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IN-HOUSE LAWYER UNDER THE NEW GERMAN LEGISLATION[1]

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ABSTRACT

Recently professional regulations regarding in-house lawyers have undergone a serious change that will profoundly change their occupational profile. This paper illustrates the legislative process that led to the new regulatory framework. It further discusses the potential problems arising from the cornerstones of professional conduct on the one hand and the typical daily tasks of in-house lawyers on the other hand.

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1 This article is based on a presentation for the International Legal Ethics Conference VII: *The Ethics & Regulation of Lawyers Worldwide: Comparative and Interdisciplinary Perspectives* in New York City from 14th – 16th July 2016.

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I. INTRODUCTION

They say that hard cases make bad law.[2] The following paper focuses on a legislative process in Germany in which the lawmakers followed the path of least resistance and produced a new regulatory framework for the legal profession without due justification. Following two decisions by the Federal Social Court of Germany in 2014, in which the Court held that the occupational field of in-house counsels is profoundly different from that laid out in the German Federal Lawyers' Act, a new statutory regulation for said professional group was passed and came into force by 1 January 2016.

Admittance to the bar is mandatory for lawyers in Germany and according to the Federal Bar Association's annual statistics approximately 164.000 lawyers were admitted in Germany in 2015.[3] With a population of around 82 million[4] this translates to about 200 lawyers per 100.000 citizens. In comparison, at a population of around 320 million[5] there are roughly 1.3 million attorneys[6] in the United States which results in a ratio of 400 lawyers per 100.000 citizens. The aforementioned new regulation in Germany addresses about 40.000 in-house lawyers.[7] The term 'in-house lawyer' in the context of this paper refers to lawyers who are employed at a company or corporation which is not a law firm. This distinction is essential to understand the dimension of the legislative change. The new regulation stipulates that in-house counsels as well as lawyers fall within the scope of said law. This alignment is bound to raise questions how an in-house lawyer can reasonably be expected to adhere to the same standards of professional conduct that an independent lawyer has to honor. Professional independence on the one side and being subject to directions by their superiors within the company, namely the board, might create a constant field of tension for in-house counsels. Focusing on the cornerstones of professional conduct certain issues become apparent.

II. STATUS OF THE IN-HOUSE COUNSEL BEFORE THE LEGISLATIVE CHANGE WITHIN THE FEDERAL LAWYERS' ACT

Before the new regulations came into force, academic literature assumed that an in-

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2 Hodgens v. Hodgens (1837), quoted in FRED SHAPIRO, THE YALE BOOK OF QUOTATIONS (2006).

3 German Federal Bar Association, *Member statistics*, Jan. 1, 2015, *see*: http://www.brak.de/w/files/04_fuer_journalisten/statistiken/2015/grmgstatisitik2015.pdf.

4 Federal Statistical Office, *Press release of Aug. 26, 2016 – 295/16*, *see*: https://www.destatis.de/DE/PresseService/Presse/Pressemitteilungen/2016/08/PD16_295_12411pdf.pdf?__blob=publicationFile.

5 United States Census Bureau (Jan. 15, 2017, 7:11 PM), *see*: https://www.census.gov/topics/population.html.

6 American Bar Association, *National Lawyer Population Survey* (2015).

7 *Legislative draft on the regulation of the legal profession of in-house lawyers* 13 (BT printed matter 18/5201, June 30, 2015).

house counsel could fulfill two rather different functions: On the one hand, the in-house counsel held an employment which was subject to directives by the employer; on the other hand, he could have a second occupation as a lawyer in the sense of the Federal Lawyers' Act.

The first was not considered to be typical attorney work and as such would not have to conform to the professional standards and duties set out in the Act. In his second occupation as a lawyer he was barred from representing his employer in court or in front of arbitral tribunals, cf. § 46 Federal Lawyers' Act (old version). This prohibition to represent the employer in court came into effect only in proceedings where the representation by a lawyer is mandatory. In any other proceedings, the in-house counsel could still be present as his employer's representative.[8] For the second occupation as a lawyer to be permissible, the Act required to conform with § 7 no. 8 Federal Lawyers' Act. This provision states that the applicant's envisioned occupation needs to be consistent with the profession of a lawyer in the sense of the Act. In particular, his status as an independent agent in the administration of justice and the general confidence in his professional independence must be upheld. This two-fold approach was based on a case-by-case assessment and its general compliance with the statutory regulation in § 7 no. 8 Federal Lawyers' Act was judicially accepted.

III. LEGISLATIVE BACKGROUND FOR THE NEW REGULATION AND ITS EFFECTS

The legislators aimed to ensure the pension entitlements for in-house lawyers which were endangered after rulings by the Federal Social Court. As a background, lawyers admitted to the bar are exempted from the general pension systems to which all employees have to contribute according to a statutory scale. The entitlement to the lawyers' pension fund is considerably higher compared to the state managed pension funds. This monetary incentive seems to have been the motivation for the respective interest groups to promote the legislative alignment of in-house lawyers and lawyers which ultimately led to a legislation which affects only a limited number of in-house lawyers and which results in significant conflicts regarding professional conduct. In a broader sense, it is a remarkable example for the underlying drivers in a law-making process.

A. Decisions of the Federal Social Court in 2014

With the legal amendment of the Federal Lawyers' Act, the legislator responded to two rulings by the Federal Social Court of April 3, 2014 (B 5 RE 13/14 R[9] and B 5 RE 9/14

8 WILHELM FEUERICH & DAG WEYLAND, COMMENTARY ON THE FEDERAL LAWYERS' ACT, § 46 para. 20 (9th ed. 2016).

9 *BSG: Versicherungspflicht in der gesetzlichen Rentenversicherung für Syndikusanwälte*, NEUE JURISTISCHE WOCHENSCHRIFT, 2743 (2014).

R[10]).

While it might seem odd at first sight that the decisions of the Federal Social Court led to a legislative change in the regulations regarding the legal profession, the reason for this peculiarity lies in the exemption from the statutory pension obligation for lawyers. According to § 6 (1) no. 1 Volume VI of the Social Insurance Code a lawyer can be exempt from such obligation and instead be a member of the lawyers' pension fund. This is generally considered to be preferable to the statutory pension scheme. The members of the lawyers' pension fund pay a certain percentage of their income which is oriented on the contribution rate of the statutory pension scheme. While the latter generates the pensions of its members by way of an apportionment procedure, the lawyers' pension fund achieves higher returns by means of capital-forming investments.

In the above-mentioned decisions, the Federal Social Court held that the status of an in-house counsel was not comparable to the occupational profile of a lawyer as required by the Federal Lawyers' Act with its accompanying professional duties.
The reaction to the ruling were controversial. While some would have preferred to have the issue dealt with in social legislation[11], especially the Federal Association of In-house counsels and other interest groups strongly supported a regulation in the Federal Lawyers' Act[12]. The legislator finally opted for the latter option and incorporated the occupational field of an in-house counsel in the Act.

B. The Federal Lawyers' Act of 2016

The new Act came into force by 1 January 2016. Apart from the content-related changes, the law introduced a linguistic alteration. In its § 46 (2) Federal Lawyers' Act the term 'in-house lawyer' is now used to emphasize the new status. The new regulations stipulate that in-house lawyers are lawyers within the scope of the Act and as such have to adhere to the same standards of professional conduct that an independent lawyer has to uphold. The new Act outlines the necessity that the in-house lawyer's occupation must be characterized by professional independence, cf. § 46 (3) Federal Lawyers' Act. In addition to this content-related requirement, the Act provides for a formal condition, namely the admission to the bar, §§ 46 (2), 46 a Federal Lawyers' Act. The local bar association will decide about the applicant's request to be admitted as an in-house lawyer and grant the request if the in-house lawyer fulfills the general requirements to be admitted

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10 *BSG: Keine Befreiung von der gesetzlichen Rentenversicherungspflicht für Syndikusanwälte (hier: Vorstandsreferent) und Compliance*, 39, ZEITSCHRIFT FÜR WIRTSCHAFTS- UND BANKRECHT, 1883 (2014).

11 Reinhard Singer, *Advisory opinion on the legislative draft on the regulation of the legal profession of in-house lawyers* 5 (Jan. 15, 2017, 5:17 PM), *see*: (https://www.bundestag.de/blob/381030/2dc3a0b17d11cae3bd98979b8b7671c1/singer-data.pdf).

12 Federal Association of In-house counsels, *Opinion on the position paper of the Federal Ministry of Justice and Consumer Protection* 2 (Feb. 18, 2015) (http://www.buj.net/resources/Server/BUJ-Stellungnahmen/BUJ_Stellungnahme_150218.pdf).

as a lawyer in the sense of § 4 Federal Lawyers' Act, provided that no reasons for a rejection of an application for admission exist, § 7 Federal Lawyers' Act, and the professional activity of the in-house lawyer complies with the standards set out in § 46 (2) - (5) Federal Lawyers' Act. Once the local bar association has decided about the in-house lawyer's admission, the competent pension insurance institution is bound by this decision and has to decide correspondingly with regard to the exemption from the statutory pension scheme, § 46 a (2) Federal Lawyer's Act.

At the same time the new regulation did not significantly extend the in-house lawyer's right to represent its employer in court. The in-house lawyer's right to act for his employer in court is still limited to proceedings where representation by a lawyer is not mandatory, § 46 c (2) Federal Lawyer's Act. The significant change in the Act does not concern the in-house lawyer in his function as an employee but rather his second occupation as a lawyer. Contrary to the old regulation, the in-house lawyer may now, not in his position as in-house lawyer, but in his function as a lawyer represent his employer. This result can be inferred from § 46 c (2) Federal Lawyer's Act by means of a contrario reasoning. This provision prohibits the representation in criminal or administrative offence proceedings. Neither in his function as an in-house lawyer nor within his potential second occupation as a lawyer may the in-house lawyer represent his employer or his employer's employees, § 46 c (2) Federal Lawyers' Act. In contrast to the old regulation, this provision does not stipulate a general prohibition for the in-house lawyer to act for his employer as a lawyer. Consequently, the employer can instruct his own in-house lawyer even in proceedings where representation as a lawyer is mandatory as long as he is formally instructed in his occupation as a lawyer.

The above-mentioned provision contains also one of the inconsistencies and uncertainties of the new regulation. The statutory definition of the in-house lawyer in § 46 (2) Federal Lawyer's Act should not detract from the fact that there is still the possibility for legal professionals, who are employed by a company or corporate group and work in their legal departments, to retain the status of an in-house counsel – as before – without the in-house lawyer's professional rights and obligations under the Federal Lawyers' Act. These in-house counsels are not mentioned in § 46 c (2) Federal Lawyers' Act which, consequently, does not apply to them. Provided the lawyer was not involved in the same matter within his occupation as an in-house counsel he can represent his employer or other employees in criminal or administrative offence proceedings within his second occupation as a lawyer.[13] Exactly this difference in treatment is commonly mentioned as one of the inconsistencies the new regulation has created.

[13] Martin Henssler & Christian Deckenbrock, *Keine Zulassungspflicht für Alt-Syndizi mit gültigem Befreiungsbescheid*, NEUE JURISTISCHEN WOCHENSCHRIFT, 1345, 1350 (2016).

IV. CORNERSTONES OF PROFESSIONAL CONDUCT

The year 1987 marked a turning point for the regulation of the lawyers' professional conduct in Germany. On 14 July 1987, the Federal Constitutional Court decided that the Code of Ethics and Professional Conduct by the Federal Bar Association could not supplement the rather general provision in § 42 Federal Lawyers' Act (old version). The Court held that the Code constitutes an interference with the constitutionally protected occupational freedom (cf. Art. 12 (1) Basic Law for the Federal Republic of Germany) and lacks the required democratic legitimization, in particular because the Federal Lawyers' Act at that time did not contain any provision that transferred the competence to issue regulations on professional conduct on the Federal Bar Association or any other interest group.[14]

To comply with the decision of the Federal Constitutional Court the legislator incorporated the general standard for professional conduct as well as the possibility to supplement this standard in a code of professional conduct given by the Statutory Assembly of the Federal Bar Association, see §§ 59b, 191a Federal Lawyers' Act.[15] The Statutory Assembly made use of authorization and agreed on Rules of Professional Practice for Lawyers.

As a general professional standard, the law stipulates in § 43 Federal Lawyers' Act that a lawyer must practice his profession conscientiously. The following provision in § 43a Federal Lawyers' Act lists a number of basic duties. The enumeration contains inter alia the lawyer's obligation to professional secrecy and the prohibition to represent conflicting interests. These duties as well as the prohibition to approach the other party apply for the in-house lawyer as well as any other lawyer.[16]

In its §§ 113 ff. the Federal Lawyers' Act deals with sanctions for breaches of duty by the Lawyers' Disciplinary Court, which is the competent authority to decide about such offenses. These sanctions include warnings, fines or – for severe violations – even the exclusion from the legal profession, § 114 Federal Lawyers' Act.

V. POTENTIAL DIFFICULTIES FOR IN-HOUSE LAWYERS UNDER THE NEW ACT

As mentioned before the in-house lawyer is subject to the general professional standards for lawyers. In-house lawyers are now challenged to structure their workplaces in a way

14 BVerfGE, NEUE JURISTISCHE WOCHENSCHRIFT, 191 (1988).

15 WILHELM FEUERICH & DAG WEYLAND, COMMENTARY ON THE FEDERAL LAWYERS' ACT § 43a para. 1 (9th ed. 2016).

16 Christian Wolf, *Sozialrechtliche, arbeitsrechtliche und berufsrechtliche Implikationen für den Syndikusrechtsanwalt*, BUNDESRECHTSANWALTSKAMMER-MITTEILUNGEN, 9 (2016).

that conforms to the standards set out by the law. While some problems might be solved by a new organizational structure within the in-house lawyer's legal department, other might require a rework of the new Act by the legislator. In view of the above, independence, professional secrecy and potential inherent conflicts of interests shall be touched upon with regard to problems that in-house lawyers will likely encounter.

A. Independence

The legal profession is traditionally an independent one. Professional independence is the striking characteristic commonly associated with the legal profession. Inventing an in-house lawyer with the same professional duties as a regular attorney creates a legal minefield for this profession. The new regulation tries to harmonize the in-house lawyer's employment with the characteristic professional independence by stipulating that professional independence has to be – contractually and factually – ensured by the employer, cf. § 46 (4) Federal Lawyers' Act. The law recognizes that personal independence is impossible for the in-house lawyer and instead deems it sufficient if he is professionally independent. This has been aptly described as 'independence within dependence'.[17] The delimitation issues seem to be endless in this contradictory legal framework.

B. Professional secrecy

Professional secrecy is one of the cornerstones of the legal profession. Strict secrecy between the lawyer and his client is essential to establish a relationship of trust.[18] The respective provision within the Federal Lawyers' Act can be found in § 43 (2) as well as in § 2 Rules of Professional Practice for Lawyers. In order to effectively enforce professional secrecy, the law provides several provisions to safeguard confidentiality within the professional relationship between the lawyer and his client. On the one hand violating the obligation of professional secrecy constitutes a criminal offence, § 203 (1) no. 3 Criminal Code, on the other hand the lawyer has the right to refuse to give evidence (§ 53 (1) no. 3 Code of Criminal Procedure; § 383 (1) no. 6 Code of Civil Procedure; § 84 (1) Code of Procedure of Fiscal Courts, § 102 Fiscal Code). The common objective of these provision is to protect the professional relationship between lawyer and client.[19]

Since the new regulation came into effect, the rules regarding professional secrecy in the Federal Lawyers' Act and the Rules of Professional Practice for Lawyers apply to in-house lawyers as well. They have to keep information which has become known to them in their professional practice confidential. The evident problem in this context is to

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17 Volker Römermann & Tim Günther, *Syndikusrechtsanwalt – der (un)abhängige Rechtsallrounder mit der besonderen Lizenz*, NEUE ZEITSCHRIFT FÜR ARBEITSRECHT, 71, 72 (2016).

18 Martin Henssler, *Das anwaltliche Berufsgeheimnis*, NEUE JURISTISCHE WOCHENSCHRIFT, 1817 (1994).

19 BVerfGE, NEUE JURISTISCHE WOCHENSCHRIFT, 1305 (2004); WILHELM FEUERICH & DAG WEYLAND, COMMENTARY ON THE FEDERAL LAWYERS' ACT § 43a para. 12 (9th ed. 2016); VOLKER RÖMERMANN, COMMENTARY ON THE FEDERAL LAWYERS' ACT § 43a para. 32 (12th ed. 2016).

exactly define the attorney-client-relationship. At first glance, the professional relationship will be established between the in-house lawyer and the respective employer binding the in-house lawyer to secrecy. The situation will become more complicated if the in-house lawyer is not only advising his employer, but also subsidiaries within the corporate structure of the employer. Would the in-house lawyer be obligated to report to the management of the parent company about the legal problems and his advice to the management of the subsidiary? Does the attorney-client-relationship only exist between the employing company and the in-house lawyer or is it possible for the in-house lawyer to have several different clients in one corporation? Is the in-house lawyer in a legal department which advised several companies within a corporate group then forbidden to share information within said corporate structure? The legislator obviously did not envision such scenario which will be the unfortunate reality for many in-house lawyers under the new regulation.

Furthermore, this obligation to uphold professional secrecy generally corresponds with the lawyer's right to refuse to give evidence. However, the legal situation for the in-house lawyer differs with respect to the kind of proceedings. In civil court proceedings as well as proceedings which refer to the respective rules in the Code of Civil Procedure the in-house lawyer may refuse to testify. The relevant provision can be found in § 383 (1) no. 6 Code of Civil Procedure which grants '[...] persons to whom facts are entrusted, by virtue of their office, profession or status, the nature of which mandates their confidentiality, or the confidentiality of which is mandated by law, where their testimony would concern facts to which the confidentiality obligation refers' a right to refuse testimony. Correspondingly, professionals in the above-mentioned sense are under no obligation to provide or produce documents to the extent that they are entitled to refuse testimony, § 142 (2) Code of Civil Procedure. However, in criminal proceedings the situation is quite different. The in-house lawyer is neither entitled to refuse testimony, § 53 (1) no. 3 Code of Criminal Procedure, nor is his correspondence privileged, § 97 Code of Criminal Procedure – irrespective of whether or not his professional activity includes typical attorney work like legal counseling or other business advice for his employer.[20] While one might name valid reasons for this difference in treatment particularly with regard to an effective law enforcement against large corporations, the law shows yet again an inconsistency the legislator has created by changing the professional regulations of in-house lawyers instead of amending social legislation to solve the initial problem.

C. Conflict of interest

The prohibition to represent conflicting interests can be found in § 43a (4) Federal Lawyers' Act. Its basis is the trustful relationship between the lawyer and his client, ensuring the independence of the lawyer and the public interest in his role in the administration

[20] JÜRGEN-PETER GRAF, COMMENTARY ON THE CODE OF CRIMINAL PROCEDURE § 53 para. 12 (26th ed. 2016).

of justice. These objectives are inseparable and interconnected.[21] The prohibition is further regulated in § 3 (3) Rules of Professional Practice for Lawyers. Additionally, a violation could constitute a criminal offence, § 356 Criminal Code. These provisions have the common purpose to protect the individual and general trust in the legal profession.[22] Once the lawyer realizes that a conflict of interest occurs, he has to inform his clients immediately and must cease to act for all clients involved in the same matter, § 3 (4) Rules of Professional Practice for Lawyers.

It is controversially discussed whether the conflict of interest has to be determined from a subjective or objective point of view. It is mostly assumed that the interest has to be determined subjectively according to the party's intention. Even scholars, who favor an objective determination with respect to the various protective purposes of § 43a (4) Federal Lawyers' Act, concede that such conflict can be resolved if the involved parties know about their different interests and still explicitly agree to be represented by the same lawyer. Consequently, despite their different starting point, both interpretations will ultimately lead to a similar result.[23]

The in-house lawyer may legally advice and represent his employer in its legal matters, § 46 (5) Federal Lawyers' Act. The provision explicitly specifies that this includes legal matters of affiliated enterprises in the sense of § 15 Stock Corporation Act. To put it in rather harsh terms, one might say that a conflict of interest is immanent in such circumstances.

The representation of one company itself might lead to difficulties with respect to the conflicting interest of the involved persons. In complex corporate matters the lawyer as well as the in-house lawyer needs to strictly distinguish whether he acts for the corporation, its shareholders, the executive management or even the supervisory board.[24] If the in-house lawyer is employed to advise more than one company within one corporate group the risk of conflicting interests between these affiliates increases.

The prohibition to represent conflicting interests does not only concern each individual lawyer but extends to all lawyers who are connected in a joint practice or even through shared office premises, § 3 (3) Rules of Professional Practice for Lawyers. The new Act as well as the Rules of Professional Practice for Lawyers remain silent on the question whether or not a legal department consisting of in-house lawyers are considered to be such joint practice. During the legislative process this question was raised by the Federal Bar Association in its opinion on the legislative draft. The Federal Bar Association ex-

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21 BVerfGE, NEUE JURISTISCHE WOCHENSCHRIFT, 2520 (2003).

22 VOLKER RÖMERMANN, COMMENTARY ON THE FEDERAL LAWYERS' ACT § 43a paras. 163 f. (12th ed. 2016).

23 VOLKER RÖMERMANN, COMMENTARY ON THE FEDERAL LAWYERS' ACT § 43a paras. 181 ff. (12th ed. 2016).

24 VOLKER RÖMERMANN, COMMENTARY ON THE FEDERAL LAWYERS' ACT, § 43a para. 173 (12th ed. 2016).

pressed the view that legal departments must be treated the same way as the typical joint practice – the law firm.[25] Consequently, the prohibition to represent conflicting interests would also concern the in-house lawyer's colleagues within their joint practice and substantially complicate the organization and work in the legal departments of large corporations. Without considerably restructuring the work process in the legal departments (e.g. Chinese walls) or creating new positions in each company, compliance with the professional regulations seems almost impossible under the new legislation.

These considerations show that the legislator seems to have paid little attention to the economic reality that in-house lawyers commonly not only act for one company, but for all companies within one corporate group. He himself will have to decide towards whom he feels obligated to maintain loyalty. In reality, one can hardly picture a situation where that internal conflict will not be resolved in favor of the employer paying the monthly salary.

VI. CONCLUSION

In view of the above, it appears that the legislator almost overeagerly reacted to the Federal Social Court's ruling. Dismissing to solve a social law problem within the respective field of law and developing new regulations in less than two years seems attributable to the significant political interference of lobby groups who opted for such a solution. It seems that the legislator chose the path of least resistance. Amending the social securities laws might have led to much broader discussion with the stakeholders and would most likely have provoked a discussion about the principle question why certain profession, such as the legal profession and other independent professions, are exempt from the statutory pension scheme.

Instead the legislator chose to change the regulations of the legal profession and, thereby, created regulations that assign a different legal status to legal professionals, who are essentially doing the same work. The formal requirement of the admittance to the bar cannot distract from the fact that the in-house lawyer's and the in-house counsel's occupation is hardly different. As a consequence of the new regulation, some legal professionals in the same legal department might be subject to professional regulations while their colleagues still operate under the old status of in-house counsel. This issue has raised the question whether legal professionals who fulfill the requirements set out by the law to be admitted as an in-house lawyer are obliged to make a request to that effect or if the admission is optional.[26]

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[25] Federal Bar Association, *Opinion No. 17/2015 on the Ministerial Draft for the regulation of the legal profession of in-house lawyers* 7 (May 2015).

[26] Martin Henssler & Christian Deckenbrock, *Keine Zulassungspflicht für Alt-Syndizi mit gültigem Befreiungsbescheid*, NEUE JURISTISCHE WOCHENSCHRIFT, 1345, 1349 (2016).

It will be the task of the legislator to answer this question as well as find a solution for the inconsistencies in the course of a review of the new regulations.