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Real Estate - Austria

Court reverses case law on directors' liability in M&A deals involving property

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Introduction

Under Section 12a of the Tenancy Act, if the shares in a company that rents property are sold, the landlord has the right to increase the rent to market level. The managing directors of the company must inform the landlord of the change in ownership. Failure to do so leads to the directors being held personally liable with regard to the landlord.

Under previous case law, directors were liable only for rent payments that could not be recovered from the renting company directly. However, a recent Supreme Court judgment called this rule into question.

Facts

The case concerned a company that rented premises for business purposes. In October 2000 99% of the company's shares were sold and transferred to a third-party buyer. The defendant was the managing director of the company at that time. The defendant failed to inform the landlord of the transfer.

The plaintiff landlord became aware of the change of control in April 2012. The plaintiff raised the rent to market level and filed a claim for damages against the managing director, requesting payment of the difference between the actual rent paid and the market value rent between October 2000 and April 2012, plus interest.

The defendant refused payment, arguing that she was liable for payment only if and to the extent that the plaintiff was unable to recover the increased rent and interest from the tenant. The plaintiff failed to establish that the tenant lacked sufficient funds to pay the damage.

Decision

The Supreme Court found in favour of the plaintiff, confirming that the managing director had a duty to disclose the structural changes and was personally liable for breaching this duty.

In contrast to previous case law (for further details please see "Court intensifies directors' personal liability in M&A deals involving property"), the Supreme Court ruled that the managing director was liable irrespective of whether the lessee itself was able to pay the outstanding debts.

The case was remitted to the court of first instance. The judgment is not final.

Comment

Under previous case law, the managing director's liability was limited to cases where claims against the renting company were time barred or where the renting company was insolvent or had ceased to exist.

The new case law adds an additional burden on managing directors. Landlords can now pursue claims against the company, directors or both. Thus, in some cases, the question of whether a change of control has occurred is raised only once proceedings against the managing director have begun; as such, it is often difficult to determine whether a change in control has occurred (for further details please see

"Supreme Court confirms change of control theory for rent increases"). Further, the managing director – who may no longer work for the company when the suit is filed – is typically at a disadvantage when it comes to challenging a claim, as he or she may not have access to the relevant documents proving that no change of control had occurred. The managing director will typically request the renting company to join the proceedings as an intervenor in his or her support. However, this will be difficult in cases where the company is a foreign entity.

As the Supreme Court held that the company and managing director were jointly and severally liable, there is a question over which party will have to bear the costs. In other words, to what extent can the managing director recover from the company any payments made by him or her to the landlord or vice versa?

The obligation to notify landlords is an ongoing obligation. Managing directors are also liable for failing to notify the landlord even if the change of control occurred before their appointment.

For further information on this topic please contact Martin Foerster at Graf & Pitkowitz by telephone (+43 1 401 17 0) or email (foerster@gpp.at). The Graf & Pitkowitz website can be accessed at www.gpp.at.

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