

Understanding Dispute Resolution Options in the Construction Industry

Introduction

Disputes and claims are common in the construction industry. Projects are unpredictable, and problems can occur for any number of reasons, including, but not limited to, design changes, delays, material cost increases, bad weather conditions, unexpected site conditions, payment issues, or a combination of these and other factors.

There are a number of methods available to resolve such disputes. Why should you care which method is used? You should care because efficiently resolving claims can mean the difference between the survival or failure of a project and the survival or failure of your construction business. Dispute resolution is often costly in terms of time, emotional energy, business relationships, and finances; therefore, it is critical to the health of your business that you be knowledgeable about dispute resolution options. While there are many dispute resolution options available, the most common are litigation, negotiation, mediation, and arbitration. This article provides an overview of these four methods of dispute resolution in the construction industry.

The time to decide which dispute resolution method(s) to use is not after a dispute arises on a construction project, but during the formation of the construction contract. A well-drafted construction contract will include provisions that set forth the process for the parties to the contract to follow in the event of a dispute. All standard form construction contracts have dispute resolution provisions. Some prescribe the procedures, and some allow for election of options, with a default to one particular method if no election is made. You should always review and, if necessary, negotiate the dispute resolution provisions in all contracts you consider signing.

Your surety bond producer can help you spot dispute resolution issues in your contracts, and your construction/surety attorney can advise you on the legal implications of the dispute resolution provisions and help you negotiate those provisions.

For many years the primary method for resolving construction disputes was litigation in federal or state court. The “I’ll-see-you-in-court” approach is not as favored a method to resolve disputes as it once was. The construction industry has been at the forefront of alternative disputes resolution (ADR) methods for many decades. ADR is simply any method of resolving disputes other than by litigation. ADR techniques are being used instead of protracted litigation to resolve construction disputes. While there are many forms of ADR, the most common are negotiation, mediation, and arbitration.

This article briefly describes litigation and the three common ADR methods and the advantages and disadvantages of each method of dispute resolution.

Litigation

Litigation is the time-honored tradition that begins with filing a lawsuit in a state or federal court and continues until the court issues a final decision or the parties give up and withdraw the lawsuit. Some construction firms want “their day in court.” And, unlike with many ADR methods, a party that loses in litigation has the ability to appeal the result. Litigation, however, provides the parties with less autonomy to shape their resolution than most ADR methods.

Litigation is often criticized as costly, in terms of both time and money. Not only can litigation be expensive, with attorneys’ fees and experts’ fees, among other expenses, but also litigation can take a long period of time to reach resolution of the disputed issues. Another criticism of litigation is that judges, despite years of experience, are often not knowledgeable about construction terms, procedures or standards. Jurors have even less experience and, therefore, the result of construction litigation is uncertain. Litigation is highly adversarial and seldom ends with the parties doing business together in the future. In addition, a construction firm should keep in mind that litigation is very public, and filed documents are often available online.

Alternative dispute resolution methods were developed to address and mitigate these criticisms of the litigation system.

Negotiation

Obviously, the most direct method for resolving disputes is for the parties to work out their differences through skillful negotiation. Negotiation is a voluntary process by which parties attempt to reach a mutually satisfactory agreement through discussions. It is in negotiation where the parties have the most control over the outcome of the dispute. A negotiation can be, and usually is, unassisted, where the disputing parties address the issues and arrive at an agreement without a third party. A negotiation can also be facilitated, where a neutral person is invited to guide the disputing parties towards reaching an agreement. Successful negotiators typically focus on problem solving and trying to satisfy both parties’ interests without determining who is right and who is wrong.

In the process of negotiation, the parties are in control of the outcome and can walk away from the process at any time. While the parties can use attorneys to protect their interests in the negotiation, it is not required. Negotiation is an especially valuable dispute resolution option where the parties seek a future business relationship because negotiation is less disputatious than litigation and other forms of ADR and fosters an atmosphere of cooperation.

Mediation

Mediation is a non-binding ADR mechanism in which the disputing parties use the assistance of a third party, a mediator, to help them reach a settlement. The mediator should have expertise in the construction industry. A mediator is a facilitator and does not decide who has the correct position or how much money should be exchanged to resolve the dispute. The mediator's role is to ensure the parties understand each other's position and ask tough questions to help the parties reach settlement. The mediator has no authority to force an outcome on the parties, and either party can walk away from the mediation at any time. For a mediation to be successful, all parties must enter the process with a good faith intention to settle the dispute.

While parties can agree to mediate at any stage of a dispute, many standard form contracts include a mediation provision that requires the parties to attempt mediation of disputes before resorting to binding dispute resolution, such as litigation or arbitration. Mediation is less costly than litigation and arbitration, as there is usually no discovery of documents, no motions to the court or arbitrator, and no depositions. And the time period from initiation of mediation to settlement is usually much shorter than the time period for the litigation or arbitration process.

While the use of attorneys is not required in mediation, it is often a good idea to have legal counsel to provide advice and guidance and to represent the construction firm's interests. Like negotiation, mediation is an excellent dispute resolution option where the parties seek a future business relationship.

Arbitration

In arbitration, a dispute is submitted to one or more impartial persons, usually experts in the construction industry, who decide the outcome. Unlike mediation, arbitration results in a private, binding, court enforceable decision. The arbitrator's decision may be appealed to a court having jurisdiction, but an arbitrator's decision can be reversed only in exceptional circumstances, such as obvious bias by the arbitrator or fraud. While the use of an attorney is not required in arbitration, it is prudent to have an attorney represent your construction firm's interests during the arbitration process.

Arbitrations are often by voluntary agreement of the parties in a pre-dispute contractual agreement. Many standard form construction contracts have arbitration clauses, which set forth the terms of any arbitration between the parties or which reference a third-party provider of dispute resolution services, such as the American Arbitration Association (AAA), to administer any arbitration under that contract. The parties to arbitration must pay substantial filing fees and the arbitrator's fees, but arbitration is almost always less costly than litigation.

The arbitration either has one arbitrator or, with more complex disputes, a panel of three arbitrators, usually attorneys or judges with construction industry expertise, and sometimes an engineer or contractor. Although arbitration is more structured than

negotiation or mediation, and is quasi-judicial in nature, it is more flexible, and generally less costly, than litigation. Arbitration involves typically limited discovery and simplified rules of evidence. An arbitration hearing can last one day to many weeks, depending on the complexity of the issues. The arbitrator or the arbitration panel issues a written decision, called an arbitral award, which is not public record. This arbitral award is final and binding on the parties, absent extraordinary circumstances. Arbitration can be as adversarial as litigation.

Conclusion

When considering dispute resolution options, a construction firm should work with its construction/surety attorney to determine the best method(s), keeping in mind that the end-game is to resolve the dispute quickly, efficiently, and cost-effectively; to maintain (if possible) the business relationship; and to focus resources on the core business. Although traditional litigation may be necessary in some cases, most construction disputes should be resolved through ADR methods. ADR procedures generally are more cost- and time-efficient than litigation, give the parties more control over the outcome, and allow the parties to preserve future business relationships. Remember that winning at all costs is seldom a real victory and that compromise of a dispute is often sound business judgment.