

ALTERNATIVE DISPUTE RESOLUTION

A REVIEW

Thursday, November, 1992

Northeast Surety & Fidelity Claims Conference
Third Annual Meeting
Hartford, Connecticut

JAMES KING, P.E.
FORCON INTERNATIONAL CORPORATION
9901 Shrewsbury Court
Gaithersburg, MD 20879
(301) 670-1262

1992 Copyright
Forcon International Corporation

ALTERNATIVE DISPUTE RESOLUTION A REVIEW

For the next few minutes we will review the history of Dispute Resolution in the construction industry, and evolution of Dispute Resolution Techniques.

By the very nature of construction, there have always been, and always will be, disputes mostly between the contractor and the owner. As early as 1888 the American Institute of Architects and the National Association of Builders produced a "Standard Form" contract between the owner and the contractor. The Architect was perceived in the construction industry, and by owners, as the "Master Builder". He was assumed to know everything required, to interpret the owners requirements for a facility which would live up to the owner's expectation. This meant that the Architect had a great deal of authority, and his statement and opinion were looked upon as "Binding Resolutions" when a dispute arose. There was no need for litigation or formal dispute resolution, because the Architect was the mediator, arbitrator, and adjudicator, all rolled into one. This procedure is still in effect in the construction industry today, and it functions reasonably well on small projects and with disputes that have minimal monetary affect on either the owner or the contractor.

The assumption that the Architect can or should be thrust into the role of mediator, arbitrator, and adjudicator have several obvious flaws.

1. The assumption that the Architect is totally impartial in resolving disputes between the owner and the contractor, is a good assumption except when the dispute arises over errors and omissions in the plans and specifications. Most successful Architects will readily recognize errors and omissions in their plans and specifications, and act fairly and quickly to reach an equitable resolution. However, as in any walk of life, there are those who hold their own interests above fairness.

2. Construction materials and methods have become much more complex and sophisticated. The contractor used to build that which was on the plans, and that was it! Today, the contractor is encouraged to propose materials and methods, which may differ from the plans and specifications, which may save time and/or money while delivering a project equivalent to, or better than that proposed by the Architect. Saving time and/or money will get the owner's attention every time.
3. In the past 20 years or so, we have seen an astronomical rise in construction litigation. People still respect the Architect's position and opinion, but they are more inclined to wish to involve third parties or for the courts to resolve disputes. I believe that the Architect should continue to be the "First Opinion" on any construction claim, because he has the most facts at hand during any point of the construction process, and he is the one who prepared the plans and specifications and understands the intent and desires of the owner. However, the Architect is neither paid for nor educated to interpret contract language nor understand case law.
4. The Architect's insurer would most certainly look with disdain on any Architect who would leave himself open to litigation by assuming the role of mediator, arbitrator, or adjudicator.

Thus, the Architect's role is limited when it comes to dispute resolution. What then is the alternative? Over the past several years the construction industry has turned to Alternative Dispute Resolution as an alternative to litigation. An exhibit which illustrates the various steps, or methods that can be used in Construction Dispute Resolution is attached. We will discuss each of them briefly, and point out the pros and cons of each. Keep in mind that this is an ever changing process, and what you see and hear here today is subject to change without notice.

I would like to note at this time, that there are many organizations which promote ADR, and more are forming every day. I heard of one the other day called DARTF, or Dispute Avoidance Resolution Task Force. The two organizations which continue to be

the leaders in Alternative Dispute Resolution are the American Arbitration Association (AAA), and the Center for Public Resources (CPR). There are also many service organizations which offer construction industry dispute resolution services. The ASFE publication, ADR, pre-listed in 1988 lists 43 such organizations, and I am sure there are many more organizations at this time.

All of this suggests that many people truly believe in the need for an alternative to litigation in resolving construction related disputes.

The first step is Prevention. Obviously, if we can prevent disputes, we don't need Alternative Dispute Resolution, and everyone is happy all the time.....

There are several very basic steps that can be used to help prevent or at least limit the impact of disputes on construction work.

1. Contracts must be written which provide for realistic risk allocation. Contract language, which shifts responsibility from the owner to the contractor, may not even be enforceable. It also immediately creates a defensive attitude on the part of the contractor, since he has little or no control over the issues. Not a good way to begin a project..... This defensive attitude will more than likely become a full blown adverse relationship over time. If risk-shifting sounds like a good deal for the owner in the beginning, it truly has the potential of ending in a disaster.
2. Risks or delays and differing conditions must be clearly defined in the contract as well as in the plans and specifications. The contractor should not be asked to assume the risk of a delay claim for delays caused by the owner, nor for delays beyond the control of the contractor. Neither should the contractor be forced to accept the risk for conditions which differ from those defined in the plans and specifications. However, if there is a claim by either party for delay or differing conditions, a properly defined dispute resolution technique should be in place, within the contract, to resolve the

issues quickly.

Some other techniques which may be used to prevent disputes involve a major effort to establish a closer relationship between owner and contractor from the very beginning of a project. Incentives can be incorporated into the contract, which clearly spell out bonuses the contractor can earn through accelerating the completion schedule or bringing the project in below an established budget. My experience with incentives, however, is that they are not very effective and can lead to another dispute as to whether or not the contractor is entitled to the bonus, and if not who was at fault! I have not had too much positive feedback on this approach.

Another method, currently in use by the Corp. of Engineers, is Partnering.

The Construction Industry Institute defines Partnering as:

"... a long term commitment between two or more organizations for the purpose of achieving specific business objectives by maximizing the effectiveness of each participant's resources. The relationship is based upon trust, dedication to common goals and understanding each other's individual expectations and values. Expected benefits include improved efficiencies and cost effectiveness, increased opportunity for innovation and continuous improvement of quality products and services."

Partnering requires a strong commitment from top level people from the very beginning of the project, and carrying on through completion. Partnering has the advantage of posturing a "We" attitude as opposed to the more traditional "Us vs them" attitude. This process is reported to be very successful on large projects, which involve innovative or non-standard construction techniques, and where large amounts of money as well as high risks are involved.

The second step is Negotiation, which is the simplest and least expensive method of dispute resolution except for the normal Architect's interpretations and decisions.

Two types of negotiations are used regularly. There are direct negotiations with the principals involved in the dispute. This type of negotiation is simple, takes time and is routine on most construction projects. The shortcomings are:

1. When the "Negotiators" do not have the authority to make firm commitments to resolve the problem.
2. When an adverse relationship has built up between the "Negotiators" because of personality conflicts, previous problems which were not resolved mutually, one or both parties refuse to listen to the other party's position, or the "I'm the owner, therefore I'm always right" - "I'm the contractor, and know what I'm doing" routine.

The second type of negotiation is a logical progression of the first, and that is step negotiation. In step negotiations, which must be clearly defined in the contract, the dispute is re-directed to a higher level of decision makers in each organization, should the original "Negotiators" fail to come to agreement. This method is especially effective if one or both of the original negotiators don't want to get their boss involved fearing that such involvement might adversely affect their personal standing with the boss. The downside to this approach is that the higher step negotiators are probably not as familiar with the facts and background of the dispute, and thus more time and effort is needed to bring the new negotiators up to a speed.

The next step is the Standing Neutral concept. This concept is relatively new and my research did not develop any feeling to the extent to which it is being used, nor to its effectiveness. However, my analysis is that it has many more pluses than minuses, and many more pluses than any other currently used methods of Alternate Dispute Resolution.

The Standing Neutral concept involves placing a pre-selected individual or panel (such as Forcon) to serve as a dispute resolver throughout the construction of the project. The individual or panel is referred to as a Dispute Review Board, Standing Mediator,

Referee, Standing Arbitrator, or Adjudicator. This independent neutral entity is put in place at the beginning of the project's construction phase and serves to resolve any issues that the parties to the contract cannot resolve themselves. The independent neutral is immediately available, at all times, to respond to any request for dispute resolution. The immediate availability of the independent neutral allows for prompt resolution of disputes and helps to prevent the development of adverse relationships between the contractor and the owner.

The process of establishing the independent neutral are generally as follows:

1. The contract between the owner and the contractor must specify that an independent neutral will be used, and it must specifically define its role.
2. The parties to the contract select one or three persons, who have the trust and the confidence of both parties to serve as dispute resolvers.
3. In some cases the neutral will be entirely independent. In other cases, each party will nominate one member, and the two nominated members will select a third member; however, even in such cases it is typically required that every panel member be acceptable to both parties, and that all panel members be independent and impartial, without any special allegiance to the nominating party.
4. Depending on the wishes of the parties, the neutral will be given authority to act on disputes by rendering either (1) a non-binding evaluation or recommendation or (2) a binding decision.
5. The neutral is initially given a basic introduction to the nature, scope and purpose of the project, and is equipped with a basic set of contract materials and documents.
6. Sometimes the neutral is requested to meet periodically at the project site with key project personnel for a basic review of project progress, even if there are no disputes to be dealt with at the time.
7. Whenever the contracting parties and the Architect are unable to resolve a dispute, that dispute is immediately referred to the neutral for a prompt recommendation or decision.

8. If the neutral is empowered to make only a recommendation rather than a binding decision, and in the event that a party wishes to challenge the neutral's recommendation, the neutral's recommendation will typically be admissible as evidence in any subsequent litigation.
9. The expenses of the neutral are generally absorbed equally by the owner and the contractor.

"Advantages"

The advantages:

1. The dispute can be resolved speedily.
2. The neutral is voluntarily selected by the parties, before any dispute arises.
3. The neutral has construction expertise.
4. Pre-selection of the neutral saves the time and difficulty which would be required to select the neutral after a dispute has arisen.
5. The neutral has the benefit of familiarity, continuity and accumulated experience on the project.
6. The dispute can be resolved while facts are still fresh.
7. The parties are more likely to accept the recommendation or decision as fair, because they have confidence in the expertise, knowledge, and integrity of the neutral.
8. Where the decision is made by an arbitrator, it is final and binding, and thus there is no uncertainty about the outcome of the dispute.
9. By including the provision in bidding documents, the owner is likely to obtain lower bids, because this procedure shows that the owner is interested in prompt and fair decisions, cooperative relationships, and making fair payment for changes and changed conditions, and the contractor need not include as high a contingency for the possibility of unresolved claims.
10. Payment to the contractor for any changes is speeded up.
11. The dispute is resolved before it becomes unmanageable.

12. The disruptive effects on job progress of deferred and accumulated unresolved disputes are avoided.
13. The heavy expenses, risks and uncertainties to all parties of a massive project-end lawsuit or arbitration proceeding are avoided.
14. It requires the parties to identify problems early and deal with them promptly.
15. It encourages the parties to communicate with each other.
16. It encourages the parties to evaluate their positions realistically.
17. It encourages straightforward dealing and discourages game-playing and posturing.
18. It improves relationships between the parties.
19. The certainty that the problem will be resolved promptly and fairly by the neutral encourages the parties to seek a mutual solution to their problem without even involving the neutral.

The Disadvantages:

1. Cost of setting up this panel or individual.
2. Difficulty in obtaining high quality panel members.
3. Undue early attention to a negative subject.
4. Resistance to a new and unfamiliar concept.
5. Possible animosities created by diverting attention to disputes at a time when parties should be working together to construct the project.
6. Detrimental effect on the project of diverting valuable resources from construction activities to hearings.
7. Possible resentment of party who loses the decision.
8. If the process calls for a final and binding decision, this takes control away from the parties.

The conclusion about the Standing Neutral concept is that appears to be the best alternative in Alternative Dispute Resolution. It is based upon independent judgement, is job site related, and reasonably cost effective.

The next step is Non-Binding Resolution thru mediation, mini-trial, advisory opinion, and advisory arbitration.

Mediation is very simple in concept and is currently the most widely used and accepted procedure in Alternative Dispute Resolution. Mediation is a process of resolving disputes through settlement conferences conducted by a neutral third party. The mediator does not have decisions favoring either party but; can identify and re-state the issues causing the dispute; bring to the disputants attention consequences of favoring either position or neither position; can seek to find common areas of agreement; stimulate communications; identify internal and external influences and delay consequences.

The mediator must be absolutely impartial and non-decisional. He or she must earn the trust and respect of the disputants by demonstrating the impartiality and preserving the confidentiality of each party's protected information.

Obviously the skills of the mediator are paramount to successful mediation. A good mediator need not be a lawyer, architect, or a person with heavy construction experience, but a person with excellent communicative skills, a dedicated listener, and a good "Persuader". These individuals are very hard to find, but the American Arbitration Association (AAA) and the Center for Public Resources (CPR) are probably the reliable places to begin.

The mini-trial is a more formal and structured example of Non-Binding Resolution involving discovery, formal presentation of each party's position, and negotiations between decision making representatives of the disputants. The advantages to a mini-trial are that more details of each party's positions are made available and the process requires decision making Principal's involvement. The drawback is that this process lacks the "Third Party" who could move things off of dead center and attempt to persuade resolution.

The concept of Advisory Opinion or Advisory Arbitration is sometimes used where the resolution requires an expert or experts in the field for which the dispute is about. The experts are chosen by much the same process as a mediator might be. This process is cumbersome due to the problem of finding experts who are agreeable to both parties, the process is expensive and time consuming due to the cost of the experts, it is time consuming due to the time it takes the experts to prepare, and has the potential of further dividing the disputants by fact based firm positions of the experts. Again the absence of the "Third Party" could be the difference between resolution and litigation.

Most of you are only too familiar with the last two steps Binding Resolution and Litigation, so I will skip over them. These issues, while extremely important and valuable to the process of Construction Dispute Resolution, are the most expensive and time consuming of all of the dispute resolution techniques now being considered. What we have tried to do here is to outline several procedures involving extensive discovery, high cost, lengthy litigation, and absolute adverse relationships.

Of the techniques presented, we favor the Standing Neutral concept as previously stated. However, I am sure the Insurance and Construction Industries, the Lawyers, and the Consultants will continue to further develop means and methods to resolve the inevitable disputes which are always a part of the complex process of construction.