

**TRADING UNDER THE LAWS
OF GERMANY**

**U. S. DEPARTMENT OF COMMERCE
BUREAU OF FOREIGN AND DOMESTIC COMMERCE**

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NOTICE

The present Government of Germany has been given power for a 4-year period to legislate by decree not subject to the ordinary constitutional limitations. As a result new laws may be made effective at any time. Changes affecting the topics dealt with herein will be published in the Foreign Legislative News Service of the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

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FOREWORD

Germany occupies an interesting position among the nations of Europe. Its population (now perhaps 65,000,000) is large and consumes a goodly percentage of the better products and raw materials of trade and commerce; its territory is extensive (over 185,000 square miles), sustaining a highly industrialized population on a satisfactory wage basis in normal times; its industries, requiring markets for their own manufactures, have taught its people that they must consume foreign goods and thus create balances which will stimulate their international trade. In 1932, among the countries of Europe, Germany was outranked in trade with the United States only by the United Kingdom, supplying \$73,500,000 worth of our direct imports and taking \$133,500,000 worth of our direct exports. In a commerce of such proportions many legal questions naturally arise.

Business men realize that a knowledge of business conditions alone is not sufficient to attain the best results in international trade and maintain the smooth flow of commerce. Such knowledge must be supplemented by acquaintance with at least the more commonly known aspects of the law of the country with whose citizens they propose to deal. It is to furnish such a background that this bulletin has been prepared.

This publication does not attempt to give complete information on all German law nor even all German laws governing commerce or any particular phase thereof. It does, however, discuss the outstanding features of German law affecting trade; the salient points of company law and the law of contracts, agency, negotiable instruments, and bankruptcy; industrial property, taxation, and a brief exposition of the judicial machinery of Germany.

To supplement this information, current changes in the laws herein discussed will be noted in the Legislative News Bulletin and the more important changes given in greater detail in the General Legal Bulletin issued by the Commercial Laws Division of the Bureau.

FREDERICK M. FEIKER, *Director,*
Bureau of Foreign and Domestic Commerce.

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ABBREVIATIONS

H.G.B.	Handelsgesetzbuch	Commercial Code.
B.G.B.	Buergerlichesgesetzbuch	Civil Code.
Z.P.O.	Zivilprozessordnung	Civil practice act.
E.G.	Einfuehrungsgesetze	Introductory laws.
D.G.	Depotgesetz	Custody of securities act.
T.C.	Uebereinkommen ueber den Eisenbahnfrachtverkehr.	Traffic convention.
E.V.O.	Eisenbahnverkehrsordnung	Railway traffic regulations.
G.m.b.H.G.	Gesetz betreffend Gesellschaften mit beschraenkter Haftung.	Limited-liability company act.
K.O.	Konkursordnung	Bankruptcy law.
W.O.	Wechselordnung	Bill of exchange law.
R.G.	Reichsgericht	Decisions of the German court.
S.G.	Scheckgesetz	Check law.
G.u.W.	Gesetz gegen den unlauteren Wettbewerb.	Law against unfair competition.

TRADING UNDER THE LAWS OF GERMANY

I. INTRODUCTION

The treatment of certain aspects of German law presents an entirely different problem from that presented by a study of similar aspects of either English or United States law.

During the Middle Ages, England, because of its position on the outskirts of the cultural sphere of Europe, enjoyed an isolation which gave it opportunity to evolve its own common law more or less free from foreign influence; whereas Germany, located in the center of the maelstrom of the development of laws as well as of other cultural influences of the time, built up a veritable maze and confusion of conflicting rules out of the laws of each of its separate States, the laws of its Roman conqueror, and the laws of the surrounding nations.

In the nineteenth century, therefore, it was easy for England, with a unified system of substantive law, to continue to develop that system gradually by adding decisions in specific cases to make its present body of law; and it was just as difficult for Germany, with a confusion of laws, to reduce these laws to a unified system in any way but by codification—in other words, by practically clearing away the entire law structure and replacing it with a new one.

So different indeed has been the concept of the development of law forced upon Germany by the necessity for building a unified system out of medieval chaos that decisions, although they are accorded a limited evidentiary value, have never been considered precedents even for courts of inferior jurisdiction. At present, however, since the unified system has come into existence, an increasing recognition is being given by German lawyers and judges to the persuasive force of decisions.¹

CONSIDERATION OF THE SOURCES OF GERMAN LAW

This study, therefore, embraces a consideration of German codes and special statutory enactments, with their commentaries, as follows:

1. The Civil Code (*Bürgerliches Gesetzbuch*), 1896, and the civil practice act (*Zivilprozessordnung*);
2. The Commercial Code (*Handelsgesetzbuch*), 1897, and various supplementary codes — (*a*) the negotiable instruments law (*Wechselrecht*), (*b*) limited-liability company act (*Gesetz betreffend die Gesellschaften mit beschränkter Haftung*), 1898, (*c*) custody of negotiable instruments act (*Gesetz betreffend die Pflichten der Kaufleute bei der Aufbewahrung fremder Wertpapier*), 1896, (*d*) patent law, (*e*) trade mark law, (*f*) copyright law, (*g*) bourse law (*Boersengesetz*), (*h*) check law (*Scheckgesetz*), (*i*) unfair competition act, and (*k*) bankruptcy law (*Konkursordnung*) as amended in 1898; and

¹ See Gray, *Nature and Sources of the Law*, pp. 193-198.

3. Other statutes—(a) the judiciary act as amended in 1898, (b) land registry act, 1897, and (c) law of executions against real property, 1897.

PURPOSES OF CODIFICATION

Broadly speaking, the substantive law of Germany is embodied in the Civil Code. The sources of the substantive law can be clearly traced in the reports of the proceedings of the compilers of the several codes, a complete bibliography of which is given in Borchard's Guide to the Law of Germany. Professor Gareis, in his Science of Law (pp. 114–118) summarizes these sources as:

1. Roman law (*Gemeines Recht*), "received" 1495;
2. Prussian law (*Landrecht*), crystallized in 1794 after years of preparation;
3. French law of the upper Rhine region (*Code Napoleon*); and
4. Saxon code of 1863.

The Civil Code and what might be called its supplement, the Commercial Code, taken together, do not comprise the whole substantive law, nor even the whole law on the subjects with which they deal. Indeed, they were not intended to reduce the whole law to a compact mass. In each attempt at codification of German law, the customary and private law was to remain in force, except insofar as the codes expressly changed or abolished its provisions; but the endeavor was also made to evolve a system based on a philosophy of law and a clarification of general principles, from which, by well-founded interpretative methods, a completely modern system could be developed.²

HISTORY OF THE DISTINCTION BETWEEN THE CODES

Germany's juridical system, patterned, as are the systems of most of the nations of continental Europe and of South America, on code and statute the source of which is Roman law, has retained the historical distinction between civil and commercial law in its two codes bearing these names. In England, however, where the common law in its development embraced all substantive law, the mercantile law (law merchant) also merged with it.

Under Roman law no distinction was made between merchants and nonmerchants nor between transactions mercantile and non-mercantile. However, as trade, travel, and nationality broadened, with the consequent rise of the merchant class to a position of recognized power, certain privileges were slowly gained by this class through purchase from kings and rulers and otherwise.

The attempt to solidify and extend these privileges and to protect their continued enjoyment was one of the causes which led to the formation and extension of associations of merchants in guilds. And as trade expanded and passed over nations' boundaries, and as guilds became stronger, the necessity increased for a definite law for merchants more or less similar in its content and provisions in each country.

In this manner merchants came to have a law of their own, the provisions of which were not extended to dealings with persons who were not merchants.

² See Schuster's Introduction, pp. 10–13.

HISTORY OF THE DEVELOPMENT OF THE CODES

The Civil Code is the crowning achievement of codification of German private law. The advisability of codification was a subject bitterly disputed at the beginning of the nineteenth century by two schools of thought; but the advantages of the working of the Code Napoleon seemed to tip the balance in favor of codification, and the idea grew in Germany simultaneously upon and consequently with the attempt at German confederation.

In 1849 the delegates of the States of the German customs union (Zollverein) met at Leipzig and took the first definite steps toward codification when they drafted a uniform bill of exchange law (Wechselordnung), which, with few amendments, was adopted by all German States.

In 1861 the Diet of the German confederation recommended to the States the enactment of a Commercial Code, which, with some intermediate steps, prepared the way for the making of the Civil Code under the Empire.

By a constitutional amendment of December 20, 1873, the Imperial Government assumed legislative power over the entire sphere of civil law. Thereupon the Federal Council (Bundesrat) appointed five jurists as a commission to report on a plan for constructing a Civil Code. The report was submitted and approved, and another commission, consisting of 6 judges, 3 officials in the Ministry of Justice, and 2 professors, was appointed to perfect the work. A third commission reported a revised draft to the Bundesrat, which gave it, with an introductory act, to the Reichstag, where it was adopted August 18, 1896, to come into force January 1, 1900.

Enactment of the Civil Code necessitated the enactment of and amendments to other laws (1) to furnish a transition between the old law and the new, (2) to harmonize local law with imperial law, (3) to regulate matters still left to States—for all the foregoing the States passed intermediate laws (Ausführungsgesetze). Other new codes and statutes also were adopted.

The Commercial Code antedated the Civil Code and came into existence in 1861, to be adopted by all the German States in 1866. The enactment of statutes on specific branches of law and the final codification of the Civil Code, embodying and somewhat altering much of the material of the older Commercial Code, made the recasting of the Commercial Code necessary. This was accomplished by the enactment of the code on May 10, 1897, to go into effect simultaneously with the Civil Code on January 1, 1900.

ADMINISTRATION OF CIVIL AND COMMERCIAL LAW

In the administration of its law Germany has carried over the distinction between merchants and nonmerchants and between commercial and noncommercial transactions, and this fact must be remembered and kept distinctly in mind today in coming to a determination with regard to any particular case throughout the whole^a of German law.

The relation of the two codes is governed by article II of the introductory statute (Anhang) to the Commercial Code: "In com-

^a Bankruptcy is the one field of German law where this distinction is not made.

mercantile matters the provisions of the German Civil Code apply insofar as there is no other provision in the [Commercial] Code or this statute." And conversely the Commercial Code contains the rules relating to mercantile traders and mercantile transactions only insofar as they differ from the general rules.

Although the Commercial Code provides exclusively for regulation of mercantile trade in the ordinary course of business of mercantile traders, it embraces also transactions of other descriptions entered into by them. So that acts of merchants will be presumed (in the absence of proof to the contrary) to be mercantile; and any transaction which, as far as one of the parties is concerned, is mercantile is governed as regards both alike according to the Commercial Code, its usages, customs, standards, and interest charges.*

The general basic distinction between commercial and civil law is maintained in the preparation and presentation of cases in court, so that litigation involving mercantile transactions goes to the commercial branch of the court and suits involving nonmercantile transactions go to the civil branch. It is true that the distinction is not carried to the extent of organizing different courts for the handling of commercial and of civil cases nor of housing the courts in different buildings. The cases are really administered by the same courts, but by different parts thereof and by different judges; and the courts themselves are differently constituted, in that the civil court is presided over by professional judges whereas the commercial court has one professional judge and two merchant judges.⁵

Shuster suggests⁶ to the investigator of German law not to be satisfied to refer to provisions of the Civil Code and the Commercial Code or other federal statute alone, but to ascertain also whether the subject of the inquiry is one on which State law (including the *Ausfuehrungsgesetze* of the particular State) contains supplementary provisions, whether any national customary law affects the particular subject, and whether, in the event the subject is one which may be affected by State law, any local customary law relating thereto is in existence.

PERSONS AS DEFINED IN GERMAN LAW

NATURAL PERSONS

"Persons" in German law are "entities with capacity for acting as to things." Under this definition individual entities are either natural (*singuli*) or juristic (*universitates*) persons. The rights of natural persons are inherent; those of juristic persons are acquired by express conferring by the authority of the people.

As to natural persons, no distinction is made under German law between foreigners and German citizens,⁷ provided they have legal competency.

* H.G.B. 343-347, 352. (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

⁵ For an excellent presentation of the judicial system of Germany, see J. J. Cook in No. 1 *Judicial Review*, 1889, and von Levinski in 5 *Ill. Law Rev.*, 1910, pp. 193-202. (See also "Judicial power," at p. 202 of this present study.)

⁶ See introduction to *Principles of German Law*.

⁷ In Germany dealings with certain classes are somewhat restricted, as, for example, with military persons, also officials, teachers, the clergy, and members of reigning houses. (See B.G.B. 15, 411, 470; E.G. 57-58.)

For Germans, legal competency (*Geschäftsfähigkeit*) depends on majority (21 years), although a minor over 18 may be declared of age by the court. The exceptions to this are (a) persons mentally impaired, (b) minors under 7 without the consent of their legal representatives, and (c) judicially declared incompetents for prodigality, drunkenness, etc.⁸

For foreigners, those who in their own country would have the right to sue and be sued, contract, or otherwise engage in business or enter relationships (that is, enjoy legal competency) are granted equal privileges in Germany; and it naturally follows that such foreigners who become merchants in Germany—provided they subject themselves to and comply with the duties of German merchants—enjoy the same privileges as Germans. But a foreigner who undertakes an action in Germany for which he lacks legal capacity, or possesses only limited capacity, under his national law is not bound by such limitation except to the extent of his capacity under German law.⁹ Confirming this, article 55 of the civil practice act declares: "A foreigner incapable of appearing individually as a party to a suit in accordance with the laws of his national country is considered competent to appear, provided he has the necessary capacity under the rules of the jurisdictional court."

The only disability experienced by foreign individuals is that as claimants they must furnish bond at the request of defendants for court costs in some actions and that orders of arrest against them, to keep them from leaving the jurisdiction, are more readily granted.

JURISTIC AND QUASI-JURISTIC PERSONS

As all other countries, Germany has not only laws regulating the relations between natural persons but also laws with regard to legal entities other than natural persons.

Where natural persons associate to secure certain benefits or advantages directly resulting from such combination and not obtainable by individual effort, whether in a business or other endeavor, many legal problems arise. The most important of these are (1) as to the right of the association to acquire, hold, and dispose of property, (2) as to the rights of the individuals composing the association to bind it for their acts and commitments for its benefit, (3) as to the rights of the individuals composing the group to withdraw or otherwise dispose of their undivided shares in the association property, and (4) as to the compensation from profits or the contributions to make up losses to which the individual members are entitled or obligated.

At first these questions were answered in the same manner as for natural persons. The rights in the property and affairs of the association were personal to the individuals composing it, as were the obligations. With the increasing complexities of business and other relationships the questions became correspondingly more involved, and they could no longer be answered by placing the rights and obligations on the individuals composing the group. The necessity

⁸ B.G.B. 2.

⁹ Art. VII of the introductory act to the Civil Code.

for the creation of a fictitious entity on which to hang¹⁰ these rights and obligations became apparent; and since this entity was recognized to be a legal fiction, a sanction, or the sponsorship of the law, was required. The law having created it, the rules and regulations governing its functions, its rights, and its liabilities were supplied by the same agency. Thus the quasi-juristic person—the partnership and the association—came into being.

But the regulations governing partnerships and loose associations never got away from the individuals who composed them, and business required a legal entity which could assume all responsibility and rights of association property and free the individuals from responsibility, and which would continue after the individuals had ceased to exist or distinct from them. Governments once again extended their authority to supply a new, strictly juristic person—the company.

The actual workings of these entities—the partnership, the association, and the several types of companies—will be treated under appropriate headings herein.

STATUS OF FOREIGN CORPORATIONS

Foreign corporations doing business in Germany through a branch may attain¹¹ legal status by registering such branch in accordance with the provisions of sections 21 and 22 of the Civil Code.

This right of recognition is accorded to a branch of a foreign corporation by article X of the introductory act to the Civil Code: "Concerning nonrecognized [nonregistered¹²] foreign associations * * * the provisions of the Civil Code as to partnership as well as the provision of section 54, sentence 2, are applicable." This indicates that foreign corporations whose branches in Germany are not registered have only the rights of partnerships, whereas their branches which obtain recognition through registration acquire actual juristic personality.

As a matter of fact, however, there has been constant discussion in Germany among lawyers and textwriters as to the nature and extent of the recognition to be accorded branches of foreign corporations. One side maintained that a corporation should have authority only in the jurisdiction in which it applied for and obtained same. The other side maintained that the corporation having legally obtained authority elsewhere should have like authority for its branch in Germany as well, in exactly the same way that a foreign private person would have it. The question was finally decided by a judicial interpretation of article X,¹³ whereby it was held that this article was not meant to include foreign business corporations. As a result of this ruling, branches of foreign business corporations now possess full rights of juristic capacity from the moment of creation.¹⁴

¹⁰ Even as to natural persons the necessity for creating a fictitious person to and upon whom the rights and obligations of a natural person could attach was early realized in the case of an incompetent or a dead person. The estate of an incompetent or a dead person is considered in law as a "person"—not a natural one, it is true, but a person, nevertheless, who may have rights to things.

¹¹ B.G.B. 23.

¹² H.G.B. 13. (See also "Registration of foreign companies" at p. 9 of this chapter.)

¹³ "Das Aktienrecht," by Dr. Rudolf Fischer, pp. 38-39.

¹⁴ Journal du Droit International Prive, 1905, p. 1058; and Michigan Law Review, XXIX, No. 1, November 1930, p. 36.

Notwithstanding this interpretation, in practice the requirement for registration still stands,¹⁵ and a foreign corporation desiring to do business in Germany must first obtain recognition there.

The situation is entirely different when a foreign corporation organizes a German subsidiary. The German corporate subsidiary is, naturally, organized, conducted, and regulated by German corporate law. (See discussion of German companies, pp. 21 to 57, following.)

MERCHANT TRADERS AND THEIR DUTIES

In German law "merchant traders" are those entities—individuals, partnerships, associations, companies—that carry on a mercantile trade having for its object one of the following kinds of business:

1. The production and resale of movable things (merchandise) or negotiable instruments, irrespective of whether such merchandise is resold without change or after being worked upon or altered in some way;

2. The undertaking of work upon or alterations of merchandise for others so long as such trade exceeds the limits of mere handicraft;

3. The undertaking of insurance for a premium;

4. The business of banker and money changer;

5. (a) The business of forwarding goods or the carriage of passengers by sea; (b) the business of carrier of goods; (c) the conducting of any undertaking for the carriage of passengers by land or on inland waters; (d) the business of towage;

6. The business of commission merchant, forwarding agent, or warehouseman;

7. The business of mercantile agent or broker;

8. The business of publisher and all other businesses concerned with book or art dealing; and

9. The business of printer, so long as it exceeds the limits of mere handicraft.

Any undertaking not mentioned above, which is carried on for the purpose of trade and which requires a mercantile organization, is—provided the undertaker's trade name is entered in the mercantile register—also a commercial trade, except that agriculture and forestry are not commercial unless the undertaker avails himself of his right to enter his trade name in the mercantile register. Nor do the rules of the Commercial Code apply to handicraftsmen or persons whose business does not exceed the limits of a small trade unless it is carried on in the form of a partnership or other business aggregation.

The outstanding general duties of merchant traders as just defined are:

(a) Registration in the public registry;¹⁶

(b) Installation of a uniform system of bookkeeping;¹⁷

(c) Preservation of books and correspondence;¹⁸ and

(d) Other duties, such as rendering accounts as required by law, the obligation to execute orders given by customers unless promptly declined, a special obligation concerning the custody of goods or

¹⁵ Journal of Comparative Legislation, XIII, pt. 4, November 1931, pp. 218-219.

¹⁶ H.G.B. 29.

¹⁷ H.G.B. 38-47.

¹⁸ H.G.B. 44.

securities intrusted, and the additional duty to inspect goods for defect and to notify.¹⁹

These latter duties are required generally of mercantile traders. They will be discussed under the individual headings—commission merchants, brokers, etc.—in the main text of this study as the necessity therefor arises. The first three are briefly reviewed below.

REGISTRATION REQUIREMENTS

THE MERCANTILE REGISTER

The Commercial Code makes it obligatory for individuals engaging in business as a profession to register as merchants. Registration is not required of merchants who conduct a small mercantile business; it is, however, mandatory upon an aggregation of individuals who come together to engage in business, in order that they may obtain for the aggregation legal recognition upon which to base their right to do business, to acquire, hold, and dispose of property, wares, and merchandise, and to sue and be sued.

Registration takes place in the Handelsregister, a record under the control of the courts kept by a secretary of the court, with definite powers in regard thereto. It is open to public inspection, and copies of specific parts can be obtained upon proof of the applicant's legitimate interest. The court may also be called upon to certify the existence or nonexistence of certain entries therein. The court must publish the register entries in toto (where not otherwise ordered by law) in the German Official Gazette (Reichsanzeiger) and in at least one other paper.²⁰

The entries in the mercantile register acquire an effective presumption of accuracy, and persons will be estopped from objecting to or contradicting such entries if, knowing them, they do not correct inaccuracies.

NECESSARY FORMALITIES

Under the Commercial Code an individual merchant or a partnership must file with the appropriate court of the district in which the head establishment is located, for entry in the mercantile register, (*a*) a statement of the mercantile trade name and (*b*) the address of the head establishment,²¹ together with (*c*) a specimen signature of the trade name for retention by the court. Similar registration must be made in every other district in which the individual merchant or the partnership has a branch establishment.²²

In the case of a German corporate body the application must be made by the board of directors (Vorstand) collectively and must have annexed (*a*) a copy of the regulations of the corporate body (bylaws) and (*b*) documents relating to the appointment of the directors. The objects of the undertaking, the names and signatures of the directors, and any special provisions contained in the regulations as to the power of agency of the directors on behalf of the corporate body or as to the period for which the undertaking is to remain must likewise be included.

¹⁹ H.G.B. 377.

²⁰ H.G.B. 8-10.

²¹ Which may be different from the principal place of business.

²² H.G.B. 13.

The regulations as to proper designation of mercantile trade names for (a) a person without a partner, (b) an unlimited partnership, (c) a limited partnership, (d) a share company, (e) a limited-liability company, and (f) a partnership limited by shares are carefully set forth.²³

Notice must be given and entry made in the mercantile register of (a) any change in a firm name or in its ownership or a discontinuance of its use, (b) adjudication in bankruptcy or the setting aside, annulment, or revocation thereof, (c) the names and signatures of the liquidators and their powers, (d) removal of an establishment to a different place, and (e) every other change of facts required to be registered.²⁴

EFFECTS OF REGISTRATION

Such matriculation will only establish a presumption in favor of the individual or aggregation so registered that he or it has attained to the status of a merchant. It is rebuttable by actual proof. The matriculation is as important to the merchant as to third parties with whom he deals, for, although the third party is thereby given an opportunity of ascertaining from the public record the essential facts concerning the business of the merchant, such other party is also bound to the provisions of the documents which he may find in the registry.

The grant of authority as between a German principal and his agent is expressly limited by the registration thereof. But as against third parties the agent's power is as broad as the ordinary powers implied by German law to an agent of that type, regardless of the limitations thereupon in the registry if the third party did not know of them.

Documents and information required to be registered and not registered are not binding on third parties. But third parties may avail themselves of the facts or provisions of these documents as evidence or to enable them to sue the original parties. On the other hand, facts registered and published can be used against a third party unless he can prove that he neither knew nor should have known thereof.²⁵

REGISTRATION OF FOREIGN COMPANIES

Until recently the German courts have held that article X of the introductory act to the Civil Code refers to foreign companies which desire to establish business of a commercial or industrial nature or branches for the carrying on of such business in Germany. This article X provides: "An association belonging to a foreign state, having a legal status under its laws and unable to obtain the legal status in this country, except in accordance with the provisions of sections 21 and 22 of the Civil Code, is regarded as having legal status when the same is recognized by resolution of the Federal Council."²⁶

Under this article, taken in connection with section 23 of the Civil Code, in order to make such an application for registration and rec-

²³ H.G.B. 18, 24, 30.
²⁴ H.G.B. 31-34.

²⁵ H.G.B. 15.
²⁶ See also H.G.B. 13, 20.

ognition the foreign company must supply a certified copy of its certificate of incorporation and of its bylaws and the minutes of certain specific actions taken by its stockholders and board of directors, especially of such minutes as refer to the granting of a power of attorney to a representative of the corporation empowering him to apply for recognition in Germany. This power of attorney should be annexed to the application. All the documents must be legalized by the German consul. A certificate of the secretary of state of the state where the company has its original domicile, to the effect that the company has been legally constituted there and is still in existence, should also be filed, with a certificate of the German consul authenticating same. The company is then ready to be recognized, and thereafter its business in Germany is conducted with the same duties and obligations as an ordinary German share company.

If a branch is organized within 2 years of the date upon which the company was originally registered, then additional information must be submitted.²⁷

A foreign corporation having a branch in Germany must submit its annual balance sheet to the president of the provincial administration, and a copy must be filed with the mercantile registry at the same time. The balance sheet must also be published in the Official Gazette and, if so ordered, in other newspapers; certified copies of the minutes of the general meetings, changes in the personnel of the officers, and changes in the bylaws must be filed in the mercantile registry.²⁸

BOOKKEEPING REQUIREMENTS

Every mercantile trader must (a) keep books of account from which business done and disposition of capital are apparent; (b) upon opening of the business and annually thereafter prepare a statement, signed by all the general members, of immovable property, debts due to and by the business, cash on hand, and other assets, and a balance sheet showing assets and liabilities.²⁹

The books must be so kept that any expert can understand therefrom the business transactions and the financial situation. Share companies, limited-liability companies, and partnerships with share capital must use double-entry bookkeeping.

The entries in such books must be in a living language, with values in German currency. The books must be bound and the pages numbered consecutively; blank spaces must not be left on pages, nor may pages be torn out. The original contents of an entry must not be erased or rendered illegible.³⁰

IMPORTANCE OF KEEPING BOOKS

Fulfillment of the obligation to keep books insures that such trade books are admissible as evidence in litigation. If and to what extent they have evidentiary value depends on the free judicial interpretation of the entries therein and the methods of keeping such books. Unimportant irregularities do not necessarily weaken the

²⁷ H.G.B. 199, 201.

²⁸ Special Circular No. 332 of the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington, entitled "Company Law in Germany."

²⁹ H.G.B. 38-39.

³⁰ H.G.B. 40, 43.

evidentiary value, but the general credit to which such books are entitled depends somewhat on the manner in which they have been kept.

In litigation between two merchants, if both have kept their books in accordance with the law and the entries appearing on the books of one merchant conflict with those contained in the books of the other, then the judge of the court is by law given the right and discretion to decide the issue between such books by taking into consideration other kinds of proof which may be submitted. If, however, only one of the merchants has kept books, his books will be taken as evidence of the transaction in litigation, unless the other party can excuse his default.

A merchant is bound by the entries contained in his books and may not impeach, explain, or contradict such evidence. When an opposing party seeks to introduce evidence from the books of his adversary, he is bound by all the entries contained in those books, even though they may be unfavorable to him.

Small traders are not under obligation to keep books, nor are persons with only apparent mercantile capacity; but if a person conducts a business through another (for example, his wife), he is bound to keep books. Inability to keep books is no excuse.

In partnerships, all the partners are liable for the keeping of the books; in companies, all the directors (Vorstand). Agreements by which one of several partners or directors is to keep the books do not relieve the others from their responsibility in this regard.

Culpable failure to comply with the obligation of merchants to keep books is penalized in the event of bankruptcy or suspension of payment, as is also the keeping of books in a manner not in accordance with law or so that confusion will arise from the entries.

Although a merchant or a partner or a director is personally responsible for the keeping of the books of his business in accordance with law and the principles of good bookkeeping, he need not himself make the entries but may delegate this task to another, provided he from time to time sees that this person does so correctly and, upon such examination, he signs the entries.

INSPECTION AND EXHIBITION OF BOOKS

In the course of an action in court, the judge, upon application of either party, may order the production of the mercantile books of any party to the action. If and when the books are produced, their contents must be inspected with the assistance of the parties, but only to the extent necessary to the point at issue. In appropriate cases an extract may be taken from the books. The other contents of books produced under a court order should be exhibited to the court, but only to the extent necessary to prove that all the books of the party producing them have been kept in proper manner.

The discretion of the court decides the question whether the books are to be produced or not; but books are, as a rule, ordered to be produced only when the accuracy of certain allegations can be proven thereby, and not merely to give the other party a chance, by the inspection of the books, to put forward additional allegations.

If a party fails to comply with an order for producing books, he must take the discovery oath. If he fails to make such oath, the other party may produce copies of entries which will be binding, and any other proofs adduced by the other side will also be considered binding.³¹

PRESERVATION OF BOOKS AND CORRESPONDENCE

Mercantile traders must retain their books until the expiration of 10 years from the date of the last entry therein, and the same rule applies to inventories and balance sheets and to business letters received, copies of letters sent out, and telegrams, all of which must be kept in chronological order and with reference to some proper method of filing.³²

The obligation to keep books and to preserve documents devolves upon a person who acquires a business with its books and papers. It also extends longer than the owner's mercantile capacity, or his life in the business, or the life of the business; and it extends to his heirs, even though the heirs do not continue the business.

³¹ Z.P.O. 426-427.

³² H.G.B. 44.

II. PARTNERSHIPS AND ASSOCIATIONS

UNLIMITED PARTNERSHIPS¹

A partnership under German law is not regarded as a legal entity nor a corporate body distinct from the persons comprising it. The firm property belongs to the partners but—not in separate shares—only in joint ownership, so that each partner becomes a joint owner of the whole but not real owner of any particular portion. He is not entitled to demand distribution without the assent of the others, nor is he at liberty to dispose of his share, although a creditor may take his undivided share in pledge.²

The fact that a mercantile partnership has a distinct firm name, however, indicates that a partnership has certain rights and qualifications with regard thereto and that for certain things it operates as an identity in that it can carry on business under the firm name and obtain domicile, acquire, hold, and alienate property, and sue and be sued as such.³

FORMATION—FIRM NAME

Notice of the creation of a partnership must be inserted in the mercantile register of the court within whose jurisdiction the firm is to be domiciled, setting forth (a) the name, first name, business description, and place of residence of each partner; (b) the trade name and the place of business of the partnership; and (c) the date of the commencement of the partnership. It must be made by all the members of the firm; and the partners who are to act for the firm must send in their signatures to the court. If the firm name is changed, the domicile removed, a new partner admitted, bankruptcy commenced or disposed of in some manner, or in the event of dissolution or liquidation, the pertinent facts must be notified for registration by all the partners.

The trade name of an unlimited partnership must include either the name of at least one partner, with an addition indicating the existence of the partnership, or the names of all the partners. The names of persons other than full partners may not be inserted in the trade name of either an unlimited or a limited partnership.⁴ The effect of this limitation is to safeguard third parties who might be drawn into dealings with a partnership under a mistaken belief induced by the inclusion of a name not in the partnership or playing only an unimportant part therein. A person who allows his name to be included in a firm name thereby subjects himself to unlimited liability upon all the obligations of the firm.

¹ This subject is covered for commercial businesses in the Commercial Code, sections 105 to 177; so far as these sections do not provide to the contrary the rules of the Civil Code, sections 705 to 740, also apply.

² B.G.B. 718; H.G.B. 135. (For a list of the abbreviations used in footnotes throughout this monograph, see p. xii.)

³ H.G.B. 124.

⁴ H.G.B. 19.

LIABILITY OF THE PARTNERS

The relationship of the partners to one another depends absolutely upon the contract of partnership, which must be recorded, together with all modifying instruments. These limit and determine the partners' rights and obligations as between themselves,⁵ subject, however, to the provisions of the Commercial and Civil Codes. All limitations to be effective against third parties must be recorded.

All the members of an unlimited partnership are jointly and severally liable for the obligations incurred by the firm to the extent of their entire personal estates. Any agreement to the contrary is inoperative against third parties. Even a new partner joining is liable for the obligations of the partnership previously incurred, as is also a retiring partner to the date of his withdrawal. Any creditor of the partnership may sue any partner instead of the firm if he so desires, but he may not, conversely, sue the firm for the obligation of a partner.⁶

The contributions of the partners must be equal in value and may be paid in services or money or otherwise; and when once so paid, no partner can be compelled to contribute further to the firm's assets, even to make up losses, except when a deficit arises on dissolution, in which event the partners are called upon to contribute according to their investment and, if any cannot pay, the others are liable for his share as well.⁷

A partner is held to the same care for the business of the partnership as he shows toward his own;⁸ he is, however, responsible for gross negligence even though he is grossly negligent in regard to the conduct of his own business.

A partner acting on behalf of the partnership is entitled to reimbursement of outlays he considers necessary and also for losses he sustains as a result of transacting the business.

Claims against a partner arising out of the partnership liability become barred in 5 years from the date of the dissolution of the partnership or the retirement or expulsion of such partner; but if a creditor's claim does not fall due until after that time, the period begins on the date his claim falls due.⁹

MANAGEMENT OF UNLIMITED PARTNERSHIP

Every full partner has the implied power of agency to act on behalf of the partnership, but care must be taken when dealing with a partnership to see that this implied power has not been entirely cut off from some of the partners by the agreement of association and the registration thereof.

The affairs of a nonmercantile partnership are, in the absence of specific agreement to the contrary, to be conducted by either or any of the partners, but always with the consent of all; whereas the management and right of representation in a mercantile partnership is intrusted to those partners mentioned in the contract, and they have the sole right of management.

Such representative power is much stronger than that of an ordinary agent or procurist and extends to judicial and extrajudicial

⁵ H.G.B. 109.
⁶ H.G.B. 128, 130.

⁷ B.G.B. 707, 735.
⁸ B.G.B. 708.

⁹ H.G.B. 159.

business and all acts in law, including the alienation and pledging of real estate and the granting and recall of power of attorney; and any limitation thereupon is inoperative against third parties. This power can be withdrawn for cogent reasons upon application to and order from a court.⁹

If an authorized partner requests another to abstain from a particular transaction, the request must be complied with.

SEPARATE BUSINESS—PROFITS AND LOSSES

No partner is entitled, without the consent of the others, to transact for his own account business of the same description as that handled by his concern or to become full partner in another mercantile firm which does business of a similar kind; but he is presumed to have such permission if this connection was known to the partners at the time of the formation of the partnership and no demand was made that he discontinue.¹¹

The books of the partnership must be balanced at the end of every year and the profits and losses apportioned among the partners and entered to their accounts. Profits to the aggregate amount of 4 percent of the capital may be distributed among the partners in proportion to their interest in the firm; if the profits amount to more than 4 percent, such additional sum may be distributed as will not injure the business.¹²

TRANSFER OF INTEREST—DISSOLUTION

The transfer of an interest in an unlimited partnership is extremely difficult as a practical matter. The consent of all the other partners is naturally a prerequisite to the transfer; and when it is considered that the replacing of a partner entails the giving to the new partner the right to discharge administrative duties as well as the power to represent the firm, the consent of the other partners may be somewhat difficult to obtain. It must be remembered, too, that in admitting the new partner his financial ability to respond to the obligations of the firm must also be substituted for the responsibility of the outgoing partner.¹³ The outgoing partner, however, is obligated for a period of 5 years after his withdrawal from the firm for all obligations of the partnership contracted prior to his withdrawal.

Dissolution of a partnership is effected (a) by the passing of the time for which it was entered into, (b) by resolution of the partners, (c) by commencement of bankruptcy against the partnership or any full partner, (d) by the death of a partner (trustee takes the place of such partner),¹⁴ or (e) by notice of a partner to terminate it, enforced by judicial decree.

LIMITED PARTNERSHIPS

A limited partnership arises when one or more of the partners agrees to contribute a fixed sum, to which amount his liability is lim-

⁹ H.G.B. 126-127.

¹⁰ H.G.B. 112.

¹¹ H.G.B. 721; H.G.B. 120-122.

¹² In the transfer of the interest of a limited partner there would not be such serious objection, but even in that case the consent of the other partners would have to be obtained.

¹³ H.G.B. 146.

ited and the other partners are subject to unlimited liability.¹⁵ The general law of partnership applies insofar as sections 161 to 177 of the Commercial Code do not provide otherwise.

As in an unlimited partnership, the limited-partner relationship is created by and depends upon the contract of association, which must be notified to the mercantile registry and should contain, besides the requisites of an unlimited partnership, (a) the signatures of the limited partners and (b) the amount of the agreed contribution of each of them to the partnership capital.¹⁶

The trade name of a limited partnership must include the name of at least one of the general partners, with an addition indicating the existence of a limited partnership. The names of persons not full partners may not be included.¹⁷

The contribution of a limited partner must be expressed in money but need not be paid in money; when it is not paid in money, the limited partner is discharged from further liability for contribution as against partnership creditors only insofar as the actual value of the property given to the partnership by him corresponds to the amount he agreed to contribute. The limited partner may be called upon at any time to contribute that part of the agreed amount of his contribution still remaining unpaid. If a limited partner receive a distribution of profits in any year, he cannot be called upon to pay such amount back to make up the firm's capital if in later years a loss is sustained.¹⁸

Claims against a partner arising out of the partnership liability become barred in 5 years from the date of the dissolution of the partnership or the retirement or expulsion of such partner; but if a creditor's claim does not fall due until after that time, the period begins on the date his claim falls due.

Limited partners are excluded from the conduct of the partnership business. They do not have the right to forbid any transaction being entered into by authorized partners; but they do have the right to receive a copy of the annual balance sheet and to test its correctness by inspection of the books of the firm.

The death of a limited partner does not bring about a dissolution of the partnership.¹⁹

SILENT PARTNERSHIPS

The silent partnership (*stille Gesellschaft*) owes its general set-up to the exigencies and prejudices of conducting business in the Middle Ages, during which period this form of mercantile organization came into being and obtained recognition. Many persons had funds for investment but lacked the inclination or the ability to conduct an enterprise of their own; and, too, the engaging in business was looked upon with disfavor. They desired, and required, compensation for the use of their money, but were hampered, by the strict usury laws of the time, in exacting for their capital investments payments that could be considered an adequate return. The silent

¹⁵ H.G.B. 161.

¹⁶ H.G.B. 162.

¹⁷ H.G.B. 19. If the name of a limited partner does appear in the firm name, he becomes liable as a full partner.

¹⁸ H.G.B. 169.

¹⁹ H.G.B. 177.

partnership provided the opportunity sought, because it gave to the investor as compensation a portion of the profits of the business. It also gave to the merchant with insufficient capital a means for financing his business needs.

FORMATION—FIRM NAME

Any person desiring to contribute²⁰ property to a business in which a mercantile trade is carried on by another may do so by making his contribution the property of the owner of such business. Thereafter the owner alone acquires rights and incurs obligations with respect to such contribution in the same manner as he does with regard to his own property in the business.²¹

To effectuate an arrangement of this kind the parties must enter into a memorandum of association (in the same manner as in an ordinary partnership) regulated by the provisions of the Civil Code.²²

A mercantile trader who carries on a business with a dormant partner must use as his trade name his surname and at least one of his first names without abbreviation and with no addition (except to differentiate him from another of the same name) which would make it appear that he is trading in a partnership or which would otherwise be calculated to give a misleading impression that he is trading otherwise than by and for himself. This trade name must be notified to the mercantile register in the district in which the head office of the business is located and in all places where branches are established.²³

LIABILITY OF THE PARTNERS

The most important item in a silent partnership is the liability to be assumed by the dormant partner and his share of the profits or losses. In the absence of express stipulation in the memorandum of association, the dormant partner shares in both profits and losses in a proportion which is reasonable according to the circumstances. If only the dormant partner's share of the profits is fixed, he is impliedly responsible for the losses to the same extent; and conversely.²⁴

As a general rule, however, it is provided in the memorandum of association that he share in the losses as well as the profits; but the dormant partner may be freed from any liability for losses by the memorandum. This latter provision is possible even as against third parties,²⁵ because the dormant partnership is conducted in the name of the owner alone, without any change in the registered form of the business, and no representations are made that anyone other

²⁰ It is not necessary that the property should be actually turned over at once. It is enough that it be placed at the disposal of the owner of the business (Imp. C.C. vol. 54, p. 280). The dormant partner is liable, however, for his contribution as though he had sold it to the business (B.G.B. 445, 493). Such contribution may consist of an advance of capital made up of cash, things, rights, or other objects of value, but not mere services.

²¹ H.G.B. 335.

²² B.G.B. 705.

²³ H.G.B. 18, 29-30.

²⁴ B.G.B. 722.

²⁵ The rights of third parties are not prejudiced when an owner enters into a dormant partnership. They are actually strengthened, in that the assets of the owner in his business are enlarged to the extent of the contribution, without the assumption of any additional obligation by him except for a charge against the profits.

than the owner is interested in the business.²⁶ The dormant partner cannot be called upon to increase his contribution or to return profits already paid him unless the accounts were erroneous and the payment unjustified.²⁷

MANAGEMENT OF SILENT PARTNERSHIP

In the absence of express stipulation, the management of the business is continued by the owner, and the dormant partner is entitled only to insist that the business shall be carried on properly; but the authority to manage the business can be granted to the dormant partner by the memorandum of association, contract of employment, or power of attorney.²⁸

Each partner is required to display, in the performance of the obligations resting upon him, the same care he is accustomed to use in the conduct of his private affairs, and he will be liable for gross negligence.²⁹

SEPARATE BUSINESS—PROFITS AND LOSSES

The owner of the business may enter into other dormant partnerships unless this is forbidden in the memorandum of association; but he may not engage in a rival business.³⁰ The dormant partner, however, may do so.

At the close of every business year a profit and loss account must be drawn up and the dormant partner's share in the profits paid to him. He may demand a copy of the annual balance sheet and test its correctness by an inspection of the books; and if this privilege is not granted to him, he may enforce his right by court process unless the memorandum of association provides otherwise. Any provision limiting this right is ineffective where there is reason to believe that the business has been dishonestly conducted.³¹

TRANSFER OF INTEREST—DISSOLUTION

While the dormant partnership continues, the owner of the business may not transfer his interest to another without consent; but this prohibition does not apply to a claim for a share in the profits or what may be found due to either partner upon the winding up of the business.³²

A dormant partnership is terminated (*a*) by the lapse of the time for which it was entered into, (*b*) by agreement of the parties, (*c*) by the death of the owner of the business unless there is a provision to the contrary, (*d*) by the bankruptcy of either party, (*e*) by six months' notice given by either party before the end of any business year to terminate it at the end thereof or like notice given by the creditor of any partner, (*f*) immediately for cogent reasons, or (*g*) by the object for which the partnership was formed being attained or found to be impossible of attainment. It is not terminated by the death of the dormant partner.³³

²⁶ H.G.B. 336.

²⁷ H.G.B. 337; B.G.B. 812-814.

²⁸ B.G.B. 174-175; Imp. C.C. vol. 31, p. 30.

²⁹ B.G.B. 277.

³⁰ B.G.B. 157.

³¹ H.G.B. 337-338; B.G.B. 716.

³² B.G.B. 717.

³³ B.G.B. 723, 726-728; H.G.B. 132-133, 339.

Upon dissolution of the business the owner must proceed with the distribution of assets and pay to the dormant partner his share in cash. The latter can enforce this right to payment only after the period for making up the accounts has expired, and then only by suit for what is due him (if he is able to prove the amount) or for an accounting and payment thereupon according to the provisions of section 254 of the civil practice act.³⁴

In the event that bankruptcy is commenced against the owner of the business, the dormant partner may prove his claim as a creditor for the amount of his contribution to the business, but only to the extent that such amount exceeds the share of the losses with which he is chargeable. If he is in arrears, however, in the payment of his contribution or any part of it, the trustee can enforce payment in an amount sufficient to cover his share of the losses.³⁵

Any payment to the dormant partner within the year preceding the declaration of bankruptcy by or against the owner of the business (other than upon a distribution of profits properly made) is subject to impeachment proceedings by the trustee in bankruptcy for its recovery.³⁶

ASSOCIATIONS

RECOGNIZED ASSOCIATIONS

Associations in Germany may be commercial or noncommercial. A further distinction is made between the associations themselves—those registered and recognized (Vereine) and those not registered and not recognized (Gesellschaefften).³⁷

Recognized noncommercial associations obtain legal status³⁸ by inscription in a register of associations in the court of first instance (Amtsgericht) having jurisdiction, whereas recognized commercial associations obtain legal status through confirmation by the State where the association is located, in cases where there are no special provisions of the Federal law.³⁹ They are juristic persons.

Recognized commercial associations have their situs where the place of management is located. They have constitutions, and they have governing bodies (composed of several members) which represent them in court and in business relations, with powers defined by their bylaws—which powers and limitations are effective against third parties.⁴⁰

The governing body is appointed by resolution at a meeting of the members of the association. Affairs of the association not within the powers of the governing body are regulated by resolutions passed at the regular meetings, on due notice, by a majority of the members or by agreement of all the members in writing. A change in the bylaws of the association requires the assent of two thirds of all the members, and a change in its purposes requires the assent of all. Such change in the bylaws or purposes of the association requires

• H.G.B. 340.

• H.G.B. 341.

• H.G.B. 342.

• B.G.B. 21-22.

• A registered association obtains its rights and obligates itself in accordance with sections 53 to 79 of the Civil Code, which rights include the right to sue and be sued as an association.

• B.G.B. 23.

• B.G.B. 24-26.

confirmation by the Federal Council or the State which conferred legal status.⁴¹

Dissolution requires a three-fourths majority vote of all members. But it is also possible to effect dissolution by law (*a*) when the resolutions or acts of the governing body are unlawful or (*b*) when the association operates without the scope of its avowed purposes. When an association is dissolved, its property vests in the persons designated in its bylaws or equally in all the members. A liquidation must be made by the managing body after public notice, and all of the members of the board must concur in every step. Distribution on liquidation cannot be made until one year from the time of notice.⁴²

Such an association also loses its status if it is adjudged bankrupt. If the managing board delay in the application for bankruptcy, the members of the board will be held liable as co-debtors with the association.⁴³

NONRECOGNIZED ASSOCIATIONS

Nonregistered associations are not recognized as legal entities, although they have come to possess a sort of recognition and their members enjoy certain rights and are obligated to certain duties somewhat parallel to those of partners. They can be sued but cannot sue, and judgment against them is enforceable against their property. In transactions in the name of the association with a third party, the person acting for the association is personally liable; and if more than one acts, they are jointly and severally liable.⁴⁴

Classed with nonrecognized associations, because the limitations upon their rights and privileges are similar to those imposed upon nonregistered German associations, are those branches of foreign companies which do not fulfill the requirements for obtaining legal status in Germany. (See, however, discussion on pp. 6 and 9.)

⁴¹ B.G.B. 27, 33-34.

⁴² B.G.B. 41, 43-44, 51.

⁴³ B.G.B. 42.

⁴⁴ Z.P.O. 735-736; see also B.G.B. 705.

III. COMPANIES

SHARE COMPANIES

The German share company, or Aktiengesellschaft, corresponds in its essential elements to the private corporation in the United States more closely than does the German limited-liability company. (The points of difference between the two types of German companies are summarized on pp. 54 and 55.)

The share company has a common fund or capital, contributed by shareholders and available for the purposes of the company.

It has a firm name and juristic personality under which it acquires, holds, and disposes of property, conducts its business, and can sue and be sued.¹

It has shares which are issued to subscribers according to the amounts of their subscriptions and which fix the proportionate interests of the subscribers in its capital. The holders of its shares are not entitled to any part of its property (except in the event of liquidation), but only to an interest in its net profits as shown on the annual balance sheet. They may dispose of such shares in the absence of provisions to the contrary. Shareholders are subject to liability for the acts of the corporation only to the amount of their fully paid subscriptions to capital.²

It has a business which is conducted by a board of directors (Vorstand), whose acts are supervised by a board of supervisors (Aufsichtsrat). Neither the directors nor the supervisors are personally liable so long as they act properly in the interest of the company and in its name according to the law, the provisions of the charter, and the resolutions of the shareholders.

It is presumed to be a full mercantile company, but its business is commercial only when it carries on some mercantile trade.³

Its duration usually is fixed by its charter⁴ and is not affected by the duration of the lives of those who organized it.

FORMATION

MEMORANDUM OF ASSOCIATION (CHARTER)

For the formation of a German share company not less than five organizers are necessary. They may be natural persons, partnerships, or other companies, domestic or foreign, or the representatives of any of them so long as they have the power to bind those they represent. They may even be straw men.⁵

¹ H.G.B. 20, 210. (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

² H.G.B. 211.

³ H.G.B. 6, 210, 343-344.

⁴ H.G.B. 292.

⁵ After the company has come into existence, everyone is estopped from alleging that the acceptance of shares was only apparent or by mistake, fraud, or duress. The parties who have accepted the shares are liable as shareholders thereafter. Whether the founders accept the shares for themselves or for others is immaterial. Even straw men who accept the shares are held to be founders and assume all the rights and obligations of such upon the shares which they accept.

They draw up a memorandum of association (*Satzung*) subject to the provisions of the Civil Code⁶ dealing with associations, and this must be certified by notarial or judicial act.

The memorandum of association or charter must specifically set forth (*a*) the name and domicile of the company, (*b*) its objects, (*c*) the methods of appointing and constituting the board of directors, (*d*) the way in which general meetings may be called, (*e*) the form in which public notices are to be given by the company, and (*f*) the amount and type of shares subscribed.⁷

If the subscriptions are paid otherwise than in money, the charter must set forth the facts upon which the value fixed to cover such subscriptions or property was based. It must also show business already done for the company with a view to gain and the prices paid for stock of other companies. Where a business is to be transferred to the company, the results of its operations during the last 2 years must also be shown.⁸

The charter constitutes an agreement between the founders and the shareholders, and every deviation or change not expressly set forth therein is invalid against the company. The founders may themselves become responsible to claimants for other representations made to induce them to purchase shares. Every special right granted to particular shares also must appear in the memorandum of association, and likewise the different rights of different classes of shares, especially as to the division of profits and distribution of the company property.⁹

If the charter does not mention the above essential provisions, any shareholder, director, or supervisor may ask the court to issue a writ to declare the company a nullity; but certain defects may be rectified by the resolution of a general meeting summoned by public notice in the journals in which the notices of the company must appear.¹⁰

FIRM NAME

The trade or firm name of a share company usually bears a reference to the object of the undertaking but must in every case include the designation "Aktiengesellschaft" (or the abbreviation "A.G."). The directors must furnish (to the court in the district of its domicile) a statement of the name and the address of the head establishment for entry in the mercantile register.¹¹

"Every new trade name must be clearly differentiated¹² from all trade names already existing at the same place or in the same communal district and entered in the mercantile register. * * * If in a place or communal district where it is desired to institute a branch establishment the same trade name has already been registered, an addition * * * must be introduced into the trade name registered for the branch establishment."¹³

⁶ B.G.B. 705.

⁷ H.G.R. 182, 185.

⁸ H.G.B. 191.

⁹ H.G.B. 185-186.

¹⁰ H.G.B. 309-310.

¹¹ H.G.B. 29, 33.

¹² The trade name when registered becomes the exclusive right of the company. It cannot be adopted by another. "Clearly differentiated" is interpreted to mean difference in language and sound so distinctive that it is apparent with ordinary attention (R.G. vol. 20, p. 72).

¹³ H.G.B. 30.

DOMICILE

The fixing of the domicile of a share company is necessary to establish the place at which it may sue and be sued. The domicile as given in the charter is the "seat" of the company¹⁴ and is regarded as the seat of the chief establishment of the company even though it has in fact no establishment there. All other establishments of the company are considered branches. If there are independent branches, the company may also sue and be sued at these other locations—but only in connection with business transacted there.

If the charter provides otherwise, general meetings of the shareholders need not necessarily be held at the domicile of the company. They may even be held in foreign countries. The required publication of notices, however, must take place at the domicile.

DURATION

There is no specific limitation upon the life (*Zeitdauer*) of a company. Since the code provides that the dissolution of a company is effected "by the lapse of the time for which it was formed"¹⁵ the duration of a company must, by implication, be fixed for a definite period. (Ninety-nine years has been used.) When fixed by the charter, it must be registered.¹⁶

The duration of a corporation can be extended in the same manner as other alterations in the charter are effected. Because its change or extension may defeat shareholders' rights to a proportionate distribution on liquidation, however, such action requires the consent of all the shareholders, unless otherwise provided.

SUBSCRIPTION TO SHARES

The founders may take all the shares, in which case they must constitute the first board of directors (*Vorstand*) and the first board of supervisors (*Aufsichtsrat*). This procedure is known as "Simultangruendung."¹⁷

Formerly the founders were not compelled to subscribe for all the shares, but the remainder could be subscribed to by the public, before the association could be actually formed.¹⁸ A general meeting was then necessary to elect the directors and supervisors, and thereafter the court called a second general meeting to adopt the resolutions for the formation of the company.¹⁹ This form of incorporation was known as "Successivgruendung."²⁰ These provisions were removed by the amendments of September 19, 1931 (*Verordnung des Reichspräsidenten ueber Aktienrecht u.s.w.*), published in *Reichsgesetzblatt* No. 63 of 1931, pages 493 to 501.²⁰

EXAMINATION AND REPORT

All the members of the *Vorstand* and of the *Aufsichtsrat*²¹ must examine all steps leading to the formation of the company as to (a)

¹⁴ H.G.B. 189.

¹⁵ H.G.B. 292.

¹⁶ H.G.B. 33, 198.

¹⁷ H.G.B. 190.

¹⁸ H.G.B. 189.

¹⁹ H.G.B. 196.

²⁰ Subsequent references in this chapter to "recent amendments" are to this law.

²¹ Where one of these has a special interest in the formation of the company, someone chosen by a body officially representing the commercial profession or the court of domicile of the proposed corporation must act as examiner for him (H.G.B. 192).

accuracy and completeness of the statements made by the founders regarding offers to subscribe and contributions to capital,²² (b) the particulars set forth in the memorandum of association, (c) the prices paid for property and the previous transactions which led to the acquisition of property by the company, and (d) whether there is doubt as to the adequacy of the amounts set apart to represent what has been contributed or taken over by the company.²³

The results of the examination must be reported in writing, copies furnished to commercial organizations, and the original held open to public inspection.

If upon examination differences of opinion arise between the official examiners (see footnote 21, p. 23) and the founders, the commercial body which appointed the official examiners decides. The certificate of examination must not be issued until the founders and the examiners agree or the founders accept the decision of the commercial body which appointed the examiners.²⁴

NOTIFICATION TO THE COURT

All the founders, Vorstand, and Aufsichtsrat are required to notify the court of the district within which the company has its principal domicile of its formation, that such fact may be registered in the mercantile register.

The notice must be accompanied by²⁵ (a) the memorandum of association, including a statement of the kind of shares to be issued and the amounts which the founders will take; (b) if money is not to be paid for the shares, the contracts by which the amount of compensation is fixed and all other contracts and arrangements already carried out to effectuate such contracts, together with costs to the company for its formation and fees paid therefor, their character, and to whom paid; (c) the documents relating to the appointment of the Vorstand and the Aufsichtsrat; (d) the report of the findings and the results of the examination by the Vorstand and the Aufsichtsrat, together with the documents upon which such examinations are based and, where the examination was made by official examiners, proof that a copy of their findings has been sent to the commercial chamber which appointed them; (e) where the objects of the undertaking require the authorization of Federal States, the certificates of such authorization; and (f) the signatures of all the members of the Vorstand for registry with the court.

The notification must also set forth that the amount represented by subscriptions upon shares has been paid in cash and is now in the control of the directors²⁶ except where payment in another way

²² As the old German law required that, where a contribution was made to the capital of the company other than money, a special examination be made and the results thereof published, the founders of a company often made their initial contributions in cash and thereafter substituted the contribution other than money, because the old law did not require subsequent contributions to be subjected to special examination. Under recent enactments every contribution to the capital of a share company other than money now requires a special examination, and the validity of any subsequent contribution other than money depends upon the consent of a general meeting, and the requirements for examination, report, notification to the court, registration in the mercantile register, and publication thereof must be fulfilled.

²³ H.G.B. 193.

²⁴ H.G.B. 194.

²⁵ The documents must be the originals or certified copies.

²⁶ Under the old law the 25 percent was deposited but later withdrawn; this is no longer permitted. The entire sum must now be put definitely at the disposal of the Vorstand and retained by it as part of the company capital.

is fixed. The issue value of the shares and the amount paid in cash for each of them must also be given. At least one fourth of its nominal value must be paid on each share. When the shares are to be issued at a premium, the 25 percent must be paid on the total.²⁷

Recently power was given to the courts to refuse registration, especially if the examination report is unsatisfactory.

REGISTRATION

After the notification to the court the directors must apply for registration of the company in the mercantile register at its domicile. For this purpose certified copies of the memorandum of association and the other documents must be filed. Registration must also be effected wherever branches of the company are formed.²⁸

In registering a company the firm name and seat of the company, the objects of the undertaking, the amount of capital, the date on which the charter was concluded, and the names of the members of the Vorstand must be given; and if the charter contains special clauses concerning the declaration of the company or the powers of the directors or of the liquidators, these statements also must be registered.²⁹

German branches of foreign corporations must also furnish proof of the legal existence of the parent corporation and that its objects have been approved for Germany.³⁰

A company acquires juristic personality only after registration. Prior thereto it has no existence.³¹ It is merely a society without legal capacity, but it can have rights and liabilities for things done to bring it into legal existence.³²

PUBLICATION

After registration, the Vorstand must insert notice of the organization of the company in the publications specified in the charter.³³ There must be set forth the particulars required for registry and the particulars concerning the charter, the amounts for which the shares are issued, the names, occupations, and addresses of the founders and of the members of the board of supervisors (Aufsichtsrat), a statement as to the result of the examinations (when official examiners have been called in to make the audit),³⁴ and certificate that the report of such examination was filed.

INTERESTS IN THE COMPANY

CAPITAL

The capital of a share company must be at least 50,000 marks; otherwise it is not limited. Because of organization taxes, the cap-

²⁷ H.G.B. 195.

²⁸ H.G.B. 201.

²⁹ H.G.B. 198.

³⁰ H.G.B. 201.

³¹ H.G.B. 200. If any transaction is attempted in the name of the company before registration, the person so doing is personally liable; and if there be more than one person, they are jointly and severally liable. Share rights cannot be transferred as against the company before registration, nor can shares or intermediate certificates be issued. If issued, they are void.

³² Imp. C.C. vol. 32, p. 98, and vol. 58, p. 56; unless the charter provides that such acts must be expressly confirmed by the charter (H.G.B. 186).

³³ Publication in the Reichsanzeiger is obligatory; usually another paper is specified also.

³⁴ H.G.B. 199. German branches of foreign corporations must insert in the Reichsanzeiger all notices the home corporations may be required to publish in the press of their own country.

ital at the outset should be fixed as low as possible,³⁵ but should be made commensurate with the declared objects of the corporation. Determination of the amount of capital required may more easily be made after experience in the actual operation.

The amount of capital is fixed by the articles of association, and the sum to be paid up on organization (registration) must be at least one fourth of the nominal value of the shares. If shares are issued at a premium, the 25 percent must include the sum in excess of the nominal value.³⁶

Only payments made in German currency are considered as cash.³⁷ Where the contribution or payment is made in property, however, the property is valued at the values fixed in the charter and considered cash.

SHARES

Subscribers to shares of a share company are liable only to the extent of their commitments for the shares which they have purchased. They have no personal liability other than for payment of the nominal value of such shares plus the premium, if any, agreed to be paid at the time of sale.³⁸

The capital, as fixed by the charter, is divided into and represented by shares of equal value,³⁹ in denominations of not less than 100 marks. "No par value" shares are unknown in Germany. The shares themselves may not be divided, but one certificate may be issued for any number of shares of one kind. They represent aliquot parts of the aggregate capital.

They may be issued to bearer or to a named person, but bearer shares may not be issued until fully paid. No shares or intermediate certificates may be issued for less than the nominal value. If issued for less, or prior to registration of the company, they are void, and those who issued them are liable for any loss occasioned the holders.⁴⁰

Shares issued to a named person can be transferred only with the consent of the company, as installments may later become due on them. This limitation on transfer must appear on the face of the certificate, together with a notice of the amount already paid.⁴¹

Bearer shares must be registered in the appropriate stock books of the company. The name, address, and occupation of the holder are entered. Such shares may be transferred without the company's consent by mere endorsement in the absence of provision to the contrary, except where shareholders are liable for periodical contributions other than money. When transfers of bearer shares are made, the company should be notified for recording in its stock-transfer book, to enable the transferee to receive dividends and

³⁵ Where a corporation is undercapitalized and is financed by loans (as may often be the case with German subsidiaries of foreign corporations), the tax authorities may attempt to charge an additional corporation-organization tax on the basis of the capital actually required, unless it can be proven that such loans are in reality made, that interest is paid thereupon, and that they vary from time to time in amount and are paid.

³⁶ It is not sufficient that 25 percent of the company capital (plus the premiums for which the stock is issued) has been paid; 25 percent at least must be paid by each holder for every share subscribed.

³⁷ H.G.B. 195.

³⁸ H.G.B. 178.

³⁹ Unless they be of more than one kind, in which case each kind may have a different value; but the shares of each kind must have the same value.

⁴⁰ H.G.B. 179, 184, 209.

⁴¹ H.G.B. 179-180.

notices. No person is regarded as a shareholder except the registered holder.⁴²

The charter may also provide different classes⁴³ of shares conferring upon the holders different rights (*a*) as to voting, (*b*) as to priority of payment upon distribution of assets, (*c*) as to division of profits, or (*d*) as to cumulation of dividends.

For a time, due in large measure to the influx of foreign capital into German industry, plural-voting shares were very popular (ratios running as high as 100 votes or even 1,000 votes to 1). These plural-voting shares were frequently held either by the board of supervisors (Aufsichtsrat) or by other local investors directly interested in the company. However, the tendency now is to limit, so far as possible, the issuance of shares with greatly disproportionate voting power.⁴⁴

Recent amendments to the company law permit a share company, in the ordinary course of its business, to acquire its own shares or to take them as a pledge up to 10 percent (or less if so fixed by the Government) of its capital to prevent loss or injury to the company. When it acquires shares, it may neither vote them nor receive dividends thereon. Shares may be amortized only in accordance with charter provisions.⁴⁵

In some instances the German competitors of foreign-owned German subsidiaries operating German factories, employing German labor exclusively, have used the foreign ownership of the capital to prejudice the customers of the subsidiary. To obviate this possibility, some owners of such subsidiaries have found it expedient to designate a bank in their own country as trustee for the stock, which bank in turn nominated a German bank as trustee, the foreign ownership of the stock of the subsidiary thus not appearing in the registers.

The certificates of stock are not, properly speaking, shares; they only represent shares. There is no provision as to form. However, the certificates must provide for endorsement. Signatures appearing on them may be affixed by mechanical means.⁴⁶

Shares or dividend warrants, if lost or destroyed, can be canceled by public notice, unless the charter provides otherwise. Dividend warrants go with the shares and are canceled with them. If shares or dividend warrants are damaged or defaced, they may be replaced by the company on payment of the expense. The replacements are not liable to stamp duty.⁴⁷

DIVIDENDS AND RESERVES

So long as a share company is in existence shareholders are not entitled to a distribution of the company's property, but only to participation in the profits of the business shown on the annual balance sheet insofar as this distribution is not prohibited by law or by the charter. Interest in the profits is further determined by

⁴² H.G.B. 212, 222-223.

⁴³ Different kinds of shares may also be created by alteration of the charter; but in so doing the fundamental principle of equality of rights of shareholders should not be violated. In fact, no change of the charter will be allowed which tends to oppress the minority (R.G.B. 138).

⁴⁴ H.G.B. 185.

⁴⁵ H.G.B. 226-227.

⁴⁶ H.G.B. 181.

⁴⁷ H.G.B. 228-230; B.G.B. 799-800; Z.P.O. 946-1003; stamp law, sec. 5.

the proportionate amount of shares held in each class upon which dividends are declared.⁴⁸

Ordinarily German corporations have only one class of stock, and shareholders are entitled to at least 4 percent per annum upon payments already made on their shares. If, however, after setting up the reserves provided by law and the charter the profits are not sufficient, the percentage is on a lower basis. Other methods for the division of profits (especially where there is more than one class of shares) may be provided by the charter.⁴⁹ The shareholders, by a resolution of a stated majority, authorize the distribution of the profits recommended to them at general meetings by the board of supervisors. Any agreement to pay a fixed percentage is not permitted; a fixed rate may be guaranteed during the formation of the company, but the charter must specify the time limit.

Directors who allow the payments of dividends unlawfully (without reference to the balance sheet or upon fraudulent balance sheets) or in excess of the net profits are personally, jointly and severally, liable.⁵⁰ The company cannot demand repayment of dividends already paid unless such payments were in violation of the code.⁵¹

Profit warrants (*Genussscheine*) may be issued with the shares, providing for payments either out of the reserves of the company in years when no dividend is earned or from profits only.

A reserve fund must be created, in which must be deposited, until the fund equals one tenth of the company capital (or more, if so provided in the charter): (a) At least one twentieth of the net profits in each year; (b) all premiums received from the sale of shares, less costs; and (c) any sums paid by shareholders for preferential rights if the capital is not increased, unless such sums are written off to cover losses.⁵²

RIGHTS AND LIABILITIES OF THE PARTIES

SHAREHOLDERS

The German law with regard to the formation and subsequent administration of the affairs of a share company are framed to minimize the possibility of fraud against prospective shareholders. This is accomplished by the exhaustive examinations and the publicity required regarding all acts of the company and the individual responsibility imposed on all parties (especially founders, directors, and supervisors) in connection with their acts and statements for the company.⁵³

Resident shareholders.—Resident shareholders are liable only to the amounts of their interest in the company, which is fixed by the nominal or par value of the shares subscribed for;⁵⁴ if shares are issued at a premium, the liability extends to the issue price. Additional obligations other than money (for example, periodical services) may be imposed upon shareholders by the charter.⁵⁵

⁴⁸ H.G.B. 213-215.

⁴⁹ H.G.B. 214.

⁵⁰ H.G.B. 241.

⁵¹ Claims of this kind may only be urged by the company within 5 years from the payment thereof (H.G.B. 217).

⁵² H.G.B. 262.

⁵³ See articles by Dr. Jur. Carl G. Grossman in the *Panel* (New York) for May and June, 1932.

⁵⁴ If shares are fully paid, the owner cannot be called upon for additional contributions.

⁵⁵ H.G.B. 211-212. For such additional duties, the shareholders may be paid the value thereof (H.G.B. 216).

The original subscriber and subsequent holders of shares are liable severally for any unpaid balance due on shares until 2 years after divested of such ownership, any agreement between the parties to the contrary notwithstanding.

When shares not fully paid are issued, the company may call for the balance as and when required unless a time for payment is fixed in the subscription certificate. The holder of the shares must pay promptly.⁵⁶ Interest accrues on all installments after the date on which they were due. Damages and penalties also may be collected for nonpayment or delay in payment when the charter so provides.⁵⁷

If upon notice there is failure to pay any installment, an additional published notice must be given wherein a time (not less than 1 month) must be fixed within which payment must be made or the shares forfeited. If upon the expiration of the time limit the installment is still unpaid, the company may cancel the shares, and the parties are thereafter excluded from rights therein.⁵⁸ The canceled shares are then sold at public auction. The defaulting shareholders, however, still remain liable for damages for nonpayment as well as for future calls, and also for the expenses of the sale and interest; against which is set off the amount received from the sale of the shares.⁵⁹ This liability extends for 2 years after a transfer and to all predecessor holders, any one of whom may pay upon call. If one does so, the shares are transferred to him, and he is entitled to a new certificate.⁶⁰

A shareholder who knowingly uses a false certificate of deposit to vote (see footnote 85, p. 34) or who without authority votes shares of another is criminally liable. A shareholder who agrees to use his vote in a certain manner for a consideration also is criminally liable, as is likewise the person who offers the consideration to him.⁶¹

A shareholder is not entitled to a refund of his subscription unless the company is not formed, in which case he has a claim against the founders but not against other persons.

Shareholders control the administration of the business of the company through the election of the board of supervisors (Aufsichtsrat). At the general meetings they may review the acts of their elected representatives, but otherwise they have no voice in the conduct of the business. They have, however, the right to intervene in the affairs and management of the company by passing resolutions at the special meetings.⁶² (See "General meeting" at pp. 33 to 35.)

Shareholders also have certain other rights which cannot be curtailed—(a) the right to vote at general and special meetings, (b)

⁵⁶ The liability of a shareholder to pay installments does not cease upon bankruptcy of the company. The trustee enforces this obligation, and the only defense which a shareholder may interpose is that the payment is unnecessary to meet the claims of creditors (H.G.B. 311; Imp. C.C. vol. 45, p. 155, and vol. 51, p. 38). The liability of the shareholder to render periodic services other than money ceases, but revives if a general meeting of the company resolves on the continuance of the business.

⁵⁷ H.G.B. 218.

⁵⁸ In the event of suit by a shareholder to recover canceled shares, the Vorstand need only prove that it has given adequate notice by publication and proper warning in accordance with the provisions of the charter and the law to free itself of the liability to respond in damages. The company is not in any case liable in such a proceeding.

⁵⁹ H.G.R. 219-220.

⁶⁰ On single shares owned by more than one party, all the parties are jointly liable and can only vote through an agent representing all of them, and notice to any one of them is notice to all (H.G.B. 225).

⁶¹ H.G.B. 316-318.

⁶² H.G.B. 250.

a proportional interest in the distribution of net profits, (c) the right to restrain the Vorstand and the Aufsichtsrat from releasing company debtors without payment, (d) the right on dissolution to have the assets distributed as provided for in the charter, (e) the right to oppose proceedings objected to,⁶³ (f) the right to have a matter declared invalid,⁶⁴ (g) the right to equality of treatment with other shareholders of the same class, and (h) the right to transfer their shares subject only to the provisions of the charter.

Recent amendments to the law give minority shareholders new rights to have transactions examined and to bring suits against the Vorstand and the Aufsichtsrat. Minority shareholders owning at least one tenth of the capital stock may request the court to appoint accountants if they do not have confidence in the examiners appointed by the general meeting. Suits against the Vorstand and the Aufsichtsrat for damages for failure to comply with the law may be demanded by a majority of the shareholders or even by a minority representing 10 percent⁶⁵ of the shares of the company if suit is commenced within 3 months after the meeting.⁶⁶

Nonresident shareholders.—The German law imposes no restrictions—not even an extra tax—on the sale of shares abroad. No discrimination against foreigners is permitted under article 276 of the Treaty of Versailles. Voting at general meetings by proxy is permitted if written and duly authenticated.

FOUNDERS

Founders and other persons attempting to transact business in the name of a company are jointly and severally liable for acts executed prior to the final organization (registration). Those who issue shares or interim certificates before the company is registered are also liable to the holder for any damage caused thereby. If a company is not formed, the expenses of promotion are borne exclusively by the founders, without recourse against subscribers. The founders of a de facto company are also unlimitedly jointly and severally liable with the directors for all sums received for shares and for the debts of the company or damages to third parties for nonperformance of the obligations contracted in the name of the company.⁶⁷

The founders are jointly and severally liable to the company (a) for the accuracy of statements made by them respecting offers to subscribe for shares and payments made thereon,⁶⁸ (b) for all statements regarding the consideration paid for shares (where payment

⁶³ H.G.B. 271. Within 1 month of its passage a shareholder may impugn the validity of any resolution of a general or special meeting by an action at law, the company being defendant. If the verdict is in favor of the company and it is damaged by the suit, the shareholder bringing the action must indemnify it (H.G.B. 271-273).

⁶⁴ H.G.B. 309.

⁶⁵ Under the new amendments the 10 percent required is reduced to 5 percent when the report of the examiners indicates a possibility of mismanagement.

⁶⁶ H.G.B. 269-270. Under the old law it was difficult to carry out successfully such minority action, as the stock of the minority shareholders (and the additional security fixed by the court) was required to be deposited during the entire course of the lawsuit. This burden often made it impossible for the minority to proceed. Under the new law the additional security is demanded only under special circumstances, and the court may return the minority shares before the end of the litigation. The minority is liable to the company for the costs of proceedings instituted at its insistence.

⁶⁷ H.G.B. 200, 209.

⁶⁸ Founders and other persons who within 2 years of the registration of the company offer shares for sale are jointly liable for the incorrectness of statements made by them, provided they knew of the incorrectness or should have known of it by the exercise of the diligence of careful business men (H.G.B. 203).

is made otherwise than in cash) and concerning contracts preferential to certain shareholders, (c) for losses sustained by falsely reporting capital subscribed and payments for shares falsely stated to have been made, (d) for all losses sustained by the company through the insolvency of a subscriber for shares, (e) for any promotional expenses paid but not thereafter allowed by the company, and (f) for loss occasioned by reckless dealings of any of them concerning contributions to capital and purchase of plant.⁶⁹ Actions on claims so arising are instituted by resolution of a general meeting and may be instituted by a minority representing only one tenth of the company capital.⁷⁰

The founders may also be liable to the shareholders and creditors of the company if their relationship with any of these parties in connection with their transactions cause an injury recognized by German law.

Founders are criminally liable who knowingly give false information for registry or for publication with regard to subscriptions or the payment of the original capital, the price at which shares were issued, or as to the acquisition of the plant of the company.⁷¹

DIRECTORS

Directors (Vorstand) are liable to the company for due observance of the limitations on the scope of their power of agency as imposed by the charter or the resolutions of general or special meetings. They are not excused if they carry out a resolution of a meeting which might subject them to criminal punishment or to the liability to pay damages to creditors; in these circumstances they must apply to the courts to impugn the resolution.⁷²

They may not, without the consent of the company, carry on business for themselves or for a third party in the same line of trade as that in which the company is engaged, nor may they be interested in a mercantile enterprise as a general partner. If they violate this provision, they are liable to the company. They must obtain the consent of the Aufsichtsrat to any personal credits or loans allowed them.⁷³

They must, in the conduct of the business of the company, apply the diligence of careful business men, and claims against them can only be based upon a neglect of this duty or on misconduct or bad faith. This liability is especially impressed upon them in investigating the circumstances attending the promotion of the company.⁷⁴ They are jointly⁷⁵ and severally liable for a breach of the above duties and for improper transactions such as (a) repaying to shareholders contributions to capital, (b) paying interest or dividends improperly, (c) buying, taking as security, or canceling shares of the company, (d) distributing assets in whole or in part, and (e)

⁶⁹ H.G.B. 202. Persons who cooperated with them in causing loss by bringing into the company contributions in property or assets of questionable value are liable with them.

⁷⁰ H.G.B. 208.

⁷¹ H.G.B. 313.

⁷² H.G.B. 235, 271.

⁷³ H.G.B. 236, 240a.

⁷⁴ H.G.B. 204, 241.

⁷⁵ Each director is liable only for the damage he has caused. It is only when several have joined in bringing about the same loss that they are jointly liable.

making payments after the company has become insolvent.⁷⁶ The company's creditors can also enforce their claims against the members of the Vorstand insofar as they are not satisfied out of the company's funds.⁷⁷

The directors must (under disciplinary penalties) carry out their duties by (a) summoning general meetings to be informed of the financial condition of the company if it has lost more than one half its capital; (b) rendering reports to the Aufsichtsrat; (c) preparing balance sheets, profit and loss accounts, and reports within 3 months after the close of the business year; (d) allowing auditors to inspect the books and investigate all matters pertaining thereto; and (e) publishing notice of impugning the resolutions of general meetings. They are also jointly responsible criminally and civilly for the proper keeping of the books of the company.⁷⁸

The directors (and supervisors as well) are also liable criminally (a) if they willfully act to the disadvantage of the company; (b) if they knowingly give false information as to subscriptions or payments of original capital, the price at which shares were issued, or the arrangements for the purchase of plant; (c) if they misrepresent or conceal the true state of the company's affairs in their speeches, statements, or reports at general meetings or elsewhere; (d) if they issue shares illegally; (e) if they allow the Aufsichtsrat to remain for more than 3 months without a sufficient number of members to form a quorum; or (f) if they do not initiate bankruptcy proceedings as soon as they know the company is insolvent.⁷⁹

The provisions as to liability of directors apply also to persons (procurists) representing them.⁸⁰

SUPERVISORS

Formerly the supervisors (Aufsichtsrat) controlled the general affairs of the company. Emergency decrees have changed this responsibility; but in limiting the scope of control the responsibility has been increased with regard to specific details. Supervisors have become responsible for knowing more completely what is going on in the business and for a much closer supervision of the finances of the company.

This was accomplished by three new measures: (1) Reports regarding the developments of the business situation, which formerly were rendered only to the chairman of the Aufsichtsrat, must now be submitted by the directors to all the supervisors; (2) the details which the directors are required to include in the annual balance sheet, profit and loss account, and accompanying explanatory report have been considerably extended; (3) the Aufsichtsrat must be convened on the written demand of any member, and two members may call a meeting themselves,⁸¹ to apprise the members of the

⁷⁶ The company's right of action in these matters can only be enforced after resolution of the majority at a general meeting or upon insistence of a minority of at least one tenth of the share capital (H.G.B. 268).

⁷⁷ H.G.B. 241. Such claims are barred after 5 years.

⁷⁸ H.G.B. 239-240, 245, 260, 267, 272, 319; Criminal Code 244.

⁷⁹ H.G.B. 240, 312-314. Liquidators are criminally liable in the same manner as directors for (a), (c), (e), and (f). They can also be forced, through court order, to draw up a balance sheet at the commencement of liquidation and at the end of every business year thereafter, and be made to hold and safeguard the books of the company for 10 years (H.G.B. 302, 319).

⁸⁰ H.G.B. 242.

⁸¹ H.G.B. 160-162, 239a, 244a.

workings of the company and to discuss unsatisfactory acts of directors.

Formerly the supervisors were jointly liable to the shareholders for continued bad management of the company, but those not knowing this condition were freed from this liability. Now, under the new laws, there is less possibility of such a defense. Supervisors are also liable for acts of bad faith by officials of the company other than directors, if they approved the appointment and were not diligent and careful in their choice. They are now also called upon to specifically approve any credits allowed the directors and are liable to creditors for losses occurring through neglect to carry out this duty.⁵²

Creditors of the company may proceed against the supervisors if the assets of the company are insufficient to meet claims, but only if the supervisors have acted illegally. Other parties also may proceed against them if bad faith can be shown.

Practically the same joint and several liability provided for directors applies to supervisors. This is especially true if they fail to exercise the diligence of careful business men as to the investigations and reports to be made by them concerning the circumstances attending the promotion of the company or if they permit shares to be issued for an improper amount or before registration of the company.⁵³ Their criminal liability also is the same as that of directors. (See p. 32.)

CONDUCT OF THE BUSINESS

THE GENERAL MEETING

Meetings of stockholders of a share company are most important. The shareholders collectively are the repository of the company's power, and no other means are provided by law for the exercise of this power.

The meetings of shareholders may be ordinary or extraordinary. The former are held periodically as fixed by the charter and bylaws; the latter may be called at any time at the instance of the directors, the supervisors, or the shareholders.

Every company must convene at least one general meeting of shareholders in every fiscal year. This meeting is held within 3 months (but under no circumstances later than 6 months) after the termination of the fiscal year. It is held at the domicile of the company unless the charter of the bylaws provide for holding it elsewhere, in which event it may even be held outside Germany.

The power to summon a general meeting rests with the directors unless conferred on others by the charter. In addition to those specified by law or the charter, meetings must be called upon all occasions made necessary by the interests of the company. A meeting may also be summoned by the supervisors when the interests of the company specifically require it, and must be called if a demand is made in writing by shareholders owning at least one twentieth of the capital stock of the company (but the charter may give this right to a smaller percentage).⁵⁴

⁵² Credits granted to the directors, advance payments of compensation, and other loans exceeding the scope of their contracts must be specifically approved by the Aufsichtsrat. For certain kinds of credits this approval may be given in advance, but never for a longer period than 3 months (H.G.B. 240a).

⁵³ H.G.B. 204, 209.

⁵⁴ H.G.B. 246, 253-254.

The general meeting is summoned in accordance with the provisions of the charter. Notice of a meeting must be published 2 weeks before the date fixed, exclusive of the day on which the notice is given. If shares must be deposited to enable a person to vote, the notice period must be extended by the time required for the deposit.⁸⁵ If there is no provision for the deposit of shares, notice of intention to take part in the meeting must be given by every shareholder not later than 3 days before the meeting.⁸⁶

The purposes of the meeting must be stated in the public notice, and a copy of the proposals to be laid before the meeting must be given to every shareholder who applies for it. A resolution cannot be passed except after notice of at least 1 week (if more than a majority required, 2 weeks) before the meeting. No notice is required for resolutions to hold an extraordinary meeting or to discuss particular proposals held over from previous general meetings.⁸⁷ Meetings are competent only to deal with company affairs and not with the affairs of the shareholders.

To pass a resolution⁸⁸ at a general meeting a bare majority (numerical majority of the votes cast) is sufficient; but such a majority at least is absolutely necessary, and a larger majority may be required by law or by the charter.⁸⁹

Every share is entitled to a vote, and the decision is made on the basis of the nominal or par value of the shares voted (except where there are plural-voting shares). The right to vote may be exercised by written proxy authenticated and deposited with the company. No one is permitted to vote upon questions involving his obligations to or his business transactions with the company.⁹⁰

Each shareholder who deposits his stock may demand special notice of the meeting and its objects. He is also entitled to a copy of any resolution passed at such meeting.⁹¹

A list of the shareholders and their proxies who have signified their intention to be present, giving names, addresses, and holdings of shares, must be posted for inspection before the meeting.⁹²

In order to validate it, every resolution must be authenticated by a minute taken by a notary⁹³ or a judicial officer. Such minute must state (*a*) the place, (*b*) the date, (*c*) the name of the notary or judicial officer, (*d*) the method of passing, (*e*) the result of the vote upon the resolution, (*f*) a list of the persons present, (*g*) the documents proving that the meeting had been properly summoned unless such documents are specified and their contents merely indicated, and (*h*) the signature of the notary or judicial officer. An authen-

⁸⁵ The deposit of shares with a notary is sufficient unless the charter specifically provides otherwise. Companies issuing bearer shares may provide that certificates of deposit of banks in which such shares are kept will be sufficient evidence of ownership to enable the holders to vote the shares at any meeting. They may, however, require that the shares be deposited in a named bank and kept there from a certain time before until after the meeting.

⁸⁶ H.G.B. 253.

⁸⁷ H.G.B. 256.

⁸⁸ Resolutions cannot be dispensed with in the share company even if all the shareholders consent in writing.

⁸⁹ H.G.B. 251.

⁹⁰ H.G.B. 252.

⁹¹ H.G.B. 257.

⁹² H.G.B. 258.

⁹³ Notarial fees are fixed by the Government and are dependent upon the amount of the capital stock of the company. They must not be changed by the notary without the consent of the overseer of notaries.

ticated copy of the minute must be filed by the Vorstand for entry in the mercantile register immediately after the meeting.⁹⁴

Resolutions may be impeached by shareholders or by the Vorstand or the Aufsichtsrat. The company is the defendant in such actions.⁹⁵

The ordinary functions of the general meeting are to approve (by resolution) the submitted balance sheet (discussed on p. 36), to provide for the distribution of dividends, and to consider and (if found in order) approve the activities of the Vorstand and of the Aufsichtsrat for the previous period, so relieving them of their responsibility. To the extent that the balance sheet is not defective it must be accepted. Exoneration of the Vorstand and the Aufsichtsrat is only as to claims arising from such failure to discharge their duties as the general meeting or the special investigators appointed for such purpose knew or should have known. The members of both these bodies are entitled to this exoneration and can enforce this right by suit.⁹⁶

A bare majority is required to enforce the appointment of the auditors for the investigation of the circumstances attending the formation of the company,⁹⁷ but even a minority holding one tenth of the shares of the company may demand and obtain this. For the investigation of the balance sheet and report of the Vorstand, official examiners must be elected at each annual general meeting. The members of the Vorstand and of the Aufsichtsrat may not vote in this election, but either body or a minority of the shareholders may object to the auditors so elected and ask the court to appoint others.

MANAGEMENT ⁹⁸

The management of the business of a share company is intrusted to the directors; their number and their powers in relation to the company⁹⁹ (but not as to third parties) are limited by the charter.¹ The law, however, imposes no restrictions upon their selection nor as to nationality or residence;² they need not be shareholders.³ They are chosen in the manner prescribed by the charter (usually by the Aufsichtsrat, which in so doing makes a contract of employment with them) and may be removed at any time by the power which appointed them—with, however, a claim for damages. The charter itself usually specifies the manner of filling vacancies, but in urgent cases courts may appoint until the vacancy is filled in the regular way.⁴

All judicial and extrajudicial transactions for the company are carried out by the directors, who represent the company in its relations with third parties and in the general conduct of the business.

⁹⁴ H.G.B. 259.

⁹⁵ H.G.B. 271-272.

⁹⁶ H.G.B. 260.

⁹⁷ H.G.B. 266.

⁹⁸ See also "Rights and liabilities of directors" at p. 31 and "Directors as agents" at pp. 126-128.

⁹⁹ Certain duties, such as the giving of notice, the signing of contracts and obligations for the company, and the supervision of the bookkeeping, cannot be taken from the directors.

¹ H.G.B. 231.

² The same is true of supervisors. A member of the board of directors, however, may not be a member of the board of supervisors at the same time or before receiving his discharge as a director.

³ H.G.B. 248.

⁴ B.G.B. 29.

Any limitations upon their powers imposed by the charter or by resolution of a general meeting must be carefully observed,⁵ but no liability attaches to them for errors of judgment⁶ or for acts in which they have not taken part or to which they have been opposed. The doctrine of *ultra vires* is unrecognized in German law.

Directors having a personal or conflicting duty or interest in a transaction for the company may not participate in the deliberations.

Besides the preparation of reports⁷ on the condition of the business for the Aufsichtsrat and the drawing up of balance sheets,⁸ profit and loss accounts, and reports for submittal to the general meeting⁹ (see below and p. 37), it is obligatory upon directors to present for entry in the mercantile register (*a*) the application for registration of the company upon formation; (*b*) the application for registration in the places where branches are formed; (*c*) copies of the minutes of general meetings; (*d*) every change in the membership of the Vorstand or the Aufsichtsrat and in the authority of the members of the Vorstand; (*e*) the appointment of procurists; (*f*) the annual balance sheet, profit and loss account, and report; (*g*) the decisions of the courts on the impugning of resolutions; (*h*) any alterations in the charter; (*i*) notice of dissolution except through bankruptcy; (*j*) names of the first liquidators appointed upon the commencement of liquidation; and (*k*) notice of intention to carry on the company after it has unsuccessfully attempted to merge with another or when bankruptcy proceedings are annulled.¹⁰ The directors must also furnish their signatures to the courts at the principal place of business of the company and at all branches.

Liquidation of a company is carried out by directors except where the charter or a resolution of a general meeting provides otherwise.¹¹

Balance sheet.—Within 3 months (and under no circumstances later than 6 months) after the close of each business year an annual balance sheet must be prepared by the Vorstand. It is presented to the Aufsichtsrat for comment and submitted with these comments to the general meeting. The new amendments have enlarged the scope and extended the details required to be set out in this balance sheet, which now “must be drawn so clearly and concisely as to give anyone interested as accurate an insight as possible into the company’s condition.” So much stress is laid upon the details of the balance sheet and the accompanying report that the provisions covering these items take up the greater part of the new law. The Government even supplies blank forms for balance sheets and profit and loss accounts.¹²

⁵ H.G.B. 236.

⁶ They may not, however, blindly carry out the resolutions of a general meeting if in doing so they would become liable under the law to others, but must bring an action to impugn such resolutions.

⁷ H.G.B. 239a.

⁸ The method of accounting to be used in the balance sheet and the items to be covered are set forth specifically and at great length in H.G.B. 260–262. (See also “Balance sheet” below.)

⁹ However, the directors are not bound to disclose to a general meeting anything except the balance sheet, profit and loss account, and the report commenting thereon. They are not even compelled to show the books of the company to substantiate their figures. If they give to the general meeting too much information or information to which it is not entitled, they may be liable for any losses occasioned thereby (Imp. C.C. vol. 2, p. 239; H.G.B. 312).

¹⁰ H.G.B. 195, 201, 207, 234, 244, 250, 265, 273, 277, 280, 284, 289, 291, 293, 296, 307, 310.

¹¹ H.G.B. 295.

¹² H.G.B. 260–263.

The balance sheet, profit and loss account, report of the Vorstand, and the comments of the Aufsichtsrat thereupon must be open for inspection by shareholders at least 2 weeks before any general meeting.¹³

The old law provided for the appointment of auditors to check the balance sheet if demanded.¹⁴ Under the new law the annual balance sheet must be subjected to examination in connection with the books of the company upon which it is based by one or more official expert auditors¹⁵ before submittal to the general meeting.¹⁶

Acceptance of the balance sheet may be postponed by a resolution of a majority, or even by a minority holding one tenth of the company's capital stock; but only when objection is made to specific items. No additional postponement can be obtained unless the explanations requested have not been satisfactorily given.¹⁷

On being approved, the balance sheet and profit and loss account must be published in full in the public prints and, together with the report of the Vorstand and the comments of the Aufsichtsrat, deposited in the mercantile registry where the principal office and branches of the company are located.¹⁸

Reports.—Reports on the financial condition of the company must be made by the directors to the supervisors, orally or in writing, at least every 3 months and oftener if necessary.

The law now enumerates specifically the items which must be set out in these reports. They include, among others, (a) a statement of the shares received by the founders, and, if such shares have been sold during the business year, information regarding the sale and the use of the proceeds; (b) the number of the company's shares owned by itself or for its account, and, if such shares have been bought or sold during the business year, information as to the purchase or sale price and the use of the proceeds; (c) a statement of the nonnegotiable shares of the company outstanding; (d) bonus or extra shares issued during the business year; (e) liabilities not appearing on the balance sheet, including contingent liabilities and orders secured by pledge, transfers of securities, and obligations arising from negotiation of bills of exchange and checks; (f) total sums received from the company by members of the Vorstand and the Aufsichtsrat; (g) the company's membership or participation in associations and agreements for regulation of prices and output; and (h) transactions of special importance undertaken during the business year.¹⁹

¹³ Shareholders are entitled to a copy of the balance sheet and profit and loss account.

¹⁴ H.G.B. 266.

¹⁵ These auditors are elected by the general meeting before the end of each business year. The Vorstand and the Aufsichtsrat may not vote at that election, but either of them or a minority of the shareholders may object to the selection. The court will then decide on the validity of their objections and, if sustained, choose other auditors. The auditors must be given access to the books, documents, cash on hand, securities, and stock of the company for examination. The Vorstand (under penalty for default) must furnish to them any explanation, proof, or voucher required. After the examination they must report in writing and comment upon the points of their examination (especially on "whether there are any vital objections to its final results") (H.G.B. 262 b, d, and e).

¹⁶ H.G.B. 262a.

¹⁷ H.G.B. 264.

¹⁸ H.G.B. 265.

¹⁹ The tax office has ruled against the capitalization of goodwill unless actually paid for in connection with the acquisition of another business. An annual write-off must be made, and moneys expended for advertising or otherwise to increase the goodwill must not be considered an asset.

This report (together with the annual balance sheet) must be examined by expert official auditors before submittal to the general meeting.²⁰

"The business report must state in detail the condition of the company and of its property and explain the annual balance sheet. In this explanation important divergencies from the previous balance sheet will be discussed. * * * It will also deal with the company's relations with subsidiary and affiliated concerns."

SUPERVISION ²¹

In the absence of charter provisions, the board of supervisors (Aufsichtsrat) consists of three members. Under no circumstances may the number exceed 30. There is no limitation as to nationality or residence, and supervisors need not be shareholders; but no person may be a member of the Aufsichtsrat of more than 20 companies. A supervisor may not at the same time act as a director of the same company; but the Aufsichtsrat may appoint one of their number to act during the incapacity of a director for a period fixed in advance—during which time he may not also act as a supervisor.²²

The members of the first board of supervisors are elected for the period ending with the conclusion of the first general meeting. Their compensation for this period is fixed by the charter ²³ and for subsequent years by resolution of the general meetings. (Art. VIII of the new law.) After the first year supervisors are elected by the general meeting for a term not exceeding 3 years; but their term of office may be revoked at any time by a majority holding three fourths of the capital represented at such meeting, unless the charter provides otherwise. A minority of at least one tenth of the capital is entitled to one representative on the board of supervisors.

Formerly only the chairman of the Aufsichtsrat was empowered to call the meetings of his board. Under the recent enactments the board must be convened on the written demand of any member; and if two of them demand it, they may call the meeting themselves. They carry out their administrative functions according to the law as set forth in the Commercial Code. The board adopts resolutions in meetings of its members, who must be notified of the meetings and the resolutions to be considered. The decisions are made by the votes of the majority of members present; but a valid resolution can be made without the members coming together, provided all of them give their written assent to it. The representative authority of the board is a joint one, and all the members must therefore join in exercising it. The board, however, may authorize individual members to carry through certain work.²⁴

The Aufsichtsrat as a complete board ²⁵ may summon a general meeting when the interests of the company require, and the charter

²⁰ H. G. B. 262a.

²¹ See also "Rights and liabilities of supervisors" at p. 32.

²² H. G. B. 248.

²³ H. G. B. 243.

²⁴ H. G. B. 244a, 246.

²⁵ Unless the membership of the Aufsichtsrat is complete, it may not do any particular act, but the charter may permit it to act without full membership if at least three members are present (H. G. B. 243).

may impose other duties upon it.²⁶ Supervisors may delegate their duties, and the degree of care for which they are responsible is the ordinary diligence of careful business men.²⁷

The new law increased the duties of the supervisors with regard to the control of the business and especially by imposing upon them the duty to make themselves more familiar with the conditions and circumstances attending the management.

The Aufsichtsrat acts for the company in transactions between the company and the Vorstand and conducts all legal proceedings against the latter for the company. If the members of the Aufsichtsrat may become liable, they may proceed against the Vorstand without the authority of a general meeting or even in opposition to a resolution.²⁸

CORPORATE CHANGES

ALTERATIONS IN THE CHARTER

An alteration in the charter of a company can be made with the consent of all of the shareholders, and can also be made by resolution of a majority fixed by the charter; but the charter may not prohibit alteration altogether.

Mere assent to an alteration is not sufficient; action must be taken by the general meeting by resolution, a minute of which must be made by a notary and filed in the mercantile register. Power to make changes in the charter in matters of form may be given by resolution of a general meeting to the supervisors.²⁹

To bring about an alteration in the charter there must first be publication of a notice calling a general meeting so to do. This notice must set forth the essential details of the alteration and contain the summons to the meeting. The resolution must then be passed by such general meeting by a majority representing at least three fourths of the capital present (unless otherwise stipulated in the charter).

If the alteration involves relations between two classes of shares, to the prejudice of one of them, a special vote of the prejudiced shareholders³⁰ is also required.³¹

A resolution to impose upon any shareholder the obligation to make an additional contribution (other than money) requires the unanimous consent of those affected, unless such additional contribution is provided for in the original charter. This applies also to any extension of the liability of shareholders.³²

After an alteration of the charter is authorized by a resolution of a general meeting, such action must be notified for entry in the mercantile register by all the directors, and the alteration itself takes effect only when this registration has been made at the principal seat of the company.³³ To register such alteration the docu-

²⁶ The charter cannot limit the legal rights and liabilities of the members of the Aufsichtsrat. It can, however, add to them; but in so doing it cannot impose upon or delegate to them the duties which properly belong to the Vorstand.

²⁷ H.G.B. 246, 249.

²⁸ H.G.B. 247.

²⁹ H.G.B. 274.

³⁰ A separate special meeting of the prejudiced shareholders is not required so long as their votes are formally taken. The same majority of votes of such shareholders is required as in the general meeting to accept the alteration.

³¹ H.G.B. 275.

³² H.G.B. 274.

³³ H.G.B. 277.

ments³⁴ by which it has been effected must be filed with the court in the domicile of the company. The filing is merely a formality, the court having no jurisdiction over the subject matter.

Public notices of alteration must be made and must conform to all the rules for publication of any notices as specified in sections 199 and 201 of the Commercial Code.

Increases in capital.—Increases in capital are considered alterations of the charter. The requirements of the law and of the charter must be met. Increases cannot be made until the shares already issued have been paid in full.³⁵

Resolutions to increase capital must set forth the maximum amount to which it is to be increased. The increase may be made conditional on the results of the public subscription.³⁶

If there are several classes of shares in existence, a resolution (in addition to the resolution of the general meeting) must be passed separately by the holders of each class. No separate meeting for this purpose is necessary. When new shares are to be issued for more than their nominal or par value, the resolution should fix the minimum amount below which no shares should be issued.³⁷

Where the increase in the capital is to be used to procure things other than money, or where the company is to pay with the increased stock for property or a business which it takes over, the resolution for increase must specify the things to be contributed or taken over, the person from whom they are to be acquired, and the shares or the sum in payment which the company is to give for what it receives. Any agreement of this character made without resolution of the general meeting is void as against the company.³⁸

Notices of intention to increase the capital must be given for registry by all the members of the Vorstand and the Aufsichtsrat, and when the contemplated alteration is actually effected another notification must be given to the registry; but both notices may be filed simultaneously.³⁹

Each shareholder (unless the resolution providing for the increase in capital specifies otherwise) is entitled on request to an allotment of the new shares corresponding to his holding of old at the time. The extent to which the new shares are to be allotted to old shareholders must be published by the Vorstand, and it must fix a time within which the old shareholders should exercise the allotment rights (which may not be less than 2 weeks). A preferential allotment is valid only if actually specified in the resolution for increase. It cannot

³⁴ Where an alteration is only in form, registration may be effected simply by referring to the documents deposited in court.

³⁵ Insurance businesses, however, may provide to the contrary in their charters. Insignificant arrears in called payments may be disregarded.

³⁶ Public subscriptions must be made upon certificates of subscription drawn up in duplicate showing (a) the date of completion of the memorandum of association, with all its particulars; (b) the names, occupations, and residences of the founders; (c) the amount at which each class of the shares already issued has been issued, and the amounts due on the installments on the new shares; (d) the date of the resolution authorizing the increase in capital; (e) the arrangements for contributions other than cash and purchases to be made with the increased capital; (f) if different kinds of shares are issued, the total amount of each class; and (g) the date on which the subscription will cease to be binding (H.G.B. 281). Any limitations of rights or obligations of subscribers which do not appear upon the certificates of subscription will be invalid.

³⁷ H.G.B. 278.

³⁸ H.G.B. 279.

³⁹ H.G.B. 280, 284, 285.

be enforced if it is only an understanding between the shareholders at the time the resolution is passed.⁴⁰

Until the registration of the increase of capital stock has been made, the increase is not legally effective. Shares and interim certificates for new shares may not be issued before that time; and if issued, they are void.⁴¹

If, on allotment of shares, any shareholder is entitled to a fractional part of a share, the company may allot parts of such single share to several shareholders, and they have a joint and common ownership in such fractional parts.⁴²

Reductions in capital.—Reductions of capital are also considered alterations in the charter, and the general provisions under alteration govern.

A resolution of shareholders owning three fourths of the capital represented at the meeting for the reduction of the capital is necessary unless the charter provides otherwise. The resolution must state the amount to which the capital is to be reduced. It need only give the minimum, and the reduction is then made dependent upon the extent to which a voluntary surrender of the shares takes place.

The general meeting held for the purpose of considering the advisability of reducing capital must determine the object of the reduction and state whether its purpose is to make a partial repayment of capital to shareholders and the manner in which it is to be carried out. Where there are several classes of shares there must be separate votes of the holders of each of them in addition to the resolution of the general meeting, and such separate votes require the same majority as in the case of increases of capital.⁴³

The notice to shareholders of the intention to reduce the capital and the subsequent resolution of the general meeting to carry out this purpose must be notified by all the members of the Vorstand and the Aufsichtsrat for registration in the mercantile register in the same manner as for increases of capital.⁴⁴

After the registration of the decrease in capital the Vorstand must immediately call upon all creditors to send in their claims, at the same time advising them of the reduction. This notice must be published three times in the public prints in which the company is required to give notice. The claims of creditors must be paid in full or satisfactorily secured before any repayments can be made to shareholders; and in no case may a distribution of capital or repayment to shareholders be made until at least 1 year from the publication of the last notice to creditors.⁴⁵

If the reduction is to be brought about by the return of shares and they are not sent to the company, it may declare them canceled. The notice to send in the shares should warn the holders of this possibility. The new shares issued for the shares canceled must be sold by the company for the persons entitled to them at the price fixed on the exchange or at public auction; and the price received must be paid to the parties whose shares were so canceled.⁴⁶

⁴⁰ H.G.B. 282-283.

⁴¹ H.G.B. 287; B.G.B. 134.

⁴² H.G.B. 225; B.G.B. 741.

⁴³ H.G.B. 288.

⁴⁴ H.G.B. 291.

⁴⁵ H.G.B. 289.

⁴⁶ H.G.B. 290.

DISSOLUTION AND LIQUIDATION

A company is dissolved by (a) expiration of the term of duration (Zeitdauer), (b) resolution of a general meeting passed by a three-fourths majority of all the capital held by those voting (unless the charter requires additional formalities), or (c) the commencement of bankruptcy proceedings against the company; ⁴⁷ also, rarely, (d) if the purposes are unattainable or (e) if public welfare is endangered. (See p. 52.) Dissolution of a company (except by bankruptcy) must be notified to the registry by all the directors.⁴⁸

Where a company is dissolved (except by bankruptcy), the work of liquidation will be carried on by the directors as liquidators, unless the charter or the bylaws of the company make other provision or unless the Aufsichtsrat or holders of at least one twentieth of the capital apply, on good grounds, for the appointment of other liquidators. In urgent cases the court, on application of an interested party, may appoint the liquidators. Liquidators may at any time be removed in the same manner as appointed, without prejudice to their claims for fees.⁴⁹

The directors must notify for registry in the mercantile register the appointment of the first liquidators, and the latter in turn must notify any subsequent changes in appointment or powers. The liquidators must sign the firm name to all their acts and upon qualifying must file their signatures in the court of registry.⁵⁰

The relationship between the liquidators and the company in liquidation is governed by the general principles of agency, and they usually are given the same rights as the members of the Vorstand enjoyed. They have the power to continue and carry on the business, subject always to the supervising power of the Aufsichtsrat exactly as the directors are subject to that supervision before liquidation. They are responsible for and must prepare a balance sheet on entering upon their duties and at the close of each business year thereafter. Upon completion of the dissolution and distribution and after final account by the liquidators, they must give notice of that fact for entry in the mercantile register. The books and documents of the company in their possession must be kept safely for 10 years thereafter, during which time they must be available for inspection.⁵¹

The bodies which represent the company continue their duties during liquidation (except the Vorstand, which may be replaced by liquidators). The general meeting of shareholders is to be regularly held to consider the balance sheets presented by the liquidators and to appoint new liquidators to fill vacancies or remove a liquidator when this is deemed advisable. These meetings of shareholders must also decide questions arising in connection with transactions which are not properly for the liquidators to decide.

It is the duty of liquidators to call upon creditors to file claims. One year after publication of this notice the property remaining

⁴⁷ The bankruptcy of a company implies its insolvency or overindebtedness. Any director or company creditor may file the petition, and the directors must file the petition when the company is insolvent. The trustee in bankruptcy administers the business and represents the company, but the Vorstand and the Aufsichtsrat and the general meetings of shareholders continue to act and to carry out all their functions (K.O. G. 207-208; H.G.B. 240).

⁴⁸ H.G.B. 292-293.

⁴⁹ H.G.B. 231, 295, 298.

⁵⁰ H.G.B. 286.

⁵¹ H.G.B. 611 et seq.; H.G.B. 298-299, 302. See regulations for carrying on the business, H.G.B. 149-158.

in the possession of the company after the debts have been paid or otherwise secured will be divided by the liquidators among the shareholders. Distribution must be made according to the value of the shares held and according to the several rights of the different kinds of shares. It usually is made in cash after realization⁵² upon assets, but it may be accomplished in another manner if the general meeting decides that it shall be done without sale. The right to claim a share in the distribution is barred after 3 years. Liquidators need not pay shareholders or others except upon formal receipt or, where shares have been surrendered, upon the certificates therefor.⁵³

LIMITED-LIABILITY COMPANIES

The limited-liability company, or Gesellschaft mit beschränkter Haftung (G.m.b.H.), has no exact parallel in American law. It partakes partly of the nature of the American business corporation and partly of the nature of a partnership. It has juristic personality, a separate firm name, capital and property rights separate and distinct from its members, and the right to sue and be sued.⁵⁴

Unlike the share company, the capital of the limited-liability company is not divided into shares, and consequently certificates can be neither issued nor negotiated; but the individual holdings of the members in the company may be transferred in whole or in part by notarial or judicial act, subject to the consent of the company.⁵⁵

The limited-liability company is represented by one or more managers (Geschäftsführer). Supervisors are optional. Members must pay in capital to the amount agreed in their subscriptions set forth in the memorandum of association (charter). They have no further liability for payment to capital except for additional calls in the ratio of their holdings (as limited by the charter).⁵⁶

The acts of a limited-liability company do not require the publicity exacted of the share company, nor are changes so completely covered by legal supervision.

The duration of the company depends, as does that of the share company, upon the charter; and, like the share company, the limited-liability company is deemed a mercantile association within the meaning of the Commercial Code.⁵⁷

FORMATION

MEMORANDUM OF ASSOCIATION (CHARTER)

Two⁵⁸ or more persons may come together and form a limited-liability company. They must sign and execute a memorandum of association (charter) by a declaration before a notary or a judicial officer. They may be natural persons, or partnerships, or share com-

⁵² Realization of the company's assets by sale of its property as a whole is only permitted when a general meeting so provides by resolution passed by a majority of at least three fourths of the capital taking part in the vote unless further requirements are imposed by the charter (H.G.B. 303).

⁵³ H.G.B. 300-301, 308; B.G.B. 797.

⁵⁴ G.m.b.H.G. 13.

⁵⁵ G.m.b.H.G. 14-15, 17.

⁵⁶ G.m.b.H.G. 26.

⁵⁷ G.m.b.H.G. 3, 13.

⁵⁸ After formation has been effected the company may continue in existence with only one manager (Gesellschafter) (R.G. vol. 68, p. 172). To distinguish between the director (member of the Vorstand) of a share company and the Geschäftsführer of a limited-liability company the latter word will be translated and hereafter appear in this text as "manager."

panies, or even other limited-liability companies and may be either German or foreign, resident or nonresident. Signing by power of attorney is permissible if the document is properly authenticated.⁵⁹

The memorandum of association must state (a) the name and the principal place of business of the company;⁶⁰ (b) the objects of the undertaking; (c) the amount of capital; (d) the amount to be paid by each member into the capital; (e) the duration of the company,⁶¹ if fixed; (f) duties other than contribution to capital, if agreed upon;⁶² and (g) if contributions to capital are to be made otherwise than in cash, the names of the members so contributing, a description of the property, and the cash value at which it is taken.⁶³

If the charter does not contain these provisions, or if any of them are null and void, any member, manager, or supervisor may, by writ, apply to have the company annulled; but defects in the charter as to name, place of business, or the object of the undertaking may be remedied by unanimous vote or consent of the members.⁶⁴

FIRM NAME

The name of the company must either refer to the object of the undertaking or include the name of at least one member, with an addition signifying the existence of the company. It cannot include the names of persons other than members (except when under section 22 of the Commercial Code the company has acquired this right). It must in any event have appended to it the designation "Gesellschaft mit beschränkter Haftung" (or its abbreviation, "G.m.b.H.")⁶⁵

Foreign companies may use their own corporate name when organizing a German subsidiary.

NOTIFICATION TO THE COURT

The managers (Geschäftsführer) of a limited-liability company⁶⁶ must notify⁶⁷ the court of the district in which the principal place of business is situated⁶⁸ of the formation of the company and the execution of its memorandum of association and must request permission to register the company in the mercantile register.⁶⁹ With the application there must be submitted (a) the charter, accompanied by the duly authenticated powers of attorney of those who signed for the principals; (b) the documents giving the managers their authority (if not fixed by charter); (c) a list of the members, their occupations and residences, and the amounts of their respective contributions, signed by the persons making the

⁵⁹ G.m.b.H.G. 2.

⁶⁰ The principal place of business (Sitz) need not be where the plant is located.

⁶¹ To prolong the duration of a limited-liability company the consent of all the members is necessary if the rights of any are diminished. Otherwise it is effected as any other alteration.

⁶² G.m.b.H.G. 3.

⁶³ G.m.b.H.G. 5.

⁶⁴ G.m.b.H.G. 75-76.

⁶⁵ G.m.b.H.G. 4.

⁶⁶ G.m.b.H.G. 9.

⁶⁷ The court merely formally accepts the documents for filing without any jurisdiction or power with regard to them. Any right of decision is acquired by the courts only subsequent to registration.

⁶⁸ Similar notice must be given the court in the district where a branch is located (G.m.b.H.G. 12).

⁶⁹ G.m.b.H.G. 7.

application; (*d*) the state license (when required); and (*e*) a statement that at least one fourth of the contributions other than those not in cash have been paid (but in no case less than 250 marks per subscriber) and that this money is at the complete disposal of the managers.⁷⁰

The managers must at the same time furnish the court specimens of their signatures.

REGISTRATION AND PUBLICATION

After notice of the intention to register is filed with the court, notice of the formation of the company must be given to the mercantile registry in the district where the principal office is located (and to the registries in the districts of all branches as well). A notice for registration must include (*a*) the name and principal place of business of the company, (*b*) its objects, (*c*) the amount of capital, (*d*) the date of the execution of the charter, (*e*) the duration of the company, (*f*) the names of the managers, and (*g*) the powers of the managers and liquidators (if specified).⁷¹

Before registration the company has no existence, and persons trading in its name or on its behalf before that time are jointly and severally liable.⁷²

An announcement that registration of the formation of the company has been effected must be published at the principal place of business of the company and at the places of business of all the branches. The publication at the principal office must include the facts required for registration, the facts and circumstances surrounding contributions to capital made otherwise than in cash, and the requirements of the charter as to publication of notices by the company.⁷³

INTERESTS IN THE COMPANY

CAPITAL

The capital in forming a limited-liability company must be at least 20,000 marks.⁷⁴ The subscription of each member must be at least 500 marks, but may be any larger sum so long as the amount is divisible by 100. The aggregate of the contributions must equal the entire capital.⁷⁵

Contributions to capital may also be made by any member in property other than cash, in which event the names of the members so contributing, a description of the property, and the value at which it is taken must be set forth in the memorandum of association. Such contributions can only be allowed by the charter or amendment to it and can never be for services.⁷⁶

⁷⁰ G.m.b.H.G. 8.

⁷¹ G.m.b.H.G. 10, 12.

⁷² G.m.b.H.G. 11.

⁷³ The registration is published in the German Official Gazette and usually in two daily newspapers.

⁷⁴ The organization costs are comparatively reasonable. They include notarial and registration fees, expenses of publication, and an organization tax on capital of 4 percent. (See Journal of Comparative Legislation, Nov. 1931, p. 221.)

⁷⁵ The entire capital of a limited-liability company must be subscribed for, and an amount equal to at least one fourth must be paid in cash on each share (and not merely on the total), except where a contribution is made in other than cash, before an application for inscription in the mercantile register is permitted. Contributions other than cash must be freely available, although real property cannot be transferred to the company before registration (G.m.b.H.G. 7).

⁷⁶ G.m.b.H.G. 5; R.G. vol. 82, p. 303.

SHARES

The capital of the limited-liability company is divided into membership shares (*Geschaeftsanteile*) which correspond to the contributions of the members. The share of an individual member in the business is determined by the amount of his contribution.⁷⁷ No certificate is issued; but, if an attempt is made to issue a certificate, the certificate is only considered proof of an undivided interest in the business (under no conditions transferable as such). However, dividend warrants are issuable by the limited-liability company.

Shares entitle the members to an undivided portion of the company's property. They are nonnegotiable and can be transferred only by declaration before a notary or judicial officer and, if required, upon consent of the company. Where the charter requires consent, this must be written and specify the name of the transferee and the amount of each of the new shares created out of the original contribution. Shares may pass by transfer or by inheritance (both of which may be limited or prohibited by the charter). If a member acquires shares other than his own, they must remain separate and independent, and the share (*Anteile*) of any member must remain undivided as long as it is in his possession and may be split up only on transfer or on inheritance. A division may be prohibited even then.⁷⁸

Where a member transfers his share, he must give proof thereof to the company, and the person named therein shall be deemed the only transferee. An agreement between the transferor and the transferee as to the rights and liabilities of the company is operative between them, but both are liable to the company for payment to capital after the time of transfer, notwithstanding any agreement.⁷⁹

Under no circumstances may shares which are not fully paid be acquired by the company; and fully paid shares may be so acquired only when the company has property in excess of its capital from which the price can be paid. Amortization of shares of the company is allowed only if expressly provided by the charter.⁸⁰

RIGHTS AND LIABILITIES OF THE PARTIES

MEMBERS

The members of a limited-liability company are liable to the company, but not to creditors, for the amount of their contributions.⁸¹ This liability extends only to the unpaid portion of their contributions. The payments to be made on a contribution are determined in proportion to the amount subscribed;⁸² and a member may not be excused or allowed to defer payment of an installment except in the event of a reduction of capital, nor is he allowed to pay by set-off.⁸³ If a member delays in the payment of an installment

⁷⁷ G.m.b.H.G. 14.

⁷⁸ G.m.b.H.G. 15, 17.

⁷⁹ G.m.b.H.G. 16.

⁸⁰ G.m.b.H.G. 33-34.

⁸¹ In case of dissolution they must pay what they have agreed so far as is necessary to enable the company to fulfill its obligations (G.m.b.H.G. 77).

⁸² If an undivided share is held by several as joint owners, they can only exercise the rights to such share in cooperation and are jointly and severally liable for all the payments to be made thereupon. A common representative acts for all; and all the duties of the company to the shareholder are performed and satisfied by performance to such representative or to any one of the coowners direct (G.m.b.H.G. 18).

⁸³ G.m.b.H.G. 19.

upon a contribution, interest is chargeable,⁵⁴ and other penalties and damages may be added if specified by the charter.

If a member delay in the payment of his subscription, demand is made by registered letter, with notice that payment must take place within 1 month or the company will cancel his share. Upon default in payment after such notice the company declares the share (and all payments previously made) forfeited. This declaration must be communicated to the defaulting shareholder by registered letter, and he remains liable for the amount due thereupon and for subsequent contributions.⁵⁵

Not only is the member who defaults in payment of an installment (and thereby loses his stock) liable, but his predecessors in title within the 5 preceding years are liable as well, in the reverse order of their succession. If any such predecessor pay the installment, he acquires the share of the defaulting member. If no predecessor pays, the company may sell the share at public auction (sale by other methods allowed only on consent of forfeiting shareholder).⁵⁶

If the amount of the installment cannot be obtained by sale, the remaining members of the company are compelled to make good the deficiency in capital by contributing in proportion to the amount of their shares; and if any of the members fail to pay, the others must make up the deficiency proportionately.⁵⁷

This liability on the part of members to make up the subscribed capital is also enforced where there is an increase in capital. All the members, new owners as well as old, must take up the capital to the full amount, and the owners of the old stock must subscribe to such increase even though they voted against it. No agreement may free a member or his predecessor in title from this liability.⁵⁸ The process for the collection of these amounts from members may be made more summary or direct by charter. The company cannot relinquish its right to the forfeiture of shares by the defaulting member for nonpayment.

Only by the charter or by the consent of all the members may a limited-liability company provide for additional calls on shares (Nachschuessen) over and above the amount of the originally agreed contribution. When additional contributions are to be collected, they must be in the ratio of the holdings of the members, and the charter may specify the limits of such additional contributions.⁵⁹

When the liability for additional payments is not limited by charter, members can free themselves from additional calls (only if their original contribution is paid in full) by declaring, within 1 month, their share at the disposal of the company for meeting such call. Also, if any member does not pay an additional call, the company may demand that his share be deposited with it for sale by public auction. In either of these cases, the member is entitled to any surplus realized. If, however, the share cannot be sold,

⁵⁴ G. m. b. H. G. 20.

⁵⁵ G. m. b. H. G. 21.

⁵⁶ G. m. b. H. G. 22-23.

⁵⁷ G. m. b. H. G. 24. The necessity for these contributions arises because the creditors of the company are entitled to be assured that the full amount of the capital stated in the memorandum of association has been paid. Such other members, however, are only secondarily liable, or, in other words, can only be held after an attempt has been made at collection from the others.

⁵⁸ G. m. b. H. G. 25.

⁵⁹ G. m. b. H. G. 28.

it becomes the property of the company and may be sold thereafter at any time for the account of the company alone.

Where additional calls are limited by charter, no member can avoid additional calls within the limit. If he does not pay, the company may declare the share forfeited and sell it.⁹⁰

Members who give false information in connection with the inscription of the company in the mercantile register are liable to imprisonment and fine.⁹¹

In the absence of statutory provisions to the contrary, the rights of members are regulated by the charter, and unless there are special provisions the law of limited-liability companies applies.⁹² (The rights of members to participate in the general meetings of the company are discussed on pp. 49 and 50.)

Members of a limited-liability company are entitled to the net profits shown in the balance sheet unless the charter provides otherwise.⁹³ The distribution is made in proportion to holdings, but other methods of distribution may be specified in the charter. Assets necessary to keep the capital intact must not be paid out, but additional calls which are not necessary may be refunded. Members will not be called upon to pay back sums received in good faith as their share of profits unless such payments were improperly or incorrectly made; and if the repayment cannot be enforced, the deficits must be replaced by the other members. Claims of the company for the recovery of such payments are barred after 5 years.⁹⁴

MANAGERS

The managers are jointly and severally liable for repayment to the company by members of deficiencies in the capital, if payments to members were illegally or incorrectly made.⁹⁵

The managers must use the diligence of careful business men in conducting the business and are jointly and severally liable to the company for failure to use this degree of care.⁹⁶ That they acted pursuant to resolutions of the general meetings does not extinguish their liability. Claims so arising are barred after 5 years.⁹⁷

The managers are subject to imprisonment and fine (*a*) if upon the formation of the company they give false information concerning payment of subscriptions for entry in the mercantile register or to the court; (*b*) if, to effect the registration of a reduction of capital, they knowingly give to the court false assurance as to the satisfaction or security of the company's creditors; (*c*) if in public communications they knowingly misrepresent or conceal the condition of the company's affairs;⁹⁸ and (*d*) if they do not apply for adjudication in bankruptcy for the company when they should do so.⁹⁹

⁹⁰ G.m.b.H.G. 28.

⁹¹ G.m.b.H.G. 82.

⁹² G.m.b.H.G. 46-51.

⁹³ A limited-liability company is not compelled, as is a share company, to allocate a part of its profits to a reserve fund before distributing dividends to its members.

⁹⁴ G.m.b.H.G. 29-32.

⁹⁵ G.m.b.H.G. 31.

⁹⁶ G.m.b.H.G. 43.

⁹⁷ All rules affecting managers affect also the persons appointed to act as their substitutes (G.m.b.H.G. 44).

⁹⁸ G.m.b.H.G. 82.

⁹⁹ The bankruptcy act, secs. 239-241, applies to managers of a limited-liability company (as also to directors of a share company) if they have dealt in a manner therein penalized, after bankruptcy (G.m.b.H.G. 83).

CONDUCT OF THE BUSINESS

THE GENERAL MEETING

In the absence of statutory provisions, the charter regulates the rights of members with reference to the affairs of the company. In default of provisions in the charter the limited-liability company act, sections 45 to 51, apply and provide for resolutions at general meetings of the members.

General meetings are summoned by the managers¹ when the company's interests demand (and especially when more than half of the company's capital has been lost) as well as in cases expressly prescribed.² They may also be called by the Aufsichtsrat.³ Members the aggregate of whose shares is not less than one tenth of the capital may, upon stating their reasons, demand that a general meeting be called and, under the same conditions, may also demand that a particular matter be placed on the agenda for any meeting. If their request is not met, they may do it themselves.⁴

A general meeting is summoned by notice sent by registered letter to members at least 1 week before such meeting, stating the purpose for which the meeting is called.⁵ If a meeting is not properly summoned, the resolutions can be adopted only if all members are present and agree. The same rule applies to the adoption of resolutions where notice of the subject matter has not been given at least 3 days prior to such meeting.⁶ A general meeting may be held anywhere, even outside Germany.

Where a board of supervisors is provided for in the charter, the general meeting of a limited-liability company has exactly the same functions as those of a general meeting of a share company. If the charter makes no provision for a board of supervisors, the general meeting adds the functions of such board to its own.

Resolutions of a general meeting are necessary for (a) approving the annual balance sheet⁷ and a distribution of the net profits shown thereon, (b) making calls for contributions, (c) repayment of additional calls, (d) division and cancelation of shares, (e) appointment and removal of managers and the granting of their discharge from liability, (f) the conferring of powers of procuration and mercantile agency on persons to be authorized to conduct the business of the company, and (g) enforcing the company's claims against the managers or members arising from promotion or management.⁸

Required resolutions affecting the affairs of the company must be passed by a three-fourths majority of the votes cast. Each member has one vote for each 100 marks represented by his share. Voting by proxy is allowed provided such proxies are in writing.⁹ A member

¹ The managers cannot be deprived of this right, and procurists acting for them cannot exercise it.

² G.m.b.H.G. 49.

³ Under G.m.b.H.G. 52, referring to the Commercial Code, sec. 246.

⁴ G.m.b.H.G. 50.

⁵ One of the advantages of the limited-liability company is that although, in principle, resolutions should be passed at a general meeting it is unnecessary to hold the meeting if all the members consent in writing or consent to their votes being given in writing. A copy of the resolution may therefore be sent to each member and he can communicate his vote by letter. A meeting need never be held when a limited company is controlled by one party (G.m.b.H.G. 48).

⁶ G.m.b.H.G. 51.

⁷ Publication of the annual balance sheet of a limited-liability company is not required.

⁸ G.m.b.H.G. 46.

⁹ A proxy may vote the shares of more than one member, and he need not necessarily be a member; but the charter may provide that the proxy may only be granted to another member (R.G. vol. 41, p. 99).

cannot vote his own or another's shares on questions of releasing him from obligations to the company or other actions or settlements in which he is involved.¹⁰

MANAGEMENT

The business of the limited-liability company is in the charge of one or more managers (*Geschaefstfuehrer*), who may or may not be members of (subscribers to) the company and who may be either Germans or foreigners. They are appointed by the general meeting or in the same manner as directors of a share company and may be removed at any time by those appointing them; but the charter may limit removal to "cogent grounds" (gross neglect of duty or incapacity).¹¹

The managers have the same right to represent the company in dealing with third parties and in the conduct of the business as the directors of a share company. (See "Directors and managers as agents", p. 236.) They act in all judicial and extrajudicial transactions and sign¹² on behalf of the company in the manner specified in the charter, and the company acquires rights and incurs liabilities by reason of the transactions on its behalf by the managers.¹³

The managers collectively must make application for entry in the mercantile register of (a) the formation of the company, (b) increases and reductions in capital, (c) changes in the appointments of managers and the limitations upon their powers, (d) dissolution of the company except by bankruptcy, and (e) the names of the first liquidators.¹⁴

They are liable to the company for the observance of the limitations imposed upon their authority either by the charter or the general meetings, but this limitation does not affect third parties.¹⁵

The specified duties of the managers are (a) to see that the books of the company are properly kept; (b) within the first 3 months of each business year¹⁶ to draw up a balance sheet¹⁷ and profit and loss account for the preceding year;¹⁸ and (c) in January of each year to file with the court in charge of the mercantile register a list of the members of the company, with their addresses, occupations, and the amounts of their respective contributions.¹⁹

SUPERVISION

In a limited-liability company a board of supervisors (*Aufsichtsrat*) is not required by law and is necessary only when the charter

¹⁰ G.m.b.H.G. 47.

¹¹ G.m.b.H.G. 6, 38, 46.

¹² The managers must supply the court with specimens of their signature (G.m.b.H.G. 39).

¹³ G.m.b.H.G. 35-36.

¹⁴ G.m.b.H.G. 7, 39, 57-58, 65, 67, 78.

¹⁵ G.m.b.H.G. 37. The doctrine of *ultra vires* is unknown in German law. Directors of an American corporation obtain their powers by grant from the stockholders, whereas managers (*Geschaefstfuehrer*) of a German limited-liability company and directors (*Vorstand*) of a German share company obtain their powers directly by law. The powers of such managers and directors may be implied from their positions, with one exception—the charter or a majority vote of a general meeting may provide that two or more managers or directors must act jointly to bind the company.

¹⁶ The charter may extend this period to 6 months; and if business is carried on beyond the seas, to 9 months (G.m.b.H.G. 41).

¹⁷ The details to be reported in the balance sheet are by no means so carefully set forth or complete as for share companies. The balance sheet of a limited-liability company must follow the rules of the Commercial Code, sec. 40, as modified by the limited liability company act, sec. 42.

¹⁸ G.m.b.H.G. 41.

¹⁹ If there has been no change since last filed, a declaration to that effect suffices (G.m.b.H.G. 40).

so stipulates. Otherwise the duties of the supervisors are discharged by the general meetings of members.

When the charter provides for supervisors, the same laws²⁰ which apply to supervisors in a share company²¹ apply to them.

Usually a board of supervisors for a limited-liability company is desirable only if supervision by the general meetings is unwieldy because of the large number of members attending.

CORPORATE CHANGES

ALTERATIONS IN THE CHARTER

Changes in the charter of a limited-liability company are effected in the same manner as for share companies, that is, by a resolution passed by the members at a general meeting. The necessity for the general meeting and the resolution may be dispensed with, however, in the case of a limited-liability company, if the approval of all the members to such alteration is obtained in writing or they consent that their votes be given in writing.²²

The resolution, when necessary, ordinarily requires a majority of three fourths of the votes cast, but additional requirements may be imposed by the charter. It must be authenticated by a notary or judicial officer, as must any other resolution of a limited-liability company or a share company.

An alteration in the obligations of members from those imposed by the charter requires the consent of all.²³

To effect a change in the charter of a limited-liability company, that fact must be notified for entry in the mercantile register and must be published in accordance with the provisions of the charter. The change does not become legally operative until it has been so entered in the register in the place in which the company has its principal business office.²⁴

Increases in capital.—For an increase in the capital (which is considered an alteration of the charter) of a limited-liability company the same requirements as for any other alteration must be complied with. The subscription for the new capital must be executed in the form of a declaration drawn up and authenticated by a notary or judicial officer.²⁵

If the contributions to new capital are to be made otherwise than in cash or are to be set off against the purchase price of property to be acquired by the company, the name of the person contributing or selling the property, the nature of the contribution or of the property purchased, and the price at which such contribution is valued or the property is to be purchased must be recited in the resolution and must also be specified in the declaration of subscription.

The new shares may be allotted to the existing members or to others. The latter become members of the company upon signing the subscription declaration. Any obligations (other than the amount of their subscription) assumed by such new members must be re-

²⁰ H.G.B. 243-249; and claims for compensation against such supervisors for breach of their obligations are barred in 5 years.

²¹ G.m.b.H.G. 52. (See also "Supervision", p. 38 hereof.)

²² G.m.b.H.G. 48.

²³ G.m.b.H.G. 53.

²⁴ G.m.b.H.G. 54.

²⁵ G.m.b.H.G. 55.

cited in the declaration of subscription, otherwise they will not be bound to them.²⁶

When the new capital has been provided,²⁷ application must be made for entry in the mercantile register and be accompanied by the declaration of subscriptions to the increased capital (or an authenticated copy thereof) and a list of the persons and the amount subscribed by each. The persons making the application are jointly and severally liable to the company for the correctness of the information supplied.²⁸

Reductions in capital.—For a reduction of capital (which also is considered to be an alteration in the charter) the same requirements as in the case of other alterations must be complied with. The resolution therefor must be published by the managers three times in the newspaper specified in the charter, and such notification must contain a request to creditors to file their claims.²⁹ Creditors who give notice of their claims and withhold consent to the reduction of capital must be satisfied or secured. The application for registration of the reduction in the mercantile register must not be made before one year from the date of the publication of the third notice to creditors.³⁰ The application for registration must have annexed to it the public notice of the resolution, and the managers must certify that creditors who have filed claims and withheld consent to the reduction have been satisfied or secured.

The resolution for the reduction of capital must not leave the company with capital less than that ordinarily required for a limited-liability company (20,000 marks).³¹

DISSOLUTION AND LIQUIDATION

A limited-liability company is dissolved for the same reasons and upon the same grounds as a share company, namely, through expiration of the period for which formed, by resolution of a general meeting, or bankruptcy.³² (See "Dissolution" under share companies, p. 42.) It can also be effected by order of the court at the principal place of business of the company if the objects for which it was formed become unattainable or for cogent reasons connected with the affairs of the company.

In the latter cases the action therefor must be brought against the company as the defendant and can be brought only by members whose shares aggregate at least one tenth of the capital.³³ It may also be effected by the State authorities where the public welfare is endangered because the members of the company insist upon passing illegal resolutions or knowingly allow illegal transactions to be entered upon.³⁴

²⁶ G.m.b.H.G. 56.

²⁷ The subscriptions for increase of capital must be made available in the same manner as original subscriptions. One fourth of the amount subscribed by each member must immediately be deposited with the managers (G.m.b.H.G. 7).

²⁸ G.m.b.H.G. 57.

²⁹ An additional special request must be sent personally to all creditors known as such.

³⁰ The registration of the reduction of capital must also be made wherever the company has branches, but such registration is not required to be as complete as the registration at the principal place of business (G.m.b.H.G. 59).

³¹ G.m.b.H.G. 58.

³² G.m.b.H.G. 60.

³³ G.m.b.H.G. 61.

³⁴ G.m.b.H.G. 62. A share company also may be dissolved for these reasons.

Where the dissolution of a company is brought about by bankruptcy,³⁵ the trustee administers the estate (see "Bankruptcy," p. 175); but the managers and general meetings continue to assist in the supervision of the business.

The dissolution of a limited-liability company, unless caused by bankruptcy, must be notified for entry in the mercantile register, as must also the continuance of such company in the event bankruptcy proceedings against it are stopped. Public notice of the dissolution must be given, requesting creditors to file their claims in the same manner as in a reduction of capital.³⁶

The dissolution, except by bankruptcy, is carried out by the managers unless others are designated in the charter or by resolution of the general meetings. Members whose contributions equal one tenth of the company capital may also apply to the court for the appointment of liquidators on cogent grounds. Liquidators may be removed under the same conditions as those under which they were appointed; and even if such liquidators were appointed by the court, they may subsequently be removed by resolution of the members.³⁷

The names of the first liquidators must be notified by the managers for entry in the mercantile register, but subsequent changes in the personnel or in the powers of the liquidators must be notified by the liquidators themselves.³⁸

During liquidation the legal position of a company and of its members and its managers is regulated by the same rules that govern them before liquidation. The managers (unless superseded by liquidators), the general meetings, and the board of supervisors (if any) perform the same services to the company during liquidation as before.³⁹

The liquidators must execute declarations and sign in behalf of the company collectively (unless otherwise provided), by affixing their own names with that of the company, with an indication that the company itself is in liquidation. They terminate pending transactions, perform obligations of the company, demand and collect debts, and convert the property of the company generally into cash. They may even enter into other transactions in order to terminate pending obligations. They act on behalf of the company in place of the managers and with the same powers. They have the same rights and liabilities as managers and as such must prepare balance sheets immediately upon the commencement of the liquidation and annually thereafter.⁴⁰

Upon liquidation, the members are entitled to a distribution of the property of the company in proportion to their respective shares unless the charter provides otherwise, but only after the company's debts are paid or security given therefor.⁴¹ Under no circumstances

³⁵ In the event of bankruptcy the managers must immediately apply for adjudication and are liable for all payments made by them after the time when they should have done so. Bankruptcy must be instituted when the liabilities exceed the assets or in case of alleged insolvency. The rules as to such proceedings, which apply alike to limited-liability companies and share companies, are contained in K.O. 207-208 (G.m.b.H.G. 63-64).

³⁶ G.m.b.H.G. 65.

³⁷ G.m.b.H.G. 66.

³⁸ G.m.b.H.G. 67.

³⁹ G.m.b.H.G. 69.

⁴⁰ G.m.b.H.G. 68, 70-71.

⁴¹ When creditors whose identity is known do not file claims upon request, the sums owing them must be deposited with the public authorities for their benefit.

are the members entitled to any distribution before a year has elapsed from the time of the third publication of the request to creditors to file their claims. Liquidators are liable for any breach of their duties with regard to distribution and for any wrongful distribution.⁴²

After liquidation the books and papers of the company must be deposited with a member or with someone specified in the charter or by resolution of a general meeting or appointed by the court for that purpose, to be kept by him for 10 years and to be readily accessible and open for inspection to any interested party.⁴³

DISTINCTIONS BETWEEN THE A.G. AND THE G.M.B.H.

Germany has two important forms of corporate organization, the share company (Aktiengesellschaft, or A.G.) and the limited-liability company (Gesellschaft mit beschränkter Haftung, or G.m.b.H.), both embodying basic principles characteristic of the American corporation and especially the limited liability of the shareholders or members. Either may be the more suited for a particular need, and to determine which is the more desirable in any given instance all factors of cost, administration, flexibility, corporate control, etc., must be considered. The chief points of difference between the two are:

A.G.	G.m.b.H.
Responsibility of shareholders limited to the amount of their subscriptions (H.G.B. 178).	Responsibility of members limited, but subsequent additional payments can be provided in charter (G.m.b.H.G. 26).
The capital is divided into a definite number of shares with definite par value, of which shareholders may acquire any amount.	The participation holdings of members are not separate from, nor a divisible portion of, the company holding (G.m.b.H.G. 14, 15; but see 17, 55).
The transfer of shares is unobstructed and free (H.G.B. 179-180).	The transfer of member rights is surrounded by statutory difficulties (G.m.b.H.G. 15).
The shares are indivisible (H.G.B. 179).	The participation holdings are in certain cases divisible (G.m.b.H.G. 17).
Acquisition of its own shares by the treasury is limited (H.G.B. 226).	Acquisition of its own member holdings is less restricted (G.m.b.H.G. 33).
All contributions to capital must be paid in for the uses of the company and are not returnable.	Additional payments may be refunded unless required to cover losses of original capital.
The guaranty that the original capital is subscribed is insured by the liability of the founders, directors, and supervisors for their statements to that effect, required to be published and registered by them (H.G.B. 190, 203).	The members are jointly liable for supplying the original capital in full and for seeing that no unjustified refunds (reducing capital) are permitted (G.m.b.H.G. 24, 31).
Internal affairs generally regulated by law.	Internal affairs to a certain extent regulated by the charter (G.m.b.H.G. 45).
Minority rights numerous (H.G.B. 251, 264, 266-268, 295).	Minority rights limited (G.m.b.H.G. 50, 61, 66).
Five founders are required.	Two founders are sufficient.

⁴² G.m.b.H.G. 74.

⁴³ G.m.b.H.G. 73.

A.G.	G.m.b.H
Supervisors (Aufsichtsrat) obligatory (H.G.B. 190).	Supervisors optional (G.m.b.H.G. 52).
Management of company intrusted to directors (Vorstand).	Management of company intrusted to managers (Geschaeftsfuehrer).
Directors removable at any time (H.G.B. 231).	Managers removable, but "wichtige Grunde" may be provided for or be necessary (G.m.b.H.G. 38).
Directors directly liable to creditors (H.G.B. 241).	Managers not directly liable to creditors (G.m.b.H.G. 43).
Drawing up of balance sheets required by law (H.G.B. 239, 260, 263).	Drawing up of balance sheets optional (G.m.b.H.G. 45-46).
Balance sheet must be published (H.G.B. 265).	Publication of balance sheet necessary only in the case of a bank (G.m.b.H.G. 41).
The laws governing the preparation of the balance sheet are stringent (H.G.B. 261).	The laws governing the preparation of the balance sheet are not stringent (G.m.b.H.G. 42).
Shareholders can decide the affairs of the company only at a general meeting and by resolution (H.G.B. 250).	The written consent of the required majority is sufficient, in deciding company matters (G.m.b.H.G. 48).
For alterations in the charter only a three-fourths majority (or less) is required (H.G.B. 274-276).	For alterations in the charter at least a three-fourths majority is necessary (G.m.b.H.G. 53).
A majority can vote preferential shares (H.G.B. 275).	Issuance of preferential shares requires the consent of all the members (G.m.b.H.G. 53).
Capitalization must be at least 50,000 marks.	Capitalization must be at least 20,000 marks.

PARTNERSHIPS LIMITED BY SHARES

A partnership limited by shares (Kommanditgesellschaft auf Aktien) is a form of association no longer much used in Germany. It represents a combination of legal concepts, some of which are peculiar to the limited partnership and some to the share company.

It is in some respects a juristic person, in that it has independent rights attaching to its firm name and can acquire, hold, and dispose of property and sue and be sued.⁴⁴ The firm name of the partnership limited by shares must include its designation as such (Kommanditgesellschaft auf Aktien) and must be entered in the mercantile register⁴⁵ at the principal place of business and at all the branches as well.⁴⁶

Ownership of the property of the company is in the company itself. It is not divisible among the partners except upon dissolution or liquidation. The capital of the company upon formation must be in the hands of the personally liable partners, to be subsequently deposited to the account of the company.

FORMATION

MEMORANDUM OF ASSOCIATION (CHARTER)

The formation of the partnership limited by shares is accomplished in much the same manner as the formation of a share company. It requires a memorandum of association, examination (by

⁴⁴ H.G.B. 210, 320.

⁴⁵ In the entry in the mercantile register the names of the personally liable partners must be stated (H.G.B. 323).

⁴⁶ H.G.B. 20, 29-30.

special official examiners) of the circumstances attending formation, declaration for entry in the mercantile register, and publication.⁴⁷

A partnership limited by shares is brought about by the association of not less than five persons, who enter into and execute an agreement under notarial or judicial supervision and sanction. The personally liable partners must all join in its execution, and the limited partners who accept shares may also participate.⁴⁸

In the document itself must be set out (a) the number of shares subscribed for by each of the interested parties; (b) the firm name and the seat of the partnership; (c) the amount of the partnership capital and the par value of each share; (d) the way in which the general meetings of the partners may be called; (e) the form in which public notices are to be given by the company; (f) the names, occupations, and addresses of the personally liable partners; (g) the contributions made to property by the partners personally liable, with the value of such contributions and their nature; and (h) the special privileges to be enjoyed by the partners personally liable.⁴⁹

DIVIDENDS AND RESERVES

Dividends to limited partners may be declared out of profits shown by the balance sheet, but personally liable partners are not entitled to their dividends unless the capital assets exceed the aggregate of the liabilities.⁵⁰

A reserve fund must be created, in which must be deposited, until the fund equals one tenth of the company capital (or more if so provided in the memorandum of association): (a) At least one twentieth of the net profits of the personally liable partners; (b) all premiums received from the sale of shares, less costs; and (c) any sums paid by partners for preferential rights if the capital is not increased, unless such sums are written off to cover losses

RIGHTS AND LIABILITIES OF THE PARTIES

A partnership limited by shares must be composed of at least one general partner who is unlimitedly liable to creditors of the business and any number of other members who are involved only to the extent of their subscriptions paid on the shares into which the capital is divided.⁵¹ The personally liable partners have rights, duties, and obligations similar to those of general partners in a limited partnership, while the limited partners have the rights, duties, and obligations of shareholders in a share company.⁵²

CONDUCT OF THE BUSINESS

MANAGEMENT

The rules and regulations as to directors of share companies apply to personally liable partners,⁵³ and they are entitled to manage the company in the same manner as directors of share companies. Their liability and duties with regard to the partners with limited liability

⁴⁷ H.G.B. 182, 321-323.

⁴⁸ H.G.B. 321.

⁴⁹ H.G.B. 182, 322.

⁵⁰ H.G.B. 329.

⁵¹ The personally liable partners need not hold any of these shares, but they are permitted to do so.

⁵² H.G.B. 320.

⁵³ H.G.B. 325.

are the same as those of general partners to limited partners in a limited partnership.

They are not permitted to engage in business of the same kind as that conducted by the partnership without the consent of all the partners with limited liability expressed in a general meeting.⁵⁴ The personally liable partners have no vote at general meetings even if they hold shares of the company; but their consent is required to resolutions of general meetings whenever in a limited partnership the agreement of the general partners would be necessary.

They have no authority to vote either for the appointment of examiners where the partners with limited liability wish to appoint them or where the minority shareholders wish to bring suits for claims arising out of the formation of the association.⁵⁵

SUPERVISION

The resolutions of general meetings of limited partners are to be carried out by the board of supervisors, unless the charter provides otherwise, and these supervisors also institute legal proceedings against the personally liable partners when this action is necessary. The personally liable partners cannot be supervisors.⁵⁶

CORPORATE CHANGES

DISSOLUTION AND LIQUIDATION

Dissolution may be effected in the same manner and for the same reasons as in the case of a limited partnership. A partnership limited by shares is dissolved by the bankruptcy, retirement,⁵⁷ or expulsion of the personally liable partners; but it is not dissolved by the bankruptcy, retirement, or expulsion of a partner with limited liability. The limited partners, in order to dissolve the company, must do so by resolution of a general meeting passed by a three-fourths majority of the company capital present and voting, unless the charter provides for a larger majority.⁵⁸

Where it is not otherwise provided in the charter, liquidation is carried on by the personally liable partners with one or more additional liquidators chosen by the general meeting, but the personally liable partners may apply to the court for the appointment of liquidators or the removal of those appointed.⁵⁹

CONVERSION TO SHARE COMPANY

This form of company can be changed to a share company by resolution of a general meeting according to the rules relating to a change in the charter of a share company.⁶⁰ The aggregate of the shares of the majority of the limited partners voting in favor of the conversion must represent at least one fourth of the share capital of the company not held by personally liable partners, and the resolution therefor must carefully set forth the measures necessary to carry out the conversion, the firm name to be used, the method of appointing the directors, etc.⁶¹

⁵⁴ H.G.B. 326.

⁵⁵ H.G.B. 327.

⁵⁶ H.G.B. 328.

⁵⁷ Personally liable partners may not retire unless authorization so to do is given in the charter (H.G.B. 330).

⁵⁸ H.G.B. 329.

⁵⁹ H.G.B. 331.

⁶⁰ H.G.B. 274.

⁶¹ H.G.B. 332.

IV. TAXATION OF BUSINESS

WHAT CONSTITUTES "DOING BUSINESS"

Upon the post-war stabilization of German currency, many foreign business men went to Germany to study the situation, with the introduction of their goods into the German market or a continuance of their already established business relations there in view. Although this trade-promotive effort has been somewhat interrupted by the unstable conditions of the past few years, it will undoubtedly be resumed when times again are normal; and a consideration of the problems of foreign commercial organizations when doing business in Germany is therefore appropriate.

Germany boasts that its commercial law allows the enjoyment and exercise of the principles of freedom of trade. It guarantees to foreigners the same rights and benefits as are accorded its own citizens. Article 151 of the Constitution grants "freedom of commerce and trade", and article 1 of the regulations of trade (*Gewerbeordnung*) sounds this same note in the words, "everybody is free to exercise a trade." Of course, however, freedom of trade necessarily is granted, to both nationals and foreigners, only under the authority and supervision of the Government.

DOING BUSINESS "WITH" GERMANY

When a foreign concern desires to sell goods to German customers, it is confronted with three problems. The primary question is whether it is "doing business in Germany." The other two are secondary and dependent on the answer to the first; they are the necessity for registration of the business and the liability for taxation. It can readily be seen that an answer in the negative to the first question obviates consideration of the others, because a firm not doing business in Germany is not obligated to register and is not liable for taxes.

If a foreign firm stays at home and takes orders there for shipment to Germany, it may be said to be doing business *with* Germany rather than *in* Germany. Virtually the same rules then obtain that prevail in the United States when business is carried on between merchants in different States. There will be no necessity for registration of the business in Germany, and there will be no liability to taxation¹ because such transactions will not be construed as "doing business in Germany." The right of foreign firms in such cases will be exactly the same as the right of German nationals to sue and be sued in Germany if jurisdiction can be obtained by the courts. The only disability which the foreign firms may suffer is that they will probably be required by the courts to give security for costs and legal fees; but they may avoid even this by assigning their claims to a German and allowing him to sue in his own name.

¹ This is true except in the case of a contract for the use of a foreign patent, trade mark, or copyright in Germany, when a tax on the income derived is payable—usually by the German firm. (See "Industrial-property tax" on p. 65.)

DOING BUSINESS "IN" GERMANY

Difficulties begin to arise, however, when the foreign firm has its own agents traveling in Germany, or sells through a commission agent in Germany, or sends its merchandise to a German firm on consignment. In such cases the foreign firm is held to be "doing business in Germany", and it thereby becomes liable to taxation and registration (a) if it owns property in Germany in connection with the conduct of its business, (b) if it maintains a business office in its own name or a branch or factory in Germany, or (c) if it has a permanent representative² or employee-agent residing there.

Where a foreign firm retains a German, or a resident of Germany, or a permanent representative as its agent or intermediary to the German trade, it is construed to be "doing business in Germany" and must, as any other German mercantile business, register and pay taxes.³

DOING BUSINESS THROUGH A BRANCH OR SUBSIDIARY

German branches of foreign businesses may also be organized to do business in Germany, in which event they must be registered in the mercantile register so that they may be properly qualified to do business as ordinary German mercantile organizations.⁴ It may be said in this connection from experience that the organization of a branch of a foreign business is both unwieldy and undesirable. It entails, especially in the case of a corporation, the filing of many documents, all of which must be authenticated. In the case of foreign firms generally, it subjects them to liability for all the debts and obligations contracted by the branch, and the branch never loses its disadvantage of having a foreign connection. There are very few firms conducting their business in Germany through a branch today.

The German tax authorities seem to look with suspicion upon this set-up because it gives opportunity for the foreign firm to conceal its profits made in Germany. The tax law of 1925 (art. 34) provided, therefore, that they might tax a branch on the basis of the earnings of a German firm engaged in a similar enterprise. No difficulty will be encountered, however, from this law, and the tax will be assessed correctly and according to the same law as applies to German businesses, if profits of the branch are fairly declared.⁵ To determine this, the tax authorities may, if they doubt, insist upon the production of the balance sheet of the home company covering its entire operations.

² The term "permanent representative" (staendige Vertreter) appears in the income and corporation tax laws of 1925, and parties who may be considered such subject the foreign business organization which employs them to German taxes. The Minister of Finance, in his instructions upon these laws to the tax authorities, seemed to indicate that for the time being the term would not embrace general commission merchants and other such intermediaries so long as they remained independent and could not be construed to be employees of the foreign firm; but his instructions may have been only temporary and therefore subject to change at any time.

³ When the foreign firm does business in Germany continuously through its own employees an understanding may be reached with the Minister of Finance whereby a lump sum can be paid in liquidation of such tax liability.

⁴ See "Registration requirements", pp. 9-10.

⁵ To facilitate payment of the Gesellschaftsteuer on the capital invested in the branch and the Vermoegensteuer on operating property, it is often desirable for the home company to allocate by resolution a certain amount of capital for the branch, so that formal proof may be at hand to establish the working capital of the branch on which the tax authorities may assess.

Where a foreign corporation or other business enterprise organizes a German subsidiary, such subsidiary, obtaining its recognition and privileges through German law, incurs all the tax liability of a German company.

THE FEDERAL TAX SYSTEM*

The tax system of the National Government includes the following levies of principal interest to American individuals and firms:

1. Income tax (Einkommensteuer)—10 to 40 per cent.
2. Crisis tax (Krisensteuer).
3. Corporation tax (Koerperschaftsteuer)—20 percent (levied on corporate income).
4. Securities tax—10 percent.
5. Industrial-property tax.
6. Industrial charges (Industriebelastung)—4.5 percent.
7. Property tax (Vermoegesteuer)—5 per thousand (average rate).
8. Inheritance tax (Erbschaftsteuer)—2 to 60 percent.
9. Turnover tax (Umsatzsteuer)—2 percent.
10. Bills of exchange tax (Wechselsteuer)—1 per thousand.
11. Transfer of capital tax (Kapitalverkehrsteuer)—(a) tax on corporate rights (Gesellschaftsteuer), 2 percent; (b) tax on securities (Wertpapiersteuer); (c) stock-exchange turnover tax (Boersenumsatzsteuer).
12. Purchase of land tax (Grunderwerbsteuer)—3 percent.
13. Automobile tax.

Where the tax is required to be withheld at source, as in the case of wages and of income from capital property such as dividends, the debtor of the income must forward the proper tax amount to the tax office in his district within 1 week after the payment falls due.

LIABILITY OF FOREIGNERS TO TAXATION

In general, a foreign individual who has his domicile in Germany or has lived there for more than 6 months is under the same tax liability as a resident German.

A foreign firm which sells direct to a German dealer or through a regular commission agent or broker in business for himself should not encounter tax liability on the German business thus concluded.

But a foreign firm becomes liable to taxation in Germany if it owns property, or maintains an establishment of some kind (Betriebsstaette), such as a branch, sales office, or factory, or has a permanent representative (staendige Vertreter) there;⁷ or if it does business continuously through one of its own employees or through a German individual or firm under circumstances that cause the latter to be regarded as its employee in the strict sense.

Foreign individuals and companies are taxed (a) on income derived from business for which they maintain an office or appoint a

* From this point on the discussion of taxation is, in the main, condensed from articles by Joseph H. Barkmeier which appeared in the issues of Feb. 8 and 16, 1933, of the General Legal Bulletin (C.L. 347 and 348) published by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

⁷ See footnote 2, p. 59.

permanent representative in Germany,⁸ (b) on dividends on shares of a German share company or limited-liability company, (c) on interest on obligations secured by real estate⁹ situated in Germany, (d) on income derived as a dormant partner in a German business, (e) on interest on debentures issued in the open market when the borrower is located in Germany,¹⁰ (f) on profits realized from the sale of real estate in Germany when the acquisition is made for speculative purposes¹¹ and the aggregate profits in 1 year exceed 1,000 reichsmarks, and (g) on income derived from the lease of patent rights for exploitation in Germany.

Dividends on shares of share companies and limited-liability companies, earnings as dormant partners, interest on mortgages or other rights secured by real estate, and interest on debentures are taxed by deductions at source.

Certain State and municipal taxes on profits, salaries, and real estate may also come into consideration.

INCOME TAX

Only physical persons are subject to the income tax.¹²

Unlimited liability to the income tax arises when an individual has his domicile (Wohnsitz) or habitual residence (Aufenthalt) in Germany. If a foreigner is domiciled in Germany or has lived there for more than 6 months, he becomes subject to unlimited tax liability on the same footing as a domiciled or resident German; that is, he is assessed on his total income from all sources, foreign as well as domestic, regardless of whether any part of it has been assessed elsewhere. If a foreigner has no residence in Germany, he is subject to taxation only on income from sources within Germany (limited liability).¹³

When the rules regarding unlimited liability have entailed hardship for the taxpayer, the Ministry of Finance has in the past

⁸ No tax is levied should such a foreign corporation, during the first year, operate in Germany at a loss or show profits sufficient only to cover organization and overhead; but if, through questionable bookkeeping, the net profits from the German business of the firm are reduced or are evidently in disproportion to the average earnings in similar German businesses, the tax authorities may assess a fictitious income based on the average earnings of like enterprises or upon the usual return of interest on the capital invested in the German branch; and the tax authorities need not prove their suspicion.

⁹ But not if secured on movables in Germany.

¹⁰ But not on debentures of German companies issued abroad and not listed on German stock exchanges.

¹¹ But not on profits realized from speculation on German stock exchanges or even from the sale of goods outside the scope of his business.

¹² The German income tax law distinguishes between two tax-paying groups, namely, Lohnsteuer (wage or salary tax), which is withheld and paid by the employer, and Einkommensteuer der Veranlagten (assessed income tax), which is declared and paid by individuals who have income from an independent occupation or source.

¹³ An order of the Finance Minister, issued Dec. 30, 1931, discussing the fourth emergency decree of Dec. 8, 1931, states: "When a person has no domicile in the country and has not remained in it longer than 6 months, he has not unlimited liability to taxation unless it appears from the circumstances in the case that he intended to make more than a temporary stay. Accordingly, all circumstances in each case must be considered. It may be of special importance to know whether the sojourn is for business reasons that recur every year and are therefore of some permanence. If, for example, a person domiciled abroad is the chief owner (from a business viewpoint) of a domestic concern and sojourns in the country for several months each year, devoting himself to the affairs of such concern as an individual merchant or member of the managing board, it must be ascertained whether such visits show an intent to make more than a temporary stay in the country. It is impossible to lay down generally applicable rules owing to the varying conditions in individual cases; it is rather the particular situation in each case that must be taken into consideration. The main things to be considered are the business interests of the taxable person, on the one hand, and the importance of the proper execution of the tax laws, on the other."

entered into agreements whereby certain kinds of income would be exempt for a period or permitted the payment of a lump sum.

COMPUTATION OF TAX

A person whose income is less than 1,300 reichsmarks a year is not subject to the income tax. This exemption is increased for a family man by 100 marks for the wife, 100 marks for the first child, 180 marks for the second child, 360 marks for the third child, 540 marks for the fourth child, and 720 marks for the fifth child and for each additional child less than 18 years of age. These provisions, as well as deductions from the income¹⁴ such as family allowances, do not apply to persons subject to restricted liability. In computing the net taxable income, 720 marks is tax free if the income is not over 10,000 marks a year.

For the purpose of computing the tax, the net income minus allowable deductions, such as special contributions (social-insurance premiums, etc.) and the tax-free amount, is rounded off as provided by the emergency decree of December 1, 1930. Incomes above 12,000 marks are rounded off to the next full thousand, embracing 500 marks below and 500 marks above—for example, amounts between 12,500 and 13,500 marks are rounded off to 13,000 marks.

The income-tax rates are graduated according to the taxable income. Since the basic income-tax law was passed in 1925 the rates have been substantially unchanged, but there is, of course, no assurance that they will so continue. The current rates start at 10 percent for the first 8,000 reichsmarks and increase to 40 percent.¹⁵

PAYMENT OF TAX

In the case of salaried persons, the tax (at present 10 percent) is paid by the employer for the account of the employee, and the employer reimburses himself by deducting the tax when paying the salary. If the income of the wage earner exceeds 8,000 marks, he must declare it and pay the balance of the tax himself.

When dividends are distributed by a German share company, the company deducts the income tax of 10 percent and delivers this amount to the tax office. The resident shareholder must include the dividends in his taxable income but may credit the tax already paid. The nonresident shareholder bears only the 10 percent tax.

The assessed income tax¹⁶ is payable in four installments—on the 10th days of March, June, October, and December. The previous year is taken as the basis of assessment. If the taxpayer is unable to meet the payments, an appeal for an extension may be made, upon a full presentation of the circumstances. The extension, if granted, seldom exceeds a few weeks.

Individuals whose incomes are over 8,000 marks or who are subject to the assessed income tax pay a surtax (*Zuschlag zur Einkom-*

¹⁴ To facilitate computation of deductions for dependents (which are given in the law as specific sums of money or as percentages of income), the German Finance Ministry has published charts showing the amount to be deducted from the tax itself, varying according to the number of dependents and according to whether less or more than 50 percent of the income is derived from wages.

¹⁵ Prompt notice of changes in the income-tax rates appears in the General Legal Bulletin issued by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

¹⁶ See footnote 12, p. 61.

mensteuer) of 5 percent. The surtax on the income tax of single persons is applicable at the rate of 10 percent in the case of wage earners when their income is over 2,640 marks (220 marks monthly), and in the case of persons subject to the assessed income tax when their income is over 2,160 marks a year.

Effective March 31, 1933, a special tax (independent of the income tax) was placed on remuneration of every kind paid by public or private companies to member of their supervisory boards (Aufsichtsrat), the tax to be paid by withholding at source. The rate is 10 percent when the recipient of the fees, bonuses, etc., is subject to unlimited tax liability and 19 percent when he has restricted liability (not domiciled or habitually resident in Germany). If the firm itself assumes the tax, the rates are increased to 11.11 percent and 21.11 percent, respectively. The company is jointly liable with the supervisor for the withholding and payment of the tax.¹⁷

CRISIS TAX

The crisis tax (Krisensteuer), established by the emergency decree of June 5, 1931, to raise funds for social-welfare purposes, was placed, in the case of wage earners, on the gross monthly wage or salary, ranging from 1 percent on wages up to 300 marks a month to 5 percent on wages of 3,000 marks or over. A decree of June 14, 1932, abolished the crisis tax insofar as it pertained to wage earners and established a tax for unemployment relief (Abgabe zur Arbeitslosenhilfe), which is much the same in principle.

All recipients of wages or salaries who have their domicile or habitual residence in Germany are subject to the tax. Profit-sharing and other income in lieu of or supplementing salary are included under salary. Government employees whose salaries were reduced by the decrees of June 5 and December 8, 1931, are taxed at the rate of 1.5 percent. The tax on wage earners is withheld by the employer and deducted from the gross monthly wage or salary; it ranges at present from 1.5 percent for wage earners receiving up to 125 marks a month to 6.5 percent on wages or salaries amounting to 3,000 marks or over.

The decrees of June 6, 1931, and June 14, 1932, provide for the assessment of a crisis tax (Krisensteuer der Veranlagten) on persons subject to the assessed income tax. This tax is payable on the net yearly income shown on the income-tax return before the tax-free portion and the family allowances are deducted. At present this tax ranges from 0.75 percent on net incomes up to 3,600 marks to 4 percent on net annual incomes of 1,000,000 marks and over.

CORPORATION TAX

The corporation tax (Koeperschaftsteuer) is levied on the income of foreign and domestic corporations, including the share company (Aktiengesellschaft) and the limited-liability company (Gesellschaft mit beschaenakter Haftung). If the seat or the principal

¹⁷ For additional information on the computation and payment of this tax see General Legal Bulletin 29 (C.L. 366), issued by the Commercial Laws Division, Bureau of Foreign and Domestic Commerce, Washington.

administrative center is situated in Germany, the corporation is assessable on its entire income from all sources. The nonresident company is taxable only on property owned in Germany or income derived from German sources. If a foreign concern organizes under German law a subsidiary company, the local enterprise will be taxed on its entire profits in the same way as any other German company, and the parent concern on the distributed profits flowing to it in the form of dividends.

In general, the German branch (*Zweigniederlassung*) or permanent agent (*staendige Vertreter*) of a foreign enterprise is liable to tax only in respect of income derived from German sources. However, as such establishments have sometimes endeavored to conceal the profits actually made in Germany, the income tax law and corporation tax law contain provisions whereby, in such cases, the tax authorities may assess the branch at an amount that is earned by similar German independent enterprises and equal at least to the customary interest on the capital allotted to the branch, inclusive of operating capital and stock on hand. The same rule applies where the profits of the German subsidiary company of a foreign concern are obviously out of proportion to the earnings of similar German companies. If such profits are difficult to ascertain, an understanding may be reached with the Minister of Finance whereby a lump sum can be paid in liquidation of the tax liability.

The tax authorities are allowed considerable discretion in selecting the method of assessment where the net profit of the branch is in doubt; sometimes the ratio of the gross profits realized in Germany to the total gross profits is used. The fiscal authorities have the power to agree to an estimated lump sum (*Pauschbetrag*) in payment of the corporation tax, which frequently applies to several years.

In practice, the tax office is satisfied with the balance shown by the properly kept books of the branch; but if they have any reason to doubt the accuracy of the accounts submitted, the officials may call for the balance sheet of the home company covering its operations in all countries, or may make an arbitrary assessment as previously described. A German subsidiary in any case must submit a copy of its balance sheet along with its tax declaration.

TAX RATE

The corporation tax rate is 20 percent of the net profits.¹⁸ Reduced rates are accorded the limited-liability company with a capital not exceeding 50,000 reichsmarks; it pays the graduated income tax applicable to individuals up to a maximum rate of 20 percent of the net profits.

The tax is payable in four installments—on the 10th day of March, June, October, and December. The previous year is taken as the basis of assessment. If the taxpayer is unable to meet the payments, an appeal for an extension may be made, upon a full presentation of the circumstances. The extension, if granted, seldom exceeds a few weeks.

A claim based on the taxable profits is outlawed after the lapse of 5 years (art. 121 of the federal tax regulations), but such limita-

¹⁸ A German company holding at the beginning of any fiscal year at least 25 percent of the shares of another company pays no income tax thereon.

tion is interrupted if the authorities take any official steps against the particular firm within this time toward the assessment or collection of taxes. In cases of fraudulent failure to pay taxes the term of limitation is extended to 10 years.

SECURITIES TAX

A decree of October 16, 1930, abolished as of January 2, 1931, the withholding of a 10 percent tax on income from fixed-interest-bearing securities, which include (a) loans which are registered in a German public register and (b) loans represented by bonds (Teilschuldverschreibungen). According to the fourth emergency decree of December 8, 1931, the 10 percent rate of tax on gross income (restricted liability) applies to foreign companies and individuals on the following incomes only: Interest from mortgages (Hypotheken), land charges (Grundschulden), dividends and other income from stocks, mining shares, limited-liability company shares, and participations in other types of German companies.

The tax on income from shares in a limited-liability company is not subject to withholding at source, as in the other cases enumerated, but is assessed directly against the shareholder.

INDUSTRIAL-PROPERTY TAX

Under the basic income tax law of 1925 (art. III, par. 2, (3)), income from artistic, literary, and industrial property rights in general is liable to the full rates of income and corporation taxes. Considerable uncertainty existed relative to the tax liability of nonresident individuals and firms on income received from the leasing of industrial-property rights and copyrights of various kinds in Germany; decisions of the court of tax and customs appeals (Reichsfinanzhof) held that unless registration in a German public register was effected (see "Industrial-property rights" at pp. 185 to 201) income from such sources would not be subject to tax.

The presidential decree of December 8, 1931, however, extended this tax to specifically cover the temporary leasing of all literary, artistic, and industrial copyrights and industrial processes, and since that date tax liability has been considered as broadened to include such rights, whether registered in Germany or not. All that is required to make a licensor liable to this tax is that the right to use has been granted for a consideration.

The decree also empowered the Minister of Finance to establish the rate of tax and to provide for its deduction at source on certain types of copyright income when paid by resident German individuals and firms to nonresidents. Ministerial regulations effective January 1, 1933, made persons subject to restricted liability (that is, not domiciled in Germany) liable to a 10-percent tax on gross income received from independent professional activity of a literary or artistic nature which is exercised in Germany and from the temporary leasing of literary and artistic copyrights. The tax is now to be withheld by the debtor (licensee) for the account of the creditor (licensor), but need not be if the income is not expected to exceed 500 marks during a calendar year. If during the year the income

should exceed 500 marks, the tax for the full amount must be deducted from later payments to the licensor.

Royalties paid by a German under a licensing agreement to an American individual or organization are taxed as income of the American owner. This tax not being subject to deduction at source, the American licensor must declare such profit and pay a tax thereon—of 20 percent if a company and the usual income-tax rate if an individual.

INDUSTRIAL CHARGES

There is a law for the production of the industrial charges (Aufbringungsgesetz) under the Dawes Plan, whereby a tax has been assessed in accordance with the provisions of the industrial charges law (Industriebelastungsgesetz). While the industrial charge was extinguished on reparations account when the Young Plan came into force in May 1930, the German Government is free to continue it for internal purposes and, in fact, has retained it with certain modifications.

The Government has reduced the charges gradually, and according to the law of March 31, 1931, they will be discontinued at the close of the fiscal year 1936. In the fiscal year 1932 only industrial and commercial enterprises having a working capital of over 500,600 reichsmarks were liable.

The rates are based on the working capital as assessed for the property tax (Vermögensteuer). The rate for the fiscal year 1933 is 4.5 per thousand, payable in two equal installments on August 15, 1932, and February 15, 1933.

PROPERTY TAX

Individuals having their domicile or residence for more than 6 months in Germany and corporations having their seat and principal administrative center there are subject to the property tax (Vermögensteuer) on the assessed value of their entire real and personal property located in Germany and abroad. Nonresident individuals and corporations are taxable only with respect to real and certain personal property¹⁹ situated in Germany. In the case of persons having unlimited tax liability, the first 20,000 reichsmarks of property is exempt.

The tax falls due in quarterly installments on the 15th day of February, May, August, and November.

The normal rate of the tax is 5 per thousand on the assessed value of the property rounded off to the last 100 marks. The rate is reduced on amounts less than 50,000 marks and increased on amounts over 250,000 marks.

INHERITANCE TAX

The inheritance tax, with rates ranging from 2 to 60 percent, is payable on (1) property acquired by descent or will, (2) gifts inter vivos, and (3) gifts causa mortis and inter vivos subject to the fulfillment of a definite purpose or condition. The entire estate is tax-

¹⁹ No tax is payable by them on securities of any kind, objects of art, cash, automobiles, furniture, etc., in Germany acquired for private and not for business purposes.

able if the testator at the time of his death or the beneficiary at the time when liability to taxation arises is resident in Germany. The term "resident in Germany" includes foreigners having their domicile or permanent residence in Germany and corporations having their seat or principal administrative center there.

In all other cases the tax is collected only on domestic agricultural, forestry, and horticultural property, domestic operating (Betriebsvermoege*n*) or landed property, rights of usufruct to such property, and titles (Rechten) the transfer of which involves registration in domestic records.²⁰

Insofar as the estate consists of foreign real property, claims against foreign debtors, and titles the transfer of which is conditional upon registration in foreign records, the inheritance tax collected by the respective foreign State may, upon request, be deducted from an estate or, in lieu thereof, the amount of the foreign tax may be charged to the German inheritance tax in accordance with more detailed regulations to be issued by the Minister of Finance.²¹

When a part of the property is removed from German taxation by international treaties, the tax on the remainder is to be applied at the rates which correspond to that on the entire inheritance.

TURNOVER TAX

The turnover tax (Umsatzsteuer) is levied on sales²² made and (with certain exceptions) services rendered in Germany against consideration by an individual or firm engaged in an independent business or profession. The turnover tax law of January 30, 1932, increased the rate from 0.85 to 2 percent, effective February 15, 1932, and extended the tax to imports which theretofore had been exempt. The rate is increased to 2.5 percent for wholesale enterprises whose total sales in the previous taxable period, including tax-free sales, exceeded 1,000,000 reichsmarks. The tax on grains, flour, and bran, and bakery products therefrom is 0.85 percent; but if the sales of a wholesale concern during the previous taxable period amount to more than 1,000,000 reichsmarks, the rate is increased to 1.35 percent.

The tax on imports is termed an equalization tax (Ausgleichsteuer), and the rate is 2 percent (except on bread grains and certain flours, when it is 0.85 percent), based on the import price of the goods, including insurance, freight, etc. There are certain exemptions from the equalization tax, which are confined to a special free list, prepared by the Finance Ministry, consisting of raw materials essential to German industries and not produced in sufficient quantity within the country. All imports except those on the special free list are subject to the equalization tax, the tax to be collected with the duty on entering the German customs area.

Among exemptions from the turnover tax are sales of drafts, securities, and company shares (Anteile), which are subject to special taxes discussed later. Contributions subject to the tax on corporate rights (Gesellschaftsteuer) also are exempted, as are, in general,

²⁰ For example, when testator had foreign residence and the beneficiary is not a German resident, German banking credits are tax free.

²¹ For decision in individual cases see Reichsminister der Finanzen, Aug. 30, 1922, III-V. 6592.

²² It usually is added to the sale price and borne by the purchaser.

sales of real estate, which pay the purchase of land tax (Grunderwerbsteuer).

For the purpose of encouraging exports, the turnover tax has not been applied to export sales. (Such of the enforcement regulations of the turnover tax law of June 25, 1926, as have not been modified by subsequent regulations or the new tax law of June 30, 1932, are still effective.) In addition to this and with the same end in view, a decree of November 28, 1932, effective December 1, 1932, grants to exporters a bonus of 0.5 percent of the invoice (less transportation charges and insurance) of exported goods. This bonus amounts to a refund of one fourth of the turnover tax levied immediately prior to the goods reaching the exporter and is given to him in the form of an export bonus (Ausfuhrverguetung). Numerous products, mostly raw materials, are listed in the decree for which the exporter will not be entitled to the benefits of this refund provision.

Tax-refund certificates (Steuergutscheine) are issued in the case of the turnover tax to the amount of 40 percent of the sums due and paid between October 1, 1932, and September 30, 1933. These negotiable certificates will be accepted in payment of all taxes, except income and corporation taxes, during the fiscal years 1934 to 1939.²³

Under a recent decision of the Finance Ministry, all subsidiaries of foreign companies, organized under German law as share companies (Aktiengesellschaften), limited-liability companies (Gesellschaften mit beschränkter Haftung), etc., are entitled to the full benefit of the tax-refund certificates. A previous decision had denied the right of such subsidiaries to obtain the tax certificates.

BILLS OF EXCHANGE TAX

Bills of exchange, drafts, promissory notes, acceptances in blank, and other forms of commercial obligations are subject to the bills of exchange tax (Wechselsteuer), payment of which is made by affixing stamps obtainable at all post offices, under the law of July 12, 1930. Post-dated checks are subject to taxation in the same manner as bills of exchange, but not ordinary checks currently dated or traveler's checks.

The normal rate of the tax is 0.10 reichsmark per 100 reichsmarks or part thereof. Drafts drawn in foreign countries on German residents, provided they are payable in Germany and are expressed in reichsmarks, pay one half the normal rate. Half the normal rate applies also to drafts drawn by German residents on foreigners and payable abroad; such drafts, however, are exempt from the tax if they are payable at sight or within 10 days after they are issued and sent abroad without being circulated in Germany. In case the amount of the bill is left blank, the tax is to be reckoned on the basis of 10,000 reichsmarks; but if a larger sum is inserted, the additional tax must be paid. If a bill has been incorrectly taxed, a refund can

²³ For a more detailed discussion of this refunding method, which applies to the turnover (Umsatz), trade (Gewerbe), and land (Grund) taxes, see General Legal Bulletin 12 (C.L. 342), issued by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

be obtained from the Finance Ministry if application therefor is made within 1 year.

Taxes on bills of exchange are due before the bills are circulated or, if originating in foreign countries, before their being circulated by the first German recipient. When a bill is forwarded for acceptance without endorsement, the acceptor must pay the tax before negotiating the bill. Every endorser is legally obliged to see that the tax is paid, if previous endorsers have neglected to do so.

TRANSFER OF CAPITAL TAX

The transfer of capital tax (*Kapitalverkehrsteuer*) includes three separate taxes—on corporate rights (*Gesellschaftsteuer*), on securities (*Wertpapiersteuer*), and on stock-exchange transactions (*Boersenumsatzsteuer*).

Tax on corporate rights.—The tax on corporate rights is levied on the founding of German companies and the establishing of German branches of foreign companies. In the first instance it is assessed on the amount of the capital stock of the company; in the second, on the amount of capital to be employed in the branch enterprise. It is also collected on increases of capital by a company, and on loans of members where the capital is inadequate. The rate is 2 percent, but in the case of merging of corporations or of changing their legal form the tax is reduced to 1 percent.

Tax on securities.—The tax on the issuance of industrial debentures is 0.10 reichsmark for each 10 reichsmarks or fraction thereof and that on stocks and shares 0.20 reichsmark. This tax is paid only once on each security and is based on the par value. The minimum tax is 0.10 reichsmark. The rate of tax is reduced to 0.05 reichsmark per 10 reichsmarks on bonds and "Renten" deeds issued by domestic public corporations, domestic land credit and mortgage banks, etc., provided they were issued with Government authorization.

Exchange turnover tax.—The exchange turnover tax is levied on transactions in various kinds of stocks and bonds that take place between (1) brokers, (2) brokers and customers, and (3) between other individuals. Transactions concluded in a foreign country are subject to the tax if one of the contracting parties is resident in Germany. The tax applies to foreign securities sold in Germany. The tax on shares of a limited-liability company (*G.m.b.H.*) is 0.50 reichsmark per 100 reichsmarks or part thereof, with a minimum of 3 reichsmarks. The rates on other securities range according to the parties from 0.02 to 0.15 reichsmark per 100 reichsmarks.

PURCHASE OF LAND TAX

The transfer of real estate in Germany is subject to the purchase of land tax (*Grunderwerbsteuer*) amounting to 3 percent of the value of the property or of the sales price if that be the higher. Although both vendor and vendee are personally liable, the tax usually is borne by the latter. Additional percentages may be added by the States and municipalities which may not exceed 2 percent.

The Federal rate is reduced to 2 percent and the additional percentages of the States and municipalities do not apply in transfers

of real estate which occur as a result of the fusion of companies or a change from one type of company to another or on the acquisition of land by a company in exchange for shares in the company.

AUTOMOBILE TAX

An annual tax on motor cars (Kraftfahrzeugsteuer) is provided by the law of March 16, 1931.²⁴ It is levied on piston displacement or on net weight of vehicle as follows:

(a) Motor cycles driven by combustion engines: For each 100 cubic centimeters of piston displacement or fraction thereof, 8 reichsmarks;

(b) Passenger cars driven by combustion engines, except motor busses: For each 100 cubic centimeters of piston displacement or fraction thereof, 12 reichsmarks;

(c) Motor busses and trucks driven by combustion engines: For each 200 kilos net weight of the vehicle ready for use or fraction thereof, 30 reichsmarks (this rate to be increased by two-tenths if the vehicles are not fitted on all wheels with rubber tires); and

(d) Electric or steam-driven motor vehicles and tractors without space for carrying freight, and other motor vehicles not specifically mentioned: For each 200 kilos net weight of the vehicle ready for use or fraction thereof, 20 reichsmarks.

²⁴ A new decree, issued Apr. 10, 1933, exempts newly registered domestic and foreign passenger motorcycles and cars from this tax.

V. CONTRACTS

THINGS

In the consideration of the law of contracts attention must first be directed to the rights which may be acquired under a contract and the things to which those rights attach. German law contemplates that persons have certain rights (Rechte) with regard to things (Sachen) and then goes on to define "things" as "only corporeal objects."¹ When the law of things is studied, it is observed that things may include objects which are not corporeal, for they include things in possession and things in action. So it may be said that German law embraces the same basic concept of "things" as does English and American law.

Things themselves fall into general classifications such as (a) movables (personal property) and immovables (real property), (b) consumables (verbrauchbare Sachen) and nonconsumables, and (c) fungibles (vertretbare Sachen) and nonfungibles, which are further defined as follows: A thing is an immovable when it cannot be moved without being broken up, and the transfer of an immovable implies its transfer in toto. (For example, in the sale of a house the land upon which it stands would impliedly be included.) But in any attempt at definition or distinction it must be borne in mind that certain things which are in reality movables are considered immovables, such as ships.

Consumable things are defined as movables intended to be used for consumption (such as food, fuel) or alienation (such as money, dividends, and checks) in the ordinary course.² Movables which form part of a stock of consumable merchandise are also included so long as they are intended to be sold from time to time for consumption.

Fungibles are movables which in ordinary dealings are described by number, measurement, or weight.³

COMPONENT PARTS

Component parts of things are those which cannot be separated from each other or from the main thing without destruction of one part or the other or without change of their substance. Such component parts cannot be the subject of separate rights; they go with the main thing.⁴

It is possible that such parts, if attached to a thing, would be component parts; but where they are still in a factory and remain as mere parts, or they are dealt with in trade separately, and it is contemplated that they shall be sold or otherwise transferred merely

¹ B.G.B. 90. (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

² B.G.B. 92.

³ B.G.B. 91.

⁴ B.G.B. 93.

as parts, they are only accessories and can be the subject of separate rights and are not presumed to pass with the thing itself.

The essential component parts of land which pass with it are things firmly fixed to the ground, especially buildings and products of the earth connected with the ground (such as seed already planted).⁵

As to buildings, component parts are those things joined to such buildings for the construction thereof; but where things or buildings are attached to land or constructions are attached to buildings for a transitory purpose, they are not considered to be essential component parts thereof and do not pass with the things themselves. Rights connected with ownership, however, such as service and rents, are considered component parts of a thing and pass with it.⁶

ACCESSORIES

Accessories (*Zubehoer*) are always movable things, but they are never considered essential component parts because they become annexed only incidentally in order to serve the economic purpose of such principal thing; and not being essential component parts they do not pass with the principal thing.⁷

The criterion usually adopted is whether an object is regarded as an accessory in trade. The temporary use of a thing for economic purposes of another thing does not make it an accessory, nor does the temporary separation of an accessory discontinue its character as such.⁸

In a building which is permanently fitted for operation as a factory or mill the machinery and apparatus required for its operation are not considered accessories; and on a farm the implements and agricultural products and manure necessary for the farm also are not so considered.⁹ They pass with the building or farm.

FRUITS AND PROFITS

Fruits of a thing are defined as the products or other gains earned from it according to its purpose, and the fruits of a right are the income and profits derived from the exercise of that right. The benefits derived from a thing by virtue of temporary or other legal relation to the person entitled to the use of such thing also are considered fruits.¹⁰ The fruits and profits of a thing, like the component parts, pass with the thing.

When the fruits of a thing are payments of money for the use thereof, the money is apportioned from day to day and belongs to the person entitled to the thing from which the money is obtained. In other cases, however, the fruits belong to the party who is entitled to the use of the thing at the time of severance. An income belongs to the person exercising the right of ownership of the thing when the income falls due.¹¹

Persons who must surrender fruits taken while in temporary or unlawful possession may recover the cost of the production of such fruits if it does not exceed the value thereof.¹²

⁵ B.G.B. 94.
⁶ B.G.B. 95-96.
⁷ B.G.B. 314.

⁸ B.G.B. 97.
⁹ B.G.B. 98.
¹⁰ B.G.B. 99-100.

¹¹ B.G.B. 101.
¹² B.G.B. 102.

RIGHTS

In law the most important indication of a right in and to a thing is possession. Possession is actual control.

The right in and to a thing may pass from one party to another either by law, as on the death of the possessor (when it goes to the heir), or by an act of the free will of the transferor.¹³

When a person is deprived of the control of a thing by force or otherwise than by legal process, he has an inalienable right, sounding in possession, to resist the taking. And if he is disturbed in his possession or the enjoyment thereof, or is even threatened with disturbance therein, he is entitled to injunctive relief.¹⁴

Rights are exerted by the enjoyment of possession of a thing or by the exercise of control thereover. Control implies the ability to deal freely with the possession and even to transfer it.

When control is transferred by an act of free will and in so doing either the transferor or the transferee is injured by an act or omission in connection therewith not in contemplation of the parties, or either of them is deprived thereby of anything to which he would ordinarily be entitled by the proper working of the transfer relationship, such party obtains a right of action. The criterion, however, is always possession, and the right of action arises from disturbance thereof or distortion in connection therewith.

Rights may be exerted either as against the whole world (in rem) or as against a particular person (in personam), and the German law makes a very clear-cut distinction between the two and the remedies allowed in each type. Rights which one has against the world (Sachenrechte) are such as can be exerted because of the right itself and claims can be made against or out of the right itself because of possession (Besitz). But rights against the person (Schuldrechte) arise out of contract and can only be exerted against the person if jurisdiction is obtained against him. (A note secured by a mortgage is an example of both a right against the person and a right against the world, since the note is a right only against the person and the mortgage is a right against the world in that satisfaction may be obtained out of the thing mortgaged.)

Under contracts hereinafter to be considered, contracts for services or for work, leases, loans, sale and exchange, and agency create rights in personam (Schuldrechte), whereas mortgages, liens, and bailments create rights against the world (Sachenrechte). [In this study, agency and negotiable instruments have, for typographical convenience, been treated separately under their own titles, although, properly they fall under "Contracts."]

VOID AND VOIDABLE ACTS

When, therefore, a person desires to obtain or to rid himself of rights in anything, he declares his intention with regard thereto directly or indirectly to another who may be disposed to carry out his intention. The limitation in law at the outset is that a person may not seek an act in law which is void ab initio (nichtig). Such acts under German law are transactions (a) in violation of good

¹³ B.G.B. 854, 857.

¹⁴ B.G.B. 859, 862.

morals, (b) with a party not having legal capacity (void as to him), (c) in violation of prohibitions (gesetzliches Verbot), (d) which lack the form prescribed by law, or (e) in which one party takes advantage of the distress, recklessness, improvidence (leichtsinnig) or inexperience of another (e.g. usury and undue influence) and obtains a promise or act which so exceeds the value of the consideration that under the circumstances the profits are in striking disproportion thereto.¹⁵

An act void in part is void in entirety unless it be assumed that the parties intended the valid part to be separable and effective without the void provisions. There are also acts voidable in law (anfechtbar) which may or may not become the subject matter of a contract, a few of which require decision of the court to set aside; but generally they are impugned by an act of avoidance or by a declaration delivered to the party entitled to notice within a certain time carefully provided for in each case by the statutes.¹⁶

The grounds for such avoidance are (a) want of capacity of a party (void as to the incompetent), (b) defects or misinterpretation or misunderstanding of the declaration, and (c) fraud, threat, or other extraneous circumstance.

Confirmation of voidable acts, where possible, ends the voidability, though informal, even where the act requires formal compliance. A third party acquiring rights under a voidable act has certain reliefs if he be ignorant of its voidability.

CONTRACTS IN GENERAL

Contracts (Vertraege) entered into in Germany are subjected to rules of interpretation by the courts which are less strict than in either England or the United States. "They are to be interpreted in good faith (Treu und Glauben) with due regard to common usage", and "all acts and omissions must be interpreted with reference to common usage", which the Civil Code further limits "as good faith between the parties requires."¹⁷

The open attitude of the German court, coupled with its broad latitude in the introduction and acceptance of testimony as to the working of the minds of the parties, makes it possible to seek and obtain a decision upon the real meaning of the parties even though there has been a declared intention in writing. "In interpreting a declaration the actual intention is to be ascertained and the literal sense of the expression is not to be adhered to."¹⁸

The German attitude with regard to interpretation of contracts seems to start with the idea of the real intent of the parties and to advance slowly and grudgingly to the exceptions in which declared intentions alone are considered binding. Indeed, it is possible to avoid a contract where "real meaning" or intention is questioned on the ground of (a) mental reservation (void if known to the other), (b) fictitious (void if known to the other), (c) not to be taken seriously (void), (d) mistaken understanding, or (e) induced by craft, deception, or unlawful threat. If avoidance is attempted in cases of mistake, it must be done promptly upon discovery; in

¹⁵ B.G.B. 134-138.
¹⁶ B.G.B. 123-124, 139-141.

¹⁷ B.G.B. 157, 242, 346.
¹⁸ B.G.B. 133.

case of deception, within 1 year unless sooner discovered; in case of threat, at the time coercion ceases.¹⁹

Ordinarily a statement in a contract or correspondence of the terms, obligations, and conditions, in form such as one would make in England or America, will be given the same effect under German law.

Contracts for the benefit of third parties are enforceable in Germany by the parties and the third party as well,²⁰ if agreed upon between the parties.

ORAL AND WRITTEN CONTRACTS

As has been intimated, there is no required form for contracts in Germany, nor are there formalities or rules to which to adhere. Oral contracts, therefore, may be said to be as valid in Germany (subject always to the difficulty of proof) as are written contracts, except in those cases in which German law obligates the parties to make written contracts.

It is obligatory in German law to make written declarations in the following transactions:

- (a) Rent or lease contracts of real estate for more than one year;
- (b) Other transactions requiring public registry (corporation matters and creation of forms of agency);
- (c) Life annuity contracts;
- (d) Guaranty contracts;
- (e) Promises to pay for another and acknowledgment of debt (but not of full merchants);
- (f) Wills;
- (g) Contracts for the transfer of property or the mortgage of real estate;
- (h) Renunciation of inheritance; and
- (i) Custody of securities (changes).²¹

From the foregoing it is clear that a written contract is necessary only in cases in which one would ordinarily, from the nature of the transaction or the requirement of public registry, presume that a written document should be drawn.

AUTHENTICATION OF DOCUMENTS

Many forms of contracts and documents under German law do not require authentication to be valid, and many forms of agency agreements are not required to be authenticated in order to impose the obligations connected therewith upon the parties. But where contracts or documents require authentication, the acts of agents of foreign organizations who transact such types of business or make such contracts also require authentication.

Authentication of contracts and documents is necessary only (a) where the law requires a written form for the contract, (b) where the carrying out of the transaction involves registering in some official register, or (c) where such documents are required for production in German courts.

¹⁹ B.G.B. 116-121, 123-124.

²⁰ B.G.B. 328-335.

²¹ B.G.B. 566-581, 751, 766, 780-781, 873, 2231, 2348-2351; H.G.B. 350; Depotgesetz 2.

In transactions where the law prescribes written form or authentication, any instrument relating thereto must be signed by the signature of the party or with his mark, judicially or notarially attested; and if the transaction is attempted by an agent, the documents must be signed with his signature and proof of his power and authentication thereof must be annexed. Any contract which must be so authenticated, especially where it is to be filed in a public registry, must be signed and acknowledged by both parties on the same document. Where the contract is not to be filed in a public registry, each party may sign and have acknowledged and authenticated a duplicate original and exchange duplicate originals. Any correspondence resulting in a contract that requires authentication also must be signed, acknowledged, and authenticated by the signing and acknowledgment and authentication of the proposition or offer by the one party and the acceptance by the other party.

An excellent but perhaps not legally correct (because sometimes unnecessary) rule to follow would seem to be that all contracts or offers made in a foreign country, the terms of which are expected to be completed in Germany, should be authenticated. Especially should this be done where the contracts may become the basis for litigation or involve important matter or serious losses. It is absolutely necessary that this rule should be followed with regard to documents creating agencies of foreign companies intending to transact business in Germany and especially where these representatives intend to defend or bring suits in German courts.

Experience has taught that authentication is always valuable, because it proves the genuineness of signatures and the right to the enjoyment of the powers conferred upon agents and, more especially, it completely establishes the authority of the persons signing the contract or conferring the agency to do those acts.

METHOD OF EFFECTING AUTHENTICATION

The acknowledgment of the signatures of the persons executing the document must be taken by a local notary or other official authorized to take acknowledgments in the country where the contract is drawn, whose signature must in turn be certified by the county clerk of the county in which such notary or official has qualified. The signature of the county clerk must be certified in turn by the German consul for that district. If there be no German consul for the district, the county clerk's signature must be certified by the secretary of state of the State in which the contract was drawn, whose signature must in turn be certified by the German consul having power so to do. If there be none, the signature of the secretary of state of the State where the contract is drawn must be certified by the Secretary of State or equivalent officer of the foreign country and his signature in turn certified by the German ambassador.

If a contract or a power of attorney for use in Germany is drawn in a language other than German, the German consul may, when this is desirable, either translate the document into German himself or have the translation made. He then certifies that the translation is correct and at the same time authenticates the signatures to the document. Certification of the correctness of a translation can also be obtained in Germany from a German notary or an official translator.

OFFER AND ACCEPTANCE

One of the requisites to the formation of a contractual relationship is that one party make a declaration of intention with regard thereto, communicate it, and have it accepted. An offer becomes effective the moment it reaches a party (except that an offer to a person of restricted capacity becomes effective usually only after it reaches his statutory agent), and it immediately binds the offerer for a reasonable time, unless he provide not to be bound or unless he provide a time limit for acceptance. An offer is not impaired by the death or legal incapacity of the offerer.²²

Delayed acceptance of an offer is regarded as a new offer, and acceptance with extensions or modifications or restrictions is regarded as a refusal and a new offer.²³

As long as the parties have not agreed upon all points a contract is not consummated even though the understanding as to various items thereof has been reduced to writing, and an agreement believed to be complete which later is found to be incomplete as to a particular point is inoperative unless it is shown that the parties would have been willing to be bound even if they had been aware of the incompleteness.²⁴

An agreement later to be embodied in a formal document is, except by specific agreement, not binding before execution of such document.²⁵

A written declaration of intention delivered through an official process server in the same manner as he would serve a judicial process is good though not actually received. Or if the declarant does not know the identity or whereabouts of an addressee, a declaration may be communicated, like a semijudicial process, by public citation, that is, notice on the board of the competent court and advertisement in the official journal.²⁶

In mercantile transactions, if tacit acceptance is usual in any particular class of agreements, or if acceptance is waived, formal acceptance is unnecessary.

If a mercantile trader whose business is to trade for others is requested to transact business by a person with whom he has regular business connections or from whom he has solicited business, he is bound to refuse the offer immediately or is deemed to have accepted it.²⁷

PLACE OF PERFORMANCE

Place of performance, where not specified in a contract, may raise a question of jurisdiction. If an obligation is incurred in the course of the debtor's trade and his place of business be different from his place of domicile, the place of business is to be considered the place of performance. Otherwise and generally the place of the debtor's domicile when the obligation arose is the place of performance.²⁸

Payment of ground rent or of principal upon a mortgage is to be made at the land registry. Inspection of merchandise is to be made at the place of production or sale, as the circumstances demand.²⁹

²² R.G.B. 130-131, 145-150.
²³ B.G.B. 150.
²⁴ B.G.B. 154-155.
²⁵ B.G.B. 154.

²⁶ Z.P.O. 203-207.
²⁷ B.G.B. 683; H.G.B. 362.
²⁸ Z.P.O. 29; B.G.B. 269.
²⁹ B.G.B. 811, 1194.

A deposit must be made at the depository of the place of performance. Return of a deposited thing is to be made at the place where it is deposited.³⁰

If a movable thing which is owing is not adapted for deposit, the debtor may, upon default of the creditor, have it sold at auction at the place of performance and may deposit the proceeds.³¹

TIME OF PERFORMANCE

In the absence of an express or implied provision therefor, performance may be offered or demanded immediately. If a time is fixed, the creditor cannot claim, but the debtor may offer, performance before due.³² If a debt does not bear interest, the debtor anticipating payment may not claim interest thereon.

Performance in a mercantile transaction can be effected only during business hours on business days. An agreement to perform in a certain season is to be determined by the commercial usage in the place of performance.³³

Where interest is stipulated to be paid but the time of payment is not fixed, payment is to be made at the end of each year; or if for a shorter time, payment is to be made on repayment of the principal.³⁴

Compensation for the custody of movable things is due at the end of the contract, unless the compensation is fixed by periods, in which event it is payable at the end of each period; and if the custody ends before the expiration of any period fixed, a depository can demand a proportional part of such compensation.³⁵

If a transaction is entered into and the time fixed for the beginning or ending thereof, the contract must be performed within the time so fixed.³⁶ If upon such a contract timely performance is not obtained, the other party may withdraw from the contract or demand damage for nonperformance. In order to claim performance, however, he must, immediately upon expiration of the time set, notify the defaulting party that he will demand such performance.

INTEREST

Payment of interest is not implied under German law except in commercial transactions. In noncommercial transactions, where interest is agreed to be paid but no rate is fixed the rate is considered to be 4 percent; in commercial transactions, interest is presumed to be paid even though not expressly provided for, and where the rate is not fixed it is 5 percent. For mortgages, the interest is usually 5 percent, and when it is fixed at a lower rate it can be increased to that amount. Interest on bills of exchange is invariably 5 percent. Any rate of interest may be fixed, however, by agreement, except that it may be reduced by the court if it is unreasonable; and in any transaction in which the interest is fixed at more than 5 percent the debtor may discharge the account by payment on six months' notice at any time.³⁷

³⁰ B.G.B. 374, 697.

³¹ B.G.B. 383.

³² B.G.B. 271-272.

³³ H.G.B. 358-359.

³⁴ B.G.B. 608.

³⁵ B.G.B. 699.

³⁶ B.G.B. 163.

³⁷ B.G.B. 138, 246-247, 288, 1119; H.G.B. 352; W.O. 50-51, 81.

Compound interest cannot be contracted for except in certain minor transactions, and also except that savings banks may pay interest on interest, and in continuing bilateral accounts of merchants interest may be charged on previous balances although interest had already been included therein.³⁸

Mercantile traders charge interest on transactions from the date of maturity of claims, and on loans, advances, outlays, and other disbursements from the day of the making of same.³⁹

Interest is payable by a buyer on the purchase price from the time when income from the thing purchased belongs to him.⁴⁰ On goods manufactured for a party, interest is payable from the time of delivery. On buildings in the course of construction, interest is payable from the time of the acceptance of the work. If, under the agreement, acceptance is to be made and installments paid from time to time, interest is payable from the time the installments become due.

If a depositary of money or fungibles uses either of them for his own purposes, interest must be paid thereon for the time of such use.⁴¹

A party injured in his person or his property is entitled to interest on the amount of the claim from the time the amount of the damage is determined.⁴²

Where interest is stipulated but no time of payment is fixed, it is payable at the end of each year or, if the remainder of the period is less than a year, on repayment of the principal sum.⁴³

COMPUTATION OF TIME

The following are the rules found in the Civil Code⁴⁴ for computing time in laws, orders, and legal transactions generally:

If an event or a point of time in the course of a day determines the beginning of a term, the day upon which the event or point of time falls is not included in computation. If the beginning of a day is the point of time at which a term is to commence, that day is included; and the same rule is applicable to date of birth in computing age.

A term computed in days ends with the expiration of the last day of the term. A limitation which is fixed in weeks, months, or periods covering several months—year, half a year, quarter of a year—ends upon the expiration of that day of the last week or month which by its designation or number corresponds with the day upon which the event or the point of time falls. If in a limitation which is fixed in months the day on which the same is to expire is wanting in the last month, the limitation ends upon the expiration of the last day of that month.

In case of an extension of a limitation, the new limitation is computed from the expiration of the previous limitation.

Half a year means a limitation of 6 months; a quarter of a year, a limitation of 3 months; half a month, a limitation of 15 days. If a limitation includes 1 month or several months and half a month,

³⁸ B.G.B. 248; H.G.R. 355.
³⁹ H.G.B. 352-355.
⁴⁰ B.G.B. 452.
⁴¹ B.G.B. 698.

⁴² B.G.B. 849.
⁴³ B.G.B. 608.
⁴⁴ B.G.B. 187-193.

the 15 days are to be counted last. If a term is fixed in months or years in the sense that it need not run without interruption (consecutively), the month is computed at 30 days, the year at 365 days.

By "the beginning of the month" is meant the first, by "the middle of the month" is meant the 15th, by "the end of the month" is meant the last day of the month.

If a declaration is to be made or an act is to be performed on a certain day or within a limitation, and if that day or the last day of the limitation falls upon a Sunday or upon a general holiday so recognized by the State at the place of declaration or of performance, the next following working day takes the place of Sunday or of the holiday. In a mercantile transaction, "8 days" means what it says,⁴⁵ but otherwise it means a week.

CONTRACTS WITH CONDITIONS

Contracts with conditions precedent (*aufschiebende Bedingungen*) become effective upon the happening of the condition.⁴⁶

Contracts with conditions subsequent (*aufloesende Bedingungen*), by which they may be rescinded, are rescinded with the happening of the condition. If the happening of the condition is, in violation of good faith, prevented by a party, the condition is regarded as having happened.⁴⁷

GENERAL OBSERVATIONS

Summarizing the foregoing general observations on contracts, it is suggested that certain points be borne in mind when contracts for Germany are negotiated and drawn:

1. Contracts which are required to be in writing require the authentication of the powers conferred so to contract. (See "Agent under power of attorney", p. 147.)

2. Where the contracting parties are in different jurisdictions in Germany, they should consider the advisability of specifying the court to have jurisdiction in event of dispute, in order that the trial may be conducted before courts most familiar with the problems likely to arise.

3. Where one party is not domiciled in Germany, the contract should specify the law of which jurisdiction is to apply. This will avoid difficulty for the courts and the litigants in determining the laws of which nation will govern the transaction.

4. In a contract stipulating that work thereupon be started or completed or deliveries be made within a fixed time, it is necessary to set forth clearly and definitely the fixed time or times. There should further appear a provision that time is of the essence of the contract, and care should be exercised that a margin for unforeseen delays is allowed.

5. In all contracts the fixing of the price as "that prevailing at the time of delivery" should be avoided if possible. A definite price should be insisted upon.

6. Where security for payment is to be given, the contract should clearly state the currency desired and the rate of exchange.

⁴⁵ H.G.B. 359.

⁴⁶ B.G.B. 158.

⁴⁷ B.G.B. 158, 162.

7. In those cases where arbitration is deemed desirable, the arbitration clause should name the place of arbitration and provide for an umpire.

8. By whom the insurance of the goods is to be placed should be clearly stated; and the coverage itself should be checked, to see that the goods are covered while they are at risk, so that delay or interruption in transit will not leave the goods uninsured. (Warehouse to warehouse coverage is advisable.)

9. In a mercantile export contract a clause should be inserted fixing the time, place, and manner of inspection and acceptance of the merchandise. The best method is to arrange for inspection and acceptance at the place of shipment by a representative of the purchaser.

10. In "cash against documents" transactions, under a recent decision⁴⁸ the usual understanding that the goods are to be paid for before inspection is disregarded where the goods arrive in Germany before the documents. It is advisable, therefore, to send the documents sufficiently ahead of the merchandise.

11. In making a contract, as in all business transactions, the distinction maintained throughout German law between merchants and nonmerchants should be kept in mind, especially if the contract is with a nonmerchant or involves a nonmercantile transaction.

12. In making a c.i.f. contract, the Warsaw-Oxford rules should be consulted and so far as desirable incorporated therein. (See U.S. Chamber of Commerce, Washington, D.C., special bulletin of January 1933.)

CONTRACTS FOR SERVICES

In contracts for services (Dienstverträge) of every kind, compensation is implied at a fixed (taxe) or customary rate. For mercantile employees the rate is that fixed by local custom. The service must be personal and the liability to perform may not be transferred. The compensation is payable at the end of each period of time for which the price is fixed in the contract, except that mercantile employees must be paid at no longer than monthly intervals. An employer refusing to accept service must pay the agreed price, less any saving to the employee.⁴⁹

Sick or injured permanent employees do not lose compensation for short absences from work, but they must credit all insurance payments received. Sick employees in the home must be given nursing and medical treatment or hospitalization up to 6 weeks but not beyond the term of employment, and the cost may be deducted from the agreed compensation.⁵⁰

Employers must furnish safe and healthful places to work; and if living quarters are to be furnished, due regard must be given to health and morals. These provisions cannot be waived by agreement.⁵¹

⁴⁸ This decision is unpopular in Germany, and an attempt has been made to rectify the ruling.

⁴⁹ B.G.B. 611-616; H.G.B. 59, 63-64.

⁵⁰ B.G.B. 617.

⁵¹ B.G.B. 618-619.

TERMINATION OF SERVICE

The service is terminated at the end of the term agreed upon. If no term has been fixed, either party may terminate by notice, the time of which depends on the period for which compensation is paid: If fixed by day, on any day for the succeeding day; if by the week, only for the end of a calendar week, to be given at latest on the first workday of the week; if by the month, for the end of the month, to be given not later than the 15th; if for a trimester or longer, only for the end of the calendar trimester and at least 6 weeks in advance.⁵²

If compensation is not fixed by periods, the service can be ended by notice any time, except that full-time employees must be given 2 weeks' notice. If the service is for life or more than 5 years, 6 months' notice is required.⁵³

Employment continued after the expiration of a fixed term continues for an indefinite time unless the employer objects at once.⁵⁴

For sufficient reasons (*wichtige Gründe*), the employment can be terminated without notice. More important employees in positions of confidence not in continuous service can also be dismissed at any time, but such employees under ordinary circumstances cannot give notice unless or until replaceable. After notice to an employee in continuous service, the employer must upon request grant adequate time to find other employment.⁵⁵

The employee is entitled to a certificate as to his services and their duration.⁵⁶

MERCANTILE EMPLOYEES AND APPRENTICES

Special sections of the Commercial Code cover contracts for services of mercantile employees and apprentices, but where these do not apply the provisions of the Civil Code do.⁵⁷

A mercantile employee is defined as one engaged in a mercantile business to perform mercantile services there, to do the usual work for the usual local pay reasonable in the circumstances. Such a person may not, without the consent of his employer, carry on mercantile trade or engage in transactions in the same business as his employer. If he does so, his employer can claim the transaction or damages (barred in 3 months after the employer is aware of it or at longest in 5 years). The employer must make satisfactory arrangements for a healthful and safe place of work and provide for morality and decency. These rights cannot be limited or avoided by contract.⁵⁸

An employee, if disabled through no fault of his own, receives his salary for 6 weeks but no longer, any contract to the contrary notwithstanding. Salaries must be paid at the end of each month; and if the employee is entitled to commissions, they must be paid the same as to an agent.⁵⁹

Employment for an indefinite period is terminable by either party at the end of any calendar quarter upon 6 weeks' notice. Employment cannot be for less than 1 month; and notice can only be given at the end of a calendar month, unless the salary is over 5,000 marks

⁵² R.G.B. 620-621.
⁵³ R.G.B. 623-624.
⁵⁴ R.G.B. 625.

⁵⁵ R.G.B. 626-627, 629.
⁵⁶ R.G.B. 630.
⁵⁷ R.G.B. 611-630.

⁵⁸ H.G.B. 59-62.
⁵⁹ H.G.B. 63-65.

per year. If the employment is outside Europe, the employer must pay the employee's expenses home on termination. Notice of termination may be given by either party on cogent grounds, and the party at fault must pay damages for any loss resulting from the termination.⁶⁰

An apprentice must be taught the business and allowed time to study and attend school. The period of apprenticeship is governed by the contract, and the probationary period cannot be longer than 3 months. After that the rights of termination are the same as for an employee, and at termination a certificate must be given.⁶¹

There is also a special type of employees called mercantile agents, whose rights and duties and relations are fully set forth herein under "Agency", at page 123.

The service relationship is further complicated by social labor legislation (*a*) as to collective bargaining leading to formation of workers' contracts⁶² and (*b*) additional rights of employees in factories and aggregations (work councils law), and (*c*) compulsory insurance.⁶³

GROUND FOR TERMINATION

The term "cogent grounds" is interpreted to include: For the employee, (*a*) inability of employee to continue, (*b*) failure of employer to compensate and to furnish healthful and safe employment, and (*c*) violence or insult; for the employer, (*a*) infidelity, abuse of confidence, or breach of obligation, (*b*) absence from work or neglect, (*c*) failure to perform by reason of illness, crime, punishment, or military service over 8 weeks, and (*d*) violence or insult. At the end of his employment a mercantile employee is entitled to a certificate as to his services and their duration.⁶⁴

An agreement between the employer and the employee limiting trading after the termination is good only where the limit does not inequitably embarrass the future of the employee and is never good for more than 3 years.⁶⁵

CONTRACTS FOR WORK

A contract for work (*Werkvertrag*) contemplates the production or alteration of a thing or its transport, to be accomplished by labor or services. The employee must deliver the produced object to his employer and cause its ownership to be vested in the employer in order to fulfill his obligation under the contract. It differs from a contract for service in that the result of the work and not the work itself is contracted for. In many cases, agreements for work are with difficulty distinguishable from agreements for services and sales.⁶⁶

Where an employee agrees to produce work from material procured by him and where the object to be produced is not a fungible, the agreement is for work as to payment, risk, and remedies for

⁶⁰ H.G.B. 66-70.

⁶¹ H.G.B. 76-77, 80.

⁶² See Boris Stern in Bulletin of the U.S. Bureau of Labor Statistics No. 388; and Collective Labor Agreements in German Law, St. Louis Law Rev. 15, December 1920, pp. 1-46.

⁶³ See Bulletin of the U.S. Bureau of Labor Statistics No. 107.

⁶⁴ H.G.B. 71-73.

⁶⁵ H.G.B. 74.

⁶⁶ B.G.B. 631 (contract for work only), 651 (contract for work and delivery).

breach of warranty, but in all other respects it is considered a sale. Where the object to be produced is a fungible, however (as, for instance, a metal sold by weight by a smelter), the agreement is a pure sales contract and not a contract for work in any respect and is governed by the rules as to sale of goods under the Commercial Code.⁶⁷

Where the contractor furnishes secondary things only, the transaction is a contract for work. The rules by which a contractor obtains the right of pledge or security for the work he has done or is doing do not apply where the material is supplied by him.⁶⁸

If the agreement for work is bilaterally mercantile, the special rules applicable in mercantile sales also apply.⁶⁹

RIGHTS AND DUTIES OF CONTRACTOR AND EMPLOYER

Compensation for work produced by a contractor is presumed, and the rate therefor is determined as in the case of contracts for services. It is due and payable immediately upon delivery and acceptance of the work; where delivery is not sought, completion of the work or service takes the place of delivery. When the contract calls for payment in installments, the installments are to be proportional; and interest is chargeable from the time when payment should have been made.⁷⁰

The contractor is obligated to produce the work and vest ownership in the employer, but need not necessarily produce it himself, unless he agrees so to do. In that case his doing of the work personally is construed as a warranty, which must be fulfilled. The work produced by him must be of promised quality and with no defect which takes away or lessens its value or its adaptability to the intended use. He may not contractually relieve himself of this responsibility for a defect if the defect is known, or expected, or concealed by him.⁷¹

An employer must accept the work upon completion or accept with reservations as to defects (acceptance is sometimes imputed by completion alone), but the contractor assumes the risk until acceptance or default by the employer. Such contractor, on refusal or delay of the employer to accept, may give notice that he will rescind the contract if the employer fails to accept within a reasonable time. If he does so, he is entitled to compensation for his work and outlay, and the question of his damage is so fixed.⁷²

A contractor has a lien for work on things of the employer in his possession and is entitled to a security mortgage on the real estate where he is contractor on a building, or part thereof, even if the work is only partly completed.⁷³

DEFECTS

A demand for the removal of a defect lies, but the contractor may refuse to remedy it if doing so entails disproportionate expense. In such case, or if the removal of a defect is impossible or the contractor refuses to remedy the defect for any other reason, or if

⁶⁷ B.G.B. 651; H.G.B. 373-382.

⁶⁸ B.G.B. 651.

⁶⁹ H.G.B. 381.

⁷⁰ B.G.B. 641-646.

⁷¹ B.G.B. 631, 635, 637.

⁷² B.G.B. 640, 642-644, 646.

⁷³ B.G.B. 647-648.

he fails to remedy it within a reasonable time after notice, the employer may force the contractor to consent to the cancellation of the contract or to the reduction of his remuneration; or, unless the defect is inconsiderable, the employer may obtain damages for nonfulfillment.⁷⁴

The employer may also remedy the defect himself, after giving the contractor opportunity so to do, and deduct his expenses therefor from the agreed remuneration.⁷⁵

All claims for defects (except concealed defects) are barred in 6 months generally. As to work on grounds, however, the limit is extended to 1 year and, as to buildings, to 5 years from the time of acceptance.⁷⁶

NONDELIVERY WITHIN PROMISED TIME

In general the same remedies are given to the employer for non-delivery of work within the time specified as for defect, unless the employer is at fault because of supplying defective material or otherwise himself occasioning the delay, in which cases damage can be claimed by the workman.⁷⁷

An employer may rescind a contract for work where the contractor has given an estimate therefor, even though the contractor has not guaranteed its accuracy, when it is found that the work contracted for will require an amount for completion greatly in excess of the estimate; but if the contract is rescinded on this ground, the contractor may claim remuneration proportionate to the amount of labor already expended on the work and reimbursement for outlays not included therein. The employer may also at any time before the completion of the work contracted for rescind the agreement without giving any explanation for his actions, in which case the contractor is entitled to the whole remuneration after deducting any saving of outlay or earnings for the unfinished portions of the work.⁷⁸

LEASES

The letting of land in Germany is considered a purely contractual relationship and confers on the lessee only a contractual right. It is a relationship similar to that created by the hiring or letting of a chattel, and there is therefore no requirement or provision for registering the transaction in the land register. As a matter of practice, however, the transfer of ownership of a parcel of land effects a transfer of the rights and liabilities arising under any lease to which such parcel is subject. In other words, in Germany the law is that where a lessee, or one claiming rights through him, is in possession of premises at the time of the sale thereof, the lessee's rights are binding upon the purchaser, including the lessee's rights to the return of any security turned over to the purchaser; but where neither the lessee nor any person claiming rights through him is in possession at the time of sale, the purchaser, in the absence of agreement, is not bound to the lease. Where notice of sale is given the lessee of the premises, the lessor is released from

⁷⁴ B.G.B. 633-635.

⁷⁵ B.G.B. 633.

⁷⁶ B.G.B. 638.

⁷⁷ B.G.B. 636, 642, 645.

⁷⁸ B.G.B. 649-650.

his liability except when notice is given by the lessee of his intention to terminate the lease for the first term for which notice is admissible.⁷⁹

Where there is more than one transfer of property during the term of a lease, the original lessor and the last owner of the property are the only ones with duties, rights, and obligations with regard to the lessee, and the intermediate owners of the property are freed of all obligation to the lessee with regard thereto.⁸⁰

Any owner of property subject to a leasehold, who encumbers the property, can only give rights thereto corresponding and equal to his own; and neither the owner nor the party acquiring rights from him can exercise any rights which would prevent the lessee from using the leased object in the originally agreed manner. The lessee, like the hirer of a chattel, has the same rights to possessory remedies against parties unlawfully disturbing his enjoyment and possession as the owner.⁸¹

A distinction must be made between an ordinary lease (*Miete*) and an usufructuary lease (*Pacht*).⁸² In the former the use of the thing leased is granted during the term; whereas in the latter type the use of the thing and the enjoyment of its fruits are accorded, as in the cases generally of leases of agricultural property.

DURATION AND TERMINATION

The maximum legal term for the duration of a lease in Germany is 30 years. A lease for a longer period can be terminated by notice, the same as a lease for an indefinite term.⁸³ A lease, however, may be granted for the life of the lessor or the lessee.

A lease for a term exceeding 1 year must be in writing. If it is not in writing, it will be treated and considered as a lease for an indefinite term, which cannot be terminated before the end of the first year.⁸⁴

A lease for a definite term comes to an end with the arrival of the date named; but it may be terminated before that time, upon notice, (*a*) by breach of the agreement of lease by either party, (*b*) if the lessor withhold his consent to an assignment of the lease without good grounds for his refusal, (*c*) on the death of the lessee, or (*d*) in the event the lessee, being a military man, a minister, or a teacher, removes to another town. The notice in each case varies in length of time according to the nature of the event.⁸⁵

A lease for an indefinite period may be terminated by notice, the length of which also varies according to the nature of the lease, the longest notice being required for a usufructuary lease; and such notice terminates the lease only at the end of the year of tenancy. Notice must be given on the first business day of the half year at the end of which the tenancy expires.⁸⁶

A lease continued after the expiration of a term becomes a new lease for an indefinite period, unless notice of a contrary intention is given by either party during the prescribed time, and the lessor

⁷⁹ B.G.B. 571-572, 578, 581.

⁸⁰ B.G.B. 579.

⁸¹ B.G.B. 577, 858-860.

⁸² B.G.B. 535, 581.

⁸³ B.G.B. 567.

⁸⁴ B.G.B. 566.

⁸⁵ B.G.B. 549, 565, 569-570, 595-596.

⁸⁶ B.G.B. 595.

may demand at least the previous agreed rental and claim further damage.⁶⁷

LESSOR'S RIGHTS AND DUTIES

The lessor must give to the lessee the enjoyment of the leased premises during the term agreed upon in a condition adapted to its contractual use, together with all the fruits and income therefrom produced by good management thereof; and a stipulation relieving the lessor from liability for defect in quality or title, impairing the agreed use, is void, especially if such defect was concealed by the lessor.⁶⁸

The lessor must bear all expenses connected with the leased premises, including rates and taxes, and must reimburse the lessee for all outlays incurred by him for the preservation of the premises; but the lessee of agricultural property must make ordinary repairs, especially with regard to domestic and farm buildings, roads, ditches, and fences. Claims for such outlays are barred if not exercised within 6 months from the termination of the tenancy.⁶⁹

Where land let for farming includes the use of furniture and farm implements, the lessor must replace such parts damaged or destroyed for the damage or destruction of which the lessee is not responsible. The lessor must also compensate the lessee for fruits not reaped but grown by the lessee during his term, when the termination of the lease occurs prior to the time of such reaping.⁷⁰

The lessor is entitled to compensation for destruction or deterioration caused by an unauthorized use of the leased objects or by the lessee's willful default or negligence. All claims therefor, however, are barred after 6 months from the return of the leased object. Where the leased object is not returned on the termination of the lease, the lessor may claim rent therefor as long as the breach continues. The lessor may also terminate a lease if the lessee has not paid two installments of rent upon notice. He may also terminate the lease for unauthorized use of the premises after notice, and also in the event of the failure of the lessee to use proper diligence and care with respect to the leased premises, thereby endangering their safety.⁷¹

An assignment of rent for the current or next quarter is good against an owner by the purchaser from him, but no assignment to accrue at a later date than that is good as against a purchaser without notice.⁷²

To secure the lessee's rights, the lessor must give a lien on the property leased by him. The lessor on his part obtains a right of pledge, which serves as a security for the performance of all the lessee's obligations, including rent for the last elapsed year and for future rent. This lien extends to all things brought upon the premises by the lessee and owned by him. The lessor must, however, allow the removal of all things subject to this right of pledge in the regular course and in accordance with common practice and so long as the goods still remaining are sufficient for his security. But he can prevent such removal or can recover the things removed without

■ B.G.B. 557, 581, 586.
 ■ B.G.B. 535-536, 540-541, 581.
 ■ B.G.B. 547, 558, 562.

■ B.G.B. 586, 592.
 ■ B.G.B. 550-553, 557-558, 597.
 ■ B.G.B. 573.

his knowledge or contrary to his express orders if he does so within 1 month from his discovery of the removal, unless the lessee gives security.⁹³

LESSEE'S RIGHTS AND DUTIES

The lessee must pay rent at the time or times agreed upon or, if not agreed upon, at the end of each term. The custom is that rent for land other than for farming purposes is payable on the first business day after the end of each calendar quarter; the rent for farm land, if fixed at a yearly amount, is payable the first business day after the end of each year of tenancy.⁹⁴

If for some reason (e.g. illness) a tenant cannot use the premises let to him, he is not released from payment of the rent, but he may deduct the value of any advantage derived by his lessor from his failure to use the premises.⁹⁵

A lessee may use the leased premises for the agreed purpose, but not for any other, and is responsible for loss, deterioration, or other damage caused by his willful default or negligence or that of a third party whom he has permitted to use the leased object, even though it be with the lessor's consent. He is not responsible, however, for alteration resulting from the agreed use (ordinary wear and tear). The lessee generally is responsible for ordinary repairs; and where he takes over farm land with livestock, he must preserve and return such stock unless he has taken it at a valuation, in which case he must return all the stock up to such valuation (subject, however, to the lessor's objection thereto) and be responsible meantime for such stock as though it were his own. The lessee is also not allowed to change the mode of cultivation of a farm whereby such change would extend beyond his term.⁹⁶

A lessee may not sublet without the consent of the lessor, but where consent is refused without cause he may terminate the lease. The lessee must report to his lessor any defect discovered in the premises and suggest preventive measures to avert damage or waste or any attempt or threat of another to claim rights over the leased object.⁹⁷

On termination of a lease the premises must be returned in good condition resulting from ordinary good care. If the premises are farm land, they must be returned with enough manurance and farm produce to continue the farming operations until new produce can be obtained therefrom. The lessee, however, is entitled to the difference between the value of the things he leaves on the farm and what he obtained when he entered thereupon.⁹⁸

If the leased thing is reduced in its fitness for contractual use at any time during the term of the lease and not through the lessee's fault, he may claim a reduction of the rent, demand indemnity, or remove the defect and charge the cost of such removal. But a lessee of mortgaged property has his claims only against his landlord and subsequent owners but never against a mortgagee.⁹⁹

If the leased object is not in whole or in part delivered to the lessee, he may terminate the lease. A lease may also be terminated

⁹³ B.G.B. 559, 560-563, 585, 590.

⁹⁴ B.G.B. 535, 551, 584.

⁹⁵ B.G.B. 552.

⁹⁶ B.G.B. 548-550, 553, 582-583, 586-589, 593-594.

⁹⁷ B.G.B. 545, 549.

⁹⁸ B.G.B. 591-593.

⁹⁹ B.G.B. 537-538, 541, 581, 1125.

by the lessee where the leased premises are not delivered on time when time is of the essence of the contract, or where the lease is for a dwelling and the condition thereof endangers health.¹

In the event of the rescission of a lease for any reason, all deposits must be returned, together with interest from the date of payment thereof.²

A lessor who disputes the lessee's right to terminate a lease on the ground that he did not grant the use at the proper time to the lessee or that he did not remedy any defect after proper notice so to do must prove his allegations.³

The foregoing provisions of the law of leases are generally operative in the case of hiring and letting of chattels except in so far as the further provisions of the Civil Code specifically apply to chattels.

LOANS

Under German law, loans, if gratuitous, are designated "Leihe"; but loans of money or fungibles for hire are known as "Darlehen".⁴ In all loans the borrower acquires no right to make use of the thing borrowed other than in accordance with the agreement, nor may he loan the borrowed article to another unless it be money or fungibles. He is bound to return the loaned thing at the termination of the time fixed or, if no time is fixed, when the purpose for which the thing was borrowed is accomplished.

In any case of gratuitous loaning, by giving notice and fixing a time the lender may demand the borrowed article if he require it himself or if the borrower die or violate the agreement as to use; and the lender is entitled to the return of goods loaned even without notice. Loans of money, if more than 300 marks, must be returned on notice of not less than 3 months, whereas loans of smaller sums are payable after 1 month's notice.⁵

Mercantile loans bear interest, which is implied in every mercantile transaction; for other loans, interest must be specified in order to be collectible. Where loans are made with a fixed charge therefor, such charge is payable at the expiration of each year or upon the return of the loan.⁶

If one promises to make a loan to another, he may revoke or refuse to carry out his promise if the pecuniary position of the other change.⁷

MORTGAGES

THE ORDINARY HYPOTHEK MORTGAGE

A mortgage is a pledge on an immovable. Under German law mortgages are of three types—the hypothek mortgage, the ground debt (Grundschild), and the rent debt (Rentenschuld). Each type is convertible into the other, and the assent of those who have an equal or inferior right is not required for such conversion.⁸

A hypothek mortgage is a charge for payment of a stated sum for and in satisfaction of an existent, future, or contingent claim. Such a mortgage is to secure the repayment of a debt, and the credi-

¹ B.G.B. 542-544.
² B.G.B. 543, 555, 581.
³ B.G.B. 542.
⁴ B.G.B. 607.

⁵ B.G.B. 609.
⁶ H.G.B. 354; B.G.B. 608.
⁷ B.G.B. 610.
⁸ B.G.B. 1198-1203.

tor can, in principle, enforce his rights in and to the mortgage only so long and insofar as there is a debt. In practice, two classes of hypothek mortgage developed, and a basic distinction came to be made between them—the ordinary hypothek mortgage, which depends for its validity merely upon registration, and the security hypothek mortgage, which continues to exist only so long as the debt upon which it is based exists. The ordinary hypothek mortgage, therefore, even though the debt upon which the mortgage is based has for some reason been removed or is barred by limitation, is still good if it exists of record against the property.⁹

An ordinary hypothek mortgage to be effective must be recorded in the land register, and thereafter the entry operates as a conclusive presumption of the facts contained therein.¹⁰ It is conversely true that if a recorded right is canceled it is presumed the right no longer exists. These presumptions are allowed because any entry in the land register can only be made either with the consent of the party whose rights may be affected thereby or upon the certification of the documents therefor. It naturally follows that it is the debtor's duty and responsibility, in all cases where he alleges it, to prove the nonexistence of the debt or its reduction by part payment or set-off or otherwise.

A transferee of a mortgage debt claiming payment out of the proceeds of the sale of the property is not affected by defenses and set-offs not disclosed in the register, unless he knew of them at the date of the transfer.¹¹

It can be understood that since notice to an owner or a party to a mortgage is necessary in order to permit an entry in a register or the change of a record thereupon, the whereabouts of all the parties should be known to each other and to the local courts; and if the whereabouts of one party is not known to another party concerned in a mortgage, provision must be made for notice to such party.

For the purpose of giving the notice which is required under the recording acts, the registered owner of the property is presumed to be the actual owner. When an owner is not domiciled in Germany, or when the other party is excusably ignorant of his identity or whereabouts, the party who seeks to give notice may apply to the local court and obtain the appointment of a person to and upon whom notices can be addressed and served. The German courts even go so far as to hold that where a mortgagee is unknown he may be barred by publication if, since the last entry in the land register regarding the mortgage, 10 years have elapsed and he has not meantime been dealt with as a creditor; but where there are several parcels covered by the mortgage, only those parcels are relieved of the mortgage charge whose owners apply therefor.¹²

COVERAGE

A mortgage debt includes the sum recorded plus legal interest at 5 percent (even though not expressed), together with the cost of notices and warnings, suit, and foreclosure. If the interest provided

⁹ B.G.B. 223, 1193.
¹⁰ B.G.B. 891, 1115.

¹¹ B.G.B. 1137-1139, 1156-1157.
¹² B.G.B. 1141, 1170, 1175, 1192.

is less than 5 percent, the mortgage may without consent be extended to include interest at 5 percent.¹³

A mortgage covers products of the land until sold, severed, and removed and all accessories on the premises, as well as money or rents payable in installments, if the mortgagee claims them within a year after they are due. It also includes all other rights to recurring performance and to insurance except where the object insured is restored or replaced.¹⁴

A mortgage on several pieces of property makes each piece liable for the entire claim, and the mortgagee can exhaust his remedy against all or any of them, together or singly, until the entire amount of the claim has been satisfied from all the parcels covered thereby.¹⁵

If a piece of land is added in the land register to another piece covered by a mortgage, the existing mortgage extends to the added piece, but the rights and obligations with which the added piece is already burdened take precedence. An owner cannot mortgage a part of a property unless such part is converted into a separate parcel and severed in the register from the other parts and itself registered as independent parcel on a separate folio; but each coowner may mortgage his undivided share.¹⁶

If the security of a mortgage is endangered, the mortgagee is entitled, after notice and allowance of a reasonable time for compliance, to seek satisfaction out of the land, or he may obtain an injunction even against a threatened depreciation. Deterioration of accessories contrary to the rules of orderly management is considered to be such deterioration of the mortgaged premises as will entitle a mortgagee to relief.¹⁷

An agreement by the owner of real estate not to sell or further mortgage is void, as is also an agreement before the maturity of the mortgage between the mortgagor and the mortgagee providing that ownership of the mortgaged property shall in a certain event pass to the mortgagee or an agreement giving the mortgagee an extra-judicial power of sale.¹⁸

CREATION OF A MORTGAGE RIGHT

Every mortgage interest of whatsoever kind may be created by documents authenticated to be registered; but it may also be created by a declaration made by the owner of the mortgaged property and communicated to the authorities who register it. In any case the mortgage obtains its legal status and existence only by registration.¹⁹

The land register must contain the following records of each mortgage: The name of the creditor; the amount of the claim, and, if the claim bears interest, the rate thereof; and if there be other incidental payments to be made, their amounts and the times for payment. The entry must also contain the consent of all the parties to the recording. The record must be registered in the proper book covering the specific property.²⁰ In the event the mortgage is so

¹³ B.G.B. 1118-1119.

¹⁴ B.G.B. 1120-1123, 1126-1128.

¹⁵ B.G.B. 1132.

¹⁶ B.G.B. 1114, 1131.

¹⁷ B.G.B. 1133-1135.

¹⁸ B.G.B. 1136, 1149.

¹⁹ B.G.B. 1168.

²⁰ B.G.B. 1115.

regularly registered the general presumptions arising from registry operate except as in this section indicated.

The mortgagee of an ordinary *hypothek* mortgage is entitled to the document or a certified extract from the record in proof of the existence of his mortgage right. This may be excluded by agreement, however; but if he obtains the document or the certified extract, it is presumed to have been delivered to him, and he retains the right thereunder so long as he possesses the proof thereof regardless of payment or other satisfaction of the debt secured thereby. In a security *hypothek* mortgage, however, the granting of the document or certificate is prohibited by law.²¹

In Germany a mortgage may be placed upon record before the creation of the debt which it is registered to secure. In such cases the mortgagee is not entitled to possession of the mortgage proof until the debt accrues. During the period between the registration of the mortgage and the date when the mortgage becomes effective the owner alone is entitled to the mortgage and to any documents relating thereto, and if the mortgage does not become effective they continue at all times to belong to the owner of the property.²² For ordinary types of mortgage, delivery of the mortgage document or certificate is presumptive proof of the effective making of the mortgage, and although this proof can be rebutted, the burden of rebuttal is upon the mortgagor.

Inasmuch as the entries appearing in the register are presumed to be correct, any change whatsoever, to be effective, requires the consent of all the interested parties. It should be noted, however, that where the date or place of payment is altered, or where the benefit of the mortgage is subdivided and an agreement is made between the beneficiaries for one of them to take priority, all parties of record are not necessarily interested in the particular entry.²³

DISCHARGE OF MORTGAGE

By payment.—When the discharge of a mortgage is sought through payment, such payment must be made in accordance with the terms in the mortgage itself; or, if no provision is made therefor, then according to the general law of performance of contracts. Generally, however, when the time of payment is not specified, a demand by the mortgagee for payment after 6 months' notice or notice by the mortgagor that he will pay after 6 months, is valid; and payment becomes due in accordance with the notice and must be made at the place of registry.²⁴

When a mortgage falls due according to the agreement, the owner of the property may pay by depositing with the public official authorized to receive same or he may satisfy the mortgage by set-off. A third party whose rights would be affected by the sale of the mortgaged property can also satisfy it. When a mortgage is paid by the owner or an interested third party it becomes the property of the person who pays, and such person has a claim against the original debtor under the mortgage like a surety who pays. Where the owner pays a mortgage and discharges the obligation, only the principal

²¹ B.G.B. 1116-1117, 1185.
²² B.G.B. 1117, 1163.

²³ B.G.B. 1119, 1151.
²⁴ B.G.B. 1193-1194.

sum provided for in said mortgage remains effective but not interest, costs, or other sums paid by the owner. However, such sums, if paid by an interested party other than the owner, would become a charge under the mortgage.²⁵

If the mortgage debt is paid out of the proceeds of a judicial sale or out of income obtained through a judicially appointed receiver, the mortgage charge itself is completely extinguished. The method by which income on a mortgaged property is collected by a judicially appointed receiver and applied to the reduction of a mortgage debt is outlined in the civil practice act. Payment made from the proceeds of one or more pieces of land covered by an aggregate mortgage by judicial sale thereof or collection of income therefrom extinguishes in like manner claims against the other pieces. Where a mortgage debt is paid by the owner of one parcel of several covered in a mortgage, or where several owners become entitled to a reduction of an aggregate mortgage, each one of them is entitled to take a reduced charge on his own parcel in place of a collective reduction.²⁶

An owner or any interested third party, upon payment of a mortgage debt or other satisfaction of the mortgage, is entitled to the return of the mortgage and all other instruments required for registration in the land register or for the release of the mortgage. On partial payment the creditor is obligated to note the payment on the mortgage, to give a receipt therefor, and to submit the mortgage instrument, if he has it, to the land registry for entry in the records.²⁷

By renunciation.—A mortgagee may renounce, by document authenticated for the record or by declaration to the land registry in the same manner as that required in the making of a mortgage, the whole or any part of a mortgage claim, and when he does so the amount of said mortgage claim so relinquished becomes vested in the owner of the property. When the mortgagee renounces on a collective mortgage, all the mortgagors share in the renounced amount. He may, however, renounce his rights or claim on only one of the parcels, in which case the amount of the mortgage is reduced only as to that particular parcel.²⁸

By legal process.—Since the purpose of a mortgage is to secure payment either of a principal sum or installments and obligates the mortgagee to the payment thereof, where the mortgage debt (principal) or any interest thereupon remains unpaid, after such amount falls due, the mortgagee may seek relief from the courts and force the payment of such overdue amounts by means of a judicial sale or from income through a judicially appointed receiver. The Civil Code provides specifically: "The satisfaction of the creditor out of the land and out of the objects which are covered by the mortgage is enforced by execution."²⁹

The action for the enforcement of such charge can be brought only against the registered owner of the mortgaged property; but if the registered owner is not the true owner, the latter may intervene in the court proceedings and bring forward any right or defense to which he may be entitled against the original mortgagee or any

• B.G.B. 1142-1143, 1150, 1164, 1178.
• B.G.B. 1147, 1172-1173, 1181; Z.P.O. 869.
• B.G.B. 1144-1145, 1167.

• B.G.B. 1168, 1175.
• Z.P.O. 869; B.G.B. 1147.

assignee of such original mortgagee. The owner of the mortgaged property may also, if he is not the personal debtor, interpose any defense or set-off to which the personal debtor may have been entitled against the mortgagee.³⁰

THE CAUTIONARY OR SECURITY HYPOTHEK MORTGAGE

A strict distinction must be made between the ordinary hypothek mortgage and the cautionary or security hypothek mortgage. Originally the mortgage had only one use—to secure the payment of a debt; but business required a mortgage which would continue in existence regardless of the debt which it secured. This need resulted in a distinction between a hypothek mortgage and the so-called cautionary hypothek mortgage. The basic difference now between the ordinary hypothek and the cautionary hypothek mortgage is that for the former the record of the mortgage is conclusive for the benefit of the mortgagee, whereas for the latter there is no presumption in the record and the mortgage security is good only so long as the debt remains.

A mortgage is always considered to be a cautionary hypothek mortgage (*a*) if so designated on the register, (*b*) if expressly created as security for a debt, or (*c*) if created as collateral security for the payment of a negotiable instrument.³¹

GROUND DEBT

Land can also be burdened with a charge that a certain sum of money is to be paid only out of the land to one in whose favor the burden is created. This is a ground debt (*Grundschuld*), and it can be made in such manner as to include interest on the money and other secondary payments.³²

The provisions herein set forth in regard to mortgages generally apply also to ground debts, the only distinction being that the ground debt does not presuppose the existence of a claim. In fact, a ground debt may even be created for the benefit of the owner himself; but when he is the creditor he cannot have execution and is only entitled to a ground debt interest when the land is seized by some other person under execution.³³

RENT DEBT

A rent debt (*Rentenschuld*) is an annuity charge on property to secure the payment from time to time of certain amounts. It is in all respects the same as an ordinary ground debt except that it is for installment or annuity payments and the ground debt is for the payment of a specific sum. The same laws apply to it as to the ground debt. In burdening a property with a rent debt, however, it is necessary to provide a redemption sum (*Abloesungssumme*) which represents the amount to which the mortgagee is entitled in the event the mortgagor wishes to free the land of such installments for all time or in the event the safety of the payments is endangered by the deterioration of the mortgaged property by the mortgagor or a person holding under or through him.

³⁰ B.G.B. 1137, 1148, 1157.
³¹ B.G.B. 1184, 1190.

³² B.G.B. 1191.
³³ B.G.B. 1192, 1196-1197.

PLEDGE OR LIEN

Movables also can be employed as security for the performance of an act or for the future satisfaction of an obligation or conditional claim. Where they are so employed the right of pledge (Pfand) attaches to them, and the creditor is entitled to seek payment or satisfaction out of the article pledged. This right of pledge extends to any semblance of a right to a thing, even though it be an immaterial right, so long as the right is capable of assignment or transfer.³⁴

This right of pledge may be created in a thing (a) when the article remains in the possession of the pledgor, as in the case of a pledge on a ship, in the case of a charge on freight and cargo created by bottomry bonds, and where a lessor acquires rights to things of the lessee brought on the leased premises, or (b) when the article is deposited with the pledgee as in the ordinary contract of pledge or security, or by statutory act or law as in the case of the lien or pledge acquired by commission merchants, forwarding agents, carriers, and innkeepers, and contractors' rights in things altered or produced by them.³⁵

The same rules, insofar as practicable, apply to pledges acquired by contract as apply to those acquired under a statute or a law. The only difference between the two types of liens is that a mercantile statutory lien (Zurueckbehaltungsrecht) gives a creditor the right to satisfy his claim by the sale of the thing pledged only under an order of the court empowering him so to do, whereas a lien acquired through contract (Pfandrecht) gives the right of sale without such authorization.³⁶

Special acts for pawnbrokers have also been passed in many German States.³⁷

COVERAGE

A pledge to secure payment of money includes interest and costs and expenses incident to the enforcement of payment and sale, except that with regard to ships the amount of the pledge may not exceed the registered amount of the lien. The lien extends even to products separated from the pledge, and to profits accruing from the use of the pledge, if so provided under the contract of pledge; or such profits may be taken by the pledgee, accounted for, and deducted from the amount of the debt. It also covers fruits of the pledge, which are presumed to be the property of the pledgee in the absence of agreement to the contrary. Where the pledged object is a share or a bond, interest and dividends or coupons thereon are included when they are delivered with the pledge, provided the pledgor does not demand their return when they fall due; but, of course, such interest, dividends, or coupons are forfeited to the pledgee when the right of sale of the pledged article comes into operation.³⁸

With regard to a ship, the pledge right extends to all the accessories thereto pertaining, and an undivided share of the ship can be

³⁴ B.G.B. 1204, 1273-1274.

³⁵ B.G.B. 559, 581, 647-648, 679, 704, 1257, 1260-1271; H.G.B. 397-399, 410-411, 440-442.

³⁶ B.G.B. 1257; see also Schuster's translation of the Commercial Code, note to sec. 369

on p. 178.

³⁷ E.G. 84.

³⁸ B.G.B. 1210, 1212-1214, 1293-1296.

the proper subject matter of a pledge. Where the pledge covers several articles, all are charged with the entire debt, and satisfaction can be obtained upon default by the exercise of the right of sale of one or more until the debt is satisfied. Where the pledge is on an undivided share, the right of partition cannot be exercised until the pledgee obtains the right of sale.³⁹

The pledgee's right to the pledged article is not affected by the fact that the claim secured by the pledge is barred; and as between several pledgees, the pledge created first in time takes precedence and priority over all others even though it may have been given as security for a future or contingent claim. However, in the case of liens for forwarding of goods, as between statutory lienees priority arises in the reverse order, and such statutory rights take precedence over any other rights of pledge.⁴⁰

To obtain the right of pledge, except where provided by statute, the same contract formality is required as in the transfer or assignment of rights (except special requirements as to ships for registry in pledging of ships). The right of possession is governed by the same rules as govern the rights of ownership generally. A right of pledge may be transferred only with the transfer of the pledge itself, in which event the transferor remains liable for all obligations of the transferee. The pledge of a claim cannot be transferred by mere assignment, unless it be accompanied by notice to the original debtor. Any agreement between the pledgor and the pledgee providing for the transfer of ownership, if made before the time at which the pledgee acquires the right of sale, is void.⁴¹

RIGHTS AND DUTIES OF PLEDGEE

A pledgee's rights involving, as they do, possession of the pledged articles, he must use the same degree of diligence with regard to all pledges as though he had undertaken their custody. Where the pledged article includes fruits and profits, he is obligated to exercise proper diligence to obtain such fruits or profits, which must be applied toward the satisfaction of the debt. If he makes an outlay to preserve the pledged object, he is entitled to reimbursement therefor.⁴²

If the pledgee materially interferes with the rights of the pledgor and continues so to do after notice, the pledgor may demand that the pledged article be deposited with the public authority or with a receiver appointed by the court or he may demand redelivery upon payment of the debt secured thereby. If waste or depreciation of the pledge is even apprehended, the pledgee must give notice thereof or respond in damages therefor; and the pledgor may demand the return of the pledged article against the deposit of other security.⁴³

Where the pledged object is a ship, no question of custody arises because the ship remains in the possession of the pledgor, but on payment in such case the pledgee must return all the documents turned over to him in order to enable the pledgor to change the registry. The pledgee of articles other than ships also must, upon payment or satisfaction of his claim, redeliver the pledged object.

³⁹ R.G.B. 1222, 1258, 1265, 1272.
⁴⁰ R.G.B. 223, 1269; H.G.B. 443.
⁴¹ R.G.B. 1268, 1274, 1284.

⁴² R.G.B. 1214-1216.
⁴³ R.G.B. 1217-1218.

Where the lessor's pledge is removed, he may sue within 1 month of removal for recovery of anything taken by the lessee from the premises if not in the ordinary course of business. If the lessee threatens removal, security may be demanded.⁴⁴

RIGHTS AND DUTIES OF PLEDGOR AND THIRD PARTY

The pledgor's rights in the pledged article before the pledgee acquires the power of sale are outlined above. The pledgor's rights in and to the pledge arising from the alteration or depreciation of the pledge and all claims with respect thereto are barred after 6 months from the redelivery of the pledge. A pledgee surrendering a lien releases the surety.⁴⁵

After the maturity of the claim either the pledgor or any party whose interest may be affected by the sale of the pledge may intervene and demand delivery of the pledge upon payment to the pledgee; and if the pledgor (not being the personal debtor) or any other third party redeems the pledge, such redeemer of the pledge has a claim against the personal debtor therefor.⁴⁶

In the event the pledgee is in possession of a pledged article the title to which is defective in him or if the pledgor was without title thereto, the rules as to the acquisition of ownership of movables from persons without title apply; and where the pledged object is subject to the rights of another at the time of the pledge, the pledgee's right becomes prior to such rights, unless he at the time of the creation of his right does not deal in good faith.⁴⁷

SATISFACTION OUT OF THE PLEDGE

The purpose of a pledge is to give a pledgee, if necessary, the right to satisfy a claim or debt out of the pledged object; but this right does not accrue for his benefit before his right of sale becomes enforceable on the due date of the debt or claim secured thereby, and even then it may be enforced only by execution.⁴⁸

Where performance or payment is to be made on notice at the due date, the notice must be promptly given and to all the parties interested in the pledged article; and any party who, by the sale of the pledged article, might lose a right with regard thereto may demand and redeem the pledge any time thereafter, and such redeemer of the pledge becomes vested with the pledge and the debt against the principal debtor.⁴⁹

The pledgee has the right to dispose of the pledge before his right to the sale thereof accrues if the pledged object is threatened with deterioration or is inadequate security for the debt, but only after he gives notice to the pledgor thereof and of the fact that he intends to sell the pledged article unless the pledgor within a reasonable time gives other security. He may sell only by public auction unless the pledge is quoted on the stock exchange or has a definite market value, when sale is allowed through a private broker at the current price. In such cases, however, the proceeds of the sale take the place of the pledged object, and the pledgor may demand that the sale price be deposited until the due date.⁵⁰

* R.G.B. 560-562, 1223, 1267.

* R.G.B. 776, 1226.

* R.G.B. 1223, 1225, 1249.

* R.G.B. 1208-1209; H.G.B. 366-368.

* B.G.B. 223, 1204, 1277.

* B.G.B. 1225, 1249, 1265-1286, 1288.

* B.G.B. 1219-1221.

If payment is not obtained by the pledgee on the due date, he may take steps to enforce his claim by sale immediately; but if that which is due is not money, the sale is permissible only after the claim has been reduced to a money claim. This right of sale extends to negotiable instruments but not to ships, as to which latter the sale is to be accomplished as in the case of a sale under a defaulted mortgage on real property.⁵¹

Where the pledged article is in the joint possession of the pledgor and the pledgee, as soon as the right of sale accrues the pledgee may demand the deposit of the article with a third party in order to guarantee delivery thereof to the purchaser in the event of sale.⁵²

When the pledgor is forced to sell in order to obtain satisfaction out of the pledged article, he must first inform all parties interested therein of his intention so to do and must advise them of the amount of his claim, and a month must elapse thereafter before the sale; but where the transaction is mercantile or the pledge is statutory the sale may be conducted within one week. To effectuate a proper legal sale the time and place thereof must be publicly announced, and notice must also be given to the owner of the pledged article and to third parties having rights therein. For the purpose of notice to the owner the pledgee may, in the absence of knowledge to the contrary, consider the pledgor such owner.⁵³

Where there are several pledgees, the right of sale may be exercised by any of them. A prior pledgee need not deliver the pledged article to a subsequent pledgee to sell, but he cannot oppose the sale of the pledged article for the account of a subsequent pledgee unless he wishes to sell it in satisfaction of his own rights.⁵⁴

Where several articles are pledged together to secure a debt or claim, a pledgee may sell such as he selects (in the absence of agreement to the contrary); but he is not entitled to sell more than are necessary to satisfy his claim, and insofar as the proceeds of the sale satisfy the claim such claim is deemed to be discharged.⁵⁵

When the right of sale accrues, either the pledgor or the pledgee may demand that the sale be conducted in the manner which he considers will obtain the best results even if it differs from the method agreed upon in the contract of pledge. If the consent of the other parties is refused, the question must be turned over to the local court for decision.⁵⁶

In any case where the pledgee sells the pledged article in disregard of the rules for the sale of pledged articles, he is liable for any damages due to default on his part.⁵⁷

All rights of pledge are extinguished by the sale of the pledged article.⁵⁸

Where the object is a mere pledged right, the power of sale is also given to the pledgee unless otherwise provided; and the other general rules of pledge on movables apply except as modified by the Civil Code.⁵⁹

Deposits for the purpose of security (Sicherheitsleistung) are governed by the rules of the Civil Code.⁶⁰

⁵¹ B.G.B. 1228, 1268.

⁵² B.G.B. 1231.

⁵³ B.G.B. 1233-1234, 1236, 1238-1239, 1248; H.G.B. 368.

⁵⁴ B.G.B. 1232.

⁵⁵ B.G.B. 1230, 1247.

⁵⁶ B.G.B. 1246.

⁵⁷ B.G.B. 1243.

⁵⁸ B.G.B. 1248.

⁵⁹ B.G.B. 1273-1296.

⁶⁰ B.G.B. 222-240.

BAILMENTS

Contracts of bailment arise upon delivery of an article (a movable) from one party to another, to be held according to the purpose or object of the delivery and to be returned to the depositor or delivered over to another when the purpose for which the deposit has been made is fulfilled. In this section delivery merely for the purpose of custody or safekeeping is discussed. There are, however, other bailments, such as when delivery is made to secure the performance of a promised act or satisfaction of a claim, in which case it is a pledge and the laws of pledge apply, or when delivery is made as a loan, in which case the laws of loan or rent (*Leihe* oder *Miete*) apply.

ORDINARY CUSTODY

Where a depositary (even though he may not be a warehouseman) is called upon to undertake the custody of a movable (*Verwahrung*), compensation therefor as well as reimbursement for expenditures in connection therewith is ordinarily presumed.⁶¹ There is a special law as to the custody of negotiable instruments. (See p. 101.)

The compensation for custody must be paid at the end of the contract unless fixed by periods, in which event payment must be made at the end of each period; and if the custody ends before the termination of the period fixed, the depositary is entitled to a proportionate share of the charge.⁶² Reimbursement for outlays may be demanded immediately after the outlay.

The depositary is liable for willful default or negligence; but if the deposit is accepted without charge for custody, he is responsible only for such care as he bestows on his own things. He may not, however, without permission leave the custody to third persons or alter the mode of custody, unless he can prove that the depositor, with knowledge of the facts, would approve of the change. Ordinarily, however, he should advise the depositor of the proposed change and await instructions, unless there be danger in the delay.⁶³

The bailor may at any time, even before the term fixed, demand the return of the article deposited, and it must thereupon be delivered back at the place where it is kept. The bailee is not obligated to remove it; this is the duty of the bailor.⁶⁴

If no time is fixed, the depositary may demand the removal of the deposited article at any time; but if the time is fixed, he can demand its removal only for important reasons.⁶⁵

In cases of ordinary friendly bailment other than in the line of the bailee's business, if deposited money is used by the custodian payment for the use thereof must be made.⁶⁶ If replaceable things are deposited, things of the same kind and quality and quantity must be returned on demand; and if they are used meanwhile, compensation must be paid therefor by the depositary in the same manner as in an ordinary rent.

In certain mercantile transactions merchandise is intrusted to the care of others, not for the purpose of custody or safekeeping, but for sale, exchange, delivery, or transfer to another. The liability then does not depend upon the laws of bailment, but upon certain other

⁶¹ B.G.B. 688-689, 698; H.G.B. 420.

⁶² B.G.B. 699; H.G.B. 420.

⁶³ B.G.B. 690-692.

⁶⁴ B.G.B. 695, 697.

⁶⁵ B.G.B. 696; H.G.B. 422.

⁶⁶ B.G.B. 698.

laws regulating the rights and duties of merchants to protect, preserve, and safeguard that which comes into their possession. Such are the cases where merchandise is sent on approval or on test or on consignment or to a commission merchant for sale, or when sold the merchandise is rejected upon delivery. The Commercial Code places a duty and a responsibility upon the merchant for the safekeeping of the goods; and if the goods are perishable and there is risk that they may deteriorate in value during the time necessary to give notice to the owner and obtain his advice as to their disposition, the receiver of such merchandise may have it sold according to the rules of the Commercial Code for such sales. He is entitled to claim a commission in respect of such sale; but if he sells the goods unnecessarily or illegally, he is liable for damages. The person upon whom this responsibility is placed can claim compensation therefor, and if he warehouses the goods he can claim the warehouse expenses, together with any other expenses he incurs, with interest thereupon. If the receiver of merchandise does not fulfill his duty to warehouse the goods, ordinarily he is liable in damages, and his failure to do so may even involve a forfeiture of his right to complain of defect in the goods.⁶⁷

A merchant receiving goods becomes responsible for their care and custody and to free himself of liability must be able to prove that he and those in his service have acted with the care of prudent merchants.

WAREHOUSEMEN

One who in the regular course of trade undertakes the storage and custody of goods for compensation is a warehouseman (*Lagerhalter*).⁶⁸ The custody of movables by a warehouseman is a purely mercantile transaction. The rights and obligations of the parties are as defined by the Civil Code except where the sections of the Commercial Code make specific provisions with regard thereto.

As to receipt, custody, and insurance of goods, the warehouseman's rights and liabilities are the same as those of a commission merchant. He is responsible for loss or deterioration only if it could have been avoided by the application of the diligence of a careful mercantile trader; is not bound to insure goods unless specifically instructed so to do; and is liable for the default of his employees to the same extent as for his own default. If the goods in his charge are affected by a change or if he fears depreciation, he must immediately notify the bailor; failure so to do renders him liable for the resulting damage. He must allow access to such merchandise by the bailor for the purpose of inspection, for sampling, and to provide for its preservation.⁶⁹

In the case of fungibles, he may not, without express permission, intermix them with others of the same quality or variety, nor does he, except by definite agreement, acquire any property in such goods. However, if he does acquire property in the fungibles so deposited, he is bound to return fungibles of the same kind and quality, and he must pay for the use thereof in accordance with the law of loans.⁷⁰

⁶⁷ H.G.B. 347, 354, 362, 372, 377, 379, 388, 390-391; B.G.B. 276.

⁶⁸ H.G.B. 416.

⁶⁹ H.G.B. 417-418; B.G.B. 691.

⁷⁰ H.G.B. 419; B.G.B. 700.

A warehouseman is entitled to compensation in accordance with the agreement; if the amount, however, is not fixed either by agreement or by the custom of the locality, he must fix a fair and equitable rate. He is also entitled to compensation for all outlays for freight and duties and for other expenditures necessary in connection with the custody of the merchandise intrusted to his care. Cash disbursements are payable at once, and the other expenses and warehousing charges are usually paid every 3 months or at the time of the withdrawal of the goods. If the goods are withdrawn only in part, a proportionate part of the charges is payable upon such withdrawal, unless the goods remaining with the warehouseman are sufficient security for the entire charge. Claims for storage and for repayment of sums expended are barred as a rule in 2 years, but the period is extended to 4 years when the warehousing is carried on in the course of the depositor's trade. The period of limitation begins to run at the close of the year within which the claim arises.⁷¹

A warehouseman has a lien on the goods in his possession or so long as he exercises power of disposal over them by bills of lading or carrier's or warehouse receipts. He is bound to return that part of the goods not required for security under his lien. In realizing on his right of lien he is required to proceed with the ordinary care of a prudent merchant and is entitled to compensation for his work in satisfying his claim from the merchandise. The depositor cannot compel the warehouseman to recoup himself out of the stored goods before seeking to establish his claim against the depositor, but such depositor may resist execution levied against his other property to the extent that the claim for warehousing charges may be satisfied from the goods warehoused.⁷²

The warehouseman may not demand the removal of the goods before the expiration of the term; and if no term is fixed, not before 3 months after the deposit. If the merchandise is still in his custody after that time, he can only demand removal after 1 month's notice, except on cogent grounds.⁷³

CUSTODY OF SECURITIES

There is a special law (Depotgesetz) regulating the custody of securities. It applies only to merchants whose business is the keeping of securities for others. The law does not apply to small traders,⁷⁴ even though the depositor with such small trader happens to be a merchant himself.

This law imposes on merchant custodians of securities certain duties which are extensions of the duties of the ordinary custodian and include keeping the securities separate, maintaining records of the transactions in special books, and furnishing inventories. These duties are only incidental to the real purpose of the law. Sections 9 to 12, the really important sections, were put into the law to assure depositors that their instructions in connection with securities would be completely and correctly observed and the securities returned at the termination of the contract of custody.

⁷¹ R.G.B. 196, 201, 315-316; H.G.B. 420.

⁷² H.G.B. 421; Z.P.O. 777.

⁷³ H.G.B. 422.

⁷⁴ D.G. 13.

Breaches of the special duties do not entail criminal punishment except in the event of bankruptcy or liquidation, and then only because neglect thereof makes it difficult for the depositor to obtain the return of his security; nor is it generally necessary that it should be so, for they are really only additional safeguards to guarantee performance of agents and to insure the return of securities. The return of the security deposited and the carrying out of the instructions of principals are the only features seriously sought to be regulated by this law and their defaults punished thereunder.

DUTIES

A merchant intrusted with the care of securities must (a) so clearly mark the deposits as the property of the depositors that they are identifiable without reference to the record book and must keep them separate and distinct from his own property and the property of others, either in special envelopes endorsed with the names of the owners or in separate compartments, and (b) maintain a trade book and enter therein the securities belonging to each depositor together with their nature, nominal value, numbers, and other distinguishing marks.

These extra duties are only imposed where a merchant in the ordinary course of business receives unsealed, for custody or upon pledge, shares of stock and mining shares, scrip, renewal certificates (dividend warrants), documents of indebtedness (debentures), and other negotiable securities. Drafts, bills of exchange, checks, bills of lading, dock and warehouse receipts, bottomry bonds, policies of insurance, bank notes and paper money, and mortgage certificates are not subject to this law. The burden of proof that a transaction is not "in the regular course of business", in order to relieve a depository of compliance with the extra duty under this law, is upon such depository.

The depositor may, subject to revocation at any time, authorize the return of other securities of the same kind; but such authority must be in writing and be given specifically for each transaction (a general authorization is invalid) unless the depositor, as well as the depository, is engaged in the business of a banker or money changer. Where this authority is given, the provisions of section 1 of the law necessarily do not apply.⁷⁵

Under all contracts for the custody of merchandise or securities, it is necessarily contemplated that whatever is deposited is expected to be returned, and under this special law it is also necessarily expected that the identical securities deposited will be returned; but acceptance in kind will be considered performance. The depository, however, has a lien for his services if compensation is charged. He may satisfy himself out of the securities deposited for his own personal claim against the depositor.

A commission merchant who executes an order to buy securities must, within 3 days of the making of such purchase, give information by inventory, which shall include the name, nominal value, and numbers of the shares or other specific identification marks thereon, but such inventory need not be signed if the covering letter is signed. The right to this inventory may be waived (except in

⁷⁵ D.G. 2.

transactions with bankers, when inventories are not required) or it may be dispensed with if the securities are delivered or if an order is given for the resale thereof. The waiver of notice must be in writing and cannot be implied. If a commission agent does not give the inventory upon demand after 3 days, the principal is entitled to repudiate the bargain and claim compensation for nonperformance.⁷⁶

The commission agent who is given an order to exchange securities or to enforce a right to their acquisition must send his principal an inventory of the securities obtained within 2 weeks from the time of his receiving them unless he has handed them over to his principal in the meantime. Otherwise he is not entitled to commission for the service. Upon the dispatch of the inventory the property in the securities described therein passes to the principal if the agent has legally acquired the rights to them, unless under the Civil Code property passes before that time. As to these securities the agent is responsible in accordance with the rules and regulations of chapter I of this law.⁷⁷

COMPENSATION

This type of business is usually, but not necessarily, conducted by bankers and ordinarily without compensation, but in case of doubt compensation is payable. Many bankers render this service gratuitously to their regular customers, and in so doing they obligate themselves to do nothing but keep the intrusted securities safely and comply with the law. They may obtain compensation, however, if they are required to do something with respect to the deposits, such as collecting dividends or the interest thereon; in which latter case the contract is no longer one of mere mercantile custody but becomes a contract for services as well.⁷⁸

The obligation of the depositary to exercise care is the same as in ordinary custody; that is, if he is compensated for custody, he is responsible for the care of an ordinary mercantile trader, but if no compensation is contemplated he is responsible only for the same care as shown with regard to his own property. He is liable for the default of his employees.⁷⁹

NOTICES

A mercantile trader who, in the course of his business, deposits securities which do not belong to him, for custody, sale, or exchange, or who passes on to another the order for their acquisition, must notify such transferee that the securities are not his own or that the acquisition is for another. In such case the transferee acquires a lien against the securities only for his services in connection with the particular securities.⁸⁰ Failure to advise that the securities belong to or are for another makes the defaulting transferor responsible for damages and gives to the transferee a lien on the securities for all claims against the transferor.

If the transferor gives such notice after the deposit of the securities, the notice is inoperative because it cannot affect a general lien which has already been acquired by the transferee; but if no general lien has arisen, the notice must be accepted, and from that date it prevents a general lien from coming into existence, and

⁷⁶ D.G. 3-4.

⁷⁷ D.G. 5-7.

⁷⁸ B.G.B. 6-9, 765; H.G.B. 354; D.G. 1.

⁷⁹ H.G.B. 347; B.G.B. 278, 690.

⁸⁰ D.G. 8.

only a special lien against the securities in connection with the services to the securities can arise.

This notice may be given orally or in writing, and there is no obligation to name the principal. The burden of proof that the transferor notified the transferee that the securities were the property of another is upon the claimant, and the good faith of the transferee is presumed.

PENALTIES

Wherever a trader *wrongfully disposes* of securities intrusted to his care for any purpose, whether in his own interest or in the interest of a third party, or where the transferor makes a disposition of securities intrusted to his care not in accordance with the instructions of his principal, he is punished by imprisonment and/or fine.⁶¹ This penal liability is upon the head of a business if the wrongful dealings are carried out by his subordinates, and they become accomplices or accessories. Trading partners are all considered to be accomplices.

As has already been said, the primary purpose of this securities law is to insure the return of deposited securities. Section 9 specifically provides for punishment where the purposes of the law are defeated. The offense of wrongful disposition is a broader and more serious one than the offense of wrongful appropriation covered by section 11. Wrongful disposition may even be a temporary disposition, as, for instance, the pledge of negotiable paper belonging to another or a sale with agreement to repurchase; but the mere attempt to dispose of securities is not such a disposition nor is the using of shares merely for voting. It would seem that wrongful disposition might be defined as when the use "of such shares would jeopardize the ownership of the depositor." A disposition is also not wrongful if it is made in the interest of the depositor—e.g. to save his securities from fire or water—or if made with his authorization under section 2 of this law, or pursuant to statutory power (compulsory sale).

A trader suspending payment or becoming bankrupt is punishable if, through intentional neglect in the keeping of books or of other duties, he prejudices the right of the parties who deposit the securities to identify them and obtain their severance.⁶² Here again the penalty imposed is clearly stated as imposed only because the default of the trader prejudices the depositor's efforts to recover his security; and as a matter of fact the default of the trader is punishable only in the event that a difficulty in the recovery of the securities is the direct result thereof.

When a depositary suspends payment or becomes bankrupt, he is punished criminally if he *wrongfully appropriates* securities of another received in the ordinary course of business. This provision of the law is a general one referring to securities of all kinds. It was brought about by the demand of depositors for an extension of the law of embezzlement because the Penal Code had not provided punishment for this special kind of embezzlement. It is an extension of the bankruptcy law as well. It is not so strict as those sections which provide for wrongful disposition as it includes only wrongful appropriation, so that if a depositary merely pledges or

⁶¹ D.G. 9.

⁶² D.G. 10.

sells securities with the intention or agreement to redeem them and believes he will be able to do so the penal punishments do not apply.⁵²

The above general penal provisions apply to directors of share companies or registered societies, managers of associations with limited liability, and liquidators—in other words, to the general legal representatives of juristic persons.⁵⁴ Such directors, managers, and liquidators, under the strict interpretation of the law, are not themselves mercantile traders and are therefore not liable, but they become liable as individual mercantile traders and partners under this section.

SALE AND EXCHANGE

A sale under German law is always considered to be an agreement to sell and is therefore governed by the rules of contract. The distinction between commercial and noncommercial sales should always be kept in mind, for whether the transaction is commercial or noncommercial affects the rules, rights, and remedies governing each case.

All business transactions between merchants in the ordinary course of business are mercantile. The difficulty in making the distinction between a commercial and a noncommercial transaction arises when only one party is a merchant. The criterion adopted usually is that if the merchandise sold is intended to be resold for profit the transaction is mercantile, regardless of the status of the parties; but there are instances where one party as a merchant in the ordinary course of his business sells to or contracts with a non-merchant where the contract itself is mercantile as to the merchant and is nonmercantile as to the nonmerchant. (Example, the relationship between publisher and author.) Generally, however, in business relations between merchants and nonmerchants, if the transaction is mercantile the parties will be treated alike and their transactions will be governed by the provisions of the commercial law.⁵⁵

Sales of real property are held to be civil contracts, as are leases, except where they are upon business property or where the sale includes a business in connection with a factory.

Where sales are considered nonmercantile, the sections of the Civil Code⁵⁶ apply in the same manner as they apply in mercantile sales in the absence of appropriate sections of the Commercial Code.

It is contemplated in a sale that the seller must have or obtain the right in the thing sold and must give the purchaser proof of ownership or indicia of title (if the right includes possession of the thing, he must also deliver that to the purchaser); and the buyer must accept and pay therefor. The agreement of sale need not be in writing except in the case of the sale of an immovable or of the estate of a deceased person or an interest therein.⁵⁷

The provisions as to sales apply to exchange and all other agreements for the alienation or hypothecation of property.⁵⁸

PRICE

In a contract of sale where the price is not fixed or is in doubt, it must be determined in an equitable manner and will be presumed to

⁵² D.G. 11; K.O. 239.

⁵³ D.G. 12.

⁵⁴ H.G.R. 373-382.

⁵⁵ B.G.R. 443-515.

⁵⁶ B.G.R. 313, 433, 2033, 2371.

⁵⁷ B.G.R. 445, 493, 515.

be the market price prevailing at the time and place of fulfillment. If the market price be fluctuating, the average market price will be fixed as the purchase price; and if no market price can be established, the price will be fixed at the current figure at which the article should sell in that neighborhood. A sale in which the price is to be fixed by a third party is also presumed to be determined in accordance with equity. Such a sale is void if for any reason whatsoever the third party does not act. In a mercantile sale where price is to be determined by weight, it is to be presumed that payment will be made upon net weight. In all commercial sales interest is chargeable if payment is not made at the time title passes.⁸⁹

Payment may be stipulated in foreign currency, in which case it is payable in marks at the exchange rate current at the time and place of payment, unless there is a specific agreement that payment is to be made in foreign currency.⁹⁰

COSTS

In the absence of agreement, the cost of delivering the merchandise sold is generally borne by the seller up to the point of change of title and thereafter by the buyer; and change of title is usually effected by delivery of the thing sold. If the parties to the contract of sale are in the same place, delivery is held to be and title to pass at the place where the goods happen to be at the time of sale, and the costs of delivery and of weighing and measuring are on the seller. If the parties are in different places, title passes when delivery is made to the forwarder, provided such delivery is made according to the instructions of the purchaser, and the costs of additional carriage, forwarding, and final delivery are borne by the purchaser.⁹¹

The costs of sale and registry of transfer of an immovable are borne by the purchaser, but the costs of the assignment of a right are paid by the seller.⁹²

RISK

Generally, the risk remains in the vendor until delivery, when it, together with all the emoluments and burdens of the property, passes to the buyer. Delivery may be made by physical transfer or constructively, and where the delivery is made and transfer is accorded by delivery of documents of title or a symbolic act title passes on such transfer of documents or the act alone.

Delivery in the case of an immovable is interpreted as at the time of registration thereof, even though delivery of possession has not as yet been made. As to movables, delivery to a purchaser at the place of sale constitutes delivery for passing the risk; but where the destination is different from the place of sale, the risk passes to the purchaser on delivery to the forwarding agent or carrier, unless the vendor deviates from the purchaser's instructions regarding the mode of forwarding or in any other material respect, in which case the vendor remains liable for the damages. Delivery is presumed to be made and the risk with regard to the merchandise passes to the purchaser even when the purchaser does not accept.⁹³

⁸⁹ H.G.B. 315, 317, 452-453; H.G.B. 380.

⁹⁰ H.G.B. 244-245.

⁹¹ H.G.B. 448, 450.

⁹² H.G.B. 448.

⁹³ H.G.B. 293, 446-447.

Somewhat involved in the question of risk is the duty of merchants regarding the custody of merchandise delivered over to their care, even though rejected by them. (See H.G.B. 379 and discussion under "Bailments," p. 109 hereof.)

DUTIES OF THE PARTIES

It is well established in German law that the vendor must disclose all the essential facts as to title and material sold.⁶⁴

As to title, this representation is in the nature of a warranty, and includes the legal facts regarding ownership and claims in the case of movables and the boundaries, dimensions, provisions, charges, and burdens in the case of immovables; but the vendor of a piece of land does not vouch that it is free from taxes and other public burdens which are not proper for entry in the land register. This general warranty of title does imply, however, that the thing is sold free of the rights of others. An agreement excluding these representations is inoperative where the vendor conceals a defect.⁶⁵

In the sale of a right, warranty of title extends also to the fact of the existence of that right; in the sale of a negotiable instrument, the warranty implies that no application has been made for the canceling of the instrument.⁶⁶

As to essential quality, in the sale of merchandise the warranty implies that the material is not subject to defects which diminish its value or fitness for ordinary use or the use assumed in the contract. Where goods are sold according to sample, the quality of the merchandise delivered must be the same as the sample. There is a similar warranty where merchandise is sold by test and approval, whereby the merchandise delivered must have the same quality as the merchandise tested and approved. This same warranty of essential quality extends to the sale of merchandise generically defined, to the effect that the vendor must deliver merchandise of the promised description and average kind and quality. In commercial sales, such merchandise must be of the average mercantile kind and quality.⁶⁷

In the sale of merchandise by measurement, weight, for delivery within a certain time, or for definite currency, the provisions must be interpreted in accordance with the custom of the place where the agreement is to be performed. Where the sale is by public auction, there is no warranty of the essential quality of the merchandise if it is stated at the time that the vendor is selling as a pledgee or mortgagee.⁶⁸ It is to be remembered that accessories do not go with articles sold; only component parts and fruits and profits go. (See distinction under "Things", pp. 71 and 72.)

A sale is voidable for the breach of either the warranty of title or the warranty of essential quality, unless the defect is inconsiderable, or unless the buyer knows of the facts or except but for gross negligence he could have discovered them, and a vendor denying the presence of such a defect forces the purchaser to prove same.⁶⁹

⁶⁴ B.G.B. 444.
⁶⁵ R.G.B. 434, 436, 441, 468, 476.
⁶⁶ B.G.B. 437.

⁶⁷ B.G.B. 243, 345, 360, 459, 494.
⁶⁸ H.G.B. 345, 361; B.G.B. 461.
⁶⁹ B.G.B. 439, 442, 459, 460, 468.

REMEDIES OF THE PURCHASER

If a seller defaults in delivery, he is liable for nonperformance and can be forced to perform. A contract impossible of performance on both sides is void, but a person entering into a contract providing for an impossible performance which he knows to be so is liable in damages for the injury to the other party due to his relying upon the validity of the contract. The other party cannot claim compensation, however, if he also knows of the impossibility of performance. If a contract is only partially impossible of performance, it is valid as to those parts which can be performed; and as to those parts, a claim for specific performance will be enforceable. If a party enters into a contract impossible of performance and in so doing guarantees performance, he is liable under his guaranty. If a party enters into a contract which subsequently becomes impossible of performance, he is relieved therefrom but must pay damages. If the impossibility, however, is of an impermanent nature and can be removed, performance can subsequently be enforced.¹

Inspection and rejection.—An obligation is strictly impressed upon merchants in mercantile transactions to inspect merchandise delivered to them under a sale as soon as possible and to reject same promptly, with notice to the vendor, if rejection is necessary. The merchant must carry out this duty within a reasonable time, otherwise the contract is held to be completed. On rejection and notice the vendor must return the purchase price, together with interest thereon, take back the articles purchased, and pay all the expenses incurred by the purchaser and all costs in connection with the contract. The buyer must return the merchandise and pay a fee for its use and enjoyment if it has been used by him and any emoluments received by him for its use.²

If a seller delivers a thing with a defect in the title, which is subsequently discovered, he must remove the defect; and where this is impossible or refused, the buyer may rescind the contract and sue for damages and a penalty. For a defect in essential quality, a buyer may rescind a contract or demand a reduction of the purchase price, or, if paid for, claim damages for nonfulfillment. Claims for such defects are limited to 6 months after discovery, unless extended by agreement.³

Where merchandise designated only by species is sold, the purchaser may demand, instead of rescission or reduction, that a perfect article be delivered. A sale on probation, test, or approval leaves the approval unquestionably to the buyer, who must exercise his right of inspection and rejection within the time fixed under the contract or, if no time be fixed, within a time reasonable under the circumstances. The matter of reasonableness must be proven by the purchaser.⁴

If upon inspection a buyer discovers that a part of the merchandise delivered is defective, he may insist that the contract be canceled as to that part, provided it is inconsiderable and can be separated without disadvantage to the purchaser, and the price must be propor-

¹ B.G.B. 275-280, 306-308.

² B.G.B. 346-347, 467; H.G.B. 343-344, 377.

³ B.G.B. 462-463, 465, 480; Z.P.O. 894.

⁴ B.G.B. 495-496.

tionally reduced. If the defective part is unseverable, the purchaser may cancel the entire contract; but he cannot do so if he uses the merchandise delivered for a time or if he sells, changes, or alters any part thereof. A defective article delivered, however, can be retained by the purchaser, and a claim for damages for defect will be good provided he has notified his seller of the defect or reserved his rights upon acceptance. In such a case, however, the purchaser must elect the remedy he will pursue and is bound to the relief he chooses.⁵

When merchandise which cannot be described under a determined quality known in the trade or is not in existence at a certain place is sold, the purchaser will be entitled to examine the merchandise and to rescind the contract if the merchandise should not be satisfactory.

If in a contract in which time is of the essence performance is not made within the time specified, the purchaser may either claim performance and compensation for the delay or may rescind the agreement.⁶

A vendor is not liable for a defect in merchandise delivered if the vendee knew or should have known of it, unless the buyer accept with reservations, or if the article was sold at public auction.⁷

In any case in which a contract is not performed, the purchaser's costs must be refunded.⁸

REMEDIES OF THE SELLER

Coupled with the duty of a merchant promptly to inspect merchandise delivered to him is his duty to accept satisfactory merchandise. The vendee may relieve himself of the obligation for the completion of a contract only if upon delivery he reserve his rights as to any defects which appear therein.⁹

Where a purchaser refuses without just cause to accept merchandise, the vendor may claim performance of the agreement and compensation for the delay, or he may rescind the agreement if it is not to his advantage to enforce it. When the vendor claims performance, he may store the goods at the vendee's expense or sell them for the vendee's account upon compliance with the prescribed procedure.¹⁰

INSTALLMENT SALES

Installment selling (*Abzahlungsgeschaeft*) is very common in Germany in spite of the fact that there is little direct legal provision for the protection of the parties. The German law on this subject has no exact counterpart in English or American law. The closest analogy is the law with regard to "hire-purchase" contracts. Such a sale under German law is considered as a hiring and is governed to some extent by the rules of hiring, to which is added a provision for the passing of title upon final payment. Final payment is not considered to be made by the mere acceptance of drafts or the issuance of notes but only upon satisfaction.¹¹

The protection afforded in America by the registration of a lien against the property, thereby giving notice to third parties and protection against their rights, is not provided in Germany. There are no registers in which such transactions may be recorded; but there is

⁵ R.G.E. 249, 352, 362, 469-473.
⁶ H.G.B. 370.
⁷ B.G.B. 460-461, 464, 480.

⁸ B.G.B. 467.
⁹ B.G.B. 464.
¹⁰ H.G.B. 372-374, 379.

¹¹ B.G.B. 364, 455.

also no doctrine of estoppel working against the rightful owner of property and limiting him from exercising his rights of ownership against third parties (except as hereinafter appears), and it is allowable to bring both a civil and a criminal proceeding against the vendee, who is chargeable with embezzlement if he sell the merchandise or take it out of the country.

The seller of merchandise on installments may trace and recover his property from a third party unless the latter be an innocent purchaser for value. Where the vendee has mortgaged to an innocent third party property obtained by him through an installment sale, such third party also obtains a contractual possessory lien which is good against the original owner. Where a machine sold on installments is so placed in a factory that under the law it becomes attached to the realty, the installment owner loses his right to recovery of the machine, but recent decisions of the Reichsgericht seem to tend toward allowing an ownership reservation in the installment vendor.¹²

A third party having a claim against the vendee under an installment contract may seize the merchandise by attachment or enforce his claim by a judicial decision, but in such case the original owner may move to set aside any attempt to enforce the lien or judgment. However, where the installment seller is not advised of the seizure and the merchandise is sold at public auction, a bona fide purchaser at such sale will acquire good title as against the original owner.¹³

An installment vendor may not demand the return of his merchandise merely because the financial condition of his vendee has suffered or is weak or endangered. He can, however, obtain redress in the event of default in the payment of installments.

Where the installment vendee is a *merchant registered in the Handelsregister*, the vendor (a) may demand the payment due or the whole balance if it is agreed that the whole balance shall become due and payable in case of default, or (b) he may reclaim the merchandise and still demand payment of the balance, but in the meantime withhold delivery of the merchandise until paid;¹⁴ or (c) he may rescind the contract immediately and demand the merchandise, and, if there is no provision in the contract giving the purchaser the right to demand the return of installments, he can repossess the merchandise without repaying the installments except in the case of extreme injustice.

Where the installment vendee is *not a registered merchant*, the vendor cannot demand any further installments if he repossess or demand the return of the merchandise. The contract will be considered rescinded and both parties must return that which they have received. In other words, the vendor must refund all payments made by the vendee, with interest thereon, anything to the contrary in the contract notwithstanding; and the vendee must pay for the use of the merchandise and all expenses incurred by the vendor in connection with the transaction, as well as depreciation and deteri-

¹² B.G.B. 932-935, 946, 1207.

¹³ Z.P.O. 771, 808, 814, 930; B.G.B. 1235, 1244.

¹⁴ Where the buyer does not return the merchandise voluntarily or there is danger that it will disappear, the vendor may obtain an injunction ordering the removal of the merchandise to his custody or to a warehouse for safekeeping until right of ownership and possession is determined by the court.

oration directly attributable to the vendee.¹⁵ For accidental deterioration, destruction, or loss of the merchandise the vendee is not liable.

Where the installment vendee becomes bankrupt, the installment vendor's property does not become merged with the estate, and he can, upon application and proof, claim it and obtain its return unless the administrator of the bankrupt estate wishes to continue with the installment contract and pays the installments as they fall due. In all cases of bankruptcy of an installment vendee, notice of his claim of ownership in and to the property should be given at once by the vendor, so that the possibility of its being merged with the bankrupt estate or its sale to an innocent third party will be avoided. Where the installment vendor's merchandise has been sold by the bankrupt, he is also entitled to the money received therefor unless the money itself has been mixed or intermingled with the bankrupt estate.

SUGGESTED PROVISIONS FOR INSTALLMENT CONTRACTS

In making a contract for sale on installments in Germany, it is suggested that the contract provide, among other things:

(a) That the vendee give immediate notice to the vendor of any attempt to take the vendor's property from his possession;

(b) That acceptance of drafts or the issuance of notes shall not be construed as payment;

(c) That where machinery is to be installed in a factory the consent of the owner of the real estate be obtained to the legal separation of the machinery from the real property;

(d) That whenever possible, a sign be permanently affixed and conspicuously displayed upon the machinery (and other objects which retain their original form, such as radio cabinets, and furnishings generally) sold, giving notice to third parties that title thereto remains in the installment vendor;

(e) That in the event of destruction or deterioration or the loss of the merchandise whether through the fault of the installment vendee or otherwise, the responsibility therefor is upon the vendee;

(f) That the entire balance of the installments due becomes immediately payable upon default in any one of them; and

(g) That installment payments shall not be returned upon default and repossession of the merchandise.

CONSIGNMENT SALES

The German law relating to consignment sales (*Konsignationsgeschaeft*) has a limited similarity to that governing installment sales, in that both transactions involve the giving of possession out of the hands of the rightful owner to another.

German law protects the innocent purchaser for value, as it implies from possession of an object an unlimited right of disposition. An innocent purchaser for value from a consignee (just as from a vendee in the case of an installment sale) acquires good title in the goods purchased and paid for by him, even though the sale to him be contrary to the instructions of the consignor; and an innocent pledgee of such merchandise acquires a good pledge lien thereon.¹⁶

¹⁵ B.G.B. 346-347, 989.

¹⁶ B.G.B. 932-933; H.G.B. 366.

A consignee acts as a trustee for his consignor and must protect the interests of the latter even though his own interests suffer. He occupies the position of a commission merchant, and the duties, obligations, and rights of a commission merchant govern his relations with his consignor. (See "Commission merchants", pp. 123 to 134.)

A consignee must provide for the custody and safekeeping of the merchandise intrusted to his care, and he is responsible for the loss or damage thereof; he must examine and inspect the merchandise delivered, and if the goods arrive in a defective condition due to faulty carriage he must make proper protest to the carrier and notify his principal. He must also notify his principal if the goods deteriorate while in his keeping and, if necessary, sell them quickly to avert losses. He must keep his consignor informed of the possibility of sale and immediately upon sale advise thereof, stating all the details and especially the party to whom the merchandise is sold, and if he fails to name the purchaser he becomes personally liable.¹⁷ He must turn over the entire proceeds of the sale to his consignor.

The consignee as a commission merchant usually conducts a business in his own name; and he may also conduct his consignor's business in his own name, but always for the account of his consignor and in accordance with his consignor's instructions. He is responsible both to his consignor and to all third-party purchasers. Where the consignee conducts the business in his own name, the consignor can assert against the purchaser direct claims resulting from the sale, but only after they have been ceded or assigned to him by the consignee.¹⁸

Where the consignee deviates from his principal's instructions, he does so at his own risk.¹⁹ If he gives credit without authority, he must immediately pay the consignor (who need not wait until a loss results therefrom) unless the transaction is consummated at a place where it is customary to grant credit, and even then he cannot allow credit where he is specifically instructed not to do so.

Where a consignee becomes bankrupt before the sale of the consignor's merchandise or, if sold, before payment therefor, the consignor is entitled to have his claim against the bankrupt estate severed from the general bankruptcy and can claim, trace, and recover his goods remaining in the hands of the bankrupt and even the proceeds from merchandise sold by the bankrupt if they have not yet been commingled with the assets of the bankrupt. As a matter of fact, the consignor has a prior claim to anyone at any time except insofar as his merchandise is impressed with a lien of the forwarder, warehouseman, or carrier for services in connection therewith.

SUGGESTED PROVISIONS FOR CONSIGNMENT CONTRACTS

A foreign shipper to Germany should provide in his consignment contracts that the merchandise shall remain his property and be sold only for his account and that it shall not be mixed with merchandise of the consignee or any other property. He should also limit the consignee to deliver his merchandise only upon payment.

¹⁷ B.G.B. 324, 688-700; H.G.B. 434.
¹⁸ H.G.B. 392.

¹⁹ H.G.B. 393.

The similarity between consignment sales and installment sales makes applicable to consignment contracts certain of the provisions suggested for installment contracts on page 111.

ASSIGNMENT AND TRANSFER OF RIGHTS AND CLAIMS

Under German law all rights, present or future, are assignable, except (a) claims for wages or maintenance, military officers' claims for pay or pension up to a certain amount, and claims for payment out of sick funds or funds created under the laws of compulsory insurance (e.g., claims exempt from attachment by a judgment creditor), (b) rights which by agreement between the parties shall not be assigned, and (c) obligatory rights which would be altered in character if exercised by a person other than the original party.²⁰

The rules for the transfer of rights are the same as the rules for the transfer of claims.²¹

REQUISITES

Such assignments and transfers require no writing except in the case of the transfer of a mortgage debt or a draft; but the assignor must, at any time, on request and at the cost of the assignee, deliver to him a publicly certified written document and all the information necessary for the enforcement of the claim, together with all the instruments in his possession required in proof thereof. All security for the debt and the rights of priority therein pass to the assignee unless specifically excluded. In the case of mortgage debts (except security mortgages), the assignment of the security cannot be excluded from the assignment of the mortgage.²²

No notice of the assignment is necessary, and from the execution thereof the new creditor takes the place of the old. Between the debtor and the assignee, however, discharge by payment or performance to the assignor, or the making of an agreement between the debtor and the assignor, or the taking of a judgment by the assignor against the debtor, is binding, provided the debtor was not aware of the assignment. A debtor may demand written notice of assignment before performance for the benefit of an assignee. If the debtor has notice, neither the assignee nor the assignor can subsequently deny or withdraw it without the consent of the other.²³

It is possible in Germany to assign a claim in order to bring suit thereon. This may always be done by foreigners who wish to avoid the necessity for depositing security for costs. When such assignments are made they must be duly authenticated.

Special rules are applicable to assignments of rights in and to negotiable instruments. The transferee of a negotiable instrument may be in a better position than the assignee of an ordinary claim; the latter takes subject to all defenses available against his assignor, while the former usually can only be met by defenses as to the validity of the instrument and those available in set-off to the maker against the holder. The endorsement of a negotiable instrument accompanied by delivery transfers all the rights to the endorsee.

²⁰ R.G. vol. 55, p. 334; Z.P.O. 850; B.G.B. 399-400.
²¹ B.G.B. 413.
²² B.G.B. 401-403, 792, 1153-1154, 1190.
²³ B.G.B. 398, 407-411.

The debtor need not perform unless the instrument is delivered over to him received.²⁴

DEFENSES AVAILABLE TO THE DEBTOR

All defenses and set-offs available at the time of the assignment against the assignor are good against the assignee (except on negotiable instruments). No claim, however, acquired by the debtor against the original creditor after the assignment or which becomes due after the assignment, can be set off. The debtor's performances to his original creditor can, in the absence of a notice or knowledge of the assignment, also be set up as defenses.²⁵

If a debtor has executed an instrument acknowledging a debt, he cannot assert against an assignee of such instrument that the debt was nonexistent, or that there was an additional agreement to the effect that an assignment thereof could not be made, unless the assignee at the time he obtained such assignment knew or should have known that such were the facts.²⁶

ASSUMPTION OF LIABILITY

The German law treats the assumption of a liability (*Schulduebernahme*) in the same way as an assignment of a claim, subject, however, to the requirement of creditor's assent. A debt can be assumed by a third party by agreement with the creditor, the former taking the place of the debtor; or the debt may be assumed by the third party by agreement with the debtor, but to relieve the original debtor the creditor must assent when he is notified. In the latter case, the debtor or the third party may, before the assent or refusal of the creditor, modify or rescind the agreement, but unless rescinded it is operative as between them, even without the creditor's assent.²⁷

Upon acceptance of the new debtor by the creditor the former may avail himself of all the defenses of the original debtor, but he cannot credit himself with a claim belonging to the original debtor.²⁸

Where a debt is assumed with the consent of the creditor, the bonds and pledges given for the original debt are extinguished, unless the one to whom the pledged things belong authorizes the assumption of the debt by the new debtor.²⁹

Where one takes over all the property of another, he becomes jointly liable for the debts as well, but only to the extent of the value of the property taken over. His liability therefor cannot be excluded or otherwise limited.³⁰

Where a mercantile business is acquired and continued under the old firm name, the new owner becomes liable for the obligations incurred by the former owner in connection with the conduct of the business, any agreement to the contrary notwithstanding as against a third party, unless notice is given to such third party or registered in the mercantile register and published in the prescribed manner. Where, however, the old firm name is dropped, the new owner is not liable unless there is public notice to that effect or there are other grounds for imposing the liability on such new owner.³¹

²⁴ B.G.B. 796-800; H.G.B. 364-365.
²⁵ B.G.B. 404, 406-407.
²⁶ B.G.B. 405.

²⁷ B.G.B. 414-415.
²⁸ B.G.B. 417.

²⁹ R.G.R. 419.
³⁰ H.G.B. 25.

SURETYSHIP

An agreement of suretyship (*Buergschaft*) binds the surety to the creditor of another to answer for his performance and may be for a future or contingent liability as well as for a present unconditional one.³²

A written declaration of suretyship signed by the surety himself is necessary in order that the transaction may be valid. If the surety perform the obligation contracted although there be no written contract therefor, performance cures this defect. An instruction, however, to give credit in a *mercantile* transaction is good even though not in writing. A security given by way of pledge is not a surety contract and requires no special form and no written contract to be valid.³³

LIABILITY OF THE SURETY

The condition of the principal debt at the time the contract of surety is made determines the extent of the surety's liability. A surety is liable to the same extent (but not primarily, except in certain cases) as the principal debtor and for any increases in the debt arising from default, delay, or unlawful act of the debtor, but any enlargement of the debt due to extraordinary legal proceedings on the part of the creditor against the debtor is not included in the original surety contract. Under no circumstances is the surety liable for any change from the debtor's original liability at the date of his guaranty. He is also not liable for the full amount where he limits this liability to the assumption of only a part of the debt or to a fixed maximum or where he has given a continuous guaranty to secure a fixed maximum. He is also not liable to the full amount where he becomes a surety for a certain definite time, in which case he can be held as such surety only for the time specified unless the creditor in the meantime brings suit against the debtor and advises the surety that he will seek to hold him also.³⁴

Several sureties to the same obligation become joint debtors even though they did not assume the contract of surety jointly.³⁵

A creditor who surrenders any lien or pledge or assignment or claim against a surety which the original debtor or another gave to him as further security for the performance of his contract frees the surety thereby and to the value of the thing surrendered.³⁶

DEFENSES OF THE SURETY

A surety can use all the defenses, avoidances, and set-offs of the original debtor to defeat the claim, even if the original debtor declines to avail himself of such defenses; but he is liable to the same extent as the debtor and must pay the costs of notice and suit of the creditor against the original debtor. The creditor, however, must exhaust his remedies against the debtor and against all the properties and pledges given to secure the debt before proceeding against the surety unless (a) the surety is a mercantile trader and the guaranty is a mercantile transaction on his part, (b) the surety has agreed to become a principal debtor, (c) the difficulty of taking judicial

■ B.G.B. 765.
 ■ R.G.B. 126, 766; H.G.B. 350-351.
 ■ B.G.H. 367, 767-777.

■ B.G.B. 769, 774.
 ■ B.G.B. 776.

proceedings against the principal debtor has been increased by the debtor moving his domicile or business after the date of guaranty, or (*d*) in the event of bankruptcy of the debtor or if it is seen that enforcement of a judgment against him will not be productive.³⁷

REMEDIES OF THE SURETY

A surety may demand his release (*a*) where the financial condition of the principal debtor has materially deteriorated, (*b*) where a change in the debtor's arrangements makes judicial procedure to recover more difficult, (*c*) where the debtor has not performed his promise for which the security was given although already past due, or (*d*) where the creditor has obtained judgment against the surety on the contract. The release, however, need not be obtained by the debtor on demand if he give adequate surety to the surety therefor.³⁸

A surety who satisfies the rights of a creditor against the original debtor obtains those rights himself against such debtor, together with any pledge or documents connected therewith. Where there are cosureties (who are always liable as joint debtors), any one of them satisfying the claims of the creditor not only obtains the creditor's right against the debtor but may also proceed against the other cosureties, and he may even collect from the other cosureties any deficiencies or share of any cosurety not paid.³⁹

³⁷ B.G.B. 767-768, 770-771, 773; H.G.B. 349.

³⁸ B.G.B. 775.

³⁹ B.G.B. 401, 412, 421-426, 774.

VL AGENCY

The law of agency¹ is one of the most important and yet most difficult topics for presentation in any discussion of trading under the laws of a foreign country.

Where it is a question of an American firm doing business in Germany, for example, the rights and obligations of three types of agents to each other and to the principals they represent must be defined:

(a) The American representative of the American firm who goes to Germany to do business there under a power of attorney;

(b) The German representative who is authorized to do business as the German agent of the American firm with German commercial organizations or their representatives; and

(c) The German representative of the German firm who is authorized to do business for his firm with the American business organization or its accredited representative.

The rights and liabilities assumed by the American firm for the acts of its American representative in Germany acting under a power of attorney are governed by the laws of the State in which it has its principal place of business; but German courts will not take judicial notice of the foreign law, but will construe the agency relationship according to German law, unless the foreign litigant adduces proof as to what the foreign law is. The acts of the American firm's German agent (usually a commission merchant) and the rights and liabilities assumed by the German firm for the acts of its German agent in dealing with the American firm are governed by German law. It is therefore just as necessary to know the German law concerning all types of agents with whom one may deal in Germany as it is to know the American law on the subject.

GENERAL OBSERVATIONS

When agency relationships arise in Germany, they may be determined either according to the rules of the Civil Code for all matters not strictly commercial or under the Commercial Code for commercial transactions. Even when they are governed by the latter, if its provisions do not cover a specific situation the basic law of agency in the Civil Code applies. It is therefore important that the distinction made throughout all German law (except bankruptcy) between transactions commercial and noncommercial be kept clearly in mind in the study of any question of agency, to ascertain what law is applicable thereto.

An agency depends for its validity upon the existence of the right in the principal to deal in the object for which the agency is constituted and the right of the agent to act for the principal. Where

¹ Firms engaged in foreign trade should observe great caution in the use of the word "agent" or "agency" in referring to their representatives in other countries. Where the term is loosely employed to designate a distributor or independent dealer handling the firm's products abroad, foreign tax officials often interpret use of the term as conclusive of the existence of the agency relationship and govern their charges accordingly.

the principal attempts to make a disposition without power to do so, such arrangement cannot be made operative without the assent of the person with the right to make such disposition. Where the agent acts without authority or contrary to instructions, unless his authority may be implied his contract is void as to his principal in the absence of ratification by the latter. Where the agent acts within his authority, however, there can be no claim against him unless he is guilty of fraudulent misrepresentation. Knowledge of the principal is imputed to the agent, however, in all transactions. The power of agency remains in force until the purpose for which it was created is fulfilled or until it is extinguished by notice of termination to all parties. A minor over 7 years of age may act as an agent.²

All employees, whether they have power of procuration or mercantile power of agency or act as mercantile agents, as well as primary agents (directors of a share company and managers of limited-liability companies) are restricted in their business transactions and impliedly considered to be acting solely for the benefit of their employer, especially where the transactions involve the same kind of business as that in which they are employed. They are not allowed to do any business similar in nature to that of their own employer, in their own name or for their own benefit or in the name or for the benefit of any third party; and if they do such business without their employer's consent, he may claim damages or take over the business for himself or claim the benefits therefrom derived.³

CREATION OF AGENCY

Agents may be appointed either expressly, in writing or orally, or impliedly. The only cases where the agency relationship must be created by a written instrument are those in which the acts of the agent involve the execution of formal agreements in writing (see "Contracts," p. 75), appearances in the German courts for the principal, and where the powers and actions of the agent must be authenticated in connection with registrations in German public registries. It is advisable, however, for any American firm which contemplates "doing business" in Germany through an agent to supply him with a power of attorney, if for no other reason than to limit his authority thereunder.

The relationship of agency may also be created by legal implication. In such cases it is always (except in the last instance hereinafter mentioned) a commercial agency. Such agencies are: (a) Statutory agency (appointed to act for a person under legal incapacity); (b) agency for a corporation or aggregation other than a natural person (procurist); (c) members of a partnership, managers of a limited-liability company, or directors of a share company; (d) confidential employees; (e) mercantile employees and mercantile agents; (f) wife for a husband and parental agency.⁴ Because the power

² B.G.B. 115, 166, 168. (For a list of the abbreviations used in footnotes throughout this monograph see p. xli.)

³ H.G.B. 60-61. Attention must also be called to the use of the terms "agent", "representative", "commission merchant", and "broker" throughout this entire discussion. Distinction must be made between these terms in accordance with the definitions of each of them given herein, to avoid mistake in the law applicable to each relationship.

⁴ B.G.B. 1357, 1626-1628.

of agency in each of these cases is created by implication, the law protects the parties in such relationships by limiting and carefully defining the rights and liabilities thereunder, especially with regard to third parties.

The different types of agency may also be classed according to the conduct of the agent in representing his principal (*a*) by acting in the principal's name (as in the case of employees, partners, and directors) or (*b*) by acting in the name of the agent himself but always revealing the principal for whom he is acting. The latter type of agency is usually where the agent is engaged in his own business as an independent merchant, in which case he is also subject to all the duties of a mercantile trader, and the business transacted by him for his principal is essentially of the type out of which the agent obtains his livelihood; for example, in the case of a commission merchant, a broker, or a forwarder or carrier.

It must be clearly indicated at this point that in German law *there is no such doctrine as the doctrine of undisclosed principal*. In other words, it is impossible for any person or firm to work as agent for another without revealing the agency; and where such a transaction is attempted, the agent will be held to be acting only for himself, and his principal will not be bound by his action. The intention of an agent to contract for another, if not made manifest, will under no condition be taken into consideration.

GERMAN AGENTS ACTING FOR GERMAN FIRM

MANDATARY

There are certain relationships of agency created by act or declaration of the parties. When a principal seeks a specific act of a friend and when the transaction is to be conducted by one not engaged in that particular type of business for profit are instances of this type of agency. Such an agency, even though it be between mercantile traders, is not necessarily commercial and, if not, will be governed by the rules of the Civil Code,⁵ and remuneration is not implied. Ordinarily, however, agency agreements between merchants or even between a merchant and a nonmerchant are commercial; and, where commercial, remuneration is implied. Especially is this true where, from the nature of the transaction and the parties, custom would generally presume compensation.

Such noncommercial agency is called a mandate (*Auftrag*). A mandate may be express or implied and therefore naturally requires no writing. Such agency can be accepted formally, or by an act of the agent in its execution, or even by silence. It can be rejected by the agent only by positive act or declaration.

OBLIGATIONS OF MANDATARY AND PRINCIPAL

If the mandatory accept, he is thereafter to perform himself and is not allowed to delegate to another without express permission; and he is responsible for all losses sustained by the principal by reason of his nonexecution of the mandate. He is also liable for willful default and negligence in the same manner and to the same extent as a paid agent. He is obliged to carry out the instructions of his

⁵ B.G.B. 662-676.

principal without deviation except in certain carefully defined circumstances and to confine himself within the limits of the powers conferred. He must keep his principal informed as to the status and progress of the business in hand and immediately report when the mandate is executed, render an account of his transactions, and turn over to his principal whatever rights and benefits are received. He must even pay interest on moneys received under the mandate if he uses them.⁶

The acts of the mandatary done for the principal in accordance with instructions and within the limits of his powers must be accepted by the principal; and the principal is responsible therefor and must carry out the obligations assumed, even though they be done in the name of the mandatary. The principal must compensate the mandatary for all proper expenses in connection with the exercise of his duties, with interest thereon, or even advance sums therefor.⁷ He must also indemnify the mandatary for losses suffered in the discharge of the mandate.

TERMINATION OF RELATIONSHIP

The mandate is terminated at the successful conclusion of the business or upon expiration of the term fixed. It can also be revoked at any time by either party for cogent reasons, but otherwise it continues until revoked with notice. Usually it is extinguished by the death or incapacity of either party, but must be continued by the mandatary on the death of his principal if delay in the completion of the transaction will be occasioned by the appointment of a substitute.⁸

PROCURIST

Under German law a person who has legal capacity to engage in business in his own name may be appointed to administer an entire business or a part of a business or a branch of a business for a mercantile trader, either by himself or with another. Such an appointment can be conferred only by the owner of a mercantile business or his statutory agent; in a company, only by the directors (Vorstand) or managers (Geschaeftsfuehrer); and in a partnership, only by consent of all with authority to represent the partnership. It can only be done by means of an express declaration communicated to the person on whom it is conferred or to a third party, or by public announcement, or by registration in the mercantile register.⁹

The duty of mercantile traders to give formal notice to the world through registration and publication of their general commercial acts extends to and includes the creation of the procurist relationship.¹⁰ The procurist so appointed must also furnish to the court where his appointment is registered a specimen signature of the trade name of his company, together with his own name, to be kept in the registry records for identification.

The power of procuracy may be conferred upon several persons at one time and by the same document, for an employee to act jointly with another employee or with a partner or director, and where so

⁶ B.G.B. 664-669.
⁷ B.G.B. 669-670.
⁸ B.G.B. 671-674.

⁹ H.G.B. 116, 232, 233, 320; B.G.B. 167, 170-171.
¹⁰ H.G.B. 53.

conferred such limitation must also be registered and the specimen signatures of all appointees furnished. Joint procurists must act jointly; but where one of several may act, it is sufficient if he act and the others refrain from repudiation. Notice to any one of them is notice to all.¹¹

SCOPE OF DUTIES

The necessity for the appointment of a procurist arises from the nature of the conduct of the business itself, especially if the business is a branch. Some trusted employee must be at the head to administer the affairs generally, to negotiate purchases and sales of merchandise, carry on transactions, and represent the firm to its customers and third parties generally, and the scope of the procurist's powers are inherent in his relationship and determined by the very nature of his position. He is empowered to act on behalf of his principal in judicial proceedings, civil and criminal, and other transactions that come within the scope of his particular mercantile employment. The only restriction imposed on him is that he may not alienate or charge land unless expressly authorized to do so. As a procurist, he does not become or have the right to act as an independent merchant, but always for the account of and on behalf of his principal. If he be a branch manager, he is empowered to act only for and in the interest of the branch, unless it is under the same firm name. If his employment with his principal is in but one of the principal's activities, he is authorized to act only in connection with transactions in that particular activity.¹²

The procurist must contract only in the name of his principal and sign in all transactions for the business in such way that the signature includes his own name and the firm name (together with some indication that he does so under proper authority and power). Transactions so entered into by him are binding on the firm, and the firm can enforce them directly against the party with whom the procurist has contracted. The procurist is released from all responsibility so long as he contracts within the scope of his power.

Even where the procurist does not state that he is transacting business for his principal or does not sign as required, contracts entered into by him (when they deal with commodities or transactions which pertain to the business of his employer) will be presumed to be made for the account of his principal, and the principal can sue directly to enforce the obligation therein and conversely will be bound thereon. The procurist may also be held personally liable on such contracts. In these cases the principal is deemed to have ratified and taken over the obligations under the contract unless, immediately upon being informed thereof, he expressly repudiates same by notice to the third party.

No restriction of the scope of the authority conferred by the power of procuration is operative against third parties except where a procurist abuses his power to the prejudice of his principal and the third party participates therein with knowledge, although as between the principal and the agent the power can be restricted by agreement in any manner and to any extent.¹³

A power of procuration is not transferable even with the consent of the principal.¹⁴

¹¹ H.G.B. 125, 232. ¹² H.G.B. 49-50. ¹³ H.G.B. 50; B.G.B. 138, 826. ¹⁴ H.G.B. 52.

TERMINATION OF RELATIONSHIP

The power of procuration is not extinguished by the death of the owner of the mercantile business by whom it was conferred, nor does it terminate if the principal becomes incompetent; but it does lapse if the business is discontinued or sold. It also terminates if a partner enters the business of a principal who previously had been the sole owner, or if a partner leaves a partnership of only two persons, or if the business goes into liquidation or bankruptcy.

The power of procuration is revocable at any time despite any term fixed in the agreement by which it was conferred, but the procurist has a claim for his losses or damage occasioned by the earlier termination of his original contract. Such power of revocation can be exerted in a partnership only by the partners who have authority to contract for the partnership and in a share company or limited-liability company only by those authorized to create the power.¹⁵

The termination or revocation of the power of procuration must be communicated to all third parties concerned. Where such notice has been communicated, the revocation is effective and valid, but such notice should be made in the same manner in which the creation of the power was communicated. Where the power is evidenced by a document, such document must be returned to the principal; or if it has been lost or mislaid or its return is refused, it must be declared inoperative by order of a competent court, and such declaration must be published.¹⁶

Contracts made by a procurist up to the communication of the notification of revocation to him or before he should have known that his powers were terminated will be considered to be legally made and within the scope of his authority. Third parties need only recognize the validity of the revocation of a power if they know or should have known of it, even if the lapse or termination has been registered.¹⁷

In all cases where a power of procuration lapses or is revoked, that fact must be formally registered in the mercantile register and notice published.¹⁸

EMPLOYEE WITH MERCANTILE POWER (AGENT-EMPLOYEE)¹⁹

A lesser and more limited power of agency is created for employees in a mercantile trade, where they are authorized to act in a restricted capacity and only in certain types of transactions for their employers.²⁰ Such lesser relationship of agency (*Handlungsvollmacht*) is conferred either by declaration or by implication of the law and is not registered. It may even include limited acts of management of a business, but is usually distinguished from a procuration in that the procurist is authorized to act in connection with transactions requiring his judgment, discretion, and general respon-

¹⁵ H.G.B. 52, 116.

¹⁶ B.G.B. 171-172.

¹⁷ B.G.B. 169-173, 674; H.G.B. 15.

¹⁸ H.G.B. 53.

¹⁹ For further discussion of the rules and regulations as to agent-employees see under "Contracts for services", pp. 81-83.

²⁰ H.G.B. 54-58.

sibility, whereas the employee with mercantile power of agency (agent-employee) is limited to technical and semiadministrative acts.

The Commercial Code²¹ itself limits the power of such agent-employee to the carrying on of mercantile business or particular transactions definitely within the scope of his duties. It further limits the agent-employee so that he does not have power to alienate real property, incur obligations in connection with bills of exchange, raise loans, or carry on legal proceedings unless specifically authorized to do so. Subject to the above limitations of their power, agent-employees are held forth to the world as having the general powers inherent in their position, and any further limitation is inoperative against third parties except insofar as this is known or ought to be known to them.

Commercial travelers enjoy this implied authority, which as to them includes (but only with reference to the merchandise they have dealt in) the right to collect amounts due and allow time for payment and to receive notices of defects in goods and declarations that goods are rejected and held at the disposal of the vendor and other similar declarations.²² They may arrange for alterations in contracts negotiated by them (other than extensions of time for payment, over which detail they have no authority), but only when such alterations are customary. Small discounts for cash, for instance, may be granted by them, but they are not permitted to grant substantial discounts nor to accept cancelations of orders.

Persons employed in the principal's establishment or public warehouses are also impliedly empowered to make sales and give receipts in the customary manner and to receive payment for the merchandise sold by them (except where cashiers are provided for that purpose and notices to that effect are conspicuously displayed).

The holder of a mercantile power of agency in conducting the business of his principal must always deal as an employee and for the account of his principal. In signing he must use his signature and the firm trade name, together with an expression indicating that he is acting under such mercantile power. He must never indicate that the power under which he signs is a power of procuration, nor so sign that his power may be confused therewith. Such mercantile power of agency may not be transferred without the consent of the owner of the business.²³

The mercantile power of agency is extinguished upon the termination of the employment, and notice thereof is necessary to free the principal from obligations contracted for him by such agent-employee after his discharge or the termination of his employment, especially as to third parties.

MERCANTILE AGENTS *

There are also certain other agents (*Handlungsagenten*) not employed in the principal's establishment who are permanently engaged to transact business for him either as intermediaries or in the principal's own name in connection with the trade or business conducted

* H.G.B. 54.

* H.G.B. 55.

* H.G.B. 57-58.

* For further discussion of the rules and regulations as to mercantile agents see under "Contracts for services", pp. 81-83.

by him. This contract of agency is a contract for services within the meaning of the Civil Code, and the rules governing the relations of master and servant generally apply.²⁵

With regard to mercantile agents there is no legal implication that they are empowered to contract for their principal. This is a question of fact. They are, however, impliedly empowered to receive offers and submit them to their employers; and where they do so, and the principal accepts the offer, he is bound to accept all the details arranged by the agent with the customer unless the customer knew or should have known that the principal did not agree to certain parts of such details.

When a mercantile agent makes a contract without authority, he only is liable and not the person whom he attempted to represent. Where the principal knows of the making of a contract by a mercantile agent without his authority he may ratify and make it operative for himself. Ratification is also implied where, knowing of the transaction, the merchant does not immediately repudiate it.²⁶

Distinction must be made between the salesman with mercantile power of agency (agent-employee) and a mercantile agent acting as a traveling representative. The latter has no implied power to fix the terms of a proposed contract or to change the terms of a contract already made, nor to receive payments, but only to refer such proposals. He can, however, just as can the agent-employee, receive notifications as to defects and similar matters.²⁷

REMUNERATION—TERMINATION OF RELATIONSHIP

If no other remuneration is fixed, the mercantile agent is entitled to the usual commission on the completion of every transaction effected through him or on accounts rendered at the end of every calendar half year, but where such transactions are sales he is paid only after receipt of payment therefor. The principal is not bound to conclude any contract negotiated for him by such agent unless refusal would offend against good faith and commercial morality; and where a sale fails because the principal refuses without substantial reasons, the agent is entitled to full commission. Where such agent is engaged for a district, he is also entitled to commission on all business transactions made in his district unless he was negligent in not obtaining them himself. He is not entitled to reimbursement for costs and expenses unless the agreement has so provided or this is the custom in the district where he acts; but he may collect extraordinary expenses. To enable the agent to check his commissions he is entitled to a copy of the portion of his principal's books which deal with his transactions.²⁸

The agency ceases at the end of the contract period. An agreement for an indefinite period may be terminated by either party on 6 weeks' notice, effective at the end of a calendar quarter; either party may terminate the agreement on shorter notice for cogent grounds. It is also terminated by the death of the agent and by the bankruptcy of the principal, without giving the agent a claim for

²⁵ H.G.B. 84; B.G.B. 611.

²⁶ B.G.B. 177, 179, 184; H.G.B. 85.

²⁷ H.G.B. 86.

²⁸ H.G.B. 88-89, 91; B.G.B. 157, 242; Z.P.O. 254.

earlier termination except for things done for the principal prior to bankruptcy. It is not ipso facto canceled, however, by the bankruptcy of the agent (which is a good reason for notice of termination) nor by the death of the principal, nor usually by transfer of the principal's business.²⁹

PARTNERS AS AGENTS *

In the case of a partner, German law distinguishes between the power of management and the power to represent the firm; but the duties and obligations in connection therewith are similar and seem to be powers in the nature of agency and therefore to be considered hereunder.

All partners are both entitled and bound to carry on the management of the firm business and to represent the firm with third parties, but any of them may be excluded from such right by the original partnership agreement. This power extends to all judicial proceedings and all other acts, including alienation and charging of land and the granting or revoking of the power of procuracy. Any limitation thereof is inoperative against third parties, but as between the partners the limitation upon their powers is operative when fixed by the partnership agreement or any resolutions made by the body of such partners.³¹

LIMITATION OF POWERS

Where it is stipulated in the partnership agreement that they are to conduct the business jointly, all must concur in any transaction binding the partnership, and they must comply with any binding instructions given by the body of the partners. Where either or any of the partners may represent the partnership, the request of one partner to another to abstain from a transaction for the firm likewise must be complied with. The partnership agreement may also provide that only certain partners are authorized to manage the business and represent the partnership with third parties; and where such partners alone are authorized, the request of the authorized partners, one to another, will obligate the partner receiving the request to comply therewith, but in this case the objection of the authorized partner must be specific and refer to a particular transaction.³²

The partnership contract may also provide that two or more of the partners shall always act jointly or that where one of the partners acts alone he must act in company with the holder of a power of procuracy.³³

A limited partner can under no circumstances be called upon to manage or represent the business of the partnership, nor can he object to the acts of the authorized partners in managing the business of the firm.³⁴

The exclusion of a partner from acting as manager or representative of the firm and the creation of the joint or collective agency

* H.G.B. §2; B.G.B. 613, 672-675; K.O. 23, 27.

• For additional discussion of this topic see under "Partnerships", pp. 14 and 18.

• H.G.B. 114, 125-126; B.G.B. 718-719.

• H.G.B. 115.

• H.G.B. 125.

• H.G.B. 164, 170.

for more than one partner to act or for a partner to act with a procurist must be entered by all the partners in the mercantile register.²⁵

The scope of the authority of any partner, as limited, to manage or represent the firm extends to all transactions incidental to the ordinary course of the business of the mercantile trade carried on by the partnership. Transactions outside such ordinary course require the assent of all the partners.²⁶

When any partner acts for the partnership he must, as any other agent, keep all the partners acquainted with what is being done and furnish any special information requested of him in connection with his duties. When a piece of work he is handling is concluded, he must promptly give an account thereof and turn over to the partnership whatever he receives.²⁷

TERMINATION OF RELATIONSHIP

The power of agency can be withdrawn for any partner by order of the court upon the application of the other partners if there are cogent grounds (such as gross neglect of duty or incapacity). Also a partner can himself withdraw from representing the firm for some satisfactory reason; but he may not withdraw at an unsuitable time, and he may never withdraw where the conduct of the partnership business is intrusted by the partnership agreement jointly to all of them. Notification to the partners and to all third parties with whom the withdrawing party has dealt is necessary to terminate the agency of the partner in any event.²⁸

The exclusion of a partner from power to act on behalf of the partnership or any change in the power of agency of a partner must be entered by all the partners in the mercantile register.²⁹

DIRECTORS AND MANAGERS AS AGENTS³⁰

In a German share company or limited-liability company, as in any other form of mercantile business not conducted by the sole owner, it is necessary that one or more persons be appointed by the aggregation of owners or, because of his or their position in the company, be impliedly given the right to represent the firm in its relations with third parties and to manage the business. Such persons—the directors (*Vorstand*)³¹ in a share company and the managers (*Geschaeftsfuehrer*) in a limited-liability company—are primary agents.³²

SCOPE AND MANNER OF REPRESENTATION

In the management and representation of the business the directors and managers must act, not as independent merchants, but as mere agents for the business they represent, and must contract for it and sign documents in a way to include their own names as well as

²⁵ H.G.B. 125.

²⁶ H.G.B. 118, 119.

²⁷ H.G.B. 666-667, 713.

²⁸ H.G.B. 127; H.G.B. 671, 712, 729.

²⁹ H.G.B. 125.

³⁰ For further discussion of this subject see the chapter dealing with share companies and limited-liability companies, at pp. 31, 35, 49, and 50.

³¹ But not the supervisors (*Aufsichtsrat*). Supervisors do not have this implied power of agency—except when acting temporarily as directors; see note 43, p. 127.

³² H.G.B. 231; G.m.b.H.G. 35.

the firm name of their company or the designation of the management. They are authorized and impliedly given the power to transact all judicial and extrajudicial business of the company—in other words, to conduct all affairs of their company as though they were the sole owners thereof—to which they must apply the diligence of careful business men; and if they commit a breach of duty they are jointly and severally liable for the damage.⁴³

They must, however, in the absence of provisions to the contrary in the memorandum of association, do all these acts jointly; but they may always, among themselves, authorize a particular director or manager to undertake a specific transaction or class of transactions. When the memorandum of association does not give each director or manager the right to act as agent for the company himself, it may provide that he act always with another director or manager or with an employee holding a power of procuration.⁴⁴

LIMITATION OF POWERS

The directors and managers obtain their authority by legal implication from their position, and as to third parties their implied powers cannot be limited in any respect because all directors and all managers are supposed to have like powers; but if any director or manager abuse his power to the prejudice of his company and the third person assist him in so doing, the implication of the power with regard to such third person ceases to be valid. The powers of directors and managers, however, may be limited among themselves and toward the firm by the memorandum of association and resolutions of the general meetings. Any notice to the company is good if made to any one of the directors or managers.⁴⁵

The appointment of a director⁴⁶ and every change in the composition of the directorate or management or in the powers of agency of the individual directors or managers must be entered in the mercantile register; and specimen signatures must be furnished the court.⁴⁷

The limitation on employees that they may not do business in their own name for their own benefit or the benefit of a third party without the consent of their employer applies likewise to directors and managers.⁴⁸

TERMINATION OF RELATIONSHIP

The appointment to the office of director or manager is subject to revocation at any time, provided always that the revocation does not affect the claim to remuneration under the original contract for services; and the agency power of the director or the manager lapses with his contract of employment, but notice thereof to third parties with whom he has dealt should be given. The memorandum of association may make removal dependent upon cogent reasons—for example, gross neglect or incompetence.⁴⁹

⁴³ H.G.B. 231, 233, 241, 272; G.m.b.H.G. 35, 43.

⁴⁴ H.G.B. 232; G.m.b.H.G. 35.

⁴⁵ H.G.B. 235; G.m.b.H.G. 37.

⁴⁶ A member of the board of supervisors (Aufsichtsrat) of a share company cannot be a director; but in an emergency the board may appoint one of its number for a definite and limited time to act as a director, during which period, however, he cannot act also as a supervisor (H.G.B. 248).

⁴⁷ H.G.B. 234; G.m.b.H.G. 39.

⁴⁸ H.G.B. 236.

⁴⁹ H.G.B. 231; B.G.B. 27; G.m.b.H.G. 38.

Other details as to termination of the power of agency of a director or a manager are similar to termination of the power of agency of other employees.

GERMAN AGENTS ACTING FOR GERMAN OR AMERICAN FIRM

COMMISSION MERCHANTS

A commission merchant (Kommissionaer)⁵⁰ is defined as one who in the regular course of his own trade undertakes to buy or sell goods or negotiable instruments in his own name for and according to the instructions of another. The rules governing commission merchants also apply to transactions other than the purchase and sale of goods and negotiable instruments if they are entered into by regular commission merchants and to the transactions of merchants in general when they transact business on the instructions of others. In the ordinary case the commission merchant receives the goods of his principal on consignment to dispose of them under the rules governing consignment sales, or he may conduct a purchase of merchandise for his principal; but he only takes charge of the goods for his principal, without ever obtaining right to disposition of the goods handled,⁵¹ except under the instructions of his principal.

Commission contracts must meet the usual requirements of contracts generally. Where a mercantile trader receives an offer of a commission from a party with whom he has a regular business connection or from whom he has solicited business, he must immediately refuse to undertake the commission or he will be deemed to have accepted it.⁵² Having accepted it, both the principal and the agent will be bound until the revocation of the agency or the completion of the transaction. A commission may also be accepted by implication when the commission merchant starts to act. Where a commission for the sale of merchandise together with instructions to purchase others with the proceeds is given, the commission merchant by accepting or acting with regard to the sale impliedly accepts with regard to the purchase as well, for both transactions will be considered as parts of one indivisible commission. If the commission merchant had desired to carry out only one of the transactions, he should have so stated to his principal, and his statement to that effect would then have become a new or counter offer to be accepted or rejected by the principal.

CONTRACTS OF COMMISSION MERCHANT IN OWN NAME

Acting as he does in his own name, the commission merchant must have the capacity to engage in commerce required of all merchants under the provisions of the Commercial Code, and must keep the required books of account and conform to the other obligations imposed on merchants generally. Where in special cases specifically agreed on he uses the name of his principal in the making of a contract and does not contract in his own name, he departs from the role

⁵⁰ A distinction must be made between a commission merchant and an ordinary agent who acts as such and receives a commission for his services. The latter is known as a commission agent. Similarity of designation should not confuse the two relationships. The laws of ordinary agency govern the commission agent.

⁵¹ H.G.B. 383, 406.

⁵² H.G.B. 362.

of commission merchant and becomes an ordinary agent, subject to the rules of law applicable to ordinary agents.

The duty of the commission merchant to contract for his principal in his own name raises a barrier between the principal and the third party which precludes the principal and the third party from having any rights direct against each other; but the commission merchant has rights direct against both of them and they have rights direct against him. Claims in transactions concluded by a commission merchant can be enforced by the principal only when they have been assigned to him by the agent.⁵³ Even before the assignment, however, such claims are considered vested in the principal as between him and the agent and the creditors of the agent.⁵⁴

As to *third parties* with whom he contracts for his principal, the commission merchant cannot relieve himself of the responsibility for the performance of the contract executed by him even though he disclosed his agency to the third party at the time of making the contract and has acted in accordance with the instructions of his principal. Because of the fact that he has acted and contracted in his own name (as he is obliged to do in his character of commission merchant) he alone, and not his principal, is liable.⁵⁵ If he is sued by the third party for performance, he may (but need not) assign all his rights against his principal to the third party or may serve his principal with a notice (*Streitverkuendung*)⁵⁶ that he has been sued and request him to come in and defend.⁵⁷ But in any event the commission merchant is still, and at all times after executing the contract in his own name, primarily liable for its performance.

To the *principal* for whom he contracts he is directly responsible on the contracts made for him only (a) if he contract not in accordance with his instructions, (b) if he expressly undertakes such responsibility or (c) if such responsibility is presumed from the custom of the place where he carries on his commission business, (d) if the third party has already performed under the contract to such commission merchant, or (e) if in his report of the conclusion of the transaction to the principal he does not name the third party with whom it has been concluded.⁵⁸

DUTIES OF COMMISSION MERCHANT

The commission merchant is charged with carrying out his commission with the diligence of a careful mercantile trader; he must safeguard his client's interests; follow his principal's instructions

⁵³ H.G.B. 392.

⁵⁴ The principal is entitled to expressly require that his claims for any rights acquired by the agent for him and the principal's merchandise consigned to the agent should be freed from charges of others and transferred to him where the creditors of the agent take his rights or his goods under execution or even where the trustee in bankruptcy of the agent attempts to bring them into the bankrupt estate (B.G.B. 771; K.O. 43-46).

⁵⁵ France, Mexico, and countries generally under civil or code law follow this law (except Chile and Colombia, where a commission merchant may be relieved of his responsibility if he reveal the name of his principal). (See Obregon, "Latin American Commercial Law", pp. 330-331; and Leon Lacour, "Précis de Droit Commercial", p. 623.)

⁵⁶ Z.P.O. 72-75.

⁵⁷ This is a remedy similar to interpleader granted in American law, whereby the equities of the parties may be determined in one suit without waiting for the judgment to be obtained by the third party against the commission merchant and then compelling him to sue his principal. The principal is not compelled, however, to come into the suit. The principal may himself demand this right (*Nebenintervention*) even if he is not served with notice (Z.P.O. 66-71).

⁵⁸ H.G.B. 384-385, 394. (b and c are *del credere* transactions.)

(except when to follow them would appear to be prejudicial to his principal's interest): supply his principal with all necessary information and especially inform him without delay upon the execution of any order given; render an account of every transaction; hand over everything received in connection therewith; and where he reports the execution of a transaction, he must name the third party with whom it has been concluded or himself be liable for its completion.⁶⁰

As a mercantile trader the law imposes a special duty on a commission merchant for the custody, preservation, and immediate examination and acceptance or rejection of merchandise intrusted to him by his principal or bought or otherwise received for his principal. He is responsible for loss or damage to such goods unless this could not have been averted by the care which an ordinary merchant would have exercised. (See "Bailments", p. 100.) When goods are received by a commission merchant in a damaged or defective condition apparent by outward appearance, he must safeguard all rights of his principal against the carrier of the goods by preserving the evidence of this condition upon delivery and inform his principal forthwith. Failure to do so renders him liable. If the goods are perishable or are affected subsequently, or if there is no time to obtain instructions of the principal as to disposal of the merchandise, or if the principal delays in giving or does not give any instructions with regard thereto, the commission merchant may sell the goods himself according to the rules for the sale as outlined in the Commercial Code.⁶¹

A commission merchant is liable for failure to insure goods only if his principal had instructed him to insure them.⁶²

Cash received by a commission merchant for the account of his principal is held subject to the merchant's risk until paid over, and if he use the moneys in the meantime he must pay interest. His duties as to the care, custody, safekeeping, and return of securities intrusted to him are outlined in the custody of securities act.⁶³ (See pp. 101 to 105 hereof.)

Where a principal has not given full instructions, or when instructions are delayed, or when such an agent has to deal with an unforeseen contingency, or where he is expressly authorized to do so, a commission merchant may, at his discretion, carry out a transaction according to his own best judgment without assuming any liability or subjecting himself to any claim therefor, provided only that he acts as a careful mercantile trader would have acted in the transaction if it had been his own and according to the accepted usages of commerce in similar cases.

ACTS NOT IN ACCORDANCE WITH INSTRUCTIONS

If a commission merchant does not deal in accordance with his instructions, he is liable in damages or the principal may refuse to let the transaction stand for his account; but the principal must, immediately upon receiving notice of the transaction, declare his intention to repudiate it, as otherwise he is deemed to have ratified the departure. Where the principal does not ratify the transaction,

⁶⁰ H.G.B. 259; H.G.B. 384.
⁶¹ H.G.B. 273, 277, 379, 388-391, 434.

⁶² H.G.B. 390.
⁶³ D.G. 3. 5. 11.

the commission merchant is personally liable to the third party thereupon and also to the principal for any damages resulting therefrom. If a commission merchant, buying for more or selling for less than instructed, offers to bear the difference, the principal may not repudiate the transaction; but if the commission merchant conclude a deal more favorably than instructed, this is not to be considered a deviation from his instructions, and the principal is entitled to all the accruing benefits, without being called upon to pay an extra commission or bonus.⁵³

Where the commission merchant acts fraudulently, the principal may impeach the contract and claim damages. If a commission merchant makes an advance or allows credit in connection with a transaction, he does so at his own risk and is liable for immediate payment to his principal unless the custom of the place where the transaction is concluded allows such credit; but he may allow no such credit if he has instructions to the contrary. In such cases, however, the principal may adopt the transaction and is thereafter not entitled to claim damages. The commission merchant, however, is not responsible for the performance of the contract by, nor for the solvency of, the third party with whom he deals except where he is guilty of negligence or fraud or where he has failed to name the third party.⁵⁴

COMMISSION MERCHANT AS THIRD PARTY

In the absence of instructions to the contrary, a commission merchant may sell to or buy from his principal goods which have a market price or securities which are quoted on a public exchange, if he fixes a favorable market price, which must not be less than that officially quoted. (He does not lose his claim for commission on such transactions.) Otherwise, he may not buy from nor sell to his principal without the principal's express consent. Where the commission merchant takes the contract for himself and by greater diligence could have made a more favorable deal, the principal is entitled to the most favorable price obtainable; and if the commission merchant, before he notifies his principal, sells the article so purchased at a greater price, he must pay that price to his principal.⁵⁵

A notification by the commission merchant of the execution of an order for his principal must expressly state that he constitutes himself the third party, if he does so; otherwise the transaction is presumed to be for the account of the principal with a third party, and any agreement to the contrary is void. Where a principal revokes his order and his commission merchant receives notice of the revocation before he sends off a notification of the execution of the order, the agent cannot constitute himself principal to carry out the transaction.⁵⁶

FEES AND EXPENSES

The business of a commission merchant being commercial and accepted for the purpose of gain, in the absence of agreement it is presumed that the principal will pay a fee for the services according to commercial custom and usage at the place where the commission

⁵³ H.G.B. 355-387.

⁵⁴ B.G.B. 123, 823; H.G.B. 385, 393-394.

⁵⁵ H.G.B. 400-401, 403.

⁵⁶ H.G.B. 405.

is to be performed. This presumption for the payment of a fee, however, will not be extended to a commission outside the scope of the commission agent's general business. Fees in such cases must be specifically provided for.

Fees are due when the business undertaken is carried out; or, even if it is not carried out, when the agent turns the prospect over to his principal, if payment is customary in his locality. He can also claim a fee where he brings the parties together and the business would have been carried out but for some obstacle interposed by the principal.⁶⁷

The commission merchant is also entitled to reimbursement for all expenses incurred in the performance of a commission which might be held necessary under the circumstances, but not for losses sustained unless they are attributable to the principal's fault.⁶⁸ He is even entitled to ask for advances to cover necessary expenses;⁶⁹ and he obtains a lien therefor on the goods in his possession or over which he has the power of disposal and also on payments due from third parties for the transactions in which he himself has acted.⁷⁰ The claim of the commission merchant under such lien must be paid in preference to the claim of every other creditor, after deduction of transportation and warehousing charges.

The lien of the commission merchant on the goods of his principal may be asserted at any time (even after bankruptcy) in order to relieve the consignee from the duty of returning the consigned merchandise until he has been paid all sums of money for which his lien attaches, but it only extends to the merchandise on consignment which still remains in the possession of the consignee or subject to his right of disposition.

The lien of the commission merchant, however, may be exercised by him only against the particular goods which are the subject of the transaction out of which his claim arose, and not with respect to other goods covered by other transactions, even though such other goods may also belong to the same principal.

MIXING OF CONSIGNED MERCHANDISE

There is a mercantile duty imposed upon all commission merchants upon the receipt of goods on consignment to so keep them that they may be distinguished from other goods, either by not removing marks already appearing upon them or by placing identifying marks thereon. This duty is especially impressed upon the consignee when he receives goods which are not easily identifiable in and of themselves but which can be mixed and sold from a general stock. In these cases he is under an additional duty not to mix the goods with the merchandise of any other person unless he is given the express right so to do or unless he is permitted to take title thereto himself.

This general duty of commission merchants not to mix consigned merchandise and to keep the merchandise delivered identifiable by

⁶⁷ H.G.B. 396.

⁶⁸ B.G.B. 276, 670, 675.

⁶⁹ B.G.B. 669, 675. The term "necessary expenses" covers reimbursement for warehouse costs, transportation, current accounts, advances and loans, and all proper liabilities assumed in connection with the transaction (H.G.B. 396).

⁷⁰ H.G.B. 397, 399.

markings is based upon the desirability of having traders keep the title to such merchandise deliveries clear, to avoid fraud and confusion and, generally, to enforce the rights of consignors upon consigned merchandise so that it may be disposed of only in accordance with their instructions, and, further, to enable owners, in the event of the bankruptcy of consignees, to trace and reclaim their own goods.

If the mercantile duty not to mix consigned merchandise or remove identifying signs therefrom has been carried out, such consigned goods in the hands of a commission merchant who becomes bankrupt may be easily identified. When so identified or when otherwise identifiable they are considered in law to belong to the principal and are traceable and recoverable by him upon payment of any lien charges thereupon. The German law, recognizing the doctrine of "stoppage in transitu", extends this right of lien where merchandise is being shipped. The party shipping will not lose his ownership in or lien upon the goods if they are still in transit, but he may instruct the shipper to hold them for his account or to redirect and return them to him. Where the commission merchant has sold consigned goods before the commencement of his bankruptcy or his trustee has done so after the commencement thereof, the consignor may claim an assignment of the right to the consideration still outstanding or out of the assets of the bankrupt insofar as such consideration has passed into the assets since the commencement of the bankruptcy. Otherwise the consignor may only pursue his claim as an ordinary creditor.¹¹

TERMINATION OF RELATIONSHIP

The commission merchant's agency is terminated (a) upon the successful conclusion of the transaction which was the object of the agency, (b) by the revocation thereof by either party at any time, or (c) by the bankruptcy of the principal; but the bankruptcy of the agent does not necessarily terminate the agency (although it is a good ground for such termination). The death of the principal or the fact that he has become incapacitated to conduct his own business does not necessarily terminate the agency, especially where the operation which constitutes the object of the agency is to be completed after that time and there is or may be a danger or risk that the deal may not be consummated because of delay in the appointment of a successor agent by the heirs of the deceased person or the statutory agent of the incompetent.

Generally the relation of the commission merchant and principal may be terminated at any time by notice of either party to the other; but such merchant may not, except for substantial reasons, give notice to terminate the agency at an improper time; and if he does so, he is liable in damages therefor. Notice of termination in any case must be given in order to free the parties from obligations thereunder.¹²

Where a commission merchant acts strictly in accordance with his agency rights and transacts business for his principal in his own name, notice of termination of such agency to third parties is not necessary. This is because the commission merchant contracts in

¹¹ K.O. 44-46.

¹² B.G.B. 627, 675.

his name and on his own responsibility and becomes directly liable to the party with whom he contracts. There is no implied power of agency in such contracts which is required to be terminated to avoid liability to third parties. Indeed, a third party, even though the agent represents that he is still acting for his principal, may neither proceed against the principal nor hope to prevail in a lawsuit against the principal for the enforcement of a contract after the assignment of the agent's claim to him, unless he can prove the authority of the agent and the fact that such authority has not been revoked. A contract of a third party with a commission merchant in his own name can, in all cases, bind the alleged principal of such commission merchant only in the event it can be proven that the commission merchant still has the power and authority unrevoked to act for such principal.

However, when the commission merchant, by express agreement or otherwise, merely acts as a general agent and contracts in the name of his principal, he is subject only to the rules governing an ordinary agent. Under such conditions he may bind his principal directly for his acts, in which case notice to the third party is necessary.

It may be generally said, therefore, with regard to termination of the commission agency, that it is always advisable to notify third parties with whom the agent might have dealt to safeguard the rights of the principal and free him from any claims that third parties may have arising out of the agency relationship. This notice of termination should be given, and all other precautions which are found in the general provisions for the termination of an ordinary agency relationship should be followed.

DEL CREDERE AGENTS ⁷³

When a commission merchant or other agent agrees with his principal to assume the risk of the third party with whom he deals in a contract negotiated for the benefit of his principal, he accepts a del credere commission. He thereby becomes directly and personally liable to the principal for the performance of the contract as well as for the payment of the amounts due thereunder as if he were the actual buyer. This form of commission contract is sometimes also imposed upon a commission merchant by the custom of the place where the business is carried on.⁷⁴

Where the commission merchant assumes this responsibility, he becomes directly liable to his principal for the strict performance of the agreement and is liable for any damages due to change, delay, or default of the third party but not for any enlargement of the liability arising out of any agreement between the principal and third party.⁷⁵ He is entitled to use all the defenses open to the third party.

In a del credere commission the amount of fee properly payable depends upon the risk assumed by the agent in each particular case, and unless such fee is fixed it will be determined by commercial usage in the particular locality where the agency is conducted. The fee,

⁷³ The law relating to del credere agents is the same as that applying to commission merchants except as regards liability of the agent and payment for his services.

⁷⁴ H.G.B. 394.

⁷⁵ B.G.E. 787.

however, is always larger than the commission to which the commission merchant is entitled under the ordinary commission contract.⁷⁶

A commission merchant purchasing a bill of exchange for his principal is bound to endorse it in the customary manner and without reservation as to his liability,⁷⁷ and such a commission also is in the nature of a *del credere* commission.

BROKERS

A mercantile broker (*Handelsmaekler*) is defined as a person who in the regular course of his trade acts as an intermediary on behalf of other persons without being in continuous contractual relationship with either of them in the formation of contracts relating to (a) the purchase and sale of goods or negotiable instruments, (b) the placing of insurance, and (c) the forwarding of goods, bottomry and affreightment, or other objects of mercantile intercourse. Transactions in connection with immovable property, however, even though entered into by a broker as an intermediary, are not considered under this heading.⁷⁸

The Civil Code further defines a broker as one who indicates the opportunity for the conclusion of a contract or assists in the negotiation of its terms. He need not necessarily take steps to bring about the contract, however, or even bring the business to a conclusion; but if he does so, he must conduct himself with the prudence of an average trader and must also answer for the acts of his representatives and assistants.⁷⁹

Insofar as special provisions are not laid down in the Commercial Code,⁸⁰ the sections of the Civil Code⁸¹ govern these transactions, except that in no case do they apply to retail sales of merchandise or the broker acts of small traders.⁸²

QUALIFICATIONS AND FUNCTIONS

The broker who accepts a brokerage contract (*Maeklervertrag*) is always an independent merchant who conducts his own business and must also, therefore, have legal capacity and subject himself to the rules and regulations of the Commercial Code as to merchants generally.

The functions of a broker should be clearly distinguished from those of an ordinary agent as well as from those of a commission merchant. The ordinary agent or mandatary deals for his principal and in his principal's name, and the commission merchant deals for his principal but in his own name; whereas the broker acts merely as an intermediary to bring two contracting parties together. He steps out of the role of broker when he contracts in the name of either principal and when he contracts in his own name for another; in the former case he becomes an ordinary agent, and in the latter a commission merchant.

A RELATIONSHIP OF TRUST

The broker, therefore, acting as an intermediary between two contracting parties, occupies a position of trust as to both of them, and

■ H.G.B. 394.
■ H.G.B. 395.
■ H.G.B. 393.

■ B.G.B. 278, 562.
■ H.G.B. 94-104.
■ B.G.B. 652-656.

■ H.G.B. 104.

such a relationship in and of itself forces him to assume, and impresses upon him, duties similar in nature to those of a public officer or the recipient of a public trust. In view of this fact, the several German States, in order to limit, define, and control their activities generally, and to impress the relationship with an additional solemnity, require brokers to have certain definite qualifications and to apply for public authorization and to register; and when they have been accepted, authorized, and registered as such brokers, they are further obligated to take an oath that they will conduct themselves properly with regard to the responsibilities which they have assumed. A like obligation is impressed upon exchange brokers under the bourse law. As such public officer, if a transaction is liable to stamp duty, the broker must, under penal liability, provide such stamps and see that they are affixed to the documents.⁸³

The broker, although he assumes a relationship of trust with his principal by his oath, is not obligated, in the absence of special provision therefor, to investigate the ability of the parties to fulfill the contract or the competency of the parties to contract; but he must communicate to those for whom he acts as intermediary any circumstances or disabilities of which he is or becomes cognizant, even though they may be calculated to deter either of the parties from entering into the business proposed. He must also generally watch over the interests of both of his clients with faithfulness, diligence, and conscientiousness, and especially not work against the conclusion of the contract. The information intrusted to him by the parties must be treated as strictly confidential and not be revealed from one to the other. He must of necessity disclose certain information received from each party to the other in order to bring them together, but under no circumstances may he make a disclosure to a third party concerning the contemplated contract. He may not even disclose the names of the parties one to the other until the necessity therefor arises in the negotiations.

Acting as he does for both parties, he must be careful to conserve and serve the interests of both alike and act with complete impartiality; and when he does so act he is guilty of a breach only if he violates the agreement or the instructions of either of the parties, and only in such cases does he forfeit his claim for commissions.

BOOKKEEPING REQUIREMENTS

Brokers being merchants, the law imposes upon them the duties of merchants generally to keep books and records of their transactions. They are also additionally specifically obligated to keep a journal, in which all transactions are to be entered daily and in chronological order, including (a) the names of the parties for whom they contract, (b) the subject matter and terms of the contracts negotiated, and (c) where the transactions involve merchandise or negotiable instruments the numbers, price, and time of delivery thereof. They are not called upon to make the entries themselves, but must see that they are made and sign them when made.⁸⁴

They are also obligated to supply to the parties at any time signed extracts of all the entries in their books with respect to transactions negotiated for them. They are not permitted to charge for furnish-

⁸³ Boersengesetz 34; stamp law 15, 25, 27.

⁸⁴ H.G.B. 43-44, 190.

ing such extracts. Further, they must allow inspection of the relevant entries in their books to the interested parties on demand. The courts may also, independently of the request of either party, require the production of such books in order to see whether they are consistent with the contract note issued by the broker, the signed extract from his books, or other evidence.⁶⁵

ADDITIONAL DUTIES

Besides the primary duties imposed upon a broker as an independent merchant and the duty to obtain public authority and register in the several States of Germany for brokers in general and under the bourse law for exchange brokers, a broker is specifically obligated in the conduct of his daily transactions as intermediary to furnish contract notes to the parties for whom he is acting.⁶⁶

Except when he is expressly excused by the parties or by local custom, the broker must, immediately upon the conclusion of a transaction, deliver to each party a signed contract note containing the same details as he is compelled to enter in his books concerning each transaction. Where the contract is to be completed at once, duplicate contract notes must be prepared by the broker and presented to both parties for their signatures immediately, so that they may exchange the copies signed by them one with the other. If either party refuse to sign a contract note, the other party must be immediately notified of such refusal by the broker.⁶⁷

A broker may not represent both parties if there is an express prohibition in his contract of employment with one of them to that effect; and if he does so, his claim for commission will be barred. Nor may a broker, without the consent of his principal, become a party to a contract with him. Particularly is this true of an exchange broker, who cannot become such a party even with the consent of his principal unless he cannot obtain another suitable third party to accept the transaction; but where he does legally become a contracting party with his principal, he does not lose his right to a commission.⁶⁸

He may, however, be forced to become a contracting party and carry out the contract with his principal under certain circumstances—if, for instance, he sends a contract note to his principal in which he reserves the right to nominate the other contracting party subsequently and the principal properly refuses to accept the nominee. Where the principal accepts a contract note of this kind he is bound thereby unless a well-founded objection can be made against the other party when he is nominated. The nomination must take place within the time prescribed by local custom or, if there be none, within a reasonable time. If there be no nomination made by the broker or it is untimely, or if there be a well-founded objection to the party nominated, the principal may force the broker to perform himself.⁶⁹

The broker is not deemed to have authority to receive payments or to give a receipt or discharge to either party for any service stipulated in the contract.⁷⁰

To assist the parties in mercantile transactions to prove their contentions in the event of litigation, the commercial law also im-

• H.G.B. 101-102; R.G.B. 810.
• H.G.B. 94, 95.
• H.G.B. 94.

• B.G.B. 654; Boersengesetz 32.
• H.G.B. 95.
• H.G.B. 97.

poses upon a mercantile broker, unless excused by the parties or by local custom, the duty, in a sale of goods by sample, to retain such samples and mark them for identification until the goods sold have been accepted without objection or until the transaction is otherwise ended. Either party during the time the samples are so kept may demand their production for inspection.⁹¹

COMPENSATION AND REIMBURSEMENT

The transactions of a broker being in most cases entirely commercial, his compensation is implied. Where such compensation is not fixed, it is the tariff rate; if there be none, then the usual compensation is presumed. Even where the compensation is fixed, however, it may be reduced by the court of competent local jurisdiction on application if it is considered to be exorbitant under the circumstances, except that in no case will it be disturbed where it has already been paid.⁹²

The broker, from the very definition of his relationship, is impliedly an intermediary; but where one of the parties has made an express limitation against a broker acting for both of them, he is not permitted to do so, and if he does so he is not entitled to a commission fee therefor. Usually, however, he does act for both parties and is entitled to charge each of them one half of the commission; but if either of them fails to pay, his half of the fee is not collectible from the other party. The broker is also entitled to his commission even where he becomes one of the contracting parties in the transaction. He can claim remuneration only when the transaction effected through his efforts is concluded or embodied in a contract. If, however, the transaction depends on a contingency, the broker has no claim for commission until the happening of the contingency; and if it is subject to a condition by which it may be canceled, his claim may be made only in the event the condition does not arise, and if he is paid meanwhile the fee must be returned.⁹³

The broker may claim compensation from both parties for whom he has acted as intermediary, even though they have not engaged his services, where they know or should have known that they have been brought together by such broker or he was instrumental in the successful termination of the business.⁹⁴ Extreme care should be taken to avoid relationships that might lead to unfounded claims for brokerage.

If the transaction which the broker has brought to the attention of the parties for whom he is acting as intermediary fails, he cannot claim payment.⁹⁵ But if one of the parties is guilty of fraud and the contract is impugned, the broker is entitled to his commission notwithstanding. The broker's claim is not defeated when the contract is not completed because of faulty delivery on the part of one of the contracting parties. If the contract for the making of which the parties have been brought together by the broker is not completed, but another contract is effected, the broker may claim fees for the completion of the new contract, provided it fulfills the same commercial object as the original proposal or the broker has actively participated in bringing about the new contract.

⁹¹ H.G.B. 96; B.G.B. 809, 811.

⁹² B.G.B. 653, 655; H.G.B. 99.

⁹³ B.G.B. 652, 654; H.G.B. 95, 99.

⁹⁴ R.G. vol. 47, p. 255.

⁹⁵ R.G. vol. 29, p. 230.

Ordinarily the broker is entitled only to commissions, unless reimbursement for expenses is also specifically agreed upon;⁹⁶ but in no case are expenses to be repaid to the broker if the contract for which he has brought the parties together is not concluded, except when such repayment is definitely provided for.

TERMINATION OF RELATIONSHIP

Either the broker or any party for whom he acts as an intermediary may terminate the relationship at any time without notice. However, notice cannot be given after the broker has brought the parties together if as a result of his introduction the parties subsequently contract concerning the contemplated matter. It is conversely true that the principal need not conclude the contract if the party to whom he has been introduced by the broker is unsuitable. The onus in such cases is on the person commissioning the broker, and he must justify the objections which he raises against the contracting party introduced by the broker. Since the broker, when he acts only within his authority as a broker, conducts himself as a mere intermediary and has nothing to do with the making of the contract for either party, it can be clearly seen that notice of revocation to the other party is not necessary.⁹⁷

FORWARDERS **

A forwarding agent (*Spediteur*) is defined as one who in the regular course of his trade undertakes the forwarding of goods by carriers on land or sea in his own name but on the instructions of another.

The rules and regulations applying to forwarders also apply to merchants generally (even though they may not be forwarders) where in the course of their trade they act as such.

Upon all points not specifically regulated by the Commercial Code⁹⁸ forwarders' rights and liabilities are regulated generally by the rules applying to commission merchants. (See "Commission merchants", pp. 128 to 134.)

DUTIES OF THE PARTIES

The forwarder must act with the diligence of a careful mercantile trader, protect the interests of the principal, and carry out his instructions. He must, where possible, see that the acts of the carrier he selects are conducted with dispatch, but he is not liable for the default of his subagent where the goods have already departed from the locality in which he does business. He is liable only if he does not exercise care and good judgment in the selection of his subagent; but he is liable at all times for the defaults of his own employees or even of a subagent where he appoints such subagent to relieve himself of work. This liability extends not only to the transport of the goods but to everything he is required to do in connection therewith; and if he is guilty of willful breach of any

⁹⁶ B.G.B. 652.

⁹⁷ R.G. vol. 47, p. 255, and vol. 35, p. 105.

⁹⁸ Forwarders are included in this chapter because their relationship is really in the nature of agency, in that they perform acts under the instructions of a principal, although their duties are specifically limited to transactions involving transportation of merchandise.

⁹⁹ H.G.B. 407-415.

of these duties, he must indemnify the sender for any loss sustained. He must give all necessary information to the sender with regard to the transportation of the goods, and when the carriage is completed he must render an account thereof.¹

No legal relationship arises between the forwarder and the consignee. The forwarder cannot demand his commission from the consignee, and the consignee cannot enforce rights against the forwarder as he can against a carrier or a shipowner.² A forwarder, however, may demand from the consignee payment for the merchandise of the consignor if instructed so to do by the latter, and he must not deliver the merchandise until he is paid as instructed. In all cases the forwarder is under a duty not to hand over the goods until the carrying charges are paid by the consignee, even in the absence of such instructions.

FEES AND DISBURSEMENTS

The forwarder is compensated for his services by a commission, which may be fixed or may be the commission usual in such cases. The commission is assessed on the amount of the freight bill. The forwarder must charge the freight to his principal at the rate it is billed to him, and he is entitled to his commission when the goods are delivered to the carrier. He acquires a lien upon the goods forwarded by him for the freight paid, for his commissions, and for all expenditures and advances made on the goods. This lien he retains so long as he retains the goods in his possession or can dispose of them by bill of lading or by carrier or warehouse receipt. This lien is transferable interchangeably between the agent and the sub-agent, depending only on which one pays the carrying charges and assumes any liability or makes any disbursements. It is not a general lien but extends only to the particular goods and for the particular claims arising out of work in connection therewith. The holder of this lien is also entitled to claim commissions for work done in realizing upon his right of lien.³

The forwarder has the right to perform the carriage himself if it is not contrary to his agreement, and thereby he assumes the rights and obligations of the carrier as well as the right to charge for such services in addition to the charges he is entitled to make as a forwarder; but where he agrees to charge a fixed rate for the entire carrying operation, his rights and liabilities become those of a carrier exclusively, and he cannot charge a forwarding agent's commission in addition to the fixed rate unless this has been expressly agreed. The forwarder may, where authorized by custom, demand advances to cover the necessary expenses of transportation, but only to the extent that such charges are not adequately covered by the goods themselves.⁴

Forwarders' claims for commission and expenses are barred in 2 years, but where the sending is done in the course of the sender's trade the period is extended to 4 years. Claims against a forwarding agent for loss, deterioration, damage, or late deliveries of mer-

¹ H.G.B. 408; B.G.B. 276, 278, 613, 666-675.

² B.G.B. 433, 512, 563, 592.

³ B.G.B. 354, 611-612; H.G.B. 408-411.

⁴ H.G.B. 396, 411, 413; B.G.B. 669.

chandise are barred in 1 year unless extended by agreement. These provisions of prescription do not apply where the claims arise from the willful acts of the forwarder.⁵

Termination of the relationship is effected in the same manner as for a brokerage agreement. (See p. 139.)

CARRIERS *

A carrier is one who in the usual course of his trade undertakes to complete the forwarding of goods or passengers. A carrier by land, river, or inland waters is called a *Frachtfuehrer*; a carrier by sea, a *Verfrachter*. A mercantile trader not a carrier who in the course of his business undertakes the forwarding is governed by the same rules. These rules as to "carriers" have no application to forwarding by mail.⁷

So far as the Commercial Code⁸ does not otherwise provide for contracts of carriage, the appropriate sections of the Civil Code⁹ apply. The railway traffic regulations (*Eisenbahnverkehrsordnung*) and the goods-in-transit convention (*Uebereinkommen ueber den Eisenbahnfrachtverkehr*) are additional enactments regulating the relationship and defining the rights and obligations of the parties.

The contract of carriage, whether it be for passengers or for freight, is not required to be in any particular form, except that it cannot provide a limitation on the rights and duties of the parties as outlined in the two carriage acts and the general law of carriers.¹⁰

SIGNIFICANCE OF WAYBILLS

The carrier, upon accepting a forwarding instruction, may demand a waybill, which must include (*a*) place and date of issue, (*b*) name and address of the carrier, (*c*) name of the consignee, (*d*) place for delivery, (*e*) description of the goods (e.g. nature, quantity, and marks), (*f*) description of the papers accompanying the goods for customs, excise, and police examination, (*g*) agreement as to amount of carriage payable and acknowledgment of payment in such case, (*h*) arrangement between the interested parties as to time of delivery, compensation in case of breach, and payments upon which making of delivery is conditioned, and (*i*) signature of the consignor.¹¹

The waybill is considered to be merely evidence of the contract from the consignor's point of view and therefore only primarily evidence against him, but it becomes evidence against the carrier as well when he expressly or impliedly assents thereto. Even in this circumstance, however, its terms are not considered to be conclusive proof of their truth, and either party may show that it does not correctly set forth the contract as to number of articles, weight, or carriage charges. However, the consignor is by law responsible for the accuracy and sufficiency of the items contained in the bill, and he must also deliver to the carrier all papers necessary for the

⁵ R.G.B. 196; H.G.B. 414.

* Carriers are included in this chapter because their relationship is really in the nature of agency in that they perform acts under the instructions of a principal, although their duties are specifically limited to transactions involving transportation.

⁷ H.G.B. 425, 451-452.

⁸ H.G.B. 425-473, 556-663.

⁹ R.G.B. 631 et seq. and especially 675.

¹⁰ H.G.B. 471.

¹¹ H.G.B. 426; E.V.O. 55-56; T.C. 6.

authorities and is liable to the carrier for consequences due to the absence, insufficiency, or incorrectness thereof.¹²

The railway carrier must on demand sign a duplicate of the waybill for the sender.¹³

DUTIES OF THE CARRIER

An ordinary carrier is not obligated to accept every forwarding instruction offered; but when he does accept a carriage contract he is bound to perform with the care shown by an ordinary, prudent merchant, not only in the transporting but also as to any other action he has to take. He is also responsible for the acts of his servants and those of his subcarriers as though they were his own acts. He and his subcarrier are jointly liable, and inability of either of them to respond for the damages sustained by the sender renders the other liable for the deficiency.¹⁴

A railway as a carrier may not refuse to receive goods for transportation at any station if the consignor comply with all the regulations, except when forwarding must take place immediately and the railway has not the facilities therefor. Ordinarily forwarding is to be effected in the order of priority of receipt unless there are cogent reasons for preference. The railway is also liable for the acts of its servants and subcarriers.¹⁵ Liability in carriage by sea is governed by the Commercial Code.¹⁶

A carrier must deliver within the time fixed in the contract; if none is fixed, then according to local custom or, in the absence thereof, within a reasonable time under the particular circumstances.¹⁷

In the case of a railway the time of delivery is fixed by the two Government carriage acts.

The carrier must notify the consignee of the arrival of the goods at the place of delivery and deliver the goods to the person mentioned in the carrier's receipt or, if made out "to order", to the holder of a properly endorsed bill. The last carrier (unless otherwise provided in the waybill) must collect from the consignee the carrying charges and all other sums owing to preceding carriers on payment of which delivery is conditioned, and must not relinquish the lien without such payment. If he does so, he is responsible in damages to the preceding carriers or forwarders, but his claim against the consignee remains good.¹⁸

If a consignee cannot be found or refuses to accept, or if delivery is prevented, the last carrier must immediately notify the sender (even where the sender has ceased to have the right to give instructions as to the disposition of the goods) and obtain his directions unless circumstances render this impracticable. In the latter event, or where the sender fails to give directions, or where he issues directions that cannot be carried out, the carrier may deposit the goods in a public warehouse or other safe place. If the goods are perishable or if delay involves risk, he may have the goods sold as provided in the Commercial Code. Always, however, he must immediately advise the consignor (and where possible the consignee) of all steps taken. Failure to do so renders him liable.¹⁹

¹² H.G.B. 426-427; E.V.O. 57; T.C. 7, 10.

¹³ H.G.B. 455.

¹⁴ H.G.B. 431; B.G.B. 347, 422-424, 426.

¹⁵ H.G.B. 453, 458; E.V.O. 3, 5; T.C. 29.

¹⁶ H.G.B. 662 et seq.

¹⁷ H.G.B. 428.

¹⁸ H.G.B. 441-442, 447; E.V.O. 79.

¹⁹ H.G.B. 373, 439, 443.

The duties of railroads in connection with the carriage of passengers are defined in the railway traffic regulations.²⁰

RIGHTS OF THE CARRIER

A contract of carriage where no express agreement is made to pay a sum to the carrier is a commission within the meaning of the Civil Code: otherwise it is a contract for services, and in either case compensation is implied. The sum to be paid for carriage is, in the absence of agreement, fixed in accordance with the tariff; where there is no tariff, it is settled by custom. Where no custom exists, the carrier must not claim beyond what is equitable. Where the agreement is that the charge should be based on the weight of the goods, this weight is to be the weight of the goods on delivery.²¹

If the goods are lost by accident, the carrier is not entitled to claim the carriage charges on them. If they are lost through the fault of the person having the right to dispose of them, the carrier's right to compensation is still good, less whatever he has saved by not proceeding with the transport and also less whatever he has gained in any other way. If the goods are lost in consequence of an inherent defect or through the following of instructions given by the person having the right to dispose of them, and there is no contributory circumstance for which the carrier is responsible, the carrier can claim a proportionate part of the carriage charges as well as any amounts expended by him on the goods.²²

The sender of the goods may give notice to terminate the contract of carriage at any time while the goods are in transit, and the carrier then is entitled to the carriage rates less whatever he has saved by not fully carrying out the contract. If the beginning or a continuation of the carriage is prevented by circumstances not the fault of the sender, he may rescind, but must pay the carrier for as much as the latter has done, provided the carrier has not been to blame. If the carrier is responsible for temporary delay in transport, he is not entitled to claim compensation and especially not for the carriage, but he is entitled to be paid to the extent of any accession of value to the goods brought about by his services.²³

Where the transport is temporarily delayed solely because of the fault of the sender, the rules of the Commercial Code²⁴ apply, and the carrier may take into account such advantages as he has lost by the delay and claim damages for having been prevented from carrying out his contract. If, however, both parties are responsible for the circumstance which caused the temporary delay, the Civil Code²⁵ governs.

Where a railroad contracts to deliver to a place not situated on the railway, it may be stipulated that the company shall be liable as a carrier only for the transport of the goods to the most convenient railway station and that as to any further transport it shall be liable as a forwarding agent.²⁶

Railroads are also required to publish schedules of rates for carriage to which they will be bound.²⁷

²⁰ H.G.B. 477; E.V.O. 10-29.
²¹ H.G.B. 215-314, 632, 662.
²² H.G.B. 324, 644-645.
²³ H.G.B. 649, 612; H.G.B. 428.

²⁴ H.G.B. 324.
²⁵ H.G.B. 254, 324-325.
²⁶ H.G.B. 458.
²⁷ T.C. 11-13.

CARRIER'S LIEN

The carrier has a lien to secure claims arising out of the contract of carriage covering the carrying charges, demurrage, duty, and other outlays and advances. This lien is enforceable so long as the carrier retains the shipment or can exercise the right of disposal, and even after delivery provided he enforce it judicially within 3 days of delivery and the goods are still in the consignee's possession. To collect his claim out of the pledged goods by sale thereof, however, he must give notice to the consignee in accordance with the Civil Code,²⁸ and in some cases also to the consignor.²⁹

The lien of the carrier is not a general one. It occurs only on claims arising out of a particular contract of carriage and attaches only to the goods involved in that contract. A carrier may not withhold delivery to a consignee because of some old claims against the consignor.³⁰

The lien of all preceding carriers remains enforceable until the extinction of the right of the last carrier, and any carrier or forwarder satisfying the claim of any other acquires the other's rights.³¹

Where more than one lien arises in a carriage contract, the liens rank inversely to the time at which they arose—the later taking priority over the earlier; and all such rights take priority over pledges or liens arising otherwise.³²

The carrier may issue a signed receipt stating his obligations with regard to delivery, and the sender must upon request furnish the carrier with a copy of it countersigned by him. This receipt is decisive as to the rights and liabilities existing between the carrier and the consignee. The contract of carriage is decisive as to relations between the carrier and the consignor.³³

LIABILITIES OF THE CARRIER

A carrier is liable for damage due to loss or injury to goods while in his control and for late delivery unless due to circumstances which could not have been avoided by the diligence of a careful carrier. He is not liable for loss or damage of valuables, works of art, money, or negotiable instruments unless informed of their nature or value when intrusted to him.³⁴

Railroads are liable for damage due to loss or deterioration unless caused (a) by default of the person entitled to the disposition of the goods, (b) by vis major, (c) by defect in packing not apparent on the outside, or (d) by the nature of the goods themselves. If damage occurs to goods exposed to the above circumstances, the damage will be presumed to have been occasioned thereby. A railroad may further limit the amount of its liability by allowing a special tariff rate for the carriage, especially as to valuables where the liability is based upon the tariff as established by the railway traffic regulations.³⁵

Where compensation is to be made *for loss*, a carrier must pay the market value or the ordinary value of goods of the same description and quality at the place and time when delivery should have been made, less the amount saved in customs, other expenses, and

²⁸ B.G.B. 1234, 1237, 1241.

²⁹ H.G.B. 440.

³⁰ H.G.B. 369.

³¹ H.G.B. 441.

³² H.G.B. 443.

³³ H.G.B. 444-446.

³⁴ H.G.B. 429, 606-607.

³⁵ H.G.B. 456, 459, 461-462, 467, 606.

carriage charges. When compensation is to be made *for injury*, the carrier must pay the difference between the selling value and the ordinary market value. The amount and the question of such liability are further limited and restricted for railroads by the traffic regulations act.³⁶

For default in prompt delivery a railroad is not liable if the default occurred through an event which it neither caused nor could have prevented; otherwise it may be liable for the entire amount involved in the default in prompt delivery, but only where provided for in the waybill and in no case if the amount be more than that fixed by the regulations as the railroad's limit of liability.³⁷

Payment of carriage charges and other sums due, accompanied by acceptance of the merchandise shipped, extinguishes all claims against the carrier unless damage or deterioration is certified by official experts prior thereto. But where such damage or deterioration is not discoverable by outward condition, claim can be made against the carrier if the defect is certified by such experts immediately upon discovery any time within 1 week after acceptance.³⁸

A railroad is liable for loss of or damage to baggage up to 300 marks unless due to the negligence of the owner in packing or to "act of God", the burden of proof of which is upon the carrier. Baggage is "lost" if it cannot be given to owner in 3 days after the arrival of the train by which it should have been sent, but there is no liability on the railroad if the baggage is not called for within 14 days after its arrival at destination. If personal baggage is left in its cars, a railroad is liable only when guilty of default. The burden of this proof is on the owner.³⁹

Notwithstanding the above, this liability of either ordinary carriers or railroads is not limited where they are guilty of willfulness or gross negligence, in which event full damages may be recovered.⁴⁰

Where a carrier delivers over a part of the carriage to another carrier he remains liable under the contract of carriage to the time of delivery, and the new carrier also becomes a party to the contract and directly takes over the obligations. Where one of several carriers becomes obligated for damages, he has a right of indemnity against any other carrier in the transaction who can be proved to have been guilty of the default which caused the damage. Where the responsibility cannot be fixed on any one of them, all must contribute proportionally to the amount of carriage charges paid to each. As between carriers, the liability is determined on the basis of the carrier's receipt.⁴¹

Where several carriers effect the carriage, claims arising thereunder can be enforced only against the first or last carrier or the one on whose line the damage occurred. A carrier need not deliver goods unless his receipt be returned with acknowledgment of delivery of the goods endorsed thereon.⁴²

RIGHTS OF THE CONSIGNOR

The consignor may vary his instructions to the carrier as to delivery, but he must pay the extra costs incurred thereby until the merchandise arrives at the place of delivery or the consignee claims

• E.V.O. 64-69, 93-100; T.C. 30-46.
 • H.G.B. 463, 466.
 • H.G.B. 438, 464.
 • H.G.B. 465; E.V.O. 36.

• H.G.B. 430, 457, 465.
 • H.G.B. 432, 449.
 • H.G.B. 448, 469.

them. However, where the carrier gave a receipt for the goods or a railway signed a duplicate waybill, such carriers may not obey the consignor's instructions unless the receipt or duplicate waybill is returned; and if they do, they are liable for the value of the goods to the holder of the receipt or waybill.⁴³

RIGHTS AND LIABILITIES OF THE CONSIGNEE

The consignee has the right, even before the arrival of the goods, to provide for their preservation and disposition (just as the sender has the right when no carrier's receipt is issued), and for this purpose he may instruct the carrier; but he can only require the carrier to deliver the goods before arrival if the carrier has the consignor's permission so to do. If, however, the consignee renounce or refuse his right to give instructions, or if he instruct that the goods be returned, he loses the right to instruct the carrier as to disposal of the goods.⁴⁴

After the arrival of the goods at the place of destination the consignee may enforce all the rights arising out of the contract of carriage, provided he perform his own obligations thereunder, unless the carrier receives contrary instructions from the sender (who still retains this right).⁴⁵

The arrival of the goods at the place of delivery and the handing over of the waybill to the consignee merely give the consignee the right to instruct as to their disposal and impose on him no obligation to pay the carrier. This obligation accrues only when he accepts the goods or in some other way makes himself liable (as, for example, by issuing instructions). The consignee may claim the right to inspect the goods before payment of any charges.⁴⁶

Any reservations made on the receipt of goods unless agreed to by both parties are of no avail; but if the consignee declares that he takes the goods only as the carrier's agent and on the carrier's account, the consignee will not be held to have accepted the goods.

Acceptance of the goods and waybill renders the consignee liable for all payments to the carrier under the waybill, and he must give a receipt for the goods at that time if it is demanded.⁴⁷

AGENTS ACTING SOLELY FOR AMERICAN FIRM

EXCLUSIVE AGENT

An exclusive sales agreement is valid under German law. The method is much used in the sale and distribution of foreign manufactured products. Under such agreements the establishment and maintenance of fixed prices is permissible, and they are enforceable in German courts because violation of such price agreements would be actionable as in the case of an ordinary breach of contract.

In making sales arrangements of this kind the American firm must take care that it does not become involved in tax liability, by keeping such representation strictly separate and apart from its American business. To accomplish this, under no circumstances should the exclusive agent be hired as a salaried employee of the American firm or conduct a branch office thereof. (See "Liability of foreigners to taxation", p. 60.)

⁴³ H.G.B. 433, 447, 455.
⁴⁴ H.G.B. 434, 447; B.G.B. 333.

⁴⁵ H.G.B. 433, 435.
⁴⁶ B.G.B. 436, 809-811.

⁴⁷ B.G.B. 368.

AGENT UNDER POWER OF ATTORNEY

Agency relationships are also created for American firms "doing business" in Germany by a formal declaration by the principal, accomplished by the execution of a document therefor. These are agencies under power of attorney as that relationship is known in English and American law. The power is conferred expressly and in writing and is only as broad as authorized by the instrument itself.

German law does not require a power of attorney to be in any certain or particular form. A power drawn in a foreign country in accordance with the laws of that country is entirely satisfactory and acceptable for all purposes specified therein and before all courts and for filing in German official registries, provided the document is duly and properly legalized. The power may be in the language of the foreign country and need not be translated into German and if translated need not be certified. It frequently is advisable, however, to translate the power when it is required to be recorded in a German registry and especially where the transactions under the power are to be conducted with Germans who may not understand the language in which it is written. It is also good policy to make a power of attorney conform as nearly as possible to the forms familiar in Germany in order to avoid misunderstanding, difficulty, and delay, and particularly to avoid the possible necessity of proving the foreign law in the event of litigation.

ADVISABILITY OF FORMAL POWER OF ATTORNEY

The German courts and German business men will imply an agency relationship or recognize one created by mere act or oral declaration in the case of the representative of a German firm; but the law is quite clear that they must not and cannot imply powers or authority for the representative of a foreign firm, or even recognize his agency, under a like act or mere oral declaration.

It is true that in some cases a telegram or a letter or other identification from the home office will be accepted by a German firm in trading with the representative of the foreign firm; but the German firm will act only with hesitation and guardedly, and the best results cannot be obtained, in important transactions conducted under such conditions. Neither can the foreign firm itself be protected against unauthorized or misconstrued acts of its agents under this loose method of dealing. This leaves out of consideration those cases where a contract is to be entered into which requires formal proof of the agent's authority and where the courts or the official records or registries for such transactions demand authentication of the power under which the agent acts, in which cases a power of attorney is absolutely necessary.

From all points of view, therefore, where a foreign organization enters Germany to do business through its representative, it should, as a general rule, furnish him with a formal document authorizing him and limiting his powers and proving the authority for the delegation of such powers.

INTERPRETATION OF POWERS

The laws of the country where a power of attorney is drawn up may be at variance with the laws of Germany as to the interpretation of the powers mentioned in the document. In this connection

it cannot be too often repeated that German law presumes no implied powers to agents under a foreign power of attorney.⁴⁸ In interpreting such documents the German courts will (in the absence of proof which is most difficult to adduce) accept only those powers as are actually conferred—which are clearly contained within the “four corners of the document”—and such documents will have force and be binding only to the extent of the wording and contents. As an instance of this strict construing, a power to sell property does not give the right to sign a deed unless that power is specifically set forth.

The drawing, therefore, of a power of attorney for use in Germany should be given the most careful attention and scrutiny. Where possible, the power should be worded in accordance with the German laws relating to the transactions proposed to be carried out by the representative in all their details. For this purpose the attorney called upon to draw the power should be fully acquainted with German law.

PROOF OF RIGHT TO CONFER POWER

When an American power of attorney is granted to do business and to carry on transactions in Germany, extreme care should be taken to see that proof of the right to grant such power is given in or with the document itself. It is quite simple for a *sole owner* of a business to give proof of his authority to confer power of attorney on his representative. He does so by reciting in the document that he is such sole owner and affixing his signature.

Proof of this authority to grant the power is more difficult if the American firm is a *partnership*. Where all the partners sign the power of attorney, to prove the authority of such partners it is only necessary to recite in the document that they are all the partners. Where one of the partners, however, signs the power of attorney for the partnership, the document should contain a copy of the partnership agreement—or at least the clauses thereof which authorize the person signing to execute the power on behalf of the partnership. The notary who acknowledges the signature of such partner must also certify that the transcript of the clauses of the partnership agreement are correct and correspond to the original, with which he has compared it.

Where an American *corporation* grants a power of attorney for use in Germany, such power must contain all the facts which establish the right of the person granting the power in the name of the corporation to confer it, including (a) the sections of the general corporation law of the State in which the corporation has its domicile as to the powers of the board of directors; (b) the appropriate sections of the articles of incorporation and the bylaws of the corporation relating to the powers of the board of directors; (c) the resolutions of the board authorizing the officer of the corporation who signs the power of attorney to execute it on behalf of the corporation, together with proof that the meeting of the board which

⁴⁸ It is quite true that if a power of attorney issued under the laws of another country is used in Germany, international law will dictate that the document be interpreted according to the laws under which it was drawn; but it will be difficult to prove those laws and even more difficult to establish all the presumptions allowed thereunder, and in the absence of such proof the German courts will not permit the presumptions to be recognized.

passed the resolution was regularly and legally held and, if and where possible, the recital in the resolution itself of the form of the power of attorney authorized to be conferred; (d) the minutes of the stockholders' meeting showing that the persons conferring the power and the board of directors authorizing the execution of the power of attorney had been duly elected; and (e), if such power of attorney includes the right to bring or defend a suit for the corporation, a certificate of the secretary of state of the domicile of the corporation to the effect that the corporation was duly authorized and is presently existing.

(As to the necessity for authenticating documents, see pp. 75 and 76.)

REVOCAION OF POWER

A power of attorney legally drawn and properly authenticated by an American firm for its representative to do business in Germany continues until the purposes for which it is created are accomplished or until its revocation with notice to all parties concerned is properly effected. The power is revocable at any time at the will of the grantor except where it is coupled with an interest in the grantee.

A power of attorney so created by formal document given to the representative becomes effective only when it is communicated to the third parties with whom such representative deals by the exhibition of the document itself, and, under German law, it is held to continue in force and effect so long as the document itself remains in the representative's possession. Inclusion of a provision for its return on notice by the grantor of the revocation of such power is therefore highly desirable. Such clause becomes especially necessary in view of the German law, because if an agent refuses to return the document it must be revoked and declared null and void by public proclamation, ordered and provided for by the German courts upon application therefor. It would be extremely difficult, if not impossible, for the German courts to obtain jurisdiction of the parties in order to be in a position to enforce their decrees in this respect where grantor and grantee are not domiciled in Germany.

Attention must also be called to the possibility that an agent acting under a power of attorney once exhibited to his customers as proof of the existence thereof may continue to act and deal with them under the semblance of such power even though revoked and even after he has returned the document, because repetition of the proof of agency by the production of the document is not usually demanded each time they deal with such agent. To obviate this possibility, in revoking a power of attorney the American firm should not be satisfied with the mere return of the document itself but should go through all the precautions of informing the customers and prospects of the former agent by registered letter, publication, and all other methods of bringing knowledge of the revocation to third parties, as in the case of the revocation of an ordinary agency. In this connection it may be observed that, although the publication of the notice of revocation in the newspapers of the locality where the agent acted has only a practical or deterrent effect and no legal significance or binding force, publication is always advisable, especially where the activities of the agent have been extensive and have been given wide publicity.

Where the power of attorney might have been recorded in a mercantile register or land register in Germany, or where the power was or might have been filed with a German court preliminary to bringing or defending a suit for the grantor, the revoking instrument also should be filed in such registries and with such court if for no other reason than as a precaution. The provision for publication of the fact of the revocation of a register entry in the newspapers must also be carefully complied with.

By reason of these difficulties in making effective a revocation of authority, it is advisable that the German custom of granting agency powers only for definite periods should be followed by American corporations in conferring powers of attorney; and from the difficulties encountered in preparing the power of attorney and in specifying the powers to be conferred thereunder, coupled with the difficulty arising from the necessity of proving the authority of the person to confer such power, it also appears advisable that in granting a power of attorney for use in Germany a power of substitution should also be included therein, whereby an alternate may act as and for such agent in the event the original nominee should be incapacitated.

UNAUTHORIZED AGENCY

The rule of unauthorized agency applies only in those cases in which a person without authority to do so represents that he acts on behalf of a named principal. Any contract made by such unauthorized agent may be repudiated at any time by the third party before ratification of the act is communicated to him. This is true, however, only in the event the third party does not actually know of the absence of authority of the agent; if he knew of it, he may not repudiate the contract for two weeks, during which time the person for whom the unauthorized agent acted may ratify the unauthorized act.

A person who acts as an unauthorized agent is himself liable to the party with whom he contracts except where (a) such party knew, or by the use of proper care should have become aware of, the absence of authority,⁴⁹ or (b) the unauthorized agent is a person of restricted capacity (except where he acts with the approval of his statutory representative). Subject to these exceptions, the unauthorized agent must either himself carry out the contract or respond in damages; but such damages are in any event limited solely to the interest of the other party in the validity of the contract.

If an unauthorized agent is not willful in his incorrect representation of the fact of his agency (because he excusably misunderstood the principal's intentions or he excusably had not received notice of the revocation of the agency⁵⁰), the party with whom he contracts can claim damages only for his negative interest in the agreement and not complete damages for the nonperformance of the contract.

Certain acts of unauthorized agents are not subjected to the rigid rules of personal liability for the agent. Where an agent, although unauthorized, acts to avert imminent danger threatening the princi-

⁴⁹ B.G.B. 179.

⁵⁰ B.G.B. 172.

pal, the agent is responsible only for gross carelessness. Where an unauthorized agent acts in fulfillment of the duty of the principal in the public interest or for maintenance of his legal dependents, the will of the principal opposing the act is disregarded and the act itself is considered to be ratified. Where the agent assumes the management of a business transaction, although unauthorized, if the interest of the principal is served or his probable will is carried out, the unauthorized act is deemed to be ratified and the manager or employee who takes the responsibility therefor may demand reimbursement for his expenditures in connection therewith.⁵¹

Ordinarily, however, where the unauthorized agent acts directly contrary to the will of his principal and must have known in so doing that he does so, he is obliged to indemnify the principal for any damage arising, even though he is not chargeable with any other default.⁵²

It is the duty of all persons acting without authority to inform the principal for whom they are acting as soon as practicable concerning their acts, and, unless there is danger in delay, they should await his further determination.⁵³

ACTS DISTINGUISHED FROM UNAUTHORIZED AGENCY

Where a person has the intention to act for another but does not manifest it, the absence of desire or intention to act on his own behalf cannot be considered, as German law does not recognize the doctrine of undisclosed principal. This case, therefore, is not one of unauthorized agency at all;⁵⁴ for if a person does not profess to act for a named principal he is not considered an agent, nor can a person not named as principal by the agent be treated as a principal. The relationship of agent and principal never existed.

Nor does the question of unauthorized agency arise where there is a ratification of an unauthorized act of a self-constituted agent,⁵⁵ as the ratification of the act is sufficient to obligate the person so ratifying to all the provisions of the contract made for him by such unauthorized agent from the time of such ratification as though the agent contracted for him with full powers. It is thereby taken out of the category of unauthorized agency and becomes an agency transaction.

When a commission merchant contracts in his own name but for the benefit of the principal, he does not bind the principal. The question of unauthorized agency does not arise in this instance because the commission merchant himself is liable on the contract he executed. He must be in a position to prove that he has actual authority in order to enforce against the principal the obligation which he has contracted for him. The commission merchant binds only himself to such a contract.

RATIFICATION OF RELATIONSHIP

The *agreement* of an unauthorized agent may be made operative by ratification by the alleged principal. The agency relationship is then considered as though created as of the time of the unauthorized

⁵¹ B.G.R. 679-680, 683 (in the case of the manager, even if his act is against the will of his principal).

⁵² B.G.B. 678.

⁵³ B.G.R. 681.

⁵⁴ B.G.B. 164.

⁵⁵ B.G.B. 177.

act. If the third party demand ratification of the alleged principal, the principal must make his decision by declaration to the third party within 2 weeks of such demand (and any ratification or refusal which the principal has made to the unauthorized agent meantime becomes ineffective); and if in reply to this demand the principal makes no declaration, he is deemed to have refused to ratify. However, up to the time of ratification by the principal, the third party has the right to rescind the contract by notice to the principal or to the unauthorized agent, unless when the contract was made he knew or should have known of the absence of the representative power of the agent.⁵⁶

Where *unilateral acts* are sought, the law differs from where agreements are made. In such cases the third party may and should demand the production of a written power to prove the agency before acting. If such proof is not forthcoming on demand, he is in a position to repudiate the transaction and can do so; but if he does not question the alleged agency, or, knowing that it does not exist, he acquiesces in the fact, the position of both parties to the act is the same as in the case of an agreement, and the third party can only repudiate after 2 weeks, during which time the principal has the right to ratify the contract and bind the third party thereto.⁵⁷

In a unilateral transaction, representation without authority is not permissible; but if the act of the unauthorized agent is permitted by the principal, or if the principal does not object when he is informed of it, it is held to be ratified in the same way as any other act of an agent. An unauthorized agent is also not allowed to enter into a transaction for his principal with himself or with himself as representative of a third party unless the transaction consists in the fulfillment of an obligation.⁵⁸

SUGGESTED PROVISIONS IN AGENCY CONTRACTS

In the creation and continuance of any agency relationship for Germany certain points should not be overlooked:

Any agency, wherever created, should contain the provision that it is to terminate within a limited, definite time.

In the execution of a power of attorney proof of the authority of the person executing it must appear in the body thereof, accompanied by the quotation of appropriate extracts from the records of his business organization giving him this authority.

Every agency created under a power of attorney should expressly provide for an alternate to act for such agent in his absence or during his incapacity. This may also be accomplished by specifically giving the agent himself the power of substitution in certain carefully and clearly defined contingencies.

Copies of the power of attorney should be furnished to the grantee so that they may be protocolized by the proper German authority in those cases where copies are required to be produced.

Every agency created by documents should provide for the return of the documents immediately upon demand.

Every agency relationship, even though the duty may be implied thereunder, should provide that the agent, upon the conclusion of

⁵⁶ E.G.R. 177-178.

⁵⁷ E.G.R. 174, 180.

⁵⁸ E.G.R. 180-181.

any transaction, shall give the principal a full and complete report thereof, and that he furnish his principal at least once every month with the names of all the parties to whom he has represented himself as such agent. The latter provision is for the protection of the principal upon revocation, that he may communicate notice of the termination to each customer and prospect of the agent.

In dealings with all agents for the sale and distribution of the principal's merchandise, all patent and trade-mark rights of the principal, together with all variations and subsequent registrations thereof, should always be retained in the name of the principal.

Since German taxes may from time to time and under changing conditions be levied on business carried on in connection with or under the agency relationship, the advisability of the assumption of such taxes by the American firm should be carefully considered. Where it is possible, of course, provision should be made that they be borne by the agent. This is true also of his expenses contracted in connection with the exploitation of the agency.

Subagents of the agent should be employed entirely at the expense of the agent, and he should be responsible for their acts in the same manner as for his own acts.

The financial standing of every agent appointed by an American firm should be carefully investigated and established before entering into an agreement with him, because there is no better guaranty that the agent will perform his agreement in accordance with the authority and instructions of the principal than that he may be called upon and will have the financial ability to respond for any breaches thereof. For the same reason extra consideration should be given to an agent with a long continuity of the same kind of business experience as that contemplated in the agency, and who has conducted same successfully, rather than a new organization which may be little more than an experiment, although the determination should not be made solely on this basis.

The difficulties of notifying the agent and third parties of revocation of any agency should be minimized by providing in the contract for notice of revocation to the agent by registered letter mailed to a fixed and unchanging address in Germany, and for notice of revocation to third parties by (a) registered communication to all the known customers and prospects of the agent, (b) publication in the newspapers of the locality where the agent acted, and (c), when the acts of the agent required the registration of his power, registration in the same places of the revocation thereof. These precautions as to notice to third parties, though they may assume formidable proportions, should not discourage an American firm from entering into an agency relationship so long as due care is exercised in the selection of the agent. The precautions themselves are only necessary where confidence in the representative is lacking and where there is a fear that the representative may involve the firm in serious losses or may subject it to considerable embarrassment.

VII. NEGOTIABLE INSTRUMENTS

BILLS OF EXCHANGE¹

The law with respect to bills of exchange is embodied in the code bearing that name (*Wechselordnung*) as further limited, defined, and regulated by the Civil and Commercial Codes, the civil practice act, and the bankruptcy act, together with the amendments to all of them.

Every person who is capable of binding himself to a contract may become a party to a bill of exchange.² Persons occupying governmental or public positions—soldiers, teachers, and Government officials generally—are “capable”, as also are unmarried and married³ women of full age, bankrupts,⁴ and deaf, blind, and illiterate persons.

Under the Civil Code only three classes of persons are incapable of entering into a legal transaction and therefore also incapable of becoming parties to a bill of exchange, namely, those who have not completed their seventh year, those who by disease of mind have no free will, and those declared incapable of managing their own affairs on account of mental disorder. Their contracts on bills are null and void even if entered into with the consent of their legal representatives, but their legal representatives can bind them to a bill (usually only with the sanction of the court).⁵

There are others who have a limited or imperfect capacity—minors between 7 and 21 years of age, persons declared incapable of managing their affairs because of imbecility, prodigality, or dipsomania, and persons placed under temporary guardianship.⁶ Their contracts upon bills of exchange require the consent of their representatives to validate them.⁷

If the signatures of persons incapable or partially incapable of incurring obligations on bills of exchange are found upon bills, this fact has no effect on the liability of the other parties.⁸

REQUISITES

A bill of exchange must contain:⁹

1. A description as a bill in the body of the instrument. Use of the word “*wechsel*” or similar expression is required; or if the bill

¹The laws covering bills of exchange and promissory notes are similar in many of their provisions. This section should accordingly be read as covering promissory notes also, except in those particulars where inherent difficulties preclude applicability.

²W.O. 1. The onus is on the defendant, in the event of litigation, to prove his own incapacity. (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

³Only the separate property of married women is subject to their engagements contracted on a bill of exchange. Their dowry or their joint property is subject to the bill only if the husband has given his consent (B.G.B. 1399, 1412, 1460).

⁴The assets of the bankrupt are not bound by liability on a bill of exchange after the commencement of the bankruptcy.

⁵B.G.B. 104, 1643, 1822-1825.

⁶B.G.B. 107-114, 1906.

⁷The consent of the legal representative need not appear on the bill itself. It can be given without formalities or by acts implying it—for example, acceptance.

⁸W.O. 3.

⁹W.O. 4.

is in a language other than German, a corresponding expression in that language.

2. A statement of the amount payable. The amount must be definitely and simply stated, as well as the currency. Payment may be made in German money unless the words "in specie" appear. If the amount is in letters and figures and they differ, the amount expressed in letters governs. If the amount is in letters only or in figures only and is repeated inconsistently in the bill, the amount which is smallest governs.¹⁰

3. The name of the payee or payees. Jointly but not in the alternative or in succession. Bearer and blank bills are not permitted, but bills to "X or bearer" are good. The drawer can be named as payee, but not the drawee.¹¹

4. A statement of the time of payment, which must be for the whole sum. This must be definite and clear, but abbreviations may be used. A bill contingent on the occurrence of a future event is invalid.

5. The signature of the drawer or drawers. This must be placed under the body of the bill. If it is made by mark, it must be attested by the court or notary.¹² The name of the firm may be affixed by stamp or be printed, but the person signing for the firm must sign his own signature.

6. A statement of the date and place of drawing.

7. The name of the drawee.

8. The place where payment is to be made. The address need not be given in the body of the bill, but must appear on its face if no other place of payment is stated. If omitted, the place of payment is by implication the residence of the drawee. However, in a domiciled bill (one in which the place of payment is other than the address of the drawee), the place where payment is to be made must be set forth. The place of payment is that for presentation, protest, and fulfillment of all obligations on the bill.

When a bill does not conform to these requirements,¹³ it is not a valid negotiable instrument, and its transfer operates as a mere assignment.¹⁴

A bill need not contain the words "to order" or their equivalent to make it negotiable. Negotiability is inherent in the bill itself unless otherwise expressly limited in the body of the instrument. But if a bill contains the words "not to order" or their equivalent, endorsement and transfer effect only its assignment.

Stipulations in a bill (a) promising interest or (b) not to present immediately are disregarded and have no effect. Stipulations in a bill which void it are (a) for a specific consideration, (b) inserting a condition, (c) excluding the liability of the drawer, and (d) disclosing the nature of the transaction upon which the bill was founded.

ENDORSEMENT

A bill may be transferred by delivery alone (when the endorsee takes only the rights of the endorser) or by delivery with endorse-

¹⁰ W.O. 37.

¹¹ W.O. 6.

¹² W.O. 94.

¹³ The above are the requirements of a German bill. Requirements of bills drawn elsewhere than in Germany depend upon the law of the country in which they are drawn. (See "Conflict of laws", p. 166.)

¹⁴ W.O. 7.

ment¹⁵ (when the endorsee acquires rights in the bill similar to those of a holder in due course under English and American law). In the latter case, the rights which the debtor may have against the endorser or prior parties have no effect against the endorsee. The endorsement is made by the signature of the endorser affixed to the bill itself, or a copy thereof, or upon a paper annexed to the bill or the copy.¹⁶ The signature of the party signing a bill must actually be affixed by him, although the name of the company for which he signs may be printed or rubber-stamped.

An endorsement may be (1) special, in which case it specifies the person to whom or to whose order the instrument is payable, and the endorsement of such endorsee is necessary to further negotiate the bill; (2) in blank, where it specifies no endorsee, in which case it is payable to bearer and thereafter is negotiable by delivery; (3) restrictive, whereby it either prohibits further negotiation or constitutes the endorsee as the agent of the endorser or vests title in the endorsee only in trust for or to the use of another;¹⁷ (4) qualified, when it contains the words "without recourse" or similar expression, and gives the endorsee a mere assignment, although it still is transferable;¹⁸ and (5) conditional.

Endorsements in blank allow any holder to properly complete them to make a chain of title.

When an endorsement is made, the time of making (date) should be affixed, otherwise the burden of proving the time of the endorsement, where essential, is upon the party maintaining it. A partial endorsement is void.

An endorser, unless he add the words "without guaranty" or a similar phrase, is responsible for the existence and the enforceability of the claim and is jointly and severally liable with the preceding endorsers for nonacceptance as well as for nonpayment of the bill.¹⁹

No one who is a party to a bill is competent to prohibit further endorsement except the drawer. The drawer may do so by expressly providing that the bill is "not to order", and thereafter any endorsement is given no effect. Further transfer of a bill, however, may be limited by any endorser, and those who become holders thereafter are mere assignees with no rights of recourse.²⁰

An endorsement "per pro", "for collection", or similar limitation as to authority conveys rights to the endorsee merely as an agent, but does not transfer full ownership of the bill. He may demand payment or may protest, sue, or even endorse it further if not restricted by his principal, but for the designated purpose only.²¹

An endorsement after protest for nonpayment or nonacceptance or after the time to do so has expired operates as a mere assignment. The assignee acquires the same rights which his assignor has. Inasmuch as failure to protest operates to release certain of the parties, an endorsement after time for protest gives the endorsee rights only

¹⁵ If the drawer has forbidden transference in the bill by the use of the words "not to order" or similar expression, the endorsement has no effect, according to the law of bills (W.O. 9).

¹⁶ W.O. 11.

¹⁷ W.O. 15, 17.

¹⁸ W.O. 14.

¹⁹ W.O. 13.

²⁰ W.O. 9, 15.

²¹ W.O. 17; B.G.B. 626 et seq., 671-675.

against the drawee and those who endorsed the bill after the time for protest for nonpayment had expired, whereas a bill which has been protested for nonpayment before endorsement gives the endorsee rights against the drawer, acceptor, and those who endorsed the bill before protest.²²

ACCEPTANCE *

The acceptance to be valid must contain the signature of the drawee upon the bill itself or a copy thereof. It usually is placed across the face of the bill, when the signature alone will suffice; but when it is written elsewhere, the word "accepted" or similar term should be added. It must be unconditional except as to sum, and where given will be presumed to be so. It cannot be retracted. It can be made at any time before the time for protest for nonpayment has passed.

If the date of acceptance is not stated, it must be proven by the party who must maintain it as a basis for his claim.

If a bill states a place of payment other than the residence of the drawee, in accepting the drawee must name the person at the place of payment by whom such payment will be made unless already mentioned elsewhere in the bill; otherwise the presumption is that he will be there to pay it himself.

Any attempted limitation on acceptance other than as to the sum payable entitles a holder to immediately protest for nonacceptance.

PRESENTATION FOR ACCEPTANCE

Presentation for acceptance can be made by any holder and at any time before expiration of the time for protest. It is optional with the holder, except in the case of bills payable after sight. Where the bill is not presented within the time limit expressed in the bill (where there is no such provision it is presumed to be 2 years from the day of drawing) the liability thereon is extinguished.²⁴ Presentation must be made at the residence of the drawee, and upon refusal should be protested to prove timely presentation.

If a bill is presented for acceptance and acceptance is refused, the drawer and the endorsers (who as such have guaranteed acceptance) may be forced by the court, on application of the holder, to deposit security for the payment of such bill when due.²⁵ The drawer and endorsers, however, in the meantime and before the due date are not subject to other recourse, as they would be under American law.²⁶

ACCEPTANCE OR INTERVENTION FOR HONOR

Refusal to accept a bill of exchange by a drawee not only damages the credit of the drawer but also subjects him, and the endorsers as well, to the necessity of posting security for the payment of the bill at maturity. To avoid these occurrences, the drawer or any endorser may designate on the bill a person or persons known as "drawees in case of need" to accept and pay the bill should the original drawee fail to do so. Where the drawer and endorsers do not,

* W.O. 16.

²² Naturally this section does not apply to promissory notes. (See "Promissory notes", pp. 166-167.)

²⁴ W.O. 19-21.

²⁵ W.O. 25.

²⁶ Negotiable instruments law, sec. 156.

for any reason, wish to name "drawees in case of need", they may have such a drawee without designating him on the bill itself. This is called "acceptance or intervention for honor."

The bill must be presented to the original drawee for acceptance, and, if he refuses to accept, it must be protested before presentation for acceptance to the drawee in case of need. Where there are several such drawees, preference is to be given to the one whose payment would free the greatest number of endorsers.²⁷ The law does not require the bill to be presented to the drawees in case of need unless it can be so presented at the place of payment. Presentation to the drawees in case of need must be made before security for nonacceptance can be demanded of the drawer and the endorsers.

A holder is not required to permit acceptance for honor by a person not named in the bill itself; ²⁸ but where the address of a drawee in case of need appears on the bill or copy he has the right to accept and pay, and the holder cannot disregard him. If such holder refuses acceptance by any intervener named in the bill, he loses his recourse against the party for whose honor the offer was made and against his successors.

Any party subject to recourse can name a drawee in case of need, who may even be a party to the bill itself; and when he is named it is merely an indication of an invitation to intervene but is not binding upon him even though signed by the drawee in case of need himself.

An acceptance by intervention or for honor must so specify and be written upon the bill itself or a copy and must be signed by the intervener. A limited acceptance for honor is considered a refusal to so accept. The acceptance must also designate the party for whose honor or upon whose behalf it was given; and if the name of the party in whose behalf it was given be omitted, acceptance will be deemed to have been made on behalf of the drawer and proof to the contrary is inadmissible.²⁹

The acceptor for honor must obtain the protest for nonacceptance by the original drawee (paying the cost thereof) and must have his acceptance noted. Within 2 days after the protest has been taken he must mail the protest, together with a notice of his intervention, to the party for whose honor he is accepting or he will be liable for damages caused by the omission so to do.

The acceptor for honor is responsible to all endorsers who follow the party on whose behalf his acceptance was made, but this liability is extinguished if the bill is not presented to him for payment at the latest on the third business day after the date upon which payment should be made.³⁰

When a bill is accepted for honor by a drawee in case of need, it extinguishes the rights of successors to the party for whom he accepts to move for security for nonacceptance or nonsecurity; but the party for whom he honored the bill (or his predecessors in title) may move for such relief, although the acceptor for honor has no such right.³¹

²⁷ W.O. 56.
²⁸ W.O. 57.

²⁹ W.O. 59.
³⁰ W.O. 60.

³¹ W.O. 61.

RECOURSE FOR SECURITY OR NONACCEPTANCE

If acceptance is refused or is limited other than as to amount, after protest for nonacceptance but before maturity of a bill, any or all of the endorsers and the drawer can be forced, by suit in the competent court, to furnish security that the bill or the balance of the amount not accepted will be paid on the due date. Parties so liable may deposit such security in court or with an institution empowered to receive it, and the holder of the bill acquires a lien upon the deposit. This security is for the benefit of all successors of the depositor and is returned only (a) on subsequent acceptance (with repayment of costs), (b) if no suit is brought for payment against the depositor within 1 year from the maturity of the bill, (c) if the bill is paid, or (d) if it loses its effect by failure to protest for nonpayment or otherwise.³²

A holder of a bill has the same remedy when the financial condition of the acceptor is in doubt, but only where (a) bankruptcy is commenced against him or he suspends payment, or (b) execution against his property is returned unsatisfied. In such cases, the demand must be made and suit instituted first against the acceptor or acceptors (if one of them be in bankruptcy or be insecure financially, the security can be first demanded of him only); and after failure by the acceptors to so deposit, the holder may proceed against the endorsers and drawer on proof of such protest and such failure.

PROTEST

Protest is a solemn act required by law to preserve rights. Where not waived, it cannot be replaced by any other method of proof; and where necessary, it can be excused neither by accident nor even by vis major. Any holder may protest for nonacceptance, for nonsecurity of the acceptor, or for nonpayment.

The advisability of protest for nonacceptance or nonsecurity of the acceptor indicates the almost imperative necessity of presenting a bill for acceptance as soon as it comes into one's possession; for unless a holder present for acceptance and thereafter protest for nonacceptance, he acquires no right to demand security from the drawer and endorsers for payment of the bill at maturity. However, where a bill originates in the United States, presentation and protest become a necessity, inasmuch as under American law the right of recourse against drawers and prior endorsers may be lost through delay. In the United States presentation must in all cases be made within a reasonable time.

FORMALITIES OF PROTEST

Every protest must be made through (1) a notary, (2) an official of the court empowered so to do, or (3) a postal official. The last-named is restricted in his authority and cannot act (a) for nonpayment in amounts over 800 marks, (b) where the bill is in a language other than German or (c) for foreign currency "in specie", (d) on bills which contain names of referees in case of need or acceptors for honor, and (e) bills in several parts.

³² W.O. 25, 27; B.G.B. 232-240.

Every protest must be noted on the bill itself or on a paper annexed thereto with the notarial seal at the point of attachment, and must contain (a) the name of the party for whom made; (b) the name of the party against whom made; (c) statement that the party against whom made has been requested to pay, has not been found, or his residence or business not found or closed; (d) statement of place where and date when he was requested to pay or the attempt was made therefor; (e) when accepted or paid for honor, a statement of for whom and how it was done; (f) in protest for nonacceptance or nonsecurity, statement of the particulars, together with legitimization (chain of title); and (g) in protest against a dead party, the fact of his death, and where he died. It must be signed by the protesting officer and bear his official seal and be completed in the period allowed for protest.

The protesting official must have all the documents before him, which he will return to the holder of the note, together with a copy of the protest.

Protest must be made in the place where the bill, according to its terms, is to be paid. A domiciled bill must be presented for payment at the specified place and protested against the party nominated.

NECESSITY OF PROTEST

Protest for nonacceptance or nonsecurity does not excuse any holder from protest for nonpayment, because the drawee may accept at any time before maturity or before protest for nonpayment or within the time in which to do so, and without protest for such nonpayment there would not be proof available that he had not been willing to pay.³³

Protest for nonpayment may be made on the day of maturity and must be made at the latest on the second business day thereafter. It is a generally accepted rule that protest for nonpayment should always be made to preserve rights and obtain proofs against all parties liable. Presentment and protest for nonpayment, however, are not necessary to hold the acceptor.³⁴

The holder of a protested bill must give his immediate predecessor notice in writing of the dishonor, by mailing such notice within 2 days of the date of protest, and each party receiving such notice must give his predecessor like notice within an equal period. (An endorser without recourse need not be notified, and the notice is sent to his predecessor.) Failure to give such notice makes the failing party liable to his predecessors for the damage caused by his omission, but the right of recourse of the preceding parties is not lost thereby. Any endorser who negotiates a bill without adding his address to his signature need not be given notice, but notice must be given to his predecessor.³⁵

WAIVER OF PROTEST

The death of the drawee or the fact that he has gone into bankruptcy does not excuse any holder from protest for nonpayment; and

³³ This question is not completely covered by the law but is interpreted from arts. 25 and 23 read together.

³⁴ W.O. 44.

³⁵ W.O. 45, 47.

if protest is not effected, the endorsers and their guarantors, but not the drawer or acceptor, are discharged.

A waiver of protest may be made by any party liable to recourse and may be oral, but the party so requesting must assume the burden of proof if punctual presentation is denied. The holder may refuse such request and protest, collecting the expenses and costs therefor notwithstanding.

PAYMENT

TIME OF PAYMENT

On bills of exchange, the date of maturity must be certain, and payment of the whole amount is due at that time. The statement of the due date may be given in one of five forms:

1. A definite day—generally a date on the calendar (for example, December 31, 1932, or 31 XII 32, or the last day of December 1932, or Saint Sylvester day, or the first Sunday after Whitsun). If a definite day is fixed in a bill as the date of payment, payment must be made and maturity occurs on that date.³⁶ Bills drawn in a country using the old-style calendar are presumed to be dated according to it; and, when brought into Germany, all such dates appearing on the bill are translated into dates under the new calendar (which is used in Germany) for further interpretation under the German law.

2. At sight: This makes the bill due immediately upon presentation to the drawee.³⁷

3. At a certain time after sight: Presentation fixes the time at which the period specified after sight begins to run.³⁸

4. At a certain time after date: Date of drawing fixes the time in this case from which the period specifies begins to run.³⁹

5. Fair or market bills: These mature at the time fixed by law where the market is held; if none is fixed, the day preceding the legal termination of the fair or market.⁴⁰

INTERPRETATION OF DATES

If a certain time after date or after sight is specified, the period starts to run from the date of the bill or presentation, as follows: If the period is in days, on the last day of the period (day on which drawn is not counted); if the period is in weeks or months, on the day of the week or month corresponding to the day of drawing or, if there is no corresponding day of the month, on the last day.⁴¹

If the middle of the month is specified, it is the fifteenth day; if the beginning or end of the month, it is the first or the last day.

“Half month” means 15 days; and where 1 month or several months and a portion of a month are specified, the portion of a month must be figured last.

No days of grace are allowed in Germany, but where a bill is payable abroad days of grace allowed at the place of payment are recognized.⁴²

If the day upon which payment is to be made is a general holiday, payment must be made on the next succeeding business day.

• W.O. 30.
• W.O. 31.
• W.O. 19. 32.

• W.O. 34.
• W.O. 35.

• W.O. 32.
• W.O. 33.

If at the place of payment there are general pay days, a bill falling due between them need not be paid until the next succeeding one (unless "at sight"), but it may be protested meanwhile.

Further definitions of periods are given under "Prescription" in the Civil Code.⁴³ (Prescription is discussed herein at pp. 206 to 208.)

PAYMENT DETAILS

A bill must be presented for payment at the place appointed in the bill; and if such a place is not fixed, it is presumed to be the residence of the drawee.

A matured bill must be presented for payment on the due date to the drawee even though he refused to accept it when previously presented for acceptance. If the drawee refuses to pay, then the holder must protest.

After maturity and protest, any person liable may pay the bill and in so doing is not required to investigate the genuineness of the endorsements. Such person may demand delivery of the bill and the protest. If refused, he may deposit the money in court.⁴⁴ If several offer payment, that one is preferred whose payment would release the most parties.

Part payment may not be refused even by the protesting official, who is empowered, as is any holder, to give a receipt therefor and endorse the payment on the bill. If part payment is refused, endorsers are released to the amount of the offer.⁴⁵ If the bill is paid in full in addition to costs, expenses, and commissions, it must be surrendered.

If payment is not demanded at maturity, the debtor may, without notice to anyone after the time for protest has expired, deposit the amount in court or with an institution authorized to receive it, and the risk and costs thereafter are for the holder. Such deposit cannot be returned (even if it later becomes a part of the debtor's bankrupt estate) until it remains unclaimed for 30 years from the date of deposit.⁴⁶

AMOUNT AND CURRENCY

Amounts stated in a bill in foreign coinage may be paid in marks at the market value unless expressly provided to be paid "in specie."⁴⁷

If the amount stated in the bill is in letters and figures and they differ, the amount in letters governs. If the amount is in figures only or in letters only and is variously repeated, the amount which is smallest governs.⁴⁸

A holder who protests for nonpayment is limited to receive in payment the amount of the bill plus interest at 6 percent, the costs of protest and other expenses, and a commission of one third of 1 percent.⁴⁹

A subsequent endorser who takes up the bill is entitled to the sum paid plus 6 percent from date of payment, his expenses, and a commission of one third of 1 percent.⁵⁰

Any holder may draw a new draft at sight for the amount of his claim, adding thereto the cost of negotiation and stamp duty; if it is not paid, these costs can be added to the original amount due.⁵¹

⁴³ B.G.B. 187-193.
⁴⁴ B.G.B. 293-304.
⁴⁵ W.O. 38.

⁴⁶ B.G.B. 373-382; W.O. 40.
⁴⁷ W.O. 37.
⁴⁸ W.O. 4.

⁴⁹ W.O. 50.
⁵⁰ W.O. 51.
⁵¹ W.O. 53.

PAYMENT BY INTERVENTION OR FOR HONOR

If a bill of exchange has been accepted by a third party (drawee in case of need), such acceptor is bound to the payment of the bill.

If a bill of exchange is not paid by the drawee or any other party designated to do so, it may be paid by a third party not mentioned in the bill itself, and such payment is known as payment by intervention or for honor. If the holder refuses an offer of payment for honor, he loses recourse against the successors of the party for whose honor payment is offered. If, however, the holder accepts the offer of payment for honor, the payer is subrogated to the rights of the party for whom he pays. So if such intervener has made payment on behalf of the drawer, all endorsers are discharged; and if he has made payment on behalf of a particular endorser, all subsequent endorsers are discharged.

At maturity, the bill, even though it has been protested for the nonacceptance of the drawee and has been accepted by a third party, must be re-presented to the drawee for payment and protested for nonpayment before it can be presented for payment to the third party who accepted it. In such case, if the drawee wishes to pay, payment must be accepted from him in preference to the third-party acceptor, provided the drawee is willing to pay the expenses incurred in connection with the protest for nonacceptance. An acceptor for honor, even though he is never called upon to pay, has a claim for commission of one third of 1 percent from the party who does pay.⁵²

At maturity, after presentation and refusal of payment by the drawee and protest therefor the bill, together with such protest, must be delivered to the intervener upon payment by him.⁵³

When several interveners offer to pay a bill, preference should, but need not, be given to the one whose payment releases the greatest number of parties to the bill. Where intervention is allowed to one intervener when better releases could be obtained, the endorsers between the intervener selected and the intervener rejected are also released.⁵⁴

LIABILITY OF THE PARTIES

Drawer.—The liability of the drawer of a bill as a principal obligee does not depend on protest.⁵⁵ He guarantees to any holder that the instrument will be accepted and paid, and if it is not he is jointly and severally liable with all the other parties to the bill.⁵⁶ He seems, under German law, to have the power to revoke a bill (but only in the hands of the party receiving it from him) before acceptance; but if the drawee disregards the revocation and accepts the bill, the drawer's attempt at revocation is not considered. His liability when extinguished by limitation remains in favor of the holder alone, but only to the amount that the drawer would be enriched at the holder's expense.

⁵² W.O. 65.

⁵³ W.O. 63.

⁵⁴ W.O. 64.

⁵⁵ Where, however, a bill is drawn in the United States and transferred to Germany, protest will be necessary to hold the drawer because the law of the country where the bill is delivered governs the transaction, and American law requires that protest of a foreign bill must be effected to hold the drawer.

⁵⁶ W.O. 8, 61.

Drawee.—The liability of the drawee arises only on acceptance and is similar to that of the drawer in that it does not depend upon protest. Where the drawee's liability is extinguished by limitation, he remains liable to the holder alone and only to the amount that he would be enriched at the holder's expense. The defense of forgery is not allowed to him, as acceptance of the bill admits the genuineness of the drawer's signature.

Endorser.—All persons signing a bill of exchange as endorsers without limitation are alike liable. Fulfillment by one of them subject to recourse releases those who signed contemporaneously with or subsequently to him. Whenever an endorser takes up a bill, he may cross out his endorsement and those of his successors.⁵⁷ Any debtor on a bill may interpose in a suit thereon only those defenses that arise from the bill of exchange law or that he may himself have against the party claiming from him. Where the liability is extinguished by limitation, no claim remains in the holder of a bill against an endorser.

Holder.—A holder of a bill dishonored upon presentation for acceptance and protested can force the indorsers and the drawer jointly and severally to post security for payment of the bill at maturity. The same remedy is given to a holder when the acceptor has gone into bankruptcy, or has suspended payment, or has had an execution against him returned unsatisfied.

At maturity a holder of an unpaid bill may sue⁵⁸ and exhaust his remedies against all, some, or one of the parties liable to him according to his own choice and without losing his rights against the others. He may even attempt to use several remedies simultaneously.⁵⁹

The holder of a lost or destroyed bill may make a motion for extinction in the court of the district where payment is to be made, and in the meantime demand payment of the bill if he deposit security until the bill is declared extinguished by the court. If he does not deposit security, he can only demand that the amount due be deposited with the court or an institution empowered to receive such deposits.⁶⁰

The holder of a bill who can prove chain of title can be made to surrender up the bill by one who can prove former ownership of it only when such holder obtained it in bad faith or was guilty of gross negligence in its acquisition. Good faith is satisfied if he took it so; and gross negligence arises only by obvious forgery or omission to satisfy himself as to the identity of the holder.

COURT ACTIONS

Suits on bills of exchange are regulated⁶¹ and the jurisdiction in which they must be brought is fixed⁶² by the civil practice act. When suits are brought the defenses to the bill itself are (a) absence

⁵⁷ W.O. 55.

⁵⁸ A bill must have been presented, presentation and default substantiated by protest, and legitimization (chain of title) established in a holder to enable him to secure payment by suit (W.O. 41-56).

⁵⁹ W.O. 49.

⁶⁰ W.O. 73; see also Z.P.O. 946-958, 1003-1018.

⁶¹ Z.P.O. 110, 538, 592-605, 708.

⁶² Z.P.O. 603.

of essential formality,⁶³ (b) prejudice if protest is necessary to maintain rights,⁶⁴ (c) limitation,⁶⁵ (d) payment⁶⁶ or receipt, (e) deposit,⁶⁷ (f) bill declared extinguished,⁶⁸ (g) lack of capacity of defendant,⁶⁹ (h) absence of authority,⁷⁰ (i) falsification of name or forgery,⁷¹ (j) exclusion of liability by endorsement,⁷² and (k) signature under duress; and the defenses allowed between the parties who dealt personally are (a) absence of consideration, (b) renewal promised, although not in the bill itself, (c) failure of consideration, (d) illegality of consideration, (e) accommodation signature, (f) account current disputed, (g) signature only for giving security, (h) fraud, mistake, or duress, and (i) payment.

BILLS OF QUESTIONED VALIDITY

To maintain negotiability of bills, the fact that they contain false or forged signatures or signatures of parties who lack capacity or who may not even exist does not invalidate the instruments for the other parties thereto.⁷³ (As to lost bills, see "Holder", on p. 164 preceding.)

Signatures made by crosses require attestation by a court or notary; illegible signatures do not.

A person of limited capacity is not bound on a bill, but an agent who signs without authority is personally liable except to those who knew or should have known of his lack of authority; and his principal is not bound by his signature. If an agent is sued, he has the burden of proving his authority.

A bill which is altered is good against all parties thereon, but only in accordance with the terms of the bill existing at the time each became a party.

BILLS IN A SET

The drawer of a bill of exchange in a set must allow to the payee, on demand, the duplicate parts thereof. Such bills must be designated in their context as first, second, third, etc. Otherwise each is regarded as an independent single bill. An endorsee can also demand the duplicate of the bill from his immediate predecessor, on which all the existing endorsements shall be repeated. These requests of endorsees for duplicates must be referred to the drawer, who is the only party with the right to draw duplicates. Anyone, however, may make a copy of a bill; but such copies, when made, are not valid unless there are original endorsements contained thereupon.⁷⁴

If one of several duplicate bills is paid, the others lose their force; but there remain liable upon the other parts (a) endorsers prior to the party paying and (b) acceptors on parts of the duplicate bills

⁶³ W.O. 4, 9.

⁶⁴ W.O. 41.

⁶⁵ W.O. 77-79.

⁶⁶ W.O. 39.

⁶⁷ W.O. 40.

⁶⁸ W.O. 73.

⁶⁹ W.O. 1.

⁷⁰ W.O. 85.

⁷¹ W.O. 75-76.

⁷² W.O. 14.

⁷³ W.O. 8, 75.

⁷⁴ W.O. 66, 70-71. Bills in a set are uncommon except in troublous times.

not given up upon payment. A party who sends away one of several parts of a bill for acceptance must note upon the remaining parts where such part is to be found. Failure to do this, however, does not deprive the bill of its force.⁷⁵

LIMITATIONS

All claims on a bill against the maker or acceptor are barred 3 years after maturity.⁷⁶

The right of a holder or endorser to recourse against the drawer or preceding endorsers is barred (1) in 3 months if the bill is payable in Europe, (2) in 6 months if payable in coast countries or islands of Asia or Africa, and (3) in 18 months in any other country.⁷⁷ These limitations begin to run, as to the holder, on the day of protest or, if protest is waived, from the last day allowed for protest; and as to the endorser, from the day he pays without suit or, if sued, from the day he is served.

CONFLICT OF LAWS

In Germany the capacity of a foreigner to become a party to a bill is determined by his nationality and not by his domicile; but he is also held in Germany if he is capable under German laws of undertaking the liability.

The requisites of a bill drawn abroad or signed abroad are those of the law of the place where the contract is made or the act is done; but if the bill conforms to German requirements it is legal. The place where a foreigner incurs the liability is the criterion and not the residence of the debtor or the place of payment. Transactions of Germans abroad with other Germans are good if they comply with German law.⁷⁸

The methods used in the necessary proceedings to preserve or exercise rights in a bill drawn or accepted abroad (e.g. presentation, protest, notice, and days of grace) are governed by the law in force at the place the act occurs.

STAMP DUTY

All bills of exchange are subject to stamp duty except (1) foreign instruments drawn and payable abroad and (2) bills drawn in Germany on a foreign country and payable abroad at sight or 10 days from drawing and transmitted abroad directly by the drawer. Bills which mature more than 3 months after the date drawn must have extra stamps. Where there are duplicate bills, stamps are necessary only on the original unless original endorsements appear on the duplicates, in which case they are considered originals. (For stamp tax on negotiable instruments see p. 68.)

PROMISSORY NOTES

The law of promissory notes is similar to that of bills of exchange insofar as similarity is not precluded by inherent difficulties. The distinction is mainly in the formal requirements in the two instru-

⁷⁵ W.O. 87-88.

⁷⁶ W.O. 77, 100; for interruptions of this period see B.G.B. 202-222.

⁷⁷ W.O. 78-79.

⁷⁸ W.O. 84, 86.

ments and in the fact that acceptance and protest are not required on a promissory note. In other respects the law of promissory notes may be said generally to follow, article for article, that of bills of exchange.⁷⁹ In view of the comprehensive treatment accorded bills of exchange in the pages immediately preceding, a detailed discussion of promissory notes is not deemed necessary.

A promissory note must contain (1) a self-contained description as a note, (2) the sum of money payable, (3) name of the party to whom the maker will pay, (4) time when payment will be made, (5) signature of the maker, and (6) place and date of making.⁸⁰

Stamp duty must be paid on promissory notes as on bills of exchange.

CHECKS ^a

Until 1860 checks were entirely unknown in Germany, whereas in England there was a highly developed use of checks for business. The German law on checks resulted from agitation by merchants, chambers of commerce, the press, and legal authors for the adoption of this facile method of transferring moneys and credits enjoyed in England.

Only gradually did checks come into use in Germany, and at first they were used only as a means of transfer of payments and not as a general method of exchange. In 1892 the first draft of a check law was submitted for consideration, but nothing was done until Austria in 1906 passed its laws relating to checks. Thereafter Germany seriously took up the codification of its own check law (*Scheckrecht*) and embodied this law in its code (*Scheckgesetz*) of 1908.

The law of checks is the same as for bills of exchange as to (1) presentation and protest,⁸² (2) request not to protest,⁸³ (3) checks in parts, (4) letters and figures,⁸⁴ (5) obligation to notify preceding holders of claim by way of recourse and their right to take up checks and power to strike out endorsements,⁸⁵ and (6) stamp duty.

REQUISITES

In Germany checks, like bills of exchange and promissory notes, must meet certain prescribed requirements without which they are not negotiable instruments. There must appear on the face of a

⁷⁹ W.O. 98.

⁸⁰ W.O. 96.

^a The League of Nations invited both signatory and nonsignatory countries to an international conference to discuss unification of the law on bills of exchange, promissory notes, and checks. This conference resulted, in February 1930, in certain recommendations, pursuant to which, in December 1932, a new check law was proposed to the Reichstag. If this new law is adopted and accepted into the German law, notice to that effect will appear in the Legislative News Bulletin and in Commerce Reports, published by the Bureau of Foreign and Domestic Commerce, Washington. The following are some of the important proposed changes in the present law:

(1) A check may not be drawn on the drawer himself unless by one establishment against another belonging to the same drawer.

(2) The defenses allowed to a drawer of a check against the holder are curtailed, in that personal defenses between the parties are ruled out.

(3) Presentation of checks in Germany is reduced from 10 to 8 days, and for foreign checks reduced to 3 weeks or 1, 2, or 3 months, according to distance.

(4) Provision is made for the "crossing" of checks (as in England), both generally and specially. A check crossed generally can be paid only to a banker or customer of the drawee; one crossed specially can be paid only to a named banker or, if he is the drawee, only to his customer.

(5) Actions for recourse on checks payable in Europe will be barred after 6 months.

⁸¹ W.O. 87-88, 90-91.

check (a) a statement (in the body of the instrument) that it is a check, (b) a direction by the drawer to pay to the payee a certain definite sum out of the property of the drawer in the hands of the drawee, (c) the signature of the drawer in writing below the complete text,⁶⁶ and (d) a statement of the place and date of drawing.

Where forms are supplied by the bank in which the drawer has his property or funds, these forms should be used. Although not provided in the law, some banks refuse, by custom or by particular understanding with their depositors, to honor checks not drawn on their own forms.⁶⁷ Check books are very carefully guarded in Germany.

Checks may only be drawn against banks or savings institutions organized under German law for that purpose and entered in the appropriate registries and subject to the German law of merchants embodied in the Commercial Code and the bank law. Instruments purporting to be checks drawn on others than the foregoing are bills of exchange. Checks payable abroad, however, may be on a drawee against whom checks may be drawn according to the law of the country where payable.⁶⁸

The limitations on legal capacity to draw a check are the same as those imposed upon the drawer of a bill of exchange.

Only one drawee may be named, who may also be the drawer. The drawee's name need not be mentioned in the text, the address being sufficient; but such name must appear somewhere on the face of the check.

Checks may be drawn payable to bearer, to oneself, or to several payees together or in the alternative.⁶⁹ Since the instrument must contain a statement that it is a check, it is presumed to be "to order" unless otherwise expressly stated. In "not to order" checks the payee alone acquires rights. A payee may become a holder or an endorser.

Checks to a payee of limited capacity are valid, but the claim attempted to be satisfied thereby is not liquidated.

ENDORSEMENT

A check drawn to a definite payee can be transferred by endorsement unless the drawer has forbidden it by the words "not to order", or words of similar import. The limitations on legal capacity to endorse a check are the same as for bills of exchange, and, generally speaking, the legal rules applying to endorsements of bills of exchange apply also to checks, but endorsements on copies of a check are invalid. Endorsement to a drawee is a receipt only, and a drawee cannot endorse in any manner. If he does so it is disregarded.⁷⁰

Parties whose signatures are genuine remain liable on checks on which the signature of the drawer or of an endorser is forged.⁷¹

⁶⁶ The name of the person drawing the check must be signed by him, although that of the firm for which he signs may be printed or stamped.

⁶⁷ S.G. 1.

⁶⁸ S.G. 2, 25.

⁶⁹ S.G. 4.

⁷⁰ S.G. 8, 10.

⁷¹ S.G. 23.

Bearer checks cannot be endorsed, and endorsements on them have no effect. They are transferred by delivery.⁹² The holder need not prove the chain of title and can only be confronted with the defense of unlawful possession.

Certification.—The custom of certifying checks, so common in the United States, is unknown in Germany, and such action by a bank would be invalid as such; but a written statement by the bank that the drawer has, in its hands, the property referred to in the check would render the bank liable. Nor may a check be accepted or in any manner endorsed by the drawee; and if it is such acceptance or endorsement will be disregarded.⁹³

PAYMENT

TIME AND PLACE OF PAYMENT

A check is payable at sight; one in other terms is not a check but merely an instruction. The address given on the face of the check is the place for payment, and if any other place is named it is disregarded. If no place is mentioned, the place of drawing is considered to be the place for payment. The "pay offices" printed on the back of checks are not significant (even when branches of the drawee bank); neither protest nor presentment can be made there. At best the list is only information that the offices named will collect the check without charge. Presentation, however, to a clearing house in which the drawee is represented and in the city where the bank is located is valid.⁹⁴

Under the Scheckgesetz post-dated checks were valid, but were subject to stamp duty⁹⁵ and treated as bills of exchange. They could not be paid before the purported date of issue, as in the meantime payment might be stopped. In 1930 the law was amended, and a post-dated check is now considered as issued on the day of presentation if presented prior to the day stated on the check, and it may be paid when presented. If no funds are available, a declaration of nonpayment must be executed on request.

PERIOD FOR PRESENTATION

Checks drawn in Germany and payable there must be presented at the place of payment within 10 days from the date of drawing. If the last day be a Sunday or a holiday, presentment must be made on the next succeeding business day. Checks drawn abroad payable in Germany must be presented within 3 weeks if drawn in Europe, within 2 months if drawn in North America, and within 3 months if drawn elsewhere. Checks drawn in Germany and payable abroad must be presented according to the law of the country where payable.⁹⁶

Expiration of the time for presentment of checks does not invalidate a check but affects it only in the following respects: (1) Recourse is conditional on timely presentation and protest (if the bank fail, the holder can only recover in the bankruptcy); (2) until the period for presentation runs, the drawee may ignore revocation (stopping of payment).

⁹² B.G.B. 932-935.
⁹³ B.G.B. 824; S.G. 10.

⁹⁴ S.G. 5, 7, 12.
⁹⁵ S.G. 29.

⁹⁶ S.G. 11.

RECOURSE

Recourse on checks is similar to that on bills of exchange. A party liable is only bound to pay upon delivery of the check and the documents which prove its presentation, dishonor, and protest. If these documents are not demanded at the time of payment, the right to demand them is lost. If a check is lost or destroyed, its delivery can be omitted, but only after court action to establish its loss and the public proclamation ordered by the court. Meantime the holder can demand payment upon giving security until the check is so declared void.⁸⁷

To enforce the right of recourse the holder must prove that the presentation of the check was timely and that the check was not paid or that presentation was attempted in vain, by (a) a statement on the check signed by the drawee giving the date of presentation, (b) a certificate of the clearing house that the check was presented to it before expiration of the period for presentation and not paid, or (c) by protest.⁸⁸

The holder of a check that has not been paid must mail notice of nonpayment to his predecessor within 2 days after preparation of the declaration certificate or protest, and every endorser in turn must notify his predecessor in the same manner. Civil suits on claims under the check law are heard before the commercial side of the court in the place where payment should have been made or where the defendant has his domicile.⁸⁹

RIGHTS AND LIABILITIES OF THE PARTIES

Drawer.—The drawer is jointly and severally liable with the endorsers for payment. He may prohibit payment in cash by writing “for account only” or a similar expression on the face of the check. It is fraud for any party to a check to negotiate it if he knows it is not covered, and this is true of the drawer even if he claims the amount is due from the bank and the bank disputes it.¹

A claim for recourse against a drawer is barred after 3 months if the claimant is in Europe and after 6 months if he is elsewhere, but it is absolutely barred in 1 year from the date of the check.²

Drawee.—A bank has a lien on all the property deposited with it for every claim it may have against the depositor even for claims and set-offs not yet due. By its relations with the depositor it enters into a contract to obey his instructions given in the form of checks, subject to the ordinary safeguards and insofar as it has his property to cover his instructions. A check drawn for a larger amount than the depositor’s account need not be paid in part.

A bank is not liable if it pay a check drawn by one deceased or by one who in the meantime loses legal capacity or without notice if the drawer becomes bankrupt.³

⁸⁷ S.G. 19, 22.

⁸⁸ S.G. 16. As to presentation and protest, arts. 87–91 of the bills of exchange law apply; presentment of checks must be proved by documents and not by witnesses or oaths. Requests not to protest are covered by art. 42 of the bills of exchange law.

⁸⁹ S.G. 27–28; Z.P.O. 603.

¹ S.G. 14–15.

² S.G. 21–22.

³ B.G.B. 647.

A bank need not accept revocation (order to stop payment) of a check by the drawer until the period for presentation has expired, but a check "for account only" is revocable at any time. After the time for presentation has elapsed the bank must not pay a check if requested not to do so by the drawer, and even before that time if it so contracts with the depositor.

A bank may not pay in cash a check marked "for account only" (zur Verrechnung) across its face. It can only transfer from account to account.

Where the drawer's signature is forged or the content of a check is altered, the holder's right to recover depends on whether the bank is connected with the drawer or the alleged drawer.

When the bank pays, it is entitled to the check, and it may pay any check any time, even after expiration of the period for presentation, unless payment has been stopped.⁴

Endorser.—An unlimited endorser of a check is, jointly and severally with other endorsers and the drawer, liable during the proper time for presentation for payment to all subsequent holders. He may, however, limit his endorsement by adding thereto "without guaranty" or similar phrase and thereby preclude the right of recourse against him. He may also prohibit payment in cash by the drawee if he endorse across the face of a check "for account only."⁵

Claims for recourse by a holder against an endorser are barred in 3 months if the claimant is in Europe and in 6 months, if he is elsewhere, from the time the holder should have presented it for payment. Claims for recourse by one endorser against a prior endorser are barred in a like period from the time the claimant paid or from the date of commencement of action against him.⁶

Holder.—The holder of a check, if he make timely and proper presentation, is entitled to recourse against all previous unlimited endorsers and the drawer. As with a bill of exchange, the holder of a check may sue all persons liable or any of them for the whole amount of the claim without losing his claim against those not sued. If, however, the holder has not presented the check on time and before it is extinguished by limitation, he loses his right of recourse and may proceed with the collection of the claim only against the drawer, who is liable, however, only to the amount he would be enriched at the holder's expense. Even this claim is barred 1 year after the date of the check.⁷

CONFLICT OF LAWS

Checks drawn abroad, if they satisfy the requirements of German law, are valid in Germany. If they do not meet the German requirements, their validity and the liability of a person becoming a party to them depend upon the law of the country where issued or where such person became a party.

STAMP DUTY

The law of stamp duties embodied in the bills of exchange law is reiterated in the law of checks⁸ and provides that checks are not subject to this tax except when drawn abroad.

⁴ S.G. 13.
⁵ S.G. 14-15.

⁶ S.G. 20.
⁷ S.G. 15, 18, 21-22.

⁸ S.G. 29.

POSTAL CHECK REGULATIONS

In an appendix to the check law there were added regulations (Postcheckordnung) which constituted the German post office an agency for the transfer of small amounts between merchants and for the use of persons not having bank accounts.

Upon application to the post office any person or business in Germany is entitled to participate in this postal transfer system. An account can be opened upon depositing 100 marks, and the total amount is not limited. The money is subject to the depositor's withdrawal for himself or for payments to others in sums up to 10,000 marks.

A depositor is given a post check number, which thereafter is unchanged and in which he acquires a distinct right. This post check number is written on all the bills and correspondence of the depositor and serves as notice to others with whom he deals that remittances may be made by them, either from their own accounts in the post office or by depositing the money with the postman (up to 800 marks) or at the post office, to the credit of that number.

Blanks furnished by the post office to its depositors must be used by them in the transfer of moneys to the accounts of others, as the post office will not accept remittances other than on the forms provided for that purpose.

No fee is collected by the post office for this service, but the transferor must pay 20 pfennige to the issuing post office to cover cost of mailing. A small charge is made when the transfer transactions of any depositor exceed a certain number in any year.

VIII. BANKRUPTCY AND ARBITRATION

BANKRUPTCY

In Germany bankruptcy is governed by a special law, the Reichskonkursordnung, originally enacted in February 1877 and later amended. It must be considered together with the Civil Code (Bürgerliches Gesetzbuch) and the civil practice act (Zivilprozessordnung).

Save for certain of its penal provisions it is applicable alike to merchants and nonmerchants, and in this respect it differs from the other German codes, which distinguish between mercantile and non-mercantile matters.

KINDS OF BANKRUPTCY

Bankruptcies may be fortuitous, culpable, or fraudulent. They are fortuitous when the bankrupt is blameless. The law realizes that in business relations some must fail, and it furnishes a method of so treating the liabilities of an insolvent estate as to distribute the losses among the creditors by invoking the general equitable principle of uniform proportionate payment of debts in such fortuitous bankruptcies. It also assists the bankrupt by allowing maintenance for himself and his family out of the assets if he is worthy and blameless.

On the other hand, a bankruptcy is culpable (simple bankruptcy)¹ where the bankrupt is to be blamed for the manner of handling his business affairs, and is fraudulent² where he is criminally guilty of misconduct in the handling of his business against the interests of his creditors; and in both cases the bankruptcy law imposes penalties against him.³

In every bankruptcy the law takes into consideration the extreme nature of the remedy and the finality of the act itself; and since its functioning enters into and affects all types of business and relations, it provides for a very close scrutiny of the act and proceedings in connection therewith by the examination and supervision thereof.

DECLARATION OF BANKRUPTCY

A bankruptcy in Germany may be either voluntary or involuntary; that is, it may be commenced by the filing of a petition either by the debtor or by a creditor.⁴ In the case of a company the

¹ Simple bankruptcy is where the debtor (a) made debts of large sums for extravagance or gambling, (b) to delay bankruptcy, obtains goods on credit and sells them below value, (c) has not kept books carefully or conceals or destroys them, or (d) omitted to draw balance sheets annually (K.O. 240). (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

² Fraudulent bankruptcy is where the debtor (a) conceals or abstracts property, (b) acknowledges debts and transactions wholly or partly fictitious, (c) omits to keep books where under a statutory duty to do so, or (d) destroys or alters his books (K.O. 239).

³ In addition to certain disabilities imposed in simple and fraudulent bankruptcies (as, for instance, the inability to put through a composition or obtain rehabilitation) penal sentences are imposed on such bankrupts and those who compound illegal acts with them (K.O. 239-240).

⁴ K.O. 103.

petition may also be filed by a manager (Geschaeftsfuehrer), director (Vorstand), or liquidator.⁵ It is predicated on the insolvency of the debtor, which is assumed when there is a suspension of payment.⁶ Excess of liabilities over assets is not a good ground for bankruptcy except in the case of a corporation.⁷ The bankruptcy of a partnership implies the bankruptcy of the responsible partners; but the bankruptcy of a partner does not imply the bankruptcy of the firm. In the latter case the share of the bankrupt partner goes to pay his personal creditors and any balance goes into the partnership assets.⁸

The debtor may file a petition when he realizes that his assets are insufficient to meet his liabilities and he is therefore forced to suspend payment. His petition must include (a) a list of his debtors, (b) a list of his creditors, (c) a statement of his affairs generally (which may be filed subsequently), and (d) the petition to the court for relief.⁹

Where the petition is filed by a creditor it must contain a statement of his claim and proof of the debtor's insolvency. It can be objected to only by the debtor.¹⁰

EFFECTS OF ADJUDICATION

The county court in the place where the debtor has his business or, failing such, his domicile has exclusive jurisdiction to undertake the bankruptcy proceedings. The determination upon the petition and all other proceedings thereafter must be conducted under its direction, the rules of civil procedure applying except where varied by the bankruptcy law.¹¹

Immediately upon the hearing and granting of the petition, the court makes an order providing for (a) the appointment of a trustee;¹² (b) the turning over to him of the entire property, papers, books, and estate of the debtor and his wife, and the subsequent management thereof solely by the trustee;¹³ (c) an embargo on all legal process by or against the bankrupt; (d) an embargo against alienation of real property of the bankrupt, with an order for the endorsement of an appropriate notation thereof upon the land registries of such properties;¹⁴ (e) a decree for payment of all outstandings to the trustee;¹⁵ (f) the fixing of dates¹⁶ for the ratification of the court's appointment of the trustee by the creditors at a creditors' meeting and for the filing of claims and examination thereof and the election of a creditors' committee;¹⁷ and (g) an order to those who have property belonging to the bankrupt to turn it over

⁵ K.O. 208. In this discussion of bankruptcy no treatment is attempted of proceedings in respect of inheritances and bankruptcies of administrators. The law on these points may be found in the bankruptcy act, sections 214-236, and the Civil Code, sections 1975-1992 and 2013. See also Schuster, p. 653, sections 536-537.

⁶ K.O. 102.

⁷ K.O. 207.

⁸ K.O. 212.

⁹ K.O. 104.

¹⁰ K.O. 105, 109.

¹¹ K.O. 71-72; Z.P.O. 40.

¹² K.O. 110.

¹³ K.O. 2, 117. Any steps taken by the bankrupt in connection with the administration of his estate thereafter are void (K.O. 6-7).

¹⁴ K.O. 113.

¹⁵ K.O. 6, 8. Payment to the bankrupt after bankruptcy operates to discharge the payer only to the extent that such payment passes into the assets, unless such payment is made without knowledge of the bankruptcy (K.O. 8).

¹⁶ The declaration of bankruptcy also starts prescription periods running, within which transactions of the bankrupt are void or voidable.

¹⁷ K.O. 110.

to the trustee and no one else under penalty of damages for delay or omission.¹⁸ This order must be published by the clerk of the court in the Official Gazette (Reichsanzeiger) and notice thereof given to the mercantile registers.¹⁹

The bankruptcy proceedings embrace the entire property of the bankrupt subject to execution which belongs to him at the time of the commencement thereof; ²⁰ but the court allows the bankrupt anything acquired subsequently or thereafter due to his mental or physical work or any gift.²¹ His person, powers of work, rights as an author, and his civil and trade name cannot be touched; and the court, where the bankruptcy is fortuitous, may also allow the bankrupt maintenance out of the assets during the proceedings.²²

FOREIGN ASSETS AND FOREIGN BANKRUPTCIES

In theory a German bankruptcy embraces property of the bankrupt outside Germany, and indeed it does so affect all such property which the trustee is able to bring under the jurisdiction of the courts; but it is difficult to enforce these rights, especially where the bankrupt himself is neither domiciled in Germany nor has his business or his assets there.²³

The German property of a debtor against whom bankruptcy has been commenced abroad is subject to execution; and, in such case, to institute bankruptcy in Germany it is not necessary to prove his insolvency.²⁴

APPOINTMENT OF TRUSTEE

The trustee is appointed by the court and may be required to give security; but such appointment may be ratified or rejected by the committee of creditors, when formed. Where there are several branches of the business, several trustees may be appointed, each of whom acts independently. The name of the trustee must be publicly announced, and he must be given a certificate of his appointment, which is returned to the court when his duties are at an end.²⁵

His duties are broadly (a) to collect, realize, and distribute the assets and (b) to ascertain the liabilities, all of which duties are performed under the supervision of the court and with the assistance and support of the creditors' committee.²⁶ He represents not only the creditors but also the bankrupt and brings the parties together. He conducts investigations and employs attorneys and accountants. He is paid for his services and is answerable for the due fulfillment of his duties to everyone and must answer for his own misconduct, intentional or negligent, as well as for that of his assistants.²⁷ He is removable by the court of its own initiative or upon motion of the creditors' meeting or committee; and on the termination of his office he must render a final account to the creditors, which thereafter must be deposited with the clerk of the court, together with all the

¹⁸ K.O. 118, 119.

¹⁹ K.O. 111-112, and see also 76.

²⁰ K.O. 1.

²¹ The bankrupt may accept or reject an inheritance or legacy which accrues; but if he does accept, it goes into the assets (K.O. 9).

²² K.O. 129, 132; R.G. vol. 58, p. 169.

²³ K.O. 238.

²⁴ K.O. 237-238.

²⁵ K.O. 78-81.

²⁶ K.O. 83, 88; Z.P.O. 794, 883, 885.

²⁷ K.O. 82, 85; B.G.B. 276, 278, 831.

documents and the comments of the committee, so that all parties may inspect and comment upon same.²⁸

MARSHALING OF ASSETS

After the court has made its order upon the petition as aforementioned, it withdraws as much as possible from the proceedings and allows the creditors, through their committee and under the trustee, to act generally in connection with the ordinary business of the bankruptcy, subject always to review.

Immediately upon his appointment the trustee starts upon his duties to collect and determine the assets. In this connection he decides upon the fulfillment of the bankrupt's incompleting commitments, upon the continuation or the winding up of the business and the release of assets upon which creditors have a right of separation and severance, and the institution of impeachment proceedings.²⁹

For these purposes he first makes a list (with values fixed by experts) of all the property in his possession and prepares an inventory and balance sheet for the court and for the inspection of the parties interested, and to this inventory he may compel the bankrupt to take the oath of disclosure.³⁰

IMPEACHMENT OF ACTS OF BANKRUPT

In collecting the assets, the trustee and the creditors may make application for the restitution of certain property to the bankrupt estate, upon return of the consideration given, by demand and suit under a power of impeachment within 1 year of the commencement of the bankruptcy, if it can be proven that the bankrupt's property was alienated (a) in prejudice of the rights of creditors, (b) for insufficient consideration, or (c) that the other party knew the debtor was insolvent.³¹

Generally, acts within 10 days of the bankruptcy, or within 1 year as between husband and wife or relatives, are particularly open to suspicion and subject to inquiry by the court and impeachment, as are gifts between near relatives made within 1 year (and under certain circumstances, within 2 years).³²

A debtor's transactions may also be impeached even where there is no bankruptcy under the provisions of a code enacted for that purpose (Gesetz betr. die Anfechtung von Rechtshandlungen eines Schuldners ausserhalb des Konkursverfahren).

FULFILLMENT OF INCOMPLETE TRANSACTIONS

The provisions of the appropriate sections of the bankruptcy law³³ affect existing engagements of the bankrupt and provide that the trustee shall be given the choice of fulfillment or nonfulfillment. They do not apply to contracts outside the bankruptcy—for instance, where the debtor has undertaken to convey or assign an article or make some performance which cannot be replaced (as the painting of a picture); but contracts for service or executory contracts generally are included.

²⁸ K.O. 84, 86.
²⁹ K.O. 17-21, 129-130, 132.
³⁰ K.O. 123-125.

³¹ K.O. 29-32, 34-39, 41, 102, 222; Z.P.O. 66.
³² K.O. 31-32, 37, 63.
³³ K.O. 17-28.

Where the trustee refuses fulfillment, the other party has a claim for damages for the loss he has actually suffered, which becomes an ordinary claim in the bankruptcy.⁸⁴ Where the trustee demands fulfillment of such incomplete contracts as are covered, he must declare his intention without delay and make payment in full therefor.⁸⁵

Where the premises are leased to the bankrupt and delivered to him before the bankruptcy, either party may terminate; if not delivered to the bankrupt, however, only the lessor may withdraw. If property is leased by the bankrupt to another before bankruptcy, the lease is irrevocable.⁸⁶

Contracts for services to the bankrupt are terminable upon notice by either party, except that, if the trustee is the one who terminates, the bankrupt estate will be subject to a claim. This is true also of a mandate (agency). The claims of both, when established, become preferred in the bankruptcy.⁸⁷

CLAIMS OF CREDITORS

IN THE BANKRUPTCY PROCEEDINGS

Form and requisites.—The claims of creditors must be filed with the court within the period fixed in the original order (which may be from 2 weeks to 3 months). However, claims may be filed after the time fixed and they are not barred, but the claimants must pay the costs of the hearing thereon. Claims need not be in any specific form and can be filed either in writing direct with the court or even orally with the clerk of the court for entry in the record. When filed they are open to inspection by all parties concerned. A person with a power of attorney may represent one or more claimants for filing as well as in the creditors' meeting. The proof of claim must always set forth (a) the consideration, (b) the amount in marks, and (c) any claim for priorities to which the claimant insists he is entitled.⁸⁸

Foreign creditors have equal rights with German creditors but should immediately give a power of attorney to a person residing in Germany to file the claim and otherwise represent them.⁸⁹

Claims allowed and disallowed.—Claims not yet due are considered to be immediately due, as also are claims subject to conditions subsequent; but claims subject to conditions precedent only give the creditor the right to security. Creditors of bankrupts owning joint property may file claims against each of them for the full amount and proceed on that basis until paid in full by either. Claims for interest after the bankruptcy, for creditors' expenses in the proceedings, fines, and gifts are not allowable.⁹⁰

Procedure.—Claimants or those who represent them may be heard personally, but they need not appear before a meeting of the creditors presided over by the trustee on a day fixed by him upon notice to the creditors. The creditors whose claims are accepted likewise are given an opportunity to be heard on claims of others. The bankrupt also is summoned to attend the hearings to explain how the claims arose, and he must at all times be ready and available to furnish full

⁸⁴ K.O. 26; B.G.R. 258.
⁸⁵ K.O. 17-18, 59.
⁸⁶ K.O. 19-21.

⁸⁷ K.O. 22-23.
⁸⁸ K.O. 138-140, 142.

⁸⁹ K.O. 5.
⁹⁰ K.O. 64-68.

information and is not allowed to leave the jurisdiction without the consent of the court; if he does so or there is fear that he may, he can be imprisoned. Those claims are considered established to which no objection has been made or, if made, is rejected.⁴¹

After discussion of each claim the court must enter the result in the schedule. This entry has the same effect as a judgment. Claimants must establish claims to which there are objections, by suit; and if they are successful in so doing, the schedules must be corrected accordingly.⁴²

OUTSIDE THE BANKRUPTCY PROCEEDINGS

Set-offs.—Entirely apart from the bankruptcy proceedings, creditors who have claims against the bankrupt and against whom the bankrupt also has claims may set them off one against the other and cancel them, without appearing or filing claims in the bankruptcy, by merely giving notice thereof as though such creditors had pledged to cover their claims.⁴³

So long as they are valid, such set-offs are allowed, whether in existence or contingent at the commencement of the bankruptcy, unless they are acquired by the creditor after the bankruptcy or are claims against the trustee.⁴⁴

*Separate satisfaction.*⁴⁵—Not to be considered a part of the bankruptcy proceedings is the adjustment of claims to be paid out of the estate before it is available for the ordinary creditors. These are (a) claims secured by pledge and mortgages⁴⁶ and (b) claims against property held by the bankrupt in joint ownership in which the other owner has the right to have his share set aside.⁴⁷ Those claiming such rights in personal property must, on demand, produce the object for the trustee's inspection and valuation.⁴⁸

*Severance.*⁴⁹—Creditors possessing such right may exert their right of severance of their property from the bankrupt estate in accordance with the general law, without appearing in the bankruptcy proceedings, provided such right be established against the trustee by his acquiescence or by suit.⁵⁰

Such rights arise from (a) claims of merchants sending goods to the bankrupt where the merchandise has not as yet reached him, in which event stoppage in transitu is permitted; (b) claims for merchandise in the possession of the bankrupt under special arrangement or on consignment (see "Consignment sales", p. 112); and (c) claims of the wife of the bankrupt to property acquired by her not with the husband's means.⁵¹

If goods to which the right of severance would apply are no longer in the possession of the bankrupt, the person having this right may

⁴¹ K.O. 95, 100-101, 106, 141, 143-144.

⁴² K.O. 145-146.

⁴³ K.O. 53; B.G.B. 388; Z.P.O. 145, 302, 322, 529.

⁴⁴ K.O. 54-55; B.G.B. 387.

⁴⁵ With regard to separate satisfaction and severance, the trustee has certain rights to determine the validity of the claimants' contentions without forcing claimants into court to prove them, just as he has with regard to the settlement of suits brought by or against the bankrupt before bankruptcy (K.O. 11, 18).

⁴⁶ The trustee notifies the real estate registry and by order of the court has the endorsement of the bankruptcy added, as well as any changes thereafter (K.O. 113-115).

⁴⁷ K.O. 4, 16, 48-49, 51.

⁴⁸ K.O. 120.

⁴⁹ See footnote 45 supra.

⁵⁰ K.O. 43.

⁵¹ K.O. 44-45.

claim the consideration therefor insofar as it is still due, and from the bankrupt estate insofar as it has been paid into the estate after the commencement of the bankruptcy.⁵²

SALE OF ASSETS

There are special rules for realizing on assets in bankruptcy. The trustee can dispose of immovable property by sale at public auction and of assets generally by compulsory or voluntary sale, even if creditors have contractual liens or similar rights. This latter right enables immediate use to be made of a favorable opportunity to dispose of the bankrupt property. The costs of the compulsory realization by the trustee become preferred debts.⁵³

Bankruptcy does not affect the right of realization of a creditor entitled to separate satisfaction. Such creditor must obtain the execution title necessary to realize on a mortgage on land or on a ship either, before the bankruptcy, against the debtor personally or, after it has commenced, against the trustee; and with respect to personal property the trustee, on his motion, may have the court fix a period within which such realization must be sought by the creditor, and only when this period has expired may such trustee proceed to realization by means of execution or sale. An execution creditor before bankruptcy may continue with and complete his execution according to the provisions of the civil practice act.⁵⁴

COMPOSITION WITH CREDITORS

Under the original bankruptcy statute a composition could be effected at any time between the first meeting of creditors and the final distribution of the assets approved by the court. The amendments of 1927 also granted authority to apply for composition to avert bankruptcy under the original rules for composition.⁵⁵ The debtor in the meantime is freed from attachments in execution, suits, and actual bankruptcy. The application on the part of the insolvent debtor for this purpose has to be accompanied by a definite proposition for the payment of not less than 30 percent.⁵⁶ Composition is inadmissible in case of fraudulent bankruptcy.

Composition is the result of the act of the parties and not a judgment of the court, so it can be had only when proposed by all the parties liable. It involves, generally, a partial waiver of creditors' claims and a guaranty of payment by friends of the debtor, but it may involve only an arrangement by which additional time for payment is given. Its objects are (a) that creditors be paid quickly and, possibly, a greater amount than in bankruptcy, (b) that expense of administration be saved, and (c) that debtors be more quickly restored to the free exercise of their earning capacity and the enjoyment and continuance of their businesses.⁵⁷

The court's approval of a composition as well as the sanction of the creditors' committee must be obtained before permission is

⁵² K.O. 46.

⁵³ K.O. 58, 126-127.

⁵⁴ H.G.B. 1147, 1219, 1228, 1233 et seq., 1257, 1268, 1272; H.G.B. 368, 371; K.O. 6; Z.P.O. 814 et seq., 835 et seq.

⁵⁵ K.O. 173-201.

⁵⁶ It has been proposed to increase this amount to 50 percent.

⁵⁷ K.O. 174, 211.

granted the debtor to offer it at an open meeting of creditors, and such composition may be accepted only by a majority in number of those creditors present and three fourths in amount. When so accepted it is good against all creditors and can be set aside only (a) if it does not pay to creditors at least one fifth of their outstanding claims, (b) if the insolvent condition has been brought about by the dishonest or reckless conduct of the bankrupt, or (c) if preference has been given to any creditor.⁵⁸

Upon the acceptance of a composition the creditors must be paid according to its terms, even if it subsequently is set aside because of fraud, preference, or other reason. If set aside, the waiver of creditors' claims is rescinded notwithstanding such payment.

DISTRIBUTION OF PROCEEDS

The bankruptcy law provides three kinds of distribution, namely, preliminary, final, and supplementary, all of which are to be carried out by the trustee. In addition, the trustee may, independently, but with the consent of the court, pay privileged claims duly proven.⁵⁹

Preliminary distribution is made after examination of the claims and as often as there is sufficient cash on hand to do so, but always with the consent of the creditors' committee. However, upon motion, such preliminary distribution may be postponed if a proposal for composition is pending.⁶⁰

Final distribution can take place only when the assets have been fully realized, and then only with the approval of the court.⁶¹

Supplementary distribution becomes necessary only if further assets become available after final distribution. This also requires sanction of the court.⁶²

ORDER OF PAYMENT

Preferred creditors' claims are paid first and in the following order: (a) Preferred claims of the first class (*Masseschulden*), which include (1) claims arising from dealings with the trustee, (2) claims on unfulfilled contracts and engagements, and (3) claims for enrichment of the bankrupt estate without cost; then (b) preferred claims of the second class (*Massekosten*), which include claims for (1) legal costs of common proceedings, (2) outlays incurred in the management, realization, and distribution of assets, and (3) maintenance to the bankrupt. Where the assets are not sufficient to pay all of the above, proportional payments are resorted to in each class when and if it is reached.⁶³

Ordinary creditors' claims are then paid in the following order of priority and also proportionally when a class is reached if assets are insufficient to pay the class in full: (a) Arrears of the last year to servants; (b) government, State, and city burdens; (c) church, school, and insurance payments; (d) doctors, chemists (druggists), and nurses; and (e) all other creditors.⁶⁴

TERMINATION OF PROCEEDINGS

The bankruptcy proceedings are terminated (a) when the estate is not sufficient to defray administration expenses, (b) when a com-

• K.O. 182, 187-188, 193.
• K.O. 61, 167, 170.
• K.O. 88, 149-150, 159-160.

• K.O. 161.
• K.O. 163.

• K.O. 57-60.
• K.O. 61.

position is effected, (c) after the final meeting of creditors to check and confirm the final accounts, or (d) if the debtor obtains the consent of all the creditors thereto; but in any case the discontinuance and grounds therefor must be publicly announced.⁶⁶

All the effects of the bankruptcy herein set forth come to an end upon its discontinuance, and the debtor recovers his right to control and freely dispose of the assets.⁶⁸

ARBITRATION

Arbitration is defined in German law as proceedings leading to the determination of a dispute by a tribunal other than the ordinary court given competency to decide by agreement of the parties.⁶⁷

Proceedings under arbitration grew in popularity gradually but were grudgingly accepted by the courts, even after the enactment of provisions therefor in the civil practice act.⁶⁸ The rules of procedure were so vaguely outlined and so strictly construed that persons of extraordinary experience were needed to conduct the hearings. This led to the formation of courts of arbitration sponsored by trade associations and chambers of commerce. The hostility of the law courts (which jealously guarded their own right to determine disputes) to this procedure was reflected in the attitude of disputants who adopted it, and of commercial circles generally, toward court rulings and the code provisions.⁶⁹

With the wider adoption of arbitration by merchants the courts became more understanding in their rulings, until now there is splendid cooperation between the courts and arbitrators. Trade associations, however, still have their own sanctions for disobedience to awards, the strongest of which is blacklisting.

REQUISITES OF ARBITRATION CLAUSES

The clause in an agreement providing for arbitration need be in no specific form and need contain no specific provisions either as to naming arbitrators or the procedure to be followed by them. An arbitration agreement may be concluded orally or in writing, expressly or tacitly, so long as it fulfills the requirement that it deal with the entire subject matter of the dispute rather than with an element thereof; and it can be had to determine rights, irrespective of whether they are present or future. It may even be provided for by testament.⁷⁰

The matters which properly may be submitted to arbitration in Germany are disputes as to legal rights which would, in the absence of arbitration, be submitted to the ordinary civil courts and in which the parties would have been entitled to compromise. This definition itself removes criminal matters from consideration under arbitration.⁷¹

⁶⁶ K.O. 107, 163, 190, 202, 204-205.

⁶⁷ K.O. 206.

⁶⁸ See article by Dr. Rudolf Kahn in the *Journal of Comparative Legislation and International Law*, vol. XII, pts. 1 and 4, of February and November, 1930; also "Commercial Arbitration under German Law", by Dr. Fritz Huber, in Brochure No. 72 (1930) of the International Chamber of Commerce.

⁶⁹ Z.P.O. 1025-1048.

⁷⁰ The provisions of the code, for example, that every award must be filed in a court of law as a condition precedent for enforcement was in the beginnings of the development of this procedure completely disregarded.

⁷¹ Z.P.O. 1026, 1048.

⁷² Z.P.O. 1025.

Anyone with legal capacity to contract (even a bankrupt) who has a right in and to the subject matter in dispute may be a party to an arbitration. This right is enjoyed by an agent; but a mercantile agent cannot refer a dispute to arbitration without express authority.⁷²

The existence of an arbitration clause in an agreement takes the dispute from determination by the courts, and in such a case they can intervene only when a plea is entered by either of the parties at the beginning of the arbitration proceedings. The court, under such an application, can only determine whether the arbitration clause itself is valid and binding.⁷³

The arbitration clause may waive recourse to the courts, but the parties may never agree to forego the right of appeal to the appellate court unless they provide in the arbitration clause itself for appeal to a higher appeal court of arbitration.

SELECTION OF ARBITRATORS AND UMPIRE

Anyone with legal capacity may act as an arbitrator, except a party himself or his representative in law, such as a director of his business. Administrative bodies also may act. A judge of any court may act, provided the particular judge is not named but merely the court from which one of the judges may be chosen; and when a judge acts he does so in his capacity as a private citizen. Women may act as arbitrators, as likewise may foreigners.

Unless specified to the contrary, it is implied that the reference is to two arbitrators, each party appointing his own. No definite form for appointment is prescribed, but the method of appointment is impliedly agreed upon. Should one party not appoint his arbitrator within 7 days after receiving notice, the other party may apply to the court to make such appointment. The defaulting party loses his right to appoint and must accept the court's selection. The court has no right to appoint the arbitrators where it is agreed that both parties together shall appoint them or where the designation of arbitrators is delegated to a third party.⁷⁴

The same method of appointment is followed if an arbitrator after appointment refuses to act or is guilty of hindering the proceedings or where it is necessary to replace a defaulting arbitrator during the proceedings.⁷⁵

An arbitrator is liable to both parties for intentional breach of duty (malice) or delay or refusal to act after his acceptance. The parties, after selection of the arbitrators, are bound by the decisions of the arbitrators on questions of law, whether such decisions are good law or bad, because by the selection of the arbitrators the parties agree to be bound by the interpretations which they hand down. This is true of all the laws except the special obligatory laws of Germany, which are binding on the arbitrators and must be followed by them.⁷⁶

At any time during the proceedings the appointment of an arbitrator may be revoked upon consent of both parties, and objection

⁷² B.G.B. 1672; H.G.B. 49, 54.

⁷³ Even while a court is determining the validity of an arbitration clause it has not the power to temporarily enjoin the continuance of the arbitration proceedings.

⁷⁴ Z.P.O. 1028-1030.

⁷⁵ Z.P.O. 1031.

⁷⁶ Z.P.O. 1042.

to an arbitrator selected by one party may be made by the other, but only for personal reasons. These reasons are the same as those which can be urged for the removal of a judge—for example, infancy or partiality.⁷⁷ They should be brought to the attention of the court as soon as they are discovered.

Provision for an umpire (Obmann) is not implied nor is the position officially recognized under German law. However, where an umpire is provided for in the agreement he is permitted to act with other arbitrators.

PROCEDURE IN ARBITRATION

It is not absolutely necessary that the parties sign a submission. It is highly desirable, however, that they draw up a memorandum of the subject matter of the dispute and of the duties of the arbitrators for the purpose of record.

In conducting the inquiry under arbitration the arbitrators may make their own rules for procedure, either at the outset or when the contingencies or necessities arise. Their discretion in the making of such rules is not limited unless there is provision therefor in the submission. The only rule of procedure which they must follow is that they must hear both parties or at least give both parties opportunity to be heard. However, if either party does not appear or plead, the arbitrators may continue without him. Arbitrators have no power to compel the appearance of a witness or to administer an oath, but when they or the parties deem it necessary they may ask the courts to do so. The arbitrators may try to conciliate the parties, but a compromise is void if it is against the law or cannot be enforced.⁷⁸

If during the proceedings an arbitrator refuses to continue to act or is unable to do so, or if he unduly delays the proceedings, the submission is declared void unless the parties have provided otherwise in the agreement.⁷⁹

Each arbitrator's vote is equal to that of any other, and if there is an even number of arbitrators the vote may be a tie, in which case it is held there is no agreement and the submission would be revoked.⁸⁰ So it is always advisable to provide for an umpire with the same right to vote as an arbitrator. It is possible to add the stipulation that the umpire should be called upon to vote only where a majority cannot otherwise be obtained.

AWARDS IN ARBITRATION

No general provision is made as to the time in which an award is to be given. However, unreasonable delay may either revoke the submission or cause the removal of the guilty arbitrator.

When an award is made, it is held to have, "as between the parties, the same effect as a valid judgment of a court."⁸¹ It does not bar a new action in the identical dispute, but if pleaded is a complete defense. It binds not only the parties but also persons claiming through or under them, except where one of the parties is or becomes a bankrupt during the proceedings.

The award must be in writing, dated, and signed by all the arbitrators; and signed duplicate originals must be served on the parties.

⁷⁷ Z.P.O. 41-43, 1032.

⁷⁸ Z.P.O. 1034-1036, 1044.

⁷⁹ Z.P.O. 1033.

⁸⁰ Z.P.O. 1033, 1038.

⁸¹ Z.P.O. 1040.

The original, with its proof of service, must be filed with the clerk of the proper court. The award must contain a statement of the grounds upon which the arbitrators base their decision, unless dispensed with by consent of the parties. It should also state the proportion of the costs to be borne by each of the parties unless this is to be decided by a separate proceeding.⁸²

ENFORCEMENT OF AWARDS

The award binds the parties as would a judgment of a court, but is not enforceable (any more than is a judgment) without obtaining a court order.⁸³ In such proceedings upon an award, in order that an execution may be granted the court examines the award only as to form and not as to merits, and the request will be refused only if the award intentionally disregards positive rules of law which the parties could not validly waive or if the formalities as to the substance of the award have not been observed.⁸⁴ Otherwise, the court grants the execution and the successful party proceeds to execution as on an ordinary judgment.⁸⁵

GROUND FOR NULLITY

An award may be set aside if notice for an appeal is served within 1 month of the time that knowledge of an irregularity comes to the party, but in no case will such an appeal be allowed after 10 years.⁸⁶

An award may be set aside (a) if the proceedings themselves are impeachable, (b) if the judgment ordered a performance forbidden by law, (c) if a party was not represented according to law, (d) if a party was not given opportunity to be heard, (e) when the award does not contain the reasons therefor, or (f) if the same judgment in a court could have been set aside.⁸⁷

If an appeal is taken, the court must suspend the order for enforcement of the award until the appeal is decided.⁸⁸

FOREIGN AWARDS

The civil practice act contains no special provision for the enforcement of foreign arbitral awards. Foreign awards may be rendered enforceable, however, by order of the court, provided they fulfill the conditions laid down in that act.⁸⁹ If the foreign award does not fulfill these conditions, but has nevertheless been validly rendered abroad, the winning party may, on the basis of this award, bring an action (Erfuellungsklage) against the losing party before the court, in order that the losing party may be ordered to fulfill his obligation to submit to the award—an obligation arising from the submission to arbitration. The court does not examine the award as to its merits.

⁸² Z.P.O. 1039, 1041.

⁸³ Z.P.O. 1040.

⁸⁴ Z.P.O. 1041-1042.

⁸⁵ An application may also be made upon an award for a declaratory judgment which will determine whether the award is valid or not. This course is pursued, however, only if it is less expensive and more direct.

⁸⁶ Z.P.O. 1044.

⁸⁷ Z.P.O. 580, 1041.

⁸⁸ Z.P.O. 1042.

⁸⁹ Z.P.O. 1039.

IX. INDUSTRIAL PROPERTY

The term "industrial property", little used in the United States, is a convenient term to denote those intangible rights which are the safeguards of business men and the public and which arise from the particular conduct of a particular business. Among these rights are patents, trade marks, trade names, and the right to conduct one's business without improper interference from others, or, generally speaking, unfair competition. Copyrights and other phases of the protection of artistic, literary, and similar effort are not included, these being, in contradistinction, termed "intellectual property."¹

Germany early established a high standard for the protection of industrial property, not alone for its own citizens but for the citizens of the other countries of the world.² As commerce developed, the older rights already existing were supplemented and given new sanctions, and new rights were recognized and added to the body of the law. These intangible rights of industrial property (immaterial Rechte) are in Germany largely the subject of legislative action. Most of the rights are not only embodied in written law but are the basis for penal sanctions.³

THE NEED FOR PROTECTION

Probably the most important subdivisions of industrial property are patents and trade marks, to the necessity for the protection of which attention should be called at the outset. In Germany, as elsewhere, they are the two such rights which require affirmative action to secure protection.

In most countries the first applicant is entitled to registration of a trade mark and to its exclusive use. In all countries an unpatented process⁴ may be utilized by anyone. The loss of the right to such article or process will usually impose a serious handicap in markets where these rights have not been protected.

In considering the advisability of patent protection, attention should be paid both to those countries where there is a substantial

¹ This distinction between industrial and intellectual property is brought out in the discussion of copyrights, on p. 198 following. Although copyrights are grouped herein with industrial property, they are not so classed under German law.

² Both Germany and the United States are signatories to the Convention for the Protection of Industrial Property, promulgated after the Hague congress of 1925. Article II of the convention pledges: "Nationals of each of the contracting countries shall, in all other countries of the union, as regards industrial-property protection, enjoy the advantages that their respective laws now grant, or may hereafter grant, to their own nationals, without any prejudice of the right specially provided by the present convention. Consequently they shall have the same protection as the latter, and the same legal remedy against infringement of their rights, provided they observe the conditions and formalities imposed on subjects or citizens. Nevertheless, no condition as to the possession of a domicile or establishment in the country where protection is claimed can be required of those who enjoy the benefits of the union for the enjoyment of any industrial-property rights."

³ In American practice much of this law is found in court decisions, and many of these rights must be enforced by civil action either by prayer for injunctive relief or by suit for damages, or both. Federal Trade Commission practice is a notable exception.

⁴ A patent may be refused if the invention upon which it is based becomes publicly known before application.

potential market and to those which, while they may not afford an internal market, are so industrially equipped that the manufacture of the invention there is feasible and its exporters thereby become potential competitors for neutral markets.

Somewhat similar considerations apply to registration of trade marks. The loss of the right to a trade mark in any market would compel the adoption and popularization of a different trade mark for that market. The benefit of all vicarious advertising would accrue to competitors, while the damage caused by an inferior product being marketed under the original trade mark is frequently far more serious than the direct loss in sales. Registration, particularly of those products customarily handled through many distributors, is also important in potential producing countries, for as a practical matter it is much easier to prevent the improper use of a trade mark by one producer than it is to act against many distributors.

Patent and trade-mark pirating flourish in all countries of the world—in Germany perhaps less than in many others; but patent protection and trade-mark registration are the only safe preventives anywhere. A patent should always be taken out and a trade mark registered either in the name of the principal or by some agency controlled by the true owner. To register a trade mark in the name of an agent or to assign a patent to him may seem expedient; but satisfactory agents may die, once good outlets may become unsatisfactory through change in stock ownership, amicable business arrangements may become unfriendly, and many other reasons may make a change in representation desirable. When any of these contingencies arise the holder of the patent or trade mark is not only placed in a strategic bargaining position but in many instances, through control of the assigned patent or trade mark, is in full control of the field and can prevent absolutely the importation and marketing of the patented article or compel the use of an entirely dissimilar (and usually unknown) trade mark in the future distribution of the trade-marked article. These considerations are not peculiar to Germany, but apply with equal force in all markets of the world.

PATENTS

WHAT IS PATENTABLE

In Germany every invention (not contrary to law or good morals) of a new industrial process or new application of known methods for obtaining an industrial result may be protected by a patent. Medicines, drinks, foods, and chemicals are not themselves patentable, but processes of manufacture of such products may be patented.

A patent application may be rejected if among other reasons (*a*) it is for an artificial food product derived from chemical substances, unless the method of production is sufficiently analyzed and approved, (*b*) it has been described in the public prints within 100 years, (*c*) it is not a technical or economic improvement, or (*d*) it is a device which cannot be operated or, if once operated, cannot be repeated.

A special form of patent, called a patent of addition, is procurable on new or distinct improvements or developments of a part of an original patent—but only by the registered proprietor of the patent to which it refers. (See p. 190.)

APPLICATION FORMALITIES

WHO MAY APPLY

Application for a patent is made in the name of an inventor or his assignee or legal successor. The first person properly applying for a patent is entitled to it; but it may be annulled if he acquired knowledge of the invention irregularly. Ordinarily a patent is applied for in the name of the inventor; but where this is not the case, under an amendment to the patent law the name of the inventor must be mentioned in the application unless he files a waiver. Applications do not require an oath.

DOCUMENTS AND DRAWINGS

An application in writing must be filed with the Patent Office in Berlin. If the applicant is a nonresident of Germany, the application must be accompanied or followed by a power of attorney, appointing an agent. Together with the application, a specification in duplicate must be filed, written in the German language, but it need not be signed. This specification must set forth the technical problem solved, the new result, and the industrial purpose served, sufficiently in detail to enable those skilled in the art to practice the invention. The claims must be stated at its end, the approved practice being first to state the former practice to which the improvement applies and then to enumerate the characteristic features which distinguish the invention under consideration. Only one invention may be claimed in each application.

Drawings must also be filed in duplicate with the application; one on bristol board, 13 inches high by $8\frac{1}{4}$ or $16\frac{1}{2}$ inches, and one on cloth, 13 inches high and any width. Where a power of attorney is necessary, this also must be filed; and where an assignment of the patent is made, the assignment, duly legalized, must likewise be submitted.

TIME FOR FILING

An application for a patent must be filed in Germany before printed publication anywhere and before public use in Germany. As Germany is a member of the Union for the Protection of Industrial Property, under article IV of the Hague convention which established the union any person who has duly applied for a patent (or for a utility model, an industrial design or model, or a trade mark) in the United States or any other member country enjoys a right of priority for 12 months* from the date of filing the first application. Subsequent application by others or publication or exploitation during this period does not invalidate the applicant's right.

EXAMINATION FOR NOVELTY AND PRIORITY

Novelty, upon which the granting of a patent depends, is thoroughly investigated, and an invention is held not to be novel if it has been so described within 100 years in the public prints or if it has been so publicly employed in Germany that its use by other persons skilled in the art is possible. It is an invention subject to patent only when it is either a new means to a known end, a known

* For patents and utility models only. It is 6 months for industrial designs and models and trade marks (Convention for the Protection of Industrial Property, art. IV c).

means to a new end, or the application of a known means to a new end provided a new and logically deducible technical effect can be obtained thereby.

Examination as to novelty is strict and thorough, and all applications are referred to an examiner, who investigates the published literature for previous publication. Reports of previous publication or anticipation are made to the applicant and opportunity offered for reply within a stated time. If the examiner is satisfied by the reply, the application is advertised in the Official Gazette (*Reichsanzeiger*) and the application, drawing, and claims are opened for public inspection.

Publication may be delayed 6 months upon request. A 3-months delay is not refused under any circumstances. The specifications are printed and letters patent issued if the patent is granted.

TERM OF PROTECTION—MARKING

A German patent is granted for a period of 18 years from the day next following the date of filing and gives an exclusive right to the exploitation of the patented article and to industrially produce, introduce, market, display, employ, and use it.

Marking of patented articles as "patented" is optional with the patentee. When patented articles are so marked, the marking is usually in the following form: "D.R.P. No. —." False marking is punished in the German courts by the imposition of a fine.

REJECTION AND APPEAL

Rejection of an application cannot be issued until the applicant is notified of the basis on which rejection is contemplated. If the applicant fails to reply within the fixed period, his application is treated as abandoned. During this proceeding the applicant or his agent may interview the examiner or be heard by the application department; but there is no obligation to permit it.

On rejection an applicant may appeal within 1 month to the board of appeals. Notice of appeal within the time limit is sufficient. The time for notice cannot be extended. Argument may be made later, but should be submitted as soon as possible; and if the applicant proposes to amend his specification and claims, this is sometimes allowed, but the amendment must be in writing. The decision of the board of appeals is final.

On appeal the applicant may request a hearing for himself (or his agent) or a demonstration of the invention.

If the application is accepted upon appeal, it is advertised and the file opened to inspection as when accepted in the first instance by the examiner.

OPPOSITION—REVOCATION

A notice of opposition to the issuance of a patent may be filed within 2 months of the date of publication, alleging that the invention is not patentable or that the applicant is not in lawful possession of the invention. The latter objection can be interposed by the injured party only. The applicant may file an answer to such opposition, and occasionally the objector replies. Either party may request

an oral discussion, otherwise it is handled by the appeal department on the petition and counterstatement alone. The decision is made by the application department, from which either party may appeal to the board of appeals. The decision of the board is final.

A patent may be revoked after 3 years (*a*) if the patentee neglects to adequately work the patent in Germany or (*b*) when it appears conducive to the public interest that licenses to use the invention be granted to others and the patentee refuses to do so for a reasonable compensation and on good security.

WORKING OF THE PATENT

If a German patent is not adequately worked in Germany within 3 years of issuance, either by the inventor or by a licensee, this failure is ground for revocation. Adequate working is usually regarded as "the extent sufficient to supply the German market by production in Germany." Reasonable grounds for failure to work may excuse the patentee from the consequences of that failure; but advertising for licensees, or manufacture by a licensee in an unsatisfactory manner, or the lack of immediate profit is not so regarded. Even though the patent was once worked, a lapse in that working may be ground for revocation. The working must be continuous, except that past interruptions are not considered when revocation is sought if the patent at that time is in fact being adequately worked.

By virtue of an agreement between the United States and Germany proclaimed August 1, 1909, and renewed February 22, 1922, the working of a patent in the territory of one of the contracting parties is considered equivalent to working in the territory of the other. Thus citizens of the United States having German patents and working these patents in the United States are considered as working them in Germany.⁶

ASSIGNMENTS AND TRANSFERS

Assignments of patents should be registered in the German Patent Office, and must be legalized. An assignment must be accepted by the assignee, and, if the assignee is a nonresident, a duly authenticated power of attorney must also be signed by him (but not necessarily legalized) and filed. Assignments not recorded are ineffective against third persons. Notices of the Patent Office are sent only to owners of record.

A patent is subject to inheritance and can also be transferred or licensed, either in its entirety or in a restricted manner, by contract.

INFRINGEMENT AND PENALTIES

An infringer with knowledge or one whose infringement results from gross negligence is liable to the patentee, who is also entitled to an accounting and judgment for the profits resulting from the infringement. If a process for manufacturing a new material is patented, other material of the same quality and kind is presumed to be manufactured under the patented process until the contrary is proved.

⁶ Germany has similar agreements with Italy and Switzerland.

A patentee is also entitled to injunctive relief against further infringement of his patent (especially if the infringement is threatened).

All actions for infringement must be brought within 3 years from the time knowledge of the infringement was first obtained.

The fact that a patent has expired or lapsed does not mean that a manufacturer is deprived of all protection. "Slavish imitation or exact copying" of an article (whether once patented or not) in an unnecessary manner, so that its manufacturing origin is misrepresented, is "passing off" and as such is unfair competition. (See "Imitation of manufactured articles" on p. 197.)

FEES AND ANNUITIES

The fees to be paid upon an application for a patent change from time to time and the incidental costs (for drawings, translations, legitimization, etc.) depend upon the nature of the invention, hence a statement of the costs of obtaining a patent is impracticable; but the yearly payments, though often changed, may be given. These annuities approximate \$7.50 for each of the first 4 years, \$12.50 for the fifth year, \$18.75 for the sixth, \$25 for the seventh, \$37.50 for the eighth, and \$50 for the ninth, and rise thereafter in \$25 steps to reach \$300 for the eighteenth year.⁷ If the owner of a patent can prove that he is in a necessitous condition, he may obtain a respite for paying an annuity or be allowed to pay it in installments.⁸

Annuities must be paid every year in advance upon a patent. An extension of 60 days is allowed without fine, and of 30 days thereafter with fine; but after 90 days there is no extension of the right to renew and pay an annuity unless it is proven that the delay in payment occurred through inadvertence.

There is also a fee required to be paid on a petition for annulment of a patent or for withdrawal of a patent and upon applications on appeal.

PATENTS OF ADDITION

A patent of addition may be obtained on a new or distinct improvement or development of a part of an original patent, but only by the registered proprietor of the patent to which it refers. The life of a patent of addition is for the unexpired term of the original patent.

A patent of addition becomes an original patent (the term of which is extended to that of the original patent) if the original patent becomes void.⁹

Patents of addition are subject only to an application fee and payment of the first annuity unless the original patent is invalidated, when the first patent of addition is continued as the original patent and is then subject to the annual fee.

DESIGN PATENTS

Although the protection of a design patent (Geschmackmuster) is little sought in Germany, such protection has been provided for by

⁷ A decree of June 14, 1932, introduced certain remissions of annual patent fees which are not taken into account in the figures given here.

⁸ Industrial Property Bulletin No. 7 (C.L. No. 325), issued by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

⁹ Under a recent amendment, the oldest patent of addition becomes an original patent if the original patent is annulled.

statutory enactment.¹⁰ The protection afforded to an owner of a new and distinctive design or model is obtainable upon application for registration (before use thereof), application being made by residents of Germany through the commercial court (Handelsgericht) in Leipzig.

A design patent is allowed without examination or proof as to the right of the applicant thereto. It is granted for 1 to 3 years, and may be extended to 15 years at the longest.

The fact of the allowance of such protection and extension of the period is published in the monthly records of the Deutschen Reichsanzeiger and paid for by the applicant.

UTILITY MODELS

The German Patent Office provides,¹¹ for German residents and for subjects of countries which are members of the Union for the Protection of Industrial Property or of countries granting similar rights to German citizens, a method for the protection of articles (not processes) adapted to manufacture or practical use but not otherwise patentable. These are known as petty patents or utility-model patents (Gebrauchsmuster) and are generally employed for small or unimportant articles upon which the payment of fees and annuities would be a burden or where sufficient novelty for a regular patent is lacking.

Unlike design patents, which protect the form, shape, and general outline, a petty patent merely protects the constructive arrangement, the combinations or modifications of inventions. The petty patent covers only the specific form shown in the application, whereas a regular patent protects the invention independent of its form.

Valid petty patents cannot be obtained upon an invention previously published in any country; ¹² but prior public use in any country other than Germany is no bar to their validity.

Such petty patents are for a term of 3 years, and are renewable for an additional 3 years. The application therefor may be made by anyone claiming to be the inventor. The filing fee and 3-year annuity costs must be paid in advance. The necessary documents are the same as upon an application for a regular patent. There is no examination as to novelty required, but the patent can be canceled upon proof shown. Where there is a conflict as to priority, the claims must be decided by the courts.

TRADE MARKS

A trade mark has always been merely a mark or symbol whose function is to identify merchandise as regards origin and ownership. These marks were first used for identification, tracing, and reclamation of articles in the event (not unusual in earlier times) the goods were captured by pirates, miscarried, or lost. In other words, at the outset the mark was an asset and its use of particular benefit to the owner.

¹⁰ Gesetz betreffend das Urheberrecht an Mustern und Modellen, January 1876.

¹¹ Gebrauchsmusterordnung of June 1, 1901.

¹² The right of priority granted by the Convention for the Protection of Industrial Property (art. IV c) on utility models is 12 months.

Subsequently, the trade mark was used as a guild enforcement method; goods were required to be marked, to the end that articles varying from guild standards could be traced and their maker disciplined. The mark thus became a liability.

Stimulation of business was not the object originally sought in the use of a trade mark; but with the increase of foreign trade manufacturers began to realize that the excellence of their goods, identified by users through trade marks, did stimulate demand; and, once the benefit was shown, guild compulsion no longer was necessary, and trade marks again became an asset. Property rights in trade marks began to be recognized and common-law rights developed.¹³

The law of May 12, 1894, as amended, is the basis for trade-mark registration and rights in Germany.¹⁴

NECESSITY FOR REGISTRATION

Registration is necessary to obtain a right in and protection for a trade mark. A trade mark is not protected even by continuous use in Germany if it is not registered, nor can any claim to ownership be acquired by such use. Registration alone is the determining factor.

On several occasions foreigners (particularly Americans) have allowed their agents in Germany to translate the wording of a registered trade mark or to otherwise alter it to strengthen its appeal to the German public without effecting a new registration or without insisting that such new registration be made in their own name. Later they discovered that they had completely lost the right to the new or altered trade mark because someone else had applied for its registration.

All trade-mark protection in Germany must be taken in the name of the original owner and never relinquished—this point cannot be too often stressed, and it applies with equal force to all modifications and alterations of trade marks.

WHAT MAY BE REGISTERED

The law does not define a trade mark. In the absence of such definition it can be assumed that any distinctive mark which is not in one of the prohibited classes may be registered. The following are not subject to registration:

1. Marks common to the trade;
2. Marks which consist exclusively of figures, letters, or words used to convey information as to kind, time and place of manufacture, quality, price, quantity, or weight;
3. Marks which contain coats of arms of a domestic or foreign state or domestic towns or communities; and
4. Marks which contain representations calculated to annoy or which are or may be misleading or deceptive.

A foreign trade mark which does not comply with the German law in nonessential elements may be registered in Germany if it has

¹³ See Schechter's *Historical Foundations of Trade-Mark Law*.

¹⁴ See footnote 2 on p. 185.

been registered in accordance with the foreign law upon which the application for German registration is based.¹⁵

Foreign trade marks registered under classifications which differ from those of the German Patent Office must be made to fall into the German classifications in order to be registered, although one registration may cover two or more classes on payment of additional fees for each class after the first.

APPLICATION FORMALITIES

WHO MAY APPLY

Registration of a trade mark is granted to the first applicant. The right to apply is independent of prior use.¹⁶ Persons not having an establishment in Germany may apply for registration only when the country in which their establishment¹⁷ is located accords protection to the trade marks of Germans to the same extent it does to similar domestic trade marks. The United States does so.

Upon filing an application for the registration of a foreign trade mark, it must be shown that the mark has been properly registered in the country where the applicant's establishment is situated.¹⁸

DOCUMENTS—TIME FOR FILING

Application must be made to the Patent Office, Berlin, and must consist of a petition, signed by the applicant or his agent, giving (a) the name, address, profession, and establishment of the applicant, (b) a full description of the mark, and (c) a statement of the classification in which the mark is to be used. An electrotype and 20 prints must be filed with the application. Where an application is based on a foreign registration, a certified copy of that registration also is necessary.

If application is made by an agent, there must be a power of attorney.

To secure the priority provided in the Convention for the Protection of Industrial Property the application must be filed within 6 months from the date of filing the application in the home country.

EXAMINATION AND OPPOSITION—TERM OF PROTECTION

Strict examination is first made as to the form of the documents and the registrability of the trade mark. If this examination is satisfactory, the Patent Office next examines for prior registration and for infringement. If the mark is anticipated, the Patent Office

¹⁵ "Every trade mark duly registered in the country of origin shall be admitted for registration and protected in the form originally registered in the other countries of the union" (Convention for the Protection of Industrial Property, art. VI).

¹⁶ "Any person who has duly applied for * * * the registration of a * * * trade mark in one of the contracting countries, or his legal representative or assignee, shall enjoy, subject to the rights of third parties, for the purposes of registration in other countries, a right of priority" of 6 months (Convention for the Protection of Industrial Property, art. IV, a and c).

¹⁷ Countries in the Union for the Protection of Industrial Property allow filing of and protection of trade marks to entities, even if they have no industrial or commercial establishment, if the trade mark is not contrary to the law of the country of origin (Convention for the Protection of Industrial Property, arts. II (2) and VII bis). Country of origin is the country where applicant has an establishment; if he has none, the country of the union where he has domicile; and if he has not such domicile in the union, the country of his nationality, in case he enjoys the benefits of the union (art. VI (3b)).

¹⁸ A foreigner applying for a trade-mark registration at the German Patent Office will be refused the right until he has obtained registration thereof in his own home country, which, when and if obtained, can be proved to the satisfaction of the German Patent Office by production of the certificate obtained. (See also footnote 2 on p. 185 preceding.)

advises the proprietor of the conflicting mark and gives him an opportunity to oppose. If he enters opposition within 1 month, the Patent Office decides whether there is an actual similarity, and an appeal may be taken from this decision if notice thereof is filed within 1 month thereafter. If there is no similarity, or if there is no opposition within the month allowed the proprietor of a conflicting mark, the registration is granted and a certificate issued. The trade mark is then published in the Trade-Mark Journal (Warenzeichenblatt).

Registration is granted for 10 years from the date of the application and is renewable indefinitely thereafter for like periods. The registration of trade marks based on foreign registration expires with the registration upon which it is based. The renewal must be made before the expiration date.¹⁹ After that time the registrant may still renew, but his application must set forth a satisfactory explanation for failure to renew. A registration which is canceled or not renewed cannot be registered by another within 2 years after such lapse without the consent of the original registrant.

CANCELATION OF A TRADE MARK

The Patent Office will cancel a trade mark from the register (a) on the request of the owner, (b) on the expiration of the term, or (c) if the registration was improper. A third party also may apply for the cancellation of a mark, (a) if it has been registered by him for similar goods, (b) if the business to which the trade mark belongs is no longer carried on by the registered owner,²⁰ or (c) if the trade mark is misleading or involves possible deception.

If the registration has been granted improperly, or if a third party applies for cancellation, the Patent Office gives notice thereof to the registered owner. If the owner does not oppose the notice within 1 month, the mark is canceled. The third party institutes court action to cancel the trade mark where he previously has registered a similar mark on similar goods or where he claims the trade mark to be misleading. To be successful he must prove these allegations.

Article VI bis of the Convention for the Protection of Industrial Property provides:

The contracting countries undertake to refuse or invalidate, either administratively if their legislation so permits or at the request of an interested party, the registration of a trade mark which constitutes a reproduction or imitation liable to create confusion with a trade mark considered by the competent authority of the country of registration to be well known there as being already a mark of a national of another contracting country and used for products of the same or similar kind.

A period of at least 3 years must be granted in order to claim the cancellation of these marks. The period shall start from the date of registration of the mark. No period shall be established to claim the cancellation of fraudulently registered marks.

MARKING OF GOODS

Indication that an article is trade-marked is optional with the owner of the mark. (The phrase "eingetragene Schutzmark" is used for that purpose when so desired.)

Foreign goods illegally marked as German or as of German origin or with a registered German trade mark are liable upon entry into

¹⁹ The Patent Office advises the owner of record of cancellation for failure to renew.

²⁰ Failure to use a trade mark does not forfeit the right to its enjoyment.

Germany to seizure and confiscation by the customs or revenue authorities on petition (with security) of the injured party. Penalties in lieu of civil damages, payable to the injured party, as well as criminal penalties are imposed. After judgment the illegal marks must be removed; and if that is impossible, the merchandise bearing such marks must be destroyed.

If German goods, on being imported into or in transit through a foreign country, are bound to contain a notification showing their German origin, or if the same, at the examination at the custom-house in respect of notification of the goods, are treated less favorably than goods of other countries, the Federal Council has the power to apply corresponding regulations to the goods of the country in question upon their import into or transit through Germany and to order the seizure and confiscation of the goods if such regulations are not complied with. The seizure will be effected by the board of customs, and the confiscation will take place by sentence of the administrative authorities.²¹

ASSIGNMENTS AND TRANSFERS—INFRINGEMENT AND PENALTIES

The right to a trade mark is transferable by assignment, inheritance, or will but only with the goodwill of the business to which it belongs. Notices of the Patent Office are sent to the registered owner of the trade mark, and assignments and transfers should therefore be recorded. To record, it is necessary to file the assignment itself (legalized), power of attorney, the original certificate of registration, and an abstract of the title of the home registration.

A person who knowingly or with gross negligence wrongfully applies to his goods or uses in his published notices with regard thereto the name, trade name, or registered trade mark of another is bound to indemnify the injured party; and any person who does so knowingly, with intent to deceive, is additionally punished by fine and imprisonment.

The hearing for final decision in civil suits in which a claim is founded on the provisions of the trade-mark law will, under section 8 of the introductory act to the judicature law, be referred to the Federal court.

UNFAIR COMPETITION

The German law against unfair competition (*Gesetz gegen den unlauteren Wettbewerb*) was passed in 1896 and amended in 1909. The statute deals with business acts done for competitive purposes; but the term "business" is interpreted in its widest sense. The law provides for:

(a) The conduct of business in good faith (*Treu und Glauben*), with due regard for common usage—a provision intended to reach those instances of unfair competition not specifically prohibited in other sections of the law;

(b) The protection of trade names²² and goodwill—which precludes both attempted appropriation of the former and threatened destruction or diminution of the latter;

²¹ See criminal procedure act, sec. 459.

²² By the Convention for the Protection of Industrial Property (art. VIII), "a trade name shall be protected in all countries of the union without the obligation of filing or registration, whether it form part or not of a trade mark."

(c) The protection of the reputation of products of a business—which covers slander of credit or goods of a competitor and protects his trade reputation; and

(d) The protection of business and trade secrets or secret processes and the prohibition of their use by another.

And it prohibits:

(e) "Dressing up"—a prohibition against competing with the original producer or distributor by the marketing of a similar product in a similar form, or by the distribution of a similar product in a form closely resembling the original product, or by the advertising of a similar article in a form resembling that employed in connection with the original article;

(f) "Passing off"—which is similar to "dressing up" and differs from it in degree and intent only, "passing off" being a deliberate attempt to induce customers to believe that the product they are buying has been manufactured or produced by another while "dressing up" only tacitly induces purchases of simulated articles by unobservant buyers;

(g) Contributory infringements—this referring to those acts of a competitor which, while they do not completely accomplish the prohibited result, assist in or contribute to the infringement of another's rights (examples would be the manufacture of an improperly similar product but not the distribution thereof, or the distribution of such a product but not its manufacture); and

(h) Misrepresentation in advertising or false assertion as to one's own goods, this including improper advertising and incorrect assertions as to weight, measure, quantity, quality, or content.

REMEDIES

The law provides for criminal prosecution and, in case of conviction for fraud, for penalties in the nature of fines as well as imprisonment. Civil action for proven damages can also be brought. Upon proving the improper conduct, injunctive relief may be obtained.

By a unique provision, serving not only to repair damage not otherwise reparable, but as an indirect punishment for offenders, the court may order,²³ on the motion of a person who has been tried and acquitted, a public proclamation of the acquittal, or in the case of civil suits for injunction the court may authorize a successful petitioner to publish, at the cost of the defeated defendant, that portion of the judgment containing the decree. The court order always stipulates the manner of publication, usually setting out the text of the advertisement and specifically mentioning the papers in which it is to appear.

RIGHTS OF ACTION

Anyone who conducts a business or who produces or places on the market merchandise or products of a similar or related kind to those produced or marketed by the party against whom complaint is made may bring an action, as may also associations for the promotion of the business interests of such producers and merchants. As a matter of actual practice, suits by individuals and complaints made to the

²³ G.u.W. 23. (For a list of the abbreviations used in footnotes throughout this monograph see p. xii.)

state's attorney have been replaced by associational action. It is now the usual custom for the German manufacturer, producer, or merchant to bring instances of unfair competition to the attention of the proper association, which body, after inquiry, seeks an amicable adjustment with the offender. If this fails, and if the law has been violated, recourse is had to a civil or criminal complaint. The state's attorney may refuse to act if he believes the public interest is not involved. If he refuses to act, a criminal prosecution can be instituted without his intervention.²⁴

All who maintain their chief places of business in Germany (regardless of citizenship) are entitled to the same protection and the same rights of action as are German citizens.²⁵ Those who do not maintain their chief place of business in Germany may claim this protection only if citizens of Germany enjoy similar protection and right of action in the courts of the place where the person seeking protection and redress maintains his chief place of business. This is a question of fact and would depend, for citizens of the United States, upon the protection afforded by either the State or Federal courts in analogous situations. However, article X bis of the International Convention for the Protection of Industrial Property, to which both Germany and the United States are parties, provides:

The contracting countries are bound to assure to nationals of the union an effective protection against unfair competition. Every act of competition contrary to honest practice in industrial or commercial matters constitutes an act of unfair competition. The following particularly are to be forbidden:

1. All acts whatsoever of a nature to create confusion, by no matter what means, with the goods of a competitor;
2. False allegations, in the course of trade, of a nature to discredit the goods of a competitor.

IMITATION OF MANUFACTURED ARTICLES

In administering the law of unfair competition the German courts will not permit a firm to exactly imitate the product of a competitor who has obtained distribution in the German market. To obtain this result they invoke the prohibition in this law against "passing off." The protection afforded thereby extends not only to patented articles but also to articles unprotected by patent or upon which patents have expired or lapsed. This feature of the German law is of extreme importance, especially to American manufacturers of machine tools, machinery, and other products. The German courts have sustained complaints against exact imitation because such imitations may work deception on the market and may result in unfair trading in and taking advantage of the inventive, distribution, and sales efforts and expenditures of another and also because there is a possibility of confusion of the substituted article with the original product.

The decisions²⁶ have said that slavish copying of a machine "is a gross offense against fair dealing, if the competitor in this way utilizes the efforts and the appearances of others to an extent that is

²⁴ G. u. W. 13, 22.

²⁵ G. u. W. 28.

²⁶ Prussian Court of Appeals decision on rotary printing machines, in the injunction matter dealing with the marketing of Multigraph Senior and Multigraph Junior, and the almost exact copying of them under the names of Dapag Junior, Dapag Major, and Dapag Minor. This was also emphasized in the milk separator and Nitro-fix book cases.

not required by the kind of machine" (in other words, an extent not necessary for the proper working of the machine); and they add that external marks of distinction should at least be shown in the substitute machine, either by changing the form or color or the ornaments or accessories used in connection therewith.

It is, however, permitted to so closely imitate the essential functions or workings of a machine formerly protected that replacement parts for the one may be substituted in the other; but it is always of extreme importance to determine whether the imitation goes farther than actual utilization requires and whether the imitation is for the purpose of trading on the good name and reputation of the firm which formerly enjoyed patent protection.

COPYRIGHTS "

Germany's present copyright law (*Verlagsrecht*) is the outgrowth of the general enactment of 1901 and its amendments.

Attention has already been called to the fact that copyrights are in law considered, not industrial-property rights, but intellectual-property rights. Philosophically, intellectual-property rights should be protected as to all intellectual productions—which fall into three classes:

1. Writings and drawings capable of being multiplied by the art of printing or engraving;
2. Designs of form or configuration capable of being reproduced upon the surface or in the shape of bodies; and
3. Inventions in what are called the useful arts, such as (*a*) books, maps, charts, music, printing and engravings, (*b*) statuary, bas-reliefs, and designs for ornamenting any surface, and (*c*) machinery, tools, compositions of matter, processes or methods in the arts.

Practically, however, in most countries intellectual-property rights are recognized as copyrights and are afforded protection only in certain of the above classes.²⁸ Property in the classes not covered by the copyright law is usually secured by patent, trade-mark, design-patent, or utility-model protection and is not considered as intellectual property but only as industrial property.

WHO MAY COPYRIGHT

Authors of literary or artistic works,²⁹ composers of musical works, and producers of figures of a scientific or technical nature (although not works of art) may seek protection under the copyright law.³⁰

An author is defined as a person who produces or performs the work. Publishers of anonymous works (or those published under a pseudonym) or of works in the public domain, the owners of post-humous works, unpublished works, or periodical publications, or collaborated works, and editors of works consisting of separate ar-

²⁸ Copyrights are here grouped under industrial property because, although the rights are differently treated from industrial-property rights in law, the difference is inconsiderable, and the layman (for whom this study is primarily intended) generally associates them with patents and trade marks, which properly do come under industrial property.

²⁹ For the classes of intellectual productions upon which protection is afforded by the German copyright law see the later sections in this subtitle.

³⁰ Sculptural figures and ornamentation are included, as also are lectures which serve the purpose of edifying, instructing, or entertaining.

³¹ Copyright law, art. 1.

ticles, translators, adapters, or compilers, and persons at whose order a portrait or photograph is made are entitled to the copyright. Co-authors whose work cannot be separated are considered joint authors, each with a fractional interest in the work. In written works with musical accompaniments or illustrations the author of each part is considered the sole author of the part he contributes.³¹

Presumption of ownership arises by appearance of a name on the title page or other suitable place in a book. When no such name appears, if the name of the publisher appears he is entitled to claim. Works publicly presented or delivered are presumed to belong to the person designated in the announcement as the writer or lecturer.³²

German subjects are entitled to copyright protection for all their works, whether published or not, but nonnationals only for original works not previously published abroad; and as to the latter, the works must be published at least simultaneously in Germany.³³ By agreement of January 15, 1892, a citizen of the United States enjoys protection on the same basis as a German subject.

The copyright registry is in the charge of the municipal council (Stadtrath) in Leipzig, which enters the registrations as applied for without investigating the rights of the applicant or the correctness of the information reported. Appeal is allowed upon refusal of registration. Appeal in the last instance is to the supreme court. Upon the granting of registration, the public will be notified at the expense of the applicant.³⁴

EXTENT AND DURATION OF PROTECTION

A copyright gives the owner the exclusive right of reproduction, adaptation, revision, and translation, as well as the exclusive right of public performance of dramatic and musical works. (This includes orchestration and other arrangements or rearrangements of musical scores.) While the work remains unpublished, the copyright owner also has the exclusive right of oral presentation of works intended for oral presentation, such as lectures and recitations. Without a copyright there is no protection to an author, although no formal application is necessary as in the United States.³⁵

The protection of a copyright ends 30 years after the death of the author. For a posthumous work it does not lapse until 10 years after the date of the first publication. If the work is not published in the 30 years subsequent to the death of an author, it is presumed that the possessor of the manuscript is entitled to the copyright. If there are joint authors, the 30-year period is figured from the date of the death of the last surviving coauthor. If a work is published anonymously or under a pseudonym or by a juristic body, the protection ends 30 years after publication unless the author properly registers his own work within such term, in which case the full time becomes operative. In works consisting of several volumes, each volume is considered a separate work in calculating the period of

³¹ Copyright law, arts. 2-6. Anyone translating a foreign work must (art. 25) clearly indicate its source.

³² Copyright law, art. 7.

³³ Copyright law, art. 55.

³⁴ Copyright law, arts. 56-59.

³⁵ Copyright law, arts. 12, 61; exceptions are noted in arts. 16-25.

protection. For the purpose of calculating the term, the period begins at the end of the calendar year in which the author died or the work was published.³⁶

Photographs are protected for 10 years and models and designs for not more than 15 years.

TRANSFERS AND INFRINGEMENTS

The right to a copyright is inheritable, and it also is transferable by contract, but both inheritance and transfer are subject to restrictions imposed. A special law provides for and defines the rights between an author and a publisher, which especially covers the rights of the parties where the publisher desires to change a thing produced without the consent of the author.³⁷

A person who intentionally or negligently violates the exclusive rights of the holder of a copyright is obligated to pay him the damage sustained. The printed copies and the devices for printing, including the forms, plates, and stones, will be destroyed upon petition of the copyright holder, though he may claim the right to acquire them. Suit for the infringement will be prosecuted by way of civil litigation or criminal proceedings.³⁸

All claims for infringement of a copyright are barred after 3 years from the date on which the circulation of the reprints first began, but a petition to destroy is good as long as the copies or devices are in existence.³⁹

CARTELS *

The method ⁴¹ adopted in the United States for dealing with combinations in restraint of trade and monopolies and the maintenance of freedom of competition by prohibiting certain actions and agreements is unique. In Germany, as in most other countries of the world, such actions and agreements are not prohibited regardless of how complete and all-embracing the combinations may be; but they are the subject of official attention and limitation when they reach the point where they are detrimental to the public interest.

Germany originally placed upon such combinations the limitation that they should not be against public morality (*guten Sitten*). This was construed to mean that no one should be condemned by the combination to commercial impotence, and that the combination should not be allowed to injure others. These provisions received the most liberal interpretation. Occasionally, however, a trust had been declared unlawful by reason of having been found guilty of extortion under the penal law. The commercial law also provided against agreements in restraint of trade—only as between a principal and

³⁶ Copyright law, arts. 29-34.

³⁷ Copyright law, art. 8.

³⁸ Copyright law, arts. 36-43, 46-47; Z.P.O. 477-479.

³⁹ Copyright law, arts. 50-52.

⁴⁰ Although the treatment of this question may not properly come under "industrial property", inasmuch as the law concerning cartels deals primarily with an attempt to group industrial combinations and combinations generally in restraint of trade it may with some propriety be considered in connection with these other intangible rights.

For a history of and bibliography on cartels see Borchard's *Guide to the Laws of Germany* (pp. 117-118), and the following publications of the Bureau of Foreign and Domestic Commerce, Washington: *International Cartel Movement*, by Louis Domeratzky (issued as Trade Information Bulletin No. 556), *Representative Cartels, Combines, and Trusts*, by Wm. F. Notz (issued as Trade Promotion Series No. 81), and *Commerce Reports* for Oct. 6, 1924, Mar. 3, 1930, Feb. 23, 1931, and Apr. 18, 1932.

⁴¹ See Sherman Act (antitrust law), Clayton Act, and Federal Trade Commission Act.

an assistant, however, but not between a principal and a third party, or even between assistants and third parties, nor between independent traders generally.⁴²

With the passage of the empowering acts (*Ermächtungsgesetze*) of 1923 an instrument was placed in the hands of the authorities to make legislation to limit combinations, and there were promulgated two decrees⁴³ which gave to the Ministry of Economic Affairs (*Reichswirtschaftsminister*) a moderate and limited control. The unofficial note to the press commenting on these decrees observed that the Government did not wish to abolish cartels, but only sought to enable them, by curtailing abuses, to help in the reforms necessary to economic adjustments and the devising of rational methods of production and unification of prices.

PROVISIONS OF PRESENT LAW

The law in force today provides that contracts of cartels executed subsequent to the effective date of the law must be in written form. Commitments not so written are invalid, as also are even written contracts which attempt to interfere with or prevent the subject matter being referred to the cartel court for review or on appeal.⁴⁴

When a cartel commitment "endangers the general economic standard or the common good" (as defined in art. 4 of the law), the Minister of Economic Affairs may advise the cartel court that the arrangement should be declared void in whole or in part or that its execution should be forbidden. This court was given the power to decide the effect of the declaration of nullity on other parts of the arrangement and to withdraw an order when the objectionable conditions cease to exist. When a cartel has been summoned for a review of its acts, the court may thereafter order all subsequent general agreements to be submitted to the court of review before action is taken under them.⁴⁵

The cartel court is also empowered to order (for important reasons and without notice) every party (including customers) to a contract that endangers the general economic standard or is inimical to the common good to cancel the contract or withdraw from commitments.⁴⁶ Right to withdraw is determined by the cartel court on appeal by an interested party, but the appeal must be filed within 2 weeks from the receipt of notice of withdrawal.

One of the logical outcomes of the development of cartels is the tremendous power obtained by them in connection with cross-licensing or pooling of patents, to which the German cartel law interposes no specific limitations.⁴⁷

⁴² R.G. vol. 53, p. 156; B.G.B. 826; H.G.B. 74.

⁴³ Decree against abuse of economic power, and decree regulating procedure before the cartel court.

⁴⁴ Cartel law, arts. 1-3.

⁴⁵ Cartel law, arts. 4-5, 7.

⁴⁶ Cartel law, art. 4: Undue restriction of economic freedom is interpreted as an important reason.

⁴⁷ This feature is elaborated in an article by Douglas Miller in *Comparative Law Series of October 1926* (C.L. 134), published by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

X. JUDICIAL POWER

COURTS AND THEIR JURISDICTION

Codification of Germany's Civil Code made necessary introductory or transitional laws relating to the organization of the judiciary (Einfuehrungsgesetze zum Gerichtsverfassungsgesetze). After these had served their purpose, permanent laws—to be found in sections 1 to 168 of the civil practice act (Zivilprozessordnung)¹—were enacted.

The German courts provided for the general administration of the law are:

1. District courts (Amtsgerichte);
2. Superior courts (Landesgerichte);
3. Courts of appeal (Oberlandesgerichte); and
4. The supreme court (Reichsgericht) in Leipzig.

DISTRICT COURTS

In ordinary civil litigation, jurisdiction is exercised by a court of first instance (Amtsgericht), one legally trained judge presiding,² in—

1. Cases involving not more than 500 marks;
2. Other cases, regardless of amount, involving (*a*) bankruptcy, (*b*) commercial registration, (*c*) land registration, (*d*) inheritance and annuities, (*e*) leases and lease relationships, (*f*) service arrangements and apprenticeships (in districts where special courts are not provided), (*g*) guardianship and relationship and kinship duties, (*h*) innkeeper and guest disputes, (*i*) cattle defect and violations of game laws, and (*j*) special matters which from their inherent nature require special expedition.³

A branch of this court is the criminal part (Schoeffengericht), presided over by one legally trained judge and two lay judges,⁴ in which a majority decides all questions. The matters which come before it involve minor transgressions and ordinary trespasses where the penalty is not great. Matters analogous to juvenile-court matters are also heard by a district court.

SUPERIOR COURTS

The superior court is a court of second instance for appeals on civil and criminal matters (first heard by the Amtsgericht or the Schoeffengericht). When so functioning it is composed of three legally trained judges. It is also a court of first instance (Zivilkammer) for civil suits if the amount is more than 500 marks. When three legally trained judges sit, as well as a criminal court (Straf-

¹ See Comparative Law Series of October 1926 (C.L. 134) issued by the Division of Commercial Laws, Bureau of Foreign and Domestic Commerce, Washington.

² Z.P.O. 22. (For a list of the abbreviations used in footnotes throughout this monograph, see p. xii.)

³ Z.P.O. 23.

⁴ Z.P.O. 29.

kammer) where possible fines and terms of imprisonment are more severe, in which cases five legally trained judges are necessary.⁵

As civil courts of first instance superior courts also hear, by specific provision, actions (a) for impeaching the validity of resolutions of a share company, limited-liability company, partnership with share capital, or cooperative association, (b) for the dissolution of one of the foregoing organizations or for declaring that such organization never had a legal existence, and (c) for the recovery of damages for wrongful representations in a prospectus by reason of which shares have been dealt in on the stock exchange.

For special and serious cases of criminal infractions not covered by the criminal part of the district courts or the supreme court, a jury court (Schwurgericht) is brought together as a special part of the superior court, consisting of 3 legally trained judges and 6 to 12 jurors. The jury decides only as to the guilt or innocence of the defendant before them. The right of sentence is in the three judges.⁶

Insofar as the county judicature think it necessary or requisite, the Landgerichte are empowered to create special tribunals of their courts for commercial matters (Kammern fuer Handelsachen). These commercial courts take the place of the earlier courts of that name, but are distinguished from them in that they are connected with and are a part of the superior courts. One legally trained judge and two lay judges preside over cases of merchants, negotiable instruments, claims between corporations and their officers and procurists and shareholders, patent and trade-mark matters, and unlawful competition.⁷

The trial of cases by this commercial side of the court depends upon proposal of the parties.⁸ The superior court may not, of its own motion, refer a case to the commercial side of the court; but a judge of the commercial side may refer a matter given to him back to the civil side when the subject matter is not appropriate for handling in the commercial side of the court.

COURTS OF APPEAL

Appeals may be taken from decisions of the courts of civil, criminal, and commercial jurisdiction of first and second instance to the court of appeals (Oberlandesgericht), which is known as the Kammergericht in Berlin. This court is presided over by five legally trained judges. Where taken in criminal cases, the appeal is merely in the nature of a review to determine whether the lower court has correctly applied the law.⁹

The highest court in Germany is the supreme court (Reichsgericht), which is located by law in Leipzig.¹⁰ This court reviews on appeal cases from the jury courts, superior courts, and appeals decided by the court of appeals; it is the court of final resort. Its sessions are presided over by a senate composed of seven members.

SPECIAL COURTS

There are also special courts organized as the exigencies arise, but only where the federal legislature prescribes or sanctions them. Such

⁵ Z.P.O. 71, 76.

⁶ Z.P.O. 79-92.

⁷ Z.P.O. 93, 95, 105.

⁸ Z.P.O. 96.

⁹ Z.P.O. 116, 119-121.

¹⁰ Z.P.O. 123.

courts are the industrial courts (Gewerbegerichte) and the merchants courts (Kaufmannsgerichte).

The functions of the industrial courts is to decide industrial disputes between employers and their workmen (including house servants) and between workers of the same employer. They roughly resemble the guild courts of earlier times, and since 1901 they have been compulsory for cities with more than 20,000 inhabitants. They are composed of a president and his deputy, chosen by the representatives of the county, and also assessors, half of whom are chosen by the employers and merchants and half by the workmen, and assistants to the assessors chosen by their colleagues, in open voting and ballot elections. One of the most interesting duties of the industrial courts is in connection with their work upon boards of arbitration, especially in the formation of trade agreements.

The merchants courts are of equal and concurrent jurisdiction with the industrial courts, except that their work is mainly concerned with the settlement of disputes between workers in purely industrial pursuits with their employers. They are maintained at the expense of the communities which have them, whereas the industrial courts are maintained at the expense of either the municipalities or the unions over which they enforce their jurisdiction.

VENUE

Essentials of jurisdictional competency are governed by the judiciary statute, but the civil practice act contains provisions with regard to local venue.

The question of jurisdiction is decided either according to the subject matter of the action or by the location of the parties; but a court which does not have local jurisdiction may assume it by consent of the parties, and if a party appears to plead or otherwise submits to the jurisdiction he can not thereafter impeach its competency.

Certain courts have exclusive local jurisdiction which cannot be surrendered, where the subject matter is already under the jurisdiction and control of the court and where it is necessary to determine rights in and to a property located within the jurisdiction of such courts; but where no court has prescribed or exclusive jurisdiction, and the parties have not agreed on a court, the action must be brought where the defendant has his general court obligation (Gerichtstand).¹¹

JURISDICTION OVER FOREIGNERS

Foreigners have the same right as German citizens to sue and be sued in Germany. This includes foreign corporations. German courts will take jurisdiction over foreigners for the purpose of suits against them if they can be served with summons personally in Germany or have personal property there,¹² and the judgments in such

¹¹ This is construed to be his residence or, if he have no permanent one, his last place of residence or wherever he is found. For persons other than natural persons (companies, associations, etc.) the Gerichtstand is determined by the seat of the management or, failing this, where the business is carried on. Jurisdiction for claims under contracts is vested in the court of the district where the obligation in dispute should have been discharged (Z.P.O. 29).

¹² In one case jurisdiction was obtained on the presence of a trunk in a hotel checked there by an American passing through Germany.

cases are enforceable. Service of process may also be effected by mail on a defendant residing outside Germany even though the defendant so served may have no property within the jurisdiction of the German court. Failure to appear after such service gives the plaintiff judgment by default; but, of course, no execution can be obtained upon the judgment unless and until the defendant acquires property in Germany upon which to levy. A person not domiciled in Germany but having assets there must be sued in the district where his assets are situated.¹³

The courts will also take jurisdiction over foreign corporations if they have property in Germany; but the mere presence in Germany of an officer or director of such corporation has been held to be insufficient. The possession of a German bank account has, however, been held to be adequate.

REPRESENTATION IN COURT

JUDGES AND PUBLIC PROSECUTORS

Professional judges.—A professional (that is, a legally trained) judge is required to satisfy certain educational qualifications before appointment. He must take a 3-year law course in a university, at least one half of which must be in a German university. During or after that time 3 additional years must be spent in obtaining practical experience, not more than 6 months in a law office under the tutelage of an attorney and the rest of the time in the several courts as an assistant to the judges.¹⁴ These periods may be extended by law. A teacher of law in any German university is also qualified to be a judge.¹⁵

It is the theory that judges should be professionally trained in their work and should make it a life profession. When appointed, the judge's position is for life, and he cannot be removed or transferred except with his consent, unless in accordance with law.¹⁶ Judges of the higher courts are appointed from the lower courts and not from among the practicing attorneys, and ordinarily the judge who presides over the highest court, instead of being chosen from members of the bar, has risen step by step through the judicial positions.

Lay judges.—Any German man (or woman) over 30 years of age, who has been a mercantile trader or a director or manager of a share company or limited-liability company in the district where he resides, may become a lay judge in such district. The term of office is for 3 years and can be renewed. Such a judge is qualified to act in any commercial case except where he would be interested in or affected by the result.¹⁷

Public prosecutors.—In every German court the public or government is represented by a prosecuting attorney, who is not a judicial officer but must be qualified for judicial office by education.¹⁸ His position is independent of the courts, and his function is to bring or defend actions involving the state or government and to institute perjury proceedings.

¹³ Z.P.O. 23.

¹⁴ Introduction to the Z.P.O., II (2).

¹⁵ Z.P.O. 4.

¹⁶ Z.P.O. 8.

¹⁷ Z.P.O. 108.

¹⁸ Z.P.O. 147-151.

ATTORNEYS AT LAW

Every person is permitted to represent himself and plead before the district courts. For higher courts, however, the services of an attorney are required. Before the industrial and merchants courts a lawyer is not permitted to represent the parties, the object there being to force the parties to appear in person and present their cases in the words and manner of a layman.

German lawyers practice in much the same manner as lawyers in the United States, dealing directly with clients and appearing and pleading in court. The German lawyer is not admitted to the bar in the American sense, but must obtain permission to practice in the courts. The educational requirements are the same as for the legally trained judge. In the course of his studies, both at the university and with the courts, he must from time to time satisfactorily pass examinations. The state departments of justice supervise the issuance of the required permit.

The qualified applicant is permitted to practice only before those courts to which he is specifically admitted. An attorney registered at a local district court may on application be admitted to practice and appear before a corresponding court in another jurisdiction only if this is held to be in the interest of the administration of justice. This disability to appear in courts of other jurisdictions is far-reaching in its effect on litigation and on the relations between attorney and client. The residence of the defendant usually determines the jurisdiction, and in choosing an attorney the plaintiff is restricted to those admitted to the particular court having jurisdiction.

The German standard of ethics is high and strict. Fees for litigation are prescribed by law, based on the amount involved irrespective of success or failure, and are payable in advance. Ethics preclude representation on a contingent-fee basis.

PROCEDURE

PRESCRIPTION (STATUTE OF LIMITATIONS)

It must be recognized that in every country the rights to property and the right to sue or otherwise proceed to enforce obligations should be surrounded by certain definite safeguards to protect and insure continued enjoyment of these rights. On the one hand those who believe that they enjoy such rights to property because they have uninterruptedly enjoyed them without question should after a certain period be confirmed in such rights against the whole world; and on the other hand those who can proceed to enforce rights and yet for some reason refrain from so doing should be held to have lost their opportunity after a certain time, so that the parties against whom they could have proceeded will have some security and immunity from legal process.

Apart from this theoretical basis, these rights to limitation seem to be confirmed by common sense and by necessity. The difficulties of proof in matters of rights in property and to action increase with the passing of time, with the destruction of documentary evidence, with the forgetting of the circumstances and conditions by living witnesses, and, of course, with the death of those who could testify.

A limitation fixed by the law of Germany bars no right. It bars only the action for the enforcement of the right; but the result is usually just the same as though the right itself had been barred. If a party bound to act and relieved from so doing by the running of the limitation performs the act, he cannot recover for the act done because he is under no legal necessity for doing it.¹⁹

An obligation barred by limitation bars also all accessory claims such as interest and costs, but where a party retains, by way of pledge, security, or otherwise, property of his debtor his rights to exercise his claim and obtain satisfaction therefrom is not barred.²⁰

A limitation cannot be excluded or extended by contract, but it can be shortened.²¹

BEGINNING OF PERIOD

The limitation period starts running:

1. Where an act or its omission is required, from the time fixed for performance unless notice of default is specified, when it is from the expiration of the notice.²²

2. Where recovery of property is claimed, from the time the property came into the possession of the predecessor of the possessor from whom recovery is sought.²³

3. Where a claim must be settled by contest (except under family law), from the time when the contest should have been commenced.²⁴

4. On claims barred in 2 or 4 years (see below), from the close of the year in which the right arises.²⁵

There are other special instances not covered by the foregoing which are provided for in the Commercial Code, sections 61(2), 133, 159, 206, 249(4), 326(3), 414, 423, 430, and 439, and in the Civil Code, sections 124, 477, 490, 558, 606, 638-639, 786, 801-802, 852, 1028, 1057, and 1226.

ENDING OF PERIOD

The ordinary limitation, in the absence of special provision, is 30 years.²⁶

Outlawed in 2 years are:

1. Deliveries or work or services done by merchants, manufacturers, and artisans unless for the purposes of a trade carried on by the debtor.

2. Deliveries of forest or agricultural products used in the household of the debtor.

3. In railroad enterprises, freight charges, fees, and outlays of draymen, seamen, drivers, and messengers.

4. Innkeepers and restaurateurs for food, drink, board and lodging, and services generally for guests.

5. For those who as a trade hire out movables for rent.

6. Servants, industrial workmen, and masters for apprentice fees.

7. Teachers, physicians, surgeons, dentists, and veterinaries.

8. Attorneys, notaries and sheriffs, and parties for advances to attorneys and witnesses and experts in litigations.²⁷

Outlawed in 3 years are:

1. Claims for damages.²⁸

¹⁹ B.G.B. 222.

²⁰ B.G.B. 223.

²¹ B.G.B. 225.

²² B.G.B. 198-199.

²³ B.G.B. 221.

²⁴ B.G.B. 200.

²⁵ B.G.B. 201.

²⁶ B.G.B. 195.

²⁷ B.G.B. 196.

²⁸ B.G.B. 852.

Outlawed in 4 years are:

1. Deliveries of work or services by merchants, manufacturers, and artisans for purposes of a trade carried on by debtor.
2. Claims for balance of interest and amounts payable on installment accounts.
3. Arrears of rent and balances of rent.²⁹

INTERRUPTION OF PERIOD

The running of the period of prescription is interrupted by legal action for the establishment of the claim, bankruptcy, third-party notice of claim, set-off by way of defense, and arbitration proceedings; ³⁰ but when such proceedings have been abandoned, dismissed, or otherwise disposed of, the period of prescription begins to run again.

Such limitation is also stayed for incapacity or decease of a party or where the obligor acknowledges the claim to the obligee by part payment, payment of interest, giving of security, or in any other way.³¹

A limitation to be used as a defense must be pleaded and proven.

DEFAULT PROCEDURE BEFORE ACTION

German law permits a default proceeding prior to litigation, putting the creditor as soon as possible and without legal delays in a position to levy execution. This is effected by an *ex parte* application by the creditor for a judicial order addressed to the debtor to pay in a short specified time or enter an appearance. If the debtor fails to appear, an execution order with the effect of a final judgment issues. Such order can be issued only when the facts alleged in the statement of claim or subsequent pleadings establish the claim of the creditor. If the debtor appears, the default proceedings stop. The defaulting judgment debtor can protest to the same court and summon his opponent for trial if the protest is made within 2 weeks after the order for the default judgment is issued.

FRAMING OF ISSUES

If the default proceeding is not productive of judgment or satisfaction, the creditor must file a statement of claim containing a designation of the parties, the court, a definite statement of the subject matter of the suit, the grounds of the claim, and the relief sought, and a summons to the defendant to plead orally before the court. As with every summons, this statement of claim must be handed to the court before service to obtain an appointed time for hearing. The prayer for relief must be definite and give precise notice of what the plaintiff demands, except in the case of a claim for an accounting or for the production of a list of property or the administration of a public oath. With the entry of the statement of claim the action first attains legal existence.

The procedure in the ordinary courts is based on their rules of pleading, on the principle of oral advocacy, on the conduct of the case by the parties, and on the principle of absolute discretion in the court in attaching credence to the evidence. The court does not

²⁹ B.G.B. 197.

³⁰ B.G.B. 209-220.

³¹ B.G.B. 206-208.

deal with the subject matter of the litigation but waits until the parties themselves present the case, and it bases its judgment on their claims, allegations, and evidence. The claims of the parties determine the scope of the relief and limit the court in its judgment for the court is not empowered to grant anything not claimed.³²

IMPORTANCE OF ORAL PLEADING

The decision is based on facts admitted or proven in spite of denial. The court on its own motion has power to inspect documents and to examine experts, but otherwise awaits the naming of witnesses and an outline of the points upon which they are to be examined. The court also has full discretion to order the production of mercantile books of account. Admissions and material allegations agreed upon or not disputed are considered true. The parties' conduct of the case is supplemented by court inquiry. The court may interrogate on its own motion to make clear obscure allegations or further question insufficient statements of fact, and may generally examine on all matters important for ascertaining the circumstances.³³

The procedure is so entirely based on oral pleading that the court can take cognizance only of those matters brought before it orally. The written pleadings have no effect and only serve as an outline to apprise the court of the nature of the suit.

AMENDMENT OF PLEADINGS

An amendment to the claim is allowed either when the defendant consents explicitly, or impliedly by answering the amended claim without attacking the amendment itself. It may also be allowed if the court decides that the defendant is not materially prejudiced by the amendment. The civil practice act expressly provides that a change is not to be considered an amendment when, without altering the basis of the claim, an allegation of fact or law is supplemented or corrected; but the prayer is amended when an additional claim is made for interest. Defenses must be pleaded, especially a counterclaim.

EVIDENCE

Evidence to be used in the German courts can be obtained by (a) inspection, (b) testimony of eye witnesses, (c) ordinary testimony, (d) expert testimony, and (e) testimony by records, and must be adduced under oath. Some persons may not be called as witnesses, and some questions need not be answered, but the reason for the exclusion of such witness or testimony must be filed with the court.³⁴

The German conception of evidence discards the often complicated, technical rules of evidence which are a part of American procedure. It may be said that the courts are bound by practically no rules of evidence except those as to inspection of documents and oaths of the parties.

The court has power of its own motion to take evidence by inspection and to examine experts and, in commercial matters, to insist on the production and examination of books; but the parties must pro-

³² Z.P.O. 308.

³³ Z.P.O. 139.

³⁴ Z.P.O. 371-444.

duce the other witnesses and outline the points upon which they are to be examined.⁸⁵

The judge is given practically absolute discretion as to the evidence that should be received after hearing all that is to be said about the subject matter of the suit. He must come to his decisions independently and in accordance with his own individual conviction. He is therefore required to consider the whole evidence and when giving judgment to formulate the reasons which have determined his decision.⁸⁶

The witnesses, when produced by the parties, are questioned by the judge but are never cross-examined. Each one is examined separately and not in the presence of the other witnesses, but the witnesses who contradict each other may be confronted one with another. Questions occurring to counsel or either of the parties may be suggested to the judge and he may use or refuse them, but no objection to his ruling is allowed.⁸⁷

The court clerk prepares the subpoena, which is served by a court official, or the witness may be otherwise invited to attend the court. The court formulates the general scope of the inquiry (*Beweisthema*), which is sent to the witness with the subpoena. Appearances of witnesses may be made dependent on the deposit of their expenses with the courts.⁸⁸

The witness is first asked to state all he knows about the matter in dispute in his own way and is thereafter interrogated by the judges. His story is not stenographically reported, but the presiding judge dictates it to the clerk of the court (adhering as closely as possible to the witness' words) after the examination. A witness may even be examined by a judge other than the one who presides over the trial court,⁸⁹ in which event the record of the case is sent to him for his information in conducting the examination. The attorneys for the parties may, but usually do not, appear at such examinations.

PARTY OATHS

The party oath occupies a peculiar position in the law of evidence. Ordinarily the parties to a litigation are not permitted to give testimony. They may, however, be called upon in exceptional cases to appear before the court and be examined. When they are called they are warned with great solemnity of the legal consequences of both taking and refusing the oath, and their statements are accorded a large degree of credence by the court in coming to a decision.

The party oath is in most cases to be taken only after an interlocutory judgment⁴⁰ and after intermediate appeals have been exhausted. Such an oath is ordered and allowed during the preliminary inquiry only when the parties explicitly agree on the form and necessity of the oath or when it serves to clear up an intermediate dispute or an independent line of attack or defense.

⁸⁵ Z.P.O. 372, 412.

⁸⁶ The judge bases his decision only on such allegations of fact as are either admitted by the other side or have been proven in spite of contest to his satisfaction. Only in special cases (arrest or interlocutory order) can the court be satisfied with *prima facie* evidence instead of proof.

⁸⁷ Z.P.O. 394, 396-397.

⁸⁸ Z.P.O. 377, 379.

⁸⁹ Z.P.O. 372, 375.

⁴⁰ Z.P.O. 460.

The oath may be either optional or compulsory. A compulsory oath is ordered by the court only if the pleadings and other evidence are insufficient to convince the court of the truth as to disputed matters. In optional oaths the willingness of a party to take the oath is tested by a "challenge to an oath." One party asks the other to substantiate his contention by oath as to the truth or falsity of the allegations. If the challenged party does not accept the challenge, the oath is considered refused, and the facts which he contends to be true are regarded as disproven. The necessity for taking the oath may be shifted from one party to the other as the burden of proof shifts from time to time on the introduction of other evidence. The party who proves his contention to the satisfaction of the court by other evidence need not submit to the oath.⁴¹ The party challenged can also counterchallenge by demanding that the other party take oath that the facts put forward by him are the true ones.

A party oath is permissible only as to the facts dealing with the disputed transaction and can be taken by only one of the parties.⁴² A party making such an oath is required to state whether a fact alleged by him is true or false. When a fact is alleged by the other party, to the truth or falsity of which the adversary cannot be expected to swear, the party oath may be merely a statement of the best knowledge and belief.⁴³

PERPETUATING TESTIMONY

Provision is made for inspection or for the examination of witnesses or experts for the purpose of perpetuating their testimony, but taking such testimony is permitted only on agreement of the parties or when the party desiring it convinces the court that there is risk of its loss or that it may become more difficult of access by delay. Ordinarily it must be taken before the court where the litigation is to be conducted and may be declared in the form of a protocol (deposition) to the clerk of such court. Where there is great danger of loss through delay, however, it can be taken before a judge where the witness happens to be. Such testimony can be taken before suit is instituted and even *ex parte*. When a party is allowed by a court to take such testimony, he should notify his opponent and give him an opportunity to protect his rights; but if this is not possible, the procedure is not invalidated. The court may provide an agent to protect the rights of an absent party in the examination.⁴⁴

DEPOSITIONS FOR USE IN FOREIGN JURISDICTIONS

Germany has always objected to the taking of testimony of German citizens for use in foreign courts under commissions to foreign diplomatic or consular officials, but will permit it if the German citizen himself is willing. The usual way is to take such depositions at the local district court or before a notary. If the German citizen is unwilling to submit to the examination, resort may be had to

⁴¹ Z.P.O. 446, 454.

⁴² Z.P.O. 445, 449.

⁴³ In recent years there has been considerable agitation in Germany to remove the provisions for the taking of party oaths from the civil procedure (*Journal of Comparative Legislation and International Law* III, vol. XIV, pt. 4, pp. 186-188).

⁴⁴ Z.P.O. 485-486, 490-494.

letters rogatory, which the German courts will execute when transmitted from the foreign State Department through its Embassy in Berlin to the German authorities through the Ministry for Foreign Affairs to the Ministry of Justice. Although counsel may appear at the examination of such witnesses, the German courts act by virtue of their own judicial authority and conduct the examinations themselves. This fact makes an open commission more desirable.

**INTERMEDIATE RELIEF
SECURITY FOR COSTS**

On application of a party to a suit the court may order the deposit of money sufficient to cover the court fees and, for a defendant, the attorneys' costs as well, the manner and amount to be determined by the court. The application can be renewed from time to time if the amount deposited is not sufficient. When and if security is ordered, it must be deposited within the time set or the case will be dropped.⁴⁵

Nonnationals are especially subjected to the deposit of security for costs except where the home court of the foreigner does not require it of Germans and in registry or Grundbuch cases and countersuits.⁴⁶

WARRANT OF ATTACHMENT AND ARREST

Provision is made for attachments to prevent debtors from dissipating their estate or fleeing to foreign countries, or otherwise anticipating legal proceedings on the part of creditors. An attachment to insure payment is allowed against movables and immovables and for claims due or conditional when there is fear that execution of the judgment will be balked or rendered more difficult, and especially where the judgment must otherwise be executed outside Germany. It is allowed, not for the purpose of satisfying the creditor, but merely as security.⁴⁷

To obtain an attachment the creditor must have a proper claim against the debtor. The claim need not be due, nor need the creditor have filed a suit to enforce it. The application therefor must contain a statement of the nature of the claim and its amount and the grounds for the arrest, and must be proven to the satisfaction of the court. The decision to grant it may be made *ex parte*.⁴⁸

The order of arrest itself must state a money payment upon the deposit of which it can be vacated, and the debtor may either free himself of the warrant by making the deposit or may contest it by advising his adversary of the grounds of his contest and summoning him for trial to the court where the process originated. The court issuing the warrant may on application fix a time within which the merits of the application will be determined, and if the parties do not appear within that time the arrest is dismissed. Ordinarily, however, the merit in the issuance of the warrant is to be decided by the court which tries the case and at the time that the entire case is tried.⁴⁹

TEMPORARY INJUNCTION

The intermediary remedy of temporary injunction (*einstweilige Veruegung*) is similar in nature to that provided under a warrant

⁴⁵ Z.P.O. 103, 112-113.
⁴⁶ Z.P.O. 111.

⁴⁷ Z.P.O. 916-917.
⁴⁸ Z.P.O. 920-921.

⁴⁹ Z.P.O. 923-924, 926-927.

of attachment. The latter temporarily secures the creditor on a claim of a financial nature, and the debtor is meanwhile deprived of his property. Injunction gives the creditor a restrictive power in respect to a claim arising out of a contractual right whereby the debtor is not allowed to do certain acts which interfere with the rights of the creditor. Since the functions of both are similar, the procedure under arrest governs that under injunction as well, except as it is changed by the civil practice act.⁵⁰

An injunction is granted where there is danger that the enjoyment of a right will be balked or rendered difficult by the act of another, or where, by allowing it pending determination of rights, irreparable injury is avoided.⁵¹

Applications for such relief are made to the court which has jurisdiction over the subject matter. The granting is completely in the discretion of the judge and can be *ex parte* and before litigation is commenced. The presiding judge himself may grant such relief. Where the injunction involves matters entered in a public register (*Grundbuch* or *Schiffsregister*), the court is empowered to order inscription therein.⁵²

If either the warrant of arrest or the injunction order be disallowed, the one who applied for it is liable for all damages occasioned.⁵³

The courts decide only rights of a private character. If they were called upon to grant an injunction in a case where interference with public rights was accompanied by violations of criminal law, they would turn the matter over to the police.⁵⁴ They also would refuse an injunction even though private rights were threatened where the decision would touch questions of administrative law of a political nature (for instance, the reviewing of acts of officials). In these cases special remedies are provided by the administrative laws of the several States or by appeals to the superiors of these officials or by suits in special courts.

JUDGMENTS ⁵⁵

Every judgment is delivered by the court in the form of a written decree signed by all the judges who have participated, containing (a) the names of the parties, (b) the court, (c) the formal judgment, (d) the statement of facts, and (e) the grounds of the decision.⁵⁶

The judgment may be final, partial, or interlocutory. If it is final, it disposes of the entire case. A partial judgment may be rendered when, of several claims in the statement of claims, only one or a counterclaim is ready to be decided. An interlocutory judgment is permissible when the immediate trial of an issue ready for judgment

⁵⁰ Z.P.O. 937-945.

⁵¹ Z.P.O. 935, 940.

⁵² Z.P.O. 937-938, 941, 944.

⁵³ Z.P.O. 945.

⁵⁴ Unlike the United States Supreme Court in *re Debs*, 158 U.S. 564, which granted an injunction.

⁵⁵ In the old Roman law, and even under common law, not every right was enforceable. Only such as were found to fit prescribed forms of action were proper for the consideration of the courts. The present German theory of law, however, is quite the opposite: if there be a recognized right, a remedy will be afforded (*Harvard Law Review* XXII, 1899, pp. 161-181).

⁵⁶ Z.P.O. 300, 313.

would otherwise be held up by the issues of attack or defense which are not ready for judgment. The defenses of prescription, account stated, and satisfaction and an objection on a point of law can be dismissed in an interlocutory judgment. Where a claim is affirmed but there is reservation of the question of amount is another instance of an interlocutory judgment.⁵⁷

The court is bound by its judgment once it is given, but clerical or arithmetical errors and obvious inaccuracies may be changed. Proceedings may also be held to make a judgment more complete.⁵⁸

The *judgments of foreign courts* are recognized as valid if judgments of German courts are enforceable in such foreign jurisdictions, except where (a) under German law the court rendering the decision had no jurisdiction, (b) the defendant was a German and either did not appear personally or was not served personally within the jurisdiction or in accordance with German formalities, or (c) the enforcement would be contrary to public policy or morality.⁵⁹ However, execution will not be allowed pursuant to foreign judgments until their admissibility is determined upon application for a warrant of execution thereunder.⁶⁰ (As to enforcement of foreign judgments see U. of Pa. Law Rev., vol. 81, May 1933, p. 795.)

SPECIFIC PERFORMANCE AND FINAL INJUNCTION

The primary remedial rights arising from a contractual relationship are for performance or nonperformance. The former is obtained by execution; the latter by injunction.⁶¹

However, public policy sometimes intervenes to set aside the right to specific performance (a) in contracts for personal services, (b) where a person may claim rescission in lieu of performance, and (c) where the circumstances necessarily change the remedy to a claim for pecuniary damages.

RESTITUTION AND PECUNIARY DAMAGES

Where a liability results from an unlawful act not necessarily arising from a contractual relationship, a right to compensation (Schadenersatz) accrues. This need not be a money compensation, but may be merely a restoration to the condition which would have existed if the event creating the liability had not happened.

Pecuniary damages are substituted for performance or restitution if those are impossible or if they do not afford sufficient compensation. Pecuniary damages may be chosen by the claimant (a) for personal injuries or damages to a thing, (b) where time has been made the essence of the agreement and he is unwilling to accept belated performance, (c) where performance is only partially possible, and so useless, or (d) a debtor may choose to pay if performance or restitution would require disproportionate outlay.⁶²

⁵⁷ The distinction is significant only because of the different remedies on appeal applicable to each. Appeals and revisions are allowed only on final judgments. Interlocutory judgments are appealable only in connection with final judgments.

⁵⁸ Z.P.O. 319-330.

⁵⁹ Z.P.O. 328.

⁶⁰ Validity of foreign judgments is governed by treaty with certain countries, but not with the United States. Full recognition is not accorded judgments of United States courts (Z.P.O. 722-723).

⁶¹ Cases under the rule requiring performance or restitution where damage has been inflicted by an unlawful act can be enforced by imprisonment or fine (Z.P.O. 883-892; but see also B.G.B. 322).

⁶² B.G.B. 249-251, 280; but see also H.G.B. 376.

MEASURE OF DAMAGES

The general rule to measure damages is that they must cover losses, including compensation for loss of profits.⁶³

In a mercantile agreement⁶⁴ of sale where time is of the essence, the difference between the sale price and the market price at the time and place where the sale should have been completed is recoverable.⁶⁵

Where on a sale there is a breach of warranty, compensation is obtained by the reduction of the purchase price.

Damages assessed against a carrier⁶⁶ for deterioration or loss of the merchandise include the profit if the damage has been caused by the willful default or gross negligence of the carrier; otherwise it is the value of the lost goods or the loss by deterioration less the saving of outlays.⁶⁷ Damages due to carrier's delay are assessed in full if they are caused by willful default or gross negligence; otherwise the amount of damage is the declared value of the shipment or, if no value is declared, is limited to the amount paid for the carriage.⁶⁸

Damages for an unlawful act or injury to a person are based on the effect on the injured party's earning power and success in life, together with recompense for physical pain and mental suffering (sometimes in the form of an annuity).⁶⁹

A person illegally depriving another of a thing must compensate for the loss or deterioration plus interest from the date serving as the basis for the calculation of the loss.⁷⁰

PENALTIES

In contracts, parties may agree to penalties in addition to full damages. Only where the amount of the penalty seems to be out of proportion will the court disturb the arrangement; but a penalty agreed upon by a mercantile trader can never be reduced.⁷¹

The penalty becomes payable immediately when a debtor is unwilling to carry out his contract or when an act is done contrary to instructions.⁷²

A person may claim performance or damages as well as payment of the penalty if the contract so stipulates. Damages may be claimed in lieu of penalty unless the contract provides otherwise.⁷³

SEQUESTRATION

In aid of execution a successful litigant may enforce his right to satisfaction against real property⁷⁴ of his debtor out of claims for payment or performance due the debtor.

⁶³ B.G.B. 252.

⁶⁴ In such transaction (*Fixgeschäft*), the party may withdraw from the contract and demand damages for nonperformance or insist upon performance, to obtain which he must, immediately upon default, notify the other party of such insistence. (See *Commerce Reports of May 20, 1929*, p. 498.)

⁶⁵ H.G.B. 376.

⁶⁶ As to the liability of the employer for acts of his employees, if the employer is in a contractual relation to the party damaged, he must pay; if not, he may be excused, if he exercised proper diligence and precaution in the selection of the employee (B.G.B. 276, 831).

⁶⁷ H.G.B. 430, 457, 611, 613.

⁶⁸ H.G.B. 429, 466.

⁶⁹ H.G.B. 824, 842-844, 847.

⁷⁰ H.G.B. 648-649.

⁷¹ B.G.B. 343; H.G.B. 348, 351.

⁷² B.G.B. 339.

⁷³ H.G.B. 340, 342.

⁷⁴ The judgment creditor has a right to seizure and sale (of property in the hands of a debtor) under the execution.

erty in the possession of the debtor is attached, on motion of the creditor, through a decree of sequester, and notice thereof is given to and entered in the appropriate land register (Grundbuch). Thereafter title cannot be changed or pledged. The property is either seized and sold for the creditor or it is placed in the hands of an administrator, to be managed by him, and he will thereafter receive the rents and profits arising from such management in trust and disburse them to the creditor until the claim is satisfied.⁷⁵

A successful litigant may require that claims for payment or performance due his debtor be not turned over to him. The third party, upon notice to that effect given by the bailiff, must retain such payments or performance for the benefit of the creditor.⁷⁶

A remedy in the nature of sequestration is also allowed the owner of a German patent or trade mark when infringing merchandise is imported.

APPEALS

Notice of appeal must be filed within 1 month. It need contain only a description of the judgment appealed and a statement that it is being brought. Within 1 month after notice has been served it must be supplemented by a statement on appeal (Berufungsbeurteilung), which must indicate in what respects the judgment will be contested and what changes will be sought. A notice of any new matter to be submitted, whether testimony or argument, must be added.⁷⁷

Within the limits set forth in the statement on appeal, the litigation is handled *de novo*. In other words, the subject matter before the court of first instance becomes the subject matter for the appellate court, except so far as the parties (on notice) submit new grounds of claim or defense or bring forward new facts and evidence. To change a statement of claim or add a new one requires the consent of the other party; but a new defense may be interposed either if consented to or upon proof by the party proposing it that he was unable to adduce it in the first hearing of the case. The judgment appealed from can be changed only insofar as change is sought in the statement on appeal.⁷⁸

REVISION AND COMPLAINT

Revision is a form of appeal, notice of which must also be given within a month. It is allowed only with respect to a final judgment of the Oberlandesgericht. It is distinguished from ordinary appeal in that the issue submitted must be on the legal side only. The facts decided by the lower court are binding, and the inquiry is limited to the question of whether the judgment is based on a violation of law.⁷⁹

Another special form of appeal allowed from decisions which are not final judgments (especially on orders made without oral hearing) and also on interlocutory judgments is appeal on complaint (Beschwerde).⁸⁰ Appeal on complaint will only be allowed from a

⁷⁵ Z.P.O. 848, 938.

⁷⁶ Z.P.O. 845.

⁷⁷ Z.P.O. 518, 518-519.

⁷⁸ Z.P.O. 525, 527, 536.

⁷⁹ Z.P.O. 545, 552.

⁸⁰ Judgments of the Oberlandesgericht are not reviewable by complaint, nor are judgments of the Landesgericht involving process costs (Z.P.O. 567)

review of the original decision of a court on complaint where a new and independent ground is found.⁸¹

EXECUTIONS

Execution is granted on all judgments, settlements made in court, and special payment orders of the courts (Zahlungsbefehle).

Executions may not be issued immediately upon the rendering of a judgment⁸² pending time for filing appeal. In certain cases provisional execution may issue immediately (a) if the court so orders, (b) pursuant to a default judgment, (c) where the debtor acknowledges the judgment, (d) where the case is based on a written document or a bill of exchange, if the sum involved is not more than 500 marks, (e) between lessor and lessee, master and servant, hotel and guest, or (f) where the creditor gives security before issuing the execution.⁸³ Such provisional execution is always granted at the risk of the creditor. If the judgment is reversed or altered, he must return to the debtor whatever he received upon the execution and compensate for loss suffered because of the execution.

In those cases not specifically mentioned as being subject to provisional execution, the successful party must sue out a writ in the court to obtain execution (Vollstreckbareausfertigung), in which proceeding the court again reviews the legality of the judgment.

Provisional execution upon foreign judgments cannot be obtained. The competency (correctness) of the judgment must be passed upon by a German court, which will issue a writ of execution if satisfied.⁸⁴ The writ is granted without determination of the merit of the decision of the foreign court; it is only necessary that the judgment of the foreign State be enforceable according to its own laws and that it comply with the German requirements as to form.

ENFORCEMENT OF EXECUTIONS

When a writ of execution is granted, either provisionally or upon final application, it is executed according to the court's order and with the help of the bailiff, as follows:⁸⁵

Where the order is to pay money, property in the possession of the debtor and belonging to him is attached by the bailiff and sold at public auction after a reasonable time.⁸⁶ Property which is not in the hands of the debtor but in which he has some right is attached by the bailiff by giving notice to the third party in whose possession the property is, forbidding such third party to dispose of the property or pay the debtor (sequester). Real property of the debtor is seized by the bailiff, and the court orders a security mortgage placed against this property in the land register.⁸⁷ Such property is then sold at public auction by the bailiff or is sequestered and managed by a trustee and the returns and profits are turned over to the creditor until he is fully paid.

⁸¹ Z.P.O. 568.

⁸² An execution against a military man cannot be issued in any case until the matter has been submitted to the military authorities for permission (Z.P.O. 752, 790).

⁸³ Z.P.O. 707-709.

⁸⁴ Z.P.O. 722-723.

⁸⁵ Z.P.O. 754.

⁸⁶ This is also true if the property is a ship (Z.P.O. 870).

⁸⁷ Z.P.O. 868-870.

When the order is to deliver personal property alleged to be in the possession of the debtor, if it is not in his possession the debtor must take oath that he does not have it and does not know where it is. If he refuses to take such an oath, he is fined for contempt and imprisoned.⁸⁸ Upon a return of the execution so reciting, the creditor may claim damages. If the thing to be delivered is in the possession of a third party, a sequester notice is served by the bailiff.⁸⁹ If it is an immovable or a ship, the bailiff transfers possession to the judgment creditor.⁹⁰

Where the order is to make a declaration upon a judgment for entry in a public register or similar purpose, it is deemed to have been done and the entry in conformity therewith can immediately be made.⁹¹

Where the defendant is ordered to perform an act, if such act can be done by another the court will appoint such other to perform the act and decree that he be paid by the debtor therefor. If the act can be done only by the debtor and he refuses, he is heavily fined or is imprisoned.⁹²

An order to forbear or delay action not obeyed renders the party liable to a penalty or imprisonment. In such a case the successful party may also, on motion, insist that security be posted against further recurrence of the act.⁹³

⁸⁸ Z.P.O. 883-884, 899-915.

⁸⁹ If the third party feels that the execution is against his interest in the property attached, whether in his possession or in the possession of the debtor, he may bring an action to set the bailiff's execution aside in the court out of which the execution issued (Z.P.O. 771).

⁹⁰ Z.P.O. 885-886.

⁹¹ Z.P.O. 894-896.

⁹² Z.P.O. 887-888.

⁹³ Z.P.O. 890.