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Commercial Arbitration: Germany and the United States

In both countries, arbitration is an option,
but significant differences remain

By Christian Duve and Jill I. Gross

Arbitration has deep roots in the legal cultures of the United States and Germany — and is still an important option for resolving disputes in both countries today. As far back as Colonial times, US merchants used arbitration to settle industry disputes, and in the early 19th century, American stockbrokers resolved intra-industry disputes through arbitration at the New York Stock Exchange.¹ In Germany, a country with a civil law rather than a common law tradition, commercial arbitration has been practiced for centuries: the first draft of the German Code of Civil Procedure from 1877 included a section establishing the legal foundations of arbitration.

In both countries, what started as a relatively simple alternative to litigation, one in which a third-party neutral or neutrals gave each party an opportunity to be heard and then issued a final binding award, has

evolved into a complex process with procedural rules and norms that look more and more like litigation. That process of change has yielded some key differences in modern domestic arbitration practice in the United States and Germany. Some features of that practice now common in the United States, such as extensive discovery and dispositive motions, are unheard of in Germany. In Germany, where judges take a more active role than most US judges, arbitrators tend to advise parties more often than their US counterparts do. Furthermore, over time, both users of the US and German systems and outside reviewers — primarily judges — have developed differing attitudes toward the process, resulting in distinct domestic perceptions of the process and concerns about its increased use. In the United States, many have criticized what they see as the increasing, unwarranted use of arbitration to

resolve disputes stemming from adhesive commercial contracts, those that are generally drafted by the stronger party. In Germany, in contrast, some German judges are concerned about how increased use of arbitration will affect case law.

Legal Framework

The Federal Arbitration Act (FAA)² and, to a lesser extent, state arbitration laws³ provide the legal framework for commercial arbitration in the United States. Section 2 of the FAA provides that written agreements to arbitrate are “valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.” Courts must apply that substantive rule in both state court and federal court to all arbitration contracts “involving commerce.”⁴ The remaining sections of the FAA are procedural in nature, providing, for example, remedies if a disputant resists arbitration, a method to appoint arbitrators in the absence of party agreement, and grounds for post-award enforcement and review.

In Germany, the legal framework for today’s arbitration can be found in the 10th book of the *Zivilprozessordnung* (ZPO), the German Code of Civil Procedure, which is based on the UNCITRAL’s Model Law on international commercial arbitration.⁵ Most of the ZPO’s provisions on arbitration are procedural in nature and similar to the FAA. The ZPO also provides remedies for a party’s failure to comply with procedural rules, for the appointment and recusal of arbitrators, and for rules concerning the enforcement and review of arbitral awards. Furthermore, the ZPO contains provisions that govern the interrelation between arbitral tribunals and state courts, for example in the taking of evidence.

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Arbitration Institutions

In the United States, the most widely used commercial domestic arbitration service providers are the American Arbitration Association (AAA), JAMS, and National Arbitration and Mediation (NAM), each of which offers its own procedural rules and levels of administrative support. In 2016, according to their respective websites, the AAA administered more than 8,000 business-to-business (B2B) disputes, JAMS handled more than 13,000 disputes worldwide (not broken down by domestic and B2B), and NAM handled thousands more. In the securities industry, the Office of Dispute Resolution of the Financial Industry Regulatory Authority (FINRA), the self-regulatory organization authorized by Congress to protect America’s investors by making sure the broker-dealer industry operates fairly, handles more than 1,000 arbitrations annually, either intra-industry disputes or those between a customer and a brokerage firm.⁶

For business matters in Germany, the German Institute of Arbitration (DIS) is the best-known arbitration institution with the strongest reputation. The DIS has established arbitration rules and a DIS German Court of Arbitration for Sport.⁷ While the data presented by the DIS does not reflect the total number of arbitration proceedings in Germany, it does indicate a trend: the number of arbitration proceedings increased from 72 in 2005 to a total of 172 in 2016.⁸

Types of Disputes

In the United States, arbitration is used to resolve disputes between businesses of all sizes as well as disputes between corporations and their customers or consumers (B2C). Many industries, including construction, securities, consumer financial services, Internet services, and healthcare, commonly include pre-dispute arbitration agreements (PDAAs) in their contracts. Those PDAAs typically cover a wide range of subject matter disputes that might arise in the future, such as breach of contract, fraud, employment, intellectual property, civil rights, antitrust, fraud, and disputes arising out of statutory rights. With a few narrow exceptions, no US law or regulation bans the use of arbitration for disputes between businesses and their consumers. Many arbitration institutions, however, insist on compliance with Consumer Due

Process Protocols if their services are used to resolve a dispute arising out of an adhesive PDAA.

In Germany, arbitration is commonly used for commercial disputes not involving consumers. According to German law, all claims involving a so-called economic interest (*vermögensrechtlicher Anspruch*) can be subject to an arbitration agreement. This limitation on scope excludes from arbitration, in particular, family law matters.⁹ Arbitration proceedings involving a consumer as a party are possible under German law. However, if a consumer is involved, arbitration agreements must meet far-reaching formal requirements to be enforceable. For example, arbitration agreements must be contained in a record or document that may not contain agreements other than those making reference to the arbitration proceedings. Due to these formal requirements and narrow exceptions,¹⁰ unlike in the United States, consumer arbitration is not common in Germany.

Procedural Distinctions

The arbitration process in the United States has come to resemble litigation. Though some arbitrators resist the application of the rules of civil procedure in arbitration, attorneys trained in litigation frequently invoke court procedural rules during the pre-hearing phase of arbitration. As a result, discovery has grown to include expansive document requests by each side, some depositions in larger cases, expert reports, and e-discovery.¹¹ The FAA's only provision relating to discovery imbues arbitrators with the power to subpoena non-parties to testify before the panel. To fill in this gap, each of the prominent arbitration forums provides rules and guidelines to govern pre-hearing motions and discovery. For example, Rule 22 of the AAA's Commercial Arbitration and Mediation Rules grants extensive authority to arbitrators to manage discovery, including the exchange of documents and electronic materials.

Dispositive motions are common in larger cases and are expressly contemplated by many forums.¹² However, unlike US judges, US arbitrators typically do not discuss settlement with the parties — other than perhaps encouraging the parties to try to resolve their dispute on their own — and they are not permitted to actively involve themselves in settlement discussions.

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In Germany, due to the parties' freedom to determine the procedure on their own, the different legal traditions of common and civil law are increasingly merging in arbitration proceedings.¹³ In this context, procedural rules that originated from common law systems, especially from the Anglo-American legal system, have a strong influence on arbitration proceedings in Germany.¹⁴

Under German procedural law principles, each party may use evidence in its possession only to prove its claim. Thus, in general, there is no duty to participate in investigating the facts on which the counterparty bases its case, and German arbitration law does not provide for discovery proceedings.¹⁵ One can demand the submission of documents by the opposing party only if the requesting party is able to precisely specify the documents that are subject to disclosure and if the requested documents are related to the specific dispute.¹⁶ However, state courts and arbitral tribunals are reluctant to grant such requests.

Parties can request assistance from a court in taking evidence or performance of other judicial acts that the arbitral tribunal is not empowered to carry out. However, courts can decline requests for assistance in the production of evidence not admissible under the court's rules as to the taking of evidence. When incorporating this provision into the ZPO with the German Arbitration Act, German legislators specifically meant to preclude US discovery proceedings.¹⁷ The reluctance with regard to discovery proceedings promotes efficiency of the proceedings by saving time and money for the parties. This means, however, that parties must accept a certain level of risk when

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presenting their case to an arbitrator without a complete factual basis.

German law is not familiar with the motion practice that is common in US arbitration forums. There is no legal remedy for the parties to file a motion to dismiss, for example, in order to shorten the proceedings. However, even though motion practice is not applicable directly in arbitration, an arbitral tribunal in Germany may also rely on and proceed in accordance with a statutory provision that allows a court to point the parties to crucial facts of the case on which the court's decision may be based or to the deficiencies of a claimant's case as the court currently sees them.¹⁸

Role of the Arbitrator(s)

Having been educated in German civil procedure, in which the judge takes an active role throughout the proceedings, German arbitrators tend to play a more active role in managing domestic arbitration proceedings than their colleagues from common-law jurisdictions. For example, under ZPO § 273, the judge may direct the parties to complement their written pleadings or provide further evidence on crucial points and may set a deadline for submitting explanations with regard to issues in need of clarification. Under the ZPO, German judges have a statutory duty to work toward an amicable resolution of a dispute. They are even allowed to make settlement proposals to the parties.¹⁹ This idea is reflected in the DIS arbitration rules: "At every stage of the proceedings, the arbitral tribunal should seek to encourage an amicable settlement of the dispute or of individual issues in dispute."²⁰ Therefore, German arbitrators are quite open-minded with regard to settlements; they even work toward such settlements.

Generally speaking, the passive behavior of US arbitrators, at least when compared to that of German arbitrators, demands from the parties' representatives more independent process management. Judicial guidance on crucial questions of procedural law, for example, can be expected from a German rather than from a US arbitrator. In contrast, in US arbitration, the parties must spend their time and money researching and advocating to the panel crucial procedural issues. Furthermore, US arbitrators will not usually initiate settlement negotiations.

Attitude of Judiciary

Judges in the United States by and large favor arbitration as a means of docket control. The US Supreme Court has ruled repeatedly that Congress' adoption of the FAA reflects a strong national policy supporting arbitration.²¹ Thus the Court interprets the FAA to presume that disputes are arbitrable, converting arbitration clauses into "super-contracts" that carry a presumption of validity.²² Lower-court judges must follow this interpretation and compel arbitration of disputes pursuant to a PDAA, absent a common-law ground for the revocation of any contract.

Similarly, from a legal perspective, the German judiciary tends to respect the parties' choice to arbitrate. At the same time, some judges and other



observers express concerns about the growth of commercial arbitration, while other forms of alternative dispute resolution are still held in high esteem.²³ Though one might expect the judiciary to welcome the continuously increasing number of arbitration proceedings as relief for its own workload, some judges would prefer the courts to have the final say in the most important legal cases. An issue of particular concern to them is that the development of the case law might suffer, since arbitration proceedings usually are confidential and arbitral awards are not as frequently published.²⁴ Continuously adapting the law to new economic developments, however, is crucial for legal certainty.²⁵ And legal certainty is of particular importance in complex transactions with huge economic significance, such as mergers and acquisitions.²⁶ For example, disputes arising from such merger and acquisition transactions are regularly brought before arbitral tribunals. As a consequence, case law by German state courts on current issues of major merger and acquisition transactions is very limited.²⁷

In comparison to their US colleagues, German legal practitioners are more likely to criticize the growth of commercial arbitration. Such criticism, however, is heard not only in Germany but throughout the world, and the international arbitration community is responding by intensifying efforts to render arbitration more transparent. Arbitral awards, with names and case-identifying details removed, are published in legal journals, such as the Collection of ICC Arbitral Awards.²⁸ The year 2015 saw the founding of an international arbitrator network called Arbitrator Intelligence, which aims to publish “critical information about arbitrators and their decision making.”²⁹ More transparency in arbitration also could alleviate the concerns about lack of development of the law in some fields.

Reputation

Over the past 20 years, domestic commercial arbitration in both Germany and the United States has encountered criticism — but for very different reasons. Some US commentators and observers have roundly criticized the expanding use of PDAs in adhesive consumer and employment agreements, those drafted, for example, by consumer financial service companies

for their customers and by national chain restaurants for their employees and franchise owners. In a series of articles in October and November of 2015 headlined “Beware the Fine Print,” *New York Times* reporters described this concern; observing that “arbitration everywhere” was “stacking the deck of justice.” The proliferation of adhesive arbitration clauses — sometimes combined with class-action waivers, the series said, was effectively removing people’s right to sue and join together in class proceedings.

In Germany, many professionals (clients as well as legal representatives) still hold arbitration in high esteem. In the last few years, however, as in the United States, to some extent the public perception of commercial arbitration has declined due to its lack of transparency and perceived lack of fairness.³⁰ Therefore, observers agree that proceedings should be as transparent as possible, so practitioners and institutions can show that arbitration proceedings are both fair and efficient.

Evolving Differences

Looking at domestic commercial arbitration in the United States and Germany illustrates how one process can evolve differently in different legal cultures. The fundamental adversarial nature of the US legal system has influenced domestic arbitration there, while Germany’s legal system has influenced its commercial arbitration process. The commercial arbitration process in the United States and Germany — though rooted in the same history — today might look and feel procedurally very different to an outside observer. A US commercial arbitration might last months and even years, with extensive pre-hearing discovery and motion practice, whereas a German commercial arbitration will be completed in a shorter period of time. And, of course, time in arbitration translates to money; it will cost the parties more, in general, to resolve their

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dispute in US arbitration. It is also well recognized that procedural differences can lead to disparate substantive outcomes.

Basic differences between the US common law system and the German civil law tradition also have affected the way parties and arbitrators perceive their roles. While US arbitrators are focused on maintaining their neutrality and ensuring that the parties perceive them that way, German arbitrators will intervene more overtly in the resolution. Being aware of these differences enables parties and their representatives to anticipate differences in arbitrator conduct — and be better prepared for the process. ■

Endnotes

1 See Jill I. Gross, *The Historical Basis of Securities Arbitration as an Investor Protection Mechanism*, 2016 J. DISP. RESOL. 171 (2016).

2 9 U.S.C. §1-307 (2014).

3 Most states have modeled their arbitration law on either the Uniform Arbitration Act or the Revised Uniform Arbitration Act.

4 See *DIRECTV, Inc. v. Imburgia*, 136 S. Ct. 463, 468 (2015).

5 Cf. Gesetzentwurf [Government Draft], DEUTSCHER BUNDESTAG [BT] 13/5274, <http://dipbt.bundestag.de/doc/btd/13/052/1305274.pdf> (Ger.).

6 See forum statistics at <https://www.adr.org/>; <https://www.jamsadr.com/about-jams/>; <http://www.namadr.com/>; <https://www.finra.org/arbitration-and-mediation/dispute-resolution-statisticsfinra>.

7 See <http://www.disarb.org/en/> (last visited Aug. 18, 2017); <http://www.dis-sportschiedsgericht.de/> (last visited Aug. 18, 2017).

8 DIS Statistics-2016, <http://www.disarb.org/de/39/content/statistik-id70> (last visited Aug. 9, 2017).

9 Joachim Münch, in MÜNCHENER KOMMENTAR ZUR ZIVILPROZESSORDNUNG § 1050, ¶ 6 (Thomas Rauscher, Peter Wax &

Joachim Wenzel eds., 4th ed. 2013).

10 ZPO §1031(5).

11 See Jill I. Gross, *Justice Scalia's Hat Trick and the Supreme Court's Flawed Understanding of Twenty-First Century Arbitration*, 81 BROOKLYN L. REV. 111, 119-20 (2015).

12 See, e.g., American Arbitration Association Rule 33.

13 Böckstiegel, *SchiedsVZ* 2009, 3, 6.

14 Wirth, *SchiedsVZ* 2003, 9 et seq.

15 Hunter, *SchiedsVZ* 2003, 155, 161.

16 Wirth, *SchiedsVZ* 2003, 9, 11.

17 Cf. Gesetzentwurf [Government Draft], DEUTSCHER BUNDESTAG [BT] 13/5274, <http://dipbt.bundestag.de/doc/btd/13/052/1305274.pdf> (Ger.).

18 Higher Regional Court Munich, 24 November 2015, 34 SchH 5/15, NJW 2016, 881, 882; *Martens*, *SchiedsVZ* 2009, 99, 101 (referring to arbitration in sports, according to the DIS-SportO).

19 Berger, *SchiedsVZ* 2009, 289.

20 DIS-Arbitration Rules 98, Sec. 32 (1).

21 See, e.g. *Nitro-Lift Techs., L.L.C. v. Howard*, 133 S. Ct. 500, 503 (2012).

22 See Gross, *supra* note 11, at 124.

23 The German legislature has enacted specific laws for mediation (Mediation Law, "Mediationsgesetz") and since April 2016 for dispute resolution in consumer cases (Consumer Dispute Resolution Law, "Verbraucherstreitbeilegungsgesetz").

24 Berger, *SchiedsVZ* 2009, 289, 296; Gaier, NJW 2016, 1367, 1369 et seq.

25 Gaier, *Frankfurter Allgemeine Zeitung* (Feb. 24, 2016), <http://www.faz.net/aktuell/politik/staat-und-recht/gastbeitrag-schiedsgerichte-nuetzliche-konkurrenz-14075395.html>.

26 Gaier, NJW 2016, 1367, 1370.

27 Gaier, NJW 2016, 1367, 1370.

28 Berger, *SchiedsVZ* 2009, 289, 296.

29 Arbitrator Intelligence Mission Statement, <http://www.arbitratorintelligence.org/about/> (last visited Aug. 18, 2017).

30 *Wilske/Markert/Bräuninger*, *SchiedsVZ* 2016, 127; *Risse*, *SchiedsVZ* 2014, 265.



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