Dispute Resolution in Construction Projects

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Construction disputes are fairly common, and they vary in their nature, size, and complexity. In fact, construction disputes are among the most common among arbitration proceedings.

Furthermore, the complexity of a contemporary construction project, which requires the orchestration of numerous interdependent components including information, materials, tools, equipment and a large number of personnel working for independent engineers, contractors, and suppliers, add to the complexity of the disputes arising out of or in relation to them.

When not resolved in a timely manner, arbitration disputes can consume considerable resources in terms of finances, personnel, time, and opportunity costs. The apparent expenses (e.g., costs of attorneys, expert witnesses, the dispute resolution process itself) alone are significant. Although difficult to quantify, the less visible costs (e.g., company resources assigned to the dispute, lost business opportunities) and the intangible costs (e.g., damage to business relationships) are also considerable.

Innovative Methods of Dispute Resolution in the Construction Industry

Over the past decades, the construction industry has made remarkable progress in developing more efficient methods of dispute resolution. In fact, experts frequently refer to the construction industry as being on the innovative edge in this field. However, in particular, the issue of dispute prevention appears to not have been the focus of the construction industry; dispute prevention mechanisms are frequently disregarded when drafting construction contracts and dispute resolution clauses.

Current practice in construction dispute resolution generally reflects one of two perspectives: that one resolution method fits all disputes; and that dispute resolution offers a selection of independent stand-alone choices. Still, it is
more effective to approach dispute resolution in a more analytic manner similar to, for example, a medical professional—first diagnose the problem, and then select the least invasive procedure that will correct it. Cost-effectiveness and timeliness are critical factors for dispute resolution, in particular in the construction sector. Therefore, a flexible framework—a strategic approach to dispute prevention and resolution that employs a neutral advisor, early intervention and the ability to tailor the resolution method to the particular nature of the dispute—offers a more effective method of dispute resolution than the static mechanisms currently dominant in the construction industry.

A number of different alternative dispute resolution methods are frequently utilized in the construction industry. The more common methods are:

- negotiation—a provision requiring the entities directly involved in the dispute to seek resolution through direct negotiation is frequently included in construction contracts;

- dispute review boards—such dispute review boards typically consist of one or a number of neutral experts who visit the site periodically in order to monitor potential problems. The parties can authorize the board to, upon their request, conduct informal meetings on an arising dispute and issue an advisory opinion that is not binding for the parties but may be used by them as a basis for further negotiations;

- mediation—is a forum in which an impartial person, the mediator, facilitates communication between parties of a dispute to promote reconciliation, settlement or understanding among them;

- arbitration—is a forum in which each party to a dispute and its counsel present the positions of the parties before an impartial third party, who renders a specific award.

The prevalence of construction disputes indicates that the current approach to dispute resolution is not effective enough. First, construction contracts tend to address dispute resolution by specifying the resolution method(s) to be used. Second, dispute resolution methods are too frequently viewed as a selection of stand-alone choices. What construction contract and the persons drafting these frequently overlook is that dispute prevention and dispute resolution methods can be effectively combined into more comprehen-
Three Stages of Preventing or Resolving a Dispute

The first stage addresses prevention. To successfully prevent disputes in construction projects, it is vital to understand the particulars of the specific project. In this regard it may be prudent to involve an impartial third party, i.e., a dispute review board, throughout the life of the construction project. Such a dispute review board adds value by assisting the parties in the development of applicable dispute prevention techniques, which include:

- risk assessment and allocation, including detailed project scope definition;
- partnering, including creating a set of common project goals;
- contract clauses that outline a flexible framework for dispute resolution.

The success of a construction project and the prevention of disputes depend heavily on proper risk assessment and allocation. Inaccurate risk assessment or a lack thereof can result in significant changes and rework, resulting in added costs and delays. Detailed project scope definition is a major component of risk assessment, in that scope changes pose a threat to the project’s success. Changes frequently lead to (sub)contractor claims, and while a certain number of changes are inevitable in a complex project, the author’s experience indicates that thorough project scope definitions prior to the start of detailed design avoid a large number of changes. A well-defined project scope allows the client or main contractor to effectively communicate his desires to the (sub)contractor and provides him with the information needed to execute the project to meet the client’s/main contractor’s requirements.

Inter-party Negotiations

The vast majority of disputes are resolved by inter-party negotiations without external intervention. Where inter-party negotiations fail, construction contracts commonly offer the parties only one option: to seek dispute resolution through third parties, usually by way of litigation or arbitration. Still, not every dispute that cannot be resolved by
the parties themselves requires a binding decision by a third party for resolution. As litigation and arbitration are often costly and time-consuming, it is advisable to first engage more flexible methods. At this stage, the involvement of a dispute review board adds value as such a board may conduct informal meetings to assist the parties in resolving the dispute in a timely and efficient manner before it escalates to a point that severely impacts the project. By issuing advisory opinions rather than binding decisions on the arising dispute, such a board can assist the parties in finding a basis for more focused negotiations.

The most visible benefits of this early stage dispute resolution method are its lower costs and timely resolution. In addition, assisted negotiations do not interrupt a construction project in the same manner as litigation or arbitration usually would and helps to maintain good relations between the parties.

Arbitration vs. Litigation

Nonetheless, some disputes cannot be resolved by negotiation. Therefore, a comprehensive dispute resolution framework has to include means to resolve these disputes such as mediation, arbitration or litigation. Still, in particular in complex construction disputes, understanding the construction industry and construction disputes is vital for advising and deciding on such disputes. While the parties may choose counsel who has such understanding, the parties do not have the option of selecting judges in litigation procedures. In this respect, arbitration offers an advantage. It allows the parties to choose arbitrators who have experience in construction disputes. Thereby, choosing arbitration over litigation as a means of dispute resolution may provide the parties of a construction dispute with higher quality decisions.

Best Solution: a Combination of Multiple Dispute Resolution Methods

These dispute prevention and resolution tools are not to be understood as a one-fits-all standard, but rather a selection that may be shaped to fit the specific requirements of the individual project. To do so, special attention must be paid to the construction contract’s dispute resolution clause. It should combine multiple dispute resolution methods and provide for different stages of escalation. At the least, it should combine requirements to attempt to resolve disputes through negotiation with dispute resolution through third parties. Thus, the dispute resolution clause should provide that the parties are required to seek dispute resolution through direct negotiation. At the second escalation stage, the clause should determine that where a resolution cannot be reached through negotiation within a predetermined period of time, the dispute should be referred to a third party for resolution, usually through mediation or arbitration. To provide further flexibility, the dispute resolution clause can stipulate that prior to resorting to arbitration, the parties are required involve a dispute review board that participates in the negotiations between the parties and provides suggestions for the resolution of disputes. Furthermore,
the parties may be committed to submit to mediation prior to filing a request for arbitration.

In summary, the proposed framework offers multiple benefits. It provides a comprehensive system that emphasizes prevention and collaborative resolution. In addition, it encourages resolution close to the source of the dispute, involving the parties in a participative, relationship-preserving process. Furthermore, through involving a third party, i.e., a dispute review board, at an early stage, it provides continuity regarding dispute prevention and resolution. Finally, it limits the cost and time required to resolve disputes.