

Debt recovery in Germany

Information needed (of creditor and debtor):

- Full name (if natural persons) respectively company's name, legal form (if incorporated), full name(s) of managing director(s), registration-No. with the commercial register (only of debtor)
- Complete address
- Copies of contracts, terms and conditions, correspondence, invoices, reminders
- Full names and addresses of witnesses, that are able to testify in court to certain agreements between the parties

Note: According to German law, a debtor gets into the state of „delay“ 30 days after he has received the invoice or any equivalent reminder. This is important because he then has to refund the creditor's expenses, legal-fees etc.

Furthermore the creditor may then claim the legal interest, which is 5% above discount rate.

1. Step: **extra-judicial phase**

This merely consists of more or less friendly correspondence with no effect!

2. Step: **judicial phase**

Basically, German law provides two different procedures:

a) Default action

The creditor has to apply for a formal „default summons“, issued by court and sent to the debtor, who then has a period of 2 weeks to protest.

If he does so, the case can be transferred into normal court procedures.

If he does not protest, the creditor can apply for a formal „order of payment“, also issued by court and also delivered to the debtor, who then has another period of two weeks to protest.

If he does so, the case can be transferred into normal court procedures.

If he does not protest, the order of payment will gain legal validity and the case is closed.

The order of payment, however, can be executed, even – in case of a debtor's protest - on a provisional basis.

On the other hand, this procedure might take time and there are plenty of ways for the debtor to protest and, thus, cause delay. Besides, further delay may be caused by the chancery as there are no time limits to be observed by court officials.

This alternative, therefore, is only recommended if no protest of the debtor is expected, which is the case mostly if the debtor is only a short step away from insolvency or – for other reasons – doesn't care about his business anymore...

b) law suit

The procedure usually starts with a written petition, delivered to court by the plaintiff's attorney. This petition is then forwarded to the defendant with court-order to respond within a given period (usually 3 to 5 weeks, prolongation possible). Depending on the content of the defendant's statement, the court will take further action.

In any case there will be a hearing in court, and – if held necessary by the judge – the taking of evidence. The sentence will be given usually three weeks after the final hearing.

The judgement will be delivered to both, plaintiff and defendant, by the chancery. Delivery sets off the period for appeal (1 month).

The judgement can be executed before its legal validity. This may cause compensation claims by the defendant, if the judgement is altered by the court of appeal.

3. Step: **execution**

Execution usually is conducted by the bailiff. He will – if necessary and if authorized by court - search the debtor's premises for items that might be levied. If this effort fails, the debtor can be forced to give a written overview on all his property to enable the creditor to find other objects of execution, e.g. bank accounts or real estate.

Most important: **COSTS**

Lawyer's fees and court fees in Germany are strictly regulated by federal law and directly correspond to the amount of money claimed. Therefore it is impossible to predict the costs of a lawsuit without knowing the exact amount of the claim.

BUT: German lawyers are free to negotiate fees with foreign clients. This may result in a flat-rate (very risky for the lawyer!) or in an hourly rate. Contingency fees are still a source of controversial discussion within the German Bar Association and might well be considered illegal.

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Pre-Litigation

Essential information required

Prior to commencing debt recovery proceedings the following information has to be obtained:

- a) Precise names and addresses of both creditor and debtor;
- b) In case of companies being concerned: Names of the legal representatives of the companies;
- c) All documents substantiating the debt to be recovered (written agreements, general terms and conditions, orders, order confirmations, bills of delivery, invoices, other correspondence);
- d) In case a claim cannot be substantiated with documents only, other evidence has to be provided (witnesses, expertises etc.).

Checks available to establish if the debtor is worth suing

Several credit reference agencies provide economical information on debtors. The coverage and quality of the information provided varies substantially. Especially where not commonly known companies are concerned, these agencies often are able to provide essential data justifying the cost arising from employing their services.

Additionally, enquiries concerning the question, whether a certain person or company has filed for insolvency, can be filed with Local Courts.

Letter before action/telephone collection

In Germany, usually the creditor himself tries to collect outstanding debts via telephone and/or collection letters. Once proceedings have reached a stage at which attorneys have been consulted, telephone collection in most cases is considered to be ineffective.

Once an attorney has been consulted, usually an attempt is made to recover the debt by sending an attorney's collection letter containing the warning that in case payment is not effected within a certain period of time a lawsuit will be filed.

If the debtor recognizes the debt but asks for a delay to be granted or the creditor has – in spite of the debtor’s oral recognition of the debt – doubts concerning the debtor’s willingness to pay, the former should secure his claim by prompting the latter to sign a notarised acknowledgment of indebtedness which serves as an execution deed against the debtor. Normally such a document will be combined with a payment’s agreement.

Default Summons

Concerning pecuniary obligations only, German Local Courts upon a special formal application issue default summons without examination of the justification of the claim. In case the debtor does not formally object and the creditor files a corresponding application, the courts will issue an enforceable default summons. If the debtor again does not object, this enforceable default summons automatically becomes an execution deed. If, however, the debtor does object – either reacting to the initial default summons or to the enforceable one –, the default-summons-proceedings merge into normal court proceedings.

Default interest

The right to claim default interest arises directly from the law. As far as consumers as debtors are concerned, the applicable interest rate amounts to 5 percentage-points over the respective base rate as fixed by the European Central Bank. Among companies the rate in most cases amounts to 8 percentage-points over the European Central Bank's base rate. Higher rates can be asserted either if the creditor is able to prove that he has to refinance at interest rates higher than those provided by the law or if both parties have contractually agreed upon higher rates to be applicable in case of default.

Retention-of-title-clause

Parties to a contract are free to agree upon a retention-of-title-clause. Such a clause according to German law provides for goods already delivered to the debtor and being still unprocessed and identifiable to remain in the ownership of the vendor; for the excluded cases of goods processed or mixed with other material, German law offers legal solutions which in their effect equal a retention-of-title-clause.

Such a retention-of-title clause does, however, offer only the level of security provided by full title. If, therefore, a third party acquires ownership of the goods via bona fide acquisition from

the debtor, the title passes to the third party regardless of the retention-of-title-clause, with the vendor being limited to compensation claims.

Legal Proceedings

General Remarks

Either on debtor's objection to default summons or on the formal filing of an action with a court legal proceedings commence. In either case the action will be served upon the debtor, who in turn has to respond within a certain period of time. Should the debtor/defendant fail to answer within this period, the court will – on corresponding application of the claimant – render a judgment in default according to the claimant's motion, provided the facts presented in the pleading justify the claim. On the defendant's appeal against such a judgment in default (to be lodged within two weeks) the regular proceedings will be resumed.

Depending on the proceedings chosen by the respective court and the complexity of the issue at hand a first hearing on average takes place approximately three to four months after an action has been filed. This period may vary considerably from issue to issue and from court to court. Usually, each hearing will be prepared by the exchange of written pleadings. In case of one party's non-attendance to a court hearing, the court issues – on corresponding application of the opposing party – a judgment in default against which the non-attending party has the possibility of appeal within two weeks.

The overall duration of the proceedings themselves cannot be generalized; it may vary from only one hearing in simple cases to several years in complex matters.

The German courts are obliged to try at all stages of a lawsuit to achieve an amicable settlement of the matter. If the parties agree to such a settlement, it is placed on the court record. Such an amicable settlement recorded by the court serves as an execution deed concerning all provisions set forth therein.

Competent courts / Appeal

Claims exceeding the sum of EUR 5.000 have to be tried before the Regional Courts ("Landgerichte"; before these courts the parties are legally required to be represented by an attorney) whereas lesser sums fall into the competence of the Local Courts ("Amtsgerichte";

even though the parties may plead their cases before these panels themselves, the involvement of an attorney – especially where international matters are concerned – is highly advisable).

Within the jurisdiction of the Regional Courts cases in which both claimant and defendant are merchants can under certain circumstances be brought before the commercial divisions of the Regional Court, each consisting of one legally qualified judge and two honorary judges, the latter being merchants appointed to their task by the Local Chamber of Commerce and sworn in to perform their duty as judges with full voting rights concerning the rendering of judgments.

An appeal against the decisions of both Local and Regional Courts can be lodged with the next higher court if the appealing party's interest in a different ruling exceeds the sum of EUR 600,00 or if remedy to appeal has been granted by the court of first instance. Remedy to an appeal on questions of law only may be granted by the Court of Appeal.

Limitation

According to German Law, most claims become statute-barred after three years, the period of limitation beginning with the end of the year in which the claim has accrued. This, however, is only a general rule with many exceptions both prolonging and shortening the usual three-year-period. For example, claims already confirmed by a court's final and conclusive decision become statute-barred after 30 years.

The time elapsing for purposes of limitation is suspended as soon as creditor and debtor enter into negotiations about the claim in dispute with this suspension ending as soon as one party refuses further negotiations. A suspension can also be achieved by the filing of a lawsuit or an application for default summons.

The elapsing of the period of limitation is interrupted (with the period beginning anew) by the debtor acknowledging the claim; this is, for example, the case, if the debtor sets off against the claim in dispute.

Insolvency

An insolvency petition may be filed by both the creditor and the debtor in case the debtor is either unable to pay or overindebted.

In the course of insolvency proceedings an administrator in insolvency will be appointed. With regard to treaties not yet completely fulfilled by both parties at the time of the opening of insolvency proceedings, the administrator in insolvency in most cases has a right to choose between rescinding the contract or carrying on and fulfilling the contract as agreed upon by the parties. From this general rule, however, there are many deviations and exceptions.

Insolvency proceedings usually last several years. Statistically, claims falling under such proceedings are satisfied with a quota of approximately 4-6 % of their original value. This, however, may only serve as a general indication since quotas of 30 or 40 % can also be encountered. According to the current German Insolvency Act insolvency petitions can be filed not only by companies but also by single natural persons.

Recognition of foreign judgments

Judgments of courts of member states of the European Union are recognized without further procedure unless certain restrictions arising from European Law apply. The German Civil Procedural Code provides for the general recognition of other foreign judgments with certain general exceptions. Excepted are for example judgments of courts which according to German Law are internationally incompetent, judgments relating to an action not properly served upon the defendant and such of courts of countries that do not reciprocate the recognition of judgments.

Arbitration

As an alternative to regular court proceedings the German Law offers the possibility of arbitration as an instrument of dispute settling. Arbitration according to German Law requires both parties having agreed upon such procedure in a way accessible to tangible evidence (in writing, by telex, telefax etc.); if one of the parties is a consumer, the agreement has to be personally signed by both parties.

As to the applicable procedural rules, the German Civil Procedural Code provides a rough outline. It is common, however, to agree upon different rules taylormade to the requirements of the parties to the contract in question, often declaring rules set forth by international organisations such as the ICC (International Chamber of Commerce) to be applicable. If the parties have agreed upon settling all disputes arising by way of arbitration, the courts have no jurisdiction over the matter if one party invokes the arbitration clause.

Among the parties the verdict of as well as amicable settlements reached before an arbitrator have the same value and function as a court judgment.

Legal Costs

Attorney's fees

According to German law attorney's fees are generally set by the law with their amount depending on the value of the subject matter. Attorneys can, however, agree with their clients on flat fees and/or hourly rates at will. German law prohibits an agreement upon contingency fees between client and attorney.

The client always remains the debtor of attorney's fees, the outcome of the proceedings notwithstanding. In case the client wins the lawsuit, he can only recover statutory attorney's fees from the opponent. Fees agreed upon between client and attorney exceeding the statutory fees always have to be borne by the client with no recovery possible.

Court fees

The statutory court fees have to be advanced by the claimant. The amount payable depends on the claim asserted; the court fees, however, do not rise proportionally to the sum claimed but degressively. For example, the court fees to be advanced for a lawsuit concerning a claim of EUR 15,000 amount to EUR 726.- whereas a claim of EUR 50,000.- requires an advance of EUR 1,368.-.

Apportionment of legal costs

Legal costs include attorney's fees, court fees and necessary expenses (travelling expenses, expenses for witnesses, interpreters, expertises etc.).

All legal costs arising from a lawsuit have to be finally borne by the parties to the extent to which they lose the lawsuit. If one party (claimant or defendant), for example, wins the lawsuit in all respects, all costs incurred have to be borne by the opponent. If the claimant, however, motions for the payment of 100 and the court grants only 70, the claimant has to pay 30% of all costs incurred with the remaining 70% having to be accounted for by the defendant. If the proportional loss of one party is only marginal (i.e. below 10%), all costs can be apportioned to the opposing party. The court decides about the apportionment of the costs within the judgment and without a corresponding motion of the parties being required.

The actual amount of the costs will not be fixed within the judgment but, on a corresponding petition, in a separate court ruling. This ruling in combination with the judgment is an execution deed for the recoverable costs.

Enforcement

Enforcing a judgement

With only very rare exceptions all final and conclusive judgments can be enforced by courts and bailiffs with the state occupying a monopoly on enforcement. Enforcement requires a copy of the enforceable deed issued by the court for this purpose to be served upon the debtor.

The applicable method of enforcement varies according to the kind of claim concerned. The methods at hand range from levies of execution via the attachment and judicial transfer of garnished claims to mortgages registered to enforce judgment debts and even coercive detention.

Obtaining security

Apart from the regular enforcement proceedings security for a future execution of execution deeds concerning pecuniary claims can in some cases be obtained by court order in a special procedure, resulting in a writ of attachment. This is possible, if the debtor's demeanour endangers or impedes the future execution of a pecuniary claim. Because of the possibly severe consequences of such a court order for the debtor, this legal possibility is handled by German courts restrictively; examples for debtors' demeanour considered sufficient to justify such special procedure are the intended alienation of substantial assets, wasteful spending or a frequent change of residence.

Enforcement costs

Enforcement costs generally have to be borne by the debtor. Concerning these costs normal enforcement procedures apply; the costs are practically added to the amount covered by the judgment to be enforced. If, however, the enforcement costs cannot be recovered from the debtor because the enforcement is unsuccessful and the debtor has no remaining legally accessible assets, the enforcement costs have to be borne by the creditor having initiated the enforcement procedure.

The costs incurred are defined by law depending on the nominal value of the claim to be enforced (with only partial enforcement of claims being possible); within the responsibility of the bailiff many fees are defined as flat fees.

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