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Wirecard: German Appeal Court Rules Shareholder Damages Claims Rank *Pari* to General Unsecured Claims

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At a Glance

The Higher Regional Court of Munich last week delivered an appeal verdict in the multibillion-euro *Wirecard* insolvency,[1] ruling that shareholder damages claims arising from capital markets fraud rank equally to general unsecured creditor claims. This overturns a first-instance judgment of the Munich District Court,[2] which had ruled that such claims should rank as equity behind all creditors' claims.

Investors in public companies with their centre of main interest (COMI) in Germany regularly model the impact of potential damages claims on creditors' recoveries in an insolvency. This judgment suggests that shareholder damages claims would rank *pari passu* to unsecured bondholders, lenders and other creditors, whose recoveries may be significantly diluted in the insolvency downside scenario.

Permission has been granted to appeal to the German Federal Court. The position remains uncertain pending the outcome of that appeal.

Background

Wirecard, once a prominent German DAX 30 financial services provider, filed for insolvency in June 2020 after revealing that €1.9 billion in cash — approximately a quarter of its balance sheet — was unaccounted for. In the wake of this, around 50,000

shareholders submitted claims in the insolvency proceedings seeking damages totaling c.€8.5 billion for capital markets fraud and related violations.

In November 2022, the Munich District Court dismissed a shareholder's claim for recognition of his claims as general unsecured claims in Wirecard's insolvency proceedings, ruling that shareholder damages claims were effectively subordinated (see our *Alert*).

Appeal Judgment

The Higher Regional Court of Munich has now overturned the first-instance ruling and decided that, in principle, the shareholder's claims rank *pari passu* to general unsecured claims. The Court did not determine whether the alleged claim actually exists on the merits or in the alleged amount.

The Court held as follows:

- The relevant legal relationship from which the shareholders' losses result is the share purchase agreement, which would not have been concluded without Wirecard's fraud. This decouples tortious claims from the membership in the company (associated with the purchased shares), because the buyer only becomes a member of the company upon settlement of the transaction. It follows that, contrary to the first-instance judgment, the relevant damages claims in insolvency do not necessarily have to be treated in the same way as the purchased financial instrument.
- Contrary to the first-instance judgment, the existing case law of the German Federal Court of Justice (*Bundesgerichtshof*) in *EM.TV* and other cases concurs with treating shareholder damages claims as ranking *pari* to general unsecured claims.
  - In *EM.TV* (2005), the Federal Court ruled that, at least in cases of intentional misconduct, shareholder damages claims are enforceable even if such enforcement otherwise violates capital maintenance requirements under German corporate law. The Court of Justice of the European Union (CJEU) delivered a similar judgment in *Hirmann* (2013).
  - In 2006 (and again in 2022), the Federal Court ruled that investors who subscribed to subordinated profit participation rights (*Genussrechte*, forming hybrid debt capital) after being misled about the issuer's financial situation have a general unsecured claim in the insolvency of the issuer.
  - In its 2006 and 2022 decisions, the Federal Court cited *EM.TV* as a relevant precedent. This shows that the Federal Court intends for the principles laid down

in *EM.TV* to also apply in an insolvency, without distinguishing between equity and debt investments. In respect of their damages claims, misled shareholders therefore are to be treated as third-party creditors with the consequence of a *pari*-ranking in insolvency, and not in their capacity as members (which would make them lowest-ranking).

- On the facts, all relevant damages claims arose from secondary trading. The Court held that a subordination of shareholder damages claims arising from secondary trading would contradict applicable principles of equal treatment.
  - It is not justified to treat defrauded secondary buyers and non-defrauded primary subscribers the same in insolvency, or to grant priority ranking for defrauded secondary buyers only within the lowest-ranking equity class. The equity is typically out of the money within insolvency proceedings; a differentiation only within the equity class would therefore in most cases be economically meaningless.
  - This concurs with the CJEU's judgment in *Hirmann*, according to which shareholders who have suffered a loss owing to a breach of duty committed by the company before or during the acquisition of their shares are not in the same position as the general body of shareholders.

- The Court guided that treating shareholder damages claims as equity would create inconsistencies and unresolved consequential issues within the existing legal framework, which only the legislator can resolve.
  - Shareholder damages claims would need to be factored into the balance-sheet solvency test to avoid inconsistencies, and could therefore trigger the company's insolvency. It would however be inconsistent to deeply subordinate, and in most cases assign zero recovery to, claims that caused the debtor's insolvency in the first place.
  - If treated as equity, shareholder damages claims that have been satisfied in the critical period before the opening of insolvency proceedings would need to be subject to a balanced claw-back regime. However, there are currently no claw-back provisions in the German Insolvency Code that are tailored to the special circumstances of shareholder damages claims or that can readily be applied by analogy.
  - It may be methodologically justifiable to relegate shareholder damages claims to the lowest ranking. However, while a *pari passu* ranking merely operates to dilute recoveries for other creditors and is therefore limited to economic effects, an equity ranking legally abridges claimholders' property rights. Such a result would require an explicit legislative decision and cannot be achieved by way of legal interpretation alone.

- There are many possible variations on the theme of a subordination of shareholder damages claims. For example, distinctions could be made between institutional holders and retail holders; controlling and non-controlling holders; full or partial subordination; and based on different reasons for liability. These issues are for the legislator, rather than the courts, to determine.

Implications

Investors in public companies with their COMI in Germany regularly model the impact of potential damages claims on creditors' recoveries in an insolvency. This judgment suggests that shareholder damages claims would, for the time being, rank *pari passu* to all unsecured creditors, whose recoveries may be significantly diluted in the insolvency downside scenario. The parties to the *Wirecard* litigation are expected to take the matter all the way to the Federal Court, possibly with a referral to the CJEU.

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1. OLG München, judgment dated 17 September 2024 – 5 U 7318/22 e. ↩

2. LG München I, judgment dated 22 November 2022 – 29 O 7754/21. ↩

Related Professionals

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Partner / Munich

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- 20 September 2024 Speaking Engagement Cornell Law Review's 2024 Symposium
- 19 September 2024 Kirkland Alert German Court Erases Shareholder Holdout Plays Against German Restructuring Schemes: Shareholders' Consent Not Required if Only Alternative is Insolvency
- 18 September 2024 Award Legal Business Awards 2024