European University Institute (EUI) Florence/European Private Law Forum
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Real Property Law and Procedure in the European Union

National Report

Germany

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1. Real Property Law – Introduction

1.1. General Features and Short History

The main legal body of German real property law is codified in the **third book of the German Civil Code (BGB)**, dealing with law of rights in rem in general including both movables and land. It comprises general provisions on interests in land (§§ 873-902), that is ownership (§§ 903-928, 985-1007), coownership (§§ 1008-1011), servitudes (easemenet appurtenant, easement in gross, usufruct, §§ 1018-1093), real right of preemption (§§ 1094-1104), rentcharge (§§ 1105-1112) as well as pledges on real property (mortgage, land charge and rentcharge, §§ 1113-1203 BGB). Some basic legal concepts are also to be found in the first book of the Civil Code (§§ 90-103 BGB), such as „thing" (Sachen), „component" (Bestandteile; Zubehör; Inventar), and „fruit". In general, changes relating to rights in land - property rights as well as other rights - and any transfer and encumbrance of such rights are subject to a uniform principle of law laid down in § 873 BGB. Accordingly, an agreement to the change in the right in rem between the present title holder and the acquiring party (1) and an entry in the Land Register under the regulations of the Land Registry Act are required (2).

In this context it is necessary to notice that German law distinguishes between the so-called obligatory contracts and the real contracts. By way of the obligatory contract a duty of the debtor to do or to refrain from doing something as well as the corresponding right of the creditor is established. In order to perform the obligation a further contract in rem may be required to effect a change in the title such as the transfer of ownership or the encumbrance of land. This distinction between obligatory and real contracts is said to be peculiar to German law and is known as the so-called "**Abstraktionsprinzip**", the principle of.[1] Accordingly, rights in rem are valid irrespective of the existence or validity of the underlying obligation which may bind the parties concerned to perform the transaction in question. The obligatory contract forms the causa to the real contract. Provisions to all contracts are to be found in the first book of the German Civil Code, the second book of the Civil Code deals with the law of obligations in general.

One difference between rights in rem and obligatory rights is that rights in rem and therefore all interests in land have **absolute effect** as against third parties. This means that these rights are effective with respect to anyone who interferes with a thing in fact, e. g. by depriving the title holder of his possession or trespassing against his possession. In contrast obligatory rights bind only the parties privy to the contractual relation. Since rights in rem have absolute legal effect on all third parties it is material that everybody is able to assess the scope in order to respect such rights. Thus, interests in land should be limited and the contents strictly defined. Another essential rule of the German law of property is therefore the principle of **numerus clausus** which means, that the number, kind and contents of rights in rem have in general to be defined by the legislator. To enable the public to calculate the risk caused by the absolute effect of rights in rem it is also important that these rights are made known to third parties. The disclosure is usually integrated into the act of transferring or establishing a right in rem. With movables, disclosure is required in the actual handing over of the thing; with land it is effected by the entry of the change in legal position into the Land Register. Any change of title in respect of rights in rem therefore requires an agreement and a certain act of disclosure. This is expressed by the so-**called principle of public disclosure**.

The German Civil Code was introduced on the first of January 1900. Since then, the law of real estate, which was strongly influenced by Pandectists' learning of Roman Law, has too a

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[1] cf. Kohler, in: Ebke/Finkin (ed.), Introduction to German Law, 1996, p. 231.

large extent remained unchanged. This is in accordance with the common understanding of real property law as a rather static branch of law. Nevertheless, there have been a number major statutory and judicial reforms within the last century. The provisions dealing with building lease were taken out of the Civil Code by means of the **Regulation on Building Leases in 1919** (*Verordnung über das Erbbaurecht*). The **Condominium Act of 1951** (*Wohnungseigentumsgesetz*) provides for regulations on appartment ownership which have played a major role in case law. The courts have also developed new types of rights in rem by way of judicial legislation such as expectant rights and landcharges serving as collateral. Furthermore, it has to be noticed that for land transactions not only the provisions of the third book of the Civil Code are relevant (the law of real estate in a narrow sense), but also other areas of law such as contract law in general. Especially in the field of obligations there have been major reforms within the last decade, mostly initiated by the EC-directives.

The substantive law of real property is supplemented by procedural regulations on the registration of interests in land in the land register (*Grundbuch*). The relevant provisions are dealt with in a special **Land Registry Act** (*Grundbuchordnung*) which was first introduced in 1897. As opposed to the substantive law the roots of the procedural regulations do not lie in Roman, but in Germanic law. Under the regime of the German Constitution (*Grundgesetz*) and its political and economic policies a number of public law statutes have been enacted, which are also of major revelance to the law of real property, such as the Regional Planning Act of 1997 (*Raumordnungsgesetz* - ROG), the "*Baugesetzbuch*" (BauGB - Town and Country Planning Code) of 1986 or the Federal and Provincial statutes on nature conservation (*Naturschutzgesetze*).

By and large, the real property regulation is uniform for the whole country. There are in particular no special rules for certain groups of the population. Art. 55 of the Introductory Law of the Civil Code (*Einführungsgesetz zum Bürgerlichen Gesetzbuch* - EGBGB) provides that the relevant laws of the countries were to become ineffective with the Introduction of the Civil Code, unless it was otherwise determined by an express statutory regulation. The exceptions still in force concern such branches of law as rights of fishery or dike law. Furthermore, in this context the fundamental changes to the law of real property brought about to the Eastern German Provinces by the German Reunification are to be mentioned. The Civil Code of the former German Democratic Republic of 1975 (*Zivilgesetzbuch* – ZGB-DDR) was governed by communist principles of property distinguishing between socialist ownership pertaining to the means of production and private ownership as to other objects. Instead of indivdual ownership of land special rights of use and a certain type of flat property were recognised. However, by way of the Unification Treaty (*Einigungsvertrag*) these provisions were by and large replaced. There are still a number of temporary regulations in force dealing with complex legal issues of transition.

The existing law of real property is based on the recognition of principles of private ownership giving the right to free and regular use as well as to the exploitation of its inherent economic values. These principles are to be seen against the backround of the German Constitution. They are intimately related to notions such as freedom of person, freedom of contract, liberty of trade and the free choice of occupation. As stated, in the former German Democratic Republic a different concept of planned economy and socialist property had prevailed. The property guarantee of Art. 14 GG is that of a fundamental right, its function is to give the individual a free range within the area of proprietary interests. At the same time the provison emphasizes the responsibility flowing from the ownership, its dependance on statutory provisions and its function to serve public welfare. Surely, even in an open society the exercise of freedom will always be limited by the individual rights of other persons.

The direct impact of European Community Law or the European Convention on Human Rights on the law of property stricto sensu has up to this stage been rather limited. However,

contract law relating to buildings and land has been subject to strong influence inter alia by the Directive 93/13/EEC on unfair contract terms, as well as other EU-legislation, which in Germany ultimately triggered of a fundemantal reform of the traditional law of obligations of the BGB, which came into force at January 1st 2002. It is to be expected that the European concept of property guarantee being based on the constitutional traditions of the member states will gain more influence considering the growing impact of EEC law on the national legal systems.

1.2. Property and Estates

1.2.1. Estate versus Property

German law recognises two concepts of ownership of real property being assigned to several persons at the same time:

- The first is the concept of **coownership** (*Miteigentum*, §§ 1008-1011 BGB) where the persons each own an ideal fraction of the common property. The fractions, however, are all related to the property as a whole. The characteristic feature of coownership is that every coowner is entitled to dispose of his fraction in the property without the assent of the others.
- In case of **joint ownership** (*Gesamthandseigentum*), in contrast, the property is assigned to two or more persons in such way that they can only dispose of the property together. There are only three forms of joint ownership recognised: the property of a civil law partnership (§§ 718, 719 BGB), joint marital property under a regime of community of property between spouses (§§ 1408, 1415 BGB) and joint ownership of an estate of coheirs (§ 2023 BGB). It is impossible to create further forms of joint ownership by way of contractual stipulation.

The two different forms of ownership of several persons can also be relevant to other interests in land.

The term feudalism describes the social characteristics of a historical period in the past. It is of no relevance to modern law of property in Germany.

1.2.2. Superficies solo cedit

In general, the ownership of a piece of land comprises also the ownership of buildings erected on that land. According to **§ 94 BGB** things which are firmly attached to the land and soil, such as buildings in particular, are regarded as essential component parts of that piece of land. In addition, items which are inserted, for a structural purpose, into a building form essential component parts of the building. As a consequence the ownership of the land extends to all movable things so joined to the land that they become essential components (§ 946 BGB).

There are, however, some exceptions to the rule.

- If the things are attached to the soil for a **temporary purpose** only, they do not become constituent parts of the land (§ 95 I 1 BGB). An example would be the case of a tenant erecting a garden house or a leaseholder who sets up stands for the organisation of fairs. The same applies to a building or other construction which, in the exercise of a right over another's land, have been attached to the piece of land by the person who has that right (§ 95 I 2 BGB). On the basis of this provision the owner of a building lease may acquire the ownership of the building constructed in the exercise of that right. Likewise, the owner of an easement appurtenant may, for example, acquire separate ownership of an under ground car park. It seems obvious that this exception may gain considerable importance for property dealings in Cities such as Munich or Hamburg.
- A further instance of isolated ownership of at least a part of a building is the case of an

encroachment upon adjoining land according to § 912 BGB. If the owner of a piece of land, in constructing a building, has built over the boundary line, with not intent or gross negligence attributable to him or even with the consent of the neighbour, he will become owner of the whole building. It is difficult to indicate the approximate percentage of isolated ownership of buildings without the land. To our knowledge there are no official statistics. Irrespective of the practial importance, the percentage would probably amount to less than 5 %.

– In this context, however, the **apartment ownership** may also be mentioned, which is characterized by the coownership of the land of several persons combined with individual ownership of an appartment or a commercial unit. There are an estimated 4 Million flat property units, which amounts to 11 % of all appartments and to 19 % of the owned resedential property. In the old West German states, however, most of the flat property is hired out to tenants.

1.3. Interests in Land

1.3.1. Numerus clausus

The principle of **numerus clausus** of interests in land is one of the essential rules of the German law of property. In contrast to claims arising from individual contracts or other obligations rights in rem have absolute legal effect on all third parties. If third parties are to respect such rights, it is material that they are able to assess their scope. Thus, interests in land should be limited and their contents strictly defined. At the same time the degree of negotiability is increased. Therefore, the freedom of contract is limited in the field of real property law. The parties may decide, if they want to create a land charge or a servitude and they may even determine its contents to the extent, that is admitted by the law. They may, however, not create new types of rights in rem. Certainly, the legislator can introduce further forms of interests in land, if practical needs should arise. In the past, the courts have also developed a limited number of real property concepts, such as expectant rights or trust property, which is binding only to the parties privy to the contractual relation, but may under certain circumstances offer a defence against third parties. The principle of numerus clausus does not necessarily exclude the recognition of different rights in rem from other member states of the European Union. However, since real property law is governed by the lex rei sitae, the question has been of little practical relevance.

1.3.2. System of Interests in Land and Numerus Clausus

The German law of real property distinguishes between three types of interests and land:

- Rights to use (easement) (*Nutzungsrechte*),
- security of interests (*Verwertungsrechte*) and
- preemption rights (*Vorkaufsrechte*).

1.3.3. Servitudes (usus)

There are several types of rights to use.

- The building lease (***Erbbaurecht***) grants the transferable and inheritable right to have a structure above or below the surface of the piece of land (§ 1 *Verordnung über das Erbbaurecht*, ErbbauVO). The relevant provisions are now to be found in the Regulation on Building Leases and are dealt with later.
- The owner of an usufruct has the extensive right to use the property (***Nießbrauch***, §§ 1068 sqq. BGB). This also extends to the earning of profits as in the case of rental fees. In contrast to other rights in property it is not limited to land, but may also refer to movables and

rights.

- The concept of servitudes is that the owner of land has to tolerate or ommit certain acts. The servitudes are dinstinguished according to the person who is entitled to use the land: There are easements in appurtenance, i.e. to the benefit of the owner or possessor of other, especially neighbouring land (***Grunddienstbarkeit***, §§ 1018 sqq. BGB). In this sense, one may speak of a dominant tenement (*herrschendes Grundstück*) and a servient tenement (*dienendes Grundstück*). There are easements in gross, i.e. to the personal benefit of another person (***beschränkte persönliche Dienstbarkeiten***, §§ 1091 sqq. BGB). A special form is the right to use a building or a special part of building as a residence (§ 1093).
- The servient tenement may be encumbered by servitudes in three different ways: The owner may be entitled to use the piece of land in specific respects (1), certain acts of the owner may not be allowed on the servient tenement (2) or the exercise of a right, which arises out of the servient tenement, may be excluded (3). Common examples woud be a right of way, a sanitary sewer easement, or a parking space easement.

1.3.4. Mortgages and Rent Charges

There are three different types of security interests in land.

– According to the concept of the Civil Code the main type is the **mortgage** (*Hypothek*, §§ 1113-1190 BGB), which is an accessory right, whose legal existence depends on the existence of the debt to be secured. The fathers of the Civil Code had in mind the credit transactions at the end of the 19th Century, where private credits were more common. However, nowadays a system of bank credits prevails with a stronger need of negotiable instruments.

– In practice, therefore, the **land charge** which is abstract from the underlying debt and may also be transferred independently (*Grundschuld*, §§ 1191-1198 BGB), has turned out to be more important.

– The third type of security interest is the **annuity charge** (*Rentenschuld*, §§ 1191-1198), where the owner has to make regular payments and may choose to pay a lump sum instead. The Rentenschuld is hardly ever used. In this context, the realty charge (Reallast, §§ 1105-1112) may also be mentioned. Under a reality charge recurring performances are to be rendered from the land to the person in whose favour the encumbrance runs. It is still common as a security interest amongst private parties, such as relatives, to secure current payments, as in the case of a stipulated life annuity.

1.3.5. Rights in Rem to Acquire Real Property

As right in rem to acquire real property German law recognises a right of **preemption** (*dingliches Vorkaufsrecht*, §§ 1094-1104). The person, in whose favour the encumbrance is created has the right of preemption as against the owner. This right may be granted to an individual person or in favour of another dominant tenement. The right of preemption is normally restricted to the first case of sale by the present owner, but may also be granted for several instances of sale.

The **priority notice** to protect a claim to a registrable right in landed property (*Vormerkung*, §§ 883-888) may have the same effect as a preemptive right, but is not restricted to contracts of sale and therefore more flexible.

1.4. Apartment Ownership (Condominiums)

There is a separate statutory regulation on appartment ownership in German law, which was introduced in **1951**. The relevant provisions are still to be found within the **Condominium Act** (*Wohnungseigentumsgesetz*), a separate Code outside the BGB. The appartment owner-

ship according to German Law consists of a co-owner's share in landed property combined with an individual flat property, which may also be a commercial unit (Teileigentum). The Condonminium Act provides for a set of rules to organize the relations between the several coowners and to settle potential conflicts.

– In this respect, it is also a reaction to the former "*Stockwerkseigentum*", which was common before 1900. The Civil Code does not allow the creation of new Stockwerkseigentum, which in the absence of clear rules was prone to conflicts between the owners.

– In the provinces of the former German Democratic Republic a further type of appartment ownership still exists, which is known as "*Gebäudeeigentum*".

From the common ownership flow certain duties that may put limits to the use of the property. The coowners are also free to set up rules governing their relations. Only a few provisions in the Condominium Act are mandatory law restricting the freedom of contract. The condominium bye-laws created by a contract of all apartment owners may even be applicable to future owners provided that they have been registered within the Land Register so that successors can find out about their contents (§ 10 II WEG). In some instances expressly stated in the Condominium Act a majority rule of the coowners' meeting may even be sufficient. The same applies, if the condominium by-laws provide for a simple majority rule. Where a majority vote is permitted, it is applicable to future owners without registration in the Land Register.

The appartment ownership is established by the so called partition plan (*Teilungserklärung*), which must be registered in the Land Register. The partition plan usually determines the general function of the appartment house which may be only a residence house or also serve as commercial building. It is thus for the coowners to decide, if a certain unit may also be used as a restaurant. The condominium bye-laws may also provide a regulation as to the distribution of the shared costs as, e. g., a per capita distribution, a distribution per square meters, in deviation from the distribution according to the percentage of the coownership share (§ 16 II WEG). Furthermore, the apartment owners may also forbid dogs in the apartments. However, the Bavarian Supreme Court (*Bayerisches Oberstes Landesgericht* – BayObLG) has ruled that such a general prohibition may in certain circumstances be inapplicable, as e. g., in the case of a guide dog[2]. Furthermore, some writers argue that a geneneral prohibition of pets in the appartments would contravene the principles of good faith, as the other appartment owners would not be affected by, e. g., an ornamental fish[3].

The apartment ownership right can be mortgaged by its holder without the consent of the other owners. At the same time the whole land may also be encumbered with the assent of all appartment owners. This applies in particular to servitudes granting the right to use the land as a whole in certain respects (e. g., an easement of access), but also to land charges and other interests in land. In case of destruction of the whole building, the apartment ownership right and correspondingly the interests on it continue to exist. The majority of the coowners may resolve on the reconstruction of the building, unless more than half of it has been destroyed and the damage is not covered by insurance; in this exceptional situation a single appartment owner may even demand the dissolution of the community.

1.5. Building Lease (emphytéose – bail à construction/ Erbbaurecht)

The provisions dealing with building lease used to be part of the Civil Code, but have been integrated into a separate Code, the Regulation on Building Leases (*Verordnung über das Erbbaurecht*). The building lease is defined in § 1 ErbbauVO as an encumbrance upon land

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2 BayObLGZ 2001, 306 = FGPrax 2002, 15 = NJW-RR 2002, 226 = NZM 2002, 26 = ZMR 2002, 287.

3 ERMAN/GRZIWOTZ, BGB, 11. edition 2004, § 10 WEG note 9.

consisting of the transferable and hereditary right to have a building on (or below the surface of) another person's land. The person entitled to the building lease acquires the ownership of the respective building. As stated, this is a further deviation from the principle that the ownership of land extends to all essential component parts of it. The building lease is as a rule established for a limited period of time. In theory, however, there is neither a minimum, nor a maximum period perscribed by the law. The building lease is an independent right in rem, which is treated by law as if it was land, and may therefore also be encumbered separately with a land charge or other interests in land. The economic benefit of the building lease is that the title of the property in respect of the building may be acquired without the necessity to raise capital for the land. On the part of the landowner it produces constant flow of income from the land (though it may also be granted gratuitously).

1.6. The Public Law Context of Real Property Transactions

There are only a view public law restrictions on real property transactions in German law. Most of the relevant instances are regulated in the "*Baugesetzbuch*" (BauGB) (Town and Country Planning Code). They concern areas where specific town planning measures such as the reapportionment of the plots of lands or an urban renewal are to be implemented. These restricitions are usually entered into the Land Register and therefore evident for the parties involved. A further important example is the conveyance of agricultural or forest land, which may also require a public permit. Moreover, certain corporations or public bodies such as investment companies or local municipalities may also need an admission by a senior authority in order to dispose of land.

Currently, there are still subsidies benefiting the buidling or purchase of family homes (***Eigenheimzulage***, regulated in the *Eigenheimzulagegesetz*). The repeated attempts by the government to abolish these regulations have again failed recently due to the veto of the Federal Council.

1.7. Brief Summary on "Real Property Law in Action"

During the last years there has been a process of relaxation on the property market. Especially in the Eastern parts of Germany the general decrease of population has left ist traces. In general, there is excess offer, in large Cities especially commercial buildings remain unoccupied. Therefore, selling and renting houses has become less attractive. The market is also characterized by strong regional divergences. According to recent estimations the share of tenants as opposed to property owners amounts to 43 %. As the following table shows, in this respect there are also local differences[4]:

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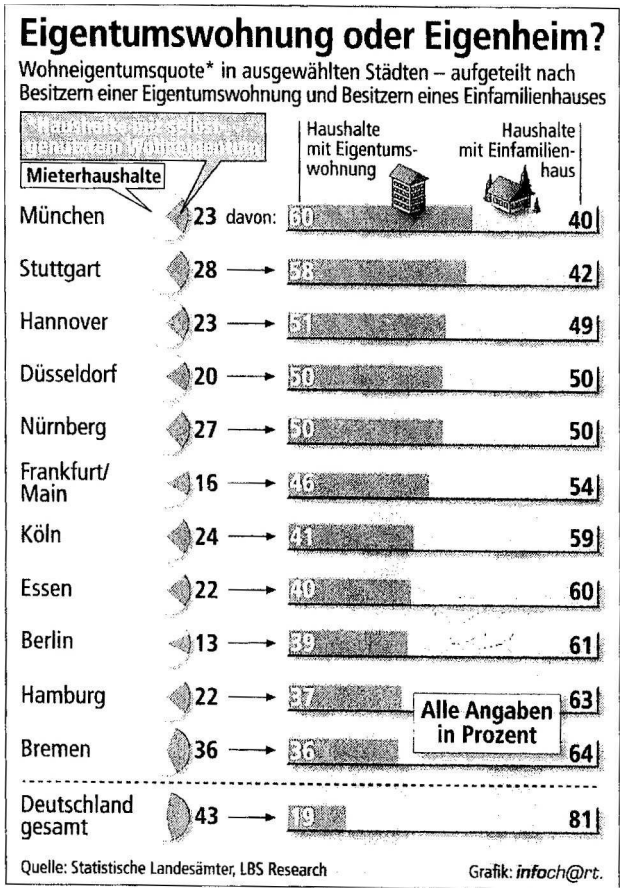
4 cf. DWW 2004, 211.



The economic importance of mortgages is largely limited to property transactions. As opposed to other countries mortgages are in general not used as security for consumer credits. Sometimes mortgages are employed for credits in order to finance the formation of enterprises.

As a contract of sale is subject to a notarial act and the conveyance of land requires entry in the land register, Notaries as well as registrars play an important role in property transactions. The Notaries are subject to statutory procedural rules, laid down in the *Beurkundungsgesetz* (Notarial Procedural Law) and the *Bundesnotarordnung* (Federal Notary Law). Since the profession of the Notary is regarded as a public office, these regulations provide for strict independence and objectivity. According to § 17 it is the duty of the Notary to ascertain the real intentions of the parties, provide impartially for the necessary **legal advice** to both sides and point out the consequences and potential risks of the transaction. In practice, the Notary not only drafts the necessary documents and certifies them, but also assists in the implementation. The notary is also **personally liable** for mistakes in the exercise of his duties. The decisions of the registrar are subject to judicial control. Many property transactions are in pracitce negotiated by the assistance of estate agents. Sometimes also mortgage or other banks act as brokers.

Real property law is sometimes also enforced by the courts. However, most cases deal with matters of registration and concern the question, if a certain legal arrangement is admissible. However, there seem to be rather few decisions dealing with disputes arising from the implementation of contracts as between the parties. Neither voluntary nor compulsory mechanisms of alternative dispute resolution are common in the field of property law. Fair and effective access to court exists to full extent. The Code of Civil Procedure also provides for a system of legal aid. There is no special jurisdiction for real property, the ordinary courts are competent. Against the decision of the registrar or a trial court an appeal and also a further appeal limited to questions of law is allowed. Real property law is a field of law where legal certainty pre-

vails, there are, in particular, no significant gaps in the law or contradicting statutes. There is also sufficient secondary literature, which is accessible to all lawyers.

2. Land Registration

2.1. Organisation

2.1.1. Statutory basis

In Germany, land registration is regulated in the *Grundbuchordnung* (Regulation on the land register).[5]

There is only one system for the whole of Germany.

2.1.2. Relevant institutions

In Germany, there are two relevant institutions for registering real estate:

- In the ***Liegenschaftskataster*** (cadaster), one may find a technical survey of the land.
- In the ***Grundbuch*** (land register), ownership and other legal rights in plots of land registered. However, the *Grundbuch* refers to the cadaster for the position, borders and size of the cadastral parcel that make up a plot of land in the *Grundbuch*.
- The **notary** plays an indispensable role in drafting most of the applications for registration.

2.1.3. Land register/registre foncier/Grundbuch

In Germany, the land register (*Grundbuch*) is a **part of the court system** in non-contentious matters (*Freiwillige Gerichtsbarkeit*), not an administrative authority. The register is administrated by the *first instance court* (*Amtsgericht*) (§ 1 GBO – *Grundbuchordnung* = land register regulation)[6].

The registration is made by **registrars** (*Rechtspfleger* - RpflG). The registrars do not have a general law degree (*Befähigung zum Richteramt* - § 5 DRiG), but they have passed a special three years legal training enabling them to work at the register (which also encompasses the company register and some matters concerning execution and succession). The registration procedure is supervised by judges.

Recently, there have been legislative proposals (by the state of Hessen) enabling also the employees of the cadastre to work for the land register. These proposals have been motivated exclusively by financial intentions, because in Hessen the cadastres have too many employees, whereas the registrars might be used for other tasks.

2.1.4. Is all real property registered?

In Germany, all real property has to be registered in the land register (Grundbuch) (§ 3 I GBO). The only exception applies to property owned by the state, by local authorities and churches, rivers and railways: These properties are registered on the application of the owner only (§ 3 II GBO). In practice, however, most of these properties have also been registered. All in all, in practice, more than 95% of the land is registered.

2.2 Contents of Registration

2.2.1. Which data are registered?

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5 The *Grundbuchordnung* (Land register law) may be found on the internet, edited and updated by the German ministry of Justice: http://bundesrecht.juris.de/bundesrecht/gbo/index.html

6 The *Grundbuchordnung* (Land register law) may be found on the internet, edited and updated by the German ministry of Justice: http://bundesrecht.juris.de/bundesrecht/gbo/index.html

According to the Grundbuchverfügung (GBV - *regulation on the land register*)[7], the German land register consists of 4 sections:

– *Bestandsverzeichnis* (referal to the cadaster) (§ 6 GBV): This section contains a referal to the cadastral number and some cadastral information (such as how the real estate is being used).

– *Abteilung* I (section I) (§ 9 GBV): registration of the owner and of a transfer of property.

– *Abteilung* II (section II) (§ 10 GBV): registration of encumbrances other than real security rights.

– *Abteilung* III (section I) (§ 11 GBV): real security rights: mortgage, land charge, rent charge.

2.2.2. Sample of Registration

An official sample registration has been published as **annex of the regulation on the land register** (*Grundbuchverfügung*). It is enclosed in a separate file (pdf) to this report.

2.3 Registration Procedure

2.3.1. Application for Registration

The demand for registration does not require any particular form. However, the necessary consent of the owner of the property or of the real right concerned requires a **certification of signature** (§ 29 GBO). The transfer of ownership requires even further a notarial deed (§ 20 GBO).

As a consequence, in practice almost all applications to the land register are drafted by a notary. Thus, there is **dual control** before any right is registered: First, the notary checks the legal requirements (and drafts the document). Second, the registrar checks the legal requirements.

2.3.2. Duties of the Registrar

The registrar applies only a **formal control**:

– First, the registrar checks, whether there is a proper **demand** (*Antrag*, § 13 GBO).

– Second, **consent** (*Bewilligung*) of the owner the registered right is required (§ 19 GBO). The registrar does not check, whether the registration is valid, but only if there is the necessary consent. The consent must be declared in a public instrument (*öffentliche Urkunde*), e.g. in a document with certification of signature (§ 29 GBO).

– The owner of the right concerned has to be registered first before any changes or the transfer can be registered (*Voreintragung*, § 39 GBO).

The registrar has to inform the applicant and the party concerned about any registration made (§ 55 GBO). If the demand or the consent have been presented by a notary, the notary will also be informed. (In the latter case, the land register used to inform the parties concerned as well as the notary. Now, in order to save money, the land register informs only the notary; the notary in change informs the parties.)

2.4 Access to information

Traditionally, registration was done on paper. Since the mid 1990's, the land registers started electronic registration. Each state decided by itself on the new electronic system. As a conse-

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7 BGBl. 1995 I, 114.

quence, there a two systems now: Most states apply a program called SOLUM-star; one state however applies a different system.

Some states (such as Bavaria) have already changed completely to the electronic systems. Other states are just halfway through[8].

At present, the main problems of the electronic systems are:

– The system is **expensive** (about 10 Euro per request for information on a parcel) plus fixed costs of about 100 Euro per month. In particular, many attorney notaries do not use it due to the high fix costs (because they do not need it so often).

– You need to register for **each state separately**. So, as a notary in Bavaria, you normally are registered for the Bavarian system. However, to get any data from a parcel situated in a neighbouring (German) state, you will still have to rely on a colleague – or ask the land register for a printed version.

In particular: Can you get access to the register :

– if you have a *ius in rem* in the real property, Yes[9]

– if you are negotiating with the owner about the purchase of the property – Yes – but not, you just want to find out who owns a property in order to make him an offer for purchasing or renting the property,[10]

– if you have an enforceable title against a debtor and are inquiring about the existence of real property to be seized in an execution procedure, Yes[11]

– if a bank wants to check whether an applicant for a loan owns real property, Yes[12]

– if the press wants to inquire on how much real property a politician owns.- No, however the Constitutional Court[13] has recognized that also a legitimate public interest expressed by the press might constitute a legitimate interest in the sense of § 12 GBO (a position completely new to the system of the German land register).

You can search for information by the registration (or cadastral) number of the land and by the owner.

2.5 Substantive Effects of the Registration

In Germany, registration in the land register has the following effects:

– Registration is necessary for the creation or the transfer of the right (**constitutive effect**) (§ 873 BGB).

– Registration gives rise to an **assumption** (*Vermutung*) that the rights registered exist and belong to the person stated in the register (and assumption that a right that has been cancelled, no longer exists) (§ 891 BGB) and to

– **protection of good faith** (*Gutglaubensschutz*) of anybody who acquires a right contractually from the person registered in the land register (§ 982 BGB).

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8 GÖTTLINGER, *Notariat und Grundbuchamt im elektronischen Zeitalter*, DNotZ 2002, 743.

9 DEMHARTER, § 12 GBO note 8.

10 BayObLG Rpfleger 1984, 351; OLG Hamm Rpfleger 1986, 128.

11 OL G Zweibrücken NJW 1989, 531.

12 KGJ 20, 173; BayObLG Rpfleger 1975, 361.

13 BVerfG Rpfleger 2001, 15 = FGPrax 2001, 53 note Demharter; OLG Hamm Rpfleger 1988, 473; OLG Düsseldorf Rpfleger 1992, 18.

2.6 Rank and Priority Notice

2.6.1. Rank (rang/Rang)

article 879 Rank among different rights

(1) The rank among different rights encumbering the same real estate is determined by the order of inscription, if the rights are registered in the same section of the real estate. If the rights are registered in different sections of the land register, the right registered under the earlier date enjoys priority; rights registered under the same date have equal rank.

(2) The rank is determined by the registration, even if the consent necessary for the creation of the right according to article 873 followed only after the registration.

(3) Any agreement on a different ranking is valid only if registered in the land register.

§ 879 Rangverhältnis mehrerer Rechte

(1) Das Rangverhältnis unter mehreren Rechten, mit denen ein Grundstück belastet ist, bestimmt sich, wenn die Rechte in derselben Abteilung des Grundbuchs eingetragen sind, nach der Reihenfolge der Eintragungen. Sind die Rechte in verschiedenen Abteilungen eingetragen, so hat das unter Angabe eines früheren Tages eingetragene Recht den Vorrang; Rechte, die unter Angabe desselben Tages eingetragen sind, haben gleichen Rang.

(2) Die Eintragung ist für das Rangverhältnis auch dann maßgebend, wenn die nach § 873 zum Erwerb des Rechts erforderliche Einigung erst nach der Eintragung zustande gekommen ist.

(3) Eine abweichende Bestimmung des Rangverhältnisses bedarf der Eintragung in das Grundbuch.

Case: Owner grants first a mortgage to A, afterwards another mortgage to B. After that, creditor C has a third mortgage registered on the same property in an execution procedure. The time of registration is as follows: First B, then C, then A. What is the respective rank of the mortgages?

Answer for Germany: According to the time of registration, B ranks first, then C, then A – irrespective of the time, the mortgages were granted. However, the parties may agree on another ranking – which also has to be registered.

2.6.2. Priority Notice

In Germany, a priority notice (*Vormerkung* - § 883 BGB) may be registered to secure a claim for the establishment or the transfer of the property or any real right in real estate[14].

– The registration requires only the consent (*Bewilligung*) of the owner of the right concerned.

– The priority notice is valid only, if the secured claim really exists.

– The priority notice does not block other registrations. However, any registration violating the secured claim is invalid – but only relatively to the creditor of the secured claim (§

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14 § 883 BGB - Voraussetzungen und Wirkung der Vormerkung
(1) Zur Sicherung des Anspruchs auf Einräumung oder Aufhebung eines Rechts an einem Grundstück oder an einem das Grundstück belastenden Recht oder auf Änderung des Inhalts oder des Ranges eines solchen Rechts kann eine Vormerkung in das Grundbuch eingetragen werden. Die Eintragung einer Vormerkung ist auch zur Sicherung eines künftigen oder eines bedingten Anspruchs zulässig.
(2) Eine Verfügung, die nach der Eintragung der Vormerkung über das Grundstück oder das Recht getroffen wird, ist insoweit unwirksam, als sie den Anspruch vereiteln oder beeinträchtigen würde. Dies gilt auch, wenn die Verfügung im Wege der Zwangsvollstreckung oder der Arrestvollziehung oder durch den Insolvenzverwalter erfolgt.
(3) Der Rang des Rechts, auf dessen Einräumung der Anspruch gerichtet ist, bestimmt sich nach der Eintragung der Vormerkung.

883 par. 2 BGB).

– There is no temporal limitation for the *Vormerkung*. However if the statute of limitations has run for the claim secured (and is objected by the debtor of the claim), the priority notice is rendered useless.

If only the rank shall be secured, a reservation of rank is also possible (*Rangvorbehalt* - § 881 BGB).

3. Sale of Real Estate among Private Persons (consumers)

3.1. Procedure in general

3.1.1. Main steps of a real estate sale

– In Germany, often the seller uses the services of a real estate agent in order to find a buyer.

– When the seller has found a buyer, the parties ask a notary to draft the contract. The **sales contract** is concluded in an oral hearing at the notary's office in the presence of both parties and laid down in a notarial document.

– Afterwards, the notary applies for registration of a **priority notice** (*Vormerkung*) in the land register (*Grundbuch*).

– Now, the buyer **pays** the purchase price to the seller.

– After payment, the seller allows the buyer into possession and the notary has the transfer of ownership **registered** in the land register (*Grundbuch*). The registration entails the transfer of the property.

3.1.2. Time frame

The time necessary varies according to the time needed by the land register (*Grundbuchamt*).

– On average, the **priority notice** (*Vormerkung*) is registered **within several days**. Normally, the notary or the parties receive the information about the registration of the priority notice about two weeks after the demand.

– The registration of the **transfer** (Auflassung) itself might take longer, up to **some weeks** (or at least it will take some time for the register to inform the notary or the parties. (That is because the registration of the transfer is not considered a priority by the registrars. After the priority notice has been registered, there is no risk for the buyer.)

– However, some land registers have a serious backlog. There, even the priority notice might take some months, the registration of transfer half a year or even a year, in some cases even longer. In the 1990'ies, the situation used to be very bad in the east. Now, it is only a few registers that have such a backlog (some also in the western states).

3.2. Real Estate Sales Contract

3.2.1. Form

In Germany, the real estate sales contract (that is the **obligation contract)** has to be concluded by **notarial instrument**; otherwise it is **invalid** (§ 311b BGB).

– If the sales contract is formally invalid, the formal defect is cured, if the transfer of property has been declared and has been registered (§ 311b BGB). However, the registration does not cure any material defects of the sales contract.

Also the **transfer of property** (*Auflassung*) has to be declared to a notary (§ 925 BGB).

– The declaration of transfer requires a German notary[15].

– The transfer has to be declared with both parties (or their representatives) present at the same time (§ 925 BGB). Offer and acceptance must not be notarized separately.

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– A notarial instrument on the transfer is required for registration (§ 20 GBO). However, the transfer is valid, even if the notarial instrument has not been validly notarized, provided that the transfer at least was declared at a notary (§ 925 BGB).

E.g. if one of the parties forgets to sign the instrument, the notarial instrument is invalid. Thus, the registrar has to deny the registration. However, if the registrar does not notice the defect, property will be transfered with the registration, since the declaration of transfer (Auflassung) was made at a notary.

3.2.2. Who drafts the contract for a real estate sale normally?

Almost all real estates sales are not only authenticated by the **notary**, but also drafted by the notary.

3.2.3. Preliminary contract

There is **no preliminary contract**. Also a preliminary contract would require notarization, if it gives rise to a duty to dispose of or to acquire real property; otherwise the preliminary contract is invalid.

3.2.4. Typical Real Estate Sales Contract

In Germany, there is no official form of a real estate contract.

Model contracts have been published by several authors, in particular in some notarial manuals:

– *Beck'sches Notar-Handbuch*, edited by BRAMBRING/JERSCHKE, 3. edit. 2001, note A I 216, 247;

– *Beck'sches Formularbuch zum Bürgerlichen, Handels- und Wirtschaftsrecht*, 8. Aufl. 2003, forms III. B. 1 and 3, pages 191, 213;

– KERSTEN/BÜHLING, *Formularbuch und Praxis der Freiwilligen Gerichtsbarkeit*, 21. Aufl. 2001, § 36;

– LAMBERT-LANG/TROPF/FRENZ, *Handbuch der Grundstückspraxis*, 2000, part 2, forms 1 (page 280-283);

– *Münchener Vertragshandbuch*, volume 5 (concerining real estate, among other), 5. edit. 2003, forms I. 1 and 3, pages 1 and 79;

– SCHÖNER/STÖBER, *Grundbuchrecht*, 13. Aufl. 2004, note 849.

As an **annex** to this report, please find a sample contract, drafted by me for a forthcoming notarial manual.

3.3. Transfer of Ownership and Payment

3.3.1. Requirements for Transfer of Ownership

What are the requirements for the transfer of ownership?

– valid obligation contract (causa), - no

– payment of the purchase price, - no

– consent on the transfer of ownership (*Auflassung*), - yes

– registration with the land register (*Eintragung*). – yes

In the German system, transfer of ownerhsip requires only a declaration of **consent** (*Auflassung*) and the **registration** with the land register (*Eintragung*) (§§ 873, 925 BGB).

– The German system of transfer of ownership is an „**abstract**“ system: The transfer of ownership is valid irrespective of the validity of the sales contract.

– However, if the sales contract was invalid, the seller may reclaim the property on grounds of unjust enrichment (*ungerechtfertigte Bereicherung*) (§§ 812 ss. BGB).

3.3.2. Payment due

Under the German system, property is transfered with registration. It is impossible to make the transfer contingent on the payment of the purchase price (§ 925 BGB). Thus, the transfer of property is split up in two steps:

– First, the **priority notice** (*Vormerkung*) is registered. Now, buyer is secured that nobody else can acquire property validly against him.

– Thus, buyer now may **pay** the purchase price to the seller without running any risk.

– After payment, the seller allows the buyer into possession and the notary has the transfer of ownership **registered** in the land register (*Grundbuch*). The registration entails the transfer of the property. (Normally the declaration of the transfer of property is already contained in the same document as the sales contract. However the parties advise the notary not to have the transfer registered until after the seller confirmed to the notary that he has received the purchase price in full).

The deposit of the purchase price on an escrow account (in particular a notarial escrow account, *Notaranderkonto*) can be another method to synchronize the payment and the transfer of the property. However, normally the synchronization works perfectly well also with direct payment.

– An escrow account is necessary to secure the seller, if the parties agree to transfer possession before payment is due.

In Germany, no insurance is used for the risks of the payment.

3.3.3. Ways of the seller to enforce the payment

In Germany, a notarial instrument is enforceable only if the debtor explicitly declares submission to direct enforcement in the contract (*Zwangsvollstreckungsunterwerfung,* § 794 I n° 5 ZPO). In almost all contracts on the sale of real estate (= more than 90%), such submission is declared by the buyer.

3.3.4. Transfer of possession to the buyer

Often, also the seller declares submission to direct enforceability concerning his duty to vacate the premises and to transfer possession to the buyer. This possibility has been included by a change in the law in 1999. Therefore, it has not yet become universal practice.

3.4 Seller's Title

3.4.1. Title Search: Ascertaining the seller's title

The notary has to check only the land register (*Grundbuch*). It is a legal duty of the notary to check (§ 21 BeurkG).

The buyer acquires the property *bone fide* and free of encumbrances not registered, even if the register is incorrect (provided only the buyer did not know that the registration is incorrect).

3.4.2. Title Search: Absence of Encumbrances

It it the duty of the notary to inform the buyer of all existing encumbrances of the real estate which are registered in the land register. The search is limited to the land register.

Second, in the contract, payment is made dependent on the deletion of existing encumbrances.

– If the creditor is a bank, the bank normally sends alls documents necessary for cancelling the mortgage from the register to the notary and advises the notary to make use of these documents only, if the bank receives a certain amount of money (that is the bank's claim still secured by the mortgage).
– The notary makes sure, that the claims of all banks can be paid from the purchase price. Then the notary informs the buyer of the bank's claim. Buyer pays directly to the bank. In the sales contract, seller has agreed that these payments may be deducted from the purchase price. Thus, seller receives only the rest of the purchase price – in some cases nothing.
– Afterwards, the bank tells the notary, that it has received the money and that now he may use the documents to cancel the bank's mortgage.
– This system does not work, if the creditor is a private person whom the buyer does not trust. Then an escrow account is being used, so that the notary can make sure the mortgage can be cancelled before he effects payment from the escrow account.

3.4.3. Title Insurance or Liability

There is no title insurance in Germany.

However, if the notary has not checked the land register properly, he is liable to the parties. Since malpractice insurance is mandatory for German notaries (up to 1 million Euro), the buyer is protected (unless the value of the property is higher than the insurance).

3.4.4. Leases

If a tenant occupies the premises before seller transfers possession to buyer, then the buyer is also bound to the lease (§ 566 BGB – *Kauf bricht nicht Miete*). Thus, if the tenant has to vacte the prat the time when the sales contract is concluded, the tenant still occupies

The tenant has a **statutory pre-emption right** only for **condominiums**, if the tenant had rented before it was split up in apartments (*Mietervorkaufsrecht* - § 577 BGB). Seller is under legal duty to inform the tenant about the terms of the sale once the sales contract has been concluded. Then the tenant has got two months to exercise his right of pre-emption. The tenant cannot waive his right of preemption before the sales contract has been concluded. Afterwards he may wave his right.

3.5 Defects and Warranties

3.5.1. Legal rules

Concerning defects of title or material defects, the buyer has the following legal rights against the seller (§ 437 BGB):

– specific performance,
– reduction of payment,
– rescission of the contract,
– damages (if the seller is responsible for the defect).

The notary is liable (§ 19 BNotO),

– if he did not warn the buyer concerning defects of title,
– or if did the draft contract did not include usual precautions to minimize the risks,
– provided that the buyer cannot claim his damages from the seller (or other parties).

3.5.2. Typical contractual clauses: the scope of *caveat emptor*

Typically, in a real estate sale among private persons, all warranties by seller are contractualy excluded. That is perfectly valid in a contract among two consumers (unlike if the seller acts in the course of his trade, business or profession).

Courts exercise control over the fairness of such clauses

– if it is a consumer contract (i.e. with an enterprise on the other side),

– or – even in a contract between two consumers – if a recently constructed house is being sold[16].

3.5.3. Liability of the Buyer for Debts of the Seller

Is the buyer liable for arrears of the seller, regarding in particular

– real estate taxes – there is a risk for fees for the development of land *(Erschließungsbeiträge* - § 127 BauGB).

– other taxes, e.g. related to buildings on the property or the business of the seller conducted on the property – No (unless the business itself is sold, § 75 AO)

– charges for garbage collection, water and gas delivery, - No

– charges for the administration of condominium apartments – no statutory liability; however liability can be regulated in the coowners' regulation (*Gemeinschaftsordnung*)[17].

How are these problems treated in typical contractual clauses? - Therefor, in the sales contract, the seller assures that he paid all fees for the development of land (or in the case of an apartement, all adminstration fees). The buyer is advised by the notary that he can check that claim with the local municipality (or with the apartment building's administrator) (before concluding the contract).

3.6 Administrative Permits and Restrictions

3.6.1. Standard Requirements

For a standard real estate sale the notary would have to check the following permits or pre-emption rights:

– For the sale of a parcel of land, the **municipality** (*Gemeinde*) might have a **right of pre-emption** (*Vorkaufsrecht der Gemeinde*, §§ 24 ss. BauGB). This right of pre-emption does not apply to the sale of apartments. For parcels of land however, the transfer cannot be registered unless the municipality certified that there is no right of pre-emption or that the municipallity does not exercise its right. However, the right is rarely used (less than 0,5% of all sales).

– For **apartments**, the coowners in their regulation (*Gemeinschaftsordnung*) may require the consent of the apartment adminstrator (*Verwalter*) or of the other coowners for every transfer of ownership. Then the sales contract and the transfer of ownership are valid only with this consent (§ 12 WEG). Therefor, the notary will check whether any consent is required in the coowners' regulation. (The regulation has to be registered in the land register.)

– Also for **apartments**, the **tenant** has a statutory **right of preemption**, if the subdivision

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16 This is a special jurisdiction by the VII. chamber of the German Supreme Court (BGH), not applied by other chambers.

17 BGHZ 99, 358; BayObLG Rpfleger 1979, 352; OLG Frankfurt OLGZ 1980, 420.

into apartments was made after the tenant had moved in (§ 577 BGB) (see above 3.4.4.).

3.6.2. Requirements for certain types of real estate sales only

In Germany, the following additional administrative permits might be applicable:

– In the estern states (***neue Länder***) the real estate sale is valid only if it has got a permit according to § 2 GVO.

– The sale of **agricultural or forest land** requires a permit according to § 9 GrdStVG (*Grundstücksverkehrsgesetz* – Law on the Sale of (Agricultural) Land). Also, preemption rights according to the laws on natural preservation or to the forest laws (which are regulated by the German states, *Länder*) might apply.

3.6.3. Control of administrative permits and restrictions

§ 18 BeurkG (Notarial Procedure Law) reads as follows: "The notary has to point out to the parties, if there are any judicial or administrative permits required or if they might be required; also he should take a note in the notarial instrument."[18]

3.7 Transfer Costs

3.7.1. Contract and Registration

The costs for the sale of a property for 100.000 Euros are:

– notary fees approximately 600 Euro (+ 16% VAT)

– registration in the land register 362 Euro (priority notice and its cancellation; transfer of property).

If the purchase price is 300.000 Euros, the approximate costs are:

– notary fees approximately:1.500 Euro (+ 16% VAT)

– registration in the land register approximately: 890 Euro (priority notice and its cancellation; transfer of property).

There is no title insurance in Germany.

3.7.2. Transfer Taxes

Taxes on the transfer of real property are regulated by a special statute (*Grunderwerbsteuergesetz*). The tax rate is **3,5%** of the purchase price. (It is very seldom that the parties do not state the real purchase price; otherwise the sales contract would be invalid.)

The notary is required to inform the tax authorities, but he does not have to withhold the tax.

However, **registration** of the transfer requires a certificate of the tax authorities that the tax has been paid (§ 22 GBO).

3.7.3. Real Estate Agents

Maybe **some 25%** of real estate sales among consumers have been arranged by real estate agents.

The agents usually charge **3,5% of the real estate price**.

Usually, **buyer pays the agent**. Often, also seller has a contractual liability to the agent. However, normally the buyer agrees to pay the fee to the agent instead of the seller.

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[18] § 18 BeurkG: „Auf die erforderlichen gerichtlichen oder behördlichen Genehmigungen oder Bestätigungen oder etwa darüber bestehende Zweifel soll der Notar die Beteiligten hinweisen und dies in der Niederschrift vermerken."

3.8 Buyer's Mortgage

In Germany, normally seller grants buyer a **power of attorney** to encumber the property sold with a mortgage even before payment of the purchase price.

- Under the terms of the security agreement, the creditor may make use of the mortgage only insofar he paid the purchase price to the seller. Normally, this condition has to be included in the document establishing the mortgage (even if it is not a clause of the mortgage, but of the underlying security agreement).
- To ensure, that the creditor keeps his promise, the mortgage can be established only for a European bank as a creditor.
- Often, the power of attorney can be used only for documents certified by this notary. Thereby, the notary takes an additional responsibility for controling the terms of the power of attorney.

4. Special Problems concerning the Sale of Real Estate (Cases)

4.1 The Conclusion of the Contract

After inspection, the buyer tells the seller that he wants to buy the house. Thereafter, both of them sign a written contract, which states that the seller will sell and the buyer will buy the house under usual conditions. The purchase price is also indicated in the written document. What, if any, legal effect does this document have?

Answer: Under German law, any real estate sales contract which has not been concluded in a notarial instrument, is invalid. Thus, a contract made by a private written document, is invalid and has no legal effect whatsoever.

There are only very few exceptions that a formally invalid real estate sales contract might be enforced, in particular if the seller deliberately prevented the buyer from fulfilling the legally required form.

4.2 Seller's title

4.2.1. Consequences of an invalid Sales Contract

A has sold real property to B. Now, B wants to sell it to C. However, before entering into the contract, C finds out that the sales contract concluded between A and B was invalid,

a) because it lacked the required form;

b) because A did not possess legal capacity;

c) because an administrative permit required for the contract has never been applied for.

May C go ahead with the contract and acquire the property validly?

Answer for Germany:

a) The transfer of real estate is valid, if the transfer was declared before a notary and if it was registered in the land register, even if the sales contract lacked the required form. Thus, B has become owner.

b) If A did not possess legal capacity, the sales contract and the transfer of property are invalid. B has not become owner and cannot transfer property to C.

c) In the last case, one has to distinguish: If the administrative permit was required also to make the transfer of property valid, then B has not become owner.

4.2.2. The Seller is not the owner

A sells his property to B, who pays the purchase price and has the transfer registered with the land register. Only afterwards, it turns out that A was not the owner, with B having however relied in good faith on A's title. (This may happen e.g. when the seller was believed to have inherited the property from his uncle by a will, but a subsequent will is found in which the uncle leaves his entire assets to a charity. To make it a case, let us suppose further that the seller has become insolvent and cannot repay the money.)

Answer for Germany: There is no problem for B: He become owner, because he acquired property in good faith on the land register (§ 892 BGB). Also, the real owner (in our case the charity) cannot claim the sales price form B (but only from A).

Alternative: B finds out, that A was not the owner, before the transfer of property:

– If B finds out only after the priority notice (*Vormerkung*) has been registered, B has ac-

quired the priority notice in good faith (and therefor, can also acquire property afterwards).

– If, however, B finds out, before the priority notice has been registered, he cannot acquire property (without the real owner's consent). However, according to the contract, payment is due only after the priority notice is registered. So, there is no risk for the buyer.

4.2.3. Execution against the Seller

After the parties have signed the sales contract, but before its registration, a creditor of the seller distrains upon the property in order to enforce a judgement against the latter.

In Germany, we have to distinguish two situations:

– If the priority notice (*Vormerkung*) has been registered, not only later dispositions of the real estate are invalid, but also enforcement by creditors (who have not yet registered a mortgage prior to the priority notice). Note: The invalidity is only a relativ invalidity as to the buyer protected by the priority notice. To all other parties, the enforcement procedure is valid.

– If an enforcement procedure started before the priority notice was registered – or if the creditor of a prior mortgage demands to enforce his mortgage, the buyer cannot stop them. However, then buyer will not pay the purchase price – unless the creditor agrees to stop the enforcement and to let the sale go ahead in exchange for receiving a part of the purchase price.

4.3 Payment

4.3.1. Delay in payment

If the buyer pays late, the seller has two remedies:

– First, buyer is liable for damages (§§ 286, 280 BGB). If payment was due on a fixed date or if it was due after buyer received the notary's notice (which is normally agreed by the parties), then liability arises even if seller did not send a reminder (*Mahnung*). Otherwise, seller has to remind buyer before he can claim damages for the delay. As a minimum damage, seller may claim statutory interest for the delay (§ 288 BGB); right now, the statutory interest is 6,13% (it changes every half year, according to the interest rates of the European Central Bank).

– Second, the seller may rescind the contract (§ 323 BGB). Before rescinding, however, the seller has to set an additional time for the buyer to effect payment.

4.4 Defects and Warranties

4.4.1. Misrepresentation

– Half a year after the buyer has moved in, a water pipe breaks and floods parts of the house. The water pipe was put in when the house was built some decades ago.

– In spring, the basement is flooded. Neighbours tell the buyer that the seller complained to them that the flooding happened every other year in spring.

– An extension of the house has been built without the necessary permit of the building authority. Now, the authority asks the buyer to tear down the extension. The seller claims that he did not know that the permit was missing, since the extension had been built years ago by the previous owner.

In **Germany**, in most real estates sales contracts among two consumers, the seller's liability for material defects is excluded.

– Seller is liable for all defects about which he should have told the buyer, because buyer could not see the defect when inspecting the house and because they are major defects. Thus, seller is liable for the damage caused by the flooding.

– It the seller himself expanded the house without obtaining the necessary permit, he was under a legal obligation to tell the buyer. However, this applies only, if seller knew that the building permit was missing.

4.4.2. Destruction of the house

After the parties have signed the sales contract, the house burns down. What are the consequences for the contract?

In **Germany**, it depends whether the possession has already been transfered:

– If possession had already been transfered, then it is the buyer's risk.

– If possession had not yet been transfered, buyer may rescind the contract. However, seller is not liable for the damage (unless he responsible for the fire). Normally, seller has fire insurance.

5. Sale of a house or apartment by the building company (vente d'immeuble à construire/Bauträgervertrag)

5.1 Statutory Basis

5.1.1. National Law

Do any special rules (e.g. on consumer protection) apply if the seller also constructs the house which he is selling? When do these rules apply?

If a property developer (*Bauträger*) not only constructs, but also sells houses and apartments, the so called "***Makler- und Bauträgerverordnung***", a special Ordinance dealing with risks from contracts with brokers and property developers, applies. The term "*Bauträgervertrag*" describes a special type of contract of a professional property developer, which consists of elements of a contract for services, sale and agency. The inherent risk of such an arrangement of the legal relations is that the property developer has an interest to receive payments before the construction is completed and the transfer of ownership has taken place. However, according to §§ 94, 946 BGB the ownership of the land extends to all essential component parts of the new building, which therefore remain with the seller until the whole contract is implemented. The main purpose of the *Makler- und Bauträgerverordnung* (MaBV) therefore is to meet the risks of insolvency of the property developer arising from advance performances of the buyer. Unfortunately, in the past there have been a number of building constructers with insufficient financial background for their projects. The seller, on the other hand, is often a private person obtaining a bank credit or investing most of his savings, so that the need for some form of protection arises.

5.1.2. Influences of EU law

The contract of the property developer is usually a **consumer contract**. Thus, in addition to the MaBV §§ 305 BGB sqq. apply providing terms control for standard term contracts as well as for consumer contracts. These provisions (and their predecessor, the former Code on **Standard Contract Terms**, *AGB-Gesetz*) were enacted in transposition of the EC Unfair Terms Directive. Since national law transposing EC directives has to be interpreted in accordance with the European legislation, it is obvious, that there is some influence of existing EU law on the contract of the property developer. The view had even been expressed that contract terms providing for payment of instalments in accordance with the provisions of the MaBV would deviate from a guiding principle of the contract for services expressed in § 632a, which was introduced into the Civil Code in the year 2000, and therefore contravene the Unfair Terms Directive[19]; the discussion even provoked an enactment of the Federal Department of Justice[20]. However, in case C-237/02, *Freiburger Kommunalbauten*[21], the European Court of Justice (ECJ) refused to scrutinize the compatibility of a clause in a building contract (stipulating that the buyer had to pay the purchase price even before the building works started, the buyer's rights being protected to a large extent by a bank guarantee covering violations of the contract as well as the insolvency of the builder) with Art. 3 of the Unfair Terms Directive. So the control of unfair terms in this field seems to remain largely national.

5.2 Procedure in general

5.2.1. Single houses

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19 THODE, ZfIR 2001, 345.

20 cf. BLANK, *Bauträgervertrag*, 2nd ed. 2002, p. 55.

21 Available online at http://www.curia.eu.

If the builder sells from a large piece of land several small parcels, which have not been surveyed by the cadaster and consequently not registered in the land register, the piece of land may be sold subject to survey of the landed property. In order to determine the object of sale in a sufficient way, its precise location has to be described in the contract, which is usually done by a map attached to the deed. The builder will then apply for the survey of the land to be made by the cadaster. With the offical record of changes to the plots of land the new parcels may be registered in the Land Register. There are some special arrangements necessary in the contracts, since the new pieces of land may not each by themselves be encumbered (e. g., with a land charge for creditors of the buyer), before the registration in the land register has taken place. Until very recently the partition of land required an administrative permit by the municipality if so provided by the local development plan. This permission for the partition has, however, been repealed by the legislator with effect as of 07/20/2004.[22] Apart from this, no special regulations apply to the sale of a fractional tract of land. The payments are usually made in instalments according to the state of progress of the construction. In this respect, the provisions of the MaBV do apply providing for the permitted amount of instalments. In case of material defects of the building the regulations of the Civil Code on the contract for services apply, which are in a consumer contract by and large mandatory. With regard to material defects of the land the builder is responsable for defects in his planning.

If the builder sells apartments in a condominium which he is planning to build, he will first have to divide the land into flat property units. This requires a partition plan, where the appartments and the common parts are exactly described. The partition plan needs to be registered in the land register. The deed of partition usually comprises a plan of the flats, a building specification and the condominium bye-laws. A permission by the public authority for the partition may be required in areas of tourism if so provided by the local development plan. Usually, the sales start prior to the registration of the partition. Therefore, the contracts must refer to the partition plan to describe the object of sale in a sufficient way. The payments are typically made in instalments according to the progress of the building. The MaBV and the provisions of the Civil Code as to material defects in contracts for services apply.

5.2.2. Renovation

Another variation: Let us assume that the builder has bought an old house which he wants to renovate and split up into separate apartments. He sells the apartments before completing the renovation. What, if any, are the differences as compared with the first and second case?

If the seller wants to renovate an old house and split it up into apartments he again needs to establish a partition plan first, which has to be registered in the land register. In the sale contracts he may also refer to the partition plan in order to determine the object of sale. The partition plan would also include a plan of the flats, a building specification in respect of the renovations to be made, and the condominium bye-laws. Unless the renovations are insignificant, the provisions of the MaBV are in principle applicable. In respect of the first instalment, however, the parts of the construction that remain unchanged, may be taken into account. The further instalments for the reconstructed parts may only be demanded according to the progress of the building, as determined in the MaBV. As regards the liability for material defects, the questions arises, if in respect of the old construction the provisions of the Civil Code on the contract of sale instead of the contract for services may apply. The distinction may be material, because in case of a contract of sale, which does not refer to a new item, the seller's liability may be excluded to a large extent (except from liability for intent, gross negligence, personal injury due to fault of himself or his employees and for the infringement of material contractual duties, cf. §§ 639, 307, 309 Nr. 7 BGB), whereas in the case of a contract for ser-

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[22] For exceptions in some of the provinces of Germany cf. DNot-Report 2004, 173.

vices most of the legal provisions are mandatory in a consumer contract (cf. § 309 Nr. 8 BGB). The rules of the contract for services apply, if the reconstruction is fundamental, if the new parts of the building are integrated into the old parts to the extent, that they can no longer be distinguished from one another or if the builder sells the house as new. Otherwise the law of sale may indeed be applicable to the unchanged parts of the old house. In case of the establishment of apartment ownership in an old house, the tenents living in the flat at the time of the registration of the partition plan in the land register also have a special preemption right according to § 577 BGB.

5.3 Conclusion of the Contract

The sales-building-contract requires a **notarial act**. According to § 311 b BGB a contract whereby one party binds himself to transfer ownerhsip of land requires notarial authentication. This also extends to all collateral agreements, which are essential for the transfer of land and hence also to the construction of the building. As a rule, no preliminary contract is concluded in practice. Such a contract would also require a notarial act, as the function of the notarial act is also to provide legal advice to the parties before they are bound.

Likewise, the buyer has no right to withdraw from the contract in the absence of a contractual agreement. However, § 17 par. 2a BeurkG stipulates that the buyer must receive a **draft of the contract two weeks before concluding** the notarial act. (§ 17 par. 2a BeurkG stipulates only a duty for the notary; the contract is valid, even if the waiting period has not been followed.)

5.4 Payment

5.4.1. Payment date

A balanced arrangement of the contractual relations usually includes performance only upon tender of counterperformance. If advance performances are to be made, there is a special need to secure the party's interests. Against this background the MaBV demands certain requirements to be met, before the payment may become due. Accordingly, the contract must be valid, all necessary permits must be given, a priority notice on behalf of the buyer must be entered in the land register, a necessary building permit must be granted or, alternatively, a corresponding negative clearance, furthermore it must be ensured that the buyer acquires the property free from encumbrances, which he did not assume. The notary has to confirm to the buyer the existence of most of the necessary prerequisites. In addition, the instalments may only be paid according to the state of progress of the status of the building. Usually, the payments are made directly by the buyer to the builder. It is only deposited on an escrow account, if there is a special need for protection, which, under the regime of the MaBV, does normally not arise. It is controversial, to what extent the buyer may submit to immediate enforceability in the sales contract, since the Federal Supreme Court has ruled that the immediate enforceability without proof that the payment is actually due, would be invalid[23]. The better view seems to be that the granting of an executed copy of the notarial deed must depend on the proof that the payments are due, whereas the progress of the building could be certified by an independent officially appointed sworn expert[24].

5.4.2. Securities

In Germany, a guarantee (normally from a bank) is required only if the parties agree upon payment to be made before the buyer's priority notice is registered in the *Grundbuch* or if the

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[23] BGHZ 139, 387 = DNotI-Report 1998, 208 = DNotZ 1999, 53 = MittBayNot 1998, 458 = MittRhNotK 1998, 373 = NJW 1999, 51 = WM 1999, 29 = ZfIR 1998, 749 = ZIP 1998, 2063 = ZNotP 1999, 34.

[24] cf. HERTEL ZNotP 1999, 3 sqq.

buyer has to pay more or earlier than under the usual instalment plan fixed by statute (which foresees certain instalments payable according to the state of progress of the construction, § 7 MaBV).

5.4.3. Acquisition of Ownership

The future ownership of the buyer is ensured by the entry of the priority notice in the Grundbuch. By this means, all later dispositions which run counter to the claim of the buyer to acquire ownership are void as against his person. The release of the object of sale of all interests in land not assumed by the buyer and with better or equal position than the priority notice is secured, if a commitment of the creditor ensures that the mortgage will be cancelled in the land register, if the building is completed upon payment of the entire purchase price, otherwise without undue delay upon payment of this part of the purchase price which equals the achieved level of construction. In the case of non-completion of the building the creditor may also reserve the refund of all payments made by the Buyer within the limits of the instalments up to the partial value of the object of sale.

5.4.4. Building

As stated above, the buyer normally has to pay instalments according to the state of progress of construction. As soon as the Object of sale is ready for occupancy the acceptance of the building usually takes place, which is of major importance inter alia for the burden of proof and prescription in respect of material defects. The Object of Sale is normally deemed ready for occupancy even if the facilities outside the building have not been entirely completed or minor works of repair or make up are yet to be done. On the occasion of the acceptance the object of sale will be inspected by the parties, during which eventually noticed material defects of missing work shall be listed in minutes of the acceptance which shall be signed by both parties. Upon acceptance of the completion of the building the possession of the Object of Sale is surrendered concurrently with the payment of the corresponding instalment of the purchase price, provided that the Buyer has performed to the Seller all obligations to payment due up to then. The last instalment will be payed after completion of the whole building.

5.4.5. Financing of the Buyer

If the buyer needs to finance the purchase price by way of a credit, the financing bank will demand sufficient security. The question therefore arises, if the buyer can set up a mortgage on his future property (most private persons cannot achieve to offer other security). In order to protect the seller from the risks of an advance performance, the buyer is normally not entitled to acquire ownership before he has payed the purchase price. Therefore, the seller will grant to the buyer a power of attorney in the contract to set up a mortgage on the object of sale even before the ownership is transferred (if the mortgage cannot be registered immediately, because, e. g., a sold parcel of land has not yet been surveyed, it may also be possible to pledge the claims of the buyer from the contract in the meantime). However, in the contract sufficient measures must be taken that the credit can only be used for the payment of the purchase price, if the land is encumbered with a mortgage of the buyer. Moreover, in case of a breach of contract on the part of the buyer, his bank would have to release the mortgage. This requires complex legal arrangements usually involving both parties to the contract as well as their banks. The bank of the buyer can only rely on the security, if the money is transferred directly to the seller or his bank and only to the extent that payments have already been made. In general, the seller also takes up a loan to finance the purchase of the land and the construction of the building. Thus, he also needs to provide security, which is usually a mortgage on the respective plots of land with first priority in the land register. However, according to the sale-construction-contract the purchase price is not due, until the bank of the seller has committed itself to waive the security upon payment of the purchase price. The bank of the buyer will therefore not pay, before the bank of the seller has promised to release its security against

payment of instalments, as provided in the sales-building-agreement. The committment of the seller's bank to release its security therefore bears a corresponding duty of care.

5.5 Builder's Duties - Protection of Buyer

5.5.1. Description of the Building

The conclusion of the contract entails a sufficient description of the construction performance. This is done by way of a building specification as well as plans in respect of the location, the sight of the building and the dimensions of the flats and rooms, which are attached to the notarial deed. The building specification must be in accordance with the transparency requirement laid down in § 307 para. 1 subpara. 2 BGB. There has been criticism expressed that the building specifications would in practice not be detailled enough to meet technical requirements[25]. However, from the legal point of view the building specifications seem to be sufficient to describe the duties of the seller in the ordinary cases[26].

5.5.2. Late Termination of the Building

The contracts usually provide for an exact date, when the building must be completed. It is often distinguished between the completion for immediate occupation and the completion of the facilities outside the building. In case the seller does not perform his obligation in time, the buyer may claim damages for the delay or - after a notice fixing an additional period of time for performance – even terminate the contract. This, however, involves the risk that his own claim is also repealed and the priority notice deprived of its effect as security. In exceptional cases the buyer therefore may be granted a right to cancel only parts of the contract.

5.5.3. Material Defects

In case of material defects of the building the buyer has the rights as provided in § 634 BGB. In the first place he may by notice to the other party allow an additional period of time for performance. If upon expiry of that period due performance has not been made, the buyer may remedy the defect himself and claim reimbursement for his outlay, he may reduce the price or terminate the contract or he may claim damages and certain other expenditures. As a rule the buyer has no claim against the companies commissioned by the builder. In practice, the seller often assigns his claims against his mandataries to the buyer, which does, however, not debar the buyer from his rights against the seller[27].

5.6 Builder's Insolvency

5.6.1. Unfinished Building

In theory, the buyer of an apartment is not really protected if the builder goes insolvent during construction. Under § 3 MaBV his claim to a share of the real estate is secured by the priority notice. However, if he is the only buyer so far, he will not have the means to complete the building, if the builder goes insolvent.

In practice, however, normally the bank which finances the builder, then takes care that the building is completed. Thereby, the bank wants to secure its loan. As a side effect, however, the buyer also gets his apartment (although belatedly).

5.6.2. Repayment

The case of the unfinished building ist the main risk for the buyer in a sale-construction-

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25 cf. PAUSE, *Bauträgerkauf und Baumodelle*, 4th ed. 2004, p. 176.

26 BASTY, *Der Bauträgervertrag*, 4th ed. 2002, p. 44 sq.

27 BGHZ 150, 226 = BB 2002, 1508 = DNotI-Report 2002, 117 = DNotZ 2002, 857 = MDR 2002, 1060 = NJW 2002, 2470 = WM 2002, 1555 = ZfIR 2002, 631 = ZIP 2002, 1356 = ZNotP 2002, 353.

contract. The buyer would normally keep his claim to acquire the legal title in respect of the flat property due to a priority notice. However, the economic value of the title is limited, as long as the building is not completed. It is normally impossible for the buyer to organize the necessary constructions himself at the prize of the remaining instalments. Apart from aspects of time and expertise the buyer cannot benefit from cost advantages arising from the professional management in relation to a number of projects. If the buyer has terminated the contract before the builder goes insolvent, the priority notice is deprived of its effect as security. In respect of the instalments already performed the buyer may demand repayment. But if the assets of the seller are insufficient, he is in no better position than any other creditor.

6. Private International Law

6.1 Contract Law

6.1.1. Conflict of Law Rule

According to Art 27 I 1 EGBGB (Art. 3 I 1 of the Rome Convention) a contract is governed by the law chosen by the parties. The general view is that this provision also applies to contracts on real property. However, German law distinguishes between so called "obligatory" (*schuldrechtliche*) and "real" (*dingliche*) contracts. By way of the 'obligatory contract' a duty of the debtor to do or to refrain from doing something as well as the corresponding right of the creditor is established. In order to perform the obligation a further "real contract" may be required to effect a change in title such as the transfer of ownership or the encumbrance of land. The provision of Art. 27 EGBGB only applies to the obligatory contract. The real contract is governed by the lex rei sitae, even if it is enclosed in the same document. If a foreign legal system does not distinguish between the obligatory and the real part of the contract (as in French law), i. e. the ownership is transferred by means of the contract of sale, the law of the country where the land is located would be mandatory.

In the absence of a choice of law, the law of the country with which the contract is most closely connected, is applicable (Art. 4 I of the Rome Convention; Art. 28 I EGBGB). In case of a contract relating to a right in land or to a right to use land there is a rebuttable presumption that the closest connection is with the country where the immovable property is situated (Art. 4 III of the Rome Convention; Art. 28 III EGBGB).

6.1.2. Formal Requirements

According to Art. 11 I EGBGB (Art. 9 I of the Rome Convention) a legal transaction is formally correct if the form requirements of the law which is applicable to the legal relation creating its substance, or the law of the state in which it is transacted is complied. If therefore a contract on the sale of land situated in Germany is concluded in Austria in writing, the contract would as a consequence be valid, since according to Austrian law in contrast to German law the written form is sufficient to establish an obligation to transfer ownership in land. The provision of § 311 b BGB requiring a notarial act is according to the prevailing view not compulsory in that sense, that it is applicable without regard to the place where the contract was made or the law by which it is governed (Art. 11 I EGBGB, Art. 9 VI of the Rome Convention).

6.2 Real Property Law

6.2.1. Conflict of Law Rule

The wording of Art. 43 I EGBGB runs as follows : "*Rechte an einer Sache unterliegen dem Recht des Staates, in dem sich die Sache befindet*" ("The rights in a thing are governed by the law of the location of the thing"). The provision also applies to land. In this respect, a choice of law is not admissible.

6.2.2. Formal Requirements

Art. 11 V EGBGB provides that a legal transaction which gives rise to a right to a thing is formally correct if it complies with the form requirements of the law which is applicable to the legal relation creating its substance. Therefore, the lex rei sitae also determines the form of the transfer of ownership. In addition, the prevailing view in Germany concludes from the regulation in respect of the conveyance in title in § 925 BGB that the transfer of real property

may only be celebrated with a German Notary[28].

Apart from historical reasons this is justified on the ground that the Notary does not only have duties as to the parties privy to the contract, but also in respect of the correctness of the Land Register. This is particularly important, since there is a special need of legal certainty and clarity in the field of real property law. In addition, the notary has to give notice of the transfer of ownership to a number of public authorities, such as the tax office, a committee of experts investigating in the value of land etc. Land is to a large extent embedded into its legal environment and cannot be transfered without sufficient expertise in respect of the underlying legal system. Moreover, this practice does not seem to be a major impediment to transnational legal transactions, since the buyer of a piece of land in Germany will in most instances also spend some time in the country, otherwise, he may grant power of attorney to a local agent or go to see the competent consular officer abroad.

6.3 Restrictions for Foreigners to acquire Land

6.3.1. Restrictions limited to Foreigners

There are no restrictions for foreigners to acquire real property in Germany, nor are there any other permits required which play a role particularly for foreigners acquiring real property.

6.3.2. Other Restrictions

See under 6.3.1.

6.4 Practical Case: Transfer of Real Estate among Foreigners

Let us suppose that a couple of nationals of another EU Member State own a vacation home in your country. They consider to transfer the ownership either to their children (as a gift) or to another couple, who are nationals of the same Member State as them. If possible, the parties want to conclude all necessary contracts in their state of origin. They ask a local lawyer/notary there to prepare the transaction. This lawyer/notary asks you about the easiest way for the parties. What way do you recommend – or what is considered to be the best practice?

One possible way would be to conclude the obligatory contract abroad and afterwards celebrate the transfer of ownership in Germany, since the transfer of ownership may only be celebrated with a German Notary. If the parties wish to conclude all necessary contracts in their state of origin, they would have to authorise an agent to conclude the contract on their behalf. Therefore a notarial power of attorney would be necessary with an apostille fixed upon it or, alternatively, a legalisation. There are certain disadvantages, if the parties conclude the obligatory contract abroad: On the one hand, the legal transaction is split up into separate documents and therefore becomes more complex. On the other hand, it may cause additional costs, since according to § 925 a BGB the notary certifying the transfer agreement is by law obliged to examine also the obligatory contract and give legal advice to the parties in this respect[29]. The preferable way would therefore be to conclude also the obligatory agreement in Germany and extend the power of attorney accordingly. It would also be possible that one member of the family would travel to Germany and conclude the contract also on behalf of the others. In this context it may be noted that the U. I. N. L. has edited forms of powers of attorney for international land transactions, which may be helpful in drafting the power of attorney.

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28 cf. DÖBEREINER, ZNotP 2001, 465.

29 cf. BayOblG DNotZ 1978, 58; OLG Hamm ZNotP 1998, 301; different OLG Düsseldorf DNotZ 1991, 410.

7. Encumbrances/Mortgages (and Land Charges)

7.1 Types of mortgages/land charges

7.1.1. Types of mortgages

In Germany, the general term is *Grundpfandrecht* („real security on real property"*)*. It encompasses the *Grundschuld* (§§ 1191 ss. BGB) and the *Hypothek* (§§ 1113 ss. BGB). The *Hypothek* is an accessory security whereas the *Grundschuld* is a non-accessory security. In the Civil Code, the default model is the *Hypothek* whereas the *Grundschuld* is regulated largely by references to the rules on the *Hypothek*.

In practice, however, the *Grundschuld* prevails, as it is more flexible and may also be used to secure later debts with the same creditor. Conversely, the *Hypothek* is not used very often, and banks in particular have a firm preference for the *Grundschuld*.

– Further subtypes of the *Hypothek* are the *Sicherungshypothek* (§§ 1184 ss. BGB), a strictly accessory mortgage, and the *Höchstbetragshypothek* (§ 1190 BGB). Whereas an ordinary *Hypothek* registered in the land register may be acquired by an assignee in good faith even if the underlying claim is no longer existing (§§ 892, 1157 BGB), the *Sicherungshypothek* can be acquired only if the underlying claim exists (§ 1184 BGB). The *Höchstbetragshypothek* (§ 1190 BGB) is a special type of a *Sicherungshypothek* according to which only a maximum amount of the mortgage is registered whereas the secured claim may be changed.

– A subtype of the *Grundschuld* is the *Rentenschuld* (§§ 1199 ss. BGB), which is however hardly ever used. Under the terms of a *Rentenschuld*, the owner has to make regular payments. However, the owner may choose to pay a lump sum instead (which is why for regular payments normally a rent charge – *Reallast*, § 1105 BGB – is chosen).

Another important distinction applies between the *Briefrecht* (a mortgage documented by a separate certificate) on the one hand and the *Buchrecht* (a mortgage documented only in the land register) on the other hand. Unless agreed otherwise, a *Brief* (mortgage certificate, § 1116 BGB) must be issued. Both the *Hypothek* and the *Grundschuld* can exist in both forms ("*Briefhypothek – Buchhypothek*; *Briefgrundschuld – Buchgrundschuld*"). However in practice, the land charge without certificate ("*Buchgrundschuld*") prevails today.

7.1.2. Legal nature

Mortgage and land charge are both a *ius in rem*. They entitle the creditor to enforce payment of a claim of money from the real estate (§ 1147 BGB).

However, the creditor still needs a title for encorcement: If the owner has not declared submission to enforcement (§ 794 par. 1 n° 5 ZPO), the creditor first has to go to court to get an enforceable title before he may start a forced sale.

7.2 Setting up a mortgage

7.2.1. Example

Under German law, a mortgage is set up under the following three conditions (with a forth condition for the *Hypothek* only):

– Normally, the owner of the real estate and the mortgagee **consent** on the setting up of a mortgage (*Einigung* - § 873 BGB). Alternatively, the parties may agree on the setting up also at a later stage. To register a mortgage in the register, only a unilateral statement of the owner is necessary (§ 19 GBO). This must be authenticated by a notary (§ 29 GBO).

As long as no consent to use the mortgage for a certain loan has been reached, the owner remains entitled to the mortgage himself ("*Eigentümergrundschuld*").

– The mortgage is **registered** in the Grundbuch (§§ 873, 1115 BGB).

– In the case of a *Briefgrundpfandrecht* (mortgage with certificate), the mortgagee acquires the mortgage only when the mortgage certificate (*Hypothekenbrief* or *Grundschuldbrief*) is handed over to him by the land owner (or by the *Grundbuchamt* with the owner's consent). In the case of a *Buchgrundpfandrecht* (mortgage without certificate), however, the mortgagee acquires the mortgage with its mere registration provided that the register entry also mentions that no certificate has been issued (§ 1117 BGB).

– For the ***Hypothek*** only, the forth condition is required that the claim to be secured by it exists. If there is no valid claim, but the other three preconditions are fulfilled, a mortgage for the land owner (*Eigentümerhypothek*) comes into existence (§ 1163 BGB). Conversely, a *Grundschuld* comes into existence and is acquired by the mortgagee, whether or not the secured claim exists.

7.2.2. Legal requirements for the loan contract affecting the mortgage

Which legal requirements does the bank have to respect when granting a mortgage loan? In particular: Must the bank give some minimum information to the customer before a valid loan contract can be signed? Are there minimum periods between the release of the information, the signature of the contract and the setting up of the mortgage? Can the mortgage been erased within certain periods if the customer wants to cancel it?

7.2.3 Formal requirements

In Germany, the consent on the setting up of a mortgage (*Einigung*) is valid without any formal requirements. However, for the **registration** in the *Grundbuch*, the signature of the owner shall be certified by a notary (*Unterschriftsbeglaubigung* - § 29 GBO).

In practice, most mortgages are set up by notarial instrument (authentic act), because only this instrument allows the debtor to submit to immediate enforcement (§ 794 sec. 1 n° 5 ZPO).

The mortgagee's acceptance is normally made informally (not even in writing).

7.2.4 Registration

In Germany, the mortgage (as all other rights in real property) comes into **existence only upon registration** (§ 873 BGB). The registration must contain the following information (§ 1115 BGB): the name of the mortgagee, the amount of the mortgage, the interest rate (if applicable); the time as of which the interest is due has to be stated either in the *Grundbuch* or in the instrument creating the mortgage (and has to be referred to in the *Grundbuch*).

7.2.5. Time and Costs

The average time for registering a mortgage in Germany should be around **two weeks**.

The notary can give an opinion to the effect that the registration of the mortgage in the foreseen ranking position is secured (*Rangsbestätigung*). This opinion is usually accepted by banks.

If it is not possible to register a mortgage, the buyer can also pledge his claim for security (*Verpfändung der Auflassungsvormerkung*). The bank's pledge will then be registered with the priority notice. Then, however the bank's security is dependent on the buyer's claim. Therefor, the bank is less secure than with a mortgage or land charge. Thus, this security is only used, if a mortgage cannot be registered (e.g. if only one piece of a larger real estate is sold and if the seller does not want to have a mortgage registered on the whole real estate, but if payment is due before the piece has been registered as a separate parcel of real estate.)

- What are the costs for establishing a typical security for (a) 100.000.- and (b) 300.000.- Euros?

– notary fees: 207 Euro or 507 Euro respectively,

– registration fee (*Grundbuchamt*) - same

– Both fees are fixed by law (§§ 36, 62 KostO)

– There are no taxes for establishing a mortgage.

7.3 Causality and Accessoriness

7.3.1. Invalid loan contract

Let us assume that the loan contract is invalid. How does this affect the mortgage - assuming that all other requirements for creating a mortgage have been complied with?

In Germany, the answer depends on whether it is a *Hypothek* or a *Grundschuld*:

– The *Hypothek* comes into existence, but it belongs to the land owner, not to the mortgagee (even though it is registered for the mortgagee) (§ 1163 BGB).

– A *Grundschuld* comes into existence irrespective of whether or not the underlying claim exists. However, if there is no claim to be secured, the land owner may claim that the mortgagee transfers the mortgage to him or that he consents to erasing the mortgage from the *Grundbuch*.

7.3.2. Right of withdrawal

Let us assume that the debtor-consumer has a statutory right to withdraw from the loan contract. The debtor exercises this right only after the mortgage on the real estate has already been established. (This might be possible if the bank did not inform the debtor properly about his right to withdraw and, as a consequence, the deadline for the withdrawal has not yet expired.)

Can the bank still use the mortgage to secure her right for repayment of the loan?

Note: In case C-481/99, *Heininger* (ECR 2001, I-234), the ECJ decided that loan contracts were covered by the doorstep sale directive when concluded under „doorstep conditions" - with the effect that the debtor may invoke the withdrawal right foreseen in that Directive against the bank. However, according to the ECJ, the consequences of a withdrawal from the loan agreement for the purchase of real property and the setting up of a mortgage were still to be determined by national law.[30] This finding has however been challenged in a follow up-reference by the *Landgericht Bochum* under the principle of effective consumer protection.[31] It is likely that the ECJ will revise the *Heininger* judgement accordingly. As a consequence, one may expect that the ECJ will establish European law minimum conditions as regards the legal consequences of the withdrawal from a consumer contract, which include the effects on security rights such as mortgages.

7.3.3. Changing the secured debt

– The debtor has repaid the loan for which the mortgage was granted. Now, he applies for another loan. Can the old mortgage be used to secure also the new loan (and if so, under which conditions)? Or is it necessary to set up a new mortgage?

Yes, a land charge can also secure the new loan. Also for a mortgage, the claim secured may

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30 Heininger Case, op. cit., No. 35.

31 See NJW (*Neue Juristische Wochenschrift*) 2003, 2613.

be changed (§ 1180 BGB).

– Let us assume that 30% of the mortgage loan have been repaid. Now, the mortgagee wants to take up another loan for his business, amounting to 25% of the old loan, but with a much higher annual amortisation and a different interest rate. Can the "free" part of the old mortgage be used to secure this loan? What has to be done for this?

If, as usually, a land charge (*Grundschuld*) has been established and according to the security agreement, all claims of the bank against this debtor are secured, there are no additional steps necessary.

– Let us assume that the debtor has agreed on a loan secured by a mortgage. However, the house to be financed is not yet build, but its completion has been agreed upon as a condition for the disbursal of the loan. Therefore, the debtors wants to take up an interim loan from another bank. Can the mortgage be used to secure this interim loan until it is replaced by the final mortgage? How can this happen?

Yes, if the land charge is assigned to the other bank.

– The bank and the mortgagor have agreed on a mortgage loan for a five year term at a fixed interest rate. Now, this period is over, and both sides want to agree on a new loan for another five years, but at a different interest rate. Can the old mortgage secure the new loan?

If, as usually, a land charge (*Grundschuld*) has been established and according to the security agreement, all claims of the bank against this debtor are secured, there are no additional steps necessary.

– What if in the last example the mortgagee wants the new loan from another bank? Could the old mortgage be used for the new loan? If yes, what steps need to be taken? Is the consent of the old bank necessary?

Then it would suffice to assign the land charge to the other bank – and to conclude a security agreement with this bank.

– What if the new loan is not designed to finance a property but a car or the mortgagee's company and is subject to different conditions, e.g. a higher interest rate and a higher amortisation?

No problem with a land charge.

– The mortgagee runs a business and is in permanent need for credit. He agrees with his bank on a maximum credit line, which is used for different loans. Can this credit line be secured by a mortgage? Are there special forms of mortgages for it?

Normally, one would just use a land charge (*Grundschuld*).

7.3.4. Independent/abstract promise of payment

Regularly, in the same notarial document in which the owner creates the land charge, he also grants the creditor an abstract promise of payment (independent debt or parallel debt – *abstraktes Schuldversprechen/abstraktes Schuldanerkenntnis* - §§ 780, 781 BGB). The debtor also submits to enforcement concerning the independent debt. Thus, the bank may enforce its claims also against movables owned by the debtor – and also against the debtor's earnings.

7.3.5. Mortgage for the land owner himself

The German system also allows to set up a land charge for the land owner (*Eigentümergrundschuld* - § 1196 BGB). Afterwards this land charge is assigned to the creditor.

Often, the *Eigentümergrundschuld* is constituted with a certificate (*Briefgrundschuld*). Then, in the land register, you can only see that there is a land charge, but you do not know who is

the creditor.

7.4 Enforcement and other rights of the bank

The debtor did not pay the interest or did not repay the loan. Therefore, the bank wants to enforce the mortgage/land charge.

In theory, the bank needs to go to court in order to make the mortgage enforceable (§ 1147 BGB). In practice, however, regularly the owner submitted to immediate enforcement when establishing the mortgage (§ 794 par. 1 n° 5 ZPO). Then, the notary may give a title to the bank. Normally, the bank asks for this title immediately after the mortgage has been registered; then the bank has got the title, just in case.

- Please describe the main steps of the enforcement procedure!
- How long does the enforcement procedure regularly take before the bank receives the proceeds of the mortgage? Can the debtor slow down the procedure, especially if the mortgage is on his residential home? Can the bank act in receivership in the meantime (*Zwangsverwaltung*)?
- Before payment has become due, the owner must not grant the bank the right to purchase or the power to sell the property by means of a normal real estate sales contract (in the event that the loan is not repaid) (§ 1149 BGB). After payment has become due, often the bank tries to find somebody interested in buying the property, because the price for a forced sale is very difficult to estimate beforehand.
- Are there any instruments for public administration or courts to stop or suspend foreclosure for social or economic reasons?
- What happens in the event that insolvency procedures over the debtor's estate are initiated? Will the foreclosure procedure be stopped? How are the mortgagee's rights protected in an insolvency procedure?

7.5 Overriding interests and priority

7.5.1. Distribution of proceeds

§ 10 ZVG regulates the distribution of the proceeds from the enforcement procedure among the creditors. Normally, only the mortgages itself are economically important. Among them, the proceeds are distributed according to their rank.

Is the distribution different in case of legal foreclosure or insolvency of the owner or the debtor?

7.5.2. Overriding interests

According to § 10 par 1 n° 3 the real estate tax and some other fiscal charges concerning the last four years (and the costs of the foreclosure procedure) take precedence over the mortgage without being registered. Economically, however, these overriding interests normally are not very important.

- Fees for electricity, heating, garbage collection or other utilities are not included.
- Neither are or the salary of workers if an enterprise is established on the land.
- Can you indicate a percentage of how much of the value of the real estate these charges usually amount to?

7.6 Scope of the mortgage

7.6.1. Buildings

As a general rule, a mortgage on a real estate encompasses also a house built on it.

A separate mortgage on a building is possible only, if there is separate ownership of the building (which still might be the case in the eastern states according the law of the former GDR).

7.6.2. Machinery

According to § 1120 BGB, the mortgage extends also accessories and products of the real estate (e.g. if there is a business on the mortgaged premises, to its assets such as machinery, cars, raw material etc.) – to accessories, however, only upon condition that they have become property of the owner of the real estate?

7.6.3. Insurance

According to § 1128 BGB, the insurer has to inform the mortgagee before paying the insurance. If the mortgagee notifies the insurer about the mortgage, the insurer may pay to the owner only with the consent of the mortgagee.

7.6.4. Right to redeem

The security agreement spells out, under which conditions the mortgagor may redeem the mortgage. He has a statutory right of redemption, if all the claims secured have been paid.

The debtor may repay the credit and cancel the loan, if he has a legitimate interest, in particular if he sells the property encumbered with the mortgage (§ 490 par. 2 BGB).

7.6.5. Redemption after foreclosure

– May the mortgagor redeem the mortgage even after foreclosure?

7.8 Security granted by a third party

Let us assume that the debtor is not able to offer any kind of security for the loan. However, his wife is willing to mortgage her real estate.

– Are there any limitations on the liability of a third party according to statutory or case law, e.g. if the mortgage is to secure the debts of the husband's enterprise, including also all future debts?

7.9 Plurality of mortgages

– If the owner has already set up (and registered) a mortgage and then wants to set up a second mortgage for another bank, can he do so without the consent of the first bank? Would the holder of the second mortgage have a direct claim against the owner? What would happen if he wanted to execute the mortgage? Could he do so without the consent of the holder of the first mortgage? What would be the consequences for the first mortgage? Would it become due – or would the property be foreclosed – auctioned with the first mortgage on it?

The second mortgage can be set up and registered without consulting the owner of the first mortgage. However, in a forclosure procedure, the first mortgage has priority. If the second mortgage is enforced, the first mortgage is not concerned by the foreclosure. If however the first mortgage is enforced, then the second mortgage is extinguished with foreclosure, even if it cannot be paid in full from the proceeds.

– What happens to the second ranking mortgage, if the loan of the first mortgage has been repaid completely or partially? Does the second mortgage get a better position or even the first rank? (Or does the owner get the right on the position for the refunded parts of the first mortgage, and the second mortgage remains at its position?)

The second mortgage gets the better rank. The second creditor may ask the owner to cancel

the first mortgage, if the owner has paid the underlying debt and therefor has acquired the mortgage (§ 1179a BGB).

– Can mortgages be of equal ranking? How can this be effected? (Only by applying for registration on the same day or even in the same minute or by a later change of the ranking?)

Mortgages can have the same rank, if it has been agreed so and if it is registered so.

– Can the ranks of mortgages be exchanged or altered by agreement of the parties involved? Please describe the necessary steps.

The rank can be altered by consent of all parties and registration (§ 880 BGB)[32].

7.10. Several properties

A mortgage may cover several properties (*Gesamtgrundschuld/Gesamthypothek* - § 1132 BGB). A mortgage can also be extended later to another property of the same or another owner; then it becomes a *Gesamtgrundschuld/Gesamthypothek*.

In foreclosure, each property is liable for the whole mortgage (but all together of course not more than the sum of the mortgage) (§ 1132 BGB).

7.11. Transfer of the mortgage

7.11.1. Transfer of the mortgage in general

– The debtor has set up a mortgage/land charge to the benefit of bank 1 to secure a loan granted to him. Now, bank 1 wants to refinance the loan with bank 2 How can bank 1 transfer the mortgage to bank 2? Please describe the necessary steps!

If it is a *Buchgrundpfandrecht*, the transfer of the mortgage requires consent (in writing on the part of the transferor) and registration. For a certified mortgage (*Briefrecht*), consent (in writing by the transferor) and the transfer of the certificat are required (§§ 1153, 1154 BGB).

– Can bank 1 transfer the mortgage without transferring also the secured claim (i.e. the claim arising out of the loan contract)? If not, are there any other options for bank 1 to use the mortgage as collateral for its debt with bank 2?

If it is a *Grundschuld*, the land charge may be transfered without the claim secured. An ordinary mortgage (*Hypothek*) however can be transfered only togethter with the secured claim (§ 1153 par. 2 BGB).

– Does the transfer have to be registered? (Is the registration necessary for the transfer to be valid or to be opposable against third parties? This question applies particularly in the insolvency of the transferring bank (bank 1).) What other ways exist to make the transfer insolvency-proof?

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[32] § 880 BGB – Rangänderung
(1) Das Rangverhältnis kann nachträglich geändert werden.
(2) Zu der Rangänderung ist die Einigung des zurücktretenden und des vortretenden Berechtigten und die Eintragung der Änderung in das Grundbuch erforderlich; die Vorschriften des § 873 Abs. 2 und des § 878 finden Anwendung. Soll eine Hypothek, eine Grundschuld oder eine Rentenschuld zurücktreten, so ist außerdem die Zustimmung des Eigentümers erforderlich. Die Zustimmung ist dem Grundbuchamt oder einem der Beteiligten gegenüber zu erklären; sie ist unwiderruflich.
(3) Ist das zurücktretende Recht mit dem Recht eines Dritten belastet, so finden die Vorschrift des § 876 entsprechende Anwendung.
(4) Der dem vortretenden Recht eingeräumte Rang geht nicht dadurch verloren, dass das zurücktretende Recht durch Rechtsgeschäft aufgehoben wird.
(5) Rechte, die den Rang zwischen dem zurücktretenden und dem vortretenden Recht haben, werden durch die Rangänderung nicht berührt.

– May the debtor or the land owner object to the transfer of the mortgage? Does the debtor or the land owner have to be informed about the transfer?

The debtor cannot object to the transfer.

– What are the approximate costs for the transfer of a mortgage – and the time required?

– Let us assume that bank 1 does not have a valid claim (as in question 7.3.1). If it transfers the mortgage to bank 2, can the latter still acquire the mortgage in good faith?

Normally, a mere obligation claim cannot be obtained by good faith. However, for the mortgage (*Hypothek*), the good faith is also protected, so that bank 2 can acquire the mortgage by transfer, even if there was not underlying claim (§ 1157 BGB).

– Let us assume that there is a valid claim, but the setting up of the mortgage is invalid. Can bank 2 still acquire the mortgage in good faith?

Then, the good faith is protected by § 892 BGB.

– If bank 1 has transferred the mortgage to bank 2, but bank 1 is still registered, how can bank 2 enforce the mortgage? (Or does bank 1 have to enforce the mortgage?)

If the signatures of the representatives of bank 1 on the assignment have been certified by a notary, then bank 2 may ask for registration and the change of the executionable title.

– If bank 1 has transferred the mortgage to bank 2, but bank 1 is still registered, whose consent is necessary for any changes in the registration (the consent of bank 1 or of bank 2)?

The land register will require the consent of the registed creditor, since it checks only formally.

7.11.2. Transfer to more than one creditor

– Typically the bank may want to split up and syndicate the loan. Can the loan and the mortgage be split up and only a portion be transferred to bank 2? Can portions be transferred to different banks? Could those banks transfer the loans and the mortgage(s) to other banks later?

The bank may split up the mortgage.

§ 1189 BGB regulates the *Grundbuchvertreter* (representative for the land register), who however is rarely used.

7.11.3. Administration of the mortgage by a trustee or fiduciary

– May the mortgage be administered by a trustee or fiduciary? In case of insolvency of the trustee, would the mortgage fall in the insolvency estate?

7.12 Conflict of Laws Issues

The real estate is situated on national territory whereas the debtor (who is also the owner of the real estate) resides in another EU-country.

7.12.1. Bank loan taken by a foreign debtor in the host country

Which law is applicable when the debtor takes a loan with a bank in the host country where the real estate is situated (to the loan contract, the security contract and the mortgage)? Could a law different from the law governing the the property be chosen for the loan contract?

– The loan contract would be governed by the law of the establishment of the bank (Art. 28 EGBGB) (unless chosen otherwise).

– The mortgage is governed by the lex rei sitae (Art. 43 EGBGB).

7.12.2. Bank loan taken in the debtor's country of residence

Which law is applicable when the debtor takes a loan with a bank in his country of residence (to the loan contract, the security contract and the mortgage)?

In this case, the loan contract would be governed by the law of the state where the debtor and the bank have their residence or establischment (unless chosen otherwise). For the mortgage, the lex rei sitae applies.

7.12.3. Bank loan taken in a third EU-country

– Which law is applicable when the debtor takes a loan with a bank in a third EU-country (to the loan contract, the security contract and the mortgage)? Could a law different from the law governing the property be chosen for the loan contract?

7.12.4. National Restrictions on the Right of a Debtor to Secure Debt with a Mortgage assessed under EU Law

Note: The right of a debtor to secure debt with a mortgage has been dealt with by the ECJ in the *Trummer*[33] case, which is a fundamental decision on the relationship of the basic freedoms and real sureties. In this case, an Austrian prohibition on registering mortgages in foreign currencies was at stake. In its decision, the ECJ first confirmed the extension of the scope of the free circulation of capital to mortgages, as these "represent the classic method of securing a loan linked to a sale of real property".[34] Then, the Court found a violation of the freedom right:

> "The effect of national rules such as those at issue in the main proceedings is to weaken the link between the debt to be secured, payable in the currency of another Member State, and the mortgage, whose value may, as a result of subsequent currency exchange fluctuations, come to be lower than that of the debt to be secured. This can only reduce the effectiveness of such a security, and thus its attractiveness. Consequently, those rules are liable to dissuade the parties concerned from denominating a debt in the currency of another Member State, and may thus deprive them of a right which constitutes a component element of the free movement of capital and payments." [35]

Following the ordinary scheme of analysis of the basic freedoms, the Court then went on to examine possible justifications of the violation. In this context, it made a statement of principle as regards real sureties:

> "It should be noted that a Member State is entitled to take the necessary measures to ensure that the mortgage system clearly and transparently prescribes the respective rights of mortgagees *inter se*, as well as the rights of mortgagees as a whole *vis-à-vis* other creditors. Since the mortgage system is governed by the law of the State in which the mortgaged property is located, it is the law of that State which determines the means by which the attainment of that objective is to be ensured." [36]

In the remainder of the case, the ECJ did not, however, accept the Austrian prohibition as a proportional limitation of the free movement of capital. Assuming that the Austrian rule is designed to attain the objective of a clear and transparent mortgage system, the Court reproaches it to enable lower-ranking creditors to establish the precise amount of prior-ranking debts, and thus to assess the value of the security offered to them, only at the price of a lack of security for creditors whose debts are denominated in foreign currencies. In addition, Austrian law is criticised for not operating the choice consistently. Indeed, the Austrian rules allow the

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[33] Case C-222/97, *Trummer and Mayer*, ECR 1999, I-1661; confirmed in case C-464/98, *Stefan*.

[34] ECJ, at no. 23.

[35] ECJ, at no. 26.

[36] ECJ, at no. 30.

value of the mortgage to be expressed by reference to the price of fine gold, which is subject to fluctuations in the same way as the value of a foreign currency. As a result, the Austrian rule was declared incompatible with EU law by the ECJ.

Question: - Does your national law contain other restrictions or de facto disadvantages for foreign debtors which might negatively affect cross border transactions involving real property and therefore fall foul of EU law?

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