

GERMANY PROPOSES HARSHER PENALTIES FOR CORPORATES

The long-awaited coalition agreement in Germany may have important implications for the law on corporate penalties. Under current proposals, the maximum amount of pecuniary penalties which may be imposed will increase to 10 per cent of a corporate's revenue. The plans also include incentives to cooperate with authorities and new rules in relation to internal investigations.

No single party secured a majority in the German parliamentary election in September 2017, leading to the formation of a coalition between the Christian-Democratic Union (*Christlich Demokratische Union Deutschlands, CDU*), Christian-Social Union in Bavaria (*Christlich-Soziale Union in Bayern, CSU*) and the Social-Democratic Party (*Sozialdemokratische Partei Deutschlands, SPD*). The coalition partners presented their coalition contract on 7 February 2018. Amongst the important features of this contract are proposals for comprehensive reform of the law on the penalties which may be imposed on corporates (in particular in relation to criminal misconduct committed by employees) and separate new regulations governing the judiciary.

Under the current law, it is only possible to prosecute individuals under German criminal law, while German administrative offences law provides that corporate administrative fines (*Unternehmensgeldbußen*) may be imposed on corporates for company-related offences committed through the conduct of senior managers (*Leitungspersonen*). Such corporate administrative fines can generally amount up to EUR 10 million for each individual case and indeed may exceed this amount in some cases where it is considered necessary to remove all gains made by a corporate entity in connection with particular misconduct.

Under the current law, a determination of corporate administrative fines on the basis of a corporate's annual revenue is provided only for breaches of antitrust or anti-money laundering laws (up to 10 per cent) and for infringing capital market laws (up to 15 per cent). It is envisaged that certain infringements of the EU General Data Protection Regulation (GDPR), which will enter into force on 28 May 2018, may lead to penalties of up to four per cent of the corporate's annual revenue. Furthermore, both German administrative offences law and German criminal law provide for a confiscation of economic benefits gained by a corporate from criminal or administrative offences by way of forfeiture orders (*Einziehungsanordnungen*), in fact without deducting any expenses that the concerned corporate entity had in connection with such criminal or administrative offences.

The most important changes announced in the coalition contract

- Introduction of an obligation to enforce and to impose penalties on corporates instead of enforcement authorities making relevant discretionary decisions
- Increase of the general maximum amount for financial penalties to 10 per cent of the concerned corporate's annual revenue
- Introduction of new, more transparent, rules for the assessment of corporate pecuniary penalties
- Introduction of "new punitive instruments", including a public announcement of imposed corporate penalties
- Implementation of specific rules and requirements governing the termination of investigation proceedings without corporate penalties
- Implementation of incentives for corporates to cooperate with enforcement authorities and rules for internal investigations

The intended changes are reminiscent of different recent initiatives. In particular, there are clear parallels with the draft law on criminal liability of corporates and other legal entities (*Entwurf eines Gesetzes zur Einführung der strafrechtlichen Verantwortlichkeit von Unternehmen und sonstigen Verbänden – Verbandsstrafgesetzbuch*) put forward by the German Federal State of North Rhine-Westphalia of 2013 and the Cologne draft law on sanctions for legal entities (*Kölner Entwurf eines Verbandssanktions-gesetzes*) presented by the research group on corporate criminal liability at the University of Cologne in December 2017. The German Ministry of Justice is reported to have worked on a similar draft law in the last legislative period. The provisions in the coalition contract should pave the way for this draft law to now be submitted to the legislative procedure under the new government.

OBLIGATION TO ENFORCE INSTEAD OF DISCRETIONARY DECISION

The coalition contract suggests that authorities should be obliged to conduct investigations and, where wrongdoing is uncovered, to impose penalties on corporates for relevant violations in the future. This would be a significant tightening in comparison to the current legal situation. At present, under the so-called "opportunity principle" in German administrative offences law, enforcement authorities currently decide at their reasonable discretion whether and, if so, to what extent they impose penalties on corporate entities or whether they terminate investigation proceedings against that corporate without a penalty.

This proposed obligation to enforce is supposed to be balanced by specific rules on when and how investigations may be concluded without the imposition of corporate penalties. The rationale behind these proposed rules is to provide the judiciary with the flexibility it requires in practice and to provide corporates with some incentive to proactively bring matters to the attention of enforcement authorities and cooperate with their investigations. The coalition contract does not specify the particular circumstances in which such settlements may be reached or how in practice they may be agreed. However, it may be expected that terminations of investigation proceedings instead of the imposition of penalties will only be possible under clearly defined and relatively narrow conditions. For example, the draft law on implementing criminal liability of corporates and other legal entities proposed by the German Federal State of North Rhine-Westphalia of 2013 stated that whether the concerned corporate entity contributed to the uncovering of violations of laws by means of voluntary disclosure, whether it cooperated with the investigation authorities and whether it implemented sufficient compliance measures to prevent further similar violations are all relevant considerations for when deciding whether a negotiated settlement may be appropriate.

HARSHER PECUNIARY PENALTIES

The coalition contract proposes that, for corporate entities with an annual revenue above EUR 100 million, the maximum amount of pecuniary penalties should be 10 per cent of the annual revenue of the entity in the future. This would amount to a significant intensification compared to the current general maximum amount for corporate administrative fines of EUR 10 million. Based on the revenues of the 30 German DAX-listed companies in 2016, which amounted to between approximately EUR 2.4 billion and EUR 217 billion,

pecuniary penalties of between approximately EUR 240 million and EUR 21.7 billion could be imposed on corporates of that magnitude.

Other measures proposed in the coalition contract include new specific and transparent rules for the determination of pecuniary penalties for corporate entities and "new punitive instruments" (although the detail of these proposed instruments is not yet known). The draft law on implementing criminal liability of corporates and other legal entities by the German Federal State of North Rhine-Westphalia, however, envisaged, amongst others, compulsory breaking up of corporates as a last resort. In any event, following the international trend of a so-called "naming and shaming", the coalition contract stipulates that penalties imposed on corporate entities should generally be announced publicly by appropriate means, similar to the current practice with regard to corporate penalties in the field of capital market law.

INCENTIVES TO COOPERATE AND RULES FOR INTERNAL INVESTIGATIONS

The coalition has made clear that it wishes to set incentives for corporate entities to contribute to investigation proceedings by means of internal investigations and subsequent disclosure of relevant findings vis-à-vis enforcement authorities. In fact, in practice, cooperation and voluntary disclosure are already factors weighing against the imposition of corporate penalties. Furthermore, German authorities and courts increasingly expect internal investigations or suggest them to corporates and their advisors. In a judgement of 9 May 2017, the German Federal Court of Justice (*Bundesgerichtshof*) also clarified that, when determining corporate administrative fines, the implementation of compliance measures designed to prevent recurrences of violations of laws is an important positive indicator. However, there is still a lack of relevant clear guidance, as opposed to, for example, in the UK and the US where corporates can, in particular, increase their chances for a declination, a penalty reduction of up to 50 per cent or a Deferred Prosecution Agreement (DPA) through early and fulsome voluntary disclosure and full cooperation according to applicable guidelines.

The coalition partners have indicated that it is their eventual aim to implement statutory rules governing internal investigations, especially regarding the seizure of relevant documents and the circumstances in which dawn raids may be conducted. In this regard, the intended reform of the law on corporate penalties must be seen against the background of several proceedings pending at the German Federal Constitutional Court (*Bundesverfassungsgericht*) regarding the permissibility of a dawn raid and seizure of documents relating to an internal investigation which were conducted at the German office of a US law firm in March 2017.

IMPLICATIONS FOR COMPANIES

It remains to be seen whether or how the new government will actually implement the announced changes through a concrete draft law. In any event though, corporates should consider even more carefully than ever whether the compliance measures aimed at preventing misconduct from occurring and the policies and procedures they have in place to conduct internal investigations and disclose findings in a timely and appropriate way are robust enough to help them avoid the worst consequences of the proposed new tougher penalties regime.

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