Understanding ADR contract clauses

Alternative dispute resolution provisions set forth the forum and procedure for any disputes; here's a look at these contract clauses. **by Scott Wolfe Jr.**

It's extraordinarily common for modern construction contracts to contain provisions detailing what must be done in the event of a dispute. These provisions are referred to as "dispute resolution" provisions or, in the event that they mandate the use of a non-litigation resolution forum like mediation or arbitration, may be referred to as "alternative dispute resolution" provisions. Everything else in the construction contract really culminates in these dispute resolution provisions because they impact any dispute between the parties. Unfortunately, like most everything in law, they are mired in shades of gray.

• **Standard ADR Provisions.**

The remainder of this article will discuss legal nuances surrounding common or bespoke ADR provisions. First, however, let's examine more standard ADR provisions and interpretations, which likely make up the majority of scenarios.

When looking at any construction contract, it's likely that the ADR provision's language comes from one of three locations: The American Institute of Architects (AIA) contract documents, ConsensusDOCS, or the recommended provision from the American Arbitration Association (AAA).

There is a healthy debate between lawyers and those in the construction industry about the fairness of these provisions to various parties, but in large part, the biggest benefit of these provisions is that they are standardized and have reliable interpretations. In other words, the parties know what they're getting into and can pretty easily digest the provision and understand its impact.

So, what is the impact?

Standard ADR provisions fall into one of three categories or levels:

1. The most basic requires that the parties submit any disputes to binding arbitration. In the event of a dispute, this simply replaces the act of filing a lawsuit with the filing of an arbitration proceeding;

2. Many will require that the parties submit disputes to mediation first, and only if the mediation is not successful can the parties proceed with a binding arbitration proceeding.

3. The AIA dispute resolution provisions recently introduced a "third party neutral" as a first decider of disputes, requiring parties to submit disputes to some third party for a preliminary decision. If the dispute continues, the parties can then proceed to mediation, and then to arbitration if necessary.

This is a high level overview of the standard ADR provisions. In practice, one can have a mix and match of all three ADR levels and even perhaps reserve the right to litigate.

Generally, the standard ADR provisions are easy to digest and provide a fairly clear understanding of the dispute resolution procedures for parties faced with a disagreement.

• **Custom ADR Provisions.**

The concept of standardized construction contracts and provisions is a beautiful one. Unfortunately, however, the reality is that these contracts and provisions are too frequently edited, re-edited, or replaced entirely, which defeats the purpose of the contract sets and leaves the parties in a more confused state than before.

Parties have different appetites for ADR. Some folks think very highly of ADR, and others don't. Sometimes companies feel like the more expensive and complicated processes can work to their benefit, as they can leverage the difficulty and expense of a legal process to push other less-funded companies to make stronger compromises.

The result of these different appetites is the creation and re-creation of thousands of different ADR provision various; each provision containing a nuance slightly different from the other. Unlike the standard ADR provisions which have reached the courts and been interpreted, custom provisions likely have not been ruled upon, and will require a judge or jury to construct it for the first time. This presents an enormous amount of uncertainty.

IN A DISPUTE

ADR provisions set forth the forum and procedure for any disputes. However, there are a lot of nuances that will significantly impact the underlying disagreements. Here are three examples.

1. The rules, procedures, and surroundings of ADR proceedings.

How will the ADR proceeding operate? Who will judge it? How long will the parties have for discovery? Can the parties take depositions? Where will it be held? These questions could go on and on. While many complain about litigation, the great thing is that all of these thorny questions are controlled by codes and years of precedent.

It helps to establish the rules within the ADR provision (i.e. we will arbitrate

pursuant to the AAA's Construction Dispute Resolution Rules). However, the AAA is just one of many ADR companies, and this is a thorny and often overlooked area that has a huge impact on the process.

2. Claim notice provisions.

Claim notice provisions are becoming more common in modern construction contracts. They require parties with a dispute to give some formal notice of the same within a defined (and usually short) period of time. If the claim notice is not provided, so argues the contract provision defenders, and the claim is waived completely.

If a contract contains this provision and the claim notice is not made, the ADR provisions become pretty irrelevant. This is just one example of many examples where other contract provisions will be more important to the dispute than the dispute forum—although, to the extent the parties will argue about these troublesome provisions, they will do so in the ADR forum.

3. Mechanics lien and bond claim rights.

Last, but not least, many believe that ADR provisions prohibit parties from utilizing mechanics lien or bond claim rights. An agreement to mediate or arbitrate, in other words, prevents unpaid parties from filing a mechanics lien or bond claim because they must conclude the mediation or arbitration before bringing the "legal proceeding" of a lien or bond claim.

This is universally untrue and a huge misunderstanding in the industry.

First, a lien or bond claim is not a "legal proceeding" or a "dispute resolution proceeding." It is a claim for security rights. It can be done at anytime that the right is legally available. Since these rights typically expire pretty quickly after the conclusion of work, they almost always must be filed before the ADR provisions. ADR provision will not extend the timeframe.

Second, a lien or bond right does not even arise out of the contract; it arises from the law. In other words, the law gives contractors or suppliers the right to file a mechanics lien or bond claim if they are unpaid for work as security for the value that the unpaid party has provided. This is completely unrelated to the right for the party to collect under the contract. Accordingly, there is even an argument that litigation about these rights are not connected to or regulated by ADR provisions at all. ■

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Clauses	Effects
Clause A: ConsensusDocs 200 (2007) 12.5: If the matter is unresolved after submission of the matter to a mitigation procedure or to mediation, the Parties shall submit the matter to the binding dispute resolution procedure designated herein. (Designate only one:) ____Arbitration using the current Construction Industry Arbitration Rules of the American Arbitration Association or the Parties may mutually agree to select another set of arbitration rules. The administration of the arbitration shall be as mutually agreed by the Parties. ____Litigation in either the state or federal court having jurisdiction of the matter in the location of the Project.	**Effect A:** The parties must submit the dispute to mediation, and thereafter, if an agreement is not reached, may proceed to a binding procedure (like arbitration).
Clause B: Example Provision 1 from AIA: Any controversy or claim arising out of or relating to this contract, or the breach thereof, shall be settled by arbitration administered by the American Arbitration Association under its Construction Industry Arbitration Rules, and judgment on the award rendered by the arbitrator(s) may be entered in any court having jurisdiction thereof..	**Effect B:** The owner can—at his or her complete whim—decide whether to require arbitration or litigation in the event of a dispute.
Clause C: Example Provision 2 from AIA: If a dispute arises out of or relates to this contract, or the breach thereof, and if the dispute cannot be settled through negotiation, the parties agree first to try in good faith to settle the dispute by mediation administered by the American Arbitration Association under its Construction Industry Mediation Procedures before resorting to arbitration, litigation, or some other dispute resolution technique.	**Effect C:** In the event of a dispute, the parties are not allowed to litigate, and instead must proceed to a binding arbitration proceeding.
Clause D: Custom Provision: Contractor agrees to resolve any disputes arising from the Agreement by binding arbitration to be held in _____ County, in accordance with the rules of the American Arbitration Association then in effect.	**Effect D:** The provision is invalid and parties can proceed however they want.

Match the different contingent payment clauses to their possible effect in the chart above.

***Answer:** Clauses A and C have effect A; clause B has effect C; clause D has effect B.*