

Core Element 4 – Rational Dispute Resolution

“Everyone is entitled in full equality to a fair and public hearing by an independent and impartial tribunal, in the determination of his rights and obligations and of any criminal charge against him.”

-Universal Declaration of Human Rights – Article 10

Courts are the public arbitrators of fairness and equality. Without an independent and accessible court system, inequalities of property and power can be perpetuated for generations. The conflict between the “landed gentry” who held property rights in perpetuity and the merchant classes in feudal England led to the creation of the property rights system that governs much of the Western world today. This system recognizes that diversification of ownership and the rise of a politically powerful middle class are essential to the development of not only property markets, but the broader economic development brought about by entrepreneurs and innovation.

In many parts of the world, citizens are still locked out of the power that comes from ownership. Access to the courts is too costly for most people and the judiciary is often highly influenced by entrenched political powers. Even in countries with developed civil or common law systems, contract enforcement is complicated, slow and costly – not only in direct costs, but in opportunity costs when properties sit vacant and unused.

Fully functioning property markets require that specialized commercial courts be developed to deal with property disputes outside the criminal court system. Respected alternative dispute resolution methods completely outside the courts are also excellent means of fairly and efficiently dealing with conflict and building property value. Finally bilateral commercial treaties between countries and regions are also essential in today’s global investment market.

Core Element Goal

An efficient institutional framework that balances the rights of the public, owners, lenders and borrowers in the event of a dispute or loan default

Lead Indicator 4.1 – Rule of Law


Core Question: Do all market participants abide by the rule of law and have confidence in the courts and ability of the police to control crime?

The rule of law is the cornerstone for all other elements of democracy. A free and fair political system, protection of human rights, a vibrant civil society, public confidence in the police and the courts, and economic development all depend on accountable governments, fair and

accessible application of the law, and respect for international human rights standards. In post-conflict settings, reestablishing the rule of law is the first step in the rebuilding process. Establishing peace and security and rebuilding justice institutions can help to develop the necessary climate for reconciliation, public confidence, and subsequent economic growth.

Sub-Indicator 4.1.1 – Impartiality

What is the confidence level of the strength and impartiality of the police, courts and contract enforcement?

- Step 1 Visit the World Bank's *Governance Matters 2008*, World Bank http://info.worldbank.org/governance/wgi/sc_chart.asp
- Step 2 Select Country Drop Down " ~ " and select your country
- Step 3 Click "Submit"
- Step 4 Click Tables 
- Step 5 Record the score for "Rule of Law," note the trend from previous years.
- Step 6 Determine the Sub-Indicator Score:
 - Very Strong 75 – 100
 - Strong 50 – 74
 - Weak 25 – 49
 - Very Weak 0 – 24

Sub-Indicator 4.1.2 – Judiciary

Can members of the judiciary be held accountable for their actions?

Judges are often the final arbiter in a property dispute. It is therefore crucial that citizens have confidence that judges are appointed fairly. Judges at all levels should be held accountable for their actions. Conflict of interest regulations should be in place and enforced and citizens should be able to gain enough information about judges to discern whether a potential conflict exists.

- Step 1 Visit the Global Integrity Website: <http://report.globalintegrity.org>
- Step 2 Select your country.
- Step 3 Click "Integrity Indicators Scorecard"
- Step 4 Record the score for "Judicial Accountability"

Note: the Scorecard uses Global Integrity's answers and scores directly rather than making a separate determination.

Sub-Indicator 4.1.3 – Costs of Crime

What are the business costs of crime and violence?

Business hates uncertainty. For property markets to thrive, investors must have confidence in the security situation of a country. Excessive costs to hire private security, loss of property due to violence or civil unrest, or internal theft from employees and managers add to the costs of doing business. Countries must have a stable security environment to attract foreign investment.

- Step 1 Visit the *Global Competitiveness Report* Web site:
www.weforum.org/documents/GCR09/index.html
- Step 2 Select the “Data Tables” Drop Down
- Step 3 Select the “I-Institutions”
- Step 4 Click the forward page arrow → to Table 1.13 – “Business costs of crime and violence”
- Step 5 Find your country on the table.
- Step 6 Record the ranking and numeric score.
- Step 7 Determine the Sub-Indicator score:

| | |
|-------------|---|
| Very Strong | 1 ST – 33 RD countries |
| Strong | 34 TH – 67 TH countries |
| Weak | 68 TH – 100 TH countries |
| Very Weak | 101 ST – 133 RD countries |

Determine the Lead Indicator Score for Rule of Law

- Step 1 Review the Sub-Indicator scores.
- Step 2 Determine the Lead Indicator Score based on the aggregate of the Sub-Indicator scores.

Lead Indicator 4.2 – Enforcement of Contracts

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| Core Question: | Are systems in place for timely and efficient enforcement of contracts? |
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Sub-Indicator 4.2.1 – Judicial Enforcement

Commercial Property

The ability to make and enforce contracts and resolve disputes is fundamental if markets are to function properly. Good enforcement procedures enhance predictability in commercial relationships and reduce uncertainty by assuring investors that their contractual rights will be upheld promptly by local courts. When procedures for enforcing commercial transactions are bureaucratic and cumbersome or when contractual disputes cannot be resolved in a timely and cost effective manner, traders depend more heavily on personal and family contacts. Banks reduce the amount of lending because they cannot be assured of the ability to collect on debts or obtain control of property pledged as collateral to secure loans.

- Step 1 Visit the *Doing Business* Web site: www.doingbusiness.org
- Step 2 From the “select an economy” drop down select your country.
- Step 3 Record your country’s rank for “Enforcing Contracts” for the current and previous year.
- Step 4 Click on “Enforcing Contracts”
- Step 5 Record the answers and scores to the following questions:
- 4.2.1.1 What is the number of procedures involved in resolving a commercial dispute?**
 - 4.2.1.2 What is the time between the filing of a lawsuit and resolution in judicial enforcements?**
 - 4.2.1.3 What is the cost of judicial enforcements as a percentage of claim value?**
- Step 6 Determine the Sub-Indicator Score and Trend.
- | | |
|-------------|---|
| Very Strong | 1 ST – 46 TH countries |
| Strong | 47 TH – 92 ND countries |
| Weak | 93 RD – 137 TH countries |
| Very Weak | 138 TH – 183 RD countries |
- Trend either ↑ or ↓ compared to previous year.

Residential Property

An efficient foreclosure process is important for residential property markets. In some countries the law gives excessive protections to borrowers who may have fallen on hard times, and these protections can impose substantial costs on lenders. When lenders adjust for these costs, the outcome can be higher interest rates, larger down payments or credit rationing.

These costly outcomes for borrowers can be avoided with faster foreclosure processes. A faster process means greater certainty in realizing collateral rights and thus lower risks for the creditor of lost interest and principal from a collapse in the real estate market or a deterioration in the value of collateral because of vandalism or poor property maintenance. It also means lower costs—and thus greater proceeds from the sale of the home. Faster processes benefit both the creditor and the debtor. It also benefits the government, through greater tax revenue.

Step 1 For countries listed on page 14, download the report *Financing Homes 2008*, World Bank and International Housing Finance Corporation:
[www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/financinghomes/\\$FILE/FinancingHomes.pdf](http://www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/financinghomes/$FILE/FinancingHomes.pdf)

For countries not listed consult with local bankers, real estate attorneys, brokers and valuers.

Step 2 Use the report or interviews with local experts to determine the answers to the following questions, *Note: the complete information gathered in this search can be included in the answer to Field Question 8.*

Survey Question 12 **What is the time between notice of intent to foreclose and loan collection in judicial enforcements?**

Survey Question 13 **What is the cost of judicial enforcements as a percentage of property value?**

Sub-Indicator 4.2.2 – Summary Proceedings

A requirement of judicial foreclosure means that a creditor cannot sell collateral without first going through the courts – to obtain a court judgment on the debt and an order of execution. That can raise lenders' foreclosure costs by as much as 10% of the loan balance and add up to 5 months to the time on average. A study of the U.S. market finds that houses in foreclosure sell for 4% less in states that require judicial foreclosure than in those that do not, presumably because of greater deterioration of the property during the longer process.

An alternative to a full judicial foreclosure is a summary proceeding. In a summary proceeding a creditor can skip the judgment phase and apply directly for an order of execution against the property. This can be done by presenting a simple case by affidavit, with or without the debtor appearing. Summary proceedings place a greater burden on the debtor to stop the sale of the property. They can be converted into full judicial proceedings by lodging permitted defenses. Often the availability of a summary proceeding hinges on the existence of a loan agreement or similar document that does away with the need to prove the debt.

Step 1 Use the report from Step 1 above or interviews to determine the answers to the following questions:

Survey Question 14 **What is the time between notice of intent to foreclose and loan collection in summary proceedings if available to lenders?**

Survey Question 15 **What is the cost of summary proceeding if available to lenders as a percentage of property value?**

Step 2 Determine the Sub-Indicator Score.

Very Strong Summary proceedings are allowed by law and the predominate method of judicial foreclosure.

Strong Summary proceedings are allowed by law and used frequently by lenders.

Weak Summary proceedings are allowed by law but not in use in the market.

Very Weak Summary proceedings are not available to lenders.

Sub-Indicator 4.2.3 – Power-of-Sale

Another alternative to judicial foreclosure is a non-judicial process that gives the creditor the power to sell the pledged property without court intervention. Under a power-of-sale procedure a creditor may proceed directly to sale of the property, by auction or private transaction, after a notice to the debtor. In practical terms the power of sale relieves the creditor of the burden of going to court and presenting a case. It instead places this burden on the debtor, who can go to court to stop the sale of the property.

Step 1 Use the *Financing Homes* report or interviews to determine the answers to the following questions:

Survey Question 16 **What is the time between notice of intent to sell and loan collection for power-of-sale agreements if available to lenders?**

Survey Question 17 **What is the cost of power-of-sale agreements if available to lenders as a percentage of property value?**

Step 2 Determine the Sub-Indicator Score.

Very Strong Power-of-sale is allowed by law and the used frequently by lenders.

Strong Power-of-sale is allowed by law and used occasionally by lenders.

Weak Power-of-sale is allowed by law but not in use in the market.

Very Weak Power-of-sale is not available to lenders.

Determine the Lead Indicator Score for Contract Enforcement

Step 1 Review the Sub-Indicator scores.

Step 2 Determine the Lead Indicator Score based on the aggregate of the Sub-Indicator scores.

Lead Indicator 4.3 – Commercial Dispute Resolution

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| Core Question: | Can commercial disputes be resolved fairly and efficiently without exorbitant costs and delays? |
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While summary judgments and power-of-sale offer efficiencies in residential mortgage default, advanced property markets also require multiple avenues for commercial dispute resolution. First specialized commercial courts need to be in place outside the criminal or constitutional courts to address the complex issues involved in commercial contract disputes. Even in developed countries there is a preference for litigation, in spite of evidence to show that litigation is the most time consuming and costly option.

Alternative dispute resolutions procedures outside the courts such as negotiation, arbitration and mediation are growing trends. Developing contracts with arbitration clauses and company policies on dispute resolution prior to disputes helps get resources back to productive use when disagreements inevitably arise. Such alternative dispute resolutions procedures require that objective third party arbitrators and structured out-of-court implementation procedures be developed. Finally global markets require increased emphasis on bilateral trade agreements and the adoption of international norms such as the Convention on the Recognition and Enforcement of Foreign Arbitral Awards – New York Convention.

Sub-Indicator 4.3.1 – Commercial Courts

Survey Question 18 Do specialized commercial courts exist for the handling of property disputes and foreclosures?

Step 1 Visit the Globalex international and foreign law research of the New York University Hauser Global Law Program
www.nyulawglobal.org/globalex/index.html

Step 2 Click “Foreign Law Research” and review information for your country.

| | | |
|--------|---|--|
| Step 3 | Conduct an Internet search using such terms as “commercial courts [country],” “property courts [country],” or “probate courts [country].” | |
| Step 4 | Consult with local real estate attorneys, developers, brokers or valuers and ask about the judicial process for handling contract disputes. | |
| Step 5 | Determine the Sub-Indicator Score | |
| | Very Strong | Commercial courts exist including property and probate courts that efficiently handle property disputes and inheritances without significant delay |
| | Strong | Commercial courts exist including property and probate courts that handle property disputes and inheritances |
| | Weak | Commercial courts exist. Separate property and probate courts not yet developed or not fully functional |
| | Very Weak | Separate commercial courts either do not exist or are not fully functional |

Sub-Indicator 4.3.2 – Alternative Dispute Resolution

Survey Question 19 Are alternative dispute resolution mechanisms in place including commercial arbitration, private mediation and community-based practices?

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|--------|---|--|
| Step 1 | Visit the New York Convention Website list of countries to see if your country is a member: www.newyorkconvention.org/new-york-convention-countries/contracting-states | |
| Step 2 | Conduct an Internet search using such terms as “alternative dispute resolution [country],” “ADR [country],” or “arbitration [country].” | |
| Step 3 | Consult with local real estate attorneys, developers, brokers or valuers and ask about their experience with negotiation, arbitration and mediation in handling contract disputes. | |
| Step 4 | Determine the Sub-Indicator Score | |
| | Very Strong | A member of the New York Convention; ADR supported by law and by numerous organizations that train and certify mediators |

| | |
|-----------|---|
| Strong | A member of the New York Convention; ADR supported by law and by organizations that train and certify mediators |
| Weak | Not a member of the New York Convention; formal ADR processes are in place |
| Very Weak | Not a member of the New York Convention; ADR processes completely informal |

Sub-Indicator 4.3.3 – Commercial Treaties

Survey Question 20 **What bilateral, regional and international treaties exist concerning business between countries?**

- Step 1 Visit the Bilaterals.org and search for information on your country: www.bilaterals.org/
- Step 2 Visit the World Trade Organization Website to find if your country is a member: www.wto.org/english/thewto_e/whatis_e/tif_e/org6_e.htm
- Step 3 Conduct an Internet search using such terms as “Ministry of Trade [country],” or “Investment [country].”
- Step 4 Consult with local real estate developers, brokers or valuers and ask about their experience with cross-border transactions and any bilateral or regional agreements.
- Step 5 Determine the Sub-Indicator Score
- | | |
|-------------|---|
| Very Strong | A member of the World Trade Organization; numerous bilateral/regional trade agreements, signed ratified and operational |
| Strong | A member of the WTO; numerous bilateral trade agreements signed or in the process of being negotiated or ratified |
| Weak | A member of the WTO; bilateral trade agreements in the process of being negotiated |
| Very Weak | Not a member of the WTO |

Determine the Lead Indicator Score for Commercial Dispute Resolution

- Step 1 Review the Sub-Indicator scores.

- Step 2 Determine the Lead Indicator Score based on the aggregate of the Sub-Indicator scores.

Determine the Core Element Score for Rational Dispute Resolution

- Step 1 Review the Lead Indicator scores.
- Step 2 Determine the Core Element Score based on the aggregate of the Lead Indicator scores.

↻ Core Element Linkages

Rational Dispute Resolution ↔ Property Rights

While a great deal of effort has been made to support property rights institutions over the last decades, less effort has been made to develop the specialized institutions necessary to resolve property disputes in an efficient and equitable manner. Without a strong dispute resolution process and timely changes to the laws and institutions that support property rights on the front end, efficient markets will be slow to develop.

The dead capital brought to life by titling, registries and formal ownership will be short lived. Citizens will find that their rise from poverty is short-circuited by organized criminal activity and lack of access to the courts. International investors will place their capital in markets where they can be assured of reasonable protection from market downturns and other risks.

Please refer to the information for Property Rights on page 7.

Field Assessment

The remaining Core Elements – Rational Dispute Resolution, Financial Transparency and Appropriate Regulation have a limited number of widely available and researched indexes that can be used as sources. These elements form the Scorecard's primary research agenda. These Core Elements contain more Survey and Field Questions. The Scorecard's goal is to provide yearly evaluations of these supporting institutions to complement the *Doing Business* and *Global Competitiveness* indexes.

Field research for these elements, rather than focusing on differences between laws and application, will focus more on recommended reforms and the development of civil society institutions.

- Step 1 Partner with an outside expert with property market experience – preferably someone with transactional experience in a formal market outside your region.
- Step 2 Together with the expert, visit local property attorneys, brokers, agents and valuers and ask them to tell you about recent experiences in dealing with dispute resolution. Be sure to include information about both judicial and non-judicial processes.
- Step 3 Determine the answers to the following question:

Field Question 8 To what extent do practitioners report the use of formal contracts and trust institutions to support contract enforcement?

Core Element Map for Rational Dispute Resolution

Legend – colors indicate the strength of institutions that support property markets.

- Very Strong
- Strong
- Weak
- Very Weak
- Unknown

