Introduction

Abstract

In the following first chapter, we will provide an introduction to the legal and economic environment to be aware of when considering doing business in Germany. Beginning with a short summary of the economic framework conditions of the German market, we will explain some basic features of the German legal system, including the structure of the legislative and judicial system, and will describe some of the most important legal frameworks. Thereupon, we will outline some of the key aspects of German business law to be considered when deciding upon establishing a business enterprise in Germany. We will continue our presentation by introducing the main options for foreign entrepreneurs to this purpose, by outlining the requirements for establishing a branch office for an existing foreign company as well as by a brief presentation of the most important non-corporate and hybrid forms of German business organizations available. Finally, we will provide a brief introduction into the German legal framework governing insolvency and restructuring of companies as a matter of utmost practical importance for any business operation.

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1.1 Conducting Business in Germany

1.1.1 Case Study

**Case Study**

A-Corporation (A) is incorporated in the state of Delaware, USA, with its headquarters in Wilmington. A manufactures components for automobile brakes. A conducts business throughout the US and is considering a future expansion of its business into Europe. John B. (B), the CEO of A, is interested in Germany in particular. He has visited the International Automobile Fair in Frankfurt/M. and has gained the impression that Germany would be well suited for the sale and distribution of A’s products. B was especially impressed by the number of visitors to the Frankfurt Fair interested in automobiles. Seeing them as potential buyers (of cars and their components, such as A’s products), B calls Peter C. (C), head of A’s legal department, to ask him to prepare a memorandum on the framework for doing business in Germany.

B asks C to address the following issues and questions:

- Elaborate on the general economic background and business climate in Germany.
- What advantages does Germany have to offer to a foreign investor?
- What are the key features of German business law?

1.1.2 Economic Background

Germany is one of the world’s leading industrial nations and, e.g. in terms of total economic output, Germany is also one of the leading economies within Europe. In 2009, Germany exported goods amounting to EUR 803.2 billion and imported goods amounting to EUR 667.1 billion. Germany has a highly developed free market system; its economy is closely linked to the other Member States in the European Union. Trademarks of Germany’s economic system are its highly developed infrastructure, its qualified workforce and its international, export-oriented focus.

Many German companies generate a great deal of their profits through exports and many jobs are dependent on foreign trade. From 2003 until 2008, Germany was the world export champion (‘Exportweltmeister’) since no other country exported more goods to other countries during this time period.\(^1\) In 2009, China surpassed

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\(^1\) Source: German Federal Statistical Office (Statistisches Bundesamt), Export, Import, Globalisierung, 2010, p. 37.
Germany, however, Germany was second, still ahead of the US. Also, with regard to the import of goods, Germany remains one of the leading countries worldwide; in 2009 only the US and China imported goods with a higher aggregate value.\(^2\) For this reason, Germany has traditionally been attractive to foreign investors looking for business opportunities in Germany. Germany’s most important trading partners are EU Member States like France and the Netherlands.\(^3\) Almost three out of four goods ‘Made in Germany’ are delivered to European countries. In 2009, 63% of goods were delivered to EU Member States. However, in 2009 the second important market for German products was Asia with a share of about 14%, ahead of the US market with a share of about 10% (Figs. 1.1 and 1.2).

In an advanced economy such as that of Germany, business organizations are important economic and social institutions. The success of these business organizations obviously depends on the legal framework surrounding them. Since Germany is a member of the European Union, cross-border commercial activities in the European market and the resulting legal issues become more and more important for investors in the German market.

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\(^3\) Source: German Federal Statistical Office (Statistisches Bundesamt), Wiesbaden 2010.
1.1.3 Core Features of the German Legal System

As its name suggests, the Federal Republic of Germany is organized as a federal system consisting of 16 federal states (Bundesländer), each of which is responsible for the government of its own state, including law-making powers in many areas, provided that they are not preempted by Federal law.

Furthermore, Germany is a Member State of the European Union (EU). This is the association of a large number of European states and, as such, the impact of European law on many areas of national law has become more and more important. This is particularly true for those areas of EU law which are either directly or indirectly applicable, such as EU Regulations or the Directives. It is also true for the case law of the European Court of Justice (ECJ) which often plays a decisive role in legal disputes when the national courts of EU Member States have to interpret the scope of applicability of the Union Treaties.

1.1.3.1 Hierarchy of Norms and Constitutional Framework

In Germany, the highest written national norm is the Federal Constitution. The Constitution or so-called ‘Basic Law’ (Grundgesetz, GG), which was promulgated by the Parliamentary Council on 23 May 1949, defines and regulates the political and legal system of the Federal Republic of Germany (Fig. 1.3).

Germany is a republic and a democracy; it is a federal state based on the rule of law and social justice. The Grundgesetz contains a catalogue of fundamental rights and values to be protected against any form of infringement, such as the dignity of man, freedom of religious belief, freedom of speech, freedom of arts and sciences, freedom of assembly, freedom of association, the right to freely choose one’s profession, the principle of equality before the law and a constitutional guarantee...
of private property. These fundamental rights are binding as to legislation, judicial decisions and the executive branch as law with immediate effect. Depending on the nature of the fundamental rights, they are not only applicable to individuals but also to legal persons such as corporations.

The Grundgesetz also includes the law on voting rights, citizenship, political parties and the regulation of the functioning of the various organs of state such as the Federal Parliament (Bundestag) and the Federal Council (Bundesrat), the Federal President (Bundespräsident), the Federal Government (Bundesregierung) and the Federal Chancellor (Bundeskanzler). However, the Grundgesetz does not prescribe any specific form of economic order (such as a free market economy) but is considered neutral from an economic policy perspective.

The fundamental rights and values codified in the Grundgesetz are primarily designed as providing protection for the individual against any infringement of her/his guarantees by the government, regardless whether such infringement results from a legislative act, any form of executive power or from the judiciary. However, the Grundgesetz may also have an impact on the legal relationships between private individuals or business entities. This so-called third party effect (Drittwirkung) was developed by the Bundesverfassungsgericht (Federal Constitutional Court) in the famous Lüth-decision of 1958.4 Dealing with the question whether a civil law injunction based on Sec. 826 of the German Civil Code (Bürgerliches Gesetzbuch, BGB) violated the complainant’s fundamental right of free speech under Art. 5 of the Grundgesetz, the court held that the civil courts should interpret the provisions of the BGB in the light of the Grundgesetz, since the Constitution represents an objective set of values always to be taken into account when deciding legal issues. Based on this concept of third party effect of fundamental constitutional rights, the

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4 BVerfGE 7,198, 15 January 1958, 1 BvR 400/51—Lüth.
Bundesverfassungsgericht, as the guardian of the Constitution, has invalidated various legal provisions on the grounds that they were incompatible with the Constitution (e.g. with respect to discrimination against gender, age etc). More generally, the Constitution always plays an important role when statutes need to be interpreted. If a statutory provision is amenable to several different interpretations, then the interpretation which would make the law compatible with the Constitution is always to be preferred. Constitutional law has, therefore, traditionally played an important role in civil law and business law.

Next in rank from the Constitution is statutory law in the form of statutes passed by the Federal parliament (Gesetz im formellen Sinne). Thereafter come ordinances passed by the Federal government (Bundesrechtliche Verordungen und Satzungen). Although they are not a product of the parliamentary process but passed by administrative authorities, these ordinances are abstract rules which are generally applicable to many cases. Therefore, they are regarded as statutes in a material sense (Gesetz im materiellen Sinne). Due to Germany’s structure as a federal republic, consisting of 16 federal states (Bundesländer), the same hierarchy of norms can be found at each state level, starting with the respective state constitution and followed by statutes (Gesetze der Länder) and ordinances (Landesrechtliche Verordungen und Satzungen) of the respective state. As a general rule, federal law always takes precedence over state law (see Art. 31 GG). This means that if the law of a particular German state collides with a law made by the Federal Government, then the federal law will prevail. Subordinate legislation at federal level will take precedence even over the constitution of a state, insofar as the Federation has the competence to pass a law on the matter in question.

1.1.3.2  Predominance of Federal Law
As indicated, and similar to the US, Germany has a federal system with the law-making powers divided between the federal government (Bund) and the individual German states (Länder). However, (unlike the US) in most areas of civil, commercial and business law, the law-making power lies with the federal government. As Germany belongs to the family of so-called civil law systems, the legal landscape has traditionally been dominated by comprehensive codes and statutes promulgated by the legislature in all major areas of the law. Most areas of civil, commercial and business law are, therefore, covered by federal statutes issued by Germany’s Federal Parliament. As one obvious advantage of such predominance of federal law, market participants will find a uniform legal framework for business throughout Germany (in contrast to the diverse legal landscape e.g., in the US). We will, therefore, look at the relevant statutory regulations and also discuss the question whether, in some cases, the statutory regime for a specific company form has been altered by the courts with judge-made rules or may be altered by the shareholders by contractual provisions.

1.1.3.3  Distinction Between Public and Private Law
Derived from its historical origins in Roman law, the German legal system still remains characterized by the distinction between private and public law, both areas
of law covering different legal issues and being dealt with by courts with different jurisdictions. Public law is usually defined as the embodiment of those rules conferring powers and imposing obligations exclusively on holders of public office. This means in particular the federal government, the German federal states and supranational organizations such as the European Union. On the other hand, private law is directed at all legal subjects (Fig. 1.4).

**Public Law**

Public law covers areas such as constitutional law, administrative law, tax law and social security law. Public law also includes the general principles of administrative law, as well as its various specialized fields, such as police law, the law of communal administration, public construction law and the law relating to foreigners and asylum. Data protection law, public service law, media law, traffic law, environmental law, the law of taxation and procedural law are also included. Furthermore, criminal law is also considered as a part of public law, since only the state has the authority to inflict punishment.

**Private Law—General and Specific Regulation**

Private law generally governs one’s private legal affairs such as entering into contracts, acquiring and transferring property, receiving compensation for injuries, or establishing a business. German private law is regulated in numerous individual statutes dealing with general issues of private law such as contracts, property or...
compensation for damages and specific issues of private law like intellectual property, labor law or the law of business associations.

The most important statutory regulation in the area of private law is the German Civil Code (*Bürgerliches Gesetzbuch, BGB*) comprising more than 2,300 sections and covering, among others, the law of contracts, the law of torts, property law, family law and the law of succession. In Germany (as in many other jurisdictions), private law is based on the fundamental assumption of private autonomy, i.e., the idea that legal subjects should, in principle, be free to arrange their private legal affairs and the law should provide institutions like contract, ownership and business forms to facilitate this freedom. However, the history of private law is also a history of defining the limits of such freedom in order to protect certain interest groups which (in the eyes of the courts and the legislature seem to) need specific legal protection, e.g. consumers, employees or creditors.

**German Civil Code (BGB)**

The German Civil Code came into force on 1 January 1900 and can be seen as a result of the unification process and of the codification movement of the 1900s. The codification movement originated in the age of enlightenment and also produced other famous European codifications of Civil Law, such as the French Civil Code of 1804 (the so-called ‘*Code Napoleón*’) or the Austrian General Civil Code (*Allgemeines Bürgerliches Gesetzbuch*) of 1811.

From the time of its enactment until today, the BGB has been amended numerous times in order to adapt the legal framework to the ever-changing political, social and economic environment. Typical amendments are the introduction of specific regulations protecting certain interest groups like consumers, employees and tenants. With ongoing European integration, further changes have become necessary to implement rules under mandatory European law, including a particularly important reform in 2002 (the Act on the Modernization of the Law of Obligations, *Schuldenrechtmodernisierungsgesetz*). However, in many respects the BGB still reflects some of its historical legal concepts, in particular, some classic ideas of ‘*laissez faire*’—liberalism, such as the notions of private autonomy and freedom of contract. Although private autonomy and freedom of contract are still regarded as the cornerstones of German private law, the original ideas of the authors of the BGB based on the rather idealistic (and somewhat artificial) concept of a contract formed by two legal subjects with equal bargaining power freely negotiating the terms of their agreement with each other. This concept had been subject to criticism even at the time of its origin, as it completely ignores social realities, and, in particular, the widespread inequality of bargaining powers between contracting parties, such as employees and employers, tenants and landlords or consumers and manufacturers. Thus, the history of the German Civil Code can be seen as a history of expanding protection of the ‘weaker party’ and, as of today, the BGB reflects an interesting amalgam of different—and in part conflicting—value sets and concepts.

Among other things, the BGB regulates general issues of contract law, as well as specific types of contracts, such as purchase, lease, service, manufacturing, surety-
ship, civil law partnership, negotiable instruments, transfer of title and real property and damages or claims for restitution in cases of unjust enrichment.

As it has been often criticized for its rather sophisticated and technical language, the BGB does offer the advantage of having quite a clear and systematic structure. The BGB consists of five books and begins with a book of general provisions (Allgemeiner Teil). This deals with fundamental concepts and issues of private law, such as the definition of general legal capacity, the definition of legal subjects and objects, the specific requirements for legal transactions (in particular for contracts), the law of agency (Stellvertretung) and provisions relating to limitation periods (Verjährung). These fundamental definitions and concepts apply to all the following sections of the BGB. The second book covers the law of obligations (Schuldsrecht) and is subdivided into a general and a specific part. The general part contains rules on the performance of contracts, remedies for non-performance, rules on the transfer of rights and duties and rules on transactions involving several creditors or debtors. The specific part deals with certain specific types of contracts, such as purchase agreements (Kaufvertrag), leasehold contracts (Mietvertrag), contracts for services and for specific services (Dienst- und Werkvertrag) and loan agreements (Darlehensvertrag). The specific part also includes rules on the compensation for delicts for unjust enrichment. The third book of the BGB deals with the law of property (Sachenrecht) comprising the legal relationships between persons and things, e.g. the right of ownership, titles of possession and other rights in rem, such as mortgages. The fourth book contains family law and deals with the law of engagement, marriage, divorce and the law of custody of children, and the fifth book contains the law of succession (Erbrecht).

The German Civil Code distinguishes between consumers (Verbraucher), meaning any natural person who enters into legal transactions for a purpose outside her/ his trade or profession, and entrepreneurs (Unternehmer), defined as a natural or juristic person or a partnership with legal personality who or which acts in exercise of her, his or its trade when entering into a legal transaction. Consumers are often protected by specific legal provisions, e.g. with regard to specific information rights or specific rights to withdraw from contractual obligations. One prominent example is the law on standard terms of contract (Allgemeine Geschäftsbedingungen or AGB). Such AGB are of considerable practical significance, as numerous businesses associations use these standardized legal tools when dealing with their customers. In order to address the risks associated with using standard terms for the contract party being subjected to them (i.e. unfair surprise by disadvantageous contract terms), German law provides for specific requirements regarding the inclusion of AGB into a contract, as well as several control mechanisms regarding their content. In principle, the provisions on standard terms apply to consumers and entrepreneurs alike. However, the level of protection provided for consumers and entrepreneurs varies considerably, since entrepreneurs and business associations are considered to have

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5 See Sec. 13 BGB.
6 See Sec. 14 BGB.
7 Or, as they are also-called, general terms of business/conditions of business.
sufficient legal knowledge to negotiate effectively and enter into agreements, i.e. they do not require the same level of protection as consumers. Therefore, only specific provisions of the law on AGB will apply to them, for example, the invalidation of terms which unreasonably discriminate against the contractual partner contrary to the requirements of good faith and fair dealing (Sec. 307 BGB).

German Commercial Code (HGB)

With regard to other important areas of private law, such as commercial law, the German Commercial Code (Handelsgesetzbuch, HGB) contains specific rules for so-called ‘merchants’ (Kaufleute), i.e. anyone who carries out a commercial activity (as defined by Sec. 1 HGB) regardless of the field of commercial activity (e.g. production, trade, services) and for commercial transactions related to them.\(^8\) The HGB contains special rules providing for the specific needs of commercial life.\(^9\) For example, a different treatment of commercial transactions is justified, since businesspeople often expect and rely on speedy transactions.

In addition, since merchants are expected to have some basic commercial and legal understanding for business operations (in contrast to consumers), they supposedly do not require the same extent of legal protection as ordinary citizens. The HGB, therefore, contains various deviations from the general rules of the German Civil Code, e.g. regarding the level of the duty of care owed by merchants or the requirements for binding contracts with regard to form. The Commercial Code is limited to the buying and selling of goods, but also comprises other areas of business life, such as transport, banking and insurance industries, manufacturing and craftsmanship.

Sources of Corporate Law

Unlike other European jurisdictions, such as e.g. the UK, Germany has no single act or codification regulating all companies and business associations, but has several statutes for various types of business associations (with or without corporate form).

The statutes most relevant to business organizations without corporate form in Germany (such as the civil law partnership or the commercial partnership) are the German Civil Code and the Commercial Code. Apart from the legal areas already mentioned above, the German Civil Code also regulates so-called civil law partnerships (BGB-Gesellschaft or GbR). The HGB includes rules for specific business forms, such as the general commercial partnership (offene Handelsgesellschaft or oHG), the limited commercial partnership (Kommanditgesellschaft or KG) and the silent partnership (Stille Gesellschaft).

\(^8\) An exception is made for private practitioners as defined under Sec. 18 German Income Tax Act (Einkommenssteuergesetz, EStG), to whom the Commercial Code is not applicable, regardless of the size and success of their enterprise, e.g. attorneys-at-law, architects or medical doctors.

\(^9\) The legal distinction between merchants and non-merchants as set forth in the HGB is not identical to the legal distinction between entrepreneurs and consumers within the meaning of the BGB; while a merchant will nearly always also be considered as an entrepreneur under the BGB, such entrepreneur may—due to the size or nature of her/his business—well not qualify as a merchant according to Secs. 1 et seq. HGB.
Corporations, on the other hand, are regulated in specific statutes. The Stock Corporation Act (Aktiengesetz or AktG) governs the German stock corporation (Aktiengesellschaft or AG), as well as the commercial partnership limited by shares (Kommanditgesellschaft auf Aktien or KGaA), the latter being a stock corporation with fully liable general partners. In addition, the Stock Corporation Act regulates affiliated companies and determines the level of liability among parent companies and their subsidiaries.

The Limited Liability Company Act (GmbH-Gesetz or GmbHG) sets out the rules for the German Limited Liability Company (Gesellschaft mit beschränkter Haftung or GmbH), which is the most popular German corporate form, especially for small and medium-sized businesses.

Moreover, the Transformation Act (Umwandlungsgesetz or UmwG), set into force in 1994, sets out provisions for reorganizations of legal entities, namely by way of mergers (Verschmelzungen), divisions (Spaltungen), comprehensive transfer of assets (Vermögensübernahmen)\(^\text{10}\) and changes of corporate form (Formwechseln).

Negotiable Instruments

In addition to the BGB and the HGB and some other important statutes in the area of company law (which will later be discussed in more detail), there are several other statutes which are relevant for conducting business, some of which should be briefly mentioned. One such area is the law governing negotiable instruments.

The legal rules regarding negotiable instruments and securities (Wertpapierrecht) are contained in various statutes, including the German Civil Code, Commercial Code, the Bills of Exchange Act (Wechselgesetz), the Checks Act (Scheckgesetz), the Stock Corporation Act (Aktiengesetz), and the Securities Deposit Act (Depotgesetz).

Competition and Antitrust Law

Competition law is governed by the Unfair Competition Act (Gesetz gegen den unlauteren Wettbewerb) and deals with various forms of competition which are considered to be unfair. This regulation aims to protect a functioning market economy. It also intends to protect individuals and business associations against unfair practices by competitors and to protect consumers against the risk of being misled and overcharged. Any person whose trade practice is classified as unfair competition (unlautere Wettbewerbshandlung) can be prevented from doing so by way of injunction and may also be liable for damages. Antitrust law (Kartellrecht) is also directed primarily at the protection of a functioning market economy; its main goal is the prevention of cartels and unfair restrictions of competition. In Germany, it is regulated in the Act against Restrictive Trade Practices (Gesetz gegen Wettbewerbsbeschränkungen) together with provisions of European Union law governing cartels and mergers.

\(^{10}\) The rules on restructuring by way of a ‘comprehensive transfer of assets’ as defined in the act are intended to provide specific rules for privatizations of state industries. In other areas of practice they are of little relevance.
Intellectual Property Law

The law on intellectual property is regulated in different statutes. Patent law, which provides special protection for technical inventions, is regulated in the Patent Act (Patentgesetz). A patent secures a right for its owners to be protected against the exploitation of the invention by other persons. The patent lasts for twenty years in Germany and requires the payment of fees. There are numerous international treaties which attempt to extend the protection of patents beyond national boundaries. To obtain Europe-wide protection for a patent, an application must be made to the European Patent Office in Munich.

If an invention does not qualify for a patent, its owner can obtain a lesser degree of protection by registering the invention as a so-called utility model (Gebrauchs muster). After a utility model has been registered, only the owner may produce it for commercial purposes and put it into circulation, use it or market it. Industrial designs and models (gewerbliche Muster und Modelle) are protected by the Design Act (Geschmacksmustergesetz) if they are new and original.

Another very important statute dealing with intellectual property is the German Act on the Protection of Trademarks (Markengesetz). A trademark is a symbol of distinction that identifies the particular products of a trader to the general public. A trader may register a trademark at the Deutsche Patentamt in Munich. She/he then enjoys the exclusive right to use the trademark in connection with the goods for which it was registered.

Finally, German copyright law is contained in the German Copyright Act (Urheberrechtsgesetz or UrhG). Traditionally, German copyright law puts a special emphasis on the relationship between a work and its author, regarding a work eligible of legal protection if it constitutes a personal intellectual creation (persönliche geistige Schöpfung). This has several consequences: First, in contrast to patent law, legal protection under the UrhG does not require a registration but applies automatically (ipso iure) to such works that meet these requirements. Second, German courts have set out considerably different standards for works of fine arts on the one hand and works of applied arts on the other. According to the so-called doctrine of ‘kleine Münze’ (‘small coin’), a work of fine art may be considered eligible of copyright protection even though it only shows a minimum of creativity, originality and individuality, while the threshold for applied arts is considerably higher. Third, from this point of view, there is neither a ‘corporate copyright’ nor a complete transfer of the author’s legal position. Although it is possible to license some or even all rights of use of a work to third parties, the author retains certain inalienable rights, especially morale rights (Urheberpersönlichkeitsrechte).

Labor Law

Another important area of private law is labor law. There is no uniform German labor act, but rather, labor law is governed by numerous different statutes. One characteristic feature of German labor law is the fact that broad areas are not regulated by statutes at all. Therefore, court decisions and judge-made law play a prominent role. In contrast to other legal regimes, German labor law is characterized by its scope of protection for employees (Schutzprinzip) as one of its guiding principles.
Despite of being a part of private law, German labor law also contains some elements of public law (e.g. regulation regarding safety measures in the workplace and maximum hours of work). German labor law is usually subdivided in the so-called individual labor law (\textit{Individualarbeitsrecht}), which deals with the relationship between employer and employees, and the law of industrial relations (\textit{Kollektivarbeitsrecht}). The law on industrial relations regulates unions and employers’ associations as specific types of association relevant in the employment sphere. \textit{Kollektivarbeitsrecht} also includes the law on industrial disputes (\textit{Arbeitskampfrecht}), on collective agreements between the various associations, i.e. agreements arising from industry-wide collective bargaining (\textit{Tarifverträge}) and on employee’s rights of representation (\textit{Betriebsverfassungsrecht}) as codified in the Employees’ Representation Act (\textit{Betriebsverfassungsgesetz}) and the Co-Determination in Industry Act (\textit{Mitbestimmungsgesetz}).\footnote{For more detail on the German system of employee participation see \textit{infra}, Sect. 2.5.}

\textbf{Relevance of Conflict of Laws}

Given the increasing importance of EU law and the growing globalization of economic relations, the question of which law applies to a commercial relationship or dispute becomes more and more decisive. Growing international relations, competition and increasing market globalization often raise the question of the applicable law. Differences among the legal systems and the fact that a unification, harmonization or assimilation of law (\textit{Rechtsvereinheitlichung}) often remains quite incomplete within the EU result in the decision on the applicable law in cross-border cases to a specific legal system to be decisive.

The question of the applicable law is answered by the rules of ‘conflict of laws’. These rules determine which national legal regime is to be applied in cases with multi-jurisdictional elements. However, the name ‘\textit{Internationales Privatrecht}’, (private international law), as this area of the law is referred to in Germany, may appear something of a paradox, since it is, to a great extent, neither private (it also covers various areas of public law), nor is it truly international. On the contrary, conflict of law rules are often not internationally harmonized, but instead are a constituent part of national law.

\textbf{Legal Sources}

German conflict-of-laws rules are embodied in various legal sources, including codified norms, as well as judicial decisions, national statutes and supra-national legislation, multilateral conventions and bilateral treaties.

In Germany, the traditional and most comprehensive set of rules regarding conflict-of-laws is provided for in Art. 3–46 of the Introductory Act to the German Civil Code (\textit{Einführungsgesetz zum Bürgerlichen Gesetzbuch, EGBGB}). Apart from some general provisions on determining the applicable law in cross-border cases (Art. 3–6 EGBGB), the EGBGB also contains conflict-of-laws principles regarding the rights of natural persons (e.g. legal capacity), the name, the form of legal transactions (Art. 7–12 EGBGB), as well as conflict-of-laws principles regarding family
law matters (e.g. marriage and matrimonial property issues, divorce, descent and adoption, see Art. 13–24 EGBGB), conflict-of-laws principles regarding succession (Art. 25–26 EGBGB) and non-contractual obligations (such as compensation for unjust enrichment and torts, see Art. 38–42 EGBGB) and finally, conflict-of-laws principles regarding matters of property (Art. 43–46 EGBGB).

Conflict-of-laws issues play a decisive role in cross-border contractual transactions. E.g., pursuant to Art. 3 para. 1 of the Council Regulation on the Law Applicable to Contractual Obligations (Rome I-Regulation) a contract is governed by the law chosen by the parties. The choice of law must be expressed or implied with sufficient certainty by the provisions of the contract or the circumstances of the case. The parties may make the choice of law for the entire contract or for a part thereof. Thus, with the exception of some consumer and employment contracts, German conflict-of-laws generally endorses the principle of free choice of law for contractual relationships. As one can easily imagine, this option can be crucial for such issues as the scope of liabilities, damages, warranty periods etc., which are typical parts of most contractual relationships.

The legal framework for cross-border transactions has been subject to considerable harmonization efforts on the European level. The most important European legal instruments are the Council Regulation on Jurisdiction and the Recognition and Enforcement of Judgments in Civil and Commercial Matters (Brussels I-Regulation), the Council Regulation on the Law Applicable to Contractual Obligations, the Council Regulation on the Law Applicable to Non-Contractual Obligations (Rome II-Regulation) and the Council Regulation on Insolvency Proceedings (Insolvency-Regulation). As, pursuant to Art. 288 of the Treaty on the Functioning of the European Union (TFEU), EU Council Regulations shall have general application in all EU Member States (i.e. not requiring to be transposed into national laws by means of implementing measures), the above-mentioned legal instruments shall take priority over any national provision on the same subject matter.

Conflict-of-laws rules may originate in international treaties and conventions, a prominent example is the Treaty of Friendship, Commerce and Navigation between Germany and the US, which governs a broad range of cross-border issues including the mutual recognition of lawfully incorporated companies. An example for a multilateral convention is the Vienna Convention on Contracts for the Interna-

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17 Treaty of Friendship, Commerce and Navigation between the Federal Republic of Germany and the United States of America (Freundschafts-, Handels- und Schifffahrtsvertrag zwischen der Bundesrepublik Deutschland und den Vereinigten Staaten von Amerika) as of 29 October 1954.
tional Sale of Goods of 1980 (CISG)\textsuperscript{18}, which entered into force in Germany on 1 January 1991. Depending on its scope of applicability, the CISG may automatically govern a cross-border sales contract if it has not been excluded by the parties to the contract.

Finally, even though Germany is a civil law country strongly relying on codified rules, conflict-of-laws principles have sometimes been developed solely in case law. One important example of judge-made rules of conflict of laws is the area of international company law, which will be discussed later on in detail.\textsuperscript{19}

**General Principles**

In conflict-of-laws rules, the so-called connecting factors (\textit{Anknüpfungspunkte}) such as nationality, domicile, location of property, statutory or real seat of a company, intention of the parties or place of tort (\textit{Deliktsort}) serve to establish a connection (\textit{Anknüpfung}) between specific elements of a cross-border case and the legal rules of a national legal system. As a result of this connection, conflict-of-laws provisions determine the international scope of applicability of a specific rule, i.e. the extra-territorial scope of the substantive law.

If the law of a foreign state is applicable according to German conflict-of-laws rules, the applicability of foreign law generally refers to all aspects of a particular dispute, including the foreign state’s conflict-of-laws rules. This principle is called ‘global remission’ (\textit{Gesamtverweisung}). However, if the foreign conflict-of-laws rules provide substantive rules for the subject matter different from those of German law, the foreign law may remit the dispute for decision according to German law (\textit{Rückverweisung}) or it may refer the dispute to the law of a third state (\textit{Weiterverweisung}). Such a situation, a so-called ‘renvoi’, may, subject to the relevant conflict-of-laws rules concerned, either affect the case as a whole, or only certain aspects of it (\textit{gespaltene Rück- oder Weiterverweisung}).\textsuperscript{20} According to Art. 4 para. 1 EGBGB the German courts are required to recognize a renvoi.

Conflict-of-laws is based on the idea that a case should be decided on the merits of the law with the closest connection to the case and, therefore, rests on the assumption of the equality of legal systems around the world. In contrast to this ideal, German law (as almost all other legal systems) provides for a so-called public policy exception as a safeguard against foreign law: if the law of a foreign state (which is applicable according to German conflict-of-laws rules) violates German public policy (\textit{ordre public}), the foreign law either shall not be applied, it shall be applied


\textsuperscript{19} See infra, Sect. 5.1.

\textsuperscript{20} For example, pursuant to Art. 25 EGBGB the law of succession is governed by the law of the country of which the deceased was a \textit{national} at the time of her/his death, regardless of what kind of property may be part of the descendant’s estate. In contrast, the conflict-of-laws rules of France and most US states distinguish between personal property and real property, the first being subject to the \textit{domicile} at the time of death, the latter being governed by the \textit{lex rei sitae}, i.e. the law of the state where the real property is located. A situation of a \textit{gespaltene Rück- und Weiterverweisung} would arise if a German court, e.g., ought to decide a heritage dispute concerning the estate of a US American citizen, resident in Hamburg, Germany and owning a summer cottage in Cannes, France.
in a different way or it shall be substituted by German substantive law. Such public policy control of foreign law applies, in particular, if an application of foreign law would violate the fundamental rights as defined in the German Constitution.

**Court System and Mechanisms of Dispute Resolution**

In Germany, the legal framework on the structure and functioning of the court system is set out in the Constitution (in particular, in Art. 20 para. 3 and Art. 92 GG), establishing the rule of law (Rechtsstaatsprinzip) as a fundamental principle and providing for the independence of the judiciary. In addition, the Judicature Act (Gerichtsverfassungsgesetz, GVG) regulates different types of jurisdiction depending on the subject matter of the dispute. The German courts are essentially divided into five groups which correspond to the main areas of the law: there are the so-called regular courts (ordentliche Gerichtsbarkeit) dealing with private law and criminal law matters, the Labor Courts, the General Administrative Courts, the Social Courts and finally, the Financial Courts competent of deciding disputes arising from taxation issues, contributions and fees. In addition to these courts, there is the German Federal Constitutional Court (Bundesverfassungsgericht), which serves as a safeguard of the Grundgesetz. The Bundesverfassungsgericht may declare null and void any statute, decision or other expression of governmental authority if it violates fundamental principles of the Constitution (in particular, any of the fundamental rights). In contrast to the court system in many other countries, in Germany there is no supreme court with general jurisdiction over all aspects of the law equivalent to the Supreme Court (formerly the House of Lords) in Britain, the US Supreme Court or the Swiss Bundesgericht.

Further details for particular branches of the German court system are regulated by various procedural acts. The most important of these are the Code of Civil Procedure (Zivilprozessordnung, ZPO), the Code of Criminal Procedure (Strafprozessordnung, StPO), the Rules of the Administrative Courts (Verwaltungsgerichtsordnung, VwGO), the Labor Court Law (Arbeitsgerichtsgesetz, ArbGG), the Tax Court Code (Finanzgerichtsordnung, FGO), the Social Court Act (Sozialgerichtsgesetz, SozGG) and the Federal Constitutional Court Act (Bundesverfassungsgerichtsgesetz, BVerfGG).

The court of first instance will always be the Amtsgericht (Municipal Court) or the Landgericht (District Court). The Amtsgerichte have subject matter jurisdiction (sachliche Zuständigkeit) over disputes with an amount in controversy (Gegenstandswert) of up to EUR 5,000 (Sec. 23 no. 1 GVG) and for matters particularly assigned to them, e.g. lessor and tenant disputes and domestic proceedings (Sec. 23 no. 2 GVG). At the Amtsgericht level, civil law disputes are decided by a single judge.

A Landgericht, one step higher, is either a district or regional court with subject matter jurisdiction over all disputes with an amount in controversy exceeding EUR 5,000 (unless the case is assigned by special statute specifically to the Amtsgericht). For claims exceeding EUR 5,000, the Landgericht is the court of first instance. Furthermore, the Landgericht is automatically the court of first instance for claims arising out of violations of official duties irrespective of the amount in controversy (Sec. 71 para. 1 GVG). At the Landgericht level, the case is decided
either by a single judge (Einzelrichter) or, if the merits of the case include special areas of law (e.g. banking, finance or insurance issues), by a panel of three judges (Kammer). However, depending on the difficulties of the case in question, it can be transferred from a single judge to the panel or vice versa (Secs. 348, 348a ZPO). At the level of the Landgericht (and superior courts) party representation by a lawyer is mandatory.

Above the Landgericht is the Higher Regional Court (Oberlandesgericht) and finally there is the highest of the regular courts, the Bundesgerichtshof or BGH (Federal Court of Justice), which has its seat in Karlsruhe and Leipzig. The BGH is one of the supreme federal courts and its territorial jurisdiction covers the whole of Germany. The Oberlandesgerichte are the highest courts of a particular state; each is responsible for several Landgerichte, which in turn are responsible for several Amtsgerichte (Fig. 1.5).

In addition to this brief overview of the German court system, the growing significance of the decisions of the courts of the European Community should be noted. These courts are the Court of First Instance and the European Court of Justice (ECJ), both of which are seated in Luxembourg. The procedural framework is provided for in EU law, in particular, the procedure for preliminary rulings of the ECJ on those questions of Member States’ law, which raise issues under EU law. According to this procedure for preliminary rulings, national courts of EU Member States can refer cases to the ECJ if the case raises a question of the scope of applicability of EU law. The decision by the ECJ is binding for the referring court (Art. 267 TFEU). By this procedure the ECJ can ensure uniform interpretation of EU legislation in all of the EU Member States.
1.2 Key Aspects of German Business Law

1.2.1 Codified Rules and Judge-made Law

1.2.1.1 German Law as a Civil Law System

From a comparative legal perspective, the German legal system belongs to the group of ‘civil law’ systems which is characterized by its numerous statutes and codified legal rules. Thus, the statutory framework relevant for doing business in Germany is mostly ‘written law’ which can be found in various codifications, such as the German Civil Code (Bürgerliches Gesetzbuch, BGB) or the German Commercial Code (Handelsgesetzbuch, HGB), the German Act on Limited Liability Companies (GmbH-Gesetz, GmbHG), the German Stock Corporation Act (Aktiengesetz, AktG), the Transformation Act (Umwandlungsgesetz, UmwG) or the Public Takeover Code (Wertpapiererwerbs- und Übernahmegesetz, WpÜG)—this list being far from exhaustive.

1.2.1.2 Importance of Judge-Made Law

However, in many areas of law, especially in all areas of business law, one also has to consider relevant case law, which has been gradually developed by the German courts when applying codified rules to business practice.

While there are considerable differences between common law jurisdictions (like the UK or the US) and civil law systems such as Germany, one should—at least from a functional point of view—not overrate them.

On the one hand, case law in Germany is not regarded as a formal source of law, since the function of the courts is seen in applying the law rather than creating it. This is a major distinction to common law jurisdictions, which are typically characterized by a predominance of judge-made law. Under the traditional rule of the binding precedent (‘stare decisis’) all courts of a jurisdiction are legally bound to follow the decisions of higher courts of the same jurisdiction insofar as the legal reasoning (‘ratio decidendi’) applies to the facts of the case. By contrast, in Germany, judicial decisions generally do not have a comparable binding legal effect, rendering a reliance on past decisions considerably more risky.21

On the other hand, even in a civil law system like Germany, court decisions, and in particular decisions of the highest courts of each judicial branch, are of great significance. Case law plays an important role in supplementing the law by expanding or narrowing the scope of its application. A complete statutory coverage of all legal issues is obviously impossible since the legislator cannot foresee all circumstances or future developments. Furthermore, statutes most often need to be interpreted, which gives judges a certain discretion when applying the law to the facts of the case. Finally, the legislator sometimes deliberately avoids specific regulation but

21 First-instance decisions generally have no binding effect at all. However, the Federal Court of Justice held that a failure of a lawyer or notary public to familiarize herself/himself with and advise her/his or her clients according to last-instance decisions is considered negligence.
leaves the development of the law to the courts. Consequently, court decisions and judge-made law play an important role in Germany.\textsuperscript{22}

### 1.2.1.3 Interpretation of Statutes

However, when interpreting statutes, the German courts tend to show more self-restraint compared to their counterparts in a common law system. German judges are not free in their application of statutes but need to abide by the following standards of interpretation developed by the courts and legal scholars:

1. According to the so-called ‘literal approach’ (*Auslegung nach dem Wortlaut*) a judge needs to analyze closely the wording and grammatical construction of the statute, including its punctuation. The literal approach is often characterized as the most important means of interpretation and may limit the application of the other methods of interpretation.

2. Under the so-called ‘systematic’ or contextual approach (*systematische Auslegung*) the judge is required to analyze the context of the statute in order to define its meaning. According to this approach, the provision is observed as being part of a bigger picture, i.e. the statute as a whole, and—in turn—the statute as a whole is analyzed as being part of an interconnected legal framework. Thus, the judge will analyze the statute as a whole, taking into consideration preceding and following sections and subsections of the statutory provision to be applied, as well as other statutes that are closely related to the subject matter.\textsuperscript{23}

3. The so-called ‘historical approach’ (*historische Auslegung*), also known as the genetical approach (*genetische Auslegung*) aims at finding the meaning of a provision on the basis of its historical origins. It is meant to reveal the original intention of the legislator at the time of legislation, e.g. by means of explanatory guidelines or reports on draft statutes. The historical approach can be of particular importance when statutes have been changed, e.g. certain provisions have been abandoned. In such cases the meaning of a provision can often be discovered by comparing the new provision with the original legal situation. On the other hand, the historical approach is arguably the ‘weakest’ interpretation method, since the current understanding of a statutory provision will usually have greater weight

\textsuperscript{22} This becomes evident when regarding general clauses (*Generalklauseln*), i.e. provisions that are intentionally worded in a most general way. For example, Sec. 242 of the German Civil Code simply states that an obligor has a duty to perform ‘according to the requirements of good faith, taking customary practice into consideration’. Despite—or one might better state because of—the concise wording of the provision courts have developed a substantive body of case law, which can be divided into four functions and more than ten different case groups, with one of the leading commentaries on the provision featuring more than 116 narrowly printed pages. The inherent principle of ‘good faith’ has thus become a general principle, influencing all areas of German law, not limited to civil law alone and can be seen as having—in parts—a similar effect to the concept of ‘equity’ in common law systems.

\textsuperscript{23} For example, the position of a provision within the context of the statute alone may reveal that it is an exception to a general rule. General rules are meant to be the standard procedure for dealing with certain aspects and exceptions. In contrast, if the provision is implemented only for a specific situation, a narrow interpretation of the provision is required.
than the original intentions of the legislator, especially if the provision in question is particularly old.

4. The so-called ‘teleological interpretation’ (teleologische Auslegung) is based on the notion of legal rules as instruments to realize certain legal, social or economic goals and values. When utilizing the teleological approach, the judge will analyze the provision as to its underlying purpose and will adapt its application to the facts of the case accordingly. Teleological interpretation often plays a crucial role in the interpretation of statutory provisions either by justifying a choice between two possible alternatives of interpretation (found according to the other methods of interpretation), as well as by supporting less obvious interpretations by reference to the injustice entailed by an alternative, and prima facie more obvious interpretation.

5. Finally, judges are bound to interpret a statutory provision in such a way that its application is in line with the principles and provisions of higher-ranking law, in particular the German Constitution and EU law. Therefore, statutes always have to be interpreted in such a way that they are in conformity with the Grundgesetz (verfassungskonforme Auslegung) and with EU law (gemeinschaftsrechtskonforme Auslegung).

1.2.2 Increasing Importance of European Law

With the increasing importance of European Union institutions and EU law, it is not surprising that European sources of law have become more relevant in the national context.

1.2.2.1 European Legal Instruments

European law is typically divided into so-called primary EU law and secondary EU law. The sources of primary legislation are the Founding Treaties and the Accession Treaties, including the various attached annexes and protocols. The Treaties are agreed upon by the EU Member States. Primary legislation lays down the basic policies of the Union, establishes and defines its institutional structure, legislative procedures and the powers of the Union vis-à-vis the EU Member States. The most significant change in the recent past has been brought about by the Treaty of Lisbon, which entered into force on 1 December 2009. The Treaty of Lisbon amended the Treaty on the European Union (Treaty of Maastricht) and the Treaty Establishing the European Community (Treaty of Rome), the latter having been renamed in the process to Treaty on the Functioning of the European Union (TFEU).

The term ‘secondary legislation’ is used for the legal sources enacted by the EU institutions based on the powers conferred to them under the Treaties. Legislative instruments available to the EU institutions comprise EU Regulations, EU Directives, EU Decisions and Recommendations, which differ as to their binding force for the EU Member States.24

24 See Art. 288 TFEU.
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