Overview of the German legal system and its role in light of Germany’s membership in the European Communities

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Foreigners interested in starting a business or investing in German companies are generally attracted by the prospect of expanding into other European markets. Germany’s membership in the European Communities (EC) is a beneficial factor when deciding whether to invest in Germany, especially, because of the recent broadening of the EC. However, there also have been concerns about the implications of the dual European and German legal systems. Investors may wonder whether a German venture requires familiarization with two, often-conflicting bodies of law, or if businesses in Germany frequently have to deal with administrative authorities at both the national and international level with regard to the same transaction. The answer to such questions is “no”. Given the structure of the EC and particularly the manner in which EC institutions pass laws, an investment in Germany does not place investors in a legal quagmire.

As a fundamental principal, the EC and its institutions possess the power to pass legislation in only those areas in which an express delegation of national authority exists. For this reason alone, large numbers of regulatory areas remain outside of the EC’s control. For example, most civil, criminal, and administrative laws remain the sole province of the Member States. In general, the EC’s authority is limited to those regulatory areas, which are essential to the establishment of a common market. Furthermore, the laws that have been passed by the EC tended to take the form of “directives.” As will be explained in detail in the Chapter entitled “Institutions of the EC”, directives do not, as a general principal, take effect until after they have been incorporated into national law. This special characteristic of directives is intended to give the Member States the flexibility of choosing the manner in which a directive becomes law in their own country. Accordingly, Member States can choose a directive that is most compatible with their particular legal system. For individuals and business enterprises alike, it is often not easy to recognize whether or not a national law is based on a European directive. In sum, EC directives do not constitute an overlay of regulations which investors must familiarize themselves with, but rather comprise an integral part of a Member State’s national law.

Much the same applies to those areas in which the EC has enacted a type of legislation known as a “regulation”. A regulation does not require incorporation into national law in order to be effective, but as a rule is implemented by the national authorities. For example, if a German administrative authority applies an EU regulation in its dealings with German residents and they feel an error has occurred, action can be taken only against the national authority and, in doing so,
such action usually operates solely within the German administrative or judicial systems.

For these reasons, the direct effect of EC law on German residents or businesses is relatively small. However, that is not to say, that the EC’s influence should be downplayed. The numerous areas of law impacting the establishment and operation of businesses in Germany are often reflective of EC law. Nevertheless, for the most part EC laws have been incorporated into national law and are subject to Germany’s legal system. It is within this system that foreign investors will predominantly conduct their business transactions.

For the most part, Germany’s legal system is stable and smooth working. It is based on the Continental European legal tradition as opposed to Anglo-Saxon law upon which the U.S. legal system is based. The primary difference between the two systems is that the Continental European legal system is based on “code law” as opposed to “case law”. In accordance with the Continental tradition, the German legal system consists essentially of written laws. Nearly all potential regulatory areas are the subject of formal and detailed codification. Many of Germany’s legal codes are the final product of decades of careful deliberation and refinement. This offers foreign entrepreneurs and investors considerable advantages. German law is so clearly structured and transparent that contract terms can be standardized to a very large extent. All the standard practices and regulations governing a business’s conduct are codified in the German Civil Code (BGB, or Bürgerliches Gesetzbuch). Therefore, if no special terms are agreed upon between the parties, the terms and provisions of the BGB automatically apply. In other words, in the U.S., business contracts require the clear and detailed statement of all the terms the parties agree to. Contracts in Germany tend to be considerably shorter, which lowers their drafting costs accordingly.

German law has undergone numerous reforms in recent years, which, for the most part, have had a very positive impact on business activities, even though there have been some less favorable developments. The Commercial Code was liberalized by broadening the definition of “merchant”, thus, making it easier for people to get started in business. Additionally, the Handcrafts Code (Handwerksordnung) was modified to make it easier to demonstrate professional qualification. Business activities in the domestic market were also facilitated through a considerable loosening of the laws regulating unfair trade.

On the other hand, disadvantageous are the new regulations in contract and civil process law. Contract law now ensures an extraordinary high degree of consumer protection at the expense of merchants. Furthermore, the extent and complexity of the reforms have led to a certain degree of legal confusion. The changes made in civil process law make it more difficult to acquire access to appellate courts, which very often necessitates cost-and-effort intensive proceedings right from the start.

As in the U.S., it is the task of the courts to interpret the written law. Because a number of German codes are more than a hundred years old, the case law pertaining to certain individual provisions of them is very extensive. The courts have the primary task of interpreting the statutes, regulations, and Constitution, and they also play a role in filling in the gaps of laws where necessary. However,