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German Tax and Legal News

Is There a Need for a Special Law on General Terms and Conditions for Companies?

The German law on general terms and conditions is very strict – even in b2b relations. Is that up-to-date?

German legal advisors often come up against incomprehension from national and international clients when they try to explain the depths of German law with respect to general terms and conditions. This applies particularly for the (im)possibilities to agree an appropriate limitation of liability e.g. based on the size of the commercial order, since companies are currently not in a position to limit their liability with legal certainty when concluding standard agreements with other companies. This was also the result reached by a study commissioned by the German Federal Ministry of Justice on "German Law on General Terms and Conditions for Agreements Between Companies – With Special Consideration of Limitations of Liability".

The background of the study was criticism from sections of the business community that the examination of the general terms and conditions disproportionately strongly restricted the contractual freedom of companies. The study carried out from August 2013 through July 2014 was to clarify whether and to what extent there is need for reform.

Previous Positions Regarding the Law on General Terms and Conditions
However, the criticism of the law on general terms and conditions is not new. The "Initiative on the Further Development of the Law on General Terms and Conditions" (Initiative zur Fortentwicklung des AGB-Rechts) was already established in 2008. It was created by law firms and business associations such as VDMA (Verband Deutscher Maschinen- und Anlagenbau – German Engineering Association) and ZVEI (Zentralverband Elektrotechnik- und Elektronikindustrie e.V. – German Electrical and Electronic Manufacturers' Association), the Chamber of Commerce in Frankfurt/Main, legal scholars and in-house attorneys. The initiative argues that the law on general terms and conditions was originally planned as a consumer protection law, since the legislation only included the possibility of examining the content of general terms and conditions as a response to the proposal by the Association of German Jurists (Deutscher Juristentag) in 1974. However, the original aim of the legislation to enable more flexibility and elasticity for the b2b sector was neglected thereby. The German Federal Court of Justice (Bundesgerichtshof – BGH) assumes in its established court practice that the prohibited clauses in § 308 and § 309 German Civil Code (Bürgerliches Gesetzbuch – BGB) are "indications for inappropriate discrimination of the contractual partner" in business transactions. It is generally assumed on this basis that the same standards apply in business transactions as towards consumers.

As a first success of the Frankfurt initiative the German federal states issued an audit assignment to the Federal Ministry of Justice; there was a hearing on the subject in March 2012. A few months later in September 2012 the 69th conference of the Association of German Jurists subscribed in its resolutions to the view that the law on the general terms and conditions required reform in the b2b sector. The 69th conference of the Association of German Jurists passed the following specific resolutions:

- The conference rejected the extensive equal treatment which was developed by court practice of general terms and conditions of business in the b2c and b2b sectors, in particular the indications in § 308 and § 309 BGB.
- The requirements for seriously negotiating contractual conditions in the b2b sector should be brought into line with the customs of entrepreneurial contractual negotiations.
- In the b2b sector the benchmark for examining the content should be aligned to good entrepreneurial practice in an industry and/or business sector.

However, there are not only supporters of a reform for the law on general terms and conditions. The counter-initiative "pro AGB-Recht" consisting of 30 business associations from every industry was also established in 2012. In a joint declaration from April 2013 the

initiative demonstrates that the law on general terms and conditions of business has also stood the test in relationships between companies.

Result of the Study by the German Federal Ministry of Justice
In its analysis of high-court practice the recent study concluded that effective limits and exclusions of liability in the scope of application of § 305 BGB are hardly possible. It is generally not possible to consider an exculpation for gross negligence since indicative effect is attached to § 309 No. 7b BGB for entrepreneurial legal transactions. In addition the prohibition of exculpation for major contractual obligations which also applies to slight negligence and is derived from § 307 Subsection 2 No. 2 BGB comes into play. The remaining possibility to limit liability is also of little practical relevance since according to the established BGH court practice the liability for infringing major contractual duties must at least cover the foreseeable damage which is typical for such agreements (foreseeability formula).

Furthermore the examination of the limitations of liability in various types of agreement which were customary for the industry resulted in the fact that particularly limitations of liability in the amount of compensation which stipulate the maximum liability at a certain percentage of the agreed salary are prevalent in entrepreneurial legal transactions and correspond to the market standard in many sectors. The latter particularly applies to agreements with regard to corporate acquisition, machinery and plant engineering, contract logistics and outsourcing where the corresponding limitations of liability are a core component of the risk allocation agreed by the parties and typically correspond to reductions in liability in the form of guarantees, contractual penalties or lump-sum compensation. The customary limitations of liability do not satisfy the standards derived by court practice from § 307 et seq. BGB.

The validity of the limit of liability therefore crucially depends on whether the clause satisfies the requirements in § 305 Subsection 1 Sentence 3 BGB for an individual agreement. It is a question here of a specific case. However, the problem is generally that typically none of the parties questions the necessity of limitations of liability in practice since they are customary in the industry. Consequently there are generally no serious negotiations about the clause (putting it up for serious negotiation) which is, however, a precondition for an individual agreement in established court practice. Furthermore the study concluded that agreements are made in entrepreneurial legal transactions to a large extent on the basis of standardized contractual conditions with little desire for particular arrangements of the agreement and negotiations and so they will therefore generally fall under the scope of application of § 307 et seq. BGB. An entrepreneur who offers proposals for the clause to another entrepreneur even if only in order to prepare for contractual negotiations can hardly avoid being seen as a party using general terms and conditions. Established court practice generally assumes that it is “pre worded contractual conditions which a contractual party offers to the other party in order to conclude the agreement” (§ 305 Subsection 1 Sentence 3 BGB). Established court practice places high demands on when a clause is considered to have been seriously negotiated.

Finally the study by the Federal Ministry of Justice comes to the conclusion that there is a need to reform the law on general terms and conditions in the b2b sector and proposes moving away from the BGH’s foreseeability formula and introducing a regulation where limitations of liability in the amount of compensation are permitted in entrepreneurial legal transactions. However, this should only be possible if the limitations of liability do not remove the incentive for the user to act judiciously, explicitly pointing out the maximum amount of liability to the opposing party. Furthermore the introduction of a limit in the amount which is linked to the value of the subject matter of the agreement is recommended. If the limit is reached, § 307 et seq. BGB would no longer apply and/or a regulation would be introduced where the examination of the general terms and conditions would apply (accordingly even above the limit) if there is considerable economic disparity.

Other Proposals for Reforming the Law on General Terms and Conditions
The reform proposal of the study by the Federal Ministry of Justice is not by any means the only one.

- Negotiation vs. Serious Negotiation

The “Initiative on the Further Development of the Law on General Terms and Conditions” and some others propose adding a new sentence 4 to § 305 Subsection 1 BGB:

„If a contractual condition is used vis-à-vis an entrepreneur, a legal entity under public law or a special fund under public law, it is considered to have been seriously negotiated if the contractual parties negotiated it individually or in connection with other provisions of the same agreement in

a manner which is appropriate for the subject of the agreement and the circumstances of concluding the agreement." (Wird eine Vertragsbedingung gegenüber einem Unternehmer, einer juristischen Person des öffentlichen Rechts oder einem öffentlich-rechtlichen Sondervermögen verwendet, so gilt sie als ausgehandelt, wenn die Vertragsparteien über sie im Einzelnen oder im Zusammenhang mit anderen Bestimmungen desselben Vertrags in einer dem Gegenstand des Vertrages und den Umständen des Vertragsschlusses angemessenen Weise verhandelt haben.)

This new sentence is intended to give entrepreneurs the possibility to circumvent the strict standard which established court practice places on the term "serious negotiation". Indications for a negotiated contractual condition could be contractual negotiations on a longer period, previous agreements with the same content, excluding modifications, knowledge or grossly negligent ignorance of the legal and economic significance of pre-worded contractual conditions, legal advice or the size of the company, for example.

This legislative proposal provides for a basis for evaluating individual cases. Under such circumstances a clause can undoubtedly be considered to have been seriously negotiated in an agreement which was negotiated by external attorneys or in-house attorneys of the contractual party even if it was not modified or only negotiated in a rudimentary manner. The BGH's view that it is not sufficient if the parties discussed the agreement in general and modified parts thereof while the respective liability clause remained unmodified can also be corrected on the basis of the proposed legislative text.

- Differentiation in Examination of Content

Furthermore the reform proposal will also modify § 310 Subsection 1 Sentence 2. Instead of "the customs and practice which apply in commercial transactions must be taken into appropriate consideration" the new Sentence 2 would read as follows:

"Contractual provisions are unsuitable which contrary to the principle of good faith strongly deviate from prevalent entrepreneurial practice." (Vertragsbestimmungen sind unangemessen, die entgegen dem Gebot von Treu und Glauben von gängiger unternehmerischer Praxis grob abweichen.)

An alternative wording is also proposed: *"Customs and practice which apply in commercial transactions as well as circumstances in entrepreneurial business transactions, in particular the need to protect certain entrepreneurs which is less than in comparison with consumers, must be taken into account." (Im Handelsverkehr geltende Gewohnheiten und Gebräuche sowie Gegebenheiten des unternehmerischen Geschäftsverkehrs, insbesondere die im Vergleich zu Verbrauchern geringere Schutzbedürftigkeit bestimmter Unternehmer, sind zu beachten.)*

The supporters of a reform wish to create a new standard here for evaluating general terms and conditions between entrepreneurs which should no longer be subject to the strict standards of consumer agreements. Instead a general clause for evaluating the examination of content should be created.

Comment
Although the publication of the study by the Federal Ministry of Justice does not constitute an example for possible legislative reform, it clearly shows together with the other reform proposals that there is a need for new legislation for b2b transactions in order to give companies legal certainty and an appropriate framework for reasonable limitations of liability in general terms and conditions. The study by the Federal Ministry of Justice and its conclusions are very welcome considering the efforts which are constantly in existence when giving practical legal advice to draft clear limitations of liability, particularly in the amount of compensation, in standard agreements and in general terms and conditions. Yet the road to a law on general terms and conditions for entrepreneurial transactions still seems very long.

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