The Banking Litigation Law Review

Third Edition

Editor
Deborah Finkler

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THE BANKING LITIGATION LAW REVIEW

THIRD EDITION

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PREFACE

This year's edition of *The Banking Litigation Law Review* demonstrates that the increase in litigation involving banks shows little sign of slowing.

Although disputes arising from the 2008 financial crises are reaching their end, what might be termed 'normal' banking litigation has resumed, and is in no short supply. This crosses the full spectrum from claims by consumers against banks (relating to losses incurred either to the bank or to third parties) to claims by banks for the recovery of loans and the enforcement of guarantees. In all these cases, cross-border issues frequently arise, and banking litigation remains an important source of developments in the conflicts of laws in international commercial litigation.

The context for much of the consumer litigation is the growing – and increasingly complex – range of consumer protection regulation in the various jurisdictions under review. However, while the courts appear content to apply that legislation in order to hold banks to account, its existence – together with the more extensive rights it affords to consumers – has meant that in many parts of the world the courts are less willing to expand consumer rights beyond the context of that regulation, instead preferring to enforce the contractual rights between banks and customers strictly.

In those circumstances, we have seen a growth in the use of class actions and representative claims, often where consumers can take advantage of friendly regulation. These mechanisms are being adopted in countries where they did not previously exist, in some cases by changes in legislation, and in others by changes to court procedure. At the same time, courts in different jurisdictions are reacting very differently to this new or growing type of litigation. In some cases this is by seeking to restrict the circumstances in which such claims can be made but in others by promoting their use. It therefore remains to be seen whether the growth of class actions and representative claims against banks is really a worldwide phenomenon.

These novel forms of litigation, and other more conventional claims, are also subject to a global trend towards making both the courts and, importantly, alternative forms of dispute resolution more available to litigants. We continue to see parties encouraged to settle their claims out of court, by way of general mechanisms such as mediation or by way of specialised banking ombudsmen. Further, some jurisdictions are promoting the use of class or group settlements, which can resolve major disputes with limited court involvement.

At the same time, the impact of data protection legislation, including the General Data Protection Regulation (GDPR) in the European Union, has opened a further means by which claimants can bring claims against banks, which are inevitably major holders of personal data. The use of the GDPR both as a tool in litigation and as a source of complaint or damages in itself is, therefore, a concern for banks, both in a regulatory and in a litigation context. This concern is only likely to grow.

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One bright spot for banks is a general trend in favour of upholding assertions of secrecy, confidentiality and privilege on the part of banks and their advisers against claimants. This is especially important in the context of investigations against banks. In common law jurisdictions in particular, courts now tend to treat such investigations as akin to adversarial litigation and after the concerns raised over the past year or two, now largely accept that many documents created during investigations should be protected by privilege.

Finally, the general political and economic uncertainty around the world remains a probable source of banking litigation, especially where that uncertainty negatively affects investors. Nobody is any closer to being able to say what the political or economic impact of Brexit will be either to the United Kingdom's banking sector or to that of the European Union. It would be dangerous to predict when clarity in this regard will be available.

Deborah Finkler
Slaughter and May
London
November 2019

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Chapter 4

GERMANY

Marcus van Bevern[1]

I OVERVIEW

In the aftermath of the 2008 financial crisis, the financial industry in Germany continues to struggle with the economic environment and particularly with the policy of low interest rates enforced by the central banks to fight the crises. In light of low or even negative interest rates impacting their business models, banks are trying to terminate high-yield long-term saving contracts and, at the same time and corresponding with requests by the banking supervisory agency (BaFin),[2] to strengthen their fee income, thus making their income basis more independent from interest rates. In view of German courts' traditional support of contract compliance and scepticism towards the lawfulness of fees, all these attempts often result in disputes, keeping courts occupied. On an individual basis and despite their overall economic importance, these disputes often concern rather small amounts in dispute. However, there is an increasing tendency for more collective actions supported by the legislature.

II SIGNIFICANT RECENT CASES

i Termination of long-term saving contracts

In a judgment rendered in May 2019, the Federal High Court (BGH) decided that a savings bank had a right to terminate a long-term high-yield savings contract after a contractual term of 15 years had expired.[3] The bank had entered into a savings plan with its customer providing for a graduated interest premium continuously increasing until the 15th anniversary of the contract after which the interest payments remained on the last level and the contract continued for an unlimited period. The BGH decided that the bank's ordinary right of termination was implicitly excluded until the 15th anniversary of the contract, because the customer had the unilateral right to decide whether or not he wanted to reach the highest premium stage. However, after the 15th anniversary, the bank would be entitled to terminate the contract with three months' notice, as the customer had no contractual right for a term exceeding the 15-year period.

The case is in line with two decisions from 2017 in which the BGH had decided that a savings bank with the specific purpose to provide funding for house building was entitled to terminate the contract with a customer 10 years after same customer had fulfilled its

1 Marcus van Bevern is a partner at Kantenwein. The author would like to thank associate Lisa Maria Oettig for her support in the preparation of this chapter.

2 *Die Welt*, dated 15 January 2015, pg 13.

3 BGH, judgment of 14 May 2019, court reference: XI ZR 345/18.

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saving obligation without demanding his or her right to be granted a loan for building a house.[4] Savings banks in the above-mentioned sense are mutual benefit societies offering their customers a right to be granted a building loan after a certain amount of equity has been saved. While in normal times the building loan would be granted at reduced rates (compared to market rates), the current economic environment results in market rates being lower than those for building loans. This is the reason why a lot of savers do not exercise their right to be granted a building loan but use the instrument as a mere savings contract. Thus, the savings banks are under pressure to get rid of such costly deposits.

ii Arrangement fees and charges

Following its landmark decision of 2017,[5] the BGH upheld in a number of decisions that arrangement fees provided for in commercial loan agreements are invalid, if the fee arrangement is to be considered a pre-formulated standard term of business and has not been individually negotiated. According to the law on standard business terms, courts may scrutinise the content of pre-formulated standard business terms and declare such business terms to be invalid if they find that the user of the terms, who wants to unilaterally deviate from what is provided for respective situation in the relevant code, unreasonably disadvantages the other party.

In the above-mentioned decisions, the court clarified a number of follow-up questions. Inter alia, it decided that the rule on the invalidity of the fee arrangement also applies to guaranteed credits where the amount the borrower is ultimately going to draw is uncertain at the beginning.[6] Further, the court held that both the mere denomination for the fee as well as a standard clause containing the borrower's confirmation that the fee had been individually negotiated, are irrelevant for the classification of the clause as an (invalid) pre-formulated standard business term. The court held that such confirmation also violates the law on standard business terms, which prohibits factual confirmations and shifting the burden of evidence to the customer in standard terms. Rather, the bank would have to provide evidence that the clause was actually negotiated individually, which would require the customer to have an actual alternative for conditions without a fee.[7] Attempts to circumvent the economic effects of these decisions range from concluding separate fee agreements governed by another law to concluding waiver agreements providing for a waiver of the right to claim the repayment of the fee. However, as far as can be seen, these type of agreements have not yet been scrutinised by the courts. As a result, there remains a significant risk that any kind of fee arrangements in the context of loan agreements are invalid and must be paid back to the borrower if the borrower demands it.

iii Cum-ex transactions

The number of civil and criminal court proceedings in connection with cum-ex transactions that took place particularly between 2005 and 2009 is likely to increase. There are multiple variants of cum-ex trades. What all trades have in common is that the parties agreed on a share purchase shortly before or on the dividend record date and, therefore, 'cum' dividend. The settlement of the trade, however, occurred after the dividend declaration, so that the

4 BGH, judgments of 21 February 2017, court reference: XI ZR 185/16 and XI ZR 272/16.
5 BGH, judgment of 4 July 2017, court reference: XI ZR 562/15.
6 BGH, judgment of 17 April 2018, court reference: XI ZR 238/16.
7 BGH, judgment of 19 February 2019, court reference: XI ZR 562/17.

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share was delivered 'ex' dividend. This structure made it possible to obtain multiple returns of capital yields tax that had only been paid to the German tax authorities once. Estimates suggest that the damage for European tax authorities amounts to approximately €55 billion.

On the civil law side, a German Higher Regional Court confirmed a ruling holding Swiss bank Sarasin liable for approximately €45 million in damages to an individual investor because of incorrect investment advisory services. The investor had suffered losses after investing into a fund based on the cum-ex trading strategy. The court held that the parties had entered into an implied investment advisory agreement and that Sarasin had failed to properly inform the investor of the functioning and risks of the cum-ex trading strategy.[8]

Another German civil court awarded a €22.9 million damage claim to German bank Helaba. Helaba had invested in a cum-ex product by acting as buyer. However, the tax office retrospectively denied the originally received tax benefit and required Helaba to return the payment.[9] The defendant, a bank that had sold the shares, was at the same time the custodian bank on the seller's side and, therefore, required to pay capital yields tax. The court argued that the defendant not only had violated its obligations towards the tax authorities but also its obligations with regard to Helaba. Not paying the capital yield tax ultimately had led to the tax office denying Helaba its tax benefits. Consequently, the defendant was liable for Helaba's damage. Generally, however, this judgment does not offer a lot of guidance regarding the liability of custodian banks on the seller's side in cum-ex constellations, as the custodian bank on the seller's side often was not the same as the seller of the shares.

On the criminal law side, it is to be expected that the trial before the Bonn district court against two individuals charged with tax evasion in a particular serious case only marks the tip of the iceberg of more criminal proceedings to come. In the event that the behaviour of the accused constitutes a crime, the court may order the confiscation of profits not only from the convicts but also from other natural or legal persons in whose interest the convicts had acted.[10] Accordingly, the court included five financial service providers in the trial and is going to examine whether it is possible to confiscate potential pecuniary benefits from them. In terms of 'deep pockets', this option may appear more favourable to the court than confiscating the profits from the accused.

III RECENT LEGISLATIVE DEVELOPMENTS

i Payment Services Directive 2

As of 13 January 2018, the Revised Payment Services Directive (Directive (EU) 2015/2366 – PSD2) has been implemented into German law. It came fully into effect on 14 September 2019. PSD2 updates the first EU Payment Services Directive of 2007 and extends its scope to all kind of payment services (other than physical or paper-based transactions) provided within the European Union in currencies of the EU member states or the European Economic Area (EEA) as well as – partially – to payment transactions in non EU/EEA currencies (e.g., US dollars), provided that one of the payment service providers is located within the EU or EEA and only with respect to those parts of the payment transaction that are carried out in the Union. Further, the PSD2 introduces strict security requirements for the initiation and processing of electronic payments and data protection.

8 Higher Regional Court Stuttgart, judgment of 14 September 2018, court reference: 5 U 98/17.

9 Reginal Court Frankfurt, judgment of 25 April 2018, court reference: 2-12 O 0262/16.

10 Section 73b German Criminal Code.

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The PSD2 requests transparency of conditions and implements a prohibition of surcharges meaning that extra fees for all kind of transactions, such as credit card payments, wire transfers and debit notes are forbidden. Further, the payer's liability for unauthorised payment transactions is limited to a maximum of €50.

The PSD2 also gives authorised and registered third-party providers (TPP) the right – subject to consent of the account holder – to have access to credit institutions' payment accounts services, which must be granted on an objective, non-discriminatory and proportionate basis (Articles 35 and 36). According to the PSD2 such access shall be extensive enough to allow the TPP to provide payment services in an unhindered and efficient manner. Account access must not be restricted unless it is necessary to safeguard against specific risks. Where a credit institution rejects a request for access, it shall provide the competent authority with duly motivated reasons for the rejection. These provisions aim at promoting technical payment innovation and, at the same time, maintaining the safety of payment transactions and payment services as well as consumer safety.

ii Payment Account Directive

Although the Payments Account Directive (Directive (EU) 2014/92) has already been implemented into German law in 2016, certain information obligations first came into force as of 31 October 2018. Since then, financial institutions are obliged to provide their customers with a stand-alone fee information document and glossary, which must be easily comprehensible and must be presented in a way that is clear and easy to read.

iii New bill on group bankruptcy

On 21 April 2018 the Act on the Facilitation of Group Bankruptcies came into force. The act aims at preventing the rupture of a group of companies in case of insolvency in order to preserve the possibility of reorganisation. Although there is no substantive consolidation and the principle of one proceeding for each insolvent company remains applicable, the act introduced the possibility of having one insolvency forum for the entire group and one single administrator for all insolvent companies plus a special procedure for coordination of the single insolvency proceedings.

iv Initiative for modernisation of the law on standard business terms

In recent years, the BGH frequently held in a number of decisions that pre-formulated standard business terms arranging and handling fees in loan agreements are invalid. Originally, the BGH had developed these principles in connection with consumer cases. Since 2017, the Court has expanded the same view to B2B cases.[11]

In the eyes of the BGH, the only valid consideration owed by the borrower for a loan facility is the interest payment. All these cases left great uncertainty in the financial industry as to the validity of any kind of fee arrangements under German law, such fee arrangements being customary in the financial markets and particularly necessary in the current economic environment. The decision caused fierce criticism, with banks and banking associations claiming that the German financial industry had been disadvantaged in comparison to its international competitors and requesting a differentiation between B2C and B2B business. As a result, there have been various initiatives for a modernisation and liberalisation of the

11 BGH, judgment of 4 July 2017, court reference: XI ZR 562/15.

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existing law. However, consumer protection agencies also strongly support the existing legal situation. In its coalition agreement of 2018, the government promised to scrutinise the law on standard terms of business and its application to B2B businesses. So far no draft bill has been introduced.[12] For the time being the situation regarding the validity of fee agreements remains unsatisfying.

IV CHANGES TO COURT PROCEDURE

On 1 November 2018 the Act on the Determination of Model Proceedings came into effect. It allows specially qualified non-governmental consumer protection associations to initiate model proceedings against private companies in order to determine certain preliminary questions (e.g., whether or not a company acted illegally) with binding effect for the claims individual consumers may have against the company. Consumers may register their claims with an official register administrated by the Federal Ministry of Justice and Consumer Protection. The model proceeding as such will be conducted between the consumer protection association and the company without a direct participation of the consumers. The proceeding ends with a declaratory judgment, which constitutes a binding basis for each subsequent individual claim initiated by the consumers against the company.

The new act completes recent attempts by the German legislature to implement elements of collective redress to the civil procedure in Germany, which has traditionally been strictly bipartisan, and combines various instruments. In 2005, the legislature had adopted the Act on Model Case Proceedings in Disputes under Capital Markets Law, which also aimed at determining preliminary questions for a multitude of parties. Contrary to the new act, model case proceedings in capital markets disputes are admissible for all kinds of parties only if the matter in dispute concerns damage claims resulting from false, misleading or omitted public capital markets information, or is based on a contract under the Securities Acquisition and Takeover Act. This limited scope has been widened significantly under the new act but at the same time the parties admitted to such proceedings have been limited.

The new act was not specifically designed for claims against the financial industry. The immediate cause was Diesel-gate and the wave of claims against the automobile industry. Nevertheless, model proceedings may also be filed against banks. In fact, one out of five model proceedings currently pending with German courts was brought by the consumer organisation of Saxony against the savings bank of Leipzig. The consumer organisation blames the bank of paying too low interest rates and requests a declaration that contractual interest rate fixing clauses used by the bank are invalid.[13]

Also in 2018, the Higher Regional Court of Saxony rendered a judgment in favour of the same consumer organisation declaring fees requested by a Saxon credit institution invalid and ordering the bank to inform its customers about the invalidity as well as to repay the fees to the concerned customers.[14] While the judgment was based on existing law allowing consumer organisations to request a declaration of nullity of standard business terms, it exceeded the legal consequences beyond such declaration, thereby creating a virtual possibility for collective relief.

12 www.bundesregierung.de › blob › 2018-03-14-koalitionsvertrag-data.

13 OLG Dresden, court reference: 5 MK 1/19.

14 OLG Dresden, judgment of 10 April 2018, court reference: 14 U 82/16.

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V INTERIM MEASURES

In general, there are two instruments of interim relief under German law: seizure and injunction. A seizure can be *in rem* in order to secure subsequent enforcement of a monetary claim against movable or immovable property if such enforcement may be jeopardised. Also, a personal seizure can be available by arresting a debtor to ensure compulsory enforcement against the debtor's property when such enforcement is at risk. An injunction can be available to either preserve the status quo or provide for a temporary status of a legal relationship that is in dispute, if such preservation or temporary relief is necessary to avoid the frustration of a party's rights or otherwise to avert significant disadvantages. In all cases, seizure and injunction must not result in a final decision of the dispute. At the discretion of the courts, orders containing seizures or injunctions may be granted *ex parte* or after hearing the counterparty. If the proceedings are not already pending, the court, having rendered the order, is legally obliged to order, upon application by the debtor, that court proceedings have to be commenced within a period to be determined.

In banking law disputes, interim relief is frequently an issue in cases concerning standby letters of credit and similar forms of bank guarantees. This is particularly true when these cases concern cross-border transactions where the applicant suspects that the money, once disbursed to the beneficiary, cannot be successfully reclaimed, because a repayment had to be claimed for and enforced in another jurisdiction. In these constellations, it is undisputed that the applicant (i.e., the debtor in the underlying transaction) may apply for an injunction against the beneficiary (i.e., the creditor in both, the underlying transaction and the letter of credit (LoC)) enjoining him or her from drawing the LoC issued in the beneficiary's favour if the prerequisites for an injunction are met, in particular when there is prima facie evidence that the drawdown would be a misuse of the creditor's rights in the underlying transaction.[15] However, neither the issuing nor the nominated bank are obliged to respect an injunction that has been issued against the beneficiary. The BGH held that an injunction issued against the beneficiary does not provide sufficient evidence of obvious misuse by the beneficiary to call his rights under the LoC, so that the issuing and the nominated bank are not obliged to respect the injunction against the beneficiary.[16]

Applicants often attempt to directly apply for interim relief against the issuing bank enjoining the latter to disburse the LoC towards the beneficiary. On the merits, it is clear that a disbursement of the LoC may only be refused by the bank, if it is obvious and blatantly provable that the beneficiary commits an abuse of contract in drawing the LoC. However, it is disputed whether, even in the case of an abuse by the beneficiary an injunction against the bank is available at all. In the past, courts held that the applicant may hinder its bank from disbursing the LoC to the beneficiary.[17] More recent judgments, however, deny the availability of this measure in general. The courts argue that the issuing bank, when disbursing the LoC, would be acting on its own risk and that the question, whether or not it was entitled (and obliged) to honour the LoC, only had to be decided subsequently when the bank claims recourse against the applicant.[18]

15 OLG Stuttgart, judgment of 20 January 2015, court reference: 10 U 102/14; *Vollkommer in: Zöller* Commentary on the Civil Procedure Code, 32nd edition 2018, Section 940, margin No. 8.

16 BGH, judgment of 10 October 2000, court reference: XI ZR 344/99.

17 OLG Frankfurt, judgment of 3 March 1983, court reference: 10 U 244/82.

18 OLG Stuttgart, judgment dated 14 November 2012, court reference: 9 U 134/12; *Vollkommer in: Zöller*, Commentary on the Civil Procedure Code, 32nd edition 2018, Section 940, margin No. 8.

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As an alternative to the aforementioned interim measures under national German law, the Regulation (EU) No. 655/2014 allows for the possibility of a European Account Preservation Order (EAPO) in order to ensure the subsequent enforcement of a creditor's pecuniary claim by freezing the debtor's bank accounts in cross border cases. With the exception of certain claims (family, inheritance, insolvency and social security law as well as arbitration), the EAPO applies to pecuniary claims in civil and commercial matters, provided either the competent court or the creditor are located or domiciled in another Member State than the one where the bank account is maintained. The preservation order is available in all cases where a judgment has already been rendered or proceedings are pending or even when they shall be initiated. It requires a real risk that the subsequent enforcement of the creditor's claim could be jeopardised and – unless a judgment has already been rendered – sufficient evidence of the likelihood that the creditor will succeed on the merits.

VI PRIVILEGE AND PROFESSIONAL SECRECY

Under the German code of civil procedure there is no general pretrial discovery or disclosure obligation. Each party of a proceeding has to submit the facts and documents supporting its claim. Only under restricted circumstances a court may direct one of the parties or a third party to produce documents, records or any other material in its possession, namely that (1) one of the parties made specific reference to the details of such documents in the course of the proceedings and its relevance for the case and (2) set forth the reasons why the party itself cannot produce the document but believes that the other party is in its possession. In general, the third party could also be an attorney. However, an attorney may not be directed to produce documents, if he or she is entitled to refuse to testify (which is usually the case).

As a result of these restricted rules, document production is scarcely applied for in civil proceedings and the question of privilege and professional secrecy is rarely raised and, therefore, often of no importance in civil proceedings. The BGH recently upheld the very restricted approach to pretrial discovery and document production: The case concerned a consumer credit agreement in which the borrower had exercised its right of withdrawal. Although the law generally provides that, in case of revocation, the contractual performances received by each party as well as the emoluments taken are to be returned, the court rejected a claim by the borrower for disclosure of the bank's specific emoluments taken from the credit amount in dispute. The court argued that there is no specific obligation by the bank to disclose its business secrets, because the consumer could rely on the general assumption that the bank had taken emoluments in the amount of the legal default interest rate.[19]

However, there may be a loophole and the situation may be different, if a civil claim can also be based on criminal offences. In general, attorneys are bound to secrecy and a breach of such duty may constitute a criminal offence. To enforce and protect such duty to secrecy, attorneys also have the right (and obligation) to refuse testimony on matters covered by their duty to secrecy in both, civil and criminal proceedings. Despite this duty to secrecy, criminal investigators have recently confiscated documents and reports held by external lawyers in a number of high-profile cases. For example, Jones Day has been raided in relation to the VW emission scandal and Freshfields has been raided in relation to the near bankruptcy of (former) HSH Nordbank AG. In these cases, the external firms had been hired to conduct internal investigations and have submitted internal investigation reports to their clients.

19 BGH, judgment of 17 April 2018, court reference: XI ZR 446/16.

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Although the criminal procedure code provides that in cases where criminal charges have been brought against a defendant, certain documents – including documents in the possession of the attorney as well as all documents relating to attorney–client communications – are exempted from confiscation by the investigating authorities, the investigators argued that there is no general prohibition to seize such reports and any related documents but that the question of seizure would depend on the individual content of the documents. In particular, the questioning and hearing of employees would not be subject to the 'bond of trust' between the attorney and his or her client, which is protected under the law. Lower courts upheld these decisions.[20] Unfortunately, the question remains unclear and has not yet been decided by higher courts. Though Jones Day filed a constitutional complaint, the constitutional court refused to decide on the merits, arguing that Jones Day as a US-based law firm could not claim a violation of the basic rights under the German constitution.[21]

Once documents have been seized by the investigation authorities, any person having a legitimate interest may demand access to the records and could then also make use of them in civil proceedings. This is also a frequent tactical strategy of claimants in banking litigation cases.

VII JURISDICTION AND CONFLICTS OF LAW

Banking disputes are typically based on contract law. Contracts usually contain choice of law clauses as well as forum clauses usually complying with the Brussels Ia Regulation. Jurisdiction and conflicts of law issues, therefore, rarely play a role in banking law disputes. Only in rare cases are the admission of a party to court and its right to sue discussed. These cases concerned parties that had been founded and had their seat in a jurisdiction outside the European Union but were, in fact, administered in another jurisdiction.

The number of cases dealing with jurisdiction and conflicts of law issues could increase in the case of a hard Brexit, in particular with respect to private limited companies under English law being administered in Germany. In the past, due to lower founding requirements and advantages regarding liability, a significant number of companies that had their administrative seat in Germany made use of English company law. These companies were either limited companies under English law or a combination of a German private limited company with an English private limited company as its general partner (Ltd & Co KG). Despite a number of legal questions and disputes that have arisen in the context, courts tended to generally see these forms of corporations as admissible in accordance with EU law and the freedom of establishment. However, should the UK leave the EU without any treaty, such companies could no longer rely on the freedom of establishment. Instead, German autonomous conflict of law rules would apply providing for the real seat theory instead of the incorporation theory recognised under Anglo-Saxon law. As a result, companies founded and registered in the UK but with their real (administrative) seat in Germany could face serious problems in court disputes, as they could probably be denied admission to the courts. This would not apply, however, to English law companies that also have their administrative seat in the UK.

Further, in case of a hard Brexit, it is to be expected that UK companies filing a lawsuit in Germany could be requested to provide collateral for the defendant's legal expenses, according to the German code of civil procedure. In general, only plaintiffs from outside the

20 LG Hamburg, resolution of 15 October 2010, court reference: 608 Qs 18/10.

21 BVerfG, resolution dated 27 June 2018, court reference: 1287/17, 2 BvR 1583/17.

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European Union or the European Economic Area have to provide a security deposit (e.g., a bank guarantee) for the costs of the proceedings, should the defendant demand so. Exceptions apply if, due to international treaties, no such security deposit may be demanded. Germany and the United Kingdom entered into the Convention for the Reciprocal Recognition and Enforcement of Judgments in Civil and Commercial Matters on 14 July 1960 (the German– British Convention). The convention excluded the provision of security deposits from parties domiciled in either state and was applicable until the Brussels I Regulation came into effect. It is unclear whether the German–British Convention will be automatically reinstated in case of a hard Brexit.

VIII SOURCES OF LITIGATION

Typical scenarios in banking disputes concern mis-selling cases and prospectus liability when the customer relied on incorrect information or flawed advice by the bank, or both. German law provides for an informed investor concept: according to the BGH, the commencement of discussions between a bank and its client concerning the recommendation and purchase of securities or other investments constitutes an implied advisory agreement.[22] This contract imposes a number of secondary obligations on the bank. In particular, the bank has to inquire about the customer's practical expertise and knowledge in the envisaged investment measures as well as his or her risk awareness and financial circumstances including the purpose and intended duration of the envisaged investment. Further, the bank's recommendation has to be based on up-to-date public information and has to reveal all relevant risks. A negligent misstatement is considered a breach of contract resulting in a damage claim for rewinding the sale. Similarly, prospectus liability requires a prospectus to fully, completely and correctly disclose all risks and circumstances relevant for the investment decision.

Mis-selling cases, however, typically follow the cycles in the stock exchange markets with a tendency to increase in bear markets. After a decade of prices on the rise, published cases seem to indicate that German courts are currently not occupied with a lot of mis-selling cases. For the same reason, prospectus liability is currently not playing a big role in the courts' practice. It is to be expected that this may change in a recession.

In recent years, a number of cases for revocation and reversal of consumer loan agreements occupied the courts. While such claims were legally based on the alleged non-compliance of reversal instructions issued by the banks with consumer protection laws, the economic reason behind them was the policy of low interest rates that induced consumers to reverse existing high interest rate loan agreements and secure lower market rates instead. Whereas there are still cases that have been decided recently, the total number of cases seems to decrease after a decade of low interest rates (bearing in mind that the usual fixed interest term is 10 years). Nevertheless, further cases could still be submitted to the courts as a reversal may even be claimed after the loan had been fully repaid.

Given the current economic environment, a number of cases concerning fee and interest issues are pending. The question in dispute is either whether fees requested by the banks are invalid due to a breach of the law on standard business terms or whether and how long banks are bound to long-term high-yield interest rates.

22 BGH, judgment dated 6 July 1993, court reference: XI ZR 12/93.

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IX EXCLUSION OF LIABILITY

Clauses excluding a bank's liability or narrowing the scope of contractual duties in order to reduce the risk of liability are frequently used in contracts. Still, they rarely prevent customers from bringing a case to court. The reason for this is that such clauses are frequently considered general terms of business and are as such, often held invalid by the courts according to the law on standard business terms. Notably, German courts frequently hold that a restriction of liability for a party's main contractual obligation is void.

X REGULATORY IMPACT

Despite increasing regulation, regulatory law has almost no impact on civil law banking disputes. Most disputes are based on contract or statutory provisions under German civil law, (e.g., the German Civil Code). The reason is that German courts frequently hold that regulatory law has no general direct effect in civil law contracts as it serves a different purpose. Only in cases the law explicitly orders so is there a direct effect.[23] Without such explicit order the BGH even refuses to take regulatory law into consideration when only interpreting a civil law contract (unless such contract directly refers to provisions under regulatory law).[24]

Exceptions may apply under the law of torts, which provides for a damage claim in case of a breach of statutory law, provided however, such statutory law is intended to individually protect another person.[25] Whether or not a tort damage claim can be based on a breach of regulatory law depends on the individual statutory provision in dispute. In this respect, German courts are also rather reluctant to grant individual claims, again arguing that regulatory law serves different purposes, in particular to protect the banking system or the public in general but not each individual. For example, whereas the offering of banking services without licence was considered a violation of individual protection, the prohibitions on insider trading, as well as ad hoc publicity and market manipulation, were not considered individual protection laws.[26] Thus, a tort action can only rarely be based on regulatory law.

However, the legislature only recently expanded the scope of action for the BaFin. In 2015 the act for the protection of small investors came into effect. Inter alia, this act allows BaFin to intervene against the sale and distribution of individual financial products causing concerns regarding the protection of investors or considered to be dangerous for the normal course or integrity of the financial markets. Based on this law, the BaFin issued two general decrees in 2019 aiming at the prohibition of binary options and contracts for difference (CFD).[27] According to the German Civil Code, contracts violating these decrees will be held void.[28]

23 BGH, judgment dated 29 April 2014, court reference: II ZR 395/12.

24 BGH, judgment dated 29 April 2014, court reference: II ZR 395/12.

25 Section 823 Paragraph 2 German Civil Code.

26 BGH, judgment dated 7 July 2015, court reference VI ZR 372/14; judgment dated 13 December 2011, court reference: XI ZR 51/10; Wagner in Munich Commentary on the German Civil Code, 7th edition 2017, margin No. 505 et seq.

27 see www.bafin.de; references: VBS 7-Wp 5427-2018/0046 and VBS 7-Wp 5427-2018/0057.

28 Section 136 German Civil Code.

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XI OUTLOOK AND CONCLUSIONS

It is to be expected that the overall economic situation will remain difficult in the upcoming months and that ECB's policy of low interest rates will continue. In such a market setting the banks will keep on struggling with long-running high-yield contracts and trying to raise their fees.

It can be expected that collective action will further be on the rise. This is not only because there is a general trend for more collective action in continental legal systems aiming for more (cost-) efficient court proceedings. As outlined above, one of the recent developments is that consumer protection agencies increasingly try to use instruments for collective relief. Furthermore, international law firms entered the German market and are also trying to foster collective action. In summary, it is to be expected that such cases will increasingly occupy courts.

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Appendix 1

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