Markesinis's German Law of Torts

A Comparative Treatise

Fifth Edition
Entirely Revised and Updated

Edited by
John Bell
and
André Janssen, in collaboration with Colm McGrath

With a Foreword by
Professor Sir Basil S Markesinis QC, FBA, LLD, Drhc (mult.)

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Specific Areas of Liability Under the Code: Economic Loss and Products

Delictual liability has grown up around a number of specific problem areas. In particular, road accidents, product liability, medical liability and economic loss have given rise to numerous scholarly debates and judicial decisions. The first three have (besides the liability under § 823 BGB spawned new legal bases for compensation which are to be found in specific legislation. These areas of law will be discussed in chapters six and seven. Two specific areas are discussed here in relation to the BGB the first is economic loss and the second is product liability. In addition, the chapter is having a short glimpse at § 824 BGB, which is a distinct form of liability that protects economic interests where the loss has been caused by untrue statements.

I. Economic Loss

Bibliography

The following is only a selection of the literature on the subject of (delictual) liability for pure economic loss and more generally the *Vertrag mit Schutzwirkung zugunsten Dritter* and *Drittschadensliquidation*:

Banakas (ed), *Civil Liability for Pure Economic Loss* (1996) ch 3 (Erwin Deutsch); Bussani/Palmer, *Pure Economic Loss in Europe* (2003); von Bar, *The Common European Law of Torts* (1998) vol 1, §§ 44–49; Canaris, 'Die Reichweite der Expertenhaftung gegenüber Dritten' *ZHR* 163 (1999) 206; Canaris, 'Schutzwirkungen zugunsten Dritter bei 'Gegenläufigkeit' der Interessen' *JZ* 1995, 441; van Dam, *European Tort Law* (2nd edn, 2013) 211–13; Hübner/Sagan, 'Die Abgrenzung von Vertrag mit Schutzwirkung zugunsten Dritter und Drittschadensliquidation' *JA* 2013, 741; Hübner/Sagan, 'Einbeziehung Dritter in Schuldverhältnisse und Drittschadensliquidation' *ZJS* 2012, 644; Keller, *Anwendungsfälle der Drittschadensliquidation und des Vertrages mit Schutzwirkung zugunsten Dritter* (2004); Palmer, 'A Comparative Law Sketch of Pure Economic Loss' in Bussani/Sebock, *Comparative Tort Law. Global Perspectives* (2015); Traugott, *Das Verhältnis von Drittschadensliquidation und vertraglichem Drittschutz* (1997).

A. Introduction

As the late Tony Weir remarked:

> There are several good things in life, such as liberty, bodily integrity, land, possessions, reputation, wealth, privacy, dignity, perhaps even life itself. Lawyers call these goods 'interests'. These interests are all good, but they are not all *equally* good … Because these interests are not equally good, the protection afforded to them by the law is not equal … As between health and wealth, the priority would seem to be clear: it is better to be healthy than wealthy (Weir, *A Casebook on Tort* (10th edn, 2004) 6.

It will have been noticed from chapter two that the protection of wealth (*Vermögen*) as such is not included in the list of enumerated interests of § 823 I BGB. This does not mean that economic losses will never be compensated. German law does not have a comprehensive regime of protection against interference with economic interests similar to the protection for bodily integrity or property under tort law (Kötz/Wagner, nos 430–39). Where economic interests are harmed as a consequence of the interference with another kind of interest, then German law readily offers compensation. A person who is injured and incurs medical expenses will receive monetary compensation both for his pain and suffering (in accordance with § 253 II BGB) as well as for his economic loss (in accordance with §§ 249 BGB ff, eg, medical expenses, lost earnings, etc). Equally, a person whose car has been damaged in a traffic accident will be able to claim compensation for it, which may also include the cost of hiring a substitute. Finally, to give one last illustration, if the defendant's negligent activities lead to the severing of an electricity cable, thereby causing a power cut which affects the claimant's electrically operated egg-hatching machines, the claimant will be able to claim both the value of the eggs and the profit he would have made on those eggs which would have hatched into chickens and then been sold (BGH, BGHZ 41, 123). In all these cases we are talking of economic loss *immediately consequential* to injury to the person or property and the only problem that the court will have to face will be one of remoteness: how much of the claimant's loss to allocate to the defendant's conduct.

By contrast, when we move to pure economic loss (*reiner Vermögensschaden*) the difficulties experienced by German law are multiplied; in addition, they are experienced in areas which are well known to common lawyers. Indeed, it could be argued that in no other area of its law of torts does German law demonstrate such an ideological affinity with the common law as in its refusal to compensate pure economic loss through the medium of tort rules. As in the common law, instead of a general principle, the law offers a number of specific solutions. The principal protection is through § 826 BGB, which provides compensation for harm caused by intentional acts which are contrary to good morals. In addition, § 824 BGB creates a right to compensation where one person issues false statements which threaten the credit or livelihood of another. Furthermore, various statutory duties that protect economic interests will give rise to duties of compensation under § 823 II BGB, if not under the specific remedies provided for in the legislation. So it would be wrong to focus on § 823 I BGB only and to conclude that there is no compensation in German law for economic loss per se.

Yet, as we shall note below, in both systems this basic premise has, in recent times, come under constant and ingenious attacks with practitioners (and judges) showing in many instances a willingness to probe for weak points in the wall of the citadel. Such an attitude,

inevitably, gives rise to the question why should this be so. The question becomes more pressing (and, to some extent has defied a conclusive answer) whenever the problem is examined against the background of French law (and its derivatives) and Austrian law. For these systems have adopted the exact opposite solution. They do not differentiate types of loss yet they have not incurred the dire consequences that common lawyers and German lawyers so fear. Professor Koziol (*Basic Questions of Tort Law from a Comparative Perspective* (2015) §§ 8/53-8/60) has commented that the precise listing of protected interests in § 823 I BGB has not led to legal certainty. German jurists consider the provision to be overly restrictive and have sought to get around the limits by interpreting § 826 BGB on behaviour contrary to good morals very broadly, by 'inventing' the precontractual liability (now § 311 BGB after the Schuldrechtsreform), and by finding duties to ensure public safety under § 823 I BGB (so-called *Verkehrssicherungspflichten*) to protect the economic interests of others.

B. Arguments against Liability for Pure Economic Loss

i. Indeterminate Liability

Stripped to its essentials, the first argument against liability is that economic loss tends to give rise to difficulties of an administrative nature such as, for example, a potentially indeterminate number of claims (and, it should be stressed, it is the indeterminacy that matters rather than the number of claims itself), unreliable evidence, and collusive actions. These fears were succinctly voiced as early as 1861 by the great German jurist Rudolf von Jhering who wrote:

> What would it lead to if one could be sued in non-contractual relations generally for gross negligence as well as intent! A careless utterance, carrying a tale, giving false information and bad advice, uttering a thoughtless judgment, recommending an undeserving housemaid one used to employ, answering a traveller's question about the way or the time, and so on, in a word, everything and anything, if grossly negligent, would make one liable for the harm it caused in spite of all *bona fides*; and in the course of such an extension the *actio de dolo* would become the veritable scourge of commercial and social intercourse, free conversation would be greatly inhibited, the most innocent word would become a snare! (von Jhering, 'Culpa in Contrahendo' (1861) 4 *Jahrbücher für die Dogmatik des heutigen römischen und deutschen Privatrechts* 1, 12).

This clearly echoes what was to become one of the best-known aphorisms of Cardozo J in his famous judgment in *Ultramares Corp v Touche* 255 NY 170, 174; NE 441, 444 (1931). Similar concerns have been voiced in England.

ii. Free Self-Determination

A second and more principled argument is expressed by Professor Canaris and Professor Larenz who conclude that the rule against recoverability of pure economic loss serves the purpose of guaranteeing individual freedom:

> Both the right to free development of his personality [Article 2 GG] and the right to compete entail that a citizen is permitted to interfere with the economic interests of another – indeed even

> frequently intentionally. Only when these interests have crystallised into property do they earn general and unconditional respect' (Larenz/Canaris, *Lehrbuch des Schuldrechts* II, (Special part, first vol, 13th edn, 1986; second volume containing the law of torts, continued by Canaris, in its 14th edn, 1994) 357; also Kötz/Wagner, no 432).

In a free market economy financial harm of some kind to some persons is to be expected: 'Competition involves traders being entitled to damage their rivals interest by promoting their own': *Home Office v Dorset Yacht Co Ltd* [1970] AC 1004, 1027 (Lord Reid). Or, as Robert Goff LJ (as he then was) put it in his Court of Appeal judgment in *The Aliakmon* [1985] QB 350, 393:

> The philosophy of the market place presumes that it is lawful to gain profit by causing others economic loss, and that recognised wrongs involving interference with others contracts are limited to specific intentional wrongs such as inducing a breach of contract or conspiracy.

The same justification for the exclusion of economic loss is given in German law. However, this does not necessarily exclude the desirability (in Germany *de lege ferenda*) of well-defined exceptions in specific circumstances. The main concern is to keep these exceptions under control in the light of the individual's right to self-determination in a market economy (see also Lord Goff's comments in Markesinis (ed), *The Gradual Convergence* (1994) 130; and Picker 'Gutachterhaftung' in Beuthien et al (eds), *Festschrift für Dieter Medicus* (1999) 397, 433).

iii. The Internal Logic of the Code

Professor Canaris also suggests that to create economic interests as an absolute right would contradict the schema of the Code and would amount to unjustified judicial lawmaking. The logic of the Code suggests that, outside specifically named protected interests, protection is offered by §§ 824 and 826 BGB for defined reasons, rather than a general principle of liability for fault (see Canaris, 'Schutzgesetze – Verkehrspflichten – Schutzpflichten' in *Festschrift Larenz* (1983) 27, 78 ff; *Münchener Kommentar*/Wagner, § 823 BGB, no 379).

iv. Insurance Considerations

A fourth argument is that 'insurance considerations' often favour the non-liability rule. On this view, 'the loss [should] lie where it falls in a situation where the claimant has taken out first-party or loss insurance or, alternatively, where he could have done so relatively cheaply' (Markesinis/Deakin, 173). It is useful to put this argument in such a stark manner since lawyers in Europe, especially continental Europe, are less accustomed to analysing tort cases in an overtly economic manner. The German decisions bear witness to the validity of this assertion, though it is no longer entirely true of academic literature. (See, Kötz/Schäfer, *Judex oeconomicus* (2003) especially cases 3 and 11. Also Kötz/Wagner, nos 82–85, 92–93.) Yet the assumption that the 'insurance factor' always favours the non-liability rule is simply not correct. The decision of the Canadian Supreme Court in *Canadian National Railway Co v Norsk Pacific Steamship Co Ltd* [1992] 1 SCR 1021 contains one of the interesting (if long) judicial discussions of the subject. (But it has not pleased all academics. Thus, see, Stapleton, 'Tort, Insurance and Ideology' (1995) 58 *MLR*, 820 ff).

Since the 1990s, English law has confirmed the position that negligently caused economic loss would be recoverable only in very specific circumstances. As a result, a comparison with German law needs to pay attention to the special cases which are recognised in English law. The new orthodoxy expressed by the House of Lords in *Murphy v Brentwood DC* [1991] 1 AC 398 and *Caparo v Dickman Industries plc* [1990] 2 AC 605 establish the very limited character of recovery for economic loss. Recovery is accepted for negligent misstatements and negligence in the performance of a service. Otherwise there are no overarching principles (see Markesinis/Deakin, 174–75 and 177; and Markesinis/Deakin, 'The Random Element of Their Lordships' Infallible Judgment: An Economic and Comparative Analysis of the Tort of Negligence from Anns to Murphy' (1992) 55 *MLR* 619).

v. The Role of Contract

Economic interests are primarily protected by contract law. As Weir put it, 'if you want your wealth preserved, you should pay a stockbroker to look after it, and sue him in contract if he fails' (*A Casebook on Tort*, 7). Recourse to contract law provides a right of compensation, but that depends on the injured party being treated as a party to the contract. Unlike German law, the English law is rather strict. Thus far, the Contracts (Rights of Third Parties) Act 1999 has not played much of a role; and the construction industry appears to be keen to exclude its application for the future. It must also be noted that the expansion of contract has come about incrementally through the activity of the courts. (See Markesinis/Deakin, 156–57, 168–73, and see below.)

C. The Specificity of German Law

i. History of German Law

In Germany, the rigid anti-compensation rule has been doubted by some academics and severely eroded in some situations by the courts, themselves, despite strong academic criticism. But, overall, the challenge has, again, been unsuccessful since the non-liability rule was clearly incorporated in the Code in accordance with the demands of both the socio-economic environment of the nineteenth century and Roman legal tradition. For the socio-economic environment clearly ranked tactile forms of property above pure economic interests, and what is more, expressed a clear preference for land over movables. Legal tradition too was also hostile towards pure economic loss, since the lex Aquilia and classical Roman Law formed part of the German common law (*Gemeines Recht*) and this system of compensation was devised for damage to physical objects.

ii. German Alternatives to Delictual Liability for Economic Loss

Many consequences follow from this basic attitude of German law. Here we can only outline a few fundamental points, and further details will be given in the annotations to the translated decisions. First, one must note that as a result of the rigidity of tort law, German contract law has been expanded (many academics would argue excessively), to meet

new situations calling for a pro-claimant solution. In particular, the interests of third parties to contracts have been protected through an expansion of the range of people who are deemed to be protected by the contract (eg, the originally judge-made *Vertrag mit Schutzwirkung zugunsten Dritter*). In particular, we will see this in the notes on the cases dealing with liability for negligent statements and the liability of attorneys towards non-clients.

Secondly, the expansion of § 826 BGB and contract law has often been the result of bold judicial creativity. This creativity has not, as already mentioned, always been met with 'enthusiasm' by the academic side of the profession. In this context, therefore, the harmonious collaboration between the two sides of the legal profession, so much the hallmark of German law (and so different from English law), has been ruptured.

Thirdly, despite the above, there remain large areas of tort law where no recovery is allowed for pure economic loss and, in this sense, German law is very close to English law in result if not in methodology. The 'cable cases' provide an obvious example, but many others exist. Thus, for example, if the defendant injures the claimant's employee, or debtor, an English claimant has no longer (ie, since 1982) an action in tort for his economic loss (though some common law systems – Australia, New Zealand, Canada – may, in limited instances, allow such claims). According to the prevailing view, interferences with contractual or quasi-contractual relations are not actionable under § 823 I BGB. This contrasts with the famous French decision (Colmar, D 1956, 723) which allowed a football club to claim the economic loss it suffered as a result of the injury of one of its leading players; this would be decided differently in Germany. (See generally, Bussani/Palmer, case 5, 241–54.)

Fourthly, demarcation lines cannot always be drawn easily, especially in cases involving pure economic loss. The distinction between damage to 'property' and economic loss has thus caused many difficulties. For example, A damages B's cable and C's factory comes to a halt. Moulten material in his electrically operated machines solidifies and has to be discarded. This, clearly, is physical damage, actionable under § 823 I BGB. But what if the solidified material can be re-melted – no doubt at an extra cost – and reused? In trying to answer this question, German courts have come up with some rather abstract analyses. (See, eg, OLG Hamm, NJW 1973, 760; Möschel *JuS* 1977, 5.)

Fifthly, the different methodology – dictated by the Code, German legal history, or legal education should not deter the reader from using 'constructively' the German ideas which may yet be transplantable into the common law. At the very least, these ideas should provide the common lawyer with food for thought. This point will be amplified in the sections that follow, and in the notes to the legal malpractice and negligent misstatement cases. Decisions such as that of the House of Lords in *Henderson v Merrett Syndicates Ltd* [1995] 2 AC 145, where comparative law was put to practical use, will surely encourage jurists to engage in such exercises in the future, in this field and elsewhere. In his leading speech, Lord Goff of Chieveley, after having carefully reviewed the available solutions in French and German law, opted for a concurrence of contractual and tortious actions. The German model, and the way it had worked in practice without any problems, clearly aided the learned Law Lord to reach his own conclusion as to what English law should be.

Finally, for the reasons already given, the economic loss cases will be grouped under different headings and discussed separately, the assumption being that different factual

situations call for different legal (and economic) analyses and, therefore, different solutions. The English law on this topic is usefully grouped in Markesinis/Deakin, 143–73. The laws on other legal systems is presented in terms of solutions to problems in Bussani/Palmer.

D. Categories of Liability for Economic Loss

i. Interference with an Established and Operating Business

In chapter two (section II.E.iii) we saw that the right to an established and operating business was recognised as a protected interest very soon after the Code came into force (see case 8). The interference with such a business is treated as analogous to the interference with property, rather than with a purely economic interest. In that way, the refusal to provide compensation for pure economic loss is preserved. But, as noted in chapter two, the conduct of the defendant will constitute an invasion of the claimant's right if it is 'business-connected'. According to the BGH this means that it must be 'in some way directed against the business as such … and must not simply affect rights and interests which are separable from the business as a functioning unit' (BGH, BGHZ 29, 65, 74, and case 9). So the injury to an ice-skating partner was not an interference with a business as such.

ii. Cable Cases

Cases 28, 35 and 36 deal with a problem that has also exercised the English courts. Their annotations will bring out particular points and provide the reader with further bibliographical references. Three points, however, should also be made at this stage. The first is the fact that English and German law essentially reach the same result in this factual situation. It is by no means clear what is the right answer to this problem. If – and we need not give a conclusive answer at this point – the law ought to be changed, the question would then arise as to how this should be done, given the rigid phrasing of § 823 I BGB. Of course, it should be noted that German lawyers have not been short of ideas in their attempts to circumvent the leading tort provision. But the BGH, apart from a brief period of hesitation, has been as quick to reject them as the practising lawyers have been to invent them.

Secondly, the cases are also noteworthy in their relatively open allusion to policy and, in this respect, they can easily be compared with some of the more recent English decisions. The awareness that policy will decide the outcome is also increasingly shared by the academics who have commented on these decisions. Once again, the *Norsk* decision contains a good discussion of the issues.

Finally, both the English and German cases reveal how various legal devices have been used interchangeably in order to produce the desired result. This equivocation between the various elements of liability must be clearly stressed, for it will accustom the common lawyer to the fact that he must often seek to find in the German theory of legal cause the answers which he tends to produce through the notion of duty. For comparative studies on this subject see: Bussani/Palmer, 220–21; Taupitz, *Haftung für Energieleiterstörungen durch Dritte* (1981). More generally on the comparative law of causation see Steele, *Proof of Causation in Tort Law* (2015).

iii. Loss of Use

Two cases (BGH, BGHZ 55, 153 and BGH, NJW-RR 2017, 219) dealing with this issue are case 37 and case 7. In essence, the cases demonstrate the way in which the effects of a fault can be characterised as an interference with the use of property (and thus an interference with property). In the more recent decision (case 7), the claimant sought compensation for the immobilisation of its ship for three days, but was awarded damages for interference of only a few hours. The thing itself was not damaged, but its use was totally prevented. That constituted an interference with property. Mere restriction of the use of a thing is, however, not an interference with property. So a blockage on the motorway which prevents a car completing its journey is not an interference with property, but is merely economic loss (see case 7). The annotations to them will make it clear that the results achieved by the courts have been seriously questioned by many academics. These cases also show how difficult it is to draw a line between what constitutes an interference with property, actionable under § 823 I BGB, and what should be called pure economic loss.

iv. Damage Caused to the Product

This is an economic loss which, arguably, should be left to contract rather than tort. Nevertheless, in Germany, tort law was expanded to cover some types of economic loss, mainly to circumvent some shorter limitation periods in contract that then applied (*Weiterfressermangel* or *Weiterfresserschaden*). The problem is whether harm caused to the product which is defective constitutes damage to property or merely economic loss. Clearly, damage caused to other property is property damage. Whereas the case law before the revision to the Code in 2002 was clear that a defect in construction did not amount to damage to the land on which it was built (case 55), harm caused to the rest of a product by a defective component might be. In the latter cases, where a defective component created harm which was 'substantially distinct' from the defect itself, this might constitute property damage within the scope of § 823 I BGB. Since 2002, the limitation periods have been standardised at three years through §§ 195, 199 BGB and the need for such interpretation has at least to some extend gone. All the same, two reasons remain. First, if the case is treated as one of delict, then the limitation period is three years instead of the two years for sales (§ 438 I no 3 BGB). Secondly, the limitation period for delict starts from the date of harm, whereas that for sales starts from the date of sale. There will thus remain incentives to treat damage to the product cases in delict (and thus as harm to property), rather than as defects in sale (and thus a form of economic loss). See the notes to cases 53–55 for more details on the future of the *Weiterfressermangel* after the Schuldrechtsreform of 2002.

v. Economic Loss as a Result of Negligent Misstatements

Here, too, we are dealing with economic loss which in the common law systems will, if at all, be actionable in tort. Negligent statements relied upon by third persons have proved troublesome. The reasons for the difficulties inherent in this subject are many. First is the belief – not always factually correct – that words travel more than acts and can thus raise the spectrum of truly 'indeterminate liability' in terms of time and persons. Though Professor von Bar suggested the opposite solution by arguing that a person giving information in

his professional capacity knowing that it will be accorded considerable importance by the recipient demonstrates an 'assumption of liability' for any harm caused by reliance on that statement ('Liability for Information and Opinions Causing Pure Economic Loss to Third Parties' in Markesinis (ed), *The Gradual Convergence* (1994) 113 and 116–17.) See also after the Schuldrechtsreform of 2002, the 'Expertenhaftung' under § 311 III 2 BGB, which is basically codified case law. Hence, the previous case law remains, in principle, applicable here.

Secondly, if we take the example of an audit report prepared for a company, but relied on by third parties, the audited client retains a good deal of control over the records upon which the auditor bases his report. Thirdly, and not entirely unrelated to the previous point, is the fact that auditors will rarely be in a position to estimate anywhere near as accurately as will be necessary, the extent of their potential liability. This 'informational asymmetry' has been examined more in the US than in England by academic literature. (See, for instance, Siliciano, 'Negligent Accounting and the Limits of Instrumental Tort Reform' (1988) 86 *Michigan Law Review* 1929.)

Situations of negligent misrepresentation can take an infinite variety of factual forms. These have been systematically analysed by Lorenz, 'Das Problem der Haftung für primäre Vermögensschäden bei der Erteilung einer unrichtigen Auskunft' in *Festschrift K Larenz* (1973) 575. Here suffice it to divide them into two groups.

In the first, the defendant makes a statement (usually a report) to the person who asked for it (and, invariably, paid for it) but knows that it will be relied upon by a specified third person. OLG München, BB 1956, 866 is such a case and it is discussed along with other similar cases in Lawson/Markesinis, *Tortious Liability for Unintentional Harm in the Common Law and the Civil Law* (1982) I, 83 ff. In the US this situation is usually described as being covered by the 'privity or near privity rule'. It finds an excellent illustration in *Glanzer v Shepard* 233 NY 236, 135 NE 275 (1922). That German law based its solution on contract whereas the American law opted for tort is mostly a matter of 'emphasis', as Cardozo J put it, adding that if necessary he, too, could have based his decision on contract.

Real difficulties appear in the second type of situation where A commissions the (negligently prepared) report from B and then shows it to others who rely on it to their detriment. Case 41 is such a case and it is here that the problem of 'indeterminate liability', so well identified by Cardozo J in *Ultramares Marine Corp v Touche* 255 NY 170, 174 NE 441 (1931), rears its ugly head. The courts, if they abandon strict adherence to the privity requirement (as they are nowadays inclined to do) are, in such cases, forced to seek a balance between two opposing positions. The first is liability resting on pure foresight (or some equivalent concept). The second is liability based only on a form of direct nexus between the representor and the representee of the kind found in the aforementioned decision of the OLG München or in the *Glanzer v Shepard* decision.

A more middling or flexible approach is that advocated by the Restatement (Third) of Torts: Liability for Economic Harm (Tentative draft 1) para 5 (2012) which rejects the private requirement and renders accountants liable not only to those persons whom they intended to influence but also towards the persons whom the accountants know that their *clients* intended to influence.

English law, too, has vacillated on this topic in a manner which has been as confusing as it is difficult to summarise with any pretence to accuracy. Since the seminal judgment of the House of Lords in *Hedley Byrne and Co Ltd v Heller and Partners Ltd* [1964] AC 465, it has been settled that there is liability for careless statements causing pure economic loss provided

there was a 'special relationship' between the claimant and the defendant *and* there was no disclaimer of liability. 'Special relationship' has obviously been a key phrase; and it has been subsequently interpreted to include a friend giving advice seriously though *not* in a professional context. The current state of the law is found in *Caparo v Dickman* [1990] 2 AC 605. In that case, the House of Lords refused to hold that the auditors of a company owed a duty of care towards the shareholders of the company who suffered losses by purchasing shares in that company by relying on that report. The judgments of at least two Law Lords – Lord Bridge and Lord Jauncey – suggest that liability can only arise if the statement was both intended to be relied upon for a particular purpose and was, in fact, relied upon. This, in the opinion of their Lordships, was not satisfied in this case. In *Smith v Eric S Bush; Harris v Wyre Forest District Council* [1990] 1 AC 831, 865, Lord Griffiths stressed

> that in cases where the advice has not been given for the specific purpose of the recipient acting upon it, it should only be in cases when the adviser knows that there is a high degree of probability that some other identifiable person will act upon the advice that a duty of care should be imposed.

Likewise, in *Caparo Industries plc v Dickman* [1990] 2 AC 605, 621 Lord Bridge argued that in these cases it is essential to prove

> that the defendant knew that his statement would be communicated to the claimant, either as an individual or as a member of an identifiable class, specifically in connection with a particular transaction or transactions of a particular kind (eg, in a prospectus inviting investment) and that the claimant would be very likely to rely on it for the purpose of deciding whether or not to enter upon that transaction or upon a transaction of that kind.

The development of the tort action in England and the US was largely brought about by the doctrine of consideration which (especially in England) made the expansion of the notion of contract impossible. (See Lord Devlin's judgment in *Hedley Byrne & Co. Ltd v Heller & Partners Ltd* [1964] AC 465, 529.) In Germany the pressure was the reverse. A tort action under § 823 I BGB was and is impossible; and an action under § 826 BGB tends to be limited to the most opprobrious forms of misconduct. Though § 826 BGB has, in recent times, received an expansive interpretation, it is still unable to deal with the most common situations. The expansion of contractual or quasi-contractual remedies was the only answer German law could produce. A number of translated German decisions deal with this problem. Though the results reached by the German courts are often identical to those accepted by the English courts – *Caparo*, for example, could have been decided in the same way under German law. However, one must also note that recently the BGH extended liability in this field. (See the controversial decision reproduced as case 44.) Notwithstanding the possible convergence in solutions, the reasoning used by these two national courts remains different. This may be largely due to the fact that in these disputes the sources of the law are multiple and highly complex. More about the contractually 'flavoured' methodology will be said in the next sub-section; and the complexity of the sources that must be used by German judges to solve these cases will be discussed in the notes to the translated decisions.

vi. Negligent Performance of Professional Services

Case 47 deals with a related topic. A notary, solicitor, or attorney is negligent in the drafting of the will of the testator and, as a result, a potential legatee is deprived of the

benefit he would have otherwise derived from the will. The lawyer's contractual and/or delictual liability towards his client is not, of course, in doubt. But can he be made liable to the 'third' party/potential legatee? German law (as indeed English and American law) has given a positive answer, but has again justified it in contractual, not delictual terms. Common lawyers have opted for a different justification of the same result, but the comparison of the various cases shows that the problem – the limit of the potential liability – is the same. Incidentally, in these cases liability can often be said to result from what the lawyer says (ie, negligent statement), but it can also result from what the lawyer does. In the annotation in this case we shall examine the English and American approaches to the problem. The advantages of contract over tort are set out in the notes to case 47.

E. Economic Loss at the Borderline of Contract and Tort

The divide between contract and tort is not always easy to draw. It becomes very vague when the tortious conduct produces pure economic loss instead of the more typical physical injury or property damage. This division, explicable by reference to history, is more rigidly maintained by the common law where some of its jurists have even produced eloquently pithy but, it is submitted, not always persuasive reasons for its maintenance. (See, eg, Weir, *International Encyclopaedia of Comparative Law* (1975) XI, chapter 12, 'Complex Liabilities', chapter 5; and, more sceptically, Markesinis, 'An Expanding Tort Law – the Price of a Rigid Contract Law' (1987) 103 *LQR* 354, 384 ff.) This is not so in the modern civil law in general and the German law of torts in particular. For there, contract and tort are seen as species of the wider notion of obligation (*Schuldverhältnisse*). In this system, codal provisions or other reasons have forced lawyers, while not abandoning the search for doctrinal clarity, to often cross the boundaries of contract, tort law, and *negotiorum gestio* (§§ 677 BGB ff) in an attempt to find a solution (not necessarily the best one) to a problem. We shall note later on in section III of this chapter how this has worked out in specific instances of potential liability. Here suffice it to sketch two of the main contractual solutions devised to overcome shortcomings of the German law of tort. They are contracts with protective effects vis-a-vis third parties (*Verträge mit Schutzwirkung zugunsten Dritter*) and the (untranslatable) concept of *Drittschadensliquidation*; and their treatment in Germany is usually found in books dealing with the law of contract or the 'general part' of the law of obligations.

Contracts in favour of third parties (*Verträge zugunsten Dritter*) give, under certain circumstances, a third party the right to demand that a promisor in a contract perform his primary obligation to him (and not to the co-contractor/promisee). They are regulated by §§ 328–35 BGB and they should not be confused with the contracts with protective effects for third parties. They are similarly recognised in many other systems. In England, the Contracts (Rights of Third Parties) Act 1999 made considerable inroads into the doctrine of privity and introduced the concept of a contract for the benefit of a third party into English law. But the common law remains otherwise rigidly faithful to all the facts of its doctrine of consideration. (For a thoughtful and critical discussion of the English common law, see: Law Commission, 'Privity of Contract: Contracts for the Benefit of Third Parties' Law Com No 242 (1996). See, also, Beatson, 'Reforming the Law of Contracts for the Benefit of Third Parties. A Second Bite at the Cherry' [1992] *Current Law* 1, where one also finds some interesting insights about the Law Commission's research into foreign (including German) law.)

Contracts with protective effect for third parties provide the beneficiary with protections similar to those of the primary parties to the contract (see Markesinis/Unberath/Johnston, 204–16). German courts have deployed the concept of a contract with protective effects for third parties in two quite different groups of cases. (The need to differentiate between these two groups is highlighted by Kötz, 'The Doctrine of Privity of Contract' (1990) 10 *Tel Aviv University Studies in Law* 195.) In the first category the function of the *Vertrag mit Schutzwirkung zugunsten Dritter* is to frame certain protective duties of care as collateral obligations under the contract (or in pre-contractual situations as *culpa in contrahendo*, see now § 311 III 2 BGB) in order to avoid the weak vicarious liability rule contained in § 831 BGB. This is well illustrated by the vegetable leaf case (case 69) in which the daughter of a shopper was given compensation for personal injuries sustained while helping her mother to pack shopping, but before the contract of sale between the mother and the shop had been concluded. The judicially created variant of contract with protective effects vis-a-vis third parties brings strangers to a contract under its protective umbrella and allows them to entertain an action for damages for breach of one of the contract's secondary obligations. The situations in which this concept has provided a solution originally involved physical injury; and this contractual device enabled the German courts to overcome the restrictive provision of liability for harm caused by third parties found in the provisions on liability for others in § 831 BGB (discussed below in chapter five). For in § 831 BGB the Civil Code stipulates that the defendant is liable for his own negligence in selecting or supervising his servant but does not impute the servant's negligence to him. Direct liability can however be secured in a contractual context by relying on § 278 BGB to create a duty to deliver performance not only to the principal contracting party, but also to a third party. Clearly, such a convoluted technique was never necessary for the common law (and, indeed, for those systems (eg, French) that opt for the true vicarious liability rule). The German 'refinement' of the traditional contract in favour of third parties has thus, understandably, escaped the attention of most common lawyers. In 2002 the legislator codified this first category of the *Vertrag mit Schutzwirkung zugunsten Dritter* (see §§ 280 I, 311 II nos 1–3, III 1, 241 II BGB). However, the old case law in this regard remains fully applicable.

The second type of situation in which the notion of *Vertrag mit Schutzwirkung zugunsten Dritter* has been used is, however, much more interesting from a common law perspective and it concerns the so-called *liability of experts* (Markesinis/Unberath/Johnston, 208–14; the Schuldrechtsreform of 2002 also codified this kind of liability, see §§ 280 I, 311 III 2, 241 II BGB). § 839a BGB has subsequently made provision for the liability of court-appointed experts. The absence (in Germany) of a tortious exception to the rule that pure economic loss is not recoverable in tort (such as the *Hedley Byrne* principle) has prompted German courts to extend contractual reasoning. It is thus in this context that the German case law deserves attention and provides useful insights into the scope and nature of liability for the negligent performance of services by professionals which lead to economic loss. For example, the liability of a lawyer to a non-client/third party that has suffered pure economic loss as a result of the lawyer's negligence: *White v Jones*. The same may be true in cases where a sub-contractor causes, through his negligence, economic loss not just to his co-contractor (the general contractor) but also the owner of the building (eg, *Junior Books v Veitchi* [1983] 1 AC 520 (Scotland and England); *J'Aire Corp v Gregory* 24 Cal 3rd 799, 598 P 2d 60 (1979) (US).) For, it will be argued (in the notes to the relevant German cases, cases 39 and 46), that in almost all of these situations (for an exception see case 44)

the defendant (lawyer or sub-contractor, as the case may be), must not be made more extensively liable towards the third party than he would be if sued by his co-contractor. For this to be achieved, however, the cause of action against such defendants will have to be contractual. If, for whatever reasons, tort terminology is chosen, it will have to be made clear that the scope and extent of any tortious duty will have to be determined by the underlying contract between lawyer/client or owner/contractor. (See Lorenz/Markesinis, 'Solicitors' Liability Towards Third Parties; Back into the Troubled Waters of the Contract/Tort Divide' (1993) 56 *MLR* 558, replying to Beatson, 'Reforming the Law of Contracts for the Benefit of Third Parties. A Second Bite at the Cherry' [1992] *Current Legal Problems* 1). This category of liability causes great conceptual difficulties in both systems. (For a more detailed account see notes to cases 41–44 and case 47.)

In English law, some have suggested actions for economic loss could be framed in contract. However, the Law Commission was at pains to emphasise that the 1999 Act does not cover situations such as *White v Jones* or *Junior Books* and expressly clarified that its reform proposal did not make allowances for the German concept of a contract with protective effects towards third parties. Whether this has been sufficiently expressed in the wording of the Act is controversial and gives rise to considerable uncertainty: see Andrews, *Contract Law* (2nd edn, 2015) 189. Hence, tort techniques will continue to dominate the reasoning in such cases outside the scope of the 1999 Act with one notable exception: the availability of an exclusion clause in the main contract to third parties who are employed in the exercise of the main contractor's duties.

Clearly, then, the above technique goes some way towards solving the kind of problem faced by Anglo-American courts in cases like *J'Aire* and *Junior Books*. However, it also challenges the doctrine of contractual privity, which is accepted by German law as it is by the common law systems (*Relativität der Schuldverhältnisse*). Some kind of workable compromise is thus needed if a right balance is to be preserved between the traditional doctrine and the judicially fashioned deviation. It follows that if the ambit of contract is to be enlarged – as it is by constructions such as the contract with protective effects vis-a-vis third parties – special care must be taken so that the expansion is kept under control. For if it is not, the dividing line between contractual and tortious liability may be blurred or, even, abolished. The way German lawyers have grappled with these, at times, incompatible aims is instructive for a number of reasons.

Noteworthy first is the fact that we are here faced with an originally judge-made doctrine. True, courts and academics have tried for a long time – as is customary in German law – to pin their views on some article of the Code. Thus, sometimes the expansion of the contract has been based on intention within § 157 BGB, relying on a broad interpretation of the contract, implied intentions of the parties, and an analysis of the end purpose of the transaction: see RG, RGZ 87, 292; RG, RGZ 98, 213; RG, RGZ 106, 126; RG, RGZ 127, 218 (an interesting decision); and RG, RGZ 152, 177. The BGH continued this practice. (See BGH, BGHZ 1, 383, 386; BGH, BGHZ 5, 378, 384; BGH, NJW 1956, 1193.) In other cases, even § 242 BGB (good faith) has been invoked to render respectability to what is a clear example of judicial activism. Larenz's scholarly writing (Larenz, *Schuldrecht I* (1st edn, 1953) 16. Larenz *NJW* 1956, 1193; *NJW* 1960, 79) changed not only the theoretical foundation of the new concept. Indeed, it also helped distinguish it from the traditional contract in favour of third parties regulated by §§ 328 BGB ff, thereby creating a new notion for German private law. This approach has greatly exercised academics. But the courts, in what has been called fits of

'pragmatism' (Markesinis, 'Conceptualism, Pragmatism and Courage: A Common Lawyer Looks at Some Judgments of the German Federal Court' (1986) 34 *American Journal of Comparative Law* 349) have refused to resolve this 'theoretical' issue, preferring to focus on the narrow aspects of each action before them. (Thus in BGH, BGHZ 56, 269, 273 the theoretical basis of the concept was deliberately left undecided; and in BGH, NJW 1977, 2073, 2074 it was regarded as irrelevant!) However, the discussions about the theoretical basis of the *Vertrag mit Schutzwirkung zugunsten Dritter* came to an end after it was codified in 2002 (see §§ 280 I, 311 II, III BGB).

A second interesting feature is, as we shall see, the emphasis on the relationship between contractual creditor and claimant/third party (which is known to the defendant/debtor) rather than on the foreseeability of the claimant/third party by the contractual debtor/defendant. The weakness of the latter (tort) approach is the potential open-endedness of the liability; an open-endedness which could, given the vagueness of the foreseeability test, lead to the blurring of contractual and tortious liability. Nevertheless, we can notice over the years a gradual weakening, or as some might say, erosion of the requirement of an interest of the creditor in including the third party in the protective scope of the contract (in one sense the most important element). As the concept of *Vertrag mit Schutzwirkung zugunsten Dritter* was first applied to situations involving physical damage to a third party, it was natural to demand that the creditor was responsible for the wellbeing (*Wohl und Wehe*) of the third party. Any injury to the latter could be analysed as an injury to the creditor himself which in turn explained the third party's inclusion in the contract (BGH, BGHZ 51, 91, 96). However, the extension of the *Vertrag mit Schutzwirkung zugunsten Dritter* into the realm of pure economic loss in the context of misstatements or other services by professionals also prompted a shift of emphasis from the relationship creditor/third party to that between third party/defendant. Here in this category of cases, of what has been called above 'expert liability' (*Expertenhaftung*), the criterion of the creditor's interest in the third party's wellbeing is much less appropriate and as a consequence was soon abandoned (see Kötz/Wagner, nos 325–26 and 488). This last point is particularly obvious from recent decisions (taken from what one might describe broadly as the banking/financial area, as well as the provision of expert opinions and legal service). Cases 43–46 illustrate this trend, which many (even in Germany) regard as dangerously expansive. The widening of the protective ambit of the contract is obvious not only in the fact that the courts no longer insist that the protected third party may be specifically identified in advance. More importantly, it is evident from the fact that the third party no longer needs to be in a close personal relationship with the creditor. Instead, the paramount question is 'in what circumstances the objective interests involved [sic] permit the inference that the parties [debtor/creditor] have [even] implicitly stipulated a duty of care towards third parties' (BGH, NJW 1984, 355, 356). While the BGH still founds the concept on implied terms reasoning and thus derives the rights of the third party from the contract between creditor and defendant (the 'expert'), the third party's (reasonable) reliance on the accuracy of the statement and the special skill of the defendant attain special weight in the individual case. (See, now, § 311 III 2 BGB, which stresses the importance of reliance.) It comes as little surprise therefore to see that some decisions also apply the concept to situations where there is a potential or actual conflict of interest between the contractual creditor and the third party (BGH, BGHZ 127, 378; for details see note to case 43). This move away from the requirement of the creditor's interest points towards a gradual convergence with the approach established

in *Hedley Byrne*. But the reader should be aware that in this area of the law it is difficult to generalise from individual cases. For instance, in BGH, NJW 2001, 514 the BGH reasserted the contractual foundations of the concept. The LG Frankfurt had argued that certain heads of damages were not included in the scope of the duty owed by the surveyor. This was confined to the creditor's (or for that matter the third party's) reliance on the correctness of the commissioned report concerning the presence of toxic substances in the soil of the development site. The BGH rejected this line of reasoning as being too restrictive. In this context the Court stressed that once the third party was included in the contract and had a relation with the promisee, reliance was not the main element in determining the extent of the surveyor's liability.

Let us then turn to the conditions required for what we shall call 'the opening of the contractual umbrella' (see case 43 and Markesinis/Unberath/Johnston, 210–11). We note that they are – in theory – three. First, the third party must come into contact with the performance of the contractual debtor and be endangered (or otherwise affected) by any misperformance in (roughly) the same way as the contractual creditor. This is commonly known as the requirement of proximity of performance (*Leistungsnähe*). Secondly, according to what is probably the better view and subject to the qualifications already made, the contractual creditor must have some interest in protecting the third party. Thirdly, the above two elements must be known to the debtor/defendant at the time of conclusion of the contract (or the commencement of the contractual negotiations).

This, as stated, is a subject rich in case law where most generalisations are dangerous; not all decisions are clearly reconcilable with one another (as German lawyers readily admit); and where the only discernible trend is for the courts – despite academic doubts – to move towards an expansion of the contractual umbrella. The codification of the *Vertrag mit Schutzwirkung zugunsten Dritter* did not change this trend – the previous case law remains applicable

The Drittschadensliquidation is a judge-made doctrine (but see § 421 I 2 HGB) which allows a creditor (the promisee) to a contract to claim (in contract) for loss resulting from the non-execution or bad execution of the contract, which falls not upon him (the creditor) but upon a third party provided that the third party has suffered a loss instead of the promisee. The advantages, if any, that the contractual approach offers over the tort reasoning will be considered in the notes to cases 47 and 48.

It is of first importance to note that the third party is entitled to have the right assigned. The principle involves an exception to the so-called doctrine of the creditor's interest according to which as a general rule a claimant can recover for his own loss only. Unlike the concept of the *Vertrag mit Schutzwirkung zugunsten Dritter* it does not affect the notion of relativity of contract for it does not enable the third party to sue directly.

Sometimes, however, a contract action may not be available, for instance where a third party to a contract of carriage damages goods in transit in an accident. If the buyer is bearing the risk, the seller will not suffer a financial loss, as he remains entitled to claim from the buyer the price of the goods (see § 447 BGB, which is however inapplicable in a business to consumer scenario, see § 474 II BGB). Yet, if the seller is the owner of the goods at the time of the accident, only he is entitled to bring an action under § 823 I BGB. The BGH (BGHZ 49, 356) allowed the action of the seller and applied the concept of *Drittschadensliquidation*. From this perspective, the concept appears as a general question of the law of damages. Still if the contract route is available, the action will most likely be in contract due to

the absence of true vicarious liability in tort, which will be examined more closely in chapter five.

The main rationale of the doctrine of *Drittschadensliquidation* (which was not codified during the Schuldrechtsreform of 2002) is to ensure that the defaulting party in the contract (or the tortfeasor) does not benefit from the fact that in these cases the loss has been shifted (*Gefahrentlastung* or *zufällige Schadensverlagerung*) from the creditor to the third party. If this exception to the doctrine of the creditor's interest had not been accepted, the defaulting party would not be liable to his creditor (since the latter has suffered no loss). Nor would the guilty party have been liable (in contract) to the third party in the absence of any contractual link between the two of them. Like all judge-made rights, however, this right is kept under close scrutiny lest it get out of control and expose the contractual debtor to an unlimited number of claims. Thus, the third party will be allowed to rely on the doctrine and seek assignment of the creditor's rights against the promisor or the tortfeasor only where special relations between him and the creditor to the contract cause the interest (and the loss) to be shifted on to him. The *Drittschadensliquidation* applies only in certain traditionally recognised situations. These are mainly three: certain agency situations, given that German law does not accept undisclosed agency; what English lawyers would consider to be trust and bailment cases; and, finally, in relation to carriage of goods. Indeed, the courts are reluctant to extend its scope except in an incremental manner. Thus, the BGH dismissed *Drittschadensliquidation* as an inappropriate way of solving the problem of product liability (see case 48), and denied its application to the factual context of the cable cases (see case 36). These two cases contain very useful comments on the scope and rationale of the doctrine.

The *fons et origo* of this development seems to be a decision of the Court of Appeal in Lübeck (Seufferts Archiv II (1857) 36, 47), where an agent was allowed to claim damages suffered by his 'undisclosed' principal. The need for a concept such as *Drittschadensliquidation* becomes obvious if one takes into account that German law does not accept undisclosed agency. Thus, on the one hand, the agent does not sustain loss because he is acting on account of the 'principal' who reimburses him, but on the other hand the 'principal' cannot sue directly on the contract. Hence, the agent is allowed to sue on behalf of the 'principal' (eg, RG, RGZ 75, 169; RG, RGZ 115, 419; BGH, NJW 1989, 3099). An equally important example of the application of the theory can be found in cases where the risk (but not the property) in goods has passed from the seller to the buyer (eg, §§ 446 and 447 BGB). In this type of situation, German law has for a long time now (see, eg, RG, RGZ 62, 331, 335; BGH, VersR 1972, 1138; BGH, VersR 1976, 168) accepted that the seller can recover damages from the wrongdoer in order to hand them over to the buyer or assign this claim to the buyer. (Indeed, because of § 285 I BGB (before 2002: § 281 BGB) he is obliged, if requested, to do so.) One should add, however, that in cases involving carriage of goods by land, the contract of carriage is normally treated as a contract for the benefit of the consignee which is a source of additional rights (see § 421 I 2 HGB as a sort of codified *Drittschadensliquidation*).

The concept of *Drittschadensliquidation* is confined to particular types of situation and is not freely available to third-party claimants (see cases 36 and 48 which contain guidelines as to when it is available). It has for instance not been applied to problems of product liability or the negligent misstatements situations discussed above, for they do not involve a transfer of a loss to a different person than the contracting party but increase the risk of liability: the product or the statement might cause loss to the contracting party but also to a per se indeterminate number of third parties. Therefore, additional controlling factors

are necessary which reasonably limit liability and which are not and cannot be provided by the more limited and special principle of transferred loss.

What unites the large miscellany of cases which the Germans have systematically brought under the heading of *Drittschadensliquidation* are two common elements. (Tägert's *Die Geltendmachung des Drittschadens* (1938) was groundbreaking in identifying these common features.) First is the fact that in these cases the invocation of the floodgates argument is inappropriate since one person only suffers a loss. Secondly, the co-contractor of the defaulting party – in our two examples the testator or the seller of the goods – will have no incentive to sue (or may simply no longer be around to sue). As German lawyers argue, in these cases the person who has suffered the loss has no remedy while the person who has the remedy has suffered no loss. If such a situation is left unchallenged, the defaulting party may never face the consequences of his negligent conduct; he (or his insurer) may receive an unexpected (and undeserved) windfall; and the person on whom the loss has fallen may be left without any redress; a meritorious claim would go down a 'legal black hole' to use the more vivid English term. The question to our mind is not whether the claimants should be allowed to recover – we believe the answer must be in the affirmative. The real question is whether the defaulting defendants should run the risk of incurring greater liability towards these claimants than they would have incurred had they been sued by their co-contractor. The German reply is negative; and their contractually flavoured solutions offer a neater explanation of this result than the tentative English attempts to harness tort for an answer.

Drittschadensliquidation has also been applied to cases of carriage of goods by sea where, as in English law, the rights under the bill of lading are transferred upon indorsement. (See BGH, BGHZ 25, 250.) To compare this concept with English law, it is useful to look at *Leigh and Sillavan v Aliakmon Shipping Co Ltd* (*The Aliakmon*) [1986] AC 785. Simplifying the facts, there the buyer, who had the risk but not the property in the purchased goods and who was not the carrier's contracting party, failed in his action against the ship owner whose negligent storage had damaged the goods resulting in the claimant's economic loss. In *The Albazero* [1977] AC 774, the House of Lords had favoured a contractual solution to the problem allowing, in principle, recovery of damages in a contractual action on behalf of a third party. However, the perceived drawback of this solution was that the third party could not compel the promisee to bring such an action. In the Court of Appeal in *The Aliakmon* ([1985] QB 350) Robert Goff LJ was thus persuaded to attempt to create a tort remedy based on the 'principle of transferred loss'. This would have enabled the third party to sue the carrier directly even though he did not have a proprietary interest in the goods or possession of them at any material time. In the House of Lords ([1986] AC 785, 817–18), Lord Brandon of Oakbrook refused to follow this line of reasoning mainly because he did not accept that there was, in this respect, a lacuna of English law. The learned judge was also suspicious of the new remedy on doctrinal grounds since, in his eyes, it amounted to a derivative action, which was contrary to its tortious nature. For the special feature of the transferred loss principle was that the liability of the carrier was 'contractually flavoured' in so far as the duty owed to the third party was shaped by the underlying duty to the goods owner. This, in turn, was determined by the exclusion and limitation clauses contained in the contract of carriage as contained in or evinced by the bill of lading. (In 1992 the problem was remedied by statute: Carriage of Goods by Sea Act 1992.)

By contrast case 46 was a decision involving land transport. The seller was the contracting party and also the owner of the goods, while the buyer was on risk. The BGH, following established case law (starting with RG, RGZ 62, 331), had no difficulty in resorting to

the theory of *Drittschadensliquidation*. This meant that the seller, was entitled to recover damages in respect of the buyer's loss, and since this right had been assigned to the claimant buyer, the latter was allowed to recover damages for his own loss from the defendant carrier. In German law the claimant buyer in *The Aliakmon* would have been entitled to require the promisee, the seller, to assign his remedy against the carrier (by relying on § 285 I BGB). In practical terms, this addresses Lord Goff's main objection against a contractually founded theory of transferred loss (see *The Aliakmon* [1985] 1 QB 350, 390) and his later comments in *White v Jones* [1995] 2 AC 207, 257 and in *Alfred McAlpine Construction Ltd v Panatown Ltd* [2001] 1 AC 518, 544–45: 'The shortcomings of this rule must, I imagine, have been that it left the initiative with the seller, rather than with the consignee who was the person who had suffered the loss of or damage to the goods'). Thus, the doctrine of *Drittschadensliquidation* also provides a solution in those cases where the promisee might not have an incentive to enforce the right on behalf of the third party.

The second and potentially significant extension of English contract occurred in the context of the promisee's remedies in respect of a third party's loss. In *Alfred McAlpine Construction Ltd v Panatown Ltd* [2001] 1 AC 518, contractual remedies were extended to cover situations where a building employer is not the owner of the development site at the time of the breach of the building contract and, as a result (arguably) suffers no financial loss. The builder/defendant in these cases based his defence on the 'no loss argument'. However, the courts allowed recovery in contract of substantial damages in respect of the site owner's loss. Andrews, *Contract Law*, 183–87 and Burrows, 'No Damages for a Third Party's Loss' (2001) 1 *Oxford University Commonwealth Law Journal* 107 consider this decision to be limited to cases where, before the 1999 Act, there was a remedial gap. The building employer is able to sue on behalf of the third party site owner/financier of the project and is required to account to that person. Accordingly, the measure of the damages recoverable by the building employer is the site owner's loss (the cost of cure and lost rental). This does come close to the *Drittschadungsliquidation*, while rejecting this terminology. (See Lord Goff's pessimistic statement that 'the concept is not an easy one for a common lawyer to grasp': Markesinis (ed), *The Gradual Convergence* (1994) 129 ff.)

The comparatist must first describe a foreign system to his readership and then see what conclusions can be drawn from it to benefit his national law. The picture of German law given thus far is, inevitably, a simplified one. The reality is infinitely more complex, if not inscrutable to the foreign observer who treads on perilous ground when expressing a critical view of this system. But even the potentially distorted appreciation of foreign law by the comparatist may be of use to the national lawyer. Four points should, thus, be made at this stage.

First, the test that will determine who is to be included within the protective umbrella of the contract is crucial if the concept of contract with protective effects vis-a-vis third parties is to be employed. Most German lawyers agree that the list of such persons must be limited; but they differ greatly as to the criteria that must be employed to achieve this aim and, as a result, as to who precisely enjoys such protection. The traditional emphasis on the creditor's interest to protect the third party/claimant seems to be the most precise test without being excessively restrictive. In any event it is probably more workable to place the emphasis on the relationship between creditor and third party/claimant (which is known to the debtor/defendant) than to operate, as the common law does, on the basis of the amorphous foreseeability test applied to the claimant/defendant relationship. However, as recent

developments show, this approach might reach its limit where there is a potential conflict of interest between creditor and third party. This demonstrates that recourse must also be had to the reliance placed on the special skill of the professional in addition to the purpose and scope of the defendant's undertaking to the contractual creditor.

Secondly, one might venture the thought that the more recent attempts to enlarge the circle of contractually protected persons threatens to undermine the security and (relative) predictability provided by the older tests. If the current trend remains limited, however, to the banking/financial services, it is understandable if not necessarily justifiable. For in these cases the German courts are essentially faced with variations of the *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465 problem which they cannot solve through tort law because of the restrictive provision of § 823 I BGB. The way they expand contract is thus, essentially, as arbitrary as our own attempts to limit tort duties in similar factual situations. Though the pressures are exerted in different directions in the two systems, the problem is the same: discovering the proper bounds of liability which modern insurance practices tend to expand outwards.

Thirdly, the concept of contract with protective effects vis-a-vis third parties and the theory of transferred loss originally had a different area of application. The first was used in cases of physical injury and property damage (mainly in order to avoid the problems created by § 831 BGB); the latter applied to cases of pure economic loss, which had not always received full and adequate regulation by the positive law. In this original context the two notions presented one further difference. In the former, the risk of the contractual debtor was *widened* by the inclusion of a third party within the contractual umbrella. For example, the concept of contract with protective effects vis-a-vis third parties was extended in 1965 by the legal malpractice case (concerning the defective will: BGH, NJW 1965, 1955) to cover pure economic loss. Therefore, one now has two essentially contractual devices for dealing with these cases of economic loss.

Fourthly, and most important, German law, once stripped of its many technicalities and competing theories, is characterised essentially by one central idea that could be useful to both English and American common lawyers. This is that these actions are contractual not tortious in nature. No matter that this approach grew out of the necessity to avoid defective or narrow tort provisions. No matter which device is used to accomplish the end aim (contract with protective effects vis-a-vis third parties or 'transferred loss'). In the end, what matters is that the result achieved through the medium of *contract* ensures that the claimant succeeds in these cases but that the defendant's liability remains similar to that which he had agreed with his co-contractor. This is not the right approach for all instances of pure economic loss; but it seems to be eminently suitable for those cases that straddle the traditional contract/tort divide.

II. Liability for Untrue Statements Under § 824 BGB

§ 824 BGB provides:

> A person who declares or publishes, contrary to the truth, a statement which is likely to endanger the credit of another, or to injure his earnings or prosperity in any other manner, shall compensate the other for any damage arising therefrom, even if he does not know of its untruth, but should know of it.

This is a distinct form of liability that protects economic interests where the loss has been caused by untrue statements. This is a relatively insignificant part of delict and is often omitted by shorter German textbooks. This is because the interests protected by this paragraph are also protected in other ways. As has already been seen, § 823 I BGB includes among 'other rights' the 'right of an established and operating business' (see chapter two, section II.E.iii). The earnings and prosperity of an individual may well be connected to a business which he runs, so § 823 I BGB would provide an alternative. § 187 StGB creates a criminal offence of defamation which punishes those who use untrue words deliberately to harm the business reputation of another and breach can give rise to civil liability under § 823 II BGB (RG, RGZ 51, 369, 375). Since §§ 823 and 826 BGB can cover situations where true statements are made but without a legitimate interest, then these may offer a better protection than § 824 BGB.

The liability here attaches to 'facts' and not to value judgements or opinion, which obviously makes liability for restaurant reviews or comparative advertising difficult.

In competition law, the Law on Unfair Competition (UWG) prohibits very specific kinds of unfair marketing or competition and breach is thus much easier to prove than the general provision of § 824 BGB. There is no need to refer to commonly accepted standards to prove a breach because the required standards are presented in the UWG. Furthermore, under the UWG, it is up to the person making the statement to prove the truth of a statement which falls within a proscribed category. On the other hand, the limitation period under § 824 BGB is longer – three years (see § 195 BGB), not six months under the UWG (see § 11 UWG).

There is a practical limitation nowadays in relation to § 824 BGB. Much marketing communication is made by internet. Whereas § 824 BGB is predicated on a direct statement by the tortfeasor (such as on its homepage), it is more difficult to bring within its scope the results of information provided by intermediaries – search engines, blogs, social media fora, tweets and so on (*Münchener Kommentar*/Wagner, § 824 BGB, no 9). We have already considered the liability of intermediaries under § 823 I BGB in chapter two.

So, while this is a potentially useful way of protecting economic interests, it is limited in its practical scope.

III. Delictual Liability for Products

Bibliography

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A. Introduction

Product Liability is now besides § 823 BGB governed first by specific legislation – the Product Liability Act (ProdHG). The ProdHG of 1989 is implementing Product Liability

Directive 85/374/EEC which aims for a complete harmonisation of the liability of producers for death, personal injury and damage to consumer property caused by 'defective' products which they have put into circulation. That said, in practice the Produkthaftungsgesetz is little used. Wagner (in Whittaker (ed), *The Development of Product Liability* (2010) 138) has commented:

> The explanation for the feeble impact of the [Product Liability] Directive is that its liability regime is much closer to fault-based liability than the framers thought, while at the same time the scope of compensable loss was restricted. Thus, a claimant-victim stood to lose very little in terms of liability but gain a lot on the quantum side if he relied on the traditional law of delict instead of the Product Liability Act. The second half of the explanation will be expounded below, namely the drying up of litigation for compensation of product-related losses. Whatever the causes may be, the Product Liability Act and the underlying Directive merit the judgment: much smoke, no fire.

For this reason, we continue to present the contractual and delictual bases of product liability in this chapter. Linked to economic loss, the topics show the relationship of contract and delict.

B. History

The law of product liability – and German lawyers have adopted this American term – was one of the most hotly debated issues during the 1960s and 1970s, the voluminous literature and case law constantly proving the theoretical and practical interest in the subject. This was a 'new' area of the law to the Germans. That is not to imply, of course, that product liability cases cannot be found before the 1960s of the last century. (See Wagner's contribution to Whittaker (ed), *The Development of Product Liability* (2010) chapter 4, which locates the earliest case in 1902: 118.) But it does mean that until about the late 1950s important instances of product liability would not only remain uncompensated, they would also pass almost unnoticed by the law reports and the academic literature. In 1956, for example, the BGH had to deal with a claim brought by a claimant whose bicycle suddenly collapsed and injured him (BGH, DB 1956, 592). The accident was not due to a defect in design but in the production of the particular bicycle. But the Court had little sympathy with the claimant's complaint and dismissed it in a cavalier manner with the statement that 'common experience suggests … that such technical defects cannot be prevented'. In the Court's view, the accident should have been treated as one of those unfortunate things that happen in life and must remain uncompensated. That the case was only reported in a specialised legal journal also indicates that it was not treated as one of general interest. With two interesting exceptions of dissertations written in the 1930s under the direction of the famous Ernst Rabel, the academic literature showed an equal lack of enthusiasm for a topic, which nowadays is, if anything, overworked.

The change came in the early 1960s when Professor Werner Lorenz published an article, which for the first time made the majority of German lawyers aware of development in this field in the US (Lorenz, 'Produkthaftung' in Mikat (ed), *Festschrift der Rechts- und Staatswissenschaftlichen Fakultät der Julius-Maximilians-Universität Würzburg zum 75. Geburtstag von Hermann Nottarp* (1961) 59 ff). The article, making excellent use of the comparative method – Lorenz had studied at Oxford with the late Professor Lawson and

later worked at Cornell with Professor Schlesinger – appeared at the right time even though in the beginning legal practitioners vehemently opposed the introduction of American ideas. However, the 1960s and 1970s were decades that witnessed a number of spectacular product liability accidents, which triggered off public interest in this problem. In 1967, for example, nearly 800,000 owners of Ford cars were informed of design defects in a particular model and were advised to take certain precautionary steps. A year later, Volkswagen in Germany had to recall some 160,000 defective cars. Already in 1961 the Thalidomide scandal (in German known as *Contergan-Skandal*) had broken out leading to the birth of thousands of seriously incapacitated children and to worldwide litigation. These events, coupled with a general increase in consumer-orientated legislation, resulted in the development of the product liability law. The German Juristentag debated the issues in 1968 and this helped to shape the thinking of the BGH in its *Fowl Pest* decision of the same year (case 48 and Wagner in Whittaker (ed), *The Development of Product Liability* (2010) 147).

As will become clear, this topic is now (also) covered by the ProdHG of 1989 (see chapter seven). But the legislation has for different reasons not been a major source of liability in Germany, and so it is still worthwhile and important as already said to consider the liability for products in contract and under § 823 I BGB. In any case, product liability has been formative in shaping delict.

C. Contractual or Quasi-Contractual Solutions to the Problem?

Broadly speaking, one can divide the development of product liability before the Product Liability Act into two phases. The first, which culminates with the seminal *Fowl Pest* judgment of the BGH in 1968 (case 48), is basically preoccupied with finding a legal basis for this essentially new heading of liability. The second was one of consolidation, elaboration and even expansion of the delictual action firmly established since 1968. A third phase came with the Product Liability Act of 1989 (see chapter seven).

The leading judgment of 1968 clearly reflects the preoccupations of academics to find a legal basis for product liability in so far as it devotes much space to the detailed consideration of the various contractual or quasi-contractual theories developed in the 1960s to meet the new situation. If a common lawyer were to express surprise that this search for a juristic basis would be conducted in the area of contract law rather than tort law he should then consider the following two points.

First, one must repeat what was said earlier on, namely that the law of contract has proved more pliable and able to expand on the civil law systems than it has in the common law. The doctrine of consideration is the main reason why the common law was forced to develop its law of torts. But wherever consideration has been taken somewhat less seriously – for example, in the US – the concurrent growth of contractual and delictual remedies has been a notable feature.

Secondly, one should note the considerable advantages that a claimant could obtain if his action was dubbed by German law as contractual or quasi-contractual. Two should be mentioned here. The first is related to the burden of proof. Though in the civil law systems (unlike the common law) fault is an element of an action for breach of contract as well as tort, the burden of proof may be different in these two actions. Thus, § 282 BGB, which

was applied, by analogy, to other contractual remedies, provided that, 'If it is disputed whether the impossibility of performance is the result of a circumstance for which the debtor is responsible, the burden of proof falls on the debtor', ie, if contested, the defendant has to disprove his fault. (This result follows now from § 280 II BGB.) On the other hand, according to the general rules of tort law, in a product liability case the claimant had to show that the product left the defendant's enterprise in a faulty condition and that the defendant, or his legally appointed representative, had not organised his business in such a way as to enable the defect to be detected. The second, and not entirely unrelated, reason that made contractual actions preferable to those founded in tort could be found in § 831 BGB. This deals with the problems of vicarious liability and will be discussed in greater detail below in chapter seven. Here suffice it to say that it does not establish a true rule of vicarious liability but makes employers liable for the unlawful acts of their employees (*Verrichtungsgehilfen*) only where they are themselves guilty of negligent selection or supervision of the employees. In contrast debtors are, according to § 278 BGB, fully liable for the faults of the persons whom they employ in the execution of their *contractual* obligations (*Erfüllungsgehilfen*). Finally, one should also bear in mind the relatively short period of limitation which used to be applicable to tort claims before the revision of the Code in 2002 (especially § 195 BGB).

Having stated the reasons which prompted German lawyers to turn to the law of contract rather than the law of tort initially, one should look briefly at the various contractual or quasi-contractual methods advanced by academic writers. The brief comments that follow should be read in conjunction with the relevant passages of the leading *Fowl Pest* case (case 48).

One way of making the manufacturer liable to the ultimate consumer is by discovering an express or implied guarantee, which is directed to the ultimate consumer and on which he relies to his detriment. But such reliance is difficult to establish.

A second *contractual* method can be found in the various attempts to discover a contract in favour of a third party or a contract with protective effects vis-a-vis third parties. The first type of contract (*Vertrag zugunsten Dritter*) is regulated by §§ 328 BGB ff. As already explained, this type of contract allows a third party (the ultimate consumer) to require performance of the contract concluded between the creditor and the debtor (eg, the manufacturer and the wholesaler). On reflection, however, this is a rather awkward notion. For what the third party/consumer needs is not the right to enforce the *primary* contractual obligation (delivery of the thing in exchange for payment of the price). Rather, his need is to be included under the protective umbrella of the *subsidiary* contractual obligations (in our case to deliver the thing in good order and with clear instruction, etc). This way of reasoning led German courts to develop the already discussed *Vertrag mit Schutzwirkung für Dritte*. In this way, third parties can be given the protection afforded to the main creditor which emanates from a cluster of subsidiary obligations which would be included in every such contract in accordance with § 242 BGB (good faith).

However, we have already noted the need to keep this expansion of the contractual umbrella under control lest it undermines the relativity of the contractual bond. To put it differently, *who* will be treated as a third party and receive such protection? Though as already stated the requirement of 'proximity to the performance' (*Leistungsnähe*), a close relationship (*personenrechtliches Fürsorgeverhältnis*) between the contractual creditor and

the third party has been relaxed by some recent decisions, this has not occurred in the context of product liability. Indeed, it is noteworthy that even those authors who have argued in favour of expanding the circle of 'protected' third parties have refused to apply their theories to this area of the law. (See, eg, Canaris, 'Die Produzentenhaftpflicht in dogmatischer und rechtspolitischer Sicht' *JZ* 1968, 494, 499 ff.)

The *Drittschadensliquidation* has also been considered but finally rejected by the courts. In the *Fowl Pest* case (case 48) the BGH, disagreeing with the OLG, would not allow the vet to demand from the pharmaceutical company (which had sold him the defective vaccine) the loss *suffered by the owner* of the chickens which died as a result of the inoculation. (If such a claim had been recognised it could have been transferred by the vet to the claimant and pursued by the latter.)

IV. Strict Liability?

In addition to the above contractual theories, the jurisprudence also dealt with a number of others, which share some common elements including the desire to justify a strict or semi-strict type of liability. Two BGH of them deserve a brief look since they are expressly referred to (and rejected) by the BGH.

The first, advanced by a leading expert in the field (Diederichsen, *Die Haftung des Warenherstellers* (1967) 297 ff, 327 ff, 345 ff) can, in a rather crass manner but for simplicity's sake, be reduced to two basic propositions. First, the basic relationship in these cases is that between manufacturer and ultimate consumer. This is one of 'reliance', irrespective of any awareness of any advertisements by the manufacturer so long as the defective goods were purchased from a sales network set up by the manufacturer and were already defective at the time they left his factory. Secondly, that this relation is *sui generis*, not regulated by the written law and must thus be shaped in its details by the judge. A corollary to this is that the liability is strict.

The Court's dislike of any theory, which cannot be pegged on a clear provision of the Code, is obvious from the way this theory is dismissed. Equally obvious – and in tune with the Court's long-established practice – is its refusal to discover new headings of strict liability in the absence of legislative intervention (BGH, BGHZ 54, 332). A third objection, not mentioned by the BGH but stressed by academics, is the following: if the manufacturer of goods is to be strictly liable, why should this liability be limited to cases where his goods were sold bearing his name (or through a sales network set up by him) and excluded whenever the same goods were sold unidentified in a department store or, even, bearing the latter's commercial brand?

Lorenz's theory ('Warenabsatz und Vertrauensschutz' (1963) *Karlsruher Forum* 8, especially 14 ff) shares a number of common points with some other theories also considered and rejected by the Court. He, too, for example, puts the emphasis on the relationship between producer and ultimate consumer and he, also, is prepared to attach considerable significance to the reliance that one person (the consumer) places on the conduct of another (the manufacturer). Like other writers, Lorenz also accepts that we are here faced with a lacuna in the written law which must be filled in a way that will ensure that the claimant is given a protection equal to (if not greater than) that enjoyed by contracting parties (moving

towards strict liability). Unlike other authors, however, Lorenz makes a clear attempt to base his solution on a specific provision of the Code and this, in his opinion, is § 122 BGB.

This provides that if a declaration of an intention is void, either because it was made in error or because it was not seriously intended, the person who made the declaration must compensate the other party for the damages he has sustained as a result of relying upon the validity of the declaration. (Incidentally, the damages in this case cover only the reliance interest and not the expectation loss.) This provision, according to Lorenz, can be analogically extended to cover the present problem, since the manufacturer, through the advertising of his products, leads the ultimate consumer to expect that his products will be free of all defects. In its judgment in the *Fowl Pest* decision (case 48), the BGH directed its criticism mainly towards Lorenz's point about the significance of modern advertising techniques and the effect they can be taken to have on the ultimate purchaser. It is submitted, however, that Lorenz's view had two further weaknesses: first, it is by no means clear (to a non-German lawyer at least) that § 122 BGB, which envisages an entirely different situation, is capable of such an extension. It would appear more likely that Lorenz is trying to make in a very ingenious way the best of a bad situation, ie, to use the Code to solve a problem which could not have really been envisaged by its draftsmen. Secondly, even if § 122 BGB could be so extended, it would not lead to the imposition of *strict* liability on the manufacturer towards the ultimate consumer (with whom the manufacturer has no contract), but to a liability based on fault (in accordance with the contract of sale) towards his (the manufacturer's) *immediate* purchaser – a solution which seems neither very reasonable nor attractive.

V. The *Fowl Pest* Decision of 1968 and the Move from Contract to Delict

The contractual or semi-contractual theories considered and rejected by the BGH in its 1968 decision (case 48) suffered from one further defect which was shared by all of them. For they all aimed at protecting the person who was in some way involved in the sales chain and somehow could justify a 'relationship' with the manufacturer by means of reliance or a guarantee or some other manifestation on his part concerning his goods. True, some theories went further by trying to include within the protective circle other persons such as the family of the ultimate consumer or others living or working in his household. But if the policy reasons for imposing liability on the manufacturer are correct – and these include his greater ability to detect and correct a defect, to insure against the risk, and to shift the cost of accident when it is realised – then the same type of protection should be afforded even to third parties, such as the proverbial bystander who is injured by the exploding ginger beer bottle. Basing liability on tort, and in particular on § 823 I BGB, provided the necessary breakthrough. The Court realised that contract law had exhausted its limits and the time had come to utilise the law of tort. When studying the judgment, the reader should, among other points, also note the following.

It is first worth noting that the BGH could and did base liability on § 823 II BGB since the defendant (vaccine manufacturer) was in breach of a special statute which was correctly deemed to be a protective statute in the sense of that provision. This is important since

the manufacturer's duties of care will, in most cases, be judge-made; but they can also emanate from the breach of duties laid down by specific statutes. The Machinery Protection Act (*Maschinenschutzgesetz*) of 24 June 1968, for example, made manufacturers (and distributors) of a whole range of machinery, tools etc liable for personal injury or death (but not property damage or economic loss) suffered by all users. (This has now been replaced by the *Geräte- und Produktsicherheitsgesetz* of 2004.) Many instances of accidents resulting from defective equipment will thus easily lead to the imposition of liability. The Pharmaceuticals Act (to be discussed in chapter seven) and the food and drug legislation should also be included in this category and can easily dispose of the manufacturer's liability. But the significance of the decision lies in the fact that it did not stop at § 823 II BGB but, instead, proceeded to state that § 823 I BGB should also apply.

As stated, the difficulty with § 823 I BGB is its requirement that the claimant needs to prove the defendant/manufacturer's fault. One way around this problem would be for the Court to invoke the prima facie rule (not dissimilar to the common law doctrine of res ipsa loquitur); indeed, this had been done successfully in several cases involving § 831 BGB. However, the Court considered this to be an inadequate measure since all too often the owner of a business can show that the defect in the product might have been caused in a way that does not point to his fault – evidence which generally relies on activities in his business and which is difficult for the injured party to disprove. Consequently, when damage has arisen within the range of the manufacturer's business risks, he cannot be regarded as exonerated *merely* because he points out that the defect in the product might have arisen without any organisation fault of his. On the contrary, he must supply positive and complete evidence that the defect in the product is not due to his fault.

The courts had already reversed the onus of proving fault in the context of § 823 II BGB. They now saw no good reason why the same should not also be done with § 823 I BGB, given the special features of product liability and in particular the victim's de facto inability to know what was happening in the manufacturer's enterprise. The development of a separate category of liability under the heading of the so-called *Produzentenhaftung* brought about a further significant departure from orthodox reasoning, namely §§ 831 and 31 BGB. § 831 BGB which – originally – was confined to negligent selection or supervision of employees was reinterpreted and widened to also encompass the very organisation of the company. It also served to found an obligation to put schemes of production in place that would ensure that the product is free from dangerous defects. The appropriateness of § 31 BGB, which imputes the negligence of members of the management to the company, also seems doubtful. Both these provisions do not fit easily into the problem of product liability. In this category we are not in fact dealing with issues of vicarious liability. For the duties of care are primarily addressed *to the manufacturer*, who has to avoid putting into circulation dangerous products. Thus, the company and not its employees or executives is the direct addressee of these duties of care to structure the manufacturing process in an adequate way. The difficulties to which this slight discrepancy between the written law and law in action has given rise, come to light more fully in the cases regarding the liability of employees or executives themselves under the heading of product liability (cases 50 and 52).

As expected, the decision resulted in the insurance market promptly producing a new form of product liability insurance for industrial enterprises. It also gave rise to a rich case law which German scholars discuss under four different headings: (i) defects in manufacture; (ii) defects in design; (iii) defects in instructions; and (iv) development risks.

These distinctions have remained in use despite a parallel regime of liability governed by the Product Liability Act.

VI. The Various Forms of Product Liability

A. The Producer's Liability for Defects in Manufacture

Here one is talking of an *individually* defective product, the defect usually being due to some kind of negligence or inattention in the manufacturing process. The leading case was precisely one of those cases so, strictly speaking, its ruling as to the burden of proof was directed only to this type of product liability situation. It will be noted, however, that subsequent cases have extended the application of the rule to include categories (B) and (C) discussed below.

In these instances, the claimant's task is usually limited to proving that his hurt emanated from the area of the producer's organisation and the risks attendant on it, and that it resulted from an objective defect of the product which made it unsuitable to be put into circulation (BGH, BGHZ 51, 91, 105; BGH, NJW 1973, 1602). This burden is easily discharged save in those cases where the evidence may suggest that the defect arose *after* it had left the manufacturer's zone of influence. (See on this Lorenz's observations in 'Beweisprobleme bei der Produzentenhaftung' 170 *AcP* (1970) 366, 381 ff, where, once again, he makes extensive use of the American case law.)

Once the claimant has established the above, the onus shifts to the defendant (manufacturer). He must then show that he, himself, was not in breach of one of his duties of care (imposed by statute or the case law) and that all persons in his employment were equally innocent of such a breach. In theory, therefore, a manufacturer of an isolated defective product – sometimes referred to as a 'runaway' (*Ausreisser*) – can escape liability. (Though this is not an admissible defence under the Product Liability Act.) Nevertheless, this exculpatory proof under § 831 BGB requires the manufacturer – at any rate whenever the manufacturing process is not fully automated – to name *every* individual involved in the manufacturing process and prove his 'innocence' (BGH, NJW 1973, 1602, 1603). This is clearly a burden of proof which makes this in name only fault-based liability but, in effect, greatly approximates the strict tort liability that is imposed by American courts. Once again, this misuse of terms has not passed without criticism, not least because the fault-based system can increase the time and cost of litigation and impede settlements out of court. This tendency to extend the area of quasi-strict liability was also underscored by a decision of the BGH in 1975 (BGH, NJW 1975, 1827) which held that the above-mentioned liability would be imposed not only on the manufacturer but also on his 'high-ranking' employees. This result, however, appears to be very dubious to say the least.

B. The Producer's Liability for Defective Design

It has been noted that the leading case dealt with an individually defective product. But the case law did not stop there. It extended the new rule to apply also to cases of defective design (case 53) and in these instances, since many products may be involved, the defend-

ant may be held liable to extensive damages. On the other hand, the claimant's position in this case *may* be more difficult than in the previous one, since he will not only have to prove that the product was defective (in the sense that the defective design was avoidable given existing scientific and technical knowledge). He will also have to persuade the court that its design was defective in a way that it created an unreasonably great risk of danger for him and/or third parties. Whether this is so, will depend on the court's appreciation of all the circumstances in accordance with the formula already given. Factors to be taken into account include the normal or extraordinary conditions of use, the type of average user, and the kind of dangers that may be specific to this type of product. Product liability may also extend to risks which arise from improper use of a product where the manufacturer should foresee that, in the light of the conditions under which the product was used, it would not always be used with the utmost care (OLG Köln, NJW-RR 1991, 285.) The court may also weigh carefully whether an alternative design would be economically feasible and to what extent it would reduce the risk of such damage occurring. If such a defect in design is proved, then the manufacturer's breach of the required standard of care will also be established.

Nowadays, many administrative regulations determine the standards that must be met by particular products, often as the result of EU harmonised legislation or ISO standards. Furthermore, in many cases the rules and standards are set by officially recognised legal institutions (eg, the Deutsches Institut für Normung, the Technischer Überwachungs-Verein, etc) and conformity with these rules will, invariably, improve the manufacturer's/defendant's position in a lawsuit involving one of his products. Compliance with mandatory regulations may now even afford a manufacturer with a complete defence in accordance with § 1 II no 4 of the Product Liability Act. Some commentators, however, feel that compliance with minimum standards may not, necessarily, exonerate the manufacturer.

The picture described above could become more complicated where the ultimate damage could be attributed to a defective component. The permutations here are innumerable. The defective component – provided by a supplier – might have been incorporated in the final product by the main manufacturer. Should his liability depend on whether he checked or ought to have checked the component before incorporating it in his product? Should the answer be different if the component was manufactured to his specifications? And what if the defect is not due to the component but is due to the way the components were put together?

The rich case law made a general answer impossible, but previously Professor Kötz (*Deliktsrecht* (2nd edn, 1979) 204) summarised the guiding principle of the law (as it then stood) as follows:

> In all these cases the strict rules of the law of product liability are applicable only in so far as their policy aims make them suitable for the occasion. This will be the case whenever the defendant is under an obligation to take the necessary measures within the organisation and area of his responsibility in order to prevent or remove the kind of defects which have led to the harm in suit.

This, for example, was the result whenever components were incorporated in a product which was finally marketed and sold under the manufacturer's own name (eg, BGH, NJW 1985, 2420). Liability was also, invariably, imposed where components were not carefully selected, tested, or constructed in accordance with the manufacturer's specifications (see, eg, BGH, BGHZ 86, 256; BGH, NJW 1985, 2420; OLG Köln, NJW-RR 1990, 414.) As a result of the enactment of the Product Liability Act in 1989, however, product liability law will apply

to manufacturers of finished products and component parts alike. (The manufacturer of the *component* is not liable if the deficiency is due to instructions given by the manufacturer of the *finished* product or is attributable to the defectiveness of the finished product.) Similarly, dealers and importers who were *generally* not liable under the old regime (BGH, NJW 1980, 121 and BGH, NJW 1987, 1009 respectively), may now be saddled with liability in accordance with the Product Liability Act.

C. The Producer's Liability for Defective Instructions

Once again the scope and extent of these duties of care are in principle fixed by the rich case law (eg, BGH, BGHZ 64, 46; BGH, NJW 1972, 2217; BGH, NJW 1981, 2514; BGH, NJW 1986, 1863). The duty to provide instructions arises at the time when the product is put into circulation though the manufacturer is under a duty to monitor new developments and, if necessary, alter the instructions that originally accompanied his product. The law on this subject was reviewed by the BGH in the 'apple-scab' case (BGH, BGHZ 80, 186; NJW 1981, 1603) where apple producers suffered serious production losses after having used a spray which was meant to prevent apple scab but which became useless after repeated use. Laboratory experiments (already published at the time of the accident) had mentioned this possibility, but the manufacturers of the spray had failed to bring this information to the attention of the apple producers. Had the knowledge that the spray was ineffective emanated from the manufacturers' own sphere of control, then the usual reversal of the onus of proof would have operated in favour of the claimants; but since it was generally available at the time of the incident, their claim was rejected. In another judgment the BGH held that the duty to provide information is linked to the intended use of the product. Thus, a manufacturer is under no duty to provide warnings against dangers that will arise if the product is put to a use other than that for which it was intended (BGH, NJW 1981, 2514). The degree of danger posed by the product and the interests likely to be affected (life, property, etc) will, however, ultimately influence the scope and standard of duty of the manufacturer. Thus, warning labels must clearly specify the kinds of danger which may arise from the use of a particular product. If considerable injury to body or health may result from the product's misuse, the consumer must be able to discern from the warning label why the product may be dangerous (BGH, NJW 1992, 560). And if infants develop cavities from constant sucking of sweetened children's tea drunk out of plastic bottles, the manufacturer of the tea is liable if he failed to place a clear warning on the product (BGH, BGHZ 116, 60; BGH, NJW 1994, 932; BGH, NJW 1995, 1286). Thus, adequate warnings must always be given in the case of pharmaceutical products likely to be misused – especially those likely to be misused by children. There is no special heading for instruction defects in the Product Liability Directive; but the issue is dealt with under the general heading of product defects (Article 6 of the Directive).

D. The Producer's Liability for Development Risks

The problems here are, essentially, different from those discussed in the earlier sections and thus make the return to the fault principle easy to recommend. Typically, in these cases

the product will have been manufactured in accordance with the technological knowledge of the time, but subsequently acquired information reveals its potentially harmful effects. Many believe that to make manufacturers carry such a risk could hinder technological progress. To make them strictly liable for such development risks would also run counter to the rationale of imposing such a strict liability in the first place. For, it will be remembered, one of the justifications of imposing strict liability on the manufacturer is his ability to detect and avoid the defect. In the present instance, however, by definition this is not possible and the manufacturer's duties are limited to an obligation to warn consumers or even withdraw their products once they become aware (or ought to become aware) of the defect or of their potential harmful consequences. The rules of the leading case have thus not been extended to this category. Article 15 VIII of the Product Liability Directive gives Member States the option of deleting the defence of state of art contained in Article 7(e) of the Product Liability Directive, but Germany has not exercised this right so the defence has been retained. (See for the state of art defence § 1 II no 5 of the Product Liability Act. Note, however, that the defence is not available under the Pharmaceutical Act; and the relationship between this enactment and the Product Liability Act has not been clarified. (See also § 15 of the Product Liability Act.) The retention of the state of art defence will not, however, absolve the manufacturer from continuously observing his products and warning users of (and if necessary recalling) products that are subsequently revealed as defective. (BGH, NJW 1987, 1009 is an interesting case since it extends the manufacturer's post-marketing duties concerning his own product to the performance of component parts.)