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COVID-19: Limitation of profit distribution (dividend)

Dividend block in case of asset reduction

Many companies are already dealing with substancial negative economic effects due to the COVID-19 crisis. In certain industries, the occurrence of losses will often be unavoidable even for normally successful companies.

As the financial year of many companies is coincident with the calendar year, the preparation and adoption of the annual financial report this year often overlaps with "COVID 19 losses". Therefore, it is necessary to draw attention to the distribution ban of § 82 (5) GmbHG, which applies to limited liability companies and is highly up-to-date to the current situation: According to this, the balance sheet profit is excluded from distribution to the shareholders to the extent that the financial situation of the company has significantly and not only temporarily deteriorated. This concerns the period between the balance sheet date and the adoption of the annual financial statements. The amount excluded from distribution shall be carried forward to new account.

In concrete terms, this means that if there is a (significant and not merely temporary) reduction in the company's assets prior to the annual financial reports are approved, any available net profit may not be distributed as a dividend (or not distributed in full).

Risk of liability and repayment obligation in the case of violation of the dividend-block

What implications does the dividend-block have for the executive bodies of the company?
If a reduction in the company's assets occurs before the annual financial statements are adopted, it is necessary to first examine wether the reduction in assets is significant and not merely temporary.

If this is confirmed, the management (and any existing supervisory board) has to inform the shareholders of this on time, prior to the resolution on the adoption of the annual financial statements.

Subsequently, the shareholders may only pass a resolution to pay out dividends to an amount that does not violate the dividend-block. If the shareholders decide a pay-out in an amount that does not comply with the dividend-block, the managing directors must refuse the pay-out - despite a contrary shareholders' resolution.

The Managing directors, the supervisory-board and the shareholders are well advised to carefully verify the existence of a material reduction of assets. If the dividend-block is violated, this can result in compensation, liability and reimbursement obligation for the aforementioned corporate bodies.

Limitations also exist outside the scope of the dividend-block!
If losses occur after the balance sheet date, pay-outs from a GmbH are not permitted without restrictions. Outside the scope of the dividend-block (this is the prevailing view, for example, if the losses occur after the annual financial statements have been approved but before a resolution on the dividend-payment of the net profit is passed), pay-outs are permitted especially if it would endanger the existence of the company. In this case, the fiduciary duty requires that no existence-endangering distributions be made.

Regardless whether or not the conditions for the statutory dividend-block apply, the executive bodies of a GmbH must therefore carefully examine the legitimacy of pay-outs in loss situations.

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We point out that the legal situation can change constantly, but we are on effort to keep the contents up to date.

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