MUNI
LAW

Interpretation of founding acts of business corporations, foundation deeds and wills

from a comparative perspective

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Survey of Contents

I. Interpretation in general
II. Interpretation of foundation acts of business corporations
III. Interpretation of foundation deeds and wills

I. Interpretation in general

- what is interpretation in a legal context?
  - process by which the meaning of a legal norm shall be determined
  - determination of the normative content
- object of interpretation in a legal context
  - any kind of (written?) law as adopted by legislation, court decisions
  - any kind of legal act by by individuals such as contracts, unilateral acts (e.g. acceptance of an offer, termination of a contract, wills), statutes of corporation, foundation deeds, resolutions of an organ of a company or a foundation etc
- why do we need interpretation?
  - any legal norm is act of communication (creator – recipient/addressee)
  - creator of the legal norm has intention about its purpose
  - recipient has to follow the norm and may understand it in a different way

I. Interpretation in general

- what are the elements on which interpretation (in private law) is based?
- protection of private autonomy
  - legal acts serve as instrument by which a person makes use of his/her private autonomy
  - specific intention (economic or other) of a person will be expressed by a declaration of will (e.g. offer to a contract)
  - which being a legal act (or becoming part of it) will be binding and can be enforced
- protection of trust of recipient
  - recipient (addressee) of a declaration of will may understand it in a specific way
  - relies on his/her understanding
  - by entering into contract the recipient makes use of his/her own private autonomy

I. Interpretation in general

- any legal system has to provide solutions for balancing the interests of both parties involved
- pandectistic movement (Germany, 19th century)
- „theory of will“ (theory of intention, „Willenstheorie“) *vs*.
  - relevance of what the person making the declaration really intended („subjective interpretation“)
- „theory of declaration“ („Erklärungstheorie“)
  - relevance of how the declaration had to be understood („objective interpretation“)

I. Interpretation in general

- modern systems are based on a combination of both theories
  - in modern contract law an objective interpretion would prevail
  - but a party would be permitted to refer to his/her actual intention if, for specific reasons, protection of the trust of the other party is not required
- result of this combination is a two step system
- step 1: interpretation
  - determination of the normative content of the legal act
  - based on the common understanding of the word that were used
    - as everybody would understand it
    - relevance of language use of professionals
    - relevance of technical terms
    - context of the the legal act has to be taken into consideration (costumer hands over item to salesperson in the supermarket as an expression of intent to buy)

I. Interpretation in general

- if both parties understand a specific term in the same way, but different from the common understanding, their subjective view prevails
- „falsa demonstratio non nocet“ (a false description does not vitiate)
  - based on protection of private autonomy of both parties
  - protection of trust not required
- see Art 18 (1) Swiss Code of obligations (OR):
  - „When assessing the form and terms of a contract, the true and common intention of the parties must be ascertained without dwelling on any inexact expressions or designations they may have used either in error or by way of disguising the true nature of the agreement.”
- see Austrian Supreme Court 4 Ob 35/10s
  - A is owner of a foreign currency account in CHF. A discusses a money transfer of 600.000 with an employee of the bank. For both parties it is clear that 600.000 CHF should be transferred. For the transfer a form is used where the currency indication „EUR“ is preprinted which remained unnoticed by the parties. 600.000 Euro are being transferred.
  - Decision of Supreme Court: Bank acted negligently because, based on the concept of *falsa demonstratio*, the order was 600.000 CHF.
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I. Interpretation in general

  - interpretation in favor of the debtor in case of a promise of donation or another gratuition contract? (*favor debitoris*)
- simple interpretation (*einfache Auslegung*) vs. supplementary interpretation (*ergänzende Auslegung*)
- simple interpretation is based on the acutal intention of the parties at the time of the legal act (e.g. conclusion of the contract)
- supplementary interpretation is a gap-filling instrument
  - a conflict arises which the parties did not foresee when concluding the contract
  - the contract does not provide a provision for this conflict

I. Interpretation in general

- solution by filling the gap by creation of a supplementary provision based on the hypothetical intention of the parties
- safeguarding the purpose of the contract
- e.g.: A sells his business to B. Next month A opens a competing business to the one he just sold next door to B. Is A permitted to do so if the contract between A and B does not provide for a non-competition clause?
- solution can be found in a supplementary interpretation which is based on sector standards
- no supplementary interpretation possible if parties did not provide for a clause in their contract by mutual intent
- supplementary interpretation vs. default provisions in the law?
- supplementary interpretation as a gap-filling instrument when a clause in the contract was found to be invalid due to a violation of mandatory law? (see especially in consumer law)

I. Interpretation in general

- step 2: avoidance of the contract due to error or misrepresentation
  - If, after the (simple) interpretation of the contract, a significent mismatch between the intention of one party and the result of the interpretation remains,
  - the contract might be avoided due to error
- again: conflict between protection of private autonomy and protection of trust
  - liberal solution in German law (§§119 ff BGB): contract may be avoided due to any kind of error (except for error in motivation), if the person subject to the mistake, compensates the other one for damages suffered from having relied on the validity of the contract
  - strict solution in Austrian law (§ 871 ABGB): avoidance of the contract only if other party should not have relied on the validity of the contract due to specific reasons (e.g. caused the error or should have noticed it)

I. Interpretation in general

– Swiss law (Art 24 OR): avoidance of the contract only in specific cases of error

II. Founding acts of business corporations

- Founding acts of business corporations (statutes) are legal acts
- subject to interpretation
- no specific methods of interpretation provided by law
- methods of interpretation of declaration of will (contracts) should be applied
- differences between a contractual relationship and statutes of a corporation should be noticed:
  - contracts are concluded between two parties (in general)
  - founding acts of corporations may be entered into by an unrestricted number of parties (or perhaps by just one person)

II. Founding acts of business corporations

  - in a contractual relationship the parties remain the same between the conclusion of the contract and its termination (in general)
  - shareholders of a corporation may change frequently
- controversial discussions on the interpretation of founding acts of corporations
- courts make a difference
  - between partnership agreements (Společnost, Veřejná obchodní společnost, Komanditní společnost) and
  - founding documents of corporations (Akciová společnost, Společnost s ručením omezeným)

II. Founding acts of business corporations

- Courts hold that
  - subjective interpretation (based on the actual intention of the partners) has to applied on partnership agreements
  - objective interpretation (based on the wording and the system of the documents) has to be applied on the founding acts of business corporations (with some exceptions)
    Austrian Supreme Court even refers to the methods of interpretation of the law (§§ 6, 7 ABGB)
- partnership agreement is considered to be contract between the partners
- Founding act of a corporation is considered to be the constitutional basis of an independent legal entity

II. Founding acts of business corporations

- should we make a difference in the methods of interpretation depending on the legal form of the company?
- we should not do so because partnership agreement are the legal basis of an independent organisation regardless the lack of legal personality
- subjective interpretation, based on the intention of the partners or shareholders of the initial partnership agreement or the founding act of the corporation, should be the starting point of any interpretation

II. Founding acts of business corporations

- however, two major restrictions have to be taken into consideration
- Founding acts of a corporation may require some formal requirement (e.g. notarial certification)
  - the purpose of the formal requirement may preclude the consideration of circumstances outside the contract document
- when partners or shareholders have changed trust of the new partners or shareholders has to be protected
  - shift towards a more objective interpretation

II. Founding acts of business corporations

- Conclusions:
  - subjective interpretation based on the intention of the partners or shareholders of the initial partnership agreement or the founding act of the corporation, provided that
  - purpose of formal requirement does not stand against
  - no new shareholders acquired share or joined the company
  - relevant especially for family businesses
- Shareholder agreements, if concluded by all partners or shareholders, can be an instrument of interpretation

II. Founding acts of business corporations

- Case 1 (RGZ 140, 303)
  - German GmbH (s.r.o.):
  - The foundation act provides a right to terminate the corporation to each shareholder
  - but only after 15 years
  - dispute among shareholders if year has to be understood as business year (hospodářský rok, starting from July, 1th) or calender year (Kalendářní rok).
  - Decision of the court: since there has been no change of shareholders, interpretation has to be based on the intention of the shareholders at the time of the founding act

II. Founding acts of business corporations

- Case 2 (Austrian Supreme Court, 6 Ob 202/10i)
  - Austrian GmbH
  - According to the statutes, voting rights of 25 % should be transferred from one shareholder to his successor at a date given
  - dispute among shareholders about the interpretation of this clause
  - Decision of the Court: actual intention of the shareholders is not relevant even if there has been no change of shareholders

II. Founding acts of business corporations

- Case 3 (based on U. Torggler)
  - Joint stock company listed on stock exchange
  - in the statutes it is laid down that investments above 1 million Euro require approval by the supervisory board
  - dispute on whether 1 million Euro is to be understood including or excluding VAT (Daň z přidané hodnoty)
  - third party (e.g. someone acquring shares at stock exchange) would understand 1 million excluding VAT because VAT is deductable and does not affect the corporation
  - objective interpretation prevails even if the intention of the founders would have been different

III. Foundation deeds and wills

- Foundation deeds and wills have two things in common
  - unilateral act (in general): there is no contractual partner whose trust must be protected
  - addressees (beneficiaries, heirs, legatees) get something for free
- consequence:
  - protection of private autonomy of the founder/testator plays a more important role than in contract law or law of corporations
  - interpretation is based on the „theory of will“
  - the true intention of the founder/testator is decisive for the interpretation of the foundation deed/will

III. Foundation deeds and wills

- however: intention of the founder/testator can only be taken into consideration insofar as it has been indicated in the document
- reason: formal requirements exist for both foundation deeds and for wills
- purpose: legal clarity, preservation of evidence on the intention of the founder/testator
  - purpose would be thwarted if an intention of the founder/testator could be considered which has not even been indicated in the foundation deed/will
  - so called „theory of indication“ (Andeutungstheorie)

III. Foundation deeds and wills

- see § 553 ABGB: „ Words shall be interpreted according to their ordinary meaning, unless the deceased associated a special meaning with certain expressions. The true intention of the deceased, which must be at least implied in the wording of the disposition, is decisive.”

- theory of indication does not preclude supplementary interpretation
  - relevance of *falsa demonstratio*?
- See Court of Appeals Munich (33 U 1473/21):
  - testator wishes his “existing cash” (vorhandenes Bargeld) to be divided among 19 persons
  - does this include money at a bank account?

III. Foundation deeds and wills

- decision of the court: Cash (Bargeld) in general does not include bank accounts
- testator was an experienced businesswoman
- if her intention had been to extend the legacy to bank accounts she would have used another word (e.g. money)
- would the court have come to a different decision if there had been only very little cash (just a symbolic amount if distributed among 19 people)?

– See Austrian Supreme Court (7 Ob 136/18b)

- will of the testator: “As heirs of all my movable and immovable property I appoint A and B”
- can this provision be understood in a way that A and B should also be designated as beneficiaries of a life insurance (which is not part of the estate in a technical sense: insurance contract as contract in favor of third party)
- decision of Supreme Court: based on the intention of the testator, according to the finding of the court of first instance, the heirs should also be beneficiaries of the life insurance