Arbitration

If you can't resolve your differences in the field, here's an alternative to court

by Andrew H. Diem

If you've ever read a construction contract, you may have come across.these words:

"Any controversy or Claim arising out of or related to the Contract, or the breach thereof, shall be settled by arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association...."

That's the beginning of the arbitration section of the American Institute of Architects (AIA) Document A201, General Conditions of the Contract for Construction (1987 edition). Arbitration provisions like this have been written in most AIA contract forms since 1888, but as our society becomes more litigious, arbitration may be taken up more frequently as a way of resolving construction conflicts and avoiding civil courts.

Simple, fast and confidential—Arbitration is a nonjudicial means of resolving disputes between two parties. A claimant wishing to initiate arbitration should use the procedures established by the Construction Industry Arbitration Rules of the American Arbitration Association (AAA). The AAA is a private, nonprofit organization with 32 offices in major cities across the country. Its headquarters are at 140 W. 51st St., New York, N. Y. 10020. Arbitration can be used to resolve disputes of many kinds, including labor, international, marital and construction disagreements. Construction arbitration is a large portion of the AAA's cases. Last year, the AAA handled 4,940 construction cases with total claims and counterclaims of almost $786 million. In contrast to civil litigation—a complex process that may seem incomprehensible to a layperson—arbitration allows parties to settle disputes in a quick, informal and generally less costly manner.

Arbitration proceedings are private, too. Hearings are held with only the arbitrator, claimant, respondent, respective attorneys and witnesses present, and the proceedings don't become part of the public record. This confidentiality is critical to those who do not want competitors to hear sensitive business information—a problem that could occur if a legal battle takes place in the public forum of court.

Also unlike litigation, which often results in an either/or decision, arbitration may result in a decided compromise rather than a total win for one party. An arbitrator bases a decision on fairness and impartiality, not on legal principles alone.

Parties select arbitrators by mutual agreement, whereas they may not choose a judge. Arbitrators can be chosen for their special knowledge of the subject matter, of the local business practices and of the relevant law. Having an expert arbitrator means that procedures are streamlined, taking much less time to get to the essence of a case than it would to present the dispute to a jury of laypersons.

How arbitration begins—If the standard AIA contract is used with the arbitration clause intact, any unresolvable claim between owner and architect or between owner and contractor must be settled by arbitration—unless both parties agree to go directly to court. It is possible to strike the arbitration clause from a contract, or simply to write a contract without one. In that case, however, you may have no choice but to go to court.

If it becomes apparent that a construction project is headed for arbitration, discuss the matter with an attorney immediately. Although you don't need an attorney for an arbitration hearing, it's a rare case that doesn't have attorneys representing both claimant and respondent. You would be well advised to use an attorney who has experience with construction litigation. After reviewing the issues of a case, the attorney may suggest hiring an expert witness to testify as to the specific standards of the industry. Integrity, experience, composure and credibility are important attributes in an expert witness.

To initiate arbitration, the claimant files a simple form called a Demand for Arbitration. On this form, the claimant names the respondent, the nature of the dispute and the claim sought. The AAA will assign a tribunal administrator to the case to help the parties prepare their positions and select an arbitrator or a panel of three arbitrators, depending on the complexity of the dispute and the amount of the claim. Often, a conference is held to discuss arbitration procedures. The AAA will send a list of names and brief biographies of qualified arbitrator candidates to the disputing parties, who must make a selection in seven days. Each side strikes out unacceptable candidates, and the tribunal administrator selects the arbitrator or panel from the remaining names.

The AAA Construction Arbitration pool is composed of 32,000 arbitrators representing all segments of the industry, including builders, subcontractors, architects, engineers and attorneys who specialize in construction law. I have found being a member of an arbitration panel both challenging and rewarding. The forum of arbitration is a natural outgrowth of my experience as an architect, traditionally the liaison between owner and contractor.

If you have construction experience and have an interest in becoming an arbitrator, contact the nearest office of the AAA for the specific requirements. If you are selected by the AAA, you'll attend several training sessions and take refresher sessions in years to come. You may ask to be excused from an occasional case if you are too busy to serve. It isn't terribly lucrative, but I feel I have a moral obligation to give a little something back to the community.

Before becoming an arbitrator, you must become familiar with the rules and regulations of the AAA and understand the tremendous responsibility and obligation you will take on. The AAA has established a code of ethics for arbitrators. The code requires that arbitrators disclose any interest in or relationship to a case that is likely to affect impartiality or create an appearance of partiality. All communications an arbitrator has with the parties should avoid impropriety or the appearance of impropriety. An arbitrator should conduct proceedings diligently and fairly and render a decision in a just, independent and deliberate manner, and should be faithful to the trust and confidentiality inherent in his office.

Costs of arbitration—The AAA rules contain a fee schedule that is determined by the claim amount and any counterclaim. The fee for a claim or counterclaim of $1 to $25,000 is 3% with a minimum of $300; a claim of $25,000 to $50,000 requires a fee of $750 plus 2% of the amount over $25,000; for a $50,000 to $100,000 claim, you'll pay $1,250 plus 1% of the amount over $50,000; and so on. At least $300 is paid upon filing the Demand for Arbitration; the remainder is due before the first hearing.

Claimant and respondent are always asked to compensate the arbitrators for expenses (parking, mileage, lunch) associated with the case and are asked to pay for the arbitrator's time if he works over one day (the first day is free). Compensation amounts for hearings

over one day are billed before the first hearing. Compensation for remaining days is suggested by the tribunal administrator, depending on the complexity of the case. Compensation for an arbitrator's time runs between $300 and $400 daily. The parties usually agree up front on the way to divide the compensation and fees; the arbitrator may also distribute fee payment requirements in his decision. Most cases are short, but lengthy arbitration involving large claims may cost more than court litigation.

Claims under $50,000 may be handled by only one arbitrator. This is the form that most residential building disputes take. Simple disputes with small claims can often be handled by expedited procedures, a streamlined process in which fees are lower, some procedures are waived and most communication is handled by phone. A three-member panel is desirable for cases with claims over $50,000 because the panel will have a range of opinions from experts with differing backgrounds. Adversely, three-member panels often require longer selection periods and may present scheduling difficulties because the panel members are likely to have other full-time jobs.

The hearing—A pre-hearing conference is called before the hearing if the case is fairly complex. During this conference, the arbitrators and the attorneys for the respective parties review the case, discuss documents to be exchanged, list witnesses to testify and devise a schedule for hearings. At this time each party is made aware of what will go on at the arbitration hearing. Usually, the parties and attorneys voluntarily agree to exchange documents and submit to deposition if requested. If they do not agree to exchange documents and permit depositions from witnesses, the arbitrator has the power to issue a subpoena, but this power is not used lightly.

The AAA does not restrict the location of the hearing itself. If all parties concur, the hearings may be held in the AAA offices, rented meeting rooms, at the construction site, or in the office of one of the parties involved. But if the problem of "home-court advantage" enters into play, a neutral ground is the best choice. If the arbitrators think it necessary, after they have heard testimony they may request a visit to the site to clarify any field condition they consider relevant.

According to the AAA, the median time from the date the demand for arbitration is filed to the date a decision is awarded is 182 days, but the average length of a hearing is one to two days. Sometimes an afternoon is sufficient for a small residential claim; a complex case may require hearings to be held every month or so throughout a year.

Decision and award—An arbitrator should let all parties have the opportunity to express themselves during the hearings. This way all parties feel that they have "had their day in court." The role of the arbitrator is to sort out conflicting evidence or testimony by listening to both sides of the issues and by reaching a fair decision within the scope of the parties' agreement.

It may take up to 30 days from the end of the hearing for the arbitrator or panel to award a decision, although I try to get the decision out as soon as possible after the hearing. The decision is given in writing to the AAA, which in turn gives it to the claimant and respondent. Arbitrators are not required to give written justification of their decision, and normally do not.

According to the AIA contract wording, an arbitrator's decision is binding. But, there are three bases for challenging an arbitration award in court. If the arbitrator appears to have acted capriciously, to have made a gross miscalculation in figuring the amount of the award, or to have been unduly influenced, then either parly may dispute in court the arbitrator's decision. Another post-arbitration function of the court may be to enforce the arbitrator's decision if the losing party does not pay the award voluntarily.

Documentation, the best defense—The old saying that the best defense is a good offense applies to arbitration. To avoid litigation or arbitration, or to succeed in either, your best bet is to document your projects. Don't rely on memory: it is essential to use a written agreement between owner and contractor. Often, only written agreements are enforceable, but even if an oral agreement is enforceable, it leaves too much open to interpretation.

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The construction contract should be specific. It should define the parties, location, scope of work, dates of commencement and substantial completion, costs and payments. It should also spell out how to deal with termination or suspension, insurance requirements and how to deal with changes. The contracts written and published by the AIA have become a standard of the industry. These are available to the public for a minimal cost from a local AIA chapter office or from the national headquarters (1735 New York Ave., N. W., Washington, D. C. 20006).

Other good sources of construction contracts are the Associated General Contractors of America (1957 E St., N. W., Washington, D. C. 20006) and construction trade associations, which provide their members with contracts specific to their trade. It's important to make certain that the contract you use is specific to the kind of work to be undertaken.

It is equally important to document everything that happens on a construction project. Changes always arise and affect both cost and time. This is especially critical with a remodeling job because not all conditions are known at the time a project is bid.

Keeping a job log is crucial for both architect and contractor. Logs track daily manpower resources, the scope of work performed, deliveries to the job, major decisions agreed upon or changes in the scope of work and other critical historical notes on the project. The notes of project meetings with owners, contractors, architects, subcontractors and various important officials should be written in the log and distributed for review. To improve credibility, the job log should contain facts only, not suppositions and personal reflections. Keep the records on hand as long as the statute of limitations is in effect for a project (the length of time varies from state to state; seven years is the norm).

It is also crucial to prepare a written punch list at the end of a job. The punch list must be agreed to by all involved and the work should be completed as soon as possible—ideally before the owner has the use of the property—so that additional items are not added to the list.

The project should be documented throughout with dated photographs of the construction work. If there is a dispute, the photographs will clearly show the extent of work performed at any given time. This can be useful if the schedule of payments can be compared with corresponding photos.

Communication is the key—Whenever disputes arise on the job site, resolve the problem immediately. Problems tend not to disappear but to fester over time. Try to assume the other person's perspective to see what he would like done. It is worth the effort. If the job is ongoing, mediation may be the step to take before disagreements become hostile. Mediation is a nonbinding method of resolving disputes in which a mediator reviews each party's case and presents suggestions to them. The parties may accept, reject or modify the mediator's suggestions. A number of AAA arbitrators are also trained in mediation.

To avoid arbitration or litigation, you must have an adequate budget and there must be a mutual understanding by all parties of the time that it takes to complete the work. In addition, everyone should understand what level of workmanship and quality of finish can be achieved within the budget given. I've seen major complications arise in arbitration over drywall finishing. All parties must acknowledge before the job begins that a drywall finish costing $.70 per sq. ft. is not the same as plaster on gypsum lath that costs $1.70 per sq. ft. The key to avoiding arbitration is to keep communication lines open at all times. ❑

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