

## The New German Law of Obligations: an Introduction

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On 1 January 2002, the so-called Act on the Modernisation of the Law of Obligations came into force in Germany.[see our bilingual translation of the [German Civil Code \(BGB\)](#) - ed] This Act has dramatically changed the German Civil Code (*Bürgerliches Gesetzbuch*, BGB). Without doubt, its amendments amount to the most important reform of the German BGB since it was originally enacted in 1900. The following is an introduction to the scope and some central issues of the new German law of obligations.

### **I. Scope and Genealogy of the Reform**

The new Law of Obligations has three different sources. The first was the necessity to transpose several EC Directives. Among them, the most important is the Consumer Sales Directive. The other two, namely the Directives on E-Commerce and Late Payment, relate to the law of obligations only in some, and less central, aspects. Their transposition within the framework of this major reform has done little to influence the character of the new law. The time of the enactment (1 January 2002) was determined by the deadline for the transposition of the Consumer Sales Directive. In the past, Germany has suffered several severe losses of taxpayers' money caused by state liability under the Francovich Doctrine because of delayed transposition of EC Directives. In consequence, the German government is now eager to transpose Directives in time. The desire to meet this target was responsible for the speed of the whole reform. Many of the complaints which in particular academics had voiced against the reform relate to the speed of the governmental and parliamentary proceedings.

The second source of the new Law of Obligations was a draft which had been prepared by a reform commission in a process which dates back to the 1970ies, and which had initially been entrusted with the task of preparing a reform of the entire German law of obligations. That committee was composed i.a. of government officials from the Ministry of Justice, judges,

and several of the most famous German law professors. In 1992, this commission produced a comprehensive draft for the reform of the German law of obligations. In 1994, a bi-annual assembly of German lawyers entitled *Deutscher Juristentag*, voted with an overwhelming majority for the enactment of the reform. But that seemed to be the end of the story. The draft was silently dropped and gathered dust in the filing cabinets of the Federal Ministry of Justice. It has been said that the main reason for this inactivity was the opposition of the mighty associations of the German industry. They claimed that the new law would have severe disadvantages for their members. However, after the European Consumer Sales Directive was passed, that situation changed completely. The Ministry of Justice at once took the old draft out of its drawers, blew off the dust and set out to transpose the Directive by enacting this draft. The reader may wonder what gave German government officials the idea to transpose a Directive by resurrecting a failed reform draft. This question will be dealt with below. At any rate, the result is that the new German law of obligations is based on the old draft, and the major characteristics of this draft are now part of the present German law.

The third source of the new German law of obligations was already part of the existing German law, but not as part of the Civil Code. Around the BGB, a corona of smaller statutes on more specific matters, which were all closely connected to private law had developed. The German legislator took this opportunity to integrate some of these statutes into the BGB. As the reader will notice, all areas of law treated below are at least partially also governed by European Directives. Taken together with the new law of the sale of goods, central parts of the new German BGB can be said to have transposed European Directives. This is one of the reasons why the reform can also be understood as Europeanisation of the BGB.

## **II. Direction of the Reform**

I will now return to the question why it was possible to make use of the old draft in order to transpose the European Consumer Sales Directive. The reason is very simple. Both the Directive and this German draft share the same ancestor. This is, unsurprisingly, the Vienna Convention on the International Sale of Goods (CISG). The two sources - Directive and old German draft - could easily flow together because they were of the same origin. In particular, their systems of remedies, and the notion that every remedy of the buyer requires a breach of contract, was similar, and so the German law could copy the system which had been developed by the old reform commission

This observation allows some first general statements on the new system of the BGB's new law of obligations. The central prerequisite for any remedy of the buyer (breach of contract) was broadened to apply to the whole law of contract. Within the German discussion, this was referred to as the "large solution". The new German law of obligations requires a "breach of duty" in order to grant remedies to the obligee. This was a fundamental change, because the BGB had previously drawn a sharp distinction between e.g. the buyer's rights in the event of defects on the one hand, and in the event of non-performance on the other. German law has now developed a general type of breach of contract – to be precise, the notion even transcends contract law, and extends, as breach of duty, to the entire law of obligations. This makes many distinctions, which had previously been necessary, either superfluous or at least easier.

With this background, the transposition of the Consumer Sales Directive was in itself an easy task. The law of contract, and in particular the law of the sale of goods is - as a rule – non-mandatory law. The parties to the contract can agree on rules which are different from the provisions of the BGB. But as the entire German law on the sale of goods is now modelled on the Directive, the German legislator could transpose the consumer aspects of the Directive by very few sections (in particular § 475 BGB), which make the provisions of the BGB mandatory in favour of the consumer in the case of a consumer sale.

### **III. A Rough Outline of Some of the Consequences**

#### ***III — 1. The new System of Remedies***

One of the most relevant issues of the German law of obligations is its new system of remedies.

Perhaps I should first make clear what I mean when speaking about remedies. In German law, we distinguish the obligee's claim for specific performance (primary claim) from other rights of the obligee which may arise in case of non-performance or insufficient performance. The latter are called secondary claims. When I speak of remedies, this only relates to the secondary rights, which could be e.g. a claim for compensation, the right to terminate the contract, or to reduce the price.

In order to understand the fundamental shift from the old system of remedies to the new one, we should first take a look at the situation which existed before the amendments came into force. Formerly, remedies of the obligee (e.g. the buyer) under the BGB depended on the type of the breach

of contract which the obligor had committed. There were four main types of breach of contract which were called:

- *Unmöglichkeit* (impossibility)
- *Verzug* (delay)
- *positive Vertragsverletzung* (positive breach of contract)
- *Gewährleistung* (obligee's rights in the event of defects)

One of the most difficult problems within the old system was how to distinguish between these four types. The distinction was necessary because the remedies which were available to the obligee for each of these types of breach depended on completely different prerequisites. The most important case may serve as an example. In many cases the obligee (e.g. the buyer) was in a relatively weak position in the event of defective performance (e.g., delivery of defective goods). His rights were subject to a very short period of limitation (in the example given, 6 months counted from the date of delivery) and he could claim compensation only in exceptional cases. However, the situation of the buyer was completely different if the seller had not delivered at all (non-performance). In this case, the buyer could generally claim compensation including consequential loss, and the limitation period was much longer (most frequently 2 years).

This led to some rather strange distinctions. For example, in one famous case the parties concluded a contract for the sale of summer wheat seed. After more than 6 months, it turned out that the seed obviously was winter wheat, which could only be sown in the autumn. Unsurprisingly, the buyer claimed compensation because he had sown the wheat in the spring and it had not grown. The crucial question was now whether the wheat which the seller had delivered was defective wheat (making this delivery of defective goods and thus a case of *Gewährleistung*) or something completely different (making this a case of non-performance). If this was delivery of defective goods, the buyer could claim compensation only within a limitation period of six months after delivery, and this period had already expired. Consequently, the buyer would have had no rights at all against the seller if the wheat delivered was considered as defective goods. On the other hand, if the wheat delivered was considered to be completely different goods ("*aliud*"), this was considered to have the same consequences as if nothing had been delivered at all. In this case, the buyer would be entitled to claim full compensation for all the damage which the delivery of the wrong wheat had caused. Incidentally, the *Bundesgerichtshof* (Federal Court of Justice) decided in favour of the buyer, but this was not undisputed. (judgment of 20 November 1967,

reported in *Neue Juristische Wochenschrift* 1968, p. 640). There are, of course, no suitable general criteria for making this crucial distinction between the delivery of defective goods and the delivery of an *aliud*.

The new BGB has changed completely its system of remedies in order to make such distinctions unnecessary, or at least much less relevant. The new central prerequisite for remedies of the obligee in case of non- or bad performance is "breach of duty", which is a very general concept. It is no longer of significant importance whether defective goods were delivered, or whether the obligor committed another breach of duty. In particular, it is recognised that the seller may commit a breach of duty purely by delivery of defective goods. The core provision which makes this clear is [§ 433](#) (1), sent. 2 BGB.

The prerequisites for the obligor's remedies now depend on the type of remedy which is sought after. These include:

- compensation
  - in lieu of performance
  - for delay
  - other damages
- termination
- other possible remedies, e.g.
  - removal of a defect
  - price reduction
  - delivery of new goods free from defects

## ***2. Greater Pressure on the Obligor to Perform***

The changes implemented for the system of remedies have in many ways changed the wording of the BGB without affecting the outcome of most cases. The purpose was primarily to make the law easier to understand. However, there are some aspects where the substantive law has really been affected and changed, so that for some situations, the new German law of obligations leads to other results than its predecessor. Several of these changes can be summarised under the headline "greater pressure on the obligor to perform and higher risk of being liable for damages caused by non-performance". I will try to exemplify this with the provisions on the so-called compensation in lieu of performance.

Imagine the following standard situation. The obligor does not perform. We do not know precisely why. An obligor who does not perform may or may not indicate reasons for this failure to the other party. But as an obligor

is under some pressure to present excuses, the obligee cannot really be sure whether the obligor is telling the truth.

Under the old BGB, § 326 BGB applied in such a case. This provision granted compensation in lieu of performance if the following, rather long list of prerequisites was fulfilled:

- non-performance
- responsibility of the obligor for the failure
- notice to perform
- fixing a reasonable period of time
- threat to refuse performance after expiry of the period
- expiry of the fixed period

Two of these prerequisites:

- notice to perform
- threat to deny performance after expiry of the period

are not indicated in black colour but in a lighter grey as if they were fading. And indeed, these two prerequisites have faded not only in colour but also in actual law. The successor of the former § 326 BGB is the new [§ 281](#) BGB. The list of its prerequisites for a claim for compensation is now much shorter:

- non-performance (which is, of course, a breach of duty)
- liability of the obligor for the failure
- fixing a reasonable period by the obligee
- and the expiry of the fixed period

A notice requesting performance and the threat to refuse performance after expiry of the period are no longer necessary under the new [§ 281](#) BGB.

The new German law of compensation has abolished these two devices, which were introduced by the original legislator of the BGB in order to protect the obligor. After the recent reform it is much easier for the obligee to terminate the contract and to claim compensation in lieu of performance. In other words: it is much more dangerous for the obligor not to perform. And this - of course - increases the pressure on him to perform. This was an explicit goal of the reform.

This tendency of the new BGB to increase the pressure on the obligor to perform can be illustrated by two more examples.

First, the limitation period for the buyer's remedies for defective goods is now much longer than it used to be. For moveable property, i.e. goods, the limitation period has been lengthened - as a general rule - from 6 months to 2 years ([§ 438](#) (1) no. 3 BGB). This was, of course, a requirement established by the European Consumer Sales Directive. However, German law has lengthened the limitation period for any sale of goods, i.e. including business to business transactions. The risk of contractual liability in the event of delivery defective goods under a sales contract has increased substantially.

Second, the risk for the seller to become liable for compensation in the event of defects is much greater than before. As mentioned above, under the old law, the buyer was allowed to claim compensation only in exceptional cases, e.g. if the seller fraudulently concealed a defect or if he gave a warranty for certain qualities of the good sold. Under the new system of remedies, the number of situations in which the seller is liable for compensation of the buyer's loss in the event of defective goods has increased dramatically. As a general rule, any delivery of defective goods amounts to a breach of duty ([§ 433](#) (1) BGB) and can thus trigger the buyer's claim for compensation. According to [§ 280](#) (1) sentence 2 BGB, the seller can only escape from this liability if he proves that he was not responsible for this breach of duty.

Taken together, this shows that one of the most important features of the reform is that it increases the pressure on the seller to perform properly in order to avoid being exposed to remedies of the buyer which are much more effective and costly compared to the system of remedies which prevailed during the first century of the BGB's existence, i.e. the 20th century.

### ***3. Freedom of Contract and Information of the Buyer***

The reform brought several new and drastic restrictions to the freedom of contract. This is partially due to the influence of EC Law, and in particular the Consumer Sales Directive. As already mentioned, the new [§ 475](#) BGB makes the provisions of the BGB which govern the sale of goods mandatory in cases of Consumer Sales, so that parties are not free to deviate from those provisions to the detriment of the consumer. But freedom of contract is also restricted in cases of sales other than consumer sales.

Two examples should suffice in the present context. [§ 478](#) BGB establishes a mandatory right to recourse by a businessperson to his supplier if the businessperson has become liable for defects in the goods sold to his

customer. And [§§ 307-309](#) BGB impose important restrictions on deviation from the BGB's provisions by way of Standard Business Terms. The result is that the new German sales law imposes much more restrictions on freedom of contract than previously.

These new limits force the parties to regulate contractual risks by using the last effective possibility to restrict the seller's liability, namely the possibility to agree on the quality of the goods sold according to [§ 434](#) (1) BGB.

Take the example of the sale of a used car. The parties write clearly into the contract that the radiator is leaking. Consequently, the object of the contract is a car with a leaking radiator, which therefore does not amount to a defect in the sense of [§ 434](#) (1) BGB. According to this provision, the thing sold is free from defects if it has the agreed quality. As it was agreed that the radiator is leaking, the car has exactly the agreed quality and is therefore free from defects. Without defects, there are no remedies for the buyer.

Such an agreement on the quality of the goods sold has the effect that it informs the buyer about the characteristics of the goods. In my view this is precisely the effect which the European and even more the German legislator wanted to create. The law makes use of restrictions of the freedom of contract in order to inform the parties to the contract, especially the buyer, about the goods which are on the market. This relationship between the new restrictions of the freedom of contract on the one hand, and the remaining possibility to agree on the quality of the goods sold on the other, could be described as creating an indirect duty of information. The informed buyer – this includes in particular, but not exclusively consumers - can decide whether he wants to acquire the goods even if they are not in an optimal condition (e.g., the radiator is leaking). The parties are thus forced to negotiate the price on a high level of information about the characteristics of the goods sold.

This effect of the new restrictions of freedom of contract is, in my view, one of the most remarkable features of the new BGB. German law has done considerably more on this point than was required by European directives. My personal impression is that we are currently witnessing a giant economical experiment in Europe, and perhaps even more clearly in Germany. It is still an open question whether the price and the quality of products can be affected by such regulatory devices as we have seen here to operate in German Law.

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Vertragsfreiheit und Informationszwang nach der Schuldrechtsreform,  
Zeitschrift für das gesamte Schuldrecht (ZGS) 2002, pp 72 ss.  
Commentary to §§ 305-310, 312-312 f BGB in: Handkommentar BGB, ed.  
by Dörner et al., 2nd ed. 2002  
Commentary to §§ 286-288 BGB and Late Payment Directive, in:  
Anwaltkommentar BGB, ed. by Dauner-Lieb et. al., 2002  
Schuldrechtsreform und Gemeinschaftsrecht (together with R. Schulze) in:  
Die Schuldrechtsreform vor dem Hintergrund des Gemeinschaftsrechts, ed.  
by R. Schulze and Schulte-Nölke, 2001, pp. 3 ss.