

# COMPARISON OF ALTERNATIVE CONSTRUCTION DISPUTE RESOLUTION MEASURES

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Construction projects often are particularly susceptible to conflicts due to their long-term character and complexity. In Germany, courts must deal with around 100,000 construction dispute litigations per year. Alternative Dispute Resolution (ADR) can be an alternative to expensive as well as time-consuming litigation and can help to relieve the judicial system. Furthermore, ADR may contribute to the satisfying settlement of a dispute between parties involved in the construction process and thus help to reach construction projects' completion on time and within budget. Often, ADR mechanisms such as adjudication, mediation, and conciliation will be used. The paper analyzes the development of ADR in Germany in conjunction with European legal aspects. With special reference to the construction industry practice in Germany, various ADR measures and their advantages and disadvantages, as well as the current situation, will be explained. The authors conclude that, although ADR in Germany has experienced an upswing since the 1990s, it is used only to a small extent for settling disputes in construction projects. An increased knowledge about the advantages and disadvantages of different ADR measures in the construction industry would lead to more frequent uses of ADR. That, and a clever and detailed contract design, which helps to avoid conflicts basing on unclear contract contents, could save money and relieve the courts from time-consuming legal proceedings.

*Keywords:* Construction Conflicts, ADR, Mediation, Adjudication, Conciliation.

## 1 INTRODUCTION

Construction disputes are of high complexity and may occur from the initial stage until the closeout stage of a project. Nevertheless, only few conflict parties use Alternative Dispute Resolution (ADR) to settle conflicts. The German Association for Alternative Dispute Resolution in the Construction and Real Estate Industry (2018) found out that people involved in construction processes know about the existence of ADR, but specific knowledge on the content, process, and pros and cons of the respective ADR measures were missing. This seems to be one of the reasons why a vast majority of construction conflicts is decided in legal proceedings. Thus, the intention of the authors is to analyze ADR measures, give definitions, show differences, and discuss the advantages and disadvantages of the most frequently used ADR methods in Germany. The information shall help to identify the appropriate dispute resolution measure for the individual conflict and, by this, to support dispute parties to decide for a suitable ADR method.

There is no uniform definition of ADR worldwide. Usually, ADR means various procedures, with involvement of a neutral party, to find an agreement or a solution for a conflict and to avoid

arbitration or legal proceedings (Stubbe 2009). Nevertheless, there are also ADR measures without involving a third party, e.g., interest-oriented negotiations (Harvard Concept).

## 2 ADR IN GERMANY

In Germany, construction conflicts are mainly solved in legal proceedings. In 2017, around 100,000 construction disputes were decided before the courts, while in only 2,000 conflicts, the parties used ADR measures (German Association for Alternative Dispute Resolution in the Construction and Real Estate Industry 2018). The offered ADR measures are manifold, such as adjudication, mediation, conciliation, expert determination, dispute resolution advisor, and dispute review board/panel (see Figure 1). In contrast to other countries, arbitration does not fall under the category of ADR in Germany because (non-state) tribunals decide the dispute by a judgement, which is normally legally binding and can be declared as enforceable in state courts.

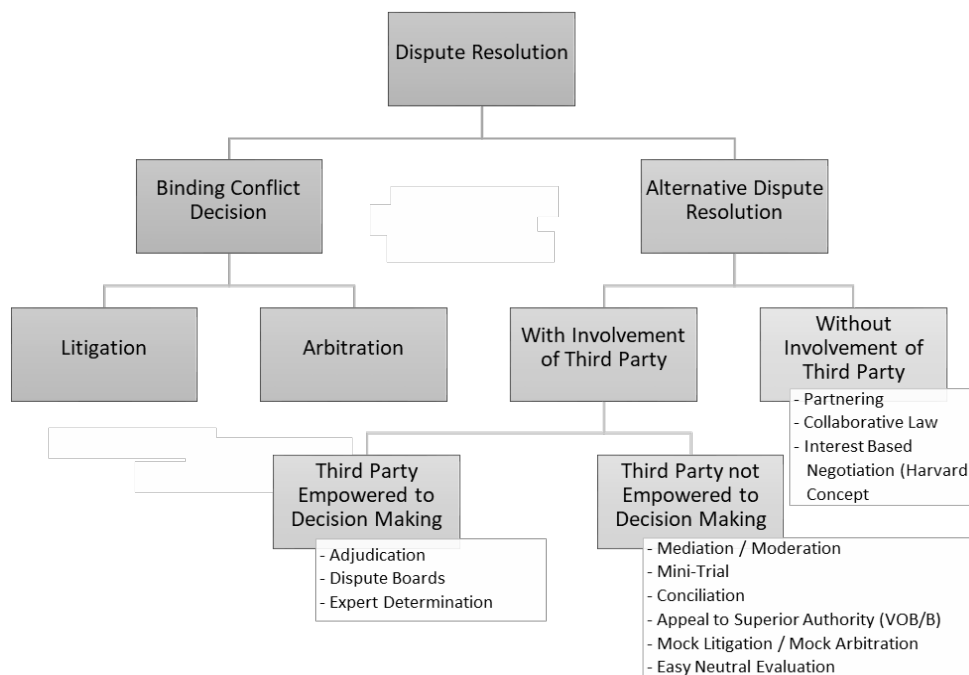


Figure 1. Overview on the dispute resolution system in Germany.

The law in Germany does not regulate ADR measures, except for mediation. On the European level, the EU Directive on Certain Aspects of Mediation in Civil and Commercial Matters (Directive 2008/52/EG of the European Parliament and of the Council 2008) deals with mediation in construction disputes. Germany passed an act, the German Mediation Act (2015), transposing the provisions of the EU directive into its national law. The German Mediation Act regulates all mediations conducted in Germany, irrespective of the nature of the dispute or the party's residence.

To facilitate the conflict parties' decision for a specific ADR method, in the following, the authors will present and discuss the most popular ADR measures in Germany (see Table 1).

Table 1. The most important measures of ADR in Germany with their German Designation and a definition.

| Measures of ADR | German Designation | Definition                                                                                                                                                                                                                                     |
|-----------------|--------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Adjudication    | Adjudikation       | A confidential process conducted by an arbitrator, developed for construction disputes. Later, the decisions can be judicially reviewed and revised by an arbitral tribunal or state court.                                                    |
| Conciliation    | Schlichtung        | Voluntary, confidential process, basing on parties' agreement, which does not follow a fixed structure and which further details will be freely agreed between the parties. The neutral conciliator has not the empowerment to make decisions. |
| Mediation       | Mediation          | A confidential and structured process in which the parties strive, on a voluntary basis and autonomously, to achieve an amicable resolution of their conflict with the assistance of mediators.                                                |
| Med-Arb         | MedArb             | MedArb is a combination of mediation and arbitration as a hybrid mechanism of dispute resolution.                                                                                                                                              |

### 3 MEASURES OF ADR

Due to page limitations, only mediation, adjudication, conciliation, and Med-Arb will be compared. An overview of their characteristics, in contrast to litigation and arbitration, is given in Table 2.

Table 2. The most important characteristics of dispute resolution measures referring to German Law.

| Characteristics   | Litigation | Arbitration | Mediation | Med-Arb | Adjudication | Conciliation |
|-------------------|------------|-------------|-----------|---------|--------------|--------------|
| Voluntary         | (-)        | (+)         | (+)       | (+)     | (+)          | (+)          |
| Binding decision  | (+)        | (+)         | (-)       | (-)     | (-)          | (-)          |
| Confidential      | (-)        | (+)         | (+)       | (+)     | (+)          | (+)          |
| Neutrality        | (+)        | (+)         | (+)       | (+)     | (+)          | (+)          |
| Structured        | (+)        | (+)         | (+)       | (+)     | (+)          | (-)          |
| Interest-based    | (-)        | (-)         | (+)       | (+/-)   | (-)          | (+)          |
| Non-adjudicative* | (-)        | (-)         | (+)       | (+/-)   | (-)          | (+)          |

\* The third party assumes a facilitative rather than an inquisitive role in the ADR process and should not investigate the case, interrogate the parties, express opinions, or give judgment or verdict.

#### 3.1 Adjudication

Adjudication, originally developed for construction conflicts, uses the opinions of neutral experts for dispute resolution. Parties freely agree about the procedural guaranties, which is normally not possible in regular arbitration procedures. That allows for faster and summary decisions.

Adjudication will be used in the planning or construction stage, especially for disputes arising in large-scale projects (German Association for Alternative Dispute Resolution in the Construction and Real Estate Industry 2014) and must be agreed on by contract. In the case of a conflict and on the proposal of one of the disputing parties, one or more neutral experts will be involved to analyze and resolve the conflict. The experts shall, within a few weeks, examine facts, hear the parties, and view the issues from a technical and legal perspective, which are the basis for the claims. The expert's decision is temporary legally binding and must be obeyed but may later be evaluated and revised by an arbitration tribunal or state court (German Association for Alternative Dispute Resolution in the Construction and Real Estate Industry 2014).

The advantage of adjudication is that conflicts will be solved and defused in an early stage, which saves money and secures the cash flow of construction companies. Disadvantageous is the lacking enforceability of the adjudication decision and the non-binding effect for subcontractors.

### 3.2 Conciliation

Conciliation is a voluntary, confidential process, basing on the parties' agreement that does not follow a fixed structure and where further details will be freely agreed upon between the parties. Conciliation, in the narrow sense, can be defined as an active mediatory, consensus-oriented activity of an independent person. The third person, the conciliator, conducts the target-oriented discussion about the dispute and may offer a specific recommendation for solving the conflict (German Association for Alternative Dispute Resolution in the Construction and Real Estate Industry 2014). In contrast to adjudication, the neutral party is not empowered to make decisions.

The parties freely decide on accepting the dispute resolution proposal. Content, kind, and duration of the process will be agreed upon between the parties and conciliator. A positive note for the parties is the possibility to organize the conciliation process free from requirements, with less formalities and paperwork, and the conciliation award with explanations.

If a party is not consensus-oriented and/or willing to settle the conflict, conciliation will not be a suitable measure. Furthermore, direct enforceability of the conciliation award or the parties' agreement is not possible. The difference in mediation is the more active part of the third neutral party at the cost of the parties' responsibility of settling the conflict.

### 3.3 Mediation

The German Mediation Act (2015) defines mediation as a confidential and structured process in which the parties strive, on a voluntary basis and autonomously, to achieve an amicable resolution of their conflict with the assistance of one or more mediators. International definitions denote mediation as a consensual process in which a neutral third party works with the disputing parties to help them explore and, if appropriate, reach a mutually acceptable resolution of some or all of the issues in dispute (Cheng and Soo 2013).

Mediators, as independent and neutral persons without any decision-making power, guide the parties through the mediation process (Section 1 of the German Mediation Act). The German regulations contain various requirements of disclosure and restrictions of activities in order to secure the mediator's independence and neutrality but without detailed rules on the procedures for conducting a mediation. Mediators have the responsibility to guarantee the skills and experience gained through the appropriate education and training to guide the parties through the mediation process.

The parties' freedom to organize the procedure and content of the mediation process, according to their preferences, gives them full control over the negotiation. The mediator shall only guide the conflict settlement and not elaborate on their own solution. Thus, mediation is the ADR measure where the disputing parties have the strongest autonomy and self-responsibility.

### 3.4 Med-Arb

Med-Arb represents a combination of mediation and arbitration as a hybrid mechanism of dispute resolution (Ng and Banaitis 2017). In the first step, the disputing parties try to settle the conflict by mediation. If mediation is not successful, the dispute resolution agreement provides for the mediator to be appointed as an arbitrator and to proceed to resolve the dispute through arbitration.

In construction disputes that may fall into one or more different types—such as contractual, technical, and legal aspects—and that may entail claims in terms of time, cost, and other elements, Med-Arb can help to resolve the conflict (Ng and Banaitis 2017).

## 4 ADVANTAGES AND DISADVANTAGES OF ADR MEASURES

### 4.1 Advantages

In theory, there are advantages of ADR methods. Beside time and cost savings, privacy, and win-win-results (Ng and Banaitis 2017), ADR may contribute to solve conflicts in an early stage. Through the discourse in mediation, the mutual understanding between parties may be improved, which is conducive to sustaining their ongoing relationship (Ng and Banaitis 2017). However, the number of ADR processes in Germany is increasing at a slow rate (Masser *et al.* 2017).

Not all construction conflicts are suitable to be solved out-of-court. ADR shall not replace dispute resolution by state courts. However, it is worth thinking about regarding active conflict management to analyze the problems in an early stage, classify them, and subsequently solve them in a target-oriented manner before the conflict escalates.

### 4.2 Disadvantages

The non-binding and potentially non-conclusive nature of ADR is a major disincentive to parties who believe that they have a strong case (Ng and Banaitis 2017). Moreover, in Germany, only around 50% of the mediations are successful. The conflict was solved in 42% of the cases “seldom or never” and in 34% “sometimes” (Masser *et al.* 2017). If there is such a low-level success rate without saving money and time, it is understandable that the construction industry still has concerns in using ADR.

Furthermore, by supporting the development of ADR and motivating conflict parties to use it, countries intend to relieve the state legal system, especially the courts, and, by this, be detracted from their obligation to maintain an effective and fair legal system. In Germany and many other countries of the world, the constitution guarantees the right to take action in the court and to have access to the jurisdiction of his or her lawful judge, e.g. Art. 101 of the Basic Law for the Federal Republic of Germany (2019), which is one of the fundamental pillars of a democratic system. Especially for small- to medium-sized market players, there is a danger in being forced to agree with ADR in construction contracts and, therewith, to exclude the right to take action in court, due to an unbalanced contract negotiation situation with big-sized contract partners.

## 5 CURRENT SITUATION

The Code of Civil Procedures in Germany contains incentives to motivate parties to settle their dispute by ADR. For example, parties must inform the court on attempts to start an ADR procedure, e.g. mediation, in the statement of claim, and if there are concerns on using ADR procedures to solve the conflict. Furthermore, the court may suggest that the parties pursue mediation or other alternative ADR procedures. Should the parties agree to pursue ADR, the court shall order the proceedings stayed, according to Section 278a of the Code of Civil Procedure (2019).

Nevertheless, in Germany, the conflict parties’ interest in ADR methods to decide their dispute is increasing at a slow rate. Many parties believe that they are able to solve the problem by themselves. Another reason may be the huge knowledge deficit on the details and pros and cons of ADR measures (Zander 2019).

A German survey among mediators, on whether enforceability of mediation results would help to promote mediation as an ADR method, showed that nearly none of the interviewed experts expected an increase in mediation if mediation results would be enforceable. This is basing on the experience that only 10% of the parties originally interested in mediation give lacking enforceability as a reason for ultimately not deciding for this ADR method. With the

57% and 34% interest in a court's decision and the high costs in mediation are the main reasons against mediation in Germany (Masser *et al.* 2017). The same applies for conciliation where normally three neutral persons will be engaged. Conciliators' hourly rates normally range between 200 and 300 euros. Due to additional lawyer costs and intern expenses, conciliation may become more expensive than litigation. Thus, ADR seems to be more suitable and interesting for big-sized market players and big-sized construction projects.

## 6 CONCLUSION

ADR measures can help to settle conflicts in construction mediation. But not every method is suitable for resolution of each kind of dispute. The authors experienced a huge knowledge deficit in the construction industry regarding the details of ADR measures. However, knowledge on the pros and cons of the measures in contrast to litigation and arbitration may help construction companies decide for or against a conflict settlement by ADR. Finally, it is worth mentioning that many construction conflicts result from unclear explanations on the parties' rights and obligations in the contract. Thus, a clever and detailed contract design may contribute to avoiding conflicts. Negotiating over the contents before closing a contract can be seen as "ADR in advance", but without an existing conflict and the frustration of the parties. Investing financial resources in skilled contract lawyers helps, in that conflicts do not emerge, which saves time and costs for dispute resolution, no matter if done by state courts or by ADR.

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