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Acquisitions in Germany: Hidden Costs and Pitfalls Await Unwary Entrepreneurs

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German labor legislation gives asymmetric rights favoring employees. In the context of an acquisition, section 613a of the German Civil Code prohibits the seller and the buyer from streamlining labor to lower the operating costs of the target company. Given this potentially high labor cost, foreign investors should take into account the effect of section 613a liabilities in order to maximize the potential gain from the acquisition of a former East German company.

In this article, the authors survey current interpretations of section 613a and analyze its elements. The authors then provide a brief description of the rights and obligations of employee, seller, and buyer under section 613a. In addition, the authors offer suggestions on how a buyer may structure her acquisition in order to avoid incurring section 613a liabilities. Where the buyer's transaction incurs section 613a liabilities, the authors suggest methods for minimizing the resulting labor costs.

I.

INTRODUCTION

With the choice of Berlin as the capital of the new united Germany, many entrepreneurs may again be looking eagerly east of the River Elbe for attractively priced businesses and enterprises in order to establish a strong presence near this flourishing capital and business center. A word of caution is in order: extensive costs unfamiliar to the North American business community may await the eager entrepreneur.

Of great concern is the fact that a purchase of any former East German enterprise requires the purchaser to assume all existing employment relationships and their corresponding liabilities. Such liabilities include (but are not limited to) accumulated pension obligations for existing employees, vacation pay, leaves of absence, unemployment insurance, medical and dental insurance and/or other miscellaneous fringe benefits, performance and Christmas

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bonuses, and special employee insurance packages. The assumption of these liabilities will undeniably and significantly increase the costs of the acquisition. The purchaser should therefore carefully strategize to minimize this unfamiliar cost effect.

Current German labor legislation mandates that all employment relationships be protected and preserved upon a change of ownership of any enterprise. This rule may very well dismay many eager "capitalists." The primary exception to this rule appears to be where the change in ownership occurs through an acquisition of shares or interests in stock ownership. However, as the ownership of many former East German enterprises is not stock-based or share-based due to previous communist ownership, the costs associated with the transfer of such enterprises must nevertheless be confronted.

The following analysis assumes that in most cases the North American entrepreneur would want to restructure the target enterprise by streamlining labor and that most former East German enterprises currently employ large numbers of redundant employees. This article confronts the problem of excessive labor costs and offers solutions to minimize them. Part II of this article will describe the statutory provisions of section 613a of the German Civil Code (*Bürgerliches Gesetzbuch (BGB)*)¹ and its current interpretations. Part III then confronts the practical effects that BGB section 613a imposes. The article concludes with suggestions on how an entrepreneur can avoid the statutory pitfalls and structure a transaction to avoid triggering the subject statutory provisions.

II.

THE INTERPRETATION OF BGB SECTION 613a

A. Statutory Provisions of BGB Section 613a

Section 613a of the BGB, a partially anti-entrepreneurial example of legislation, provides:

1. Upon the legal transfer of an enterprise or division of enterprise the new owner must assume all duties and liabilities pertaining to all existing employment relationships. These duties and liabilities are generally regulated by a collective agreement between the parties. This collective agreement will continue to provide the framework for these duties and liabilities unless the new employer itself maintains some kind of collective agreement. In the latter case, the new employer's agreement will replace the former one to provide for the framework for labor relationships with the new employee.
2. The former and new owners are jointly and severally liable for the obligations mentioned in subsection 1 for one year after the date of transfer. If any of these obligations mature after the date of transfer, the former owner

1. *Betriebsverfassungsgesetz* [The Law on Organizing an Enterprise], 1972 *Bundesgesetzblatt [BGBl]* I 13 (F.R.G.), amended by *Arbeitsrechtliches EG-Anpassungsgesetz* [Act Modifying the German Labor Law in Accordance with the European Community Labor Law], 1980 *BGBl* I 1308 & 1991 *BGBl* I 854 (F.R.G.).

is liable only for that portion of the obligation which corresponds to the remaining period of liability within the above-noted transition year.

3. Subsection 2 does not apply where a legal entity is extinguished through corporate merger, corporate dissolution, or corporate reorganization;² section 8 of the Corporate Reorganization Act³ (Umwandlungsgesetz), which regulates all such corporate transfers in the Federal Republic of Germany, remains in effect under such circumstances.
4. The termination of an employee by either the former owner or the new owner due to the "actual" transfer of the enterprise or division of enterprise is prohibited. However, the right to terminate an employee "for cause" continues.⁴

These provisions apply with some exceptions⁵ to any acquisition such that all employment obligations remain an inseparable liability element of the transaction.

B. Definitions of Statutory Components

1. "Enterprise" or "Division of Enterprise" in BGB Section 613a

As detailed in the statute, BGB section 613a is triggered upon the transfer of an "enterprise" or a "division of enterprise." For the purposes of BGB section 613a, the term "enterprise" is generally defined as an organizational unit with which the owner/employer, through the assistance of employees and the aid of tangible and/or intangible assets, pursues a specific goal or objective.⁶ The definition is broad enough to encompass not only manufacturing but also service enterprises. In a similar vein, a "division of enterprise" is generally defined as a subsidiary organizational unit which pursues its own goal or objective and is an integral but separable element within the whole of the enterprise, and which can also be the subject of an acquisition.⁷

Furthermore, note that only the "essential operating assets" of an enterprise need to be transferred in order to trigger BGB section 613a. The question is whether the material contents of the transfer effectively add up to a transfer of that operating unit. This in turn depends on the type of business being acquired.⁸

To determine whether there is an actual transfer of an "enterprise" or a "division of enterprise" sufficient to trigger BGB section 613a, the type of business which is the subject of the acquisition must first be assessed. Second,

2. In other words, subsection 2 does not apply to any stock-based or share-based transaction.

3. Section 8 of the Corporate Reorganization Act (Umwandlungsgesetz) was first published on November 6, 1969.

4. Translation provided by authors.

5. See *supra* part II.A.3 for the exceptions recognized in BGB § 613a.

6. Judgment of July 3, 1986, Bundesarbeitsgericht [Supreme Labor Court] [BAG], reprinted in 40 DER BETRIEB [THE ENTERPRISE] 99 (1987) (F.R.G.).

7. Günter Schaub, *Rechtsprobleme des Betriebsübergangs* [Legal Problems of Enterprise Transfers], 5 ZEITSCHRIFT FÜR WIRTSCHAFTSRECHT [THE BUSINESS LAW JOURNAL] 272, 274 (1984).

8. Judgment of July 3, 1986, BAG, reprinted in 39 DER BETRIEB 99 (1986) (F.R.G.).

the type of transfer contemplated for the particular type of business must effectively add up to a transfer of that operational unit. The type of transfer is judged by analyzing the material contents of the transfer.

In a manufacturing context, a transfer occurs when such a significant portion of the machinery is sold that the seller cannot pursue the original objective of the business.⁹ Correspondingly, in a service enterprise, a transfer will effectively occur where customer lists, goodwill, and know-how are sold¹⁰ to the extent that that enterprise can no longer pursue its original objective without these intangible assets. In both instances, BGB section 613a would be triggered and all employment relationships and obligations associated with the enterprise or division of enterprise would be transferred to the purchaser.

2. Definition of "Legal Transfer"

a. Generally

A "legal transfer," as required to trigger BGB section 613a, encompasses all transactions of singular succession. Generally, acts of singular succession include events such as a sale, gift or trust, lease, or usufruct.¹¹

These acts of singular succession as detailed in BGB section 613a occur even where no paperwork detailing the transaction exists.¹² An act of singular succession, or "legal transfer," also exists if the transaction is flawed or follows the actual acquisition of control of the enterprise. To trigger BGB section 613a it is enough if the new owner represents herself to the world as being the actual owner of the enterprise or division of enterprise. A "legal transfer" may also occur when the acquisition is effectuated by means of a series of legal transactions, rather than one large singular acquisition.¹³

Not included under the rubric of BGB section 613a is any change of ownership due to the acquisition of shares or interests in stock or share capital. This is due to the fact that the enterprise retains its original legal identity in the transaction and no change in legal employer has occurred. Similarly, should a partnership enterprise undergo a change in partners, BGB section

9. GÜNTER SCHAUB, ARBEITSRECHTS-HANDBUCH [HANDBOOK ON LABOR LAW] 900 (7th ed. 1992).

10. Judgment of Oct. 18, 1990, BAG, *reprinted in* 8 NEUE ZEITSCHRIFT FÜR ARBEITS- UND SOZIALRECHT [THE NEW LABOR LAW JOURNAL] [NEUE Z. ARBEITS- & SOZIALR.] 305, 306 (1991) (F.R.G.); Judgment of June 25, 1986, BAG, *reprinted in* 38 DER BETRIEB 2459 (1986) (F.R.G.); Judgment of May 5, 1985, BAG, *reprinted in* 39 NEUE JURISTISCHE WOCHENSCHRIFT [THE NEW LEGAL WEEKLY] [N.J.W.] 454 (1986) (F.R.G.); SCHAUB, *supra* note 9, at 901.

11. OTTO PALANDT & HANS PUTZO, BÜRGERLICHES GESETZBUCH [THE CIVIL CODE] BGB § 613a(II)(B) (51st ed. 1992). A gift of trust is considered an act of singular succession if the business is continued in the name of the trustee.

12. For example, this may occur when the "papering of the transaction" has been neglected or intentionally omitted.

13. Judgment of Sept. 29, 1988, BAG, *reprinted in* 6 NEUE Z. ARBEITS- & SOZIALR. 800 (1989) (F.R.G.); Judgment of May 22, 1985, BAG, *reprinted in* 39 N.J.W. 448 (1986) (F.R.G.).

613a is not applicable because the legal entity remains unchanged. Finally, for similar reasons, BGB section 613a will not apply to instances of inheritance.

b. Transfer Upon Bankruptcy

If the business or enterprise declares bankruptcy and is sold by the bankruptcy trustee during the bankruptcy proceedings, BGB section 613a nonetheless remains applicable.¹⁴ This means that despite a declaration of bankruptcy by the subject enterprise, any potential purchaser must nevertheless employ, or more precisely “re-employ,” all employees who were employed by the target enterprise directly preceding the bankruptcy. Because the purchaser is required to reinstate all these employees, the labor costs of the purchase therefore remain high despite the bankruptcy of the target enterprise.

Due to the almost oppressive effect this would have on investments into former East Germany, the Federal German legislature has temporarily amended BGB section 613a.¹⁵ The amendment provides that until December 31, 1994, BGB section 613a will not apply to transfers of enterprises in the area of former East Germany which occur during receivership or global execution proceedings.¹⁶ Receivership or global execution proceedings are currently being implemented in a number of cases in place of bankruptcy proceedings.¹⁷

Despite the amendment, the purchaser cannot bide its time in negotiations with the vendor in hopes that the bankruptcy of the enterprise will occur in the interim. Any indication that the purchaser and the vendor are colluding, either implicitly or explicitly, for the purchase of the enterprise upon bankruptcy will trigger BGB section 613a. In these circumstances, all labor costs will nonetheless be transferred since the transaction cannot be said to have occurred in good faith. The parties to the transaction will therefore be liable for punishment since the transaction violates the statutory provision for “Treu und Glauben.”¹⁸

14. Judgment of Nov. 13, 1986, BAG, *reprinted in* 40 DER BETRIEB 990 (1987) (F.R.G.).

15. Gesetz über die Spaltung der von der Treuhand verwalteten Unternehmen [Law Regarding the Division of Treuhand-administered Enterprises] [SpTrUG] § 16, 1991 BGBl I 854 (F.R.G.); Bundestag [BT], *reprinted in* Drucksache [Minutes of Federal Parliament Sessions] 12/3862; [BR] *reprinted in* Drucksache 836/92.

16. Einführungsgesetz zum Bürgerlichen Gesetzbuch [The Implementing Act of the Civil Code] [EBGG] art. 232, § 5(II) (F.R.G.) (*implemented through* SpTrUG § 16(II)).

17. Gesamtvollstreckungsordnung [Act on Receivership] [GesvO], 1991 BGBl I, *cited in* GERT COMMANDEUR, *Die Bedeutung des § 613a BGB im Bereich der ehemaligen DDR [The Importance of § 613a of the Civil Code in the Territory of the Former German Democratic Republic]*, 8 NEUE Z. ARBEITS- & SOZIALR. 705, 706 (1991).

18. Roughly translated, “Treu und Glauben” means “Good Faith.” *See infra* note 26.

3. "Existing Employment Relationships" Under BGB Section 613a

The phrase "existing employment relationships" encompasses all actual employment relationships possessed by the enterprise or division of enterprise at the date of the transfer of ownership. This definition includes all terminated employees whose employment is still ongoing at the time of transfer, or whose resignation is pending.¹⁹ All management personnel, persons enjoying any parental leave of absence, and trainees and internship participants are also protected by BGB section 613a. Not included under the rubric of BGB section 613a are positions which are not in fact employment relationships between the employee and the employer/target enterprise, such as members of the Board of Directors.²⁰

Of particular significance, however, is the continued liability for future pension disbursements for pensions guaranteed by the former owner that mature after the date of acquisition. This cost element in the transaction can alone overshadow the other previously mentioned liabilities. The new owner under BGB section 613a is thus forced to acquire pension liabilities for employees who were active in the enterprise at the date of acquisition.²¹

The new employer is not liable for pensions of former employees, of employees having left the enterprise by the date of acquisition, or of employees who have already begun drawing on their pension claims.²² However, it is responsible for all employees at the date of acquisition, regardless of whether or not they continue their employment after that date. Generally, it can be said that any obligations stemming from the original employment relationship will be protected by BGB section 613a. This includes such things as the use of a company car, performance bonuses, and Christmas bonuses, among others.

Although an agreement by the employee to the transfer of ownership is not a prerequisite to the transaction per se, an employee may nevertheless impede the transfer of her employment through the "right of objection." No reason need be given by the employee for the objection to the transfer.²³ Once exercised, the objection impedes the transfer of that employee's contract to the new owner and the employee remains with the former owner/employer. However, this employee may nonetheless be terminated by the former owner for operational reasons if it is no longer feasible to keep that employee employed.²⁴

19. Judgment of Nov. 11, 1986, BAG, *reprinted in* 40 N.J.W. 3031 (1987) (F.R.G.).

20. Günter Schaub, § 613a [*Betriebsüberhang*] [*Enterprise Transfer*], in MÜNCHENER KOMMENTAR ZUM BÜRGERLICHEN GESETZBUCH [THE MUNICH COMMENTARY ON THE CIVIL CODE] § 613a, l. 9 (Kurt Rebmann & Franz Jürgen Säcker eds., 1988).

21. PALANDT & PUTZO, *supra* note 11, § 613a, l. 20.

22. Judgment of Mar. 24, 1987, BAG, *reprinted in* 5 NEUE Z. ARBEITS- & SOZIALR. 246 (1988).

23. Judgment of Feb. 15, 1984, BAG, *reprinted in* 1 NEUE Z. ARBEITS- & SOZIALR. 32 (1984).

24. Judgment of Oct. 2, 1974, BAG, *reprinted in* 28 N.J.W. 1378 (1975).

This “right of objection” has yet to receive official legal status and in any case does not amount to an automatic resignation by the employee. As the employer is required by BGB section 613a to reveal the incumbent transfer of ownership to the employees, the employee may only access the official “right of objection” “within a reasonable period of reflection” (“innerhalb angemessener Überlegungsfrist”) once the employer has communicated the incumbent transfer to the employee.²⁵ The “right of objection” can nevertheless not be used as concerted collective pressure on the former and/or new owners either to hinder the transfer of the enterprise or to bargain for supplementary employment benefits. The “right of objection” is personal to the employee, and has evolved in German jurisprudence to safeguard the right of each worker to decide where and by whom she is employed. It therefore cannot be used towards collective coercion.²⁶

The official “right of objection” is unlikely to create many problems in the future. As all employment obligations on behalf of the employee remain safeguarded by BGB section 613a, the employee has little cause to assert this “right of objection.”

III.

EFFECTS OF BGB SECTION 613a: BUYERS INCUR ASYMMETRIC DUTIES AND OBLIGATIONS ONCE BGB SECTION 613a IS TRIGGERED

A. *Effects on Former Employer*

The former employer and the new employer are jointly and severally liable for all obligations associated with the transferred employment relationships which accrue before the acquisition and which mature before the expiration of one year’s time after the acquisition date.²⁷ This liability consists of all future pension distributions and other similar obligations, such as Christmas bonuses, expected paid holidays, and leaves of absence.²⁸ At the same time, the former employer loses all decision-making rights with respect to the employees which would normally accrue to it.²⁹

B. *Effects on New Employer*

Under BGB section 613a, the new employer “steps into the shoes” of the former employer when it assumes ownership of the firm. The new employer is liable for all costs and obligations associated with the employment relation-

25. PALANDT & PUTZO, *supra* note 11, § 613a, l. 15.

26. Günther H. Roth, § 242 [*Leistung nach Treu und Glauben*] [*Performance in Good Faith*], in MÜNCHENER KOMMENTAR ZUM BÜRGERLICHES GESETZBUCH [THE MUNICH COMMENTARY ON THE CIVIL CODE], *supra* note 20, § 242, l. 249.

27. BGB § 613a.

28. SCHAUB, *supra* note 9, at 909.

29. PALANDT & PUTZO, *supra* note 11, § 613a, l. 18.

ships existing at the time of acquisition and for all those which accrue after the acquisition.³⁰

C. *Effects on Employees*

The transferred employees are deemed to retain the same duties and obligations towards the new owner as they owed the former owner. If certain amounts are due to the employee from her employment relationship, the employee has the option of demanding this amount from either the former or the new employer/owner for one year after the date of acquisition. The employee's right to a pension continues in the new employer as do any other perquisites which were components of the employment relationship with the former employer. The employee further has the right to retain the daily specifics of the employment relationship, such as scheduled and unscheduled break allowances, and start and finish times.³¹ In addition, whether or not the employee leaves or remains in her position, non-competition covenants in the employee's contract will continue in effect.³²

D. *Effects on Collective Agreements*

Until the enactment of the European Community labor law adjustment directive,³³ no provision had been made regarding collective agreements as they pertained to BGB section 613a. With the integration of this directive into German law in 1980, BGB section 613a was modified to preserve the validity and effectiveness of any collective labor agreement existing before the takeover date in any subject acquisition. Under the current law, collective labor agreements of the former employer will continue in effect unless the new employer possesses effective labor agreements. In the latter case, the new employer's collective agreement will take precedence over agreements with the old employer.³⁴

E. *Effects on Rights of Termination*

All rights of employees to resign from their positions remain unaffected by BGB section 613a. At the same time, however, employers have been strictly curtailed in exercising their right to terminate an employee. The employers can only terminate "for cause." The former employer is strictly prohibited from terminating an employee on the grounds that the new employer does not wish to employ the employee.³⁵

30. Schaub, *supra* note 20, § 613a, I. 19; see *supra* part III.A for examples of these obligations.

31. PALANDT & PUTZO, *supra* note 11, § 613a, I. 19.

32. *Contra* Schaub, *supra* note 7, at 275.

33. 1977 O. J. (L 61) 26.

34. PALANDT & PUTZO, *supra* note 11, § 613a, I. 24.

35. BGB § 613a(4).

Termination “for cause” includes termination due to breach of an employee’s contract or termination for operational reasons. At first glance this latter ground might seem to alleviate the entire problem of employment liabilities for the new employer—the new employer would theoretically need only to devise a business plan by which it could show that a certain employee had in fact become redundant due to the restructuring of operations under the new employer.

Unfortunately, this scenario is not as straightforward as it might at first appear. Termination due to operational requirements brings with it an automatic liability on the employer to provide a mandatory social compensation package to the terminated employee. This compensation package is all too often accompanied by a rather expensive price tag. It is usually vastly more expensive than comparable “compensation packages” generally afforded to similarly terminated North American employees.

Finally, any claims for improper dismissal before the completion of the acquisition can only be brought against the former owner.³⁶ Therefore, the former owner would likely stipulate that provision be made to preserve these employment relationships in the actual text of the acquisition agreement.

IV. STRATEGIES FOR MINIMIZING THE EFFECTS OF BGB SECTION 613a

Section 613a of the BGB is mandatory law. The buyer can, however, use limited and/or gradual transfers to avoid falling within the ambit of BGB section 613a. In addition, the buyer can minimize liability by relocating the enterprise after the acquisition. Alternatively, long-term collaboration may be used to skirt BGB section 613a.

A. Limited Transfer of Assets

Since BGB section 613a is mandatory law, vendors and purchasers of enterprises cannot contract out of the legislation. They cannot circumvent the automatic transfer of employment relationships to the purchaser, as stipulated by BGB section 613a, within the actual agreement of sale.³⁷ The parties to the contract may, however, make the acquisition more cost-effective with respect to labor costs if the transfer of assets, taken together, is inadequate to satisfy the definition of “enterprise” or “division of enterprise” contained in the legislation.

To achieve this, the buyer should not purchase the organizational unit or division of the enterprise lock, stock, and barrel. The vendor should retain sufficient operating funds to keep that particular target division operational. To this end, it is insufficient merely to exclude certain individual assets, such

36. See *supra* notes 29, 34.

37. Judgment of July 14, 1981, BAG, reprinted in 35 N.J.W. 1607 (1982) (F.R.G.).

as pieces of machinery, from the transfer. It should not appear that the original operating function of the division/organizational unit is actually transferred.

Whether this approach works depends on the particular circumstances of each individual transaction, thus no general rule can be propounded. It is necessary to evaluate which assets may be acquired without transferring the entire organizational unit. Multiple contracts transferring the assets of the target enterprise must be carefully drafted so that the sale of the enterprise's capital assets remains just outside the scope of the statute.

In some cases, defining this boundary can be very difficult. Even after meticulous preparation, the possibility of litigation evolving from the transaction may never altogether be excluded. Also, the danger remains that despite this evaluation by the purchaser and the vendor, a court might reexamine the requirements of BGB section 613a some time in the future and correspondingly reevaluate which assets, if transferred, would constitute a de facto transfer of that organizational unit.

Because of the uncertainty involved in judicial interpretation, the parties to the transaction may wish to draft a section into the acquisition contract which would render the contract retroactively void should a court decide that the agreement warrants the application of BGB section 613a. A purchaser may thereby ensure against a mandatory assumption of all employment relationships upon the acquisition of the target's capital assets. Furthermore, more concise provisions may be made for a new deal, such as long-term collaboration, to automatically replace the original but now void acquisition contract.

B. Gradual Transfer of Assets

While both limited and gradual transfers may be used for the purchase of both manufacturing and service enterprises, the gradual transfer method described below might be particularly well-suited for the transfer of service enterprises. In acquiring a service-industry enterprise, the transfer of the customer lists and know-how is of primary consideration. It is difficult to avoid the application of BGB section 613a upon the transfer of customer lists and know-how. This is so because this would constitute the transfer of the essential intangible operating assets of the particular service enterprise. To circumvent these labor costs, it might be possible to go about the transfer of these intangible assets without pursuing the acquisition through a singular legal transaction.

One way to do this would be to incorporate a new corporation with its own legal identity next to the target enterprise whose know-how and customer lists are to be acquired. The target enterprise might then reduce its business gradually and refer any new customers or clientele which seek it out to the new corporation as they become available. The original enterprise may

also enable the new corporation to entice established customers away from the original enterprise incrementally.

During this period, the new corporation could simultaneously entice individual employees away from the original enterprise, whose knowledge of the customers and whose established relationships with those customers would be transferred in addition to any know-how they possess. The employees not enticed away from the original enterprise would remain employed by it. The original enterprise might eventually be put into receivership, liquidated by the original employer/vendor, or petitioned into bankruptcy.

This particular process is not based on a singular or series of legal transactions and therefore does not trigger the first section of BGB section 613a. According to the German Supreme Court's interpretation of BGB section 613a, the section applies if a service enterprise—in this case primarily consisting of customer lists and know-how—is transferred even without the benefit of any legal "papering" of the transaction.³⁸ This continues to be the current interpretation, despite the fact that the statute specifically curtails its application to transfers of enterprises under "legal transactions."³⁹ According to prominent academic and current practicing legal opinion,⁴⁰ this interpretation has evolved only to differentiate transactions of universal succession such as inheritance from ordinary agreements for purchase and sale.

Thus, the transaction may only be made cost-effective, in terms of labor costs, if all the material assets of the enterprise are not transferred. At this point in the transaction, care must be taken so that the new enterprise takes over only a portion of the clientele, builds up its own know-how or relies on third parties for this know-how, and does not entice away any significant portion of the employees of the original enterprise. Otherwise, this transfer might constitute the "enterprise" or "division of enterprise" as defined in BGB section 613a and would therefore trigger its corresponding labor cost element.

Alternatively, the vendor may transfer the clientele and the know-how of the target enterprise to two or more separate and independent new enterprises established by the purchaser. In that case, the purchaser may be able to divide the target assets such that the transfer does not have the effect of transferring two separate divisions of the enterprise. The optimum division of the enterprise depends, of course, on the particular needs of the incumbent purchaser.

38. Judgment of Dec. 12, 1990, BAG, *reprinted in* 8 *NEUE Z. ARBEITS- & SOZIALR.* 306 (1991) (F.R.G.); Judgment of Sept. 29, 1988, BAG, *reprinted in* 6 *NEUE Z. ARBEITS- & SOZIALR.* 799, 800 (1989) (F.R.G.). In other words, BGB § 613a applies to both de facto and de jure transfers.

39. See *supra* text accompanying note 1.

40. PALANDT & PUTZO, *supra* note 11, § 613a, l. 13; Schaub, *supra* note 20, § 613a, l. 25.

C. Relocation of the Enterprise

If asset transfer is not feasible, the contracting parties should at least minimize the effects of BGB section 613a. To this end, the purchaser may wish to move the entire enterprise to a new location immediately upon completion of the purchase. The new location of the enterprise should be far enough from the enterprise's old location so that a daily commute for most employees would be impracticable. The new location may, for example, be targeted outside of the provincial jurisdiction of the old enterprise. The new location may also be targeted outside of the national jurisdiction, in which case tax and other consequences of the transfer should be reviewed according to the specific local laws.

This relocation is especially costly and time-sensitive for manufacturing enterprises. Often, however, it is one of the only possible ways in which a new employer can acquire some right to terminate employees and dismantle a company's large, cumbersome, and often antiquated and atrophied worker and/or management teams. Similarly, by relocating the enterprise, it may also be possible to consolidate and modify the target enterprise with other ventures owned by the purchaser to effect even further restructuring and thereby reap the benefits of any resulting synergies.

According to the most recent judicial writings on the subject, the new employer must take on all the employment relationships and liabilities of all those employees willing to transfer to the new location.⁴¹ These relationships and liabilities remain governed by whatever collective agreement would have been in place at the old location.⁴² The particular collective agreement remains in effect for all those employees willing to relocate.

To ensure relocation by the employees, employee contracts need to be altered and any such alteration would have to be agreed to by the target employees. The employer cannot force the original employees to work at the enterprise's new location. The employee cannot be forced to relocate, as she need only fulfill her original contract. Should the employee resist becoming actively employed at the new location, this resistance has the same effect as if she had exercised her "right of objection" under BGB section 613a. The legal consequence of the employee's resistance, just as under the employee's "right of objection," is that the employment relationship is not transferred to the new employer but remains with the original employer. The original employer can often no longer offer the possibility of employment at the original location of the enterprise due to the enterprise's sale. This then gives the original employer the right to terminate⁴³ the employment relationship for operational reasons.⁴⁴

41. PALANDT & PUTZO, *supra* note 11, § 613a, I. 17; Schaub, *supra* note 20, § 613a, I. 60.

42. See *supra* part III.D.

43. Judgment of Apr. 20, 1989, BAG, reprinted in 42 DER BETRIEB 2334 (1989) (F.R.G.).

44. Kündigungsschutzgesetz [The Protection Against Wrongful Termination of Employment Act] § 1(2), 1969 BGBl I 1317 (F.R.G.).

D. Long-Term Collaboration

If relocation after the acquisition is unduly costly or other reasons speak against it, the potential purchaser can use another method to minimize costs in the acquisition in the long run. The purchaser may postpone the purchase of the enterprise entirely and initially enter into contracts with the potential target enterprise for some type of long-term collaboration. This route is available only if—as is often the case with acquisitions in the area of the former German Democratic Republic—there is an overly abundant number of employees to be streamlined.

There exist several reasons to delay the acquisition until a later time. In many cases, questions of ownership of real property remain unanswered. Moreover, the potential purchaser may wish to test and observe the viability of a former state-owned enterprise over a period of time before deciding to resort to a complete acquisition.

If the “Treuhandanstalt”⁴⁵ is unsuccessful in finding other purchasers for the enterprise, instead of immediately purchasing divisions or assets of the enterprise, an interested party may wish to enter into a contract for long-term collaboration with the target enterprise, such as for the delivery of parts or inventory. However, should another purchaser make an offer, the “Treuhandanstalt” will likely decide in favor of the latter’s offer in order to close one of its innumerable outstanding files. Again, it must be emphasized that any and all contracts with the target enterprise must be undertaken in good faith, and collusion between the vendor and the purchaser to avoid the labor cost effects of BGB section 613a is to be avoided.

A contract for long-term collaboration should bind the target company for an extended period and should also contain effective non-competition provisions. Once the target company’s business begins to consist of work done primarily for the benefit of the potential purchaser, this developing dependency will make the incumbent purchase of the target enterprise easier for that purchaser. It should be noted that care should be taken in the drafting of the non-competition provisions so as not to violate the rules of customary business practice as embodied in BGB section 613a or other applicable anti-trust legislation.

The potential purchaser can test the viability of the enterprise during this period of collaboration. During this time, the enterprise will be required to implement its own rationalization and/or “restructuring” scheme. Over the course of time, this planned collaboration will effectively develop economic dependency due directly to the resulting integration. The potential purchaser may wait for this restructuring to take place without risk to itself, and may at that time decide whether it wishes to purchase any of the assets or divisions of the enterprise.

45. The “Treuhandanstalt” is the government-established administrative trustee in charge of privatizing all former state-owned enterprises.

V.
CONCLUSION

The hidden costs associated with the transfer of enterprises in the former East Germany require careful strategizing to effectively deal with excessive labor costs imposed by the labor legislation embodied in BGB section 613a. Successful strategies to this end might include the limited transfer of the assets of the enterprise; the gradual transfer of the assets of the enterprise; the relocation of the enterprise; and the creation of contracts for long-term collaboration between the vendor and purchaser enterprises. Unless such steps are taken to plan out the structure of the transfer ahead of time, entrepreneurs may be dealt a powerful blow by extensive labor costs with the transfer of all employment relationships and their corresponding liabilities. The North American entrepreneurial and practicing legal communities would especially be well advised to learn to strategize as a preliminary practice for acquisitions in the European Community given the historical trend behind BGB section 613a.