG is also subject to the MitBestG. But s 35 (2) VAG only refers to the company constitutions act *Betriebsverfassungsgesetz* [BetrVG] of 1952. This means, that in a company with more than 500 employees, a one third participation of employees is obligatory for the supervisory board. However, in contrast to the stock corporations, the BetrVG of 1976, which makes obligatory a one-half participation of employees for a company with more than 2000 workers, is not applicable because of a lack of reference. Consequently, in the case that a VVaG has more than 2000 employees, the participation of the employees in the supervisory board is still one-third. This deviation can be explained by the fact that in the case of a VVaG, the interests of the members and the employees do not act so diametrically, as in the case of stockholders and employees within a stock corporation. Members and employees have a long-term interest in the company hence, in theory, there are no tensions between these two groups<sup>28</sup>.

Incidentally, s 35 (3) VAG merely refers to the company act provisions for the supervisory board. So the key issues for the supervisory board of a VVaG are the appointment and the withdrawal of the management board (compare to s 84 AktG), the representation of the association towards the management board (s 35 (3) sentence 1 VAG in connection with s 112 AktG) and, last but not least, the supervision of the stewardship of the company by the management board (s 35 (3) sentence 1 VAG in connection with s 111 (1) AktG). The company law provision with regard to the personal requirements and the due diligence of supervisory board members are obligatory as well.

According to s 20 sentence 2 VAG, only a person that has an insurance relation to the association can be a member. Subsequent to this, the membership relation can be distinguished from the insurance relation. Following only the membership relation will be subject of this elaboration. While a VVaG is incorporated, membership and insurance

<sup>27</sup> See § 34 S. 2 VAG iVm §§ 76, 77, 78 AktG.

<sup>28</sup> Weigel in Prölss, Vor § 15 VAG, at. 43a.; Frels, *Grundlagen des VVaG*, p 130, 133.

relation are connected. Later on, the property rights arising out of the insurance contract are independent from the membership to VVaG<sup>29</sup>. These membership rights can also be determined as creditors' rights<sup>30</sup>.

§ 36 and § 36 b VAG contain several references to the company law provisions regarding the duties and rights arising out of the membership. § 36 sentence 1 VAG, for example, refers to the provisions of the companies act regarding the general meeting (ss 118 to 147 AktG) and also to provisions regarding void decisions of the general meeting (ss 241 to 261 AktG). The members' most important administration rights are its participation -, application - and voting rights regarding the superior representation, its information - and the rights to appeal<sup>31</sup>. Additional rights can arise out of the acts (VVG, VAG, AktG) or the articles of association. The members' most important duty is the payment of their fees. At the same time, this also is the merit for the insurance (§ 1 (2) VVG). An obligation to make additional contributions or a cut down of the insurance claims for years with an extraordinary appearance of damages is lawful. But most of the VVaG's have excluded such clauses from their articles of association. The VVaG's members' position regarding its rights and duties at first sight merely merges the positions of a stockowner and a policyholder in an insurance stock corporation<sup>32</sup>.

The rights of the superior representation of the VVaG are more of a fundamental nature. It is in the position to change the articles of association, within the limits drawn by the VAG. It is concerned with the appointment of the supervisory board members (§ 35 (3) sentence 1 VAG in connection with § 101 (1) AktG). It also decides about the discharge of the managing board and the supervisory board (§ 36 sentence 1 VAG in connection with § 120 AktG), the use of the accumulated profits (in connection with § 119 (1) (2) AktG) or changes in the articles of association (§ 39 (1) VAG).

§ 29 VAG refers to two lawful but strongly divergent possibilities of embodiment for the superior representation. It can be enacted either by a plenum (*Vollversammlung*) of all members or by a board of members (*Mitgliedervertretung*). A plenum would comply with the notion of the members' self-administration. However in the course of time, most of the mutual insurance companies have chosen a board of members. Especially in the case of a large mutual, where the number of members has between six and seven

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<sup>29</sup> Müller-Weidenhorn, *VVaG im Unternehmensverbund* p 26; Weigel in Prölss, § 20 VAG, at 9.

<sup>30</sup> Müller-Weidenhorn, *VVaG im Unternehmensverbund* p 26; Weigel in Prölss, § 20 VAG, at 12.

<sup>31</sup> Compare to Müller-Wiedenhorn, *VVaG im Unternehmensverbund*, p 22, Fn. 119 f.

<sup>32</sup> Fahl, *Corporate Governance im VVaG*, p 9.

digits, the performance of a plenum would merely lead to unsolvable problems. Even in the case where just a few of the members would show up at the plenum, this would lead to the problem of random majorities (*Zufallsmehrheiten*). The plenum would be vulnerable to small and organised groups of members<sup>33</sup>.

The implementation of a board of members leads to a tactical diminution of the participation rights of the single member in the mutual unless the member of the mutual is a member of the board of members<sup>34</sup>. The only right which remains to the member is the right to elect the board of members. The legislator disposes the determination how the board of members should be composed to the members of the mutual<sup>35</sup>. Existing systems of election constitute election by direct vote (*Urwahl*), the system of objection (*Einspruchssystem*) and the cooptation. In the last case the board of members itself decides about a successor if one of its members resigns from its office<sup>36</sup>.

## 2. German Corporate Governance Kodex

As some of the supervised insurance companies are “listed companies”, the German Corporate Governance Kodex applies to those companies. As it is the case with all the other different codices<sup>37</sup>, the German Corporate Governance is a code of best practise. It only applies to listed companies. Like the other codices, the system of the German Kodex, according to s 161 sentence 1 AktG, is one of comply or explain. The duty to disclose, according to s 161 AktG, is related only to the recommendations of the code, and thus to the provisions which are characterised by a “shall” (*soll*) in their wording<sup>38</sup>. Simple encouragements like can (*kann*) or may (*sollte*) are unremarkable for s 161 AktG<sup>39</sup>.

The duty to disclose of s 161 AktG is addressed to the management- and the supervisory board but not to the company itself<sup>40</sup>. S 161 AktG constitutes the duty and therefore the competence of the management- and supervisory, to disclose their knowledge and in-

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<sup>33</sup> Raiser, *Die Zulässigkeit des Kooptationssystems bei der Bildung von Mitgliedervertretungen großer Versicherungsvereine auf Gegenseitigkeit*, ZVersWiss 1965, p 465, 466.

<sup>34</sup> Fahl, *Corporate Governance im VVaG*, p 12.

<sup>35</sup> Fahl, *Corporate Governance im VVaG*, p 13.

<sup>36</sup> Fahl, *Corporate Governance im VVaG*, p 13.

<sup>37</sup> E.g. Cadbury Committee in the UK, Sox in the US, King II in South Africa.

<sup>38</sup> Hüffer, § 161 AktG, at 3.

<sup>39</sup> Hüffer, § 161 AktG, at 8.

<sup>40</sup> Borges, *Selbstregulierung im Gesellschaftsrecht - zur Bindung an Corporate Governance Kodizes*, ZGR 2003, p 508, 527; Seibt, *Deutscher Corporate Governance Kodex und Entsprechens-Erklärung (§ 161 AktG-E)*, AG 2002, p 249, 252.



tents to the broader public<sup>41</sup>. Because the attribution of competences still follows the company law, every organ has to make the decision about a disclosure, a non-disclosure or a partial disclosure in its own field of competence<sup>42</sup>. Whether a disclosure of compliance shall be given or not, has to be decided by the management- and the supervisory board each, according to their role-book<sup>43</sup>.

(a) Consequences in the case of non compliance with regard to internal liability (Innenhaftung)

With regards to the liability of the members of the management- or supervisory board towards the company - it has to be distinguished whether, firstly, a disclosure was not given or was not given correctly or was not made public permanently, or whether, secondly, the boards have not complied with the recommendations of the Code.

With regard to the first case, it can be said that the behaviour of the organ members is a breach of their duty to disclose under s 161 AktG and that they will usually be responsible for that. However, the damage of the company and causation of the breach of their duty, for which they are responsible, is more a de facto variant<sup>44</sup>. In so far as this is the case, the relevancy for the practise seems to be rather questionable<sup>45</sup>.

With regard to the second case, it can be said that the opinions in the literature with regard to this case are non-uniform. Some parts of the literature are of the opinion that non-compliance with a recommendation can imply a breach of the duty of due care and skill according to s 93 (2), 116 sentence 1 AktG, independently from the circumstances of the particular case<sup>46</sup>. According to another view in the literature, because of their non-binding legal character, the recommendations similar to the DIN standards cannot

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<sup>41</sup> Hüffer, § 161 AktG, at 10.

<sup>42</sup> Hüffer, § 161 AktG, at 10.

<sup>43</sup> Hüffer, § 161 AktG, at 11; E.g. the income of the members of the supervisory board shall be disclosed to the general meeting according to s 4.2.5 of the DCGK. However it stays subject to the management board whether it wants to disclose its income or not. The supervisory board can not affect this decision and has to decide for itself whether it wants to disclose information's with regard to the income of the management board.

<sup>44</sup> Hüffer, § 161 AktG, at 25.

<sup>45</sup> Claussen/Bröcker, *Der Corporate Governance Kodex aus der Perspektive der kleinen und mittleren Börsen-AG*, DB 2002, p 1199, 1205; Kiethe, *Falsche Erklärung nach § 161 AktG – Haftungsverschärfung für Vorstand und Aufsichtsrat?*, NZG 2003, p 559, 564.

<sup>46</sup> Lutter, *§ 161 AktG – Pflichtverstöße und Binnenhaftung von Vorstands- und Aufsichtsratsmitgliedern*, ZHR 166 (2002), p 523, 540 ff.; Schüppen, *To comply or not to comply - that's the question! "Existenzfragen" des Transparenz- und Publizitätsgesetzes im magischen Dreieck kapitalmarktorientierter Unternehmensführung*, ZIP 2002, p 1269, 1271; Ulmer, *Der Deutsche Corporate Governance Kodex – ein neues Regulierungsinstrument für börsennotierte Aktiengesellschaften*, ZHR 166 (2002), p 150, 166 f.

be a cause for liability (*haftungsbestimmend*)<sup>47</sup>. However the better arguments exist for the second point of view, especially because the recommendations of the German Corporate Governance Kodex are not a piece of governmental legislation and because of serious constitutional doubts, especially against the informal appointment of the governmental commission and therefore the recommendations simply can not interact like a formal law<sup>48</sup>.

(b) Consequences in the case of non-compliance with regard to external liability (Außenhaftung)

In so far as s 161 AktG deals with an external liability, it appears that the shareholders can be creditors, that might have faced a pecuniary loss because of stock market losses or losses of profits, in so far as this pecuniary loss is caused by a breach of the duty to disclose, for which the director is responsible, which is an adequate cause<sup>49</sup>. Considerations for this are virtually exclusively claims out of tort (s 823 (1) BGB)<sup>50</sup>. However these fail at the objective requirements of the matter of fact (*objektive Tatbestandsmäßigkeit*) of s 823 (1) BGB, because the violation of a legally protected matter needs to be related to a single person. The non-compliance with a single recommendation, and therefore the falseness of the disclosure, however is not related to a single shareholder and therefore a violation of a legally protected matter that can be the cause for a liability (*haftungsbegründend*) is missing<sup>51</sup>. S 823 (2) BGB only applies to the extent as protective laws (*Schutzgesetze*) are violated. However the recommendations of the code do not have the nature of protective laws; to this extent the quality for a legal norm is absent<sup>52</sup>. Therefore a liability of the company seems not to be considerable.

A liability of the members of the management- or supervisory board basically can arise either out of tort or fidelity liability (*Vertrauenshaftung*)<sup>53</sup>. To the extent the claims arise out of tort, the arguments mentioned above apply *mutatis mutandis*. Therefore the problems of the objective cause of liability persist. The fidelity liability acts in accor-

<sup>47</sup> Bachmann, *Der „Deutsche Corporate Governance Kodex“: Rechtswirkungen und Haftungsrisiken*, WM 2002, p 2137, 2138; Berg/Stöcker, *Anwendungs- und Haftungsfragen zum Deutschen Corporate Governance Kodex*, WM 2002, p 1569, 1575 ff.; Ettinger/Grützediek, *Haftungsrisiken im Zusammenhang mit der Abgabe der Corporate Governance Entsprechenserklärung gemäß § 161 AktG*, AG 2003, p 353, 354 f.

<sup>48</sup> Hüffer, § 161 AktG, at 27.

<sup>49</sup> Hüffer, § 161 AktG, at 28.

<sup>50</sup> Hüffer, § 161 AktG, at 28.

<sup>51</sup> Berg/Stöcker, WM 2002, p 1569, 1578; Kiethe, NZG 2003, p 559, 565; Ulmer, ZHR 166 (2002), p 150, 168.

<sup>52</sup> Hüffer, § 161 AktG, at 28.

<sup>53</sup> Hüffer, § 161 AktG, at 29.

dance with ss 280 (1), 311 (3) BGB. According to this, a liability of the organs is, in principle, possible. However it is not obvious, what, with regard to the members of the management board, could constitute a duty to protect (s 241 (1) BGB) the shareholders e.g. as it is the case with regard to prospect liability. Specifically, there cannot be a prospect liability without a prospect in the specific sense of distribution information (*Vertriebsinformation*)<sup>54</sup>.

## V. The legal position of the special representative

In the case of an appointment of a special representative by the financial supervisor, the special representative only enters into the authorities of the organ insofar as these authorities are subject to a transfer to the special representative<sup>55</sup>. The office of the special representative includes all rights and duties, which have been transferred to his office<sup>56</sup>. By common point of view, the special representative does not become an organ of the company itself but undertakes the authority of the organ he suspends<sup>57</sup>. Therefore, the special representative can also be seen as an institution *sui generis*<sup>58</sup>. Also, the occasion for which the special representative is appointed is, for his legal status, mostly unimportant<sup>59</sup>.

The position of the special representative is essential for his duties in connection with the corporate governance framework. It seems that the legislator has posed the question as to what the legal position of the special representative is to the literature and the jurisdiction. But neither the literature, nor the jurisdiction, has strong arguments for the theory that the special representative does not become an organ himself, or that the instrument can be seen as an institution *sui generis*. Therefore it seems to be necessary to determine the position of the special representative.

Through appointment, the special representative enters into a public office (*öffentliches Amt*)<sup>60</sup>. However, a public law employment status (*öffentlich-rechtliches Dienstverhältnis*)

<sup>54</sup> Berg/Stöcker, WM 2002, p 1569, 1580f; Kiethe, NZG 2003, p 559, 565; Seibert, *Im Blickpunkt: Der Deutsche Corporate Governance Kodex ist da*, BB 2002, p 580, 584.

<sup>55</sup> Goldberg/Müller, § 81 VAG, at 34.

<sup>56</sup> Rühle, *Das Recht des Sonderbeauftragten unter Berücksichtigung der öffentlich-rechtlichen Versicherungsanstalten*, ZfV 1956, p 545, 546.

<sup>57</sup> Bähr in Fahr/Kaulbach, § 81 VAG, at 37; Mösbauer, *Die Unternehmensaufsicht im Bereich der Versicherungswirtschaft*, BB 1987, p 1688, 1690; OLG Hamburg, VersR 1963, p 129, 130.

<sup>58</sup> Goldberg/Müller, § 81 VAG, at 34.

<sup>59</sup> KG, VersR 1957, p 225.

<sup>60</sup> Rühle, ZfV 1956, p 545, 546.

nis) is not given<sup>61</sup>. Therefore the special representative is similar to other instruments, like the insolvency administrator (*Konkursverwalter/Insolvenzverwalter*) or the executor (*Nachlassverwalter*)<sup>62</sup>. For the assumption of a nature of a formal public servant (*Beamteneigenschaft*), the essential subordination relation (*Unterordnungsverhältnis*) between the public employee (*Dienstverpflichteten*) and the public employer (*Dienstherr*) or the employment penal power (*Dienststrafgewalt*) of the public employer is missing<sup>63</sup>. In fact the employer of the special representative is the insurance company and consequently the company itself<sup>64</sup>. Incidentally the special representative is not entitled to a public servant salary but rather is entitled to a salary fixed by the financial supervisor subject to be paid by the insurance company itself<sup>65</sup>. However it is not clear whether the special representative really enters into a public office, because it seems as if the jurisdiction sees the legal position of the special representative more like the one of the organ for which he is appointed<sup>66</sup>. However it can be asserted that the special representative is not in an employment relationship with the financial supervisor. This is also shown by the practical experiences in the day to day business of the financial supervisor<sup>67</sup>.

Following another point of view, the special representative has the position of a state superintendent (*Staatskommissar*)<sup>68</sup>. This point of view is problematic because the special representative is subject to supervision by the financial supervisor whereas the state superintendent is a supervisor himself. Therefore this point of view cannot be followed.

As mentioned before, the special representative, in relation to his position, seems similar to the insolvency administrator. Therefore it seems to be reasonable to have a closer look at the current theories existing for the insolvency administrator related to his position. However an analogous application of the provisions of the Insolvency Act *Insolvenzordnung* [InsO] is not considerable. An analogy is only valid, if the law contains an unintended loophole (*planwidrige Regelungslücke*)<sup>69</sup>. In addition the circumstances that have to be evaluated with regard to legal aspects have to be similar with the matter of fact which the legislator has covered with a provision, so that it can be assumed that the

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<sup>61</sup> Rühle, ZfV 1956, p 545, 546.

<sup>62</sup> Rühle, ZfV 1956, p 545, 546.

<sup>63</sup> Rühle, ZfV 1956, p 545, 546.

<sup>64</sup> Rühle, ZfV 1956, p 545, 546.

<sup>65</sup> Rühle, ZfV 1956, p 545, 546.

<sup>66</sup> OLG Hamburg, VersR 1963, p 129.

<sup>67</sup> Rühle, ZfV 1956, p 545, 546.

<sup>68</sup> Matthes, Neum. ZfV 1936, p 515, 516.

<sup>69</sup> Compare to BGHZ149, 165, 174; Larenz/Canaris, p 194 ff.; Canaris, Festschrift für Bydlinski, p 47, 82 ff.

legislator by balancing the interests (*Interessenabwägung*), by which the legislator would have been guided by the same principles as he was guided when he ordered the provision which is now considered and therefore would have reached the same solution in his process of balancing<sup>70</sup>.

Both instruments come into action in crisis situations in companies. This similarity becomes apparent with s 83a (1) (3) VAG, that enables the appointment of a special representative in the case of facts which lead to the conclusion that the insurance company might not be able to fulfil obligations arising out of the insurance contracts. However, the special representative seems to be much more flexible than the insolvency administrator. This becomes apparent with the other two alternatives, which enable the appointment of the special representative in the case of insufficient knowledge and abilities of the managing directors (s 83a (1) (1) VAG) or the breach or infringement of the supervision law and every related law (s 83a (1) (2) VAG). But even in the case of s 83a (1) (3), there are obviously differences between the special representative and the insolvency administrator. The insolvency administrator is appointed during the opening of the insolvency procedure but the special representative is appointed in the case of facts that justify the presumption of an imminent insolvency.

However, despite the fact that the regulations of the InsO cannot be applied analogical, the position of the insolvency administrator might be helpful for the determination of the position of the special representative. The insolvency administrator is a natural person who is independent from the creditors and the debtor. The governing theory for the position of the insolvency administrator is the office theory (*Amtstheorie*). Subsequently the insolvency administrator is seen as a holder of an office (*Amtswalter*) and becomes a party by virtue of office (*Partei kraft Amtes*)<sup>71</sup>. On the other hand, parts of the literature prefer the modified organ theory (*modifizierte Organtheorie*). Subsequently to this theory, the insolvency administrator in the insolvency procedure (*Insolvenzverfahren*) becomes an organ of the company.

#### 1. Modified organ theory

In two decisions the realm court<sup>72</sup> (*Reichsgericht*) made the assumption that with the opening of the insolvency procedure, the insolvency administrator enters into the posi-

<sup>70</sup> Compare to BGHZ 105, p 140, 143; BGHZ 110, p 183, 193; BGHZ 120, p 239, 252.

<sup>71</sup> Maesch, *CG in der insolventen AG*, p 47.

<sup>72</sup> The realm court was the high court in the times of the German Reich. It was the predecessor to the federal high court and its rulings are still recognised by the present jurisdiction.

tion of the organs of the stock corporation<sup>73</sup>. Further, the court also ruled that the insolvency administrator enters into the full representation of the company<sup>74</sup>. But it has to be kept in mind that the motives (*Motive*)<sup>75</sup> do not include any reference to the organ theory. However the BGH acknowledges the modified organ theory<sup>76</sup>. The modified organ theory declares the insolvency administrator as an organ himself and subsequent to this, also as a representative of the insolvent company<sup>77</sup>. However, it is granted that the insolvency administrator cannot be an organ in the sense of the company law. The insolvency administrator rather is a mandatory third organ (*Drittorgan*)<sup>78</sup> with dispossessing competences<sup>79</sup>. In to the law of liquidation he is also known as a company's mandatory foreign liquidator (*obligatorischer Fremdliquidator*)<sup>80</sup>. The foreign liquidator however can represent the company and therefore is also treated as an organ of the company.

## 2. Office theory

As mentioned before the realm court developed the leading office theory in 1892<sup>81</sup>. The court precluded the position of a representative with the argument that the powers of the insolvency administrator transcend the legal powers of a representative and therefore the insolvency administrator cannot be a representative<sup>82</sup>. He does not act in compliance with an interest, but in compliance with his legal duties<sup>83</sup>. Subsequent to this the insolvency administrator performs in a private office, which has been transferred, in his own name<sup>84</sup>. According to this point of view, the scope of duties of the insolvency administrator is the administration of foreign property, which has been entrusted to him by virtue of the law<sup>85</sup>.

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<sup>73</sup> RGZ 14, p 412, 417.

<sup>74</sup> RGZ 16, p 337, 338.

<sup>75</sup> The "motives" are the legislative materials to the civil code. They are usually used to construe the intentions of the legislator.

<sup>76</sup> Just compare to BGHZ 24, p 393, 396.

<sup>77</sup> K. Schmidt, *Der Konkursverwalter als Gesellschaftsorgan und als Repräsentant des Gemeinschuldners – Versuch einer Konkurswaltertheorie für heute und morgen*, KTS 1984, p 345, 357f.

<sup>78</sup> The term "third organship" relates to the representation of the company. The opposite is "self organship". Self organship means, that the company is represented by someone who at the same time is a member of the company, e.g. a partner in a partnership. Third organship therefore acknowledges the possibility that someone represents the company who himself is not a member of the company.

<sup>79</sup> K. Schmidt, KTS 1984, p 345, 367f.; with regard to the InsO *Ibid.*, *Haftungsregulierung in der Gesellschaftsinsolvenz – Funktion und Aufgaben des Verwalters nach Gesellschafts- und Insolvenzrecht*, KTS 2001, p 373, 374 ff.

<sup>80</sup> K. Schmidt, *Klage und Rechtshängigkeit bei Konkurseröffnung vor Klagezustellung*, NJW 1995, p 911, 913.

<sup>81</sup> RGZ 29, p 29, 36.

<sup>82</sup> RGZ 29, p 29, 36; also compare to BGHZ 44, p 1, 4.

<sup>83</sup> RGZ 29, p 29, 36.

<sup>84</sup> BGHZ 44, p 1, 4.

<sup>85</sup> BGHZ 21, p 285, 291.

Even after the introduction of the newer InsO the majority view in the literature is that the insolvency administrator is holder of an office and is a party by virtue of office who acts in his own name for and against the insolvency mass (*Insolvenzmasse*)<sup>86</sup>. The office and subsequent to this, the position of the insolvency administrator is only determined by the provisions of the act. With the opening of the insolvency proceedings, the insolvency administrator enters into the rights and duties of the debtor<sup>87</sup>. Regarding the representation theory, the supporters of the office theory allude to the fact that the insolvency administrator does not only act in the Interest of the debtor, as it would be the case if he acted for someone else<sup>88</sup>. In fact, the insolvency administrator, because of his duty for the best satisfaction of the creditors and because of his task, which is a regulatory policy, has to bear in mind different interests for the performance of his office, especially the interests of the creditors<sup>89</sup>.

### 3. Critics of the two theories

The two theories come to two different solutions with regard to the legal position of the insolvency administrator. However the theories have different approaches and are not free of criticisms. Therefore it seems to be reasonable to elaborate on these criticisms.

#### (a) Replacement of the organs

The replacement of the management organs by an insolvency administrator would be one of the strongest interferences into the company's right of self-determination. The replacement of the companies' organs by the insolvency administrator would imply that the insolvency administrator is a third organ of the company and not the holder of an office as it is assumed by the office theory. Initially the act assumes that the company itself has the right to eliminate the circumstances for the insolvency and, as the case may be, encourage into action the abolishment of the insolvency procedure<sup>90</sup>. Therefore the replacement of the organs seems to be unpractical, because neither the insolvency administrator nor the shareholders seem to be capable of ensuring the rights of the debtor during the insolvency procedure. Subsequent to this the company would not be able to act in relation to third parties (which is logical for the insolvency procedure) but even worse, would not be able to act in the insolvency procedure and therefore could

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<sup>86</sup> Uhlenbruck in Uhlenbruck *InsO*, § 80 InsO, at 53.

<sup>87</sup> Maesch, *CG in der insolventen AG*, p 52.

<sup>88</sup> Baur/Stürner, *Insolvenzrecht*, p 132.

<sup>89</sup> Baur/Stürner, *Insolvenzrecht*, p 132.

<sup>90</sup> Maech, *CG in der insolventen AG*, p 53.

not comply with the imperative rules for this procedure. However, after the opening of the insolvency procedure, a working organ structure is necessary to ensure the rights of the debtor.

(b) The insolvency administrator as a third organ

Another view in the literature points out that the insolvency administrator, after the opening of the insolvency procedure, does not replace the company's organs in toto, but that he has some eliminating competences. This point of view criticises the office theory, because it uses a quite complex model for further discussion, instead of introducing a function orientated theory for the insolvency administration under the consideration of civil and procedural principles<sup>91</sup>. The assumption that the insolvency administrator acts as a representative and therefore as a third organ during the companies' insolvency seems most capable to achieve this goal. The basis for this argumentation is a comparison between the insolvency administrator in the insolvency procedure and the liquidator in the company's insolvency. But a differentiated view of the offices (*Ämter*) is required. One difference is that the insolvency administrator, different from the liquidator, is not appointed by the company according to s 265 AktG itself but by the court. Furthermore, the company cannot get rid of the insolvency administrator itself. According to ss 57 and 59 InsO, the insolvency administrator can only be deselected by the creditor's meeting or released by the court. In addition, the insolvency administrator does not act in a foreign name but in his own name<sup>92</sup>. Subsequent to this, even the *conditio sine qua non* of an act of representation is missing.

(c) Office theory

The position of the insolvency administrator as a holder of an office also seems to be subject to criticisms. The phrase "office" referring to the insolvency administrator, can be found in several statutes in the InsO<sup>93</sup>. Furthermore s 19a of the civil procedure act *Zivilprozessordnung* [ZPO] seems to imply that the insolvency administrator is a party by virtue of office because, not the company, but the insolvency administrator is a party in the process<sup>94</sup>. In addition the special competences of the insolvency administrator, especially the rights to appeal according to s 129 f. InsO, can only be explained with

<sup>91</sup> K. Schmidt, KTS 1984, p 345, 360.

<sup>92</sup> Baur/Stürner, *Insolvenzrecht*, p 132.

<sup>93</sup> Compare to §§ 56 Abs. 2, 59 Abs. 1, 66 Abs. 1 InsO.

<sup>94</sup> Braun/Uhlenbruck, *Unternehmensinsolvenz*, p 185.



this special position in the insolvency procedure. Subsequent to this, the insolvency administrator acts in a private office that he is appointed for by the court.

Regarding the office theory, a point of criticism seems to be that it is not possible to arrange the legal position of the insolvency administrator within the systems of civil and the commercial law<sup>95</sup>. This can be put down to the fact that the legal position of the insolvency administrator is not compatible with any other legal figure of the German civil law. The structural specificities of the insolvency procedure and the involved tasks of the insolvency administrator in different areas do not permit an allocation to the known system<sup>96</sup>. In addition it needs to be kept in mind that certain rights of the stock corporation in the insolvency procedure are reserved for the organs of the company. If those organs were replaced as it is suggested by the point of view, which has been described above, those persons who acted as organs for the company would get rid of their connection to the company. Especially they would not be under the duty to act in the interest of the company.

#### (d) Solution for the insolvency administrator

At least it can be said, that even after the opening of the insolvency procedure, the organs of the stock corporation still are an integral part of the company's structure for the attendance of the company's rights. Even in the legal relationship with third parties, the insolvency administrator can not be seen as a third organ who, as a foreign insolvency administrator, is a representative of the debtor. In fact, the insolvency administrator performs a private office, for which the court appoints him. After the opening of the insolvency procedure, the insolvency administrator in legal proceedings acts for the company as a party by virtue of office. The insolvency administrator serves more than only the interests of the insolvent company so he cannot be seen as a representative and subsequent to this can not be an organ of the company.

#### 4. Impact on the special representative

The position in the literature regarding the position of the special representative seems to be closest to the office theory. The special representative acts in a public office<sup>97</sup>. It seems to be because of the special circumstances in which the special representative is appointed that the instrument is seen as one *sui generis*. However the same voice of the

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<sup>95</sup> Maesch, *CG in der insolventen AG*, p 61.

<sup>96</sup> Ott in *MüKo*, § 80 InsO, at 35.

<sup>97</sup> Rühle, *ZfV* 1956, p 545, 546.

literature saying the special representative is a holder of an office or an instrument *sui generis* also states that with the appointment, the special representative enters into all rights and duties, which are transferred to him from the organ<sup>98</sup>. But this is a strong indication for a position similar to the organ that the special representative suspends. If the special representative enters into the duties of the organ he suspends, he also enters into the fiduciary relationship. Subsequent to this, it might be possible that the organ theory fits better with regard to the special representative than does the office theory.

As we have seen before, the insolvency administrator does not become an organ or a representative of the insolvent company. One major argument for the office theory and against the representation - or organ theory - is, that the insolvency administrator has to serve different interests, especially the interests of the creditors. Subsequent to this, on the first view, the situation seems to be the same as the special representative. According to the legislative materials of s 83a VAG, the special representative primarily has to bear in mind the interests of the policyholders, in other words, the creditors of the insurance company. However, the section itself does not contain a provision saying that the special representative has to bear in mind the interests of the policyholders. So it might be possible that the special representative could be seen as an obligatory third organ following the modified organ theory. Therefore it seems to be reasonable to have a closer look at the interests the special representative has to take into concern by performing in his office.

(a) What interests has the special representative to bear in mind?

If one follows the intentions of the legislator expressed in the memorandum of the VAG, the special representative performing his office primarily has to take into concern the interest of the policyholders<sup>99</sup>. This point of view meets with criticism from parts of the literature. It has been argued that the memorandum leads to preferential treatment of the policyholders compared to the other parties like stockholders, association members, employees and the creditors of the company<sup>100</sup>. But the interests of the other parties have to be taken into account by the special representative. The outcome of this is the following question: Is the special representative, while he is performing his office, entitled to treat the interests of the policyholders preferentially over others?

<sup>98</sup> Rühle, ZfV 1956, p 545, 546; Prölls, § 81 VAG, at 108; Bähr in Fahr/Kaulbach, § 81 VAG, at 37.

<sup>99</sup> Regierungsentwurf eines *Gesetzes zur Änderung des Versicherungsaufsichtsgesetzes und anderer Gesetze* dated 24. June 2004, BT-Drucks. 15/3418, p 21.

<sup>100</sup> Bürckle, *Die Suspensierung von Unternehmensorganen durch die Einsetzung von Sonderbeauftragten der Versicherungsaufsicht*, VersR 2006, p 302, 308.

## (i) Interests of the stockholders and the creditors

While answering the question mentioned above it has to be kept in mind that the legislative interests have not expanded to the wording of s 83a VAG. On this, the BVerfG expressed that the legislative materials like the memorandum can only be consulted supportively, and with due care, insofar as they suggest to the objective content of the law<sup>101</sup>. Subsequent to this, by interpretation of the act, the so called will of the legislator or, as the case may be, the will of the parties involved in the legislative procedure, can only be taken into account insofar as they extend to the wording of the act<sup>102</sup>. The unprecedented subjective impression of the legislative instances cannot be equated with the objective content of the act itself<sup>103</sup>.

In addition, regarding the answer as to whether the interests of the policyholders can always be favoured by the special representative, it has to be kept in mind that the wording of the particular section has been changed. While in s 81 (2a) VAG (old version), the protection of the concerns of the policyholders was fixed as a principle ultima ratio, in the new version of s 83a VAG this wording was abandoned. The insuring of the concerns of the policyholders is a central and superior intention of the insurance supervision<sup>104</sup>, but it might not apply to the special representative in his function as an organ replacement who is independent from the supervising authority<sup>105</sup>. Subsequent to this, the special representative, similar to the organ he suspends, is under a duty to consider the interests of the company, the shareholders or, as the case may be, the members, the employees, the creditors and last but not least, of the policyholders<sup>106</sup>. However, the special representative like the organ he suspends is not entitled to favour the interests of the policyholders unilaterally. A preferred consideration of the interests of the policyholders however, also would constitute a collision with the express provisions of the VAG. Therefore, as an example, it can be referred to s 56a (1)(2) VAG. According to this, amounts, which are not because of a legal claim (*Rechtsanspruch*) by the insured subject to the reserve for a premium refund (*Rückstellung für Beitragsrückerstattung*), can be used for the profit participation (*Überschussbeteiligung*) not until, first of all the shareholders received a minimum dividend of 4 % of the authorised capital (*Grundkapital*). The provision for the minimum net earnings (*Mindestbilanzgewinn*) just regulates

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<sup>101</sup> Just compare to BVerfG, NJW 1952, p 737; BVerfG, NJW 1976, p 1443.

<sup>102</sup> BVerfG, NJW 1983, p 735, 738.

<sup>103</sup> Compare to BVerfG, NJW 1981, p 39.

<sup>104</sup> Winter, ZVersWiss 2005, p 105, 111.

<sup>105</sup> Bürckle, VersR 2006, p 302, 308.

<sup>106</sup> Bürckle, VersR 2006, p 302, 308.

the compensation of the competing interests between the policyholders and the shareholders<sup>107</sup>. Therefore a unilateral preference of the policyholders would contravene with the intention of compensation between the different groups of interests. In addition one could assume a violation of the protection of property rights of the shareholders according to Art. 14 (1) of the Basic Constitutional Law *Grundgesetz* [GG].

In addition, it has to be kept in mind that the unilateral consideration of the interests of the policyholders over the interests of the shareholders can lead to contradictions with the interests of insured persons of other companies<sup>108</sup>. The formation of insurance groups, (*Versicherungskonzernen*) because of principles like line separation (*Spartentrennung*) amongst others, is motivated by the supervision law<sup>109</sup>. In such a group, insurance companies participate with other insurers. If the special representative takes actions only in favour of the policyholders of the subsidiary, in which he is performing functions of the organs, this actions, by the way of the insurance company, which as a shareholder holds shares in the subsidiary, would indirectly be for the disadvantage of the insured in the share owning company<sup>110</sup>.

(ii) Interests of the employees

The appointment of a special representative also might affect the interests of the employees. However, the insurance supervision law does not provide a special consideration for the interests of the employees of the affected company. In addition, the provision of s 14 VAG (old version), that provided, that the interests of employees in the case of a transfer of portfolio according to private law had to be taken into consideration, was also abandoned in the context of the adoption of the third generation of directives (Transformation of the third generation of directives). Therefore the relevancy of the interests of the employees for the actions of the special representative cannot be derived from the insurance supervision law. Subsequent to this, a consideration of the interests of the employees can only result from company-, and as the case may be, labour law principles<sup>111</sup>.

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<sup>107</sup> Prölss, § 56 a VAG, at 13.

<sup>108</sup> Bürckle, *VersR* 2006, p 302, 308.

<sup>109</sup> Farny, *Strukturmerkmale deutscher Versicherungskonzerne im Jahr 2000*, *ZVersWiss* 2002, p 365.

<sup>110</sup> Bürckle, *VersR* 2006, p 302, 309.

<sup>111</sup> Bürckle, *VersR* 2006, p 302, 308.

## (b) Interests the suspended organs have to bear in mind

If one would follow the modified organ theory, the interests, which the special representative would have to consider must basically correspond with the interests the organ he is suspending has to consider. For this, only the management and supervisory board have to consider certain interests because they are in a fiduciary position whereas this is generally not the case for the shareholders. However, the general meeting is a representation organ of the shareholders. Its only function is to represent the shareholders, so that the answer to the question, as to what interests this organ must consider, is obvious.

In principle a director independent from being a member of the management- or supervisory board - while performing in his office has to act for the benefit of the company (*Wohle der Gesellschaft*)<sup>112</sup> or, as the case may be, in the interest of the company (*Unternehmeninteresse*). Therefore it has to be defined what interests the organs have to consider to satisfy these requirements. Surely these are the interests of the shareholders. The management- as well as the supervisory board - are in a fiduciary position. The shareholders in general elect the supervisory board. The supervisory board then elects the management board. However, besides the interests of the shareholders, there are other interests existing, which have to be considered by the organs while performing in their offices.

The basic question as to whether a manager, besides the interests of the shareholders, also has to consider the interests of other reference groups is nothing new for national or international company law<sup>113</sup>. The consideration of the interests of the shareholders in the course of the management of the company has never been expressly mentioned in the act. Instead, the legislator assumed that it is obvious that the management board, when taking actions, has to consider the interests of the shareholders, the employees and the general public.

The present literature in textbooks and commentaries understands the interest of the company as the interests of the shareholders, employees and the general public<sup>114</sup>. The recent jurisdiction however uses the terms “interest of the company” or “interest of the corporation“, but without specifying what is meant by that. According to the point of view of one member of the senate (BGH), this includes – in the sense of the stake-

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<sup>112</sup> BGHZ 135, p 244, 253f.

<sup>113</sup> Hommelhoff/Hopt/v. Werder, *Handbuch CG*, p 130.

<sup>114</sup> Compare to Hüffer, § 76 AktG, at 12; Mertens in KölKo, § 76 AktG, at 16; Semler, *Leitung und Überwachung*, at 50ff, K. Schmidt, *Gesellschaftsrecht*, § 26 II 3 c, p 768 and § 28 II 1 a, p 804 - 806.

holder-theory – the shareholders, especially minority shareholders, creditors but also employees and the general public<sup>115</sup>. Therefore a consensus can be assumed to the extent that, besides the interests of the shareholders, other groups of interests also have to be considered.

The question as to whether the interests of the shareholders can be favoured over others by the management board, however, is controversial. The prevailing opinion refuses a general preference and emphasises that the task of the management board is to deliberate conflicting interests and to balance these interests. Subsequent to this, the interest of the company would not be a constant but would have to be determined for each and every case.<sup>116</sup> According to another point of view, the interests of the shareholders are generally superordinated<sup>117</sup>. Firstly they argue that the company is something like a private party of the shareholders<sup>118</sup> and secondly that the link of the management board with the purpose of the company (s 82 (2) AktG) imposes a yield return orientated performance as long as the articles do not provide for something else<sup>119</sup>.

Finally, the second point of view does not lead to a situation where concerns other than the interests of the shareholders are not considered for the determination of the interest of the company. Besides the countless provisions of company law, which ensure the interests of employees, creditors, consumers and the general public<sup>120</sup>, for which compliance is mandatory for the management board, there are also existing terms of participation (*Partizipationsbedingungen*)<sup>121</sup> of the particular stake holder groups to ensure their future participation<sup>122</sup>. In addition, the management board is entitled to favour the interests of stakeholders over the statutory minimum limits, as far as this corresponds with the corporate expectations and maintains the reputation of the company as a good corporate citizen<sup>123</sup>. Therefore in any way the interests of the shareholders cannot generally be favoured over the interests of the other stakeholders.

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<sup>115</sup> Henze, *Leistungsverantwortung des Vorstandes – Überwachungspflicht des Aufsichtsrates*, BB 2000, p 209, 212.

<sup>116</sup> Semler, *Leitung und Überwachung*, at 51; Ulmer, *Aktienrecht im Wandel - Entwicklungslinien und Diskussionschwerpunkte*, AcP 2002, p 143, 159.

<sup>117</sup> Groh, *Shareholder Value und Aktienrecht*, DB 2000, p 2153, 2158; Wiedmann, *Gesellschaftsrecht*, § 6 II 2 b aa, p 338f.; Zöllner *Unternehmenssinnenrecht: Gibt es das?*, AG 2003, p 2, 7f.

<sup>118</sup> Wiedmann, *Organverantwortung*, p 33.

<sup>119</sup> Dazu Röhrich in *Großkomm AktG*, § 23, at. 92.

<sup>120</sup> Franke/Hax, *Finanzwirtschaft*, p 3.

<sup>121</sup> Begriff: Kreps, *Mikroökonomische Theorie*, p 521 ff.

<sup>122</sup> Franke/Hax, *Finanzwirtschaft*, p 1ff.

<sup>123</sup> Fleischer, *Unternehmenssinnen und Leitungsermessen des Vorstandes im Aktienrecht*, AG 2001, p 171, 175; Mertens in *KölKo*, § 76 AktG, at 32; Zöllner, AG 2003, p 2, 8.

Finally, the management board, when considering the interests of the insured for its actions, is well advised if it does not want to come into conflict with the supervision authority, because ensuring the concerns of the insured still is, and also will be, a central intention within insurance supervision.

In the case of a mutual, the problem of the different interests between shareholders and the insured is not apparent. The insured are regular members, so their interests are uniform. Therefore the management board of a mutual by all means has to consider the interests of the insured for his actions.

(c) Solution

So in the end it can be stated that the special representative, while performing his office, cannot privilege the interests of the policyholders. This leads us back to the theories on the position of the insolvency administrator. The major argument against the representation - or modified organ theory - is that the insolvency administrator has to take into concern different interests, like the interests of the creditors so that he cannot serve as a representative or organ. Subsequent to the aforementioned, the special representative is neither forced nor is he entitled to privilege the interests of the policyholders. So it seems to be possible to apply the modified organ theory to the special representative. It can be stated that the special representative has to take into concern the interests of the shareholders and policyholders equally. But, subsequent to the modified organ theory, the special representative would not become a part of the organ whose rights and duties are transferred to him but he would become an obligatory third organ. However, this shall not lead to undifferentiated analogies to the rights and duties of the management - and representation organs of the company - E.g. there is no doubt that the special representative has to perform actions which may derive from the tasks of the normal management organs. This follows from the special status of the special representative and the circumstances, which have to be existent for his appointment. However, this does not argue against the quality of an organ.

Subsequent to the aforementioned, the special representative does not become a part of the organ he suspends but he becomes a third organ in the supervised company. The special representative enters into a fiduciary relationship and therefore gains a position with an organ quality. In addition, the special representative is not entitled or forced to prefer the interests of the policyholders so that in fact he acts as a representative of the company. Therefore the position in the literature that the special representative acts as a

holder of an office or an instrument *sui generis* cannot be followed. The legal position of the special representative is better determined as an obligatory third organ.

(d) Other factors for the determination of the position of the special representative

The legal position of the special representative also depends on the scope of transfer of powers. This is related to what extent the special representative and the company's organ, after the appointment of the special representative, can work in coexistence. The suspended organs still persist but their powers are suspended<sup>124</sup>. Subsequent to this, the suspended organ still exists. However in the scope of the suspension it has no function<sup>125</sup>. Subsequent to this, the powers of the organ only rest in so far as they were subject to the transfer to the special representative<sup>126</sup>. In the case that a special representative is appointed to perform a transfer of the portfolio of an Insurance company, it is likely that the company's organs, like the executive board and the supervisory board, still perform their actions to the extent that their powers are not needed for the transfer of portfolio. Therefore the special representative is similar to the insolvency administrator because in the case of an insolvency, the management board is still entitled to perform management actions that are neutral to the insolvency, e.g. calling for a general meeting<sup>127</sup>.

## **VI. Corporate Governance and the special representative in Insurance Companies**

As we have seen so far the legal position of the special representative is the one of an obligatory third organ. Now it has to be determined how the special representative fits in the corporate governance framework of the supervised insurance companies. Therefore the essential question is whether the provisions of the companies act apply to the special representative.

### **1. Duties of the special representative**

The duties of the special representative are related to the cause for his appointment and the organ he suspends. So, at least, the following possibilities have to be determined.

<sup>124</sup> Mösbauer, BB 1987, p 1688, 1690.

<sup>125</sup> Prölss, § 81 VAG, at 108.

<sup>126</sup> Goldberg/Müller, § 81 VAG, at 34; Also compare to § 83 a (1) VAG: "may transfer powers ... wholly or partly".

<sup>127</sup> Maesch, *CG in der insolventen AG*, p 93.



Firstly, only the rights and duties of a part of the same organ might be suspended. Secondly, the rights and duties of the whole organ might be suspended. Thirdly, the rights and duties of two or all organs are transferred to a special representative.

As mentioned before, according to one point of view in the literature, the special representative enters into the rights and duties of the organ from whom those rights and duties are transferred. But this leads to several problems and unanswered questions in regard to the company law. Now it could be argued that the regulations from the company act do not apply for the special representative. However, it would seem unreasonable if for some reasons the company act applies and for some reasons it does not. E.g. the purpose to appoint one special representative for all organs of the company shall primarily enable a transfer of portfolio, which according to the provisions of the company law is subject to the approval of the general meeting<sup>128</sup>. Therefore it seems inconsistent if, on the one hand compliance with the provisions of the company law shall be reached for the actions the special representative has to perform, but on the other, the provisions of the company shall not or only be applicable partially for the special representative. At least the rights and duties the special representative enters into are partly granted by the companies act and not only by the articles of association.

Subsequent to the aforesaid, for the determination of the special representatives' duties, a closer examination of s 83a (1) VAG seems to be necessary. As mentioned above the special representative is a part of German public law. In public law basically the principle of the provision of the law (*Vorbehalt des Gesetzes*) is applied within the intervention administration (*Eingriffsverwaltung*)<sup>129</sup>. That means that only under a basis of authorisation (*Ermächtigungsgrundlage*) the authorities are allowed to intervene into rights of private persons<sup>130</sup>. For the appointment of a special representative, the basis of authorisation is s 83a (1) VAG. According to this, powers (*Befugnisse*), which the bodies of the undertaking hold in accordance with the law or articles of association, can be transferred wholly or partly to a special representative. Therefore the question arises as to what is meant by "powers". Does this only include the rights of the organ or does it include the duties also? However, the basis of authorisation for an intervention according to s 83a (1) VAG does not identify without problems which provisions of the company law shall be applicable, and which provisions shall not. Therefore the basis of authorisation has a lack of certainty (*Bestimmtheit*). So an interpretation of the provision is

<sup>128</sup> Vgl. Bürkle, *VersR* 2006, p 302, 304.

<sup>129</sup> Ossenbühl in Erichsen, *Allgemeines Verwaltungsrecht*, § 9, at 5

<sup>130</sup> Ossenbühl in Erichsen, *Allgemeines Verwaltungsrecht*, § 9, at 5

necessary. According to the practice of the federal courts, for this a pluralism of methods is applicable. The methods of interpretation are applied supplemental, and not in an exclusive way. No abstract ranking exists, but the importance can be levelled according to what the single method is able, in concreto, to contribute for the interpretation of the legal purpose of the provision.

First an interpretation of the wording of the provision can be considered. Therefore, it has to be determined what the meaning of the word “powers” is. According to *Rühe* the office of the special representative includes all powers of the particular organ, from which rights and obligations are transferred<sup>131</sup>. Likewise *Bürckle* assumes that the special representative enters into the rights and duties of the organ, that he suspends<sup>132</sup>. With regard to this context, *Bähr* mentions an orientation to the legal position of the original organs whose powers are transferred to the special representative<sup>133</sup>. *Prölss* however only mentions powers<sup>134</sup>. It seems *Prölss* understands the word “powers” only as the rights but not as the duties of the organ.

Generally the word “powers” means the right to undertake an action. If one understands the wording of s 83a (1) VAG in the way that only rights are transferred to the special representative, this can lead to problems e.g. with regard to the reporting duties of the management board insofar as these powers are transferred. Subsequent to this, the management board would still be under duty to report to the supervisory board. With regard to an insolvency procedure, the point of view is that the management board is still entitled to produce this kind of reports, but it is not under duty to do so anymore. Therefore, the insolvency administrator is not obliged to grant access to confidential information<sup>135</sup>. However, it seems, as this point of view cannot be easily applied on the appointment of a special representative. In the case of an appointment of a special representative, the company still exists and continues its ordinary course of business. As mentioned above, the organs keep on to exist and deal within the range of powers that have not been transferred to the special representative. Therefore, no special rules, which might release them from their duties, apply for these organs. With regard to the reporting duties, the special representative would be obliged to at least grant access to the necessary information for the remaining organ (*Restorgan*).

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<sup>131</sup> *Rühe*, ZfV 1956, p 545, 546.

<sup>132</sup> *Bürckle*, VersR 2006, p 302, 309.

<sup>133</sup> *Bähr* in *Fahr/Kaulbach*, § 81 VAG, at 37.

<sup>134</sup> *Prölss*, § 81 VAG, at 108f.

<sup>135</sup> *Maesch*, *CG in der insolventen AG*, at 93.

However, it seems conceivable that the word “powers” also includes the duties of the affected organ. E.g. the management board is under the duty to report to the supervisory board (s 90 AktG), or the duty to keep the necessary account books (*Handelsbücher*)(s 91 (1) AktG). Now, one could argue that the provisions mentioned above indeed impose a duty to take action on the management board, but they also entitle the management board to comply with these duties. Therefore, it also seems to be possible to interpret the wording of the provision so that the word “powers” also includes duties because the management board must also comply with its duties if it is also entitled to take the necessary action and has the power to do so, strictly speaking. Because of this, an exclusive interpretation with regard to the wording is insufficient.

Therefore another way to solve the problems and questions is to determine what could have been the legislators’ intention in this regard. However, it might not have been the legislators’ intention to have the companies’ act, as a whole, applied to the special representative. It seems on the one hand, the rights under the companies act necessary for fulfilling his job are applicable, but on the other hand, the duties and restrictions under the companies are not. But neither the legislation materials nor the wording of section 83a (1) VAG expressly shows these intentions.

However it also seems worth to consider a teleological interpretation, in other words, an interpretation regarding the spirit and purpose (*Sinn und Zweck*) of the provision. Such an interpretation is linked to an objective point of view<sup>136</sup>. Firstly, the special representative is an instrument for crisis management. The special representative shall ensure the fast reactivity of the supervising authority in a crisis situation. In addition, the special representative is an instrument of the deficiencies supervision (*Missstandsaufsicht*). Deficiencies shall be eliminated quickly by the special representative. Therefore the special representative is just a temporary instrument of intervention because, after the elimination of the deficiencies and the dismissal of the special representative, the original organs take over their legally designated functions. Subsequent to this, the appointment of a special representative generally is not permanent. Something else might result if the special representative is appointed according to s 83a (1)(3) VAG, and the company becomes subject to a liquidation.

However, it seems to be questionable as to whether the purpose of the provision is accommodated if the special representative acts outside of the company law provisions. If,

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<sup>136</sup> An interpretation with regard to the legislators’ intention is a subjective one.

e.g. a special representative is appointed “for all tasks” of the management board, again the question arises what happens with the reporting duties. On the one hand those duties serve the purpose of a preventive supervision of the management, on the other hand they shall avoid that the members of the supervisory board may claim that they had no information if they become subject to a claimed for damages according to ss 93, 116 AktG<sup>137</sup>. In the context of an appointment for all tasks of the management board, the special representative could be obliged to report to the supervisory board. By s 90 (3) AktG, the supervisory board would have a right to be informed (*Auskunftsanspruch*) against the special representative. The reporting duty seems to be problematical against the background, that in general the supervisory board does not seem to have a direct power, e.g. by dismissal, to influence the special representative. Subsequent to this, one could argue that the reporting duty against the background of a preventive supervision becomes obsolete. However, an application still seems to be reasonable, because the supervisory board stays informed and a sorted transition becomes possible after the resignation of the special representative. Last but not least, a possible role model status (*Vorbildwirkung*) should also be considered. Specifically in connection with s 83a (1)(1) and (1)(2) VAG, a special representative is appointed if the original organs have failed. In this case the task of the special representative is to eliminate the deficiencies, because in the case of s 83a (1)(1) VAG the special representative will work closely with the remaining part of the organ. Therefore a role model status of the special representative for the future of the company requires the application of the company law provisions for the work of the special representative.

However, a limitation has to be set where, on the one hand the act is certain enough, so that an interpretation does not become necessary and on the other hand, where the application of the provisions of the company law would undermine the spirit and purpose of the appointment of a special representative. Conceivable in these circumstances, is the case when a special representative is appointed for the management- and the supervisory board - with regard to the reporting duties of the management board against the supervisory board. Also the right of the supervisory board to dismiss members of the management board (s 84 (3) AktG) could be problematical if the special representative is appointed for the function of a member of the management board or even the whole board.

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<sup>137</sup> Hüffer, § 90 AktG, at 1.

With regard to the restrictions that exist for the managing organs it seems to be questionable whether they shall be applicable to special representative or not. In this connection, one could think about the minimum occupancy, e.g. of the management board (ss 76 (1) sentence 2, 95 sentence 1 AktG). However it seems as the wording of s 83 a (1) VAG with regard to the restrictions for the special representative is certain enough to deny the application of those particular provisions of the companies act to the special representative.

None of the methods before allow or deny a full application of the companies act to the special representative. However, it seems to be reasonable to apply at least some of the provisions of the company's act to the special representative. Hence finally a way to resolve the questions and problems arising out of the special representatives' special position in the corporate governance framework can be seen in the context of a consideration for each and every case regarding the restrictions and duties a normal organ would have to comply with. Therefore these restrictions and duties will be subject to the elaboration.

(a) Restrictions on the organs

S 76 (1) sentence 2 AktG implies that the management board of a stock corporation with a share capital of more than 3 million € has to have at least 2 management board members. This is a mandatory rule. Something similar is implied by s 95 sentence 1 AktG for the supervisory board. The supervisory board has to have at least 3 board members. However section 83a (1) VAG mentions the possibility to transfer the rights and powers of one or more organs completely or partly to only one special representative. Therefore however, the wording of the provision is certain enough, because it expressly mentions the possibility that powers can be transferred wholly or partly to only one special representative. Worth to mention in this regard is s 108 (2) sentence 3 AktG, which provides that the supervisory board only constitutes a quorum if at least three board members are present in a meeting. However the provision of s 83a (1) is certain enough so that s 108 (2) sentence 3 AktG is not applicable with regard to a special representative. The Transfer of all powers to one special representative only makes sense if he is solely allowed to perform them.

Another problem is the principle of separation of powers between the management- and supervisory board in a German stock corporation. It is a common point of view that one

special representative can replace all of the companies' organs<sup>138</sup>. This means that all the rights and duties of the management- and supervision board and even of the general meeting are united in one person. However s 105 (1) AktG rules that a member of the supervisory board cannot also be a member of the management board simultaneously. Subsequent to this, if a special representative were appointed for the management- and the supervisory board this would contravene with s 105 (1) AktG. S 105 (2) AktG seems to contain a solution for this problem. According to this section, the supervisory board can, for a limited period of time, appoint single members of the supervisory board to act as representatives of missing or impeded management board members. But according to s 105 (2) sentence 3 AktG, during the time the supervisory board members act as representatives of such management board members, they are not allowed to perform any action as a member of the supervisory board. Also in this regard, the certainty of s 83a (1) VAG is sufficient. Powers of the organs can be transferred wholly or partly to a special representative. According to *Bürckle*, the wording expressly provides the possibility to appoint one special representative for all organs<sup>139</sup>. However, it is worth having a short look at the aspect of the spirit and purpose of the provision because here an extensive intervention in the company law framework takes place.

The purpose of the provision of s 105 (1) AktG arises out of the separation of functions between management and supervisory board. Subsequent to this, the same organ cannot perform the management and supervision of the company<sup>140</sup>. If a special representative is appointed for the management- and the supervisory board, one level of control, which the legislator sees as essential, falls apart<sup>141</sup>. The possibility to appoint one special representative for all organs however is justified by enabling a transfer of portfolio according to s 14 VAG<sup>142</sup>. For such a transfer of portfolio however, the approval of all organs is necessary. This approval can be generated by only one special representative, so that a fast reactivity of the supervising authority is ensured. However, it has to be kept in mind that the special representative, with regard to his activities as a member of the management board, cannot effectively control himself. By this, the special representa-

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<sup>138</sup> Just compare to *Bürckle*, VersR 2006, p 302, 304.

<sup>139</sup> *Bürckle*, VersR 2006, p 302, 304.

<sup>140</sup> Hüffer, § 105 AktG, at 1.

<sup>141</sup> Regierungsentwurf eines *Gesetzes zur Kontrolle und Transparenz im Unternehmensbereich (KonTraG)* dated 28. January 1998, Bt-Drucks. 13/9712, p 11.

<sup>142</sup> *Bürckle*, VersR 2006, Fn. 22.

tive loses an internal level of advice, because one of the tasks of the supervisory boards is the accompanying advice for the management board<sup>143</sup>.

Furthermore, the appointment of only one special representative for all organs can be seen as a special phenomenon that will only be used by the supervising authority in the case of an appointment according to s 83a (1) (3) VAG and then only under the strict premises for the proportionality (*Verhältnismäßigkeit*) of an administrative action. Therefore it is by all means necessary to balance the intervention in the company law framework. The appointment of only one special representative for all organs therefore can be seen as an action ultima ratio.

(b) Reporting duties

S 90 (1) AktG states the reporting duties for the management board to the supervisory board. The provision primarily aims at the preventive supervision of the management<sup>144</sup>. As mentioned before, another reason for the reporting duties of the management board is to avoid the situation where the supervisory board can refer to a lack of knowledge if they are subject to a claim for damages<sup>145</sup>. So the question is whether the special representative, if he is appointed for the management board, also has to comply with the duties under s 90 (1) AktG.

If the special representative is appointed for a member or the whole management board, he enters into the position of the organ. Like the management board he operates the business according to s 76 (1) AktG in his own diligence<sup>146</sup>. If the special representative would not be subject to the reporting duties of s 90 AktG in the case of his appointment for a whole organ, this would lead to a serious lack of knowledge on the side of the supervisory board. But even in the case of an appointment according to s 83a (1) (1) VAG, if the special representative replaces a director of the management board who contravenes against the provisions of s 7a (1) VAG, the special representative is appointed for the tasks of that particular director. Subsequent to this, if the special representative would not be under the reporting duties, a lack of knowledge for the particular field the special representative is appointed for would arise, at least on the side of the supervisory board. Therefore it also would be unreasonable to put the remaining part of the management board to report on the field, which is governed by the special represen-

<sup>143</sup> Bürckle, VersR 2006, p 302, 310.

<sup>144</sup> Compare to Hüfer, § 90 AktG, at 1.

<sup>145</sup> Hüfer, § 90 AktG, at 1.

<sup>146</sup> Bähr in Fahr/Kaulbach, § 81 VAG, at 37.

tative. The special representative is closest to the information of this particular field and therefore predestined to report on this particular field. Therefore it seems reasonable to apply the reporting duties of s 90 AktG to the special representative in the position of the management board.

Subsequent to this, according to s 90 (3), the supervisory board is entitled to ask the special representative for a report. This makes sense because the special representative is subject to the supervision of the financial supervisor to the same extent as the organ he is appointed for. However, especially in internal circumstances, the supervision of the BaFin is a different one from the supervision under the companies act. The supervising authority only has the powers granted under the VAG. Therefore it seems reasonable to grant the supervisory board reporting duties and to enable the supervision of the special representative. However it has to be kept in mind that this would lead to a pure informative supervision only<sup>147</sup>.

A special situation arises when a special representative is appointed for the rights and duties of the management board and the supervisory board. In this particular case the special representative would have to report to himself what leads to the question whether this is reasonable or not. However in the case that the special representative is appointed for the management- and the supervisory board - and if, after an undetermined period of time the original organs re-enter in their positions, an abdication on the reporting duties would lead to a lack of information both on the side of the management - and the supervisory board. This would contradict the further purpose of the provision; that the members of the supervisory board, subject to a claim for damages, cannot argue that they had a lack of knowledge. On the other hand, a lack of knowledge infringes on the purpose of preventive supervision of the management board. As mentioned before, in this case a level of control is missing. However this level of control is crucial for the internal supervision. But, due to the fact that the reporting duty is one for the preventive supervision of the management board, it seems rather unreasonable to apply such duties to the special representative. However, if it is applied to the special representative in such a position the purpose of the provision for a preventive supervision of the management board becomes meaningless.

Also there are reporting duties of the management board mentioned under the German Corporate Governance Codex. According to s 3.4 (2) of the Codex, the management

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<sup>147</sup> Compare to Hüffer, § 111 AktG, at 19.



board informs the supervisory board regularly, without delay and comprehensively, of all issues important to the enterprise with regard to planning, business development, risk situation and risk management. The Management Board also has to point out deviations of the actual business development from previously formulated plans and targets, and has to indicate the reasons thereof. However it should be kept in mind that the provision of s 3.4 (2) of the Codex does not state any new reporting duties, which are different from the duties under s 90 AktG. The provision has only a repetitive character and does not provide for any particular regulation itself. It only straightens out the provision under s 90 AktG. Subsequent to this it remain with the reporting duties under s 90 AktG.

(c) Actions where principal approval is required

For some actions of the management board, the principal approval of the supervisory board or the general meeting is required by the companies act. According to s 111 (4) AktG, some kind of actions can only be performed with the approval of the supervisory board. These actions primarily are: an increase of the share capital (s 182 AktG), a reduction of share capital (s 222 AktG), a change in the articles of association (s 179 AktG) and the liquidation of the company (s 262 AktG). In connection with the introduction of the Transparency and Publicity Act *Transparenz- und Publizitätsgesetz* [TransPubG] s 111 (4) sentence 2 AktG has been changed to the effect that the general meeting and the supervisory board not only can define actions where principle approval is required, but also have to set up an index of such actions<sup>148</sup>.

Similar to the reporting duties, s 111 (4) AktG aims for the preventive supervision of the companies management<sup>149</sup>. The method therefore is the introduction of principal approvals by the supervisory board. However the power of veto enables the supervisory board to affect the management of the company<sup>150</sup>. In the case of fundamental decisions the supervisory board should be integrated in the process of decision-making<sup>151</sup>. However, if the special representative is appointed for the tasks of the management board, the requirement of principal approval could strongly affect the work of the special representative. This has to be reviewed critically, especially against the background of the special representative, because the instrument should enable a fast and efficient Action

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<sup>148</sup> Dietrich, *Der neue § 111 Abs. 4 Satz 2 AktG – Zustimmungsvorbehaltspflicht auch für unternehmerisches Unterlassen?*, DStR 2003, p 1577.

<sup>149</sup> Hüffer, § 111 AktG, at 16.

<sup>150</sup> Hüffer, § 111 AktG, at 16.

<sup>151</sup> Entwurf eines *Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz und Publizitätsgesetz)*, BT-Drucks, 14/8769, p 17.

of the supervising authority. If the supervisory board, according to s 111 (4) AktG refuses its approval, it could be questionable whether this would contravene the purpose of the special representative, especially because then a decision of the general meeting according to s 111 (4) sentence 3 AktG would become necessary if the special representative, in the function of the management board, demands it.

Therefore a consideration of the situation with an insolvency administrator might be helpful. If an insolvency administrator is appointed by the insolvency court the supervision- and approval duties and competences of the supervisory board, only extend to the performance of the procedural rights by the management board. This is because the management board, after the opening of the insolvency procedure, is precluded from managing the company because of the competence of the insolvency administrator to administrate the assets of the company (*Vermögensverwaltungsbefugnis*). Other ways of supervision or control, especially to the extent of the administration of the assets of the company through the insolvency administrator, do not exist<sup>152</sup>. The supervisory board has no competence whatsoever to supervise the management board.

For the special representative the situation seems to be slightly different. The supervision- and control activities of the supervisory board, with regard to the special representative, are highly restricted. Specifically, it has to be kept in mind that the supervising authority, with regard to the basis of authorisation and also the premises for the proportionality, is entitled to also transfer the powers of the supervisory board to a special representative. However if the necessary premises are missing, it cannot be justified why the provision of principal approval should be abrogated for the actions of the special representative. Insofar, the special representative is bound to the provisions of principal approval of the supervisory board. If he still wants to pursue his action he is entitled to demand a decision of the general meeting. Finally with regard to the special representative, the provisions of principal approval can be seen as the most extensive manner of supervision by the supervisory board.

If the special representative is appointed for the tasks of the management- and supervisory board the problems arising are similar to the problems with regard to the reporting duties according to s 90 AktG. The special representative, in his function as a member of the supervisory board, cannot control himself with regard to his function as a member of the management board. In addition, it has to be kept in mind that if the principal ap-

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<sup>152</sup> The insolvency administrator is supervised by the creditors meeting and the insolvency court (§§ 58, 69 InsO).

proval is refused, the action of the management board has to remain undone<sup>153</sup>. That means where principal approval has not been granted or where the approval has been denied the action of the special representative becomes voidable and the special representative exposes himself to an unnecessary risk of liability. Therefore, even under these extraordinary circumstances, it seems reasonable to ask for principal approval of the special representative in the capacity of the supervisory board. However s 111 (4) AktG loses its meaning as an instrument of the preventive supervision of the management of the company.

S 119 (1) AktG states the circumstances in which principal approval through a general meeting is required. However, trend-setting company decisions like a transfer of the portfolio, are not mentioned in this paragraph of the section. Therefore s 119 (2) AktG states, that the general meeting can only decide with regard to actions of the day to day management if it is explicitly asked for by the management board. However in the “*Holz Müller decision*”<sup>154</sup>, the BGH created the requirements for a mandatory consultation of the general meeting, even beyond the regulations of the act. According to the BGH in the case of “*Holz Müller-constellations*”<sup>155</sup>, the discretion of the management board whether to provide the general meeting with a proposal for a resolution or not can be reduced to zero. Indeed, to the extent that the act does not provide something else, it is in the discretion of the management board, whether it provides the general meeting with a proposal for a resolution to reduce its accountability<sup>156</sup>. However there are fundamental decisions that interfere with the membership rights of the stockholders, and interests of fortune typified in the stock property, in such an extensive way that the management board can not reasonably assume that it can make these decisions in its own stewardship without participating the general meeting. From this decision it results, that the BGH acknowledges an unwritten competence for approval by the general meeting only in literally “exceptionally” cases; namely only in the case that an action interferes with the core area of the company’s business and the company’s structure and they are fundamentally modified<sup>157</sup>. Subsequent to this, it is a matter of “blatant” cases,

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<sup>153</sup> Hüffer, § 111 AktG, at 18.

<sup>154</sup> BGHZ 83, p 122 ff.

<sup>155</sup> In general those are such decisions of the management board, which are of such an invasive nature that the company will not look the same afterwards, e.g. where the whole assets of the company shall be sold.

<sup>156</sup> According to § 93 (4) sentence 1 AktG the members of the management board are not liable if they acted with regard to a lawful decision of the general meeting.

<sup>157</sup> BGH, Urteil v. 26.04.2004 - II ZR 154/02.

which come close to an asset transfer<sup>158</sup> (which according to s 179a AktG needs the approval of the general meeting).

S 119 AktG in principle aims at a balance of power between the company's organs, especially between the management board and general meeting<sup>159</sup>. The in s 119 (1) AktG included catalogue of competences can usually be classified in regularly returning or ongoing measures and in structural measures or basic competences<sup>160</sup>. The argumentation for the application of s 119 AktG in principle is the same as for s 111 AktG. However in this case the argument is not related to the control of the management board but to the fundamental relevance of the decisions according to s 119 AktG. Especially worth mentioning are s 119 (1)(1), (1)(5), (1)(6), and (1)(8) AktG as well as the decisions which, because of their fundamental relevance according to s 119 (2) AktG, have to be decided by the general meeting.

The application of s 119 AktG does not contravene the spirit and purpose of the special representative. Similar to s 111 AktG, the supervising authority, within the basis of authorisation and the requirements for the proportionality of the action, can also appoint a special representative for the powers of the general meeting. However, if the necessary requirements for this are not satisfied, the special representative in his function as management- or supervisory board - is bound to the scope of tasks according to s 119 AktG. That means where a special representative wants to perform a transfer of portfolio according to s 119 (2) AktG he still will be under the duty to ask the general meeting for a decision. Otherwise the action e.g. the transfer of portfolio can be voidable and the special representative exposes himself to an unnecessary liability.

(d) Declaration to the German Corporate Governance Codex (s 161 AktG)

As mentioned at the very beginning of this elaboration, section 161 AktG asks the management board and the supervisory board to declare whether they have complied with the German Corporate Governance Kodex or, in the case of a non compliance, to explain themselves. Section 161 AktG is only applicable to listed companies. Therefore its relevance with regard to the special representative is not as large because only a small percentage of the German insurance industry is listed in the stock exchange.

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<sup>158</sup> Hüffer, § 119 AktG, at 18.

<sup>159</sup> Hüffer, § 119 AktG, at 1.

<sup>160</sup> Zöllner in *Kölner Kommentar*, § 119 AktG, at 13ff.

However, the purpose of the provision is the publicity of the declaration in its particular existence<sup>161</sup>. That means that the general purpose of the section is to make the declaration itself available to the public. Furthermore the purpose of the provision, by means of publicity of the compliance with the code's recommendations, is to attract a principle interest for the code<sup>162</sup>. Subsequent to this other companies' shall be encouraged to comply with the recommendations of the codex as well. In addition the provision also serves for the information of the participants in the capital markets<sup>163</sup>. The declaration duty under s 161 AktG is directed to the management- and supervisory board.

As stated above the special representative is not bound to the recommendations of the code. He also does not betake himself in the danger of a liability because the recommendations with regard to an internal liability are not formal laws, and because, with regard to the external liability, the matter of fact of the particular provision normally is not fulfilled<sup>164</sup>. However if he is appointed for one or both of the organs, he enters into their rights and duties. The sole fact that he is not bound to the recommendations does not exempt him from declaring in accordance with s 161 AktG. Firstly this is because the original organs are not bound to the recommendations as well but have to declare whether they complied with the recommendations or not. Another reason is that because one purpose of s 161 AktG is to inform the capital markets (including of course the shareholders) and the public (e.g. stakeholders) it seems to be reasonable to apply s 161 AktG to the special representative as well. That way at least the shareholders and also the other stakeholders stay informed about what happened in the company. Also, the special representative is not excessively burdened with this duty because the declaration is due only once in a year. A serious interference with his work therefore seems to be excluded. In addition, the appointment of a special representative should not lead to a further lack of transparency, because the purpose of the rule seems to be to create transparency. The appointment of a special representative on the other hand will usually also be linked to a lack of transparency in the affected company. Finally, because of the special circumstances of his appointment, the special representative should not have a problem explaining a non-compliance with the code. Therefore there are no arguments against obliging the special representative with the declaration duty according to s 161 AktG.

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<sup>161</sup> Entwurf eines *Gesetzes zur weiteren Reform des Aktien- und Bilanzrechts, zu Transparenz und Publizität (Transparenz und Publizitätsgesetz)*, BT-Drucks, 14/8769, p 22.

<sup>162</sup> Reg. Begr., BT-Drucks, 14/8769, p 22.

<sup>163</sup> Reg. Begr., BT-Drucks, 14/8769, p 21.

<sup>164</sup> Compare to Hüffer, § 161 AktG, at 25ff.

## (e) Organisational standards and bookkeeping (s 91 AktG)

S 91 AktG provides that the management board has to keep the necessary books of account (*Handelsbücher*) (s 91 (1) AktG) and that the management board has to introduce a system of supervision to the company (s 91 (2) AktG). Therefore s 91 AktG is the concretion of two aspects of the broader management responsibility of s 76 (1) AktG<sup>165</sup>. Specifically, paragraph 2 obligates an organisational standard, which should enable the early detection of dangers for the endurance of the company<sup>166</sup>. This is also known as a duty to ensure the endurance of the company. However the provision does not ask for the introduction of more or less extensive risk management system<sup>167</sup>.

However s 91 (1) AktG does not impose a duty of accounting on the management board, but it imposes a duty to control, because the necessary duty of accounting is one of the company itself<sup>168</sup>. The purpose of the duty, in principle, is the creditors' protection<sup>169</sup> by ways of self-control as well as a documentation of business transactions. The duty itself has a public law character<sup>170</sup>. The supervision of the accounting is an overall responsibility of the management board. Even in the case of a departmental division, the unconcerned members of the management board remain responsible for the supervision<sup>171</sup>. Subsequent to this, the special representative would be under the obligation of supervision, even if he were appointed just for the function of a single member of the management board. An application of the accounting responsibility to the special representative however does not contravene with the ratio of s 83a (1) VAG, especially because in the cases of s 83a (1)(3) VAG, such a supervision will be quite appropriate.

S 91 (2) AktG is however of particular relevance. The purpose of the provision is to highlight the management responsibility of the management board with regard to trends, which are dangerous for the endurance of the company. By providing organisational requirements, which are described as the early detection of dangers for the endurance of the company, and by introducing a system of supervision, the purpose of the provision

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<sup>165</sup> Hüffer, § 91, at 1.

<sup>166</sup> Hüffer, § 91, at 1.

<sup>167</sup> Hüffer, § 91, at 1.

<sup>168</sup> Compare to § 238 (1) HGB in connection with § 3 (1), § 6 HGB

<sup>169</sup> Members are only protected by this provision to the extent that they are also creditors to the company. This is obvious for the members of a VVaG because those members usually have an insurance contract with the VVaG so that they are creditors to the company under this insurance contract. With regard to an insurance stock corporation the situation is a different one. The shareholders are usually not in an insurance relation with the company and the policyholders are not necessarily shareholders of the company.

<sup>170</sup> Hüffer in *Großkomm. HGB*, § 238, at 2.

<sup>171</sup> Hüffer in *Großkomm. HGB*, § 238, at 23.

is ensured<sup>172</sup>. However the provision is not without controversy, especially because the internal supervision as a subject of an extended examination at best seems to be appropriate for listed companies, but the provision applies to all companies.

Therefore, first a concretion of the organisational requirements is necessary. As a first step, s 91 (2) AktG obliges the management board to ensure the early detection of dangers for the endurance of the company by taking appropriate actions. For this purpose "trends" do not have the meaning of "risk situation" but adverse changes specific to the company<sup>173</sup>. Dangers to the endurance of the company mean lasting changes with regard to the financial status, profit situation or the financial standing, which may have serious effects on the company<sup>174</sup>. Actions that are appropriate for the early detection have to be considered in front of the background, that trends can be detected, if they become known to the management board. The earliness is given if the trends get known by the management board before they become a danger to the endurance of the company<sup>175</sup>. The actions are appropriate if, according to experiences in the past, one can expect that the management board will be informed in time<sup>176</sup>.

In a second step the implementation of a supervision system is required. However this does not mean a general risk management system. Subject to the supervision are not the trends which might bear a risk but the compliance with the initiated actions<sup>177</sup> for an early detection of such trends. This means an internal control with regard to whether the disposed actions take place, namely, whether internal revision and control communicate their knowledge in due time to the management board<sup>178</sup>.

For the special representative s 91 (2) AktG is of some relevance, because, despite the cases of s 83a (1)(1) VAG but especially in the case of s 83a (1)(3) VAG, the early detection of actions which are dangerous for the endurance of the company has failed. The application of the provisions of s 91 AktG to the special representative does not contravene with the spirit and purpose of s 83a (1) VAG. The special representative is an instrument of danger defence (*Gefahrenabwehr*)<sup>179</sup>. As mentioned above, the special representative shall prevent and correct deficiencies. Therefore it seems reasonable that the

<sup>172</sup> Hüffer, § 91 AktG, at 4.

<sup>173</sup> Hüffer, FS Imhoff, p 91, 98f.; Seibert, FS Bezenberger, p 427, 437.

<sup>174</sup> Entwurf eines *Gesetzes zur Kontrolle und Transparenz im Unternehmensbereich (TransPuG)* dated 28. January 1998, BT-Drucks. 13/9712, p 15.

<sup>175</sup> Reg. Begr., BT-Drucks. 13/9712, p 15.

<sup>176</sup> Reg. Begr., BT-Drucks. 13/9712, p 15.

<sup>177</sup> Hüffer, § 91 AktG, at 8.

<sup>178</sup> Hüffer, § 91 AktG, at 8.

<sup>179</sup> Bürckle, VersR 2006, p 302, 303.

special representative has to take actions which lead to the early detection of such trends. In addition, the application of s 91 (2) AktG would not lead to an unreasonable burden for the special representative because he would be obliged to take actions which ensures the early detection of “only” trends which are dangerous for the endurance of the company. Within the normal course of business of the work of the special representative, he would be forced to take such actions anyway to prevent and correct deficiencies. The implication of an advanced compliance - and risk management - system would however not be burdened on the special representative. Therefore the application of s 91 (2) AktG to the special representative would not contravene with the spirit and purpose of s 83a (1) VAG.

(f) Range of applicable duties

Finally it is questionable to what extent the duties are applicable to the special representative. Against the background of an appointment of the special representative for the tasks of all organs, one could argue that it is impossible to transfer all duties under the companies act to the special representative because this would de facto disable the instrument. However it seems that the legislator expressly stated the possibility to appoint one special representative for all organs of the company and the legislative materials do not include any hint as to whether the special representative wholly or just partially enters into the duties of the affected organ.

As already mentioned above, the application of duties is limited to the extent, that it unduly constrains or even frustrates the work of the special representative. But it has to be kept in mind that most of the duties are connected to the special representative in his function as a member of the management board and according to the companies act and, in principle, it is possible to only appoint one member of the management board for the management of the company. It would also be problematical to decide which duties would be applicable and which duties wouldn't, especially where the application leads to an excessive burden. Finally, it has to be kept in mind that the appointment of one special representative for all organs is something of a special case, which is only possible under very strict requirements.

To the extent that the special representative is appointed for the tasks of a management board which consists of more persons, the question where to set a limit cannot not only be answered with regard to the single duties in which the special representative enters into, but the question is one of the discretion of the supervising authority as to how



many special representatives are appointed. Therefore with regard to the duties, there cannot be a limit to the range of application. Subsequent to this, the duties are applicable as a whole, under the condition that the single duty is applicable to the special representative.

(g) Findings

In the end it can be stated that some provisions and principles do not serve a purpose in regard to the appointment of the special representative. Especially worth mentioning are the principles of separation of powers and the provisions for the minimum members of the two boards. To this regard s 83a (1) VAG is certain enough so that the restrictions for the normal organs under the company's act cannot be applied to the special representative.

In addition, the special representative is not bound to the recommendations of the German Corporate Governance Kodex if he is appointed for an organ of a listed company. However the special representative according to s 161 AktG is under the duty to report the compliance or to explain the non-compliance with the recommendations of the Kodex.

The duties of the organs that the special representative is appointed for however, have to be fulfilled by the special representative himself. These are specifically the reporting duties under s 93 AktG. The purpose of s83 a (1) VAG is not contradicted by the application of the duties under the company's act on the special representative.

2. Relation of the other Organs to the special representative

If a special representative is appointed, the question of the relation of the remaining organs to the special representative arises. To the extent that the special representative enters into the functions of the management board, the question arises as to whether he should be supervised by the supervisory board. As already mentioned above, the special representative is to some extent similar to the insolvency administrator. Therefore a closer look at the position of the insolvency administrator is worthwhile. In addition the duties of the non-affected organs also depend on the cause for the appointment of the special representative and the organ he suspends.

## (a) Management board

The management board has the function of an entrepreneur in the company<sup>180</sup>. Therefore it is the primary representation organ of the company<sup>181</sup>. The management board manages the company in its own responsibility<sup>182</sup> and therefore has to make the necessary and fundamental decisions<sup>183</sup>. Although the obligatory constitution of the company implies a separation of powers, by which control - and supervisory rights - are determined<sup>184</sup>, the allocation of competences according to s 76 (1) AktG provides that the management board has the most excessive competences and responsibility with regard to the company.

In the case of an appointment of an insolvency administrator, in the area of company law, the management board keeps its management rights to the extent that those are neutral to the insolvency<sup>185</sup>. Regarding the insolvency administrator, those rights can be found for the area inside of the company, especially with regard to the other organs of the company. Subsequent to this, the management board's right to call for a general meeting (s 121 (2) AktG) has to be mentioned especially<sup>186</sup>. This seems to be somehow similar to the special representative because after his appointment the organ still exists and therefore can perform actions under the rights, which have not been transferred to the special representative.

However, in the case of an insolvency, it is questionable as to whether the management board, which by the opening of the insolvency procedure is mostly released of its management competences, is still in the duty to report to the supervisory board. During the insolvency procedure, the management of the company is a task of the insolvency administrator, so that the management board still might be entitled to report to the supervisory board but during the insolvency this is not a duty of the management board anymore<sup>187</sup>.

In the case of an appointment of a special representative, this has to be handled in a different way. Where a special representative is only appointed for parts of the management board, the non-affected parts are still under the reporting duty. The provision of s

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<sup>180</sup> Compare to Semler, at 1ff.

<sup>181</sup> Compare to §§ 78 (1), 111 (2) sentence 2, 112, 246 (2) sentence 2, 249 (1) sentence 2 AktG.

<sup>182</sup> Compare to § 76 (1) AktG.

<sup>183</sup> Mertens in *KöKo*, § 76 AktG, at 4.

<sup>184</sup> Compare to K. Schmidt, *GesR*, p 866.

<sup>185</sup> Hüffer in *MüKo*, § 264, at 68.

<sup>186</sup> Maesch, *CG in der insolventen AG*, p 93.

<sup>187</sup> Maesch, *CG in der insolventen AG*, p 93.

90 AktG primarily aims for the preventive supervision of the management of the company<sup>188</sup>. The provision would become meaningless if the unaffected parts would not have to report to the supervisory board, especially because the instrument of the special representative is a temporary one and would therefore contradict with regard to the circumstances, which lead to the appointment of the special representative.

However, in the case that the special representative is appointed for all the rights and duties of the management board, as in the case of the Ancora Versicherungs-AG<sup>189</sup>, the suspended management board is not under the duty to report to the supervisory board anymore, because this duty also has been transferred to the special representative. Subsequent to this the situation is similar to the situation of the insolvency administrator. The organ can only perform actions for which it is still entitled. In the case of an appointment of a special representative for all tasks of the management board, such powers cease to exist.

#### (b) Supervisory board

In the active stock corporation, the supervisory board works principally as a control organ (s 111 (1) AktG). Its control duties and rights include the supervision of the running and future businesses of the management board. However, actions of the management of the company cannot be transferred to the supervisory board. Only in the case of s 112, and s 111 (2) sentence 2 AktG the supervisory board is entitled to represent the company.

#### (i) Representation in the administrative procedure

With regard to the administrative procedure (*Verwaltungsverfahren*) it is questionable who is representing the company. The appointment is an action of the authorities, the BaFin, that rules a single case, namely the case which justifies the appointment, which has an external effect against the affected company and which is based on public law, namely the insurance supervision law which forms a special part of the trade supervisory centre. Therefore the appointment of a special representative is an administrative action (*Verwaltungsakt*) in the sense of s 35 of the Administrative Procedure Act *Verwaltungsverfahrensgesetz* [VwVfG]. The same results from a reverse of s 89a VAG,

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<sup>188</sup> Hüffer, § 90 AktG, at 1.

<sup>189</sup> First appointed at the 13.02.2006 for a part of the tasks of the management board. Amended at the 24.05.2006 for all tasks of the management board.

which excludes the suspensiveness of an objection (*Widerspruch*) or an action of opposition (*Anfechtungsklage*) for actions according to s 83a VAG.

Subsequent to this, appropriate actions against the appointment of a special representative are objection, action of opposition or an application for urgent legal protection (*Eilrechtsschutz*) aiming for recovery of the suspensiveness according to s 80 (5) of the Rules of the Administrative Courts *Verwaltungsgerichtsordnung* [VwGO]. According to s 42 (2) VwGO or, as the case may be, s 42 (2) VwGO analogy in general, the addressee of the administrative action is authorised to enter into legal. Therefore the insurance company and the members of the affected organs are entitled to enter into legal action<sup>190</sup>.

However, it is questionable who is entitled to represent the company in the legal proceedings if a special representative is appointed for all tasks of the whole management board. The representation of the company in legal proceedings by the supervisory is not expressly mentioned in the allocation of rights and duties in the company law. In fact, the management board generally, because of its right to represent the company according to s 78 (1) AktG, represents the company in legal proceedings<sup>191</sup>. However these powers, with his appointment, are transferred to the special representative. As mentioned above, the special representative is to some extent bound to the interests of the company. Therefore one could argue that in the case where reasons exist, which would justify the application of legal means, the special representative because of his legal position would be under obligation to appeal against his appointment. However it has to be kept in mind, that this would lead to a serious conflict of interest within the person of the special representative and the impartiality would not be ensured any further. Subsequent to this, it could not be ruled out that this would be to the disadvantage of the affected company.

In addition it should be kept in mind that an objection in the German administrative law procedure must not be provided with reasons, so that the company can object even if there are not reasons, which might imply a success of the objection. This is because in the administrative law, in the case of an objection, the authority is under the obligation to re-examine whether its action was appropriate and within the legal boundaries. This means that the original organ for example would not be under the duty to search for a reason for an objection. The original organ could object to the appointment without giv-

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<sup>190</sup> BVerwG, VersR 1963, p 177 (In addition the general meeting can take legal actions).

<sup>191</sup> Hüffer, § 78 AktG, at 4.

ing reasons for such an objection. However it cannot be assumed that a special representative would object to his appointment if there were no obvious reasons for such an appointment. Therefore a representation by the special representative seems to be inappropriate.

According to s 112 AktG, the supervisory boards represents the company vis-à-vis the members of the management board. Therefore it seems to be considerable, that the supervisory board must be entitled represent the company and therefore must be entitled to appeal, if the original management board powers (e.g. all powers of the management board or those powers which are related to the representation in legal proceedings) have been transferred to the special representative. This consideration requires that an analogy to s 112 AktG, with regard to the administrative procedure, is possible. In general, s 112 AktG can be used in an analogous way to close an unforeseen loophole in the law (*planwidrige Gesetzeslücke*)<sup>192</sup>.

The legislative materials of the VwGO do not seem to give any hint for such a case. Therefore one could assume that an appeal by the supervisory board should not be explicitly excluded. According to the wording of the provision it cannot be ruled out, that members of the supervisory board are entitled to represent the company in legal proceedings because under the provision of s 112 or s 111 (2) sentence 2 AktG the supervisory board can be the representing organ of the company. Subsequent to this, it has to be examined whether a situation similar to the facts of the case governed by s 112 AktG exists<sup>193</sup>, which because of a loophole in the law has to be filled with an analogous application of the provision.

Producing material as to whether two facts of the case are similar, so that they have to be rated equally, is the spirit and the purpose of the legal provision<sup>194</sup>. The purpose of s 112 AktG is the insurance of the concerns of the company, if the management board does not show the required impartiality, because it is involved in a legal transaction<sup>195</sup>. In the case of s 42 (2) VwGO, the management board is not involved in a transaction, but is representing the company in the context of an appeal. However, circumstances might arise out of the appointment of the special representative that obligate an appeal

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<sup>192</sup> Mertens in *KöIKo*, § 112 AktG, at 6; Semler in *MüKo*, § 112, at 14; Hüffer, § 112 AktG at 3; For the competence of the supervisory board with regard to litigation with the management board compare to BGHZ 135, p 244, 252f.

<sup>193</sup> Larenz/Canaris, p 202.

<sup>194</sup> Larenz/Canaris, p 202f.

<sup>195</sup> Hüffer, § 112 AktG, at 1.

against his appointment, that would question the impartiality of the special representative in the position of the management board. Therefore it seems to be conceivable that the supervisory board might estimate the existence of reasons, which justify an appeal against the appointment of the special representative, different from the special representative himself. Therefore in this case it seems to be inappropriate to expose the fate of the company to the discretion of the special representative, which according to the principles mentioned above, would be responsible for all decisions regarding the legal proceedings and their fundamentals.

One could argue that this point of view does not recognise the differences between the involvement in a legal transaction and denying an appeal by the special representative. If the company enters into a legal transaction with a member of the management board, the company will be interested in further cooperation with the member of the management board. The facts of the case are different in an omission to take legal remedies, if the special representative does not take legal remedies without a reasonable reason and against or without coordination with the supervisory board. In the case of a normal member of the management board, this would indicate a serious breach of his duties, which might entitle the supervisory board to dismiss the member of the management board. As a result of the dismissal, a new member of the management board would have to be appointed, who would be under duty to take legal remedies for the company. However the supervisory board is not in the position to dismiss the special representative. In addition, procedural deadlines could be missed because the actions of the special representative because of his legal position as an organ are attributed to the company. Therefore a *restitutio in integrum* according to s 60 (1) VwGO would be excluded. However for an analogous application of s 112 AktG, this is not essential.

The aforementioned argumentation would misconceive the spirit and purpose of s 112 AktG. Firstly, it has to be mentioned that according to the perpetual jurisdiction of the highest courts, the supervisory board also represents the company, according to s 112 AktG, against retired members of the management board<sup>196</sup>. This results from a necessary and typified consideration, which shows the abstract dangers of partial representation of the company<sup>197</sup>. This typified danger can also be seen in the cases of an omission of legal remedies by the special representative in the position of an one-headed management board of the company, because opposed to the normal case where no single

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<sup>196</sup> BGH, ZIP 1989, p 497, 497f.; BGH, ZIP 1991, p 796; BGH, AG 1991, p 269, 270; BGHZ 130, p 108, 112.

<sup>197</sup> Compare to BGHZ 130, p 108, 112.

person in the company may take legal remedies without at least giving other organ members the chance to express conflicting interests, in the case of the special representative, the launching of legal remedies would be up to the discretion of one single natural person.

In addition, with regard to s 112 AktG, another aspect has to be taken into consideration. In opposition to the company law governing the right of the GmbH, according to which the single manager can be excluded from the prohibition of self-contracting, s 112 AktG is a mandatory provision<sup>198</sup>, so that a legal transaction which is conducted by the management board in the way of self-contracting is always null and void (s 134 BGB)<sup>199</sup>. Therefore it seems to also be appropriate to apply s 112 AktG to the case of launching legal remedies with regard to the administrative procedure. Subsequent to this, because of this typified danger, the members of the supervisory board must be entitled to take legal remedies for the company, specifically because they have no right to dismiss the special representative.

(ii) Relation under company law

The main duty of the supervisory board is the active supervision of the management activities of the management board. Since the introduction of the TransPubG in the year 2002, this duty has been tightened. S 111 (4) sentence 2 AktG has been changed so that it now provides that the General Meeting and the supervisory board can not only determine business dealings which need authorized approval, but they have to create an index of such business dealings which need authorized approval<sup>200</sup>. However in the case that a special representative is appointed for the management board, the management of the company is not performed by the original management board anymore, because these rights are transferred to, and performed by, the special representative.

In the case of an insolvency, the duty to supervise the management board and the duty for authorized approval can only be extended to the rights regarding the procedure, which are administered by the management board and not by the insolvency administrator. Further methods of control, specifically with regard to the asset management (*Vermögensverwaltung*) by the insolvency administrator<sup>201</sup>, do not exist. But regarding the

<sup>198</sup> Vgl. Lutter/Hommelhoff, § 35, at 19.

<sup>199</sup> Compare to Mertens in *KölKo*, § 112 AktG, at 4f.

<sup>200</sup> Dietrich, DStR 2003, p 1577.

<sup>201</sup> General point of view, compare to Hauptmann/Müller-Dott, *Pflichten und Haftungsrisiken der Leitungsgorgane einer Aktiengesellschaft und ihrer Tochtergesellschaften*, BB 2003, p 2521, 2525.

insolvency administrator, it has to be kept in mind that the InsO provides regulations for its supervision. Ss 58 and 69 InsO provide that the insolvency administrator is supervised by the insolvency court and the creditors' meeting. Regarding the special representative, such provisions are missing. With his appointment the special representative becomes a subject to the supervision of the BaFin. But this supervision cannot be compared with the supervision of the supervisory board under company law or the supervision under the InsO. Therefore the question is how a special representative in the position of the management board can be a subject to the supervision under the company's act.

Supervision of the management according to s 111 AktG first has the meaning of a control over the actions performed by the management board<sup>202</sup>. The supervision of the management according to s 111 AktG is thereby closely connected with the reporting duties of the management according to s 90 (1)(2) and (1)(3) AktG. They are aimed at operations from the past. The actions mentioned in s 111 (2) AktG are also historically orientated.

The supervisory board however is not allowed to restrict its supervision to a historically orientated control<sup>203</sup>. Therefore the supervision also has to be preventive, and therefore has to have an effect to the future, as the supervisory board by means of consulting for the management board affects the future business policy<sup>204</sup>. Insofar, the supervisory board participates in the management task of the management board. Specifically this can be based on the reporting duties according to s 90 (1)(1) AktG and the cases where principal approval is required according to s 111 (4) AktG<sup>205</sup>.

During the supervision of the management of the company, the supervisory board has to take care that the management by the management board complies with law and order and is appropriate<sup>206</sup>, which means that the management has to be economical. The intensity of the supervision by the supervisory board depends on the situation of the company<sup>207</sup>. In the normal case it is sufficient if the supervisory board examines the reports of the management board (s 90 AktG) and where necessary, asks for amendatory re-

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<sup>202</sup> Hüffer, § 111 AktG, at 4.

<sup>203</sup> Hüffer, § 111 AktG, at 5.

<sup>204</sup> Hüffer, § 111 AktG, at 5.

<sup>205</sup> Semler in MüKo, § 111 AktG, at 246 ff.; Henze, *Neuere Rechtsprechung zu Rechtsstellung und Aufgaben des Aufsichtsrats*, BB 2005, p 165; Lutter/Kremer, *Die Beratung der Gesellschaft durch Aufsichtsratsmitglieder*, ZGR 1992, p 87, 88ff.; Scheffler, *Die Überwachungsaufgabe des Aufsichtsrats im Konzern; Der Aufsichtsrat - nützlich oder überflüssig?*, ZGR 1993, p 63, 69.

<sup>206</sup> BGHZ 75, p 120, 133; BGHZ 114, p 127, 129f.; Lutter/Krieger, *AR*, § 3, at 71ff.

<sup>207</sup> Hüffer, § 111 AktG, at 7.



ports. Breaches of duties of the management board in the sense of s 93 (3) AktG are to be prevented at any time. If the situation of the company is tense, or other risk bearing circumstances exist, the supervision by the supervisory board has to be intensified equally to the risk situation<sup>208</sup>. In a crisis situation this can even be intensified to a temporary takeover of the management of the company<sup>209</sup>.

S 111 AktG mentions the right of access to information and examination (s 111 (2) AktG), the duty and therefore the right to call for a general meeting if it is required for the benefit of the company (s 111 (3) AktG) as well as the implementation of requirements for principal approval (s 111 (4) sentence 2 AktG) as means of supervision and exercise of influence. The implementation of bylaws for the management board (s 77 (2) sentence 1 AktG) and the performance of the employer competence of s 84 AktG are of special importance. The latter should therefore not only be seen as a result of a historically orientated control (dismissal), but also as a part of the management function which also affects the future (Choice and appointment of the members of the management board)<sup>210</sup>. Finally requiring mention are actions with regard to the annual accounts, namely complaints in the auditors report to the general meeting (s 171 (2) sentence 1 AktG) and the refusal, to approve the annual accounts (s 172 AktG).

For the relation between special representative and supervisory board, s 84 AktG is of special interest. S 84 AktG in principal could be used to frustrate the appointment of a special representative, namely if the supervisory board would be in the position to immediately dismiss the special representative after his appointment. However this seems to be neither reasonable nor intended by the legislator at any time. Finally the application of s 84 AktG would contravene with the spirit and purpose of the appointment of a special representative. If the supervisory board would be in the position to execute its power as an employer (*Personalbefugnis*), the supervising authority would be hindered to temporally and closely perform its task of danger defence. The purpose of the special representative is specifically to enable a fast reactivity of the supervising authority to lead the company out of a crisis situation. Therefore it has to be kept in mind that the controlling organ, which would be entitled to dismiss the special representative, usually can be blamed for the crisis situation too. Subsequent to this, the supervisory board has no power to execute its competence as an employer according to s 84 AktG with regard to the special representative in the position of the management board. However with

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<sup>208</sup> Hüffer, § 111 AktG, at 7.

<sup>209</sup> Hüffer, § 111 AktG, at 7.

<sup>210</sup> Hüffer, § 111 AktG, at 8.

regard to other mechanisms of control, the special representative is under the duty to cooperate with the supervisory board. Fundamentally, this concerns the reporting duties according to s 90 AktG as well as the actions which require an approval by the supervisory board according to s 111 (4) sentence 2 AktG.

(c) General meeting

The general meeting is the primary organ of representation of shareholders in a stock corporation. The general meeting also is an organ for decision-making<sup>211</sup>. The general meeting in principle also has a power to control. However this power of control works more in an indirect way and is restricted to the competence to appoint and to dismiss the members of the supervisory board. A competence of supervision, like it is explicitly stated for the supervisory board, does not, however, exist for the general meeting<sup>212</sup>.

With regard to the appointment of a special representative, the personal competence of the general meeting with regard to the supervisory board seems to be problematical (s 119 (1)(1) and s 103 AktG) as well as the representation of the company if the special representative is appointed for the tasks of the management board as well as the tasks of the supervisory board. Therefore the problems arising are similar to the situation of the supervisory board for the case where a special representative is appointed for the management board.

With regard to the personal competence of the general meeting, the same principles as for the personal competence of the supervisory board apply. The general meeting, with regard to the special representative in the position of the supervisory board, cannot make any use of its personal competence. Insofar, the comments made above with regard to the supervisory board apply *mutatis mutandis*.

With regard to the representation of the company in the administrative procedure, an analogous application of s 147 (2) sentence 1 AktG has to be considered. The purpose of the provision is the practical enforcement of claims for compensation in the interest of the company<sup>213</sup>. Without a special rule this would be in jeopardy, because the representation of the company is a task of the management- or supervisory board (s 78 AktG and as the case may be s 112 AktG). One might fear that in such a case the managing

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<sup>211</sup> Hüffer, § 118 AktG, at 3.

<sup>212</sup> Schewe, *Unternehmensverfassung*, p 170.

<sup>213</sup> Hüffer, § 147 AktG, at 1.

organs could favour their own interests over the interests of the company<sup>214</sup>. Therefore the situation in principle is similar to the relation between supervisory- and management board - for the case where a special representative is appointed for the tasks of the management board. Again it is a matter of an impartial representation.

This impartial representation seems to be in jeopardy especially if one special representative is appointed for the tasks of the management- and supervisory board. But even in the case where two special representatives are appointed for the functions of the management- and supervisory board, the problem of a conflict of interest remains. S 147 (2) sentence 1 AktG tries to prevent this. Therefore an analogous application of s 147 (2) sentence 1 AktG, with regard to the administrative procedure, seems to be at least appropriate if special representatives are appointed for management- and supervisory board. In the case where a special representative is appointed only for the management board, the representation remains under the supervisory board. A conflict of interest, of the type where special representatives take over the management- and supervisory board, is unlikely.

Finally the case where a special representative is appointed for the tasks of all organs seems to be problematical. The affected members of the organs can appear in the administrative procedure but it is questionable as to who is entitled to represent the affected company in the administrative procedure. For this case the requirements for the appointment of a special representative have to be taken into consideration. The appointment of a special representative for all organs actually seems to be suitable only in the case of s 83a (1)(3) VAG, that means where the company is endangered from becoming insolvent and a transfer of the insurance portfolio shall be performed in order to secure the interests of the insured and the policy holders. However because of the principle of proportionality, only those powers of the general meeting can be transferred to the special representative, which are necessary to create the required approval of the general meeting. The transfer of further powers with regard to the proportionality of the action of the supervising authority will not be justified. As already mentioned above, with regard to non-transferred powers, the organs remain entitled to perform the non-transferred powers. Therefore an analogous application of s 147 (2) sentence 1 AktG would be suitable again.

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<sup>214</sup> Hüffer, § 147 AktG, at 1.

## VII. Similar instruments to the special representative under common law jurisdictions

The special representative seems to be a German speciality. In common law countries like the UK, Australia and South Africa for example, the financial authorities seem to be able to suspend directors but an instrument similar to the special representative seems to be unknown. However the financial supervisors in common law countries usually have some powers with regard to the directors of the supervised companies. For reasons of overview, I am only going to elaborate on the Financial Services Authority [FSA] (financial supervisor in the UK) powers concerning directors in financial institutions.

### 1. Power to remove directors

Under the Financial Services and Markets Act 2000 [FSMA], persons performing certain functions<sup>215</sup> for regulated firms in relation to their regulated activities must be approved by the FSA for the performance of those particular functions. These persons then come under the regulation of the FSA as "approved persons". Directors of financial services firms would typically come under the approved persons regime. If an approved person contravenes the provisions of FSMA, the FSA has the power to impose certain sanctions on him. One of the sanctions the FSA can impose on an approved person is to withdraw approval<sup>216</sup>. The FSA might withdraw approval if the individual is no longer a "fit and proper person" to perform the function to which the approval relates<sup>217</sup>.

The considerations typically taken into account in deciding whether an individual is a "fit and proper person" are honesty, integrity and reputation, competence and capability and financial soundness<sup>218</sup>.

The effect of approval being withdrawn is that the individual cannot carry out the controlled functions to which the approval related. If he does, the FSA could take the following steps<sup>219</sup>: First take enforcement action against the firm for which he works or second obtain a prohibition order against the individual<sup>220</sup>. Note, however, that the indi-

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<sup>215</sup> Known as 'controlled functions'.

<sup>216</sup> Other sanctions include fines or making public statements.

<sup>217</sup> Freshfields Bruckhaus Deringer, *Financial Services*, at paragraph 7.29; FSMA, s.63(1).

<sup>218</sup> Freshfields Bruckhaus Deringer, *Financial Services*, at paragraph 1.69.

<sup>219</sup> Note that the FSA will not be able to *discipline* the individual, as his conduct would no longer be 'while an approved person'.

<sup>220</sup> Freshfields Bruckhaus Deringer, *Financial Services*, at paragraph 7.37. Although, in practice, the FSA will resort to obtaining such an order only if the individual presents a degree of risk to consumers or confidence in the financial system that cannot be sufficiently addressed by the withdrawal of his approval (ibid., at paragraph 7.60).

vidual might still be able to continue performing other functions to which the approval (which was removed) did not relate.

## 2. Power to appoint directors

The FSA does not appear to have any powers to appoint directors to the boards of regulated companies or firms.

## 3. The FSA's powers in its capacity as the UK Listing Authority (UKLA)

The FSA, in its capacity as the UKLA, is the authority that regulates the activities of listed companies and companies that are seeking admission to the official list. One of the FSA's roles is to enforce the new listing regime under FSMA, Part VI (the Part 6 Rules). These rules are contained in a "Handbook", which is divided into three sections: First, the Listing Rules (covering rules relating to eligibility for listing and continuing obligations of listed issuers), second the Disclosure Rules (covering rules in relation to the publication and control of 'inside information') and third the Prospectus Rules (covering the rules outlining the circumstances in which a prospectus is required and the contents of such prospectuses). All listed companies are required to comply with these rules.

## 4. Removal of directors

The FSA's enforcement powers can be exercised against directors of listed companies if they are involved in breaches of the Part 6 Rules by the company<sup>221</sup>. Action will be taken against any person who was, at the material time, a director of the company and who was knowingly concerned in the contravention<sup>222</sup>.

The FSA's enforcement powers include: First, imposing a penalty on the individual, second, publishing a statement censuring him and third, issuing an informal private warning. The FSA does not appear to have any powers to remove such directors.

## 5. Appointment of directors

The FSA does not appear to have any powers to appoint directors to the boards of listed companies. This is not surprising, as this power typically belongs to the shareholders of

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<sup>221</sup> Freshfields Bruckhaus Deringer, *Financial Services*, at paragraphs 14.28 and 14.133.

<sup>222</sup> Freshfields Bruckhaus Deringer, *Financial Services*, at paragraph 14.133; FSA Handbook at ENF 21.6.3.

the company. It appears that, in certain circumstances, the FSA may apply to court to appoint a receiver to a listed company<sup>223</sup>.

### **VIII. Special representative and fiduciary duties**

As pointed out above the special representative is an effective instrument to deal with a crisis in an insurance company. Subsequent to this one might think about introducing the special representative to legal systems different from the German system. Therefore this part of the thesis deals with the problems, which are likely to arise if the special representative will be introduced to a common law country, shown at the example of South Africa.

Under common law as well as under German law, in addition to his statutory duties, a director is in a fiduciary position to his company. The same applies for the special representative if one follows the organ theory mentioned above. The directors and therefore the special representative owe fiduciary duties to their company. Generally, directors stand in an individual fiduciary relationship to their company<sup>224</sup>. As mentioned above, the special representative, with his appointment enters into the position of the organ he is appointed for. Subsequent to this, if the special representative is appointed for a task of the board of directors, the special representative also enters into a fiduciary position. This complies with the general definition of a fiduciary who is a person who undertakes or assumes responsibility, or is required by law, to act for, or on behalf of, and in the interest of, another<sup>225</sup>. The special representative enters into the position of the organ whose powers were transferred to the special representative. He also acts in the interest of another. The special representative is clearly in a fiduciary position. Because the fiduciary owes an individual duty, it does not make any difference whether the special representative is appointed for only tasks of one member of the board or for the tasks of the whole board.

The fiduciary duties under common law are wider than the fiduciary duties under German law. Under German law the fiduciary duty of a director is merely to act for the interest of the company. However in the common law systems a group of fiduciary duties

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<sup>223</sup> Enforcement Manual, at ENF 9.6.10(1)(d).

<sup>224</sup> Blackman, s 208, 8 – 29, Fn. 2.

<sup>225</sup> Blackman, s 208, 8 – 31, Fn. 4, 5, 6.

has to be distinguished. Subsequent to this only the fiduciary duties under common law and no statutory differences will be subject of the following elaborations.

The legislation on banking and insurance supervision deviates between the different common law countries. The same applies to the company's law. However the fiduciary duties are part of the common law and normally not written down in the single companies acts. The Republic of South Africa is one of the first common law countries that tries to fix the fiduciary duties in its companies act<sup>226</sup>. However s 91 (6) of the 2007 bill states that the duties under the Bill are an addition to, and not an substitution for, any duties of the director of a company under the common law. Therefore the fiduciary duties under the common law remain unaffected. The same applies for the situation in the UK under the Companies Act 2006. Chapter 2 of the Act is dealing with the fiduciary duties. However s 170 (3) and (4) of the Act clarify that those "general duties" are based on certain common law rules and equitable principle and straighten out that those "general duties" shall be interpreted and applied in the same way as the corresponding common law rules or equitable principles.

As mentioned before, the special representative becomes a mandatory third organ and with its appointment enters into a fiduciary relationship. Now the situation and the circumstances in which the special representative has to act seems to be quite special. The fiduciary duties, which are most likely to influence the special representative, can be identified as the duty to act *bona fide* in the interest of the company, the no conflict rule and the duty to exercise an unfettered discretion. Therefore these fiduciary duties will be subject to the following elaborations.

1. Duty to act *bona fide* in the interest of the company

If the special representative was introduced to a common law country, he would be subject to the "Duty to exercise powers for a proper purpose" and therefore would have to act *bona fide* in the interest of the company. Now it has to be determined what this means with regard to the special representative.

The duty to act *bona fide* in the interest of the company is part of the duty to exercise powers for a proper purpose. The duty states that a director must act, if he acts at all, *bona fide* in the interest of the company as a whole<sup>227</sup>. The duty is imposed on directors

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<sup>226</sup> Companies Bill 2007, Sec. 91.

<sup>227</sup> Blackman, s 208, 8 – 61, Fn. 3.

not only for the case that they exercise their powers, but also for the case they do not exercise their powers<sup>228</sup>. This means that, even not exercising his powers, the director must act in the interest of the company.

The duty is a subjective one in regard to what is to be done in order to promote the company's interest and an objective one in regard to the interests to be promoted<sup>229</sup>. The subjective part of the duty means that the director, when he acts, if he acts at all, must act as to what in his honest opinion, is for the benefit of the company as a whole<sup>230</sup>. However the question is not whether management's decision was correct or a good one under the given circumstances. The decision has to be made on grounds on which a reasonable person could have come to the same decision<sup>231</sup>. Therefore, the test is "whether, an intelligent and honest person in the position of a director at the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transaction was for the benefit of the company"<sup>232</sup>.

In addition, the primary purpose of their acting has to be in the interest of the company. Otherwise the director is in a breach of his fiduciary duty. However, there may be other purposes involved in the acting of the director. But as long as the primary purpose is in the interest of the company, the other purposes do not matter<sup>233</sup>. Furthermore the director is in a breach of his duty to the company if he fails to consider the interest of the company at all. Since the director's duty is to act, if they act at all, *bona fide* in the interest of their company, a total failure to consider the interests of the company of course indicates a breach of his duty to act, if he acts at all *bona fide* in the interest of the company<sup>234</sup>. However this might be critical if a special representative favours the interests of the policyholders over the interests of the shareholders as pointed out in the memorandum of the VAG and thereby does not even consider the interests of the company.

The test as to what it is that constitutes the interest of the company is an objective one. Therefore a director who *bona fide* but mistakenly believes that the interests he consid-

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<sup>228</sup> Blackman, s 208, 8 – 62, Fn. 3.

<sup>229</sup> Blackman, s 208, 8 – 62.

<sup>230</sup> Blackman, s 208, 8 – 64, Fn. 3.

<sup>231</sup> Blackman, s 208, 8 – 64 – 2, Fn. 1.

<sup>232</sup> *Charterbridge Corp Ltd v Lloyds Bank Ltd* [1969] 2 All ER 1185; [1970] Ch 62.

<sup>233</sup> Blackman, s 208, 8 – 65.

<sup>234</sup> Blackman, s 208, 8 – 67, Fn. 2.



ers for his acting are the interests of the company will, despite his *bona fide* belief, breach his duty to the company<sup>235</sup>.

However, for the special representative this means a major risk if one thinks about preferring the interests of the policyholders when the special representative acts. If the act does not specify that the special representative is entitled to prefer the interests of the policyholders over the interests of the shareholders, the special representative generally would be in a constant danger of breaching his fiduciary duties.

However it seems to be that the “interests of the company” is an indefinite phrase<sup>236</sup>. The phrase “the interests of the company” is often used within the context of company law but has rarely experienced a definition. Therefore it seems quite likely that it can be easily misunderstood and maybe has different meanings in different contexts<sup>237</sup>.

Generally the “interest of the company” is defined as the interests of the shareholders qua shareholders, as a general body<sup>238</sup>. Therefore it is necessary to take into concern the interests of both its present and future shareholders<sup>239</sup>. However the favouring of one shareholder over the others would not be in the interest of the company<sup>240</sup>. Furthermore, a director appointed by shareholders of one class may not identify the interests of the company with the interest of that class<sup>241</sup>. So it cannot be an argument that the special representative is appointed by the financial supervisor, which usually, with regard to insurance business, because of his goal of consumer protection, has an interest in favouring the interests of the policyholders over the shareholders. However this general rule is not free of criticism. It has been argued that the company is a legal person and therefore independent from the shareholders<sup>242</sup>. But in *Brady v Brady*<sup>243</sup> it was said that “the interests of a company, an artificial person, can not be distinguished from the interests of the persons who are interested in it”.

However, with regard to creditors, there is an exception to the general rule that the interests of the company are the interests of its shareholders<sup>244</sup>. In the case of an insol-

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<sup>235</sup> Blackman, s 208, 8 – 67.

<sup>236</sup> *Per* Dixon J in *Mills v Mils* (1938) 60 CLR 150 189-188 (HC of A).

<sup>237</sup> *Per* Nourse LJ in *Brady v Brady* [1988] BCLC 20 40 (CA).

<sup>238</sup> Blackman, s 208, 8 – 67, Fn. 8, 9, 10.

<sup>239</sup> Blackman, s 208, 8 – 68, Fn. 1.

<sup>240</sup> Blackman, s 208, 8 – 68, Fn. 3.

<sup>241</sup> Blackman, s 208, 8 – 68, Fn. 4.

<sup>242</sup> Blackman, s 208, 8 – 69.

<sup>243</sup> *Brady v Brady* [1988] BCLC 20 40 (CA).

<sup>244</sup> Blackman, s 208, 8 – 72, Fn. 5.

vency of a company, the creditors' money is at risk rather than the shareholders' proprietary interests<sup>245</sup>. In such a case the directors' duty to act *bona fide* in the interest of the company changes into a duty to the creditors, namely to act in - or at least to consider - the interests of the companies' creditors<sup>246</sup>. The duty commences if there is knowledge of a real and not remote risk of insolvency<sup>247</sup>.

In the case of an appointment of a special representative according to s 83a (1) (3) VAG, this could entitle the special representative to prefer the interest of the policyholders over the interests of the shareholders. In the case of an insolvency of the insurance company, the policyholders are also treated as creditors of the insolvent company. This becomes apparent in connection with long-term life insurances. Here the premiums of the policyholders are primarily used for saving purposes. It is also a method for retirement provisions. So if the insurance company is in danger of becoming insolvent, the savings of the policyholders and consequently their retirement provision are at risk. However, even if the special representative would be under the duty to serve the interests of the creditors it seems that he would act in a breach of this duty if he favours the interests of the policyholders over the interests of the other creditors. But this only entitles the special representative in a case of an imminent insolvency. For the cases of s 83a (1)(1) and (1)(2) VAG, the above mentioned arguments do not work as a solution. For those cases, an express term would have to be fitted in the act.

The general question as to whether directors, when acting, should also consider other interests beside the interests of the shareholders of the company has received respectable attention<sup>248</sup>. However, the centres of these considerations usually are the company's employees<sup>249</sup>, followed by the company's customers (e.g. the policyholders), the local community, the environment and the society in general<sup>250</sup>. Subsequent to this, in *Teck Corporation LTD v Miller*<sup>251</sup>, it was said that "if today the directors of a company were to consider the interests of the employees, no one would argue, in doing so, they were not acting *bona fide* in the interests of the company itself". But the directors would still act in a breach of their duty if they entirely disregard the interests of the shareholders in

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<sup>245</sup> Blackman, s 208, 8 – 73, Fn. 3.

<sup>246</sup> Blackman, s 208, 8 – 73, Fn. 4, 5.

<sup>247</sup> Blackman, s 208, 8 – 74, Fn. 1.

<sup>248</sup> Blackman, s 208, 8 – 75, Fn. 3.

<sup>249</sup> Blackman, s 208, 8 – 75, Fn. 4.

<sup>250</sup> Blackman, s 208, 8 – 75.

<sup>251</sup> (1972) 33 DLR (3d) 288 313-314.

order to e.g. confer a benefit on its employees<sup>252</sup>. However it seems that if the directors consider other interests than the interests of the company's shareholders to a "decent respect", they will not be in danger of failing in their fiduciary duty to the company<sup>253</sup>.

For the special representative, the above said means that when he is performing his office he also can consider the interests of the policyholders and therefore does not commence a breach of his fiduciary duty to the company. Therefore the situation is comparable with the situation under German law. However, if the special representative, when he is performing his office, shall be entitled to prefer the interests of the policyholders over the interests of the shareholders, this has to be expressly mentioned in the act. Otherwise the special representative would breach his duty to the company if he would favour the interests of the policyholders over the interests of the shareholders as a whole.

Furthermore, a director and therefore also a special representative, has to act *bona fide* for the company as a whole. A director acts *bona fide* when he is of the opinion that what he is doing is in the interest of the company<sup>254</sup>. First, a directors' belief must be *bona fide* in the sense that it must be a genuine<sup>255</sup> or considered belief. Secondly a director owes his company a fiduciary duty of honesty<sup>256</sup>. That means, that even if a director thinks he acts in the interest of the company, he may not act fraudulently or otherwise illegally<sup>257</sup>. This has no special impact on the special representative which might be different from the effect it has for a normal director. Of course, like a director, a special representative must act, if he acts at all, *bona fide*, because he enters into the position of the affected organ and if he does not act, if he acts at all, *bona fide*, he would expose himself to a possible liability.

As mentioned above, the duty to act *bona fide* in the interest of the company is a part of the duty to exercise powers for a proper purpose. As to whether a director acted for an authorised purpose has to be determined by subjective reasons<sup>258</sup>. Subsequent to this, the purpose of the directors' action not only must be *bona fide* in the interest of the company, but it also must be authorised. Therefore the company's memorandum and articles of association have to be considered to determine whether a purpose is author-

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<sup>252</sup> Blackman, s 208, 8 – 76, Fn. 1.

<sup>253</sup> Blackman, s 208, 8 – 76, Fn. 2.

<sup>254</sup> Blackman, s 208, 8 – 76, Fn. 4.

<sup>255</sup> Blackman, s 208, 8 – 77, Fn. 1.

<sup>256</sup> Blackman, s 208, 8 – 77, Fn. 3.

<sup>257</sup> Blackman, s 208, 8 – 77, Fn. 4.

<sup>258</sup> Blackman, s 208, 8 – 80, Fn. 1.

ised<sup>259</sup>. However if the directors breach their duty not to exercise their powers for an unauthorised or collateral purpose, the as to question whether the directors acted in what they believed to be in the best interest of the company is always irrelevant<sup>260</sup>.

This is, however, not without consequences for the work of the special representative. The special representative, because of the circumstances which lead to his appointment, often will be forced to take more or less drastic actions. It can be assumed that by performing these drastic actions, the special representative is believed to be acting in the best interest of the company. But as mentioned above, this would not excuse him from breaching his fiduciary duties if the actions he is taking are not allowed by the act, the articles of association or the company's memorandum. However there seems not to be any practical impact of this on the special representative (e.g. a transfer of portfolio in the way of a transfer of business is acknowledged in the Long Term Insurance Act, 1998 (Act No. 52 of 1998), Part V, s 37 and such a transfer will usually also be allowed by the articles of association of the company concerned).

## 2. Conflict of Interest

The rule can firstly be separated into the self-dealing and the fair-dealing rule. The rules relate to the situation where a director has an interest in a contract entered into by his company<sup>261</sup>. Therefore, on the one hand the self-dealing rule prohibits that a director acts for or on behalf of his company, in a matter in which this director has an interest that might conflict, or that actually conflicts, with the directors' duty to act in the interest of the company<sup>262</sup>. On the other hand, a duty of disclosure is imposed on the director by the fair-dealing rule, for the case where a director himself does not purport to act for the company in the matter, but nevertheless has an interest in the contract which conflicts, or which may possibly conflict, with the interest of the company<sup>263</sup>. In addition both rules render such a contract avoidable<sup>264</sup>.

As mentioned above, the self-dealing rule tries to prohibit a director acting for his company "in any matter in which he has an interest that conflicts, or may possibly conflict, with his duty to his company"<sup>265</sup>. In *North-West Transportation Co v Beatty* it was said

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<sup>259</sup> Blackman, s 208, 8 – 80.

<sup>260</sup> Blackman, s 208, 8 – 82.

<sup>261</sup> Blackman, s 208, 8 – 120, Fn. 2.

<sup>262</sup> Blackman, s 208, 8 – 121.

<sup>263</sup> Blackman, s 208, 8 – 121.

<sup>264</sup> Blackman, s 208, 8 – 121.

<sup>265</sup> Blackman, s 208, 8 – 122.

that “a director of a company is precluded from dealing on behalf of the company, with himself, and from entering into engagements in which he has a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound by his fiduciary duty to protect”<sup>266</sup>. However the rule does not try to prohibit that a director has a personal interest in the matter at all, but it prohibits that a director has a personal interest that conflicts with his duty<sup>267</sup>.

The application of the self-dealing rule is performed in a rigid way<sup>268</sup>. However a director is allowed to act on behalf of his company, even if he has a personal interest in a contract or other matter, if the director, after making full disclosure of his interest to the general meeting, obtains the consent of the general meeting to do so<sup>269</sup>. In addition, the rule can be relaxed by the articles if those permit the director to act in such matters after making full disclosure of his interest to the other members of the board<sup>270</sup>.

Now, on the first view, the relevance of this is not obvious for the special representative. However under certain circumstances a special representative can be appointed to perform a transfer of the portfolio of the insurance company. Such a transfer of portfolio is a contract, usually between two insurance companies, where one insurance company sells its portfolio of insurance contracts to another insurance company, which continues to provide insurance cover for the policyholders. This mostly happens with regard to long-term life insurances. The purpose of this is, of course, to protect the policyholders. Subsequent to this, if a special representative participates in such a transfer of portfolio, he might have a personal interest in this contract.

Usually the persons who are appointed as special representatives are former members of the board of an insurance company<sup>271</sup>. This is because they must have some knowledge of the manner in which insurance business is conducted. Now it seems to be possible that a special representative enters into a contract with regard to a transfer of portfolio with an insurance company he worked for, as a member of the board, and where he still is a shareholder. This, of course, would lead to a personal interest of the special representative in the contract which could possibly conflict with the duties he owes to the company he is appointed for.

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<sup>266</sup> (1877) 12 AC 589 593-594 (PC).

<sup>267</sup> Blackman, s 208, 8 – 123.

<sup>268</sup> Blackman, s 208, 8 – 123.

<sup>269</sup> Blackman, s 208, 8 – 123, Fn. 8.

<sup>270</sup> Blackman, s 208, 8 – 124.

<sup>271</sup> Bürckle, VersR 2006, p 302, 304.

However, the special representative could deal on behalf of the company after having made a full disclosure of his interest to the general meeting and after having received the consent of the general meeting, or where the articles permit him to act in such matters after having made full disclosure of his interests to the other members of the board. But, where a special representative is not only appointed for the board of directors but also for the competences of the general meeting, this rule does not seem to serve a purpose anymore. In the case where a special representative is appointed to perform a transfer of portfolio, he would be appointed for the board of directors and the general meeting. So in this situation a serious safeguard for the company would be missing. The next question arises as to where the articles permit a disclosure to the board of directors. So the question is: What happens if only one special representative is appointed for all the competences of the whole board? If the special representative could disclose to himself, this would lead to a serious lack of control, which should by all means be avoided.

However the last question can be answered by considering the fair-dealing rule. This specifies that if a director has an interest in a contract which may possibly conflict, or even conflicts with the interests of the company in a contract which his company proposes to enter into with a third party, the director has to, to the extent as that contract is concerned, “entirely shake off his relation with the company, act openly and in good faith and deal with the company at arm’s length”<sup>272</sup>. The fair-dealing rule therefore imposes a duty to disclose his interest in the contract on the director who has an interest in such a contract<sup>273</sup>. Thus the goal of the fair-dealing rule is to ensure that the honesty and integrity which should inform corporate dealing and, in particular, the internal management of companies, is scrupulously observed and not to protect the company against bad bargains<sup>274</sup>.

As already mentioned above, unless the articles provide otherwise, disclosure must be made to the members in general meeting<sup>275</sup>. However, the articles of a company may relax this rule to a certain extent<sup>276</sup>. Subsequent to this, the articles may permit disclosure to be made to the other directors<sup>277</sup>. But the disclosure must be made by means of informing someone about something of which he would not otherwise be aware of, and subsequent to this there has to be at least one independent member of the board who

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<sup>272</sup> Blackman, s 208, 8 – 125, Fn. 1, 2, 3; *Robinson v Randfontein Estates GM Co Ltd* 1921 AD 168 178.

<sup>273</sup> Blackman, s 208, 8 – 125, Fn. 5.

<sup>274</sup> Blackman, s 208, 8 – 126, Fn. 3.

<sup>275</sup> Blackman, s 208, 8 – 126; 8 – 131.

<sup>276</sup> Blackman, s 208, 8 – 126.

<sup>277</sup> *Centofanti v Eekimitor Pty Ltd* (1995) 15 ACSR 629 642 SC(SA).

will act as a watchdog for the company<sup>278</sup>. Furthermore it was said that the requirements of such an article, which permits the disclosure to the board, are not satisfied “where a sole director purports to make disclosure to himself, or interested directors purport to make disclosure to one another”<sup>279</sup>.

This indicates the answer to the question mentioned above. Where a special representative is appointed to perform a transfer of portfolio and where the special representative has an interest in the contract which conflicts, or may possibly conflict with the interest of the company and where the articles permit a disclosure to the board of directors, the special representative would still act in breach of his duty, under conflict of interest. However this also seems to apply in the case where a special representative is appointed for the board of directors and the general meeting, and where the articles do not include such a clause, which relaxes the disclosure rule. The case is almost similar to the case where a clause in the articles relaxes the rule. The special representative would still disclose to himself but only in another position and therefore the above mentioned principle of a “watchdog” would be infringed upon. In this case, the special representative, in the capacity of the board of directors, would act in breach of his duty unless a different person would be appointed as a special representative for the capacity of the general meeting. In addition, the special representative would disclose to a person that is already aware of the circumstances. Subsequent to this, strictly speaking, the appointment of only one special representative for performing a transfer of portfolio would still be possible, but would also be a great risk with regard to a conflict of interest.

However there seem to be two possible ways of solving this problem generally with regard to the special representative. The first one can be applied during the phase where the person, who later will be the special representative, is chosen. Therefore, in regard to the actions the special representative is going to perform, a person should be chosen who is not directly related to the business of the company, for which the special representative will be appointed. Practically, the special representative, who obviously must not be a representative or agent of the financial supervisor, will work closely with the supervising authority, e.g. he will be introduced to the case he is appointed for by the financial supervisor. Subsequent to this, it should be possible to determine risks, at least to some extent, in advance of the appointment of the special representative. However, it has to be kept in mind, that the reservoir of persons who could become a special repre-

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<sup>278</sup> Blackman, s 208, 8 – 139.

<sup>279</sup> *Movitex Ltd v Bulfield* [1988] BCLC 104 116.

sentative is somehow limited. This is because the requirements for a person to become a special representative are almost equal with the requirements for being a member of the board in an insurance company. Thus, it could be possible that all of the possible special representatives are exposed to the risk of having a conflict of interest.

The second possible solution could be a phrase in the act, which prohibits that a special representative enters in any transaction in which he has an interest, that conflicts, or possibly may conflict with the interest of the company, even after having made full disclosure either to the general meeting, or where the articles provide a regulation, to the board of directors. However, it has to be kept in mind that this would mean that a special could not perform any action in which he has an interest, which might collide with the interest of the company, even if the company would benefit the most, if this particular action would be performed. Subsequent to this, the instrument of the special representative would lose some of its flexibility.

A possible solution for this problem could be seen in a disclosure of the special representatives interest to the financial supervisor. However this has to be seen critically. First, the fiduciary relationship exists between the company and the special representative and not between the special representative and the financial supervisor. Therefore a disclosure of the interest to the financial supervisor would not free the special representative from his duty against the company. Second, to comply with the duty the special representative needs to deal with the company at arms' length. However if he discloses to the financial supervisor he does not deal at arms' length with the company. A disclosure to the financial supervisor seems only to be possible if a provision in the act would amend the fiduciary relation of the special representative in such a situation.

### 3. Unfettered discretion

Generally, a director must exercise an unfettered and independent discretion<sup>280</sup>. Therefore an independent discretion means that the director, having listened to what his colleagues have to say, still must always bring his own mind to bear on the issue, using such skill and judgement as he may possess<sup>281</sup>. Therefore a director may not blindly follow the instructions of another, nor may he act like a puppet<sup>282</sup>. Subsequent to this, even if a director is appointed by a shareholder to represent that shareholder's interests,

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<sup>280</sup> Blackman, s 208, 8 – 106, Fn. 4.

<sup>281</sup> Blackman, s 208, 8 – 106, Fn. 5.

<sup>282</sup> Blackman, s 208, 8 – 106, Fn. 6.



he may not blindly follow that shareholder's instructions, nor may he simply remain inactive when the interests of the company conflict with the interests of that shareholder<sup>283</sup>.

Again this has to be seen in connection with the legislators' intent to generally favour the interests of the policyholders over the interests of the shareholders. To this extent, the special representative could be seen as something like a nominee director; nominated not by the shareholders, but by the financial supervisor, as a nominee of the policyholders. Therefore under the duty of independent and unfettered discretion, the special representative would basically be under a duty to make up his mind independently and not with regard to the legislators' intentions, expressed in the memorandum to the VAG.

However, where the company's articles provide the appointment of directors by a shareholder to represent the interests of that shareholder, such directors may act to further those interests on the theory that in such a case it is in the interest of the company that they do so<sup>284</sup>. Now for the case of the special representative, the articles normally would never allow his appointment. But the situation between a nominee director, who represents the interests of a particular group of shareholders, and the special representative is obviously very similar. The special representative is appointed by the financial supervisor and, according to the legislators' intentions, should ensure the interests of the policyholders when performing his office. Therefore one could think about applying the view mentioned above in an analogous way. However there seem to be problems in connection with the duty to act *bona fide* in the interest of the company. It seems to be doubtful as to whether a provision in the articles of the company can relieve such directors and, therefore, the special representative of that duty<sup>285</sup>. Subsequent to this, the special representative, by preferring the interests of the policyholders, would not be in breach of his duty to exercise an independent and unfettered discretion because his similar position to a nominee director but would act in a breach of his duty to act *bona fide* in the interest of the company, as long as there is no provision that entitles the special representative to act in that way.

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<sup>283</sup> Blackman, s 208, 8 – 107, Fn. 2, 3.

<sup>284</sup> Blackman, s 208, 8 – 108, Fn. 2.

<sup>285</sup> Blackman, s 208, 8 – 108.

A director may also not fetter his discretion, and therefore making himself incapable of performing in independent judgement on the matters that come before the board<sup>286</sup>. This merely relates to the situation where directors bind themselves as to the future exercise of their fiduciary powers. However this rule does not seem to have any special impact on the special representative.

## **IX. Conclusion**

As seen during the elaborations the special representative is a highly invasive instrument of the financial supervisor. If a special representative is appointed this usually means an intervention in the corporate governance framework of the company. The appointment of a special representative leads to a different composition of the managing organs. It also can have effects on corporate governance principles like the separation of powers.

First the special representative is an instrument of the financial supervisor in the area of the public law, especially the administrative law. Therefore the appointment of a special representative is subject to the requirements of proportionality and to the discretion of the financial supervisor. Due to the fact, that the special representative is an instrument of the public law, the administrative procedure is opened to appeal against the appointment.

The special representative is an instrument made to be appointed for the powers of an organ of an insurance company. Insurance business in Germany may only be performed by insurance stock corporations and mutual insurance companies. The governance within these two types of companies is organized very similar. Both types of companies are governed by a management- and supervisory board, also known as the dualistic system of corporate governance. The major difference between the two types of companies with regard to the governance of the companies can be seen in connection with the interest of the company. Where in the case of the insurance stock corporation it has to be separated between the interests of its shareholders and its policyholders, in the case of a mutual insurance company this interests are the same because the policyholders usually also are members of the mutual.

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<sup>286</sup> Blackman, s 208, 8 – 108.

If a special representative is appointed the question arises what his legal position within the governance framework is. However the literature as well as the jurisdiction are unanimous with regard to this point and are not supported by any arguments. The leading theories are that with his appointment the special representative becomes a holder of an office or is an instrument *sui generis*. But the position of the special representative seems to be similar to other instruments of the German law, in particular to the insolvency administrator. Therefore a consideration of the theories on the insolvency administrator opens a new point of view on the legal position of the special representative. Subsequent to this the position of the special representative can be determined as the one of an obligatory third organ. The arguments are that the special representative not only is bound to the interests of the policyholders but also to the interests of the shareholders. Therefore the special representative has to serve a group of interests. However these interests are very similar to the interests the normal organs have to consider while performing their offices.

After the determination that the special representative with his appointment becomes an obligatory third organ, the question of the duties, especially the duties under the companies' act of the special representative arises. S 83a (1) VAG is not clear to the extend whether the duties under the companies act shall be applicable to the special representative. It seems to be a common point of view that when the special representative is appointed and the "powers" of an organ are transferred to the special representative the special representative enters into the rights and duties of the affected organ. However the question whether the duties under the companies act are applicable to the special representative has to be determined according to the spirit and purpose of s 83a (1) VAG.

The biggest interference of the special representative within the corporate governance framework of the company can be seen with regard to the restrictions for the managing organs of the company. The restrictions for the managing organs in total are not applicable to the special representative. This is because to this extend s 83a (1) VAG is certain enough. Powers, which the bodies of the undertaking hold in accordance with the law or articles of association, can be transferred wholly or partly to a special representative. However this has dramatic consequences for the separation of powers. Because of the certainness of s 83a (1) VAG with regard to restrictions for the management organs under certain circumstances it is possible to appoint one special representative for the two managing organs or even all organs of the company. However this eliminates

the principal separation between the management- and the supervisory board. But the appointment of a special representative like every action under administrative law is always subject to the principle of proportionality.

Therefore it has to be kept in mind that there are limitations to the application of the duties under the companies act on the special representative. The duties are only applicable with regard to the spirit and purpose of s83 a (1) VAG. This means the duties are only applicable as long as they do not interfere unreasonable or even frustrate the work of the special representative. However the question whether a single duty under the companies act is applicable to the special representative has to be answered with regard to a consideration of the spirit and purpose of s 83 a (1) VAG. Despite of that the duties under the companies act are applicable to the special representative as a whole as long as each single duty is applicable to the special representative.

Another important limitation to the duties of the special representative is that the special representative is not bound to the recommendations of the German Corporate Governance Codex. This is because the recommendations lack the requirements for a formal legal rule and secondly the Codex expressly provides the possibility to deviate from its recommendations. However the special representative in his position of a member of the management- or supervisory board of a listed insurance company is still under the duty to make the declaration according to s 161 AktG.

The reporting duties of the management board according to s 90 (1) AktG are applicable to the special representative. However if the special representative is also appointed for the tasks of the supervisory board, the reporting duties do not serve their original purpose of a preventive supervision anymore. This attests the invasive character of the special representative for the corporate governance framework.

The same applies to the actions where principal approval is required. In general the special representative is under the duty to obtain principal approval for such actions. However if the special representative is appointed also for the tasks of the supervisory board and/or the general meeting these provisions lose their original purpose of a separation of powers and control. Especially in this case the invasive character of the special representative becomes apparent again.

Finally s 91 AktG is also applicable to the special representative. However the special representative is not under a duty to implement an advanced compliance- and risk man-

agement system. But the special representative is under the duty to establish the organisational requirements to ensure the early detection of dangers for the endurance of the company.

With regard to the relation of the organs to the special representative it first can be stated that the affected organ remains to exist to the extent that powers have not been transferred to the special representative.

If a special representative is appointed for the tasks of the management board the supervisory board analogue to s 112 AktG becomes entitled to represent the company during the administrative procedure. The relation of the supervisory board to the special representative in the position of the management board is different to the relation to the original management board. Especially the supervisory board is restricted in its right to make use of its rights to withdraw a director of the management board from its office with regard to the special representative. Therefore the only method of supervision and control of the management board are the provisions which require principal approval but only to the extent that the special representative is not also appointed for the tasks of the supervisory board.

Where a special representative is appointed for the management- and the supervisory board, the general meeting becomes entitled to represent the company analogue to s 147 (2) sentence 1 AktG. However a special representative could also be appointed for the tasks of the general meeting. But with regard to the proportionality of administrative actions it seems to be most unlikely, that the rights during the administrative procedure would be subject to a transfer to the special representative.

The special representative is a unique instrument of German insurance supervision law. Insurance supervisors from the common law countries like the UK FSA have powers to remove directors but they don't have a power to either appoint new directors or to appoint something similar to a special representative.

This leads to the last question what would happen if something like a special representative would be introduced to a common law country and would be exposed to the fiduciary duties. First the special representative would be under the duty to act in the interest of the company. The interest of the company usually is defined as the interests of the shareholders as a whole but under certain circumstances it changes into the interest of the company's creditors. Therefore except of the case of an immanent insolvency the

special representative is not entitled to favour the interests of the policyholders over the interests of the shareholders.

When a special representative is appointed a conflict of interest might occur. A problem arises there where a special representative is appointed for the board of directors and the general meeting to enable a transfer of portfolio. The special representative cannot disclose to himself so the fair-dealing rule cannot apply. This exposes the special representative to a serious risk of liability. However this risk might be eliminated during the procedure where the special representative is chosen if a special representative is chosen who has no connection with the company he is appointed for.

Finally the duty to exercise an unfettered discretion becomes apparent because the special representative could be seen as something like a nominee director. The nominee would be the financial supervisor. However the special representative would still not be entitled to prefer the interests of the policyholders over the interests of the shareholders as a whole because this could conflict with his duty to act *bona fide* in the interest of the company. In addition it should be kept in mind that even under German law the special representative is independent from the insurance supervision authority and therefore not bound to any instructions from them. So finally it can be stated that if the special representative shall be entitled to favour the interests of the policyholders over other particular interests, a legal provision that entitles the special representative to do so would be necessary.