

## Dispute Resolution *During* Construction – the Value and the Process

In a construction project, parties bring unique resources and expect benefits in return. This pattern mirrors the work of skilled professionals who promptly settle disputes during a construction project. Here are a few of the many reasons prompt settlement of construction disputes is superior to any other delayed approach:

- Less expensive overall
- More accurate, and more just
- Shorter in duration and earlier in calendar time
- Produces a better finished project, in time cost and quality

### **Why successful dispute resolution during construction is rare**

Lawsuits are quite prevalent whereas successful dispute resolution, concurrent with construction, is relatively rare. Why? Mainly, it comes down to these four reasons:

1. The parties aren't ready to solve a difficult controversy.
2. They haven't budgeted for the cost of dispute resolution.
3. The "honeymoon" attitude of getting a project underway hasn't worn off yet.
4. Enamored of their positions, they don't see the value of resolution over rigidity.

Despite these hindrances, it is possible for an experienced dispute resolution professional to solve even the most complex controversies during a project. Knowledge of the tools needed for resolution and the willingness of a skilled professional to convince others of the value of prompt resolution can save time, cost and improve the quality of the construction.

The following stories and data come from large projects, usually over \$10 million. Given the right attitude and good training, prompt dispute resolution can also be done on smaller projects. We will cover some of the tools to scale these techniques to smaller projects.

## **1. *Negotiations and Global Settlements***

When a project goes bad, often the individual changes can become so numerous and interdependent as to compromise effective negotiations. When push comes to shove, numerous claims can be grouped together into a “global settlement.” Certain changed conditions, (e.g. time, productivity, multiple changes and changed changes) cause standard negotiations to bear little fruit. (Please note the “step negotiation” process, described on page 4.)

One can assemble a set of generally related unresolved changes into a single claim. The strength of this approach relies upon the coherence of the elements. The most common theme is incomplete design. If a group of unresolved changes can be identified in this way, they can be pulled out of the normal business cycle of the project and resolved in a global settlement, while the remainder of the project continues unabated. This strategy is worth considering, especially because of the improved atmosphere made possible when the uncontested portions of a project are kept moving. This is especially true when the project goes really, really bad.

### **A Large Claim and Step Negotiation During a Large Project**

When I was employed at a consulting engineering company, my staff and I worked to settle a \$5.2M claim during an airport parking garage project. The project was bid at \$35M, the time was short and construction was less than half done when the global claim was submitted. The contractor and the project team designed a global claim settlement system on site, engaging both the City’s Department of Public Works and the contractor’s parent company in Europe.

The claim elements were grouped around the central theme of the contractor’s assertion that the project, a 6-story parking garage, was rushed through design. We researched 73 claimed change orders in this group. We separated outside issues, maintained ongoing construction and developed a stepped negotiation.

The owner, my client, reviewed the individual claims with us, and we developed a scope and order-of-magnitude estimate for each claim. We created a contemporaneous time-frame schedule analysis to contest the claimed “but-for” schedule analysis. The pricing of the changed conditions included many force-account change projects. The force-account changes occurred

because agreement could not be reached on many urgent changed conditions and time extension requests.

### **Resources Needed**

The most important aspect of this portion of our project was the added resources needed to prep and respond to the claim. In our case, for each time extension request, we had to analyze the conditions when the time extension request was made. This required re-analysis of each monthly schedule update to allow for a time extension in the correct month. This was a significant effort that should have been performed monthly by the contractor, but they avoided it despite many requests. Eventually we withheld funds to force them to do the task (an approach normally seen as draconian and not a recommended except in the direst circumstances.) The fund withhold triggered the contractor to develop their claim, (and many letters of protest) so we felt that our purpose was served. The dispute resolution was underway instead of languishing.

The claim was largely a delay claim with acceleration costs and delay damages. Therefore the time analysis needed two layers of examination because the contractor said that he could have done the work on time. He added expenses to try to correct for the design errors, but missed anyway and had delay damages. We showed that both were partly true.

The delay claim was presented in a “but-for” analysis, producing approximately twice the delay caused by the owner than was reasonably appropriate. We took the schedule at the onset of the claim period and inserted approvable time extensions into each month’s updates by extending the impacted activities (not the end date) and rerunning the schedule at that point. We had requested that the contractor do this type of time analysis, however, he opted for the more advantageous (and inaccurate, in our opinion) “but-for” style of time analysis.

### **“But-for” analysis**

In “but-for” analysis, the claimant simply inserts all of his allegations of time impact into the critical path of the project. This process extends the end date of the project, solely at the burden of the owner, and hides a multitude of sins of the contractor. The name of this type of analysis comes from the assertion that “we could have finished on time ‘but for’ the actions of the owner.” Because of this conflict, the settlement took three months longer to solve than might

have otherwise been the case. During the earlier part of the project, we had to accept the incorrect monthly updates (without approvable time extensions) so that we could have the record of the as-built conditions from which to make our contemporaneous adjustments.

One additional wrinkle is that the owners purchased back an acceleration period applicable to a critical milestone. Because this was paid outside the claim, it was excluded from the claim analysis and had a separate “window” analysis. It was a short-term, urgent situation that came and went before the global settlement could be reached. The fundamental difference in velocity of the acceleration of a specific milestone and the complex negotiation of the global settlement separated them in time and process.

To accomplish the contemporaneous time extension analysis, we added a full time scheduler and half-time administrator, as well as significant time from our Assistant Project Manager, who picked up the day-to-day work of the project. I acted as Project Manager. Because of the extraordinary skills of the Assistant Project Manager, the day-to-day management of the project was significantly turned over to her. Our Principal-in-Charge invested considerable time in developing the claim analysis project. He made the proposal to the skeptical Department of Public Works and City Council.

As the global settlement process was starting up, we applied for and were granted \$500,000 for an Acceleration Program, mentioned earlier, for delivery of a major milestone about 6 months earlier than projected. The skepticism from the City staff was significant at the outset. “Claim mode” mentality was setting in to the City staff and the contractor’s staff. By this, I mean some people were becoming gloomy, unmotivated or just plain prickly. More than once I heard that the project would generate at least three years of litigation after we opened the facility. Therefore we needed to get the global settlement program up and running quickly. We needed both approvals (added staff for global settlement analysis and acceleration program) very quickly. Of course, the request for the claim analysis funding implied a future request for funding for a settlement to follow. It was a tricky period.

## **Step Negotiation**

At the outset, we analyzed all of the change orders, monthly schedule updates, and began

negotiations with the project staff on each of the eventual 73 change orders that made up the global settlement. On-site negotiations bogged down quickly, due to complexity and interrelatedness of claims.

The negotiations then became an information exchange, wherein we learned the actual costs that would make up a global settlement amount. Both parties discussed a global settlement approach and I, as Project Manager, was informed that communications were occurring between the highest levels of the owner's and the contractor's parties. We got a global settlement by developing an order-of-magnitude estimate of the individual project changes, acceleration claims and delay damage claims. Based on this preliminary assessment, I presented a range of global settlement figures to the owner's group. Those conversations created a negotiation range that might pass the necessary approvals inside the City.

The Project Manager for the contractor then met with me during a lunch at my office in the job trailer. I split my sandwich with him and asked him for a number. He said that \$2.9M was the lowest he could get approval for. I told him that I had no approval, but I didn't want to ask for approval for anything more than \$1.9M, based on the analysis we had completed so far. The higher claim didn't appear to be justifiable. He committed to make available new data, which would justify a higher settlement.

Significant in the "unknown costs" areas, were the soil and underground utility conditions for a signage program at approximately 30 locations along a 3.5-mile stretch of highway outside the airport. These would require delicate excavation by hand, still underway. Allowing for adjustment based on further information to be supplied, we worked our way toward a preliminary number of \$2.125 million.

My confidence was based on the months spent working with these numbers. I needed confidence because I was aware that this number would be difficult to adjust as soon as the contractor's project manager left the office.

### **Change Orders and Approvals**

Despite my confidence that the preparation was sufficient to justify the agreement at that figure,

my chief estimator didn't agree with the process. I had to do all the negotiation and writing of 73 change orders myself. This would have never been accomplished without the substantial added services request negotiated with the City by my Principal-in-Charge, and the skilled backup of my Assistant Project Manager. The change orders were approved, the special milestone was met, the tenant airlines moved in, and the garage opened in phases, as agreed in the settlement – and *no* litigation resulted.

## ***2. Facilitated Negotiation During the Project***

### **Facilitators**

Often a non-participant in the project can be utilized to solve a tenacious dispute during a project. I have seen skilled attorneys, disinterested parties or even peripheral but not completely independent parties solve disputes. Occasionally technical experts in a specialty can bring specific knowledge to a negotiation and solve an issue as it becomes disputed.

### **Termination**

I have worked on 50 or more termination disputes. By far, the majority of terminations have gone to mediation for issues that remained contested after the termination. These are particularly difficult, because feelings are raw, many technical issues are unresolved, and the completion of the project and resulting entitlements are hotly contested. But technically, the project is not underway and the contract applies only in the Dispute Resolution clauses. We cover those clauses below.

We need to return to the period before termination for a moment. Termination clauses in contracts are occasionally a source of dispute, when some contest can be found as to whether the contract can be terminated or not. Most of the time, the parties have commonly agreed to terminate. Termination for cause or convenience, and contentions about the cause are often disputes, however they fall beyond the scope of this paper. When a project goes bad, the choice of termination should carefully follow the contract language.

### ***3. Contract Clauses for Dispute Resolution***

Two families of form contracts are in common use in North America:

AIA, American Institute of Architecture, [www.aia.org](http://www.aia.org)

ConsensusDocs, [www.consensusdocs.org](http://www.consensusdocs.org).

The differences in clauses handling dispute resolution during the contract are informative. We have looked at two contracts from each family:

1. AIA A101, The Contract between Owner and General Contractor
2. AIA B102, The Contract between Owner and Design Professional
3. ConsensusDocs 200, The Contract between Owner and General Contractor
4. ConsensusDocs 240, The Contract between Owner and Design Professional

## **AIA Dispute Resolution Clauses**

AIA A101, Article 6 - Owner and General Contractor

At the outset of a dispute, either party can submit it to an Initial Decision Maker, or to the Architect. Additional information is contained in “The General Conditions of the Contract” A201, Section 15.2. The IDM or the Architect produces a non-binding opinion and the parties are left to negotiate further based on those findings or to proceed to a binding solution.

Binding Solutions: Article 6 continues to send the parties to Arbitration or Litigation. Additional information is contained in the General Conditions A201, Section 15.3.

AIA B102, Article 4 - Owner and Design Professional

The risk exposure for the design professional is limited to 10 years. To further protect the designer, insurance proceeds prevail, and no consequential damages are recoverable from the designer. However, the exact meaning of these clauses is beyond the scope of this paper.

Regarding dispute resolution clauses, AAA Mediation is mandatory, whereas demand for

binding solution is okay concurrently, but is stayed for 60 days. Hearing on-site, settlements binding. The choice after that is to arbitrate or sue.

## **ConsensusDocs Dispute Resolution Clauses**

General, ConsensusDocs 200 Article 12 for owner/GC

### *Conversation with Contract Clause author*

I spoke to a senior member of the committee that drafted these dispute resolution clauses. He reported that one of the main goals was the development of a flexible process. The intention was that the parties be given choices in order that they develop their own program based on their particular project. The feeling at the outset was that the AIA contracts were too protective of the designer and that all parties should approach the dispute resolution process as peers.

### *Personal Experience*

In my experience, many outside hierarchies, such as military or legal, can generate a feeling that one party should be directing or controlling the dispute resolution process more than another. This destructive attitude is one of the biggest impediments toward effective, efficient or prompt dispute resolution. Inside the world of construction, governed by well-drafted contracts, all parties should be peers; they serve the contract in their specific roles, but remain peers in the dispute resolution processes. I have learned that the approach to dispute resolution that highlights equal standing of parties at the outset is more effective, efficient and successful than any other setting for dispute resolution.

### *Step Negotiation*

In ConsensusDocs 200, between Owner and General Contractor, either party can initiate negotiation within five days of notice or knowledge of a dispute. If Negotiation breaks for more than 15 days, the dispute moves on to a Mitigation Strategy, described below.

### *Mitigation Strategies*

Mitigation strategies are the key to the difference between the ConsensusDocs and any other contract form. In a smaller project, a project neutral is named and counted upon from the outset. In bigger projects, a Dispute Review Board of three panelists (DRB) is used. DRBs

are significant tools in dispute resolution during construction and a detailed discussion follows.

#### *Mediation*

After an opinion is delivered, a negotiation follows in which an agreement is sought. If this fails, a facilitated negotiation using a mediator might be needed. Mediation, if needed, will be conducted under AAA Rules for Mediation. Such a process starts in 30 days and ends in 45 days. If there is still no resolution, a binding result can be obtained under the following steps.

#### *Binding Dispute Resolution*

Either party can file for Arbitration under the AAA rules or institute civil litigation in the appropriate court.

ConsensusDocs 240 Article 9 Owner Architect Agreement

This matches the three-step system above for Owner/GC.

### ***4. Dispute Review Board (DRBs)***

This dispute resolution process, designed to occur during the construction project, started with the Eisenhower Tunnel above Denver in 1975. Since then, the growth of DRBs has averaged 15% per year through 2010. Now DRBs are included in approximately 200 contracts per year. A foundation has been established to define and promote the process, the Dispute Review Board Foundation (drbf.org). The DRBF built an elaborate database of 1,800 projects using DRBs. In those projects 98.7% of the disputes were settled. They were primarily larger projects; only six were under \$ 1M. Many projects had no disputes at all, and many had multiple disputes. The BART extension into San Francisco Airport saw 11 disputes. Los Angeles County Metro had 24 busy panels. Caltrans has used DRBs on over 300 contracts. The Florida Department of Transportation has used DRBs in more than 400 contracts.

#### *Formation and Operation*

A DRB is part of a contract. As in ConsensusDocs, it is created after contract award, and before the beginning of construction. Selection of Board Members must include full disclosure and

acceptance of the Members by both parties. No ex-parte communications can take place with Board Members. The Members stay abreast of the project. Hearings are conducted as requested and the Board produces opinions.

### *Project Neutrals*

In most cases, the Project Neutral works in the same manner as a Dispute Review Board. Caltrans has instituted single Neutrals on Projects \$3M to \$10M.

## **5. Mediation**

This discussion of mediation pertains only to mediation conducted inside a contract during a project. As in other cases, the mediator facilitates a negotiation with special privileges, particularly ex-parte communications. A mediator is not usually used in a construction project setting because he would not be familiar with the project, like a DRB member or a Project Neutral who is engaged at the outset of the contract. The cost of bringing someone up to speed with the project in the middle is usually a hurdle.

## **6. Arbitration or Litigation**

These processes produce binding results, so the advantages of prompt dispute resolution during the project are not applicable. I will take a minute to define the term “binding.” In construction dispute resolution, binding or non-binding means enforceable by a court or not. Such enforcement includes collection procedures and so forth. Non-binding does *not* mean “unenforceable.” A non-binding finding of a DRB can be entered into an arbitration or trial. It will have great influence since well-informed parties in a neutral setting produced it at the time of the project. So non-binding does not mean pointless or without influence. It does mean faster, cheaper and, in my opinion, more likely to be accurate.

## **7. Conclusions**

Dispute Resolution during a project has advantages and costs. At the outset, the key question for the project sponsor is one of risk mitigation. It is clear that prompt resolution is less costly in terms of process cost than delayed resolution. The sponsor may feel that potential dispute outcomes are compromised, where the most elaborate and defensive positions might be

conceded for speed or efficiency in a resolution process. Following this logic, parties sometimes feel that the most elaborate and risk-averse position would be binding arbitration or litigation. In my 40 years in construction, 28 of them primarily in construction dispute resolution on over 600 dispute resolution projects, these approaches toward dispute resolution are *not* the most efficient or successful risk management tools.

#### *Costs and Comparisons*

The DRBF and other centers of dispute resolution study have given much attention to comparing the various types of dispute resolution with one another. When measuring risk, cost of a risk management technique is difficult to state clearly as an absolute. It is therefore awkward to compare any one process to having no risk management technique. Too many unknowns exist in the increasingly today's complex world of construction.

#### *Risk Management Planning*

Further, the construction industry is now sufficiently complex that one cannot just guess at it. Having no risk analysis for determining the correct dispute resolution system for a project is similar to having no dispute resolution system at all. Some risk analysis is clearly appropriate in all construction projects. All projects have very different risk exposure aspects and different dispute resolution processes are appropriate for each. The tools of prompt and efficient dispute resolution need to be considered in advance so that they can be included in the contract clauses, when appropriate.

When I'm called on for dispute resolution *during* a project, in my experience the attitudes of the most seasoned project sponsors follow a pattern:

- Risk aversion becomes risk management
- Defensiveness turns into efficiency in dispute resolution
- Posturing changes to negotiation
- Delay transforms into prompt attentiveness

Conducting dispute resolution in the midst of a construction project that has gone bad becomes a highly valuable process.

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