CONTENTS

[1. INTRODUCTION: LAW AND LEGAL FAMILIES 3](#_Toc533532573)

[1.1. LAW, MORALITY AND ETHICS 3](#_Toc533532574)

[1.2. LAW AND CUSTOMS 3](#_Toc533532575)

[1.3. LEGAL APPROACHES 3](#_Toc533532576)

[1.4. SOURCES OF LAW 4](#_Toc533532577)

[1.5. (WESTERN) LEGAL FAMILIES 4](#_Toc533532578)

[2. CONTRACTS (general contract law) 5](#_Toc533532579)

[2.1. ELEMENTS OF CONTRACT 5](#_Toc533532580)

[2.2. DECLARATION OF INTEND 6](#_Toc533532581)

[2.3. MINORS AND INCAPACITY TO CONTRACT 8](#_Toc533532582)

[2.4. LIMITED CAPACITY TO CONTRACT 9](#_Toc533532583)

[2.5. ERRORS AND VOIDABLE CONTRACTS 9](#_Toc533532584)

[2.5.1. “HONEST” MISTAKES 9](#_Toc533532585)

[2.5.2. DECEIT AND DURESS (§ 123) 10](#_Toc533532586)

[2.6. THE LAW OF AGENCY 10](#_Toc533532587)

[2.6.1. UNAUTHORISED AGENTS 11](#_Toc533532588)

[2.7. THE LIMITS OF CONTRACTUAL FREEDOM 11](#_Toc533532589)

[2.7.1. Breach of Statutory Prohibition (§ 134) 11](#_Toc533532590)

[2.7.2. Breach of Public Policy (§ 138) 11](#_Toc533532591)

[2.7.3. Non-Discrimination Law (AGG) 11](#_Toc533532592)

[2.8. STANDARD BUSINESS TERMS (AGB) § 305 I 12](#_Toc533532593)

[2.9. CONSUMER PROTECTION 12](#_Toc533532594)

[2.10. CONTRACTS AND PERFORMANCE 14](#_Toc533532595)

[2.11. BREACH OF CONTRACT 14](#_Toc533532596)

[2.11.1. COMPENSATION 14](#_Toc533532597)

[2.11.2. BREACH OF CONTRACT – PERFORMANCE 15](#_Toc533532598)

[3. SALE OF GOODS, CONSUMER PROTECTION 16](#_Toc533532599)

[3.1. IMPORTANT CONTRACT TYPES: 16](#_Toc533532600)

[3.2. Sale of Goods – Material Defect 17](#_Toc533532601)

[3.2.1. Buyer‘s rights, § 437 18](#_Toc533532602)

[3.2.2. Purchase of Consumer Goods 19](#_Toc533532603)

[3.3. Special Trade Law 19](#_Toc533532604)

[3.3.1. The trader 20](#_Toc533532605)

[3.4. Sale of goods between traders 21](#_Toc533532606)

[3.4.1. Formation of the contract between traders 21](#_Toc533532607)

[4. TORTS (LIABILITIES IN CASE WHEN YOU DON’T HAVE CONTRACT) 21](#_Toc533532608)

[5. COMPANY LAW 21](#_Toc533532609)

[5.1. TYPES OF BUSINESS ASSOCIATIONS 22](#_Toc533532610)

[5.2. LAW OF BUSINESS ASSOCIATION 22](#_Toc533532611)

[5.2.1. Partnerships VS Bodies corporate 22](#_Toc533532612)

[5.2.2. Employee participation 23](#_Toc533532613)

[5.2.3. Separation of Ownership and Control… 24](#_Toc533532614)

[5.3. Setting up a company; Internal structure and governance 25](#_Toc533532615)

[5.4. Management duties and liability; compliance 25](#_Toc533532616)

[5.4.1. Governance & Contracting 26](#_Toc533532617)

[5.4.2. Supervisory Board 28](#_Toc533532618)

[5.4.3. D&O Insurance 29](#_Toc533532619)

[5.5. LATIN PHRASES 29](#_Toc533532620)

# INTRODUCTION: LAW AND LEGAL FAMILIES

## LAW, MORALITY AND ETHICS

Example: A legal transaction which is immoral is void. (§ 134 BGB)

## LAW AND CUSTOMS

“An obligor has a duty to perform according to the requirements of good faith, taking customary practice into consideration”. (§ 242 BGB)

*Remarks from the lecture:*

1. In Germany there is no system for public defending for free.
2. Suing and being sued:

* Choose the right court (if you sue – go to their court)
* Sustain your case
* The looser pay court costs + layer

1. Courts:

* Local courts
* Magistrate courts (you don’t need layer)
* District courts (bigger matters, business issues)

## LEGAL APPROACHES

* Wording (also, see [Latin phrases](#_LATIN_PHRASES))
* Purpose (telos) – when, why, in response to what
* Systematic context
* History

## SOURCES OF LAW

* Statue
* Court decisions
* Contracts

## (WESTERN) LEGAL FAMILIES

*Remarks from the lecture:*

Law is about grey areas.

Law is about allocation of risks.

|  |  |  |
| --- | --- | --- |
| Common Law Family | (Continental) Civil Law | Nordic Law Family |
| UK, USA, Canada, (India), Australia, New Zealand, Ireland, Hong Kong   * Colonized (comparable) | French: France, Italy, Belgium, Indonesia, Scotland, many African and South American countries.  German: Origin, for example: Germany, Austria, Switzerland, Japan (China) | Denmark, Norway, Sweden, Finland |

**Main difference between common law family and civil law:**

* Language
* Doctrine of precedence (some decisions = law/opinion)
* Idea of codification (comprehensive code for different areas)

**Current development:**

* differences are going away through directives (EU law influence)
* case law + statutory law in the modern world

# CONTRACTS (general contract law)

## ELEMENTS OF CONTRACT

*Remarks from the lecture:*

Freedom of will – constitution, no forced contracts.

Freedom of contract – you can enter into contract in any form, with anyone on any topic.

Invitation to treat – you are initiating someone to make an offer. It is not binding.

|  |  |
| --- | --- |
| 1. **Offer (DoI)** | * Made by the offeror * Legally binding (§ 145 BGB) until they are accepted, refused or no acceptance can be expected any more (§ 146 BGB) * Offers must contain all essential elements of the contract * Offer vs. invitation to treat (invitatio ad offerendum) - Example – advertisement in a newspaper is an invitation to treat = invitation to make an offer, things in the shop   Letter of intend – “agreement to agree” |
| 1. **Acceptance (DoI)** | * Must match / mirror the offer * Amendments of an offer constitute a new (counter-)offer (§ 150) * No express acceptance required (implied acceptance) |
| 1. **Intention to be legally bound** |  |

**Not required**

* Consideration (required in Common law – “I do something because I get **something** back”).
  + For example, there is no consideration in donation
  + But, for example Christmas bonus or tip to the waiter are not donations, since there is a consideration there.
* Particular form (unless otherwise provided)

! Interpretation of the case almost always required.

**Legal transaction**

Definition:

* An occurrence/action that has a legal effect
* Core element is typically the DOI
* Plus, if required by law or contract, additional elements

WHO CAN ENTER INTO CONTRACT?

**Humans**

* ‘natural persons’
* Upon completion of birth (§ 1 BGB)
* Minors and mentally disabled persons have limited capacity to carry out acts that are legally binding (will be discussed later), but they do have legal capacity!

**Legal persons**

* Companies and associations
* Upon registration
* Partnerships have ‘limited legal capacity’

## DECLARATION OF INTEND

* The basis of every legal transaction and made with intention to be legally binding.
* Private declaration with the intention to trigger a legal effect.
* DOI can be implicit (nodding, taxi case)
  + But: silence is nearly always irrelevant!

Formal requirements for DOI:

* Usually no particular form required
  + But: Statutory law (or the particular contract!) can prescribe special formal requirements

Possible formal requirements

* Text form (§ 126b) [forget about electronic form, § 126a]
* Written form (§ 126)
* Official certification (§ 129) [marriage declaration]
* Notarial recording (§ 128) [contracts: property, NDA, mergers. If contract is not written full – it is not binding]
* “Higher” formal requirement is sufficient to satisfy “lower” requirement

HOW TO INTERPRET A DOI?

* **Problem 1:** Language is not precise
* **Problem 2:** People have different understandings and backgrounds
* Intention is more important than literal meaning (§ 133), Contract interpretation (§ 157)
  + but literal meaning is the starting point for interpretation

DOI

* As soon as I say something
* As soon as it is received – general rule

DOI becomes binding upon receipt

* Exception: DOI that do not need to be received
* So, when is a DOI received?

When is DoI received?

**NON-PHYSICAL DOI**

* holiday does not matter
* when heard/seen by the recipient (applies to all email addresses which are used for communication)

**PHYSICAL DOI**

* if both parties are present
  + when physically taken by the addressee
* if parties are not present
  + when the DoI enters the addressee's zone of control
  + the addressee can be expected to take notice under common circumstances (depends on: private/business persons, days, holidays).

## MINORS AND INCAPACITY TO CONTRACT

INCAPABLE to enter into contracts (§ 104 BGB)

* Persons under the age of 17;
* Persons in a permanent state of pathological mental disturbance, which prevents the free exercise of will
  + Except: everyday transactions (§ 105a BGB).

Consequence:

* DOI is void (§ 105 I BGB)
  + Also applies to declarations made in a state of temporary mental disturbance (drunk) (§ 105 II BGB)

*Remarks from the lecture:*

Protection of minors is a holly grail of German Law.

## LIMITED CAPACITY TO CONTRACT

* Minors between 7-18 (§ 106 BGB).

Consequences:

* DOI that results in legal obligations for the minor require consent of legal representative (§ 107 BGB)
  + Compare the wording of § 107 BGB – how can that be?
  + “For a DOIs as a result of which he does not receive only a legal benefit, a minor requires the consent of his legal representative.”
* Consent can be given prior to or after the transaction (legally 2 parents)
* Without consent, the transaction is void (§ 108 I BGB)

Exception § 110 BGB children can do whatever they want with pocket money, however:

* Giving the pocket money as kind of consent
* Third parties (grannies) => then children have to get parents’ consent
* For job contracts => kids need to get consent as well.

## ERRORS AND VOIDABLE CONTRACTS

Starting point: Contracts are valid and binding!

Valid voidance of DOI

* Reasons for voidance: honest mistake, duress (not for material defect)
* Declaration of voidance (contract is valid as long as declaration of voidance is not made)

### “Honest” mistakes

* If the will behind the DOI does not correlate with the content of the DOI (§ 119 I)
* Or if the DOI is transmitted incorrectly (§ 120) (to misspeak, to mistype, to mix up terms)
* If the issuer is in error about an essential characteristic (price is not a characteristic)

Consequences:

* Voidance (Rescission) needs to be declared and received (§ 142)
  + Legal language is not required
* After the error detected, the declaration needs to be made without undue delay
  + What is undue delay?
* Recipient of DOI can claim compensation for damages incurred for relying on the declaration

*Remarks from the lecture:*

If you are acting as an Agent, the effect of DOI binding not you, but the person you are acting for. You are legally neutral.

Minors can act as Agents.

### Deceit and Duress (§ 123)

Decision-making can also be influenced by

* Deceit (pregnancy lie is allowed)
  + Can also constitute fraud under § 263 of the Criminal Code
* Duress
  + Can also be criminal duress under § 240 of the Criminal Code (giving a notice)

Consequences

* DOI is voidable – declaration of voidance is possible within one year (§ 124)
* No compensation owed

Example of duress

## THE LAW OF AGENCY

* DOI are made by representatives
  + Requirements for valid representation (§ 164)
    - DOI by agent
    - In the name of the principal
      * Exception: transaction „to whom it may concern “
    - With authority / within the scope of power conferred by principal (set out in working contract)

Authority can be granted:

* …by DOI (power of attorney)
* …or by law (legal representatives)

### Unauthorised Agents

* Principal can confirm the contract, or refuse to do so (§ 177 I)
  + Principal protected more
* If principal refuses, the unauthorised agent owes compensation to the other party, § 179 (simplified)

## THE LIMITS OF CONTRACTUAL FREEDOM

### Breach of Statutory Prohibition (§ 134)

* + Only if the legal transaction is prohibited in principle

### Breach of Public Policy (§ 138)

* + § 138 I: Transaction contrary to public policy
    - …if it is against the sense of decency of “just and fair” people
    - Overpricing is not immoral
  + § 138 II: Extortion
    - … disparity between performance and consideration alone is not sufficient!

### Non-Discrimination Law (AGG)

* + Allgemeines Gleichbehandlungsgesetz (**AGG**) in force since 2006
  + Addresses discrimination based on race, ethnicity, gender, religion or comparable view, disabilities, age, sexual identity (§ 1)
  + Contains employment law and general law provisions

Scope of application, § 2 AGG

* + Inter alia (!) employment and employment related contracts, education, and goods that are generally available to the public

Prohibited discrimination under § 19…

* …in contracts that are typically entered into in a multitude of cases on similar or identical conditions without regard of the other party (simplified)
  + Consequence: does not apply to typical business situations

Exemptions

* Justification under § 20
  + In particular, private contracts which are based on trust and closeness between the parties…
  + …or safety reasons

## STANDARD BUSINESS TERMS (AGB) § 305 I

* Contract terms
* Pre-formulated (no bargaining or negotiation)
* For a multitude of contracts
* Presented by one party to the other party

Background

* Why are standard business terms used? – to be able to produce multiple contracts
* What are the risks? – one can write anything there
* What is the legal consequence? – you get into troubles

**1. Is this a Standard Business Terms**

**(§ 305 I)?**

**2. Have the terms become part of the contract (§ 305 II)?**

* by **direct reference** or (if not possible) by **giving notice of the existence of the terms** and
* gives **opportunity to take notice** of the terms and
* the other **party agrees** (typically implicitly)

NOT:

-> contract formed without the terms.

**3. EXCEPTION: Is the content permitted (§§ 307-309)?**

* §§ 308/309 contain **specific forbidden clauses,** but apply only between consumers and businesses
* Is a clause **particularly disadvantageous** (§ 307)? (If incompatible with essential principles of the statute or If is contrary to basic principles of the respective contract)

NOT:

-> Respective clause is invalid (no “reduction” of clause!).

- Statutory law fills the gap

## CONSUMER PROTECTION

\*you have buyers rights for 14 days

* Consumer (§ 13): **a natural person** entering into a contract for a purpose that is mostly for private.
* Business (§ 14): **a natural or legal person** entering into a contract for purposes mostly business-related
* Consumer protection under the German Civil Code requires a **„B2C“- situation**

Civil Code only recognizes an exceptional need for protection in case of minors and mentally incapacitated persons. Private law modify general Civil Code to protect those who is in a particular need.

Consumer protection is based on EU-Directives

Consumer protection is granted…

* …in situations in which the consumer might struggle to make up his mind properly
  + Online contracts and contracts that are formed outside of business premises
* …for contracts that put long-lasting obligations on the consumer
  + Loan agreements

Consequences:

* Business needs to provide additional information, § 312d
* Consumer has a right of withdrawal for 14 days, § 312g
* In information conveyed was insufficient, the right of withdrawal extends to one year

Off-premise contracts, § 312b

* contracts that are formed in premises that are not the trader ‘s business premises, or on trader ‘s business premises, but where the consumer has been addressed and invited to the premises just an instant earlier, or
* on an excursion that was organised by the trader

Distance Contracts, § 312c

* Contracts which are formed exclusively through means of distance communication (see examples in § 312c II)

Exceptions (§ 312g II), for example:

* customized goods
* perishable goods
* software with a broken seal / shrink-wrap
* newspapers and other periodicals

Declaration of withdrawal

* DOI that needs to be received
* But: DOI needs to be sent on time (not: received)
* No form required (any more)

## CONTRACTS AND PERFORMANCE

Basic principle: § 362 BGB

* Alternative: creditor accepts “something” instead of what was

agreed upon, § 364

How to perform with money?

* Bank transfer / cash / cards / PayPal
  + Germans love cash. Therefore, in the best case you should use cash.
* Also, important: Set-off / summation, § 389

## BREACH OF CONTRACT

### COMPENSATION

2 elements of fault. Misconduct § 276:

1. Negligence – what should the reasonable person have done
   * Simple negligence
   * Gross negligence
2. Intentional misconduct

Reverse situation – if something has been done to you: you don’t need to prove that someone was negligent, he should prove that he did take all reasonable care.

Compensation requires an element of fault – compensation and responsibility

* This includes misconduct of legal representatives, § 278
* This test can be modified in certain situations (e.g., § 311a)

What is “compensation”?

What is owed?

* Restoration, § 249 I
* If compensation is owed for injury of persons or damage of goods, the respective monetary amount can be required, § 249 II
* If restoration is not possible or only possible with disproportionate expenses, compensation is money is owed, § 251
  + Remember the sad tale of Ferdinand! (when you get paid the value of the damaged property)
* Contributory negligence, § 254 – if compensation is owed to you, but you contributed to this negligence.
* If you can’t afford compensation in certain areas there are compulsory insurances (law, finance, construction).

What is included?

* Lost profits, § 252
* For non-pecuniary (cant be fixed with money) losses only if prescribed by law, § 253 I
  + Sentimental value (emotional distress, German law does not cover these cases)
  + Reputation
  + Schmerzherz Geld (compensation for a pain)
  + Lost days of vacation
  + Heritage listed (houses which value is dependent on historical importance)

**Germany VS USA**

* USA compensation is way higher than in Germany
  + In USA they think it’s a punishment

### BREACH OF CONTRACT – PERFORMANCE

What kind of compensation can be?

* compensation instead of performance (e.g., § 283 or § 311a)
* compensation in addition to performance (e.g., § 286)

Inability to perform

1. Before the contract formed
2. After the contract formed

*Remarks from the lecture:*

General rule: people need to do what they promised to do.

|  |  |
| --- | --- |
| Performance is impossible § 275 BGB | Performance is delayed (it’s still possible) |
| Consideration   * No entitlement for performance, § 326 I (but maybe § 326 II) | Consideration is owed, unless contract is revoked |
| What about revocation (cancellation)?   * Yes, under § 326 V | What about revocation?   * Yes, under § 323 (we will discuss it for sales of goods!) * Not if breach of contract is trivial * “Right of second chance” for obligee |
| What about compensation?   * Yes, under §§ 280 I, III, 283 for ex post obstacle * Yes, under § 311a for ex ante obstacle | What about compensation?   * Yes, under §§ 281 I, III, 281 (instead of performance) * Yes, under §§ 280 I, II, 286 (in addition to performance) |

**Temporary default**

* Requirements, § 286:
  + Performance is possible and due
  + Failure to perform
  + Negligence or intention (§ 280 I)
  + Warning notice
    - Not required if a time period for performance has been specified by the parties (agreed by parties).
    - If there is a warning notice – damages can be claimed, but there is an exclusion § 286 II
* Consequence:
  + Default interest, § 288 (approx. 5% higher, than general interest rate, e.g. in Germany 0%).

*Remarks from the tutorial:*

1. Contract
2. Performance is possible and due
3. Failure to perform
4. Fault element
5. Warning notice

# SALE OF GOODS, CONSUMER PROTECTION

*Remarks from the lecture:*

All before was general contract law. Now we are about defects and material defects.

Background

• Of freedom to contract and types of contracts

• Of general contract law (§§ 241 – 432) and specific contract law (§§ 433 et seqq.)

## IMPORTANT CONTRACT TYPES

1. Sale of Goods, § 433
2. Loans, § 488
3. Lease, § 535
4. Service, § 611
5. Contract to produce a “Work”, § 631(result to be achieved by work or by service)
6. Partnerships, § 705 (Team up to achieve a common goal)

Donation contracts

* Donor is not liable for any defect
* If he, however, maliciously concealed such a defect with the result that done suffers some loss
  + Donor is liable to pay damages
* Donor may demand to return the things given

## SALE OF GOODS, § 433

### Basics

B2C situations § 476 (unless presumption is incompatible with the nature of the thing or the defect).

Parties - See § 433

General Contract Law

Sales of Goods Law

Passing of Risk

Crucial point in time = passing of risk (delivery)

1. Passing of risk, § 446
2. For existence of material defects
3. For distinction of sale of goods law (§§ 433 et seqq) and general contract law (§§ 275 et seqq)

Important

* Procurement free of defects is the seller’s main obligation

### Material Defect § 434

When risk is passed from the seller to the buyer

* Upon existence of a material defect, “curing” the defect becomes the seller ‘s main obligation

What about § 119 II?

* You can’t void the contract if there is a material defect, because rules are more specific

And § 123?

* Can apply as material defect

### Buyer ‘s rights, § 437

**CURE, § 439**

Cure has priority! - further buyer ‘s rights only apply if cure is somehow ineffective

* arg: wording of § 440; 2nd chance for seller
* compare to common law?

Procedure

* Buyer ‘s choice: repair/remedy or delivery of new thing, § 439 I
* Seller is bearing costs, § 439 ii
* Seller can refuse the buyer ‘s choice if remedy/delivery comes with disproportionate expenses, § 439 III
* If new goods are delivered, the seller needs to give back the defective goods, § 439 IV

**REVOCATION, § 440**

Prerequisites

- Material defect (of course), and

- Cure has not been effective, and

=> Seller refuses both types of cure, or

=> Cure was unsuccessful, or

=> Cure cannot be reasonably expected, or

=>If additional time period for performance has expired (§ 323 II!)

=> Material defect is not trivial, § 323 V S.2

Consequence

* Purchased item and purchase money need to be returned, § 346

**COMPENSATION, § 440**

**REDUCTION OF PURCHASE PRICE, § 441**

(since revocation is possible, reduction price is possible as well)

* Prerequisites
  + “Instead” of revocation
  + Includes trivial material defects, § 441 I S.2
  + Overpaid amount needs to be returned, § 441 IV
* Calculation, § 441 III
* Which means…

Note:

* §§ 439 et seqq set out specific requirements and relate back to §§ 275 et seqq
* No rights if buyer was aware of the defect (§ 442) (does not apply to normal negligence) or buyer ‘s rights were excluded (§ 444)
* Special rules for B2C sale of goods contracts (later)

### Purchase of Consumer Goods

Prerequisites:

* Seller is a business (§ 14) – remember?
* Buyer is a consumer (§ 13)
* Contract is about a movable thing (§ 90)

Consequences (essentials):

* Assumption of material defect if defect manifests within six months of purchase
* Contractual clauses deviating from the §§ 434 et seqq are void if detrimental to the consumer

## Special Trade Law

* Different types of actors under German civil law:
* consumer, § 13 BGB
* “normal” natural persons (not defined)
* businesses/entrepreneurs, § 14 BGB
* New: trader under the Commercial Code (Handelsgesetzbuch, HGB)

What is a trader (or: merchant)?

* Defined in §§ 1-6 HGB
* Considered by law as a savvy professional
* Traders are held to a higher standard

### The trader

Principles of trade law:

High level of knowledge of traders

* Higher speed of transactions
* Need for clarity
* Existence of special business customs

Consequence:

* Traders need to be registered (business register, “Handelsregister”)
* HGB imposes stricter rules on some types of transactions and contracts on traders

Trader – Merchant

|  |  |  |
| --- | --- | --- |
| Pursuant to § 1 HGB  (Merchant by definition) | Pursuant to § 2 HGB  (MERCHANT BY VOLUNTARY REGISTRATION) | Pursuant to § 6 HGB  (Merchant by legal form) |
| * Any commercial business carried out by a single person, unless the business does not require by reason of its nature or size, a commercially organised business operation   + Depends on size and complexity of the business * Traders need to register and are automatically subject to special trading laws | * Commercial businesses that do not require commercially organized business operations (“small businesses”) * Small businesses can register and are only upon registration subject to special trading laws | All commercial companies and partnerships   * Private Limited Company (GmbH) * Public Limited Company (AG) * Business Partnership (oHG) * Limited Business Partnership (KG)   Most important application in today ‘s practice! |

\*The principle of “lex speciales” applies (special law overrules general law): § 6 HGB overrules § 1 HGB

## Sale of goods between traders

Requirements, §377 HGB:

* Sale of goods (§433 BGB)
* Both parties are traders

Consequence:

* Purchaser is required to examine the goods upon delivery instantly (if permitted by the business), §377 I HGB;
* Purchaser needs to notify seller instantly of any material defect §377 II HGB
  + If the defect becomes apparent later (=could not be discovered upon examination), instant notice needs to be given §377 III HGB
  + If purchaser does not meet these requirements, the goods are “approved”, §377 II HGB

### Formation of the contract between traders

* DOI and Silence
  + Silence has no relevance for contracts
    - Exception: commercial confirmation letters
    - Customary law not regulated under statue
* Prerequisites
  + Both parties are traders
  + Contracts negotiations without conclusions
  + Immediate confirmation
  + Content with the scope of negotiation
* Consequence
  + Contract formed with the content of the confirmation letter

# TORTS (LIABILITIES IN CASE WHEN YOU DON’T HAVE CONTRACT)

Basics:

* Not penal in nature
* In Private law, the issue is simply compensation for the harm
* Must be proved that tortfeasor acted culpably
* Person who undertakes some essentially dangerous activities must take responsibility for any damages

Adequacy theory:

* Highly improbable and unusual claims or events generally will not form an adequate basis for imposing liability.

Rebuttable presumption justification

* Self defence
* Use of force in defence of property
* Consent of claimant

Claim for damages will only be succeed if it can be shown that rights has been infringed (only absolute rights).

# COMPANY LAW

## TYPES OF BUSINESS ASSOCIATIONS

* Choice of business structure is a business decision

## LAW OF BUSINESS ASSOCIATION

Business associations between entrepreneurial freedom and creditor protection

* Consequence 1: numerus clausus of business associations
* Consequence 2: law of business associations as national law with different ‘language’ and definitions

Influence of EU law

* Freedom of Establishment, Art 49
* Leading cases in the Court of the European Union (CJEU): Centros, Inspire Art and Uberseering
* Consequence: EU member states need to acknowledge companies from other member states if they have complied with the founding requirements in that state

### Partnerships VS Bodies corporate

|  |  |  |
| --- | --- | --- |
| Typical elements | Partnership | Bodies corporate |
|  | Registration necessary in some cases | Registration is required |
|  | Unlimited liability of partners | No liability of members/shareholders |
|  | Taxation as income of partners | Body corporate is subject to taxation |
|  | Partnership is linked to the partners | Existence of body corporate not linked to members |
|  | Partners involved in decision-making  (unanimous consent?) | Decision-making based on specific majorities  (not: unanimous decision-making) |
|  | Contractual basis  Flexible  Only suited for a number of small numbers of partners | Bodies corporate as separate legal entity  Transfer of membership is typically possible  Members not (or not all) involved in running the business |
|  | Partnership, §705 BGB  Contract + common cause + partners contributing  Business partnership, §105 HGB  Requirements of partnership (see above) + running a “substantial” business that requires a commercial business organisation  Cf. §1 HGB!  Limited liability partnership, §164 HGB  Requirements of business partnership+ at least one partner with limited liability | Registered Association (§21 BGB)   * Non-business entity * Not to be confused with charitable associations   Registered Cooperative (Cooperative Act; GenG)   * Registered Association with the purpose of promoting the businesses of its members   Private Company (Private Company Act; GmbHG)   * Registered Association based on shares, typically with a smaller number of shareholders   Public Company (Stock Company Act; AktG)   * Registered Association based on shares, can (!) go public |

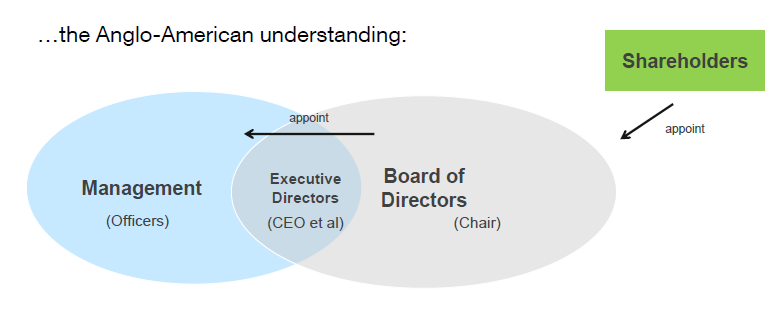
### Employee participation

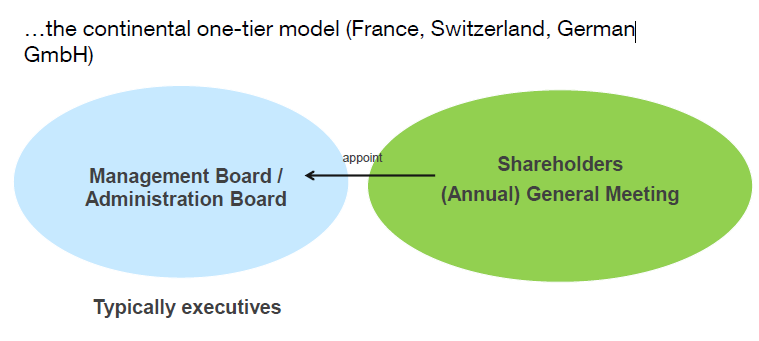
* THE particularity of German company law
* Employees and unions have a say in company supervision
* In all public companies (not: listed companies!), and in all companies > 500 FTE

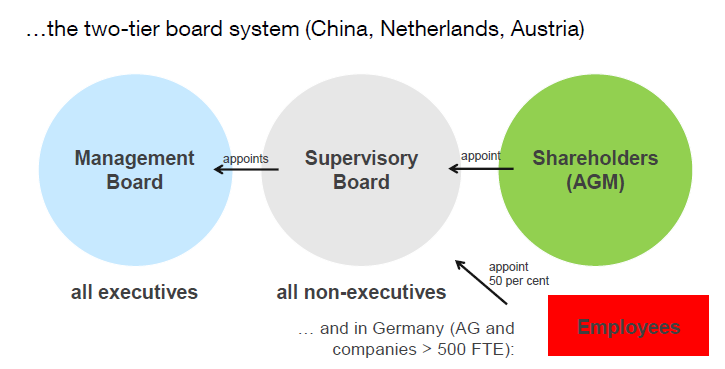
The Showrunners

* One-tier and two-tier board structures
* Management Board, Supervisory Board, Board of Directors
* Managers, Officers, Directors, Management Directors, Executive Directors, Independent Directors, Shadow Directors…

### Separation of Ownership and Control…







## Setting up a company; Internal structure and governance

1. Formation

* Setting up the Articles of Association (AA) / Company Constitution
  + Includes information on how much money needs to be contributed
  + “To contribute” mean – money is at the company’s sole and free disposal (§ 7 III GmbHG)
* Contributing the Capital

\* How much needs to be contributed before registration? - 25% of each cash contribution, but at least 50% of the statutory minimum capital stock (§ 7 II GmbHG)

\* When do I need to pay the rest? - When the managing directors call in the capital (§ 21 GmbHG)

\*If I can’t contribute - you can be stripped of your shares (§ 21 GmbHG)

\*Alternative to cash contribution - Yes, contributions in kind (§ 5 IV)

Same requirements?

* No, contributions in kind need to be made as a whole
* Reasons: riskier than cash contributions
* Worth of contribution must be assessed (and assessable!)

2. Registration

* Signing the Articles of Association before a notary
* Registration with the company register

\*Can the company enter in the agreement before registration? - Yes, but the acting directors are also liable (§ 11 II GmbHG)

3. Company comes into existence as a separate legal entity

* cf. § 13 I and § 13 II GmbHG

\*Court costs - about EUR 150, - registration fee

## Management duties and liability; compliance

### Governance & Contracting

|  |  |
| --- | --- |
| Directors | Shareholders |
| Representing the Company:   * Directors represent the company in and out of court (§ 35 I GmbHG) * Unless specified otherwise in the articles of association, directors can only bind the company when acting jointly (§ 35 II GmbHG) (cf. “managing directors”?)   Internal Governance:   * Directors have the right and the duty to run the company (§ 43 GmbHG) * Distinction between the directors’ employment/service contract and his/her appointment as a director | The general meeting…   * does not need to be a ‘meeting’ (circulation of documents instead) (§ 48 II GmbHG) * can give directions to directors (cf. AG!) * can change the articles of association (e.g., increase of share capital) with ¾ majority   Individual shareholders have the right (inter alia) …   * to vote in the general meeting (§ 47 GmbH) * to inspect the books at any time (§ 51a GmbHG) |

Remember: Internal governance can be modified by the articles of association (§ 45 II GmbHG)!

Liability: Personal liability of company or directors; individual claims

Loss: Loss accrued by the company by the end of the financial year

Directors’ Duties: For directors only. Employees and other managers are liable under employment laws only

|  |  |
| --- | --- |
| Duty of Loyalty | Duty of Care, § 43 I GmbHG / § 93 AktG |
| Written aspects of the duty of loyalty:   * Duty of confidentiality, § 93 I S.2 AktG * ‘No competition rule’, § 88 AktG * Criminal disloyalty (embezzlement), § 266 Criminal Code * Duty to follow orders of general meeting (GmbH only!)   Unwritten:   * Duty to act in the best interest of the company * Corporate opportunities rule * Unclear: Duty to disclose all conflicts of interest? * Duty of loyalty much more pronounced in the Anglo-American corporate world! | Mostly about decision making…   * Duty to prevent company from taking harm by acting with due care and diligence * Duty of legality * Duty to initiate insolvency proceedings, § 15a Insolvency Act   …but also, organizational   * Duty to organize company efficiently and monitor accordingly * Duty to establish a (real) compliance system?   Business judgement rule  The problem:   * Businesses, uncertainties and the blessing of hindsight   The solution:   * Business Judgment Rule (BJR), § 93 I S.2 AktG (‘safe harbour’):   + Business decision   + Appropriate information basis for decision, and   + Directors acting in good faith and in the best interest of the company   + Documentation is crucial!   Note:   * For breaches of the duty of care only! * No ‘legal judgment rule’! |

Consequences: Civil liability (criminal liability in some cases possible)

Directors duties and stakeholders

* The shareholder vs. stakeholder dichotomy

The legal approach

* Companies are separate legal entities
* Duties are owed to the company as a whole (not: to the shareholders)
* But what are the best interests of the company?
* Some economists and US law professors:
  + financial interests
* Overwhelming majority of judges and academics:
  + depends on the company, although generating returns will typically be the main purpose

Can directors consider outside stakeholders’ interests?

* Example: additional pay-offs for sacked employees
* Or “green” strategies (for example energy saving plans) without direct financial benefits

Relevant law: § 76 AktG

* Responsibility for running the company lies with directors, § 76
* Includes a certain level of discretion, even if detrimental to profits and dividends
* Red line: strategies and decisions that threaten the existence of the company
* Unclear: decisions which provide no financial benefits (cf. the Mannesmann case)

### Supervisory Board

Who needs it?

* + All public limited companies, § 95 AktG
  + Voluntary for private limited company and registered association
  + But: Mandatory for all businesses with more than 500 FTE, § 1 DrittelbG

Separation of management and supervision

* + Incompatibility, § 105 I
  + Managerial decisions cannot be vested in the supervisory board, § 111 IV S. 1
  + But some managerial decision required approval of supervisory board, § 111 IV S. 2

Duties:

* Supervision of company management, § 111 AktG
* § 93 applies accordingly, § 116 AktG
* Supervisory board needs to convene a general meeting if necessary, § 111 III AktG

Rights:

* Comprehensive right of inspection, § 111 II
* Appoints (and fires) the members of the management board
* Each member can call a supervisory board meeting, § 110 II

Issue: Authority and management decision *sui generis*?

Size and composition

* Statute sets out maximum sizes depending on sizes (absolute maximum: 21 seats)
* 50 % employee participation if company has more than 2000 FTE
* Since 2016: minimum of 30 % of the „underrepresented gender “, § 96 II AktG
* No member can have more than 10 (!!!) seats in supervisory boards

### D&O Insurance

Background: the benefits and risks of director liability

* Pros and cons of D&O insurance

Structure:

* Company and insurance enter into an insurance contract
* Director as beneficiary
* Typically, only for cases of negligence

Mandatory cap under § 93 II AktG

* Director needs to pay at least 10 per cent of the overall compensation (per case) …
* …with an annual cap of 1.5 times of the fixed salary

## LATIN PHRASES

Inter alia – among others

Pacta sunt servanda - contained clauses are law between the parties, and implies that nonfulfillment of respective obligations is a breach of the pact

Culpa in contrahendo - fault in conclusion of a contract

essentialia negotii - essential aspects

invitation to tread (invitatio ad offerendum)

ex ante

mora creditoris

mora debitoris

culpa in contrahendo

laissez faire – all legal subjects are equal, not only in law, but also in social power and legal skills.

lex speciales