

## DEVELOPMENTS

### *Book review* - Rainer Maria Kiesow, *Kredite in der Risikogesellschaft* (2005)

By *Andreas Maurer\**

**Rainer Maria Kiesow, *Kredite in der Risikogesellschaft*, Berliner Wissenschaftsverlag 2005, 103pp. ISBN: 3-8305-1142-6. Price: 19,80 EURO.**

It was in the early 1990s after the Berlin wall had come down and Germany had been reunified. The whole country found itself excitedly heading towards “blooming landscapes.”<sup>1</sup> In this atmosphere many investment brokers offered apparently miraculous deals where investors could save taxes and gain real estate property at the same time. And it seemed to be blindingly easy. The investors would participate in real estate funds or buy property on their own which would be financed by a loan. This loan could then be – as investment brokers promised – paid back with money obtained by renting the property and by tax savings. The property would then be self-financing and investors would have their own property after 10 years. The scheme sounded so easy and so safe that such offers could not be refused by either people with wealthy backgrounds or by those with low incomes and no funds to risk.

The story’s progress can easily be guessed: There were insufficient renters for the many apartments and buildings, or the structures were simply old and worthless, which gave them the name *Schrottimmobilien* [junk real estate property]. The promised rent that was desperately needed to pay back the loans was simply not

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<sup>1</sup> The term “*blühende Landschaften*” (blooming landscapes) was the pictorial vision of former chancellor (*Bundeskanzler*) Helmut Kohl, who used the term in a televised speech on the occasion of the introduction of the Currency-, Economic- and Social Union between the Federal Republic of Germany and the German Democratic Republic. The term was meant to explain the economic future perspective of the so-called new federal states.

earned and consequently, investors sought legal remedy. However, constructors and former owners had long gone bankrupt and investment brokers had disappeared, leaving investors with outstanding debts. The only solvent participants in those transactions were the banks that had given loans to investors. But claiming compensation from the loan-giving banks seemed counter-intuitive, as the real estate sales contracts and the loans are different businesses. In those cases, many of the banks had not only approved loans but had also participated in selling property in different and more or less obvious ways. For example, the bank may have been involved in planning and realizing the real estate project<sup>2</sup> or taken responsibilities as the property's builder and developer.<sup>3</sup> The issue is whether the bank served solely as a lender or if it was involved in the business itself by participating in the marketing of the property (p. 14).

With *Kredite in der Risikogesellschaft*, Rainer Maria Kiesow has retraced the manifold problems and difficulties that arose when courts had to cope with junk-property litigation. He gives a very precise and comprehensive overview of legal doctrine and jurisdiction that is consistently detailed without being excessive.

Kiesow starts by outlining possible claims of aggrieved investors against the loan-granting bank. These include violation of contractual information duties, violation of pre-contractual duties, flysheet misrepresentation and third party liabilities. He denies such liabilities in the majority of cases. The emphasis of his book is on the relationship between two German Acts that came into force according to European law, namely the *Verbraucherkreditgesetz* (Consumer Loan Act) and the *Haustürwiderrufsgesetz*<sup>4</sup> (Act on the Revocation of Doorstep Sales) (p. 27 et seq.). Many of the problems that German courts had with junk-property cases were caused by the ambiguous relationship between these Acts.

According to the *Verbraucherkreditgesetz*, a loan contract and a sales contract are considered *verbunden* (conjunct) when the loan is meant to pay for the sales good and both contracts can be seen as an "economic unity" (*wirtschaftliche Einheit*). If that economic unity is found, the seller can except against the loan if the purchased good is defective and can revoke the contract with certain notice. However, this conjunction between sales contract and loan is not applicable to loans that are secured by liens on property, which applies to most cases.

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<sup>2</sup> See e.g. BGH NJW 1980, 41.

<sup>3</sup> See e.g. BGH NJW 1988, 1583.

<sup>4</sup> Both acts have been integrated into the German Civil Code since the 2002 reforms, but the content of the new provisions has mainly stayed the same.

Also, according to the *Haustürwiderrufsgesetz*, a consumer can revoke a contract if it was concluded in a “doorstep situation.” This means that the contract was either concluded in the consumer’s apartment, at his workplace or in some other place where one would not expect to conclude a contract. The problem, however, is that most of the loan contracts in junk-property-cases were concluded by brokers who had the consumer’s power of attorney, but the conclusion itself was performed in the bank’s offices with the power of attorney given to a broker in a doorstep situation. Given that the *Haustürwiderrufsgesetz* was enacted to protect consumers from hastily concluded contracts, it is reasonable to extend the right of withdrawal to the entire tax-saving concept, including both the sales contract and the loan, even if they were ultimately concluded by a broker with power of attorney in cases where the broker acted on behalf of the bank and the power of attorney was given in a doorstep situation. At least some German courts ruled as such (p.32).<sup>5</sup>

However, the 11<sup>th</sup> senate of the *Bundesgerichtshof* (Federal Court of Justice, “FCJ”), with jurisdiction over cases of bank-liability and well-known for its bank-friendly jurisdiction, has repeatedly ruled that neither the relevant provisions of the *Verbraucherkreditgesetz* nor those of the *Haustürwiderrufsgesetz* are applicable to the majority of junk-property cases and therewith overruled the higher regional court of Bamberg as well as several legal scholars (p.32).

The problem with the relationship between the Doorstep Act and the Consumer Loan Act is that the former is not applicable even if a contract is concluded in a doorstep situation if it the transaction falls under the umbrella of the Consumer Loan Act. Consequently, such transactions cannot be revoked. The Consumer Loan Act, on the other hand, denies the applicability of its provisions about conjunct contracts for loans that were secured by liens, which is precisely the case in most cases on junk-properties. The disputed question is whether or not this rivalry between the Acts was intended to have the consequence that consumers cannot invoke either consumer protection law, or if the European Law principle of effective consumer protection implies a different understanding of the relationship between the Acts (p. 38).

In 2002 the European Court of Justice (“ECJ”) seemed to have made a conclusive decision.<sup>6</sup> The German Federal Court of Justice asked the European Court of Justice for a reply to two questions. The first question was whether the Consumer Loan

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<sup>5</sup> See e.g. the higher regional court Bamberg , 6 U 73/98, *Europäische Zeitschrift für Wirtschaftsrecht* 1999, 985.

<sup>6</sup> EuGH NJW 2002, 281.

Act overruled the Doorstep Act, as the court of the first instance had held before.<sup>7</sup> While this interpretation conformed with the perception of the FCJ's 11<sup>th</sup> senate<sup>8</sup> (p. 40), it involved the ECJ according to Art. 234 *Vertrag zur Gründung der Europäischen Gemeinschaft* (Consolidated Version of the Treaty Establishing the European Community), because the 11<sup>th</sup> senate saw that this interpretation could face reasonable doubts. The second question regarded the notice of revocation, which again involves the relationship between the Acts. Seemingly in favour of the aggrieved consumers, the ECJ ruled that, in order to uphold the principle of effective consumer protection, the Doorstep Act applied to junk-property cases. However, the German Federal Court of Justice ('FCJ') held that while the Doorstep Act was applicable, the Consumer Loan Act was not. In particular, the German Federal Court excluded the application of the provisions over conjunct contracts, with the consequence that loan contracts – and that was the court's sophistry – could be revoked without consequence to the sales contract for the property. The result of this ruling was that consumers could avoid their loan contracts but remained bound to the sales contracts. This put the consumer in the adverse position of having to pay back the loan *as well as* retain possession of valueless property (p. 53). The result was that the consumer remained aggrieved and banks were not liable for damages in connection with junk-properties.

It is questionable whether the ECJ's jurisdiction was intended to yield these inconsistent results, and the fight among courts continued. In 2004, the 2<sup>nd</sup> senate of the FCJ, with jurisdiction over cases in corporate law, and therefore responsible for some junk-property cases where investors joined investment funds that invested jointly in junk-property, ruled in several similar and almost equal cases<sup>9</sup> that the contract to join the property-funds and the loan contracts were conjunct contracts (p. 79). In addition, the 2<sup>nd</sup> senate of the FCJ has held that most of the loan contracts were null and void, because they were concluded by trustees who are not attorneys, in violation of the German Act on Legal Counselling. This ruling and its consequences was nothing less than a sensation. The conjunction of sales contract and loan means that the consumer can except against the loan if the property was "defective," and the nullity of the loan contract provides that consumers both do not have to repay the loan and can reclaim prior payment made to the bank. German provisions on unjust enrichment (as applied to void contracts) meant that

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<sup>7</sup> LG München I, WM 1998, 1723-1724.

<sup>8</sup> BGH NJW 2000, 521.

<sup>9</sup> II ZR 395/01 - NJW 2004, 2731-2735; II ZR 385/02 - NJW 2004, 2735; II ZR 392/01 - NJW 2004, 2735-2736; II ZR 393/02 - NJW 2004, 2736-2742; II ZR 407/02 - NJW 2004, 2742; II ZR 374/02 - NJW 2004, 2742-2743.

the consumer obtained from and therefore had to return to the bank the junk-property (pp. 77-86).

The 2<sup>nd</sup> senate's rulings of 2004 have escalated the fight among several German courts. Not only are two senates of the highest German court, namely the Federal Court of Justice for Private Law Matters (*Bundesgerichtshof*) severely discordant, but lower courts have not followed the FCJ. At present, there is no end to this battle in sight; even the latest rulings of the FCJ (its 11<sup>th</sup> senate)<sup>10</sup> have not led to a harmonization of jurisdictions. Moreover, the 11<sup>th</sup> senate made absolutely clear that it will stick to its ruling, which distributes the risks of financial investments solely to the consumer regardless of how much the bank was involved in the sales contract on properties.<sup>11</sup> Although the FCJ has shifted the burden of evidence to the bank in cases where consumers were misled by investment brokers that cooperated with the banks, this shift will seldom help consumers, because often banks can prove their lack of knowledge regarding the deception.<sup>12</sup>

Junk-property litigation seems an infinite shift of arguments, burdens of evidence and risk distribution. But Kiesow sees more behind these cases. Not only does he here provide us with a very clear and comprehensive overall analysis on junk-property-cases. He deserves particular merit for elevating the cases to a higher level of social importance and using the jurisprudence to illustrate how principles of risk-distribution function in contemporary, complex market societies. This book is a political book, as is its topic and Kiesow makes this point absolutely clear. He is outspoken in his criticism of the 11<sup>th</sup> Senate of the Federal Court of Justice<sup>13</sup> and of some well-known legal scholars, such as Dieter Medicus<sup>14</sup>. Regardless of whether or not the reader agrees with Kiesow, having read his work, one can no longer see junk-property-cases as solely a legal problem to be solved with doctrinal analysis.

The social implications of a consumer's livelihood endangering businesses and deals raises the fundamental question of modern western societies: How far should the state intervene and how much individual responsibility can our social contract tolerate? In the case of junk-property, Kiesow pleads for a strong state that can

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<sup>10</sup> BGH, 16.05.2006, XI ZR 6/04 = Europäische Zeitschrift für Wirtschaftsrecht 2006, pp. 440 *et seq.*

<sup>11</sup> *Ibid.* p. 442.

<sup>12</sup> Hoppe, Anmerkung zu BGH XI ZR 6/04, Europäische Zeitschrift für Wirtschaftsrecht 2006, p. 447.

<sup>13</sup> "... the balky (*starrsinnig*) jurisdiction of the 11th senate..." (p. 93).

<sup>14</sup> Kiesow finds Medicus' critical commentary on the 2<sup>nd</sup> senate's decisions (*Medicus, Zur Bankenhaftung beim Erwerb von Schrottimmobilen*, EWiR 2005, 231-232) unsubstantiated and his conclusion questionable (p. 92).

protect its citizens from economically dangerous situations. He is critical of Germany's reduced regulatory powers compared to France's continued efforts to attend to its citizens' interests (p. 99-100). This criticism refers to France's different doctrinal approach to junk property cases (p. 100, Fn. 228).

State intervention in favour of consumers puts the risk of venturous investments solely with banks and enterprises and therefore encroaches on private autonomy and the contract itself. Consequently, state interventions are notably contested by many legal scholars. For example, Martinek has recently criticized the "deprivatisation of private law" and the "hypertrophy of consumer protection law", and claims a "résistance of the formal ethics of freedom" to prevent a development of "deprivation of liberty".<sup>15</sup> He argues for a "re-privatization" of private law, meaning less state regulation of contract law in fields including labor law, consumer law, and landlord and tenant law, and pleads for more freedom of contract.

Indeed, the German Civil Code was built on the liberal concept of free and equal citizens. The first drafts of the German Civil Code were made in the 1870s, slightly less than 100 years after the French Revolution and the American Declaration of Independence which again were inspired by the Enlightenment. The ideas of free and equal individuals forming the state by contractual relations spread over the Western World. Freedom of contract was the new and state-of-the-art concept. However, the presumption of a society of free and equal citizens, regulating their fates and fortunes equitably by fair contracts, soon turned out to be wrong. An entire class of the population seemed to be forgotten. The poor and those without property were unable to participate in the liberal contest of the free and equal. Therefore many scholars argued against the liberal model of the German Civil Code even before it was set into force in 1900. Two of the most famous among those who challenged the new concept were Anton Menger<sup>16</sup> and Otto von Gierke, the latter of which coined the phrase "a little drop of social oil"<sup>17</sup> pleading for more rights for the poor in the new codification.

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<sup>15</sup> MARTINEK, VERTRAGSTHEORIE UND BÜRGERLICHES GESETZBUCH, VORTRAG ANLÄSSLICH DER SAARTAGE 2005 AN DER KEIO-UNIVERSITY, TOKYO, 2005.

<sup>16</sup> MENGER, DAS BÜRGERLICHE RECHT UND DIE BESITZLOSEN VOLKSKLASSEN (1908); see also Wieacker, *Das Sozialmodell der klassischen Privatrechtsgesetzbücher und die Entwicklung der modernen Gesellschaft : Vortrag gehalten vor der Juristischen Studiengesellschaft in KARLSRUHE AM 12 Dezember 1952*, Karlsruhe 1953, 10.

<sup>17</sup> Gierke, *Die soziale Aufgabe des Privatrechts : Vortrag gehalten am 5 April 1889 in der juristischen Gesellschaft zu Wien*, Berlin (1889).

The forgotten classes, especially the workers, soon sought for emancipation.<sup>18</sup> As early as 1916-1922, first steps to a new labor law were taken with the enactment of new laws<sup>19</sup> replacing and amending the law of service contracts in the German Civil Code, especially with regards to workers' participation. Since 1948 at the latest, when the German Basic Law (*Grundgesetz*) came into force, anchoring the concept of the welfare state in the German Constitution, the liberal individualistic model of the German Civil Code could no longer be maintained.<sup>20</sup> The insight that inequalities and disparities between highly professional market participants and uninformed and inexperienced consumers were realities of modern market societies led to the emergence of a completely new field of law – the consumer protection law. Starting with the Standard Contract Terms Act in the 1970s, Consumer protection quickly became a dominant concept in German private law. Due to European legislation, today more than half a dozen consumer protection laws are integrated into the German Civil Code<sup>21</sup> and harmonized with the member states of the European Union.

While the concept of the welfare state leads to substantial adjustments to the concepts of private autonomy and freedom of contract, it forces the economically stronger party not to enforce its objectives at the expense of the weaker and more inexperienced party.<sup>22</sup> Even if this development seems inevitable from today's point of view, the concept of consumer protection has not always been anchored in the German Civil Code.<sup>23</sup> It is the symbiosis of private law and the German Basic Law, the co-action of liberal individual markets and the claim for collective prosperity that led to the emergence of consumer protection laws.<sup>24</sup> This integration has been described as the replacement of formal ethics of freedom by material

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<sup>18</sup> See Esser / Schmidt, *Schuldrecht Allgemeiner Teil*, Teilband 1, Karlsruhe 1975, 4.

<sup>19</sup> The *Hilfsdienstegesetz* of 5th Dec. 1916, the *Betriebsrätegesetz* of 4th Feb. 1920 and the *Gesetz über die Entsendung von Betriebsratsmitgliedern in den Aufsichtsrat* of the 15th Feb. 1922 (See RICHARDI / THÜSING / ANNUß / DIETZ, *BETRIEBSVERFASSUNGSGESETZ MIT WAHLORDNUNG: KOMMENTAR*, München 2006, Rn.11).

<sup>20</sup> Kramer, *MÜNCHENER KOMMENTAR BGB*, Introduction to § 241 BGB, München 2002, Rn. 2.

<sup>21</sup> Zumbansen, *Law of Contracts*, in *INTRODUCTION TO GERMAN LAW. 2ND ED* (Mathias Reimann & Joachim Zekoll eds.,2005).

<sup>22</sup> ESSER / SCHMIDT, *SCHULDRECHT ALLGEMEINER TEIL*, Teilband 1, Karlsruhe 1975, 6.

<sup>23</sup> For a different view, see BTDrS 14/6040, p. 90.

<sup>24</sup> On the conflict between liberal markets and collective wealth see RAISER, *VERTRAGSFREIHEIT HEUTE*, *JURISTENZEITUNG*, 1 - 8, 6 (1958).

ethics of responsibility<sup>25</sup> or as the politicization of the Civil Law.<sup>26</sup> Most commonly, the process of transformation referred to above is referred to as the “materialization of private law”.

The 2002 modernization of the law of obligations is the current climax of consumer protection legislation by the German legislature. In particular, consumer protection provisions were amended to the sales law, and also to the law of consumer credits - which leads us back to Kiesow’s book. While Martinek demands a liberal society where individuals take responsibility for their actions, Kiesow promotes a strong state that is able to protect its citizens against risky and hazardous business transactions.

The pivotal questions raised by junk-property litigation and expounded proficiently by Kiesow are ones that will not be solved soon. They challenge fundamental structures of societies and are not only important for junk-property, but for almost every aspect of daily life. Whether it comes to health policy, social insurance, labour law, consumer protection or taxation policy, the question that is always at stake is to what degree the state should intervene. Strictly liberal models promoting a high degree of individual freedom and responsibility are no longer convincing in light of the materialization of private law, described above. However, the welfare state as it is known today faces severe structural problems. In 1981 Niklas Luhman has identified the crisis of the welfare state, most notably its economic viability.<sup>27</sup> Indeed, today Germany struggles with the costs of its welfare and social security system. But the crucial problems of the welfare state go deeper. If the materialization of private law is identified as state regulation of society, the question arises whether or not or to what degree such regulation is possible at all. The systems theory approach already denies the possibility of social regulation by the state, critiquing it for being a self-referential, autopoietic, closed system that cannot be effectively regulated. “The politic system can ... only regulate itself.”<sup>28</sup> Whether or not one may be convinced by the system theory approach, it cannot be denied that state regulation has reached several crucial points.

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<sup>25</sup> See e.g. WIEACKER, *supra*, note 15; see also REUTER, DIE ETHISCHEN GRUNDLAGEN DES PRIVATRECHTS - FORMALE FREIHEITSETHIK ODER MATERIALE VERANTWORTUNGSETHIK?, ARCHIV FÜR DIE CIVILISTISCHE PRAXIS, 1989, p. 199 - 222.

<sup>26</sup> WIETHÖLTER, RECHTSWISSENSCHAFT, Basel [u.a.] 1986, p. 179.

<sup>27</sup> LUHMANN, POLITISCHE THEORIE IM WOHLFAHRISSTAAT, MÜNCHEN (1982).

<sup>28</sup> LUHMANN, GRENZEN DER STEUERUNG IN: DIE WIRTSCHAFT DER GESELLSCHAFT, Darmstadt (2002), p. 324.



The welfare state not only encounters theoretic concerns, it is also challenged by a development that often is referred to as globalization. Where the state's influence ends, at its borders, regulation cannot be achieved. One has only to imagine what would have happened if junk-property cases had not only involved German banks, but also foreign parties. Even if German courts had jurisdiction over such cases with international banks involved and even if such banks were liquid to indemnify aggrieved investors, they may have been located in countries where German legal title is not enforced. The only thing the court could tell the aggrieved investor would be: "bad luck".<sup>29</sup> However, such problems will arise in the future. Whether a liberal global market will be able to solve such problems in (socially) acceptable ways is doubtful. It seems more likely that different social orders and "varieties of capitalisms" will lead to an inability to cope with distinct legal problems. Transnationally institutionalized private alternative dispute resolution may be a key to coping with transnational conflicts in consumer law.<sup>30</sup> But until now such institutions have not been sufficiently developed to cope with sophisticated problems like junk-property cases.

The analysis of the social and legal problems raised by the junk-property cases makes it clear that legal doctrine alone is an insufficient solution to the problem. Kiesow makes clear that much more than doctrinal analysis is required to solve the puzzle produced by junk-property; what is required is serious deliberation about where society is supposed to head. Domestic regulation is a short term solution, but it will not protect consumers in transnational cases. The increased globalization of what were once local consumer transactions, protected and regulated by local laws, amplifies the problems raised in the junk-property cases. It is therefore critical to consumer welfare to seek alternative ways of regulation and social control to sufficiently substitute state law in a transnational context.

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<sup>29</sup> Kiesow uses this phrase on p. 100 to distinguish liberal and social-democratic approaches, marking the result for the aggrieved party in case of a liberal approach.

<sup>30</sup> See CALLIESS, *GRENZÜBERSCHREITENDE VERBRAUCHERVERTRÄGE*, TÜBINGEN (2006).