



Commercial Dispute Resolution

A Comparative Study of Resolution Procedures in Germany

– Summary –

Introduction

In recent years, Germany has seen a significant increase in interest for out-of-court resolution of disputes between companies. In November 2004, PricewaterhouseCooper's Dispute Analysis & Investigations Department and the European University Viadrina Frankfurt / Oder¹ explored this development with two objectives:

- to assess current corporate preferences and expectations in handling disputes under civil law; and
- to identify the need for changes and future trends in civil dispute resolution.

For this purpose, responses to an anonymous questionnaire from 158 companies in Germany have been evaluated.

The survey was based on six types of dispute resolution procedures – negotiation, litigation, arbitration, expert determination, conciliation and mediation. The results were published in April 2005 in the PwC study, “Commercial Dispute Resolution – A Comparative Study of Resolution Procedures in Germany”, of which this is a summary.

Utilization of dispute resolution procedures

It was no surprise to find that negotiation and litigation are by far the most frequently used methods in settling disputes. However, the study's major finding proved surprising – at least at first sight. Corporate perceptions and expectations about which dispute resolution procedure should be adopted do not correspond in certain cases with the actual procedure eventually chosen. The discrepancy between perception and conduct appears in two areas:

- Litigation, the procedure most frequently used, is perceived to be least beneficial in many respects;
- Procedures involving out-of-court dispute resolution with the support of third parties, which are generally perceived to be relatively beneficial, are used very rarely.

Despite widespread knowledge of these alternative procedures, most of the companies surveyed primarily use negotiation and litigation for both national and international disputes. Indeed, 17 % of the companies who responded use only these two types of procedure.

Trends in dispute management

Overall, the survey has identified a trend towards systematic conflict management. This increases significantly in direct proportion to

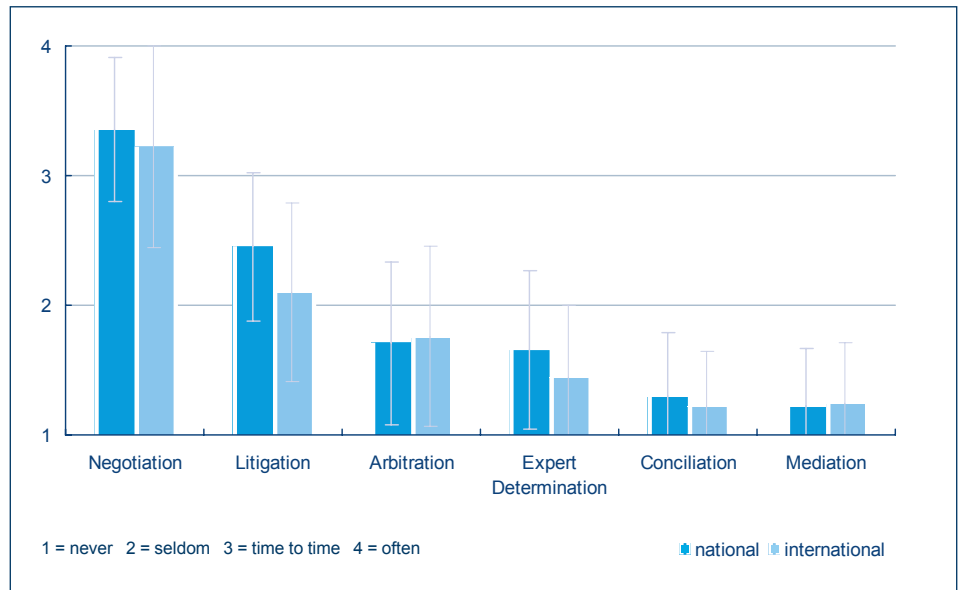


Fig. 1: Frequency of use of the procedures

Nevertheless, 80 % of companies have gained some (initial) experience with arbitration, expert determination, conciliation, and mediation. 28 % of the companies covered by the survey responded that they have already used mediation in resolving disputes. The willingness to use such procedures increases in line with the company size.

The main reasons for using court proceedings specified in the survey – i.e. the failure of previous procedures, legal action taken by the other party or a lack of willingness by the other party to consider other procedures – indicate that court action is perceived to be inevitable. However, specific advantages which are only provided by litigation were considered to be virtually insignificant.

If out-of-court dispute resolution procedures are chosen, such actions are justified mainly by corporate philosophy or by pre-existing agreements – in particular contractually defined arbitration or mediation clauses.

company size. Decisions for selecting dispute resolution procedures are taken mainly by corporate lawyers and secondly by company management. One difference is in the size of the company: in the case of small companies, management tends to take the decision, whereas the influence of the legal department rises along with an increase in company size.

Appraisal of the dispute resolution procedures

Key selection criteria for procedures such as the dollar amount involved, the sensitivity of issues being addressed, the potential financial impact, and the strength of business relationship have been presented to the companies surveyed. Where the dollar amounts involved are high, negotiation is the first choice, followed by litigation, arbitration and expert determination as equally preferred options. If, on the other hand, the dispute is of a sensitive nature, financially important or intensive business related, mediation or conciliation are the preferred options.

With regard to the question as to what benefits, (measured in terms of costs and duration of the procedure, the quality of results, sustainability, maintenance of business relations,

confidentiality and party autonomy), can be attributed to the various procedures, the discrepancy between reality and perception is particularly striking.

Participants in the study have a differentiated perception of the benefits associated with specific procedures. Negotiation received the highest value in all categories (from 77 % to 99 %), whereas court proceedings achieved the lowest values (with the exception of two categories: sustainability and quality of results).

On the basis of the overall assessment, negotiation was rated the most beneficial approach, followed by mediation, conciliation and expert determination. After arbitration, litigation is perceived to be by far the least beneficial approach.

continuation of business relations, the quality of results, and the duration of procedure. Whereas the expert determination is perceived to be very similar to arbitration in terms of quality of results and confidentiality, it is perceived to be much better in the categories of costs of procedure, duration of procedure and party autonomy.

Mediation is constantly in second place with figures varying between 68 % to 93 % (with the exception of the categories of quality of results and the sustainability of dispute resolution). Compared with other procedures, conciliation is perceived to be relatively similar to mediation. However, the absolute advantages of conciliation across all categories are on average nine percentage points behind those of mediation.

- In the handling of disputes, major emphasis is given to the continuation of existing business relations.
- And finally, along with the desire to influence the procedure and result, survey respondents strongly agreed with the statement, "Cooperation and safe-guarding of one's own interests are not mutually exclusive."

Discrepancies and initial explanations

The discrepancy between the dispute resolution procedures chosen by companies and their perceptions as to the different procedures' benefits is clear:

- Parties initially choose negotiations as their preferred procedure and then have recourse to court proceedings, although they consider litigation as the least beneficial procedure.
- The advantages of out-of-court procedures are perceived in a differentiated manner; however, in practice, they are still of minor significance.

The study does not provide any conclusive findings regarding the reasons for the discrepancy between perception and reality; instead, it provides several indicators.

Little practical experience still does not sufficiently underline theoretically existing convictions. The study shows that, with increasing company size, the frequency with which out-of-court procedures are used also increases. In combination with an equally increasing influence of the legal department, this appears to point to broader knowledge and systematic conflict management, which takes greater advantage of the different benefits of procedures.

Finally, if the reasons for choosing litigation are considered (legal action instituted by the other party and the unwillingness of the other party to consider out-of-court procedures), the following conclusion could be supported: a structured approach to dispute resolution is required in advance of a dispute arising. This will help reduce the gap between the initial perception of which procedure would

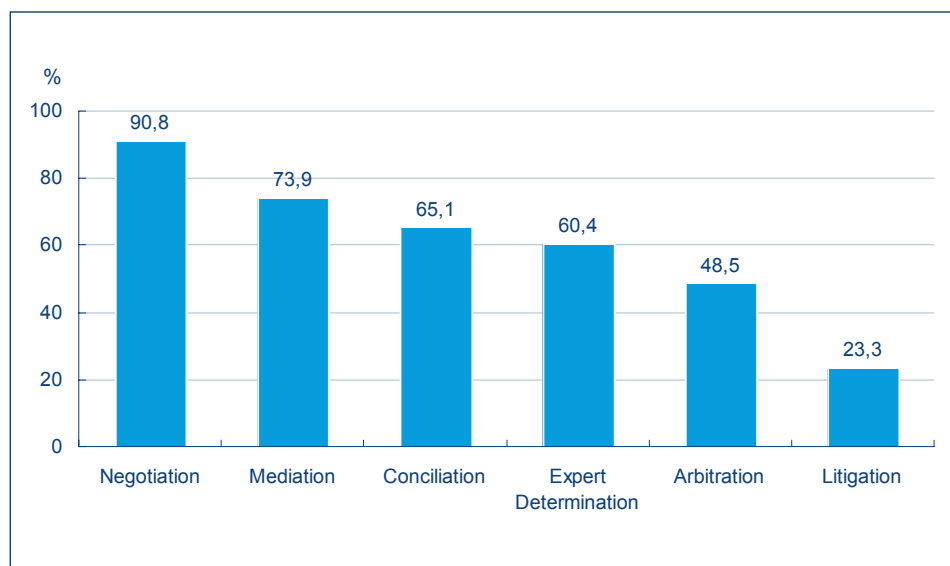


Fig. 2: Advantages of the procedures²

With ratings of 70 % to 75 %, arbitration is considered the most beneficial procedure in relation to three criteria: the quality of results, the sustainability of the dispute resolution and confidentiality. The perception profile of arbitration is very similar to that of litigation. However, there are significant differences in the evaluation of these two proceedings in the categories of confidentiality, duration of proceedings and continuation of business relations, where arbitration is perceived to be much more beneficial.

The major advantages of expert determination, with ratings of 50 % to 73 %, are evident in the categories of confidentiality, the subsequent

The discussions concerning the advantages and disadvantages of dispute resolution procedures are based on numerous assumptions. According to survey findings, the following statements generated the highest approval:

- German companies have a clear desire for greater cooperation between management and the legal department for the purpose of dispute management.
- With regard to the choice of dispute resolution procedure, it is very important for corporate decision-makers that the risks associated with a particular procedure are known and manageable. On the other hand, cost is of relatively minor significance in the choice of dispute resolution method.

² A figure of 80 % means that the relevant procedure, averaged over all eight categories, is perceived to be beneficial by 80 % of the participants.

be most beneficial and the subsequent action of choosing a different procedure.

Overall, the perceptions and preferences of the surveyed companies, as well as the trends evident in larger companies, indicate that the advantages of out-of-court procedures will be exploited to a greater extent in the future. According to survey results, of greatest promise are procedures or combinations of procedures that provide autonomy for the parties similar to that available through negotiation – along with the advantages of support by third parties such as independent experts, mediators, conciliators etc.

Conclusion and outlook

In view of the discrepancy between actual choice of procedure and

perceptions as to the benefits of dispute resolution procedures, the process could be optimised by companies taking better advantage of the entire range of available procedures – in particular out-of-court procedures involving third party support. Increasing companies' experience in the use of out-of-court procedures appears to be a high priority. In this respect, the study clearly shows that structured implementation of out-of-court procedures has a much greater impact than ad-hoc, point-by-point approaches. Such measures include the wide-spread routine use of differentiated dispute resolution clauses in contracts (in particular price adjustment clauses) or the inclusion of dispute resolution preferences in corporate philosophy.

Training internal decision-makers in the entire range of dispute resolution

procedures would appear to be another valuable strategy. Such training must communicate, in particular, the importance of assessing the situation-specific benefits and risks of the procedures to ensure that the most suitable procedure is selected. The key aim of this training should be to present a continuum in which the individual procedures do not compete with, but rather complement, each other.

Survey results indicate that a systematic approach in the management of disputes can contribute to an efficient dispute resolution process that meets the needs of all parties involved. When such solutions are implemented, due consideration should be given to the close cooperation of management and the legal department.

Our team

PwC Deutsche Revision is one of the leading auditing and consulting services organisations and, as independent member within the international PricewaterhouseCoopers network, is drawing on the knowledge and skills of more than 122,000 employees in 144 countries. In Germany, 8,200 employees generate a turnover of approximately € 1 billion in assurance, tax and advisory services at 28 locations. Focus is on assurance and business advisory services, tax services as well as transaction, process and crisis services (advisory). As part of crisis services Dispute Analysis & Investigations provides comprehensive advice and expert services in litigation and out-of-court dispute resolution procedures.

The study can be downloaded from www.pwc.com/de/dai or can be requested by telephone from +49 (69) 95 85-55 50.

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