Global Construction Disputes: A Longer Resolution

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Introduction

This is our third annual report into the construction disputes market. I hope that you will find it to be a helpful commentary into the regional trends and insights into a global industry that is often difficult to quantify.

Overall, this year's report finds that disputes are taking longer to resolve and the causes are linked to many different factors, including:

- Disputes that are not settled through negotiation tend to indicate a polarisation of interests, and are likely to only contain the most complex of issues;
- Multi-geography, mixed cultures and the need to consult and engage with head offices can prolong the time it takes for a dispute to be concluded;
- Projects are increasing in complexity and so the issues that are material to the dispute can be equally as complex, and therefore need appropriate time to consider the issues.

2012 also saw the very interesting and insightful judgement in Walter Lilly v Giles Patrick Mackay, which came out of the Technology and Construction Court in London. The relevance and application of the principles within the international market are, perhaps, still in the "incubator", but it is interesting to note that many of the features of this case also surface in our common causes discussed over the following pages.

Closer to home, our disputes team had another record year in 2012, with a 12% year on year growth. A feature of this has been the continued international expansion of our disputes practice, and with this growth I am confident that the data captured from this survey is representative of more disputes, and in particular some of the very large international disputes which we have or continue to be involved in.

Looking into 2013, there are healthy construction programmes in the Middle East, Asia and a recovering market in the USA. Combined with the continued use and growth in international arbitration and the extensive infrastructure and energy related programmes underway in established and developing countries, this indicates to me that 2013 will not reverse the previous growth of disputes worldwide and be another busy year for dispute professionals.

Mike Allen
Global Head of Contract Solutions
EC Harris

Executive summary

The key finding of this year's report into global construction disputes is that disputes are taking longer to resolve.

Overall, they are now taking over a year to resolve, with the average length of time for a dispute to last in 2012 being 12.8 months, compared to 10.6 months in 2011. This continues the trends for longer disputes - in 2010 disputes were taking 9.1 months to resolve.

Whilst dispute durations are getting longer, the value of disputes was broadly stable in 2012. The average value of global construction disputes in 2012 was US$31.7 million, down slightly from US$32.2 million in 2011.

Longer disputes times – a global trend

The average length of disputes rose across Asia, the Middle East and the UK. Disputes are taking longest to resolve in the Middle East, where disputes lasted 14.6 months on average, although Asia was not far behind with 14.3 months.

In contrast, disputes in the US and Europe were becoming quicker to resolve in 2012, with US disputes taking slightly under a year (11.9 months) to resolve.

Dispute values – a mixed picture

Although the average value of global disputes was similar to 2011, this masked some variations across the different regions. In the UK, where dispute values have been well below the global average over the past two years, construction disputes jumped to an average value of US$27 million, more than double the US$10.2 million value in 2011.

Elsewhere, dispute values fell across all regions, although the Middle East still experienced the largest disputes at an average of US$65 million. The highest value dispute handled by EC Harris during 2012 was for US$1 billion, which is just one instance of a mega-construction project being in dispute. With many billions of dollars being spent on construction over the coming years, particularly in Asia and the Middle East, it is likely that such huge disputes will be a continuing feature in the international markets.

Figure 1 – Summary of results

Region	Dispute values (US$ millions)			Length of dispute (months)		
	2010	2011	2012	2010	2011	2012
Middle East	56.3	112.5	65	8.3	9	14.6
Asia	64.5	53.1	39.7	11.4	12.4	14.3
US	64.5	10.5	9	11.4	14.4	11.9
UK	7.5	10.2	27	6.8	8.7	12.9
Mainland Europe	33.3	35.1	25	10	11.7	6
Global Average	**35.1**	**32.2**	**31.7**	**9.1**	**10.6**	**12.8**

Figure 2 – Dispute causes – failures to the fore

2012 Rank	Cause	2011 Rank
1	Incomplete and / or unsubstantiated claims	New
2	Failure to understand and/ or comply with its contractual obligations by the Employer / Contractor / Subcontractor	New
3	Failure to properly administer the contract	1
4	Failure to make interim awards on extensions of time and compensation	3
5	Errors and / or omissions in the Contract Document	2

All of the top five causes of construction dispute revolve around a mistake or failure, which makes them all avoidable to varying degrees. More specifically it is interesting to note that the causes are all directly related to contract administration, with the causes ranked 1-4 occurring post contract and rank 5 connected to the pre contract period. Two new categories have been introduced to provide greater visibility into the possible sources of the causes of disputes, and thus provide insights into possible solutions to the cause.

Resolving disputes

Figure 3

2012 Rank	Method of Alternative Dispute Resolutiion	2011 Rank
1	Party to party negociation	1
2	Mediation	2
3	Arbitration	3

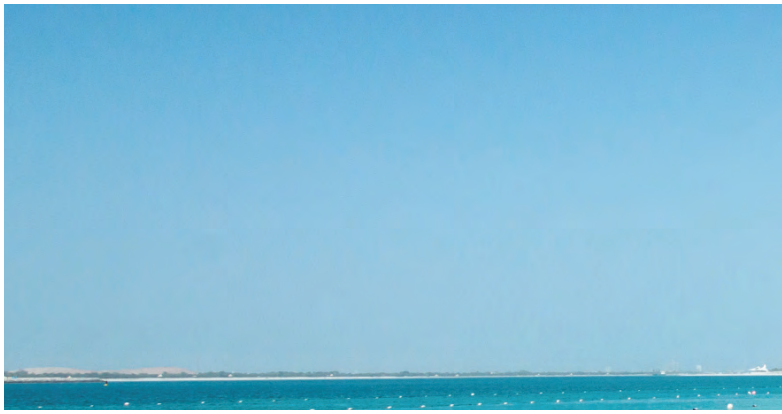
Interestingly, the most common means of resolving disputes remains the same, with better communication via negotiation and mediation the preferred method, over arbitration. This appears to support the general perception within the industry that parties who are dealing with a dispute wish to retain control and endeavour to settle the dispute themselves, all in a manner that embraces the following principles:

- Parties wish to retain control of the dispute;
- A desire to maintain the relationship;
- Speed and flexibility in working towards resolving the dispute;
- To keep costs in resolving the dispute to a minimum.

Where the parties have been unable to resolve their differences more formal methods are required.

Middle East

The Middle East region experienced the most change between 2011 and 2012. Dispute values fell from a high of US$112.5 million in 2011 to US$65 million in 2012. This is a significant drop, but values are still high enough for the Middle East to have the highest value disputes by region. There is no particular reason for this drop, and still reflects the size and scale of construction programmes being undertaken in the region.



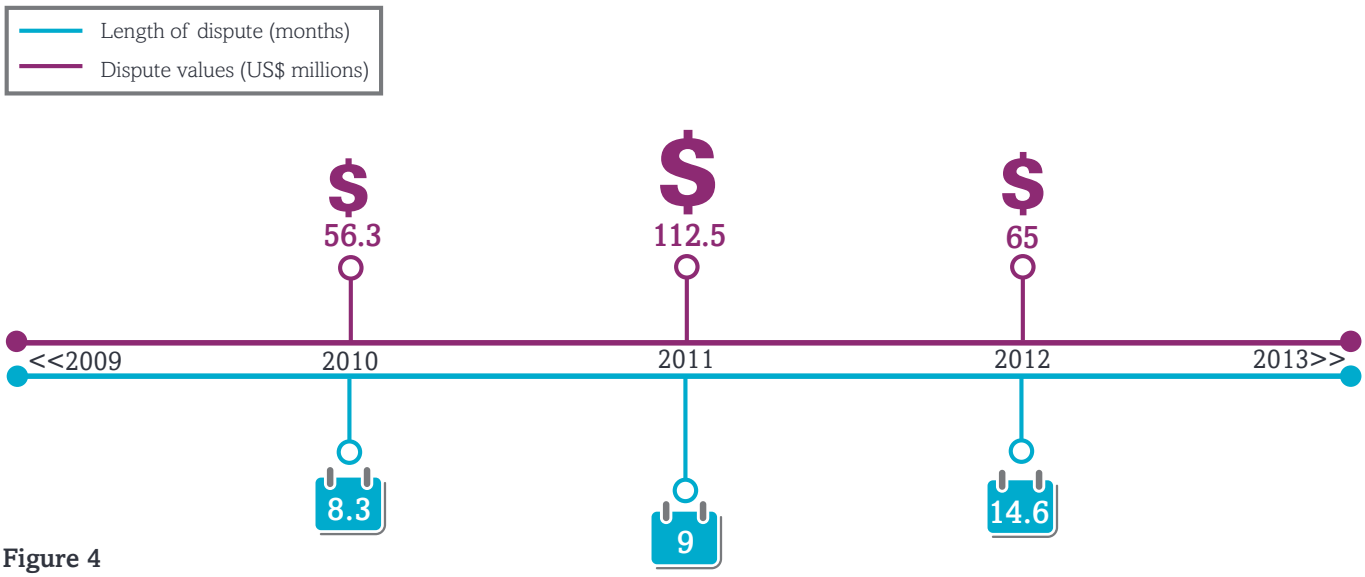


Figure 4

Dispute resolution timeframes in the Middle East followed the global trend by taking longer to resolve in 2012. Dispute resolution times in the Middle East are now the longest in the world, taking, on average, 14.6 months to resolve, up from 9 months in 2011.

The sheer volume of disputes in the Middle East is one of the reasons for this length of resolution. There are a limited number of Arbitrators and Expert Witnesses based in Middle East, so there has been, to some extent, a backlog of cases. To relieve this backlog, parties have sought to appoint Arbitrators/Expert Witnesses that live and practice outside of the Middle East which has helped, but can still cause delay.

Additional factors influencing the time taken include Arbitration timetables being extended, parties becoming better at delay and frustration tactics to put off any award and the lack of enforcement of Arbitration awards.

The top causes for construction disputes in the Middle East paint a similar picture to the previous year with a failure to properly administer the contract the most common reason. Of the other causes, one particular difference in the Middle East was the impact that the client has on the dispute taking place. Three of the most common causes can be viewed as being related to the client's responsibility, from not making interim awards on extensions of time and money, imposing change in the project and the contract not fitting with the project's characteristics. The appointed engineers or architects are often unwilling to act impartially in assessing contract variations, with any member of the engineer's/architect's team that even suggests agreeing to a contractor's contractual claims being removed from the project by the Employer.

The greater stability experienced in the region is, perhaps, the key reason for third party or force majeure events dropping to fifth place as a reason for dispute. Outside Libya, Syria, Egypt, Yemen and occasionally Bahrain, the region has settled back down which has allowed construction projects to proceed with less disruption from outside events.

Figure 5 – Top five causes of disputes in Middle East construction projects 2012

2012 Rank	Cause	2011 Rank
1	Failure to properly administer the contract	1
2	Failure to make interim awards on extensions of time and compensation	4
3	Employer imposed change	3
4	Contract selection was not a 'best fit' when compared to the project's characteristics	-
5	Third party or Force Majeure events	2

When it comes to resolving a conflict, the most common methods in the Middle East are party to party negotiation, followed by arbitration and adjudication. This is largely due to frustrations with the arbitration and possible enforcement process which results in a greater number of parties agreeing to the negotiation strategies.

2013 is likely to maintain a similar pattern to the previous year, with a gradual increase in the number of disputes in such places as Qatar, Oman and the Kingdom of Saudi Arabia.

"Dispute values fell from a high of US$112.5 million in 2011 to US$65 million in 2012."

Asia

Asia saw dispute values continue to fall from a high of US$64.5 million in 2010 to US$39.7 million in 2012. This was a dramatic 25% fall from 2011 when dispute values were over the US$50 million mark.

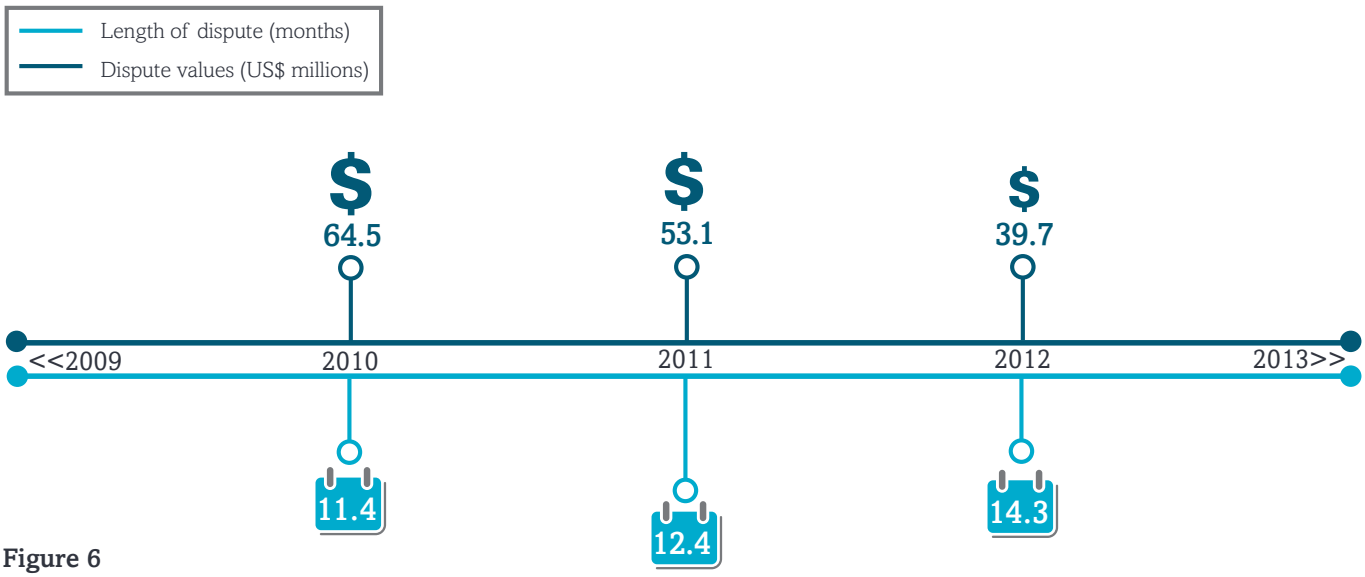


Figure 6

Care is required when reviewing and interpreting statistics, and there is generally never one single reason for why the value of disputes could be said to have fallen from previous year's data. However we have seen the following themes continue to feature in the region:

- The use of collaborative contracting and related procurement strategies;
- The use of supplemental agreements and employer's desire to progressively buy out risk on projects, and thus reduce the disputed areas;
- The settlement of some large legacy disputes in the region;
- The continued use of Dispute Resolution Advisors (DRAs) and Dispute Adjudication Boards (DABs).

In contrast, over the past twelve months the length of time that construction disputes in Asia are taking to resolve has lengthened. They are now above the global average at 14.3 months, an increase of nearly two months from 2011 when disputes were lasting 12.4 months.

This increase can be attributed to some inter-related features of the above points. Where the disputes have not been capable of being reduced or settled on an interim basis, this tends to indicate that the formalised disputes are complex and/or caused by polarised viewpoints. This can mean that the issues require the necessary time within the process to give due consideration to the technicalities of the case, as well as allow each party the appropriate time to prepare its respective case. Additionally it is a common feature in the region that parties are located or centred in different parts of the region, which can cause time tables to be adversely effected, in addition to the effects of culture, language and the need to consult and engage with head office decision making/approval requirements.

The causes of construction disputes in Asia during 2012 have changed from 2011. Where employer/ client causes featured heavily in 2011, in 2012 the inability to properly manage claims or the contract came to the fore.

Figure 7 – Top five causes of disputes in Asian construction projects 2012

2012 Rank	Cause	2011 Rank
1	Incomplete and/ or unsubstantiated claims	5
2	Failure to make interim awards on extensions of time and compensation	1
3	Differing site conditions	-
4	Failure to understand and/ or comply with its contractual obligations by the Employer/ Contractor/ Subcontractor	-
5	Failure to properly administer the contract	-

There is a continuing feature within the region that Contractors and Subcontractors typically submit incomplete and unsubstantiated claims. Reasons for this could include culture, language, poor contract administration and in some instances poor and/or incomplete advice is at the centre of the reasoning. Furthermore, given the typical relationship based culture that exists within the region, a continuing theme is the desire to undertake the minimum amount of work and then try to settle the claim without confrontation and maintain face.

This strategy may be well founded in principle, however, in application there are many examples of heavily discounted claims, lost credibility, damaged relationships due to a lack of substantiation and also the source of the claims being later exposed to lack foundation, substance and any substantive contractual or legal merit.

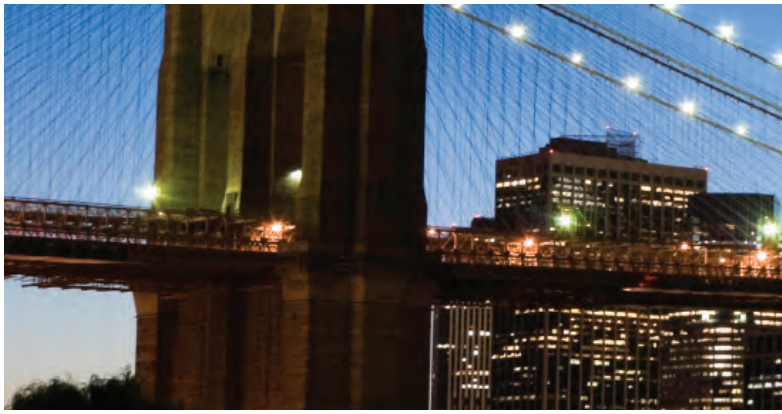
Mirroring the global trend, the top three methods of Alternative Dispute Resolution in Asia were party to party negotiation, mediation and arbitration.

Relationship and interest based dispute resolution strongly aligns with the cultural dynamics in the region, however where disputes are referred to a third party, arbitration is still the most common method. Singapore and Hong Kong are the most popular centres for arbitration references, and a growing feature is the use and application of adjudication, or similar methods.

Singapore has seen growth in the use of the Security of Payment legislation, Malaysia have introduced CIPA which was introduced with support from all sides of the industry. The HKSAR government, long time advocates of mediation, DRAs and arbitration, have commissioned a strategic review of the type of adjudication that could be introduced into Hong Kong. The current plan suggests that this could be introduced into the legal system in 2015.

US

In the US market, construction dispute values were not significantly different to the previous year, coming in at an average of US$9 million, compared with US$10.5 million in 2011.



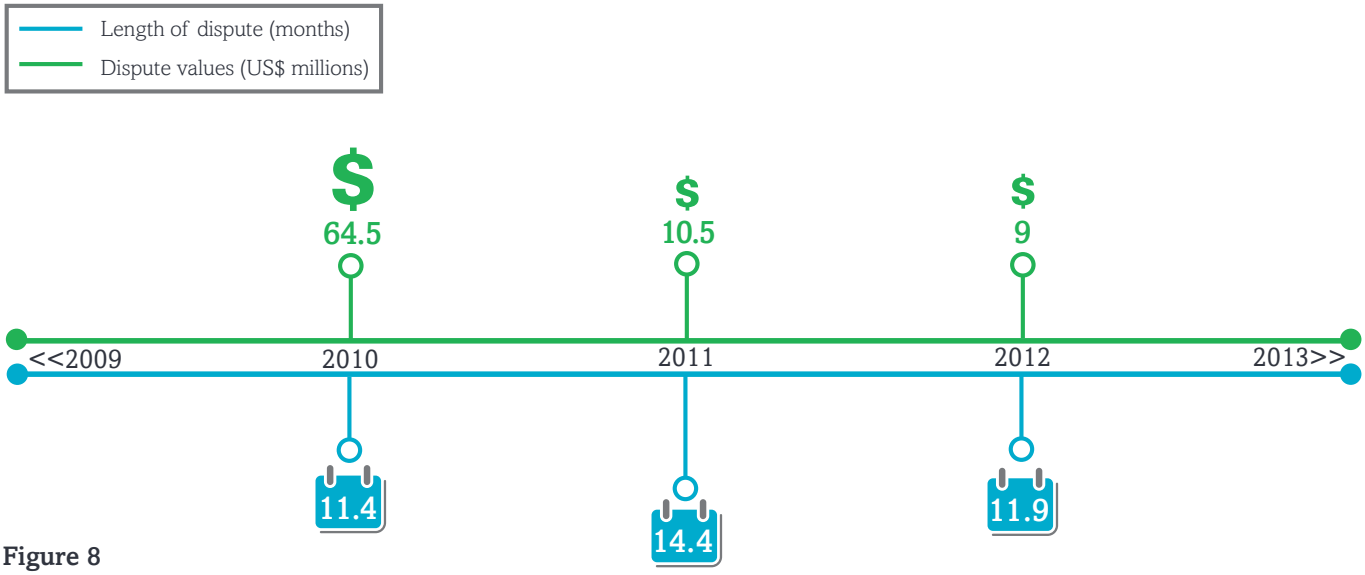


Figure 8

The average value of claims in the US continues to be lower than the global average due to the experience of the client and contractor and the culture of general claims avoidance. Most managers have dealt with claims in the past and have received extensive training in how to prevent them happening, so tend to be smarter about avoiding claims. However, this is unlikely to be sustainable. As the construction market heats up, there will be more work than available experienced managers which could lead to an increase in the number and size of claims.

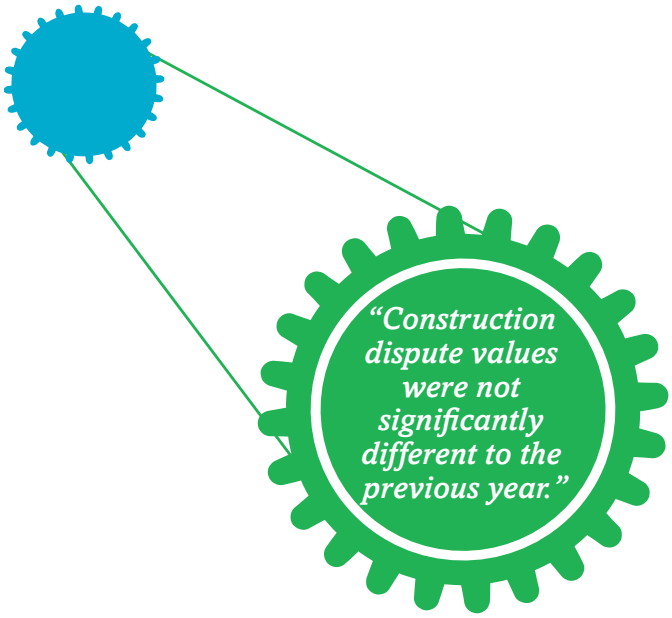
The US was one of the few markets in the world where disputes were taking less time to resolve in 2012. Average dispute lengths fell from 14.4months in 2011 to just under a year at 11.9 months in 2012. This is a function of having more available experienced staff to concentrate on responding to and resolving the disputes. Similar to the dispute size, as work increases, so the experienced people will be busier and have less available time to commit to the resolution of old disputes.

The causes of dispute in the US are significantly different to other regions covered in this report. This could reflect the maturity of the construction market; in particular instances where the client / employer is at fault were less common causes of dispute. Even so, instances of incomplete or unsubstantiated claims, errors in the Contract Document and a failure to comply to contractual obligations point to a some serious deficiencies that could be rectified given even better dispute avoidance practices.

Figure 9 – Top five causes of disputes in US construction projects 2012

2012 Rank	Cause	2011 Rank
1	Incomplete and / or unsubstantiated claims	-
2	Errors and / or omissions in the Contract Document	-
3	Failure to understand and / or comply with its contractual obligations by the Employer / Contractor / Subcontractor	-
4	Differing site conditions	-
5	Failure to make interim awards on extensions of time and compensation	4

The most common practices of Alternative Dispute Resolution in the US were party to party negotiation, mediation and arbitration.



UK

The British construction market continued to suffer in 2012, with falling construction output contributing to the UK economy dipping back into recession for a quarter. This backdrop paints the picture for the disputes taking place during the year.

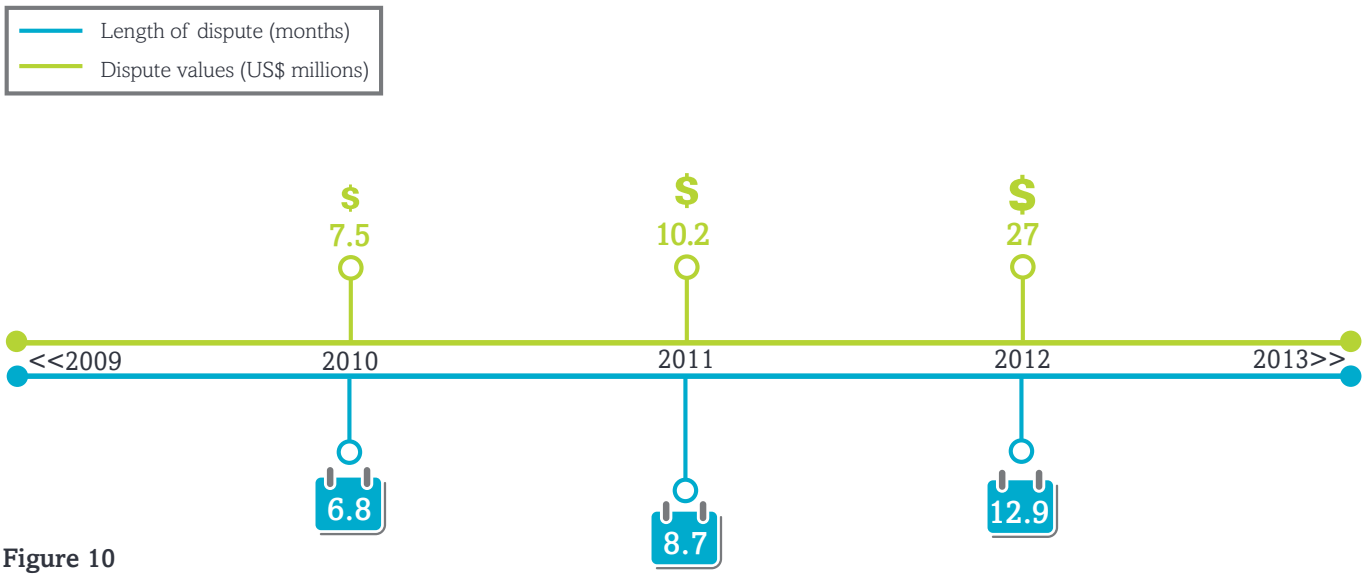


Figure 10

Dispute values rose in the UK to US$27 million (£17.7 million), compared with US$10.2 million (£6.5 million). As explained earlier in the report, there is no single reason for such a major increase, however it is likely to be been influenced by the team working on an unusually high number of disputes on major programmes of work.

The length of time taken to resolve UK disputes also increased in 2012, taking four months longer to resolve than in 2011 - up to 12.9 months from 8.7 months in 2011.

One reason for this is that the Technology & Construction Court (TCC) encourages the use of the Pre-Action Protocol and as more parties decide to litigate rather than adjudicate or arbitrate the trend is for the Pre-Action process to slow down the resolution of disputes. The majority of cases that went to Court ordered mediation in the first instance.
The most common cause of dispute in the UK was a failure to properly administer the contract for the second year running. Taking the top five as a whole, UK disputes tend to be attributable to parties taking a less collaborative approach to projects than in other markets. For example, the employer imposing change and conflicting party interests feature highly.

2012 saw an increase in disputes arising from parties failing to understand their contractual obligations which on the larger, mega projects often arise as a result of clumsy, sometimes over legalistic, drafting of the generally bespoke contracts. If owners / employers adopted standard forms with less amendments this problem could be reduced.

Figure 11 – Top five causes of disputes in UK construction projects 2012

2012 Rank	Cause	2011 Rank
1	Failure to properly administer the contract	1
2	Failure to understand and / or comply with its contractual obligations by the Employer / Contractor / Subcontractor	-
3	Employer imposed change	4
4	Conflicting party interests	2
5	Incomplete and / or unsubstantiated claims	-

For the UK, adjudication, arbitration were the two most common means employed followed by party to party negotiation.

One the highest profile disputes in the UK during 2012 involved the construction of the Shard in London. The dispute between steelwork companies Cleveland Bridge UK and Severfield-Rowen Structures first came to light in early 2010, but was only resolved in January 2013 following a lengthy dispute that ended up in the High Court. Cleveland Bridge was ultimately ordered to pay £824,478 in damages to Severfield-Rowen for delays and defects which were estimated to cause a delay of 42 days on the Shard's construction.

Mainland Europe

2012 was a difficult year for the Eurozone countries, still reeling from the financial crisis and the debt laden countries of Southern Europe. The construction market similarly suffered, but unlike other Western economies, disputes in Europe tended to reach resolution more quickly and fell in value than in previous years.

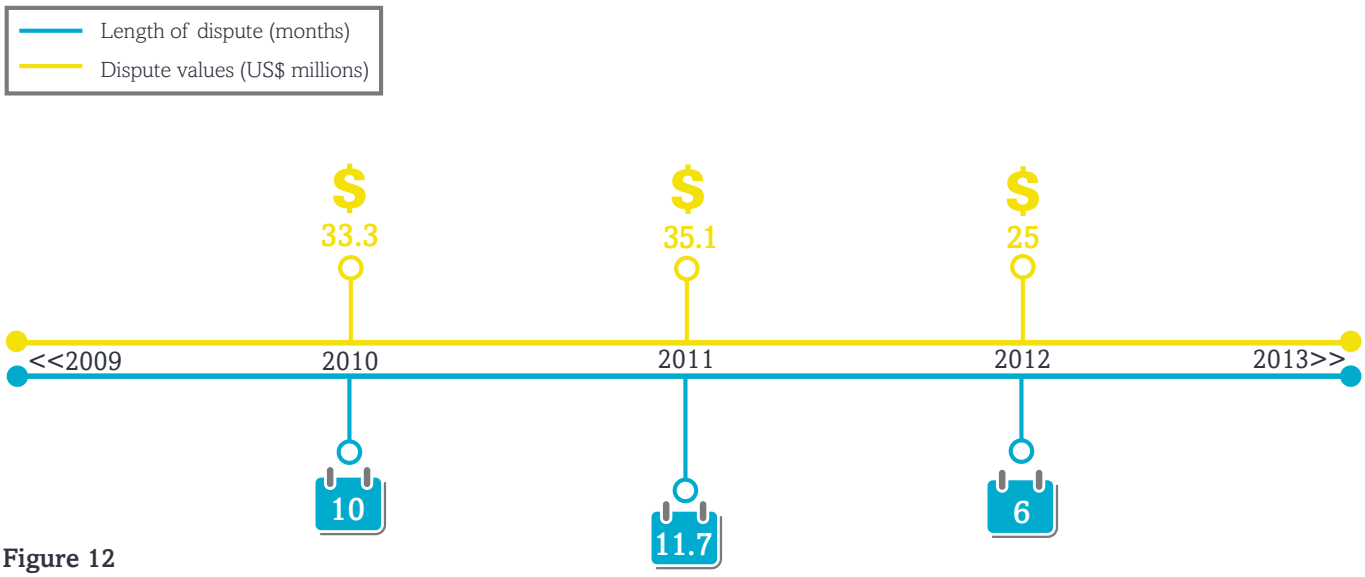


Figure 12

Disputes handled by EC Harris in Europe had an average value of US$25 million (€19.6 million) in 2012, compared with US$35.1 million (€27.5 million) in 2011. This was even lower than in 2010 when dispute values were US$33.3 million (€26.1 million).

Having increased in length in 2011, European construction disputes shortened in 2012 to just six months, making them the swiftest disputes to reach resolution in the report.

The most common cause of dispute in 2012 was a failure by the Employer / Contractor / Subcontractor to understand and / or comply with their contractual obligations. Other common reasons also involved a breakdown in relationship or understanding from an unrealistic transfer of risk to the contractors to out and out conflicting party interests.

Party to party negotiation was the most common methods of Alternative Dispute Resolution in Europe followed by arbitration and mediation.

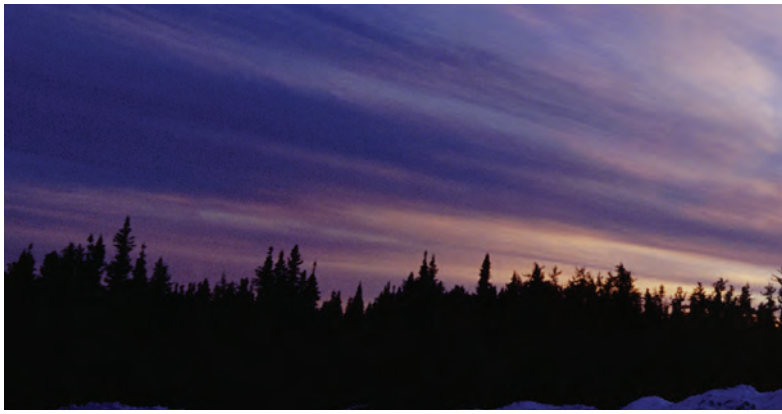
Figure 13 - Top five causes of disputes in Mainland Europe construction projects 2012

2012 Rank	Cause	2011 Rank
1	Failure to understand and / or comply with its contractual obligations by the Employer / Contractor / Subcontractor	-
2	Unrealistic risk transfer from Employers to Contractors	-
3	Failure to make interim awards on extensions of time and compensation	4
4	Conflicting party interests	-
5	Third party or Force Majeure events	-

"2012 was a difficult year for the Eurozone countries, still reeling from the financial crisis and the debt laden countries of Southern Europe."

Cause and resolution

In previous years we have focused our analysis on the particular causes of dispute, however this year we take a look at firstly how likely it is for a dispute to occur during a Joint Venture (JV) arrangement and secondly, the role of the Project Manager or Engineer in the dispute.



Focus on JVs

Joint venture agreements are becoming more prevalent, particularly where a project is of such a large size and scale or there is a need because of licensing requirements for a local JV Partner. This is particularly the case in markets such as the Middle East and Asia where long term, multi-billion dollar contracts are being awarded.

EC Harris found that, where a JV was in place, a JV related difference was likely to drive a dispute on approximately one in five (19%) occasions. This is a significant number of cases, so more needs to be done in order to ensure that the JV itself does not end up in dispute.

Potential strategies include:

- Clear agreements between the respective partners;
- Aligned interests and objectives, with defined and agreed common objectives;
- Clear demarcation of the roles and responsibilities within the JV;
- The use and application of a common platform and information sharing system;
- The selection and appropriate use of the respective partner strengths;
- Clear tender and commercial strategies;
- Recognition and consideration given to cultural and language differences (local and international partners).

Role of the Project Manager and Engineer

Delving into further detail about the cause of the dispute, this year's research also looked closer at the role of the Project Manager (PM) and Engineer. Asked how important the PM or Engineer's conduct was to how the dispute crystallised, nearly half (46.3%) of the disputes team said that their actions were 'very often' at the heart of the problem.

The most common problem relating to the PM or Engineer, which then became a material influence in the dispute, was:

1. Being too partial to the Employer's interests
2. A lack of understanding of the procedural aspects of the contract
3. A lack of authority that is limited by levels of authority issued by the Employer i.e. not allowed to issue Variation Orders over a certain value

There are a number of ways in which these problems can be avoided at the outset. These include:

- Training for the Employer and Consultant in understanding the role, responsibilities and also raising awareness of the implications of not fully fulfilling the role set out under the contract;
- Clear and comprehensive assessments during the pre-contract stage of the contractual machinery and the need to align internal employer authorities and timelines for decision making;
- The use of proactive, prospective methods and techniques to assess time and monetary impacts;
- The use of regular joint meetings to proactively raise and resolve / mitigate problematical issues;
- Making sure that the right person is in the right role, and is trained and allowed to perform in that role.

Delivering better business outcomes

Construction projects, no matter what the size - from a small domestic extension to a building a new city - will always have the propensity to involve disputes. With so many different parties involved, and vast sums of money at risk, each individual wants to protect their own interests as such difficulties arise.

However, there are certain approaches to take when dealing with construction disputes, from trying to avoid them happening in the first place to mitigation, resolution and mediation.

Avoidance

Prevention is better than cure, so at the beginning of a construction project, identify the potential risks and put in place procurement strategies and contract structures that are most likely to allow the project to progress smoothly. The size and complexity of many programmes of work mean that disputes are still likely to happen, but up front work can help avoid as many as possible.

Mitigation

Should a dispute arise, recognising the problem and dealing with it quickly is key. Having the right expertise available to isolate and manage issues swiftly will mitigate the effects of the dispute, thus avoiding expensive and lengthy difficulties.

Resolution

When a dispute does escalate and formal proceedings are needed, resolution will require an independent expert witness to provide advice and opinion about the matter. To aid this, both parties should ensure that they have captured comprehensive data about the project which can be made available for the resolution process.

Mediation

The mediation process is a private, confidential and voluntary process that allows both parties to resolve the issue without the need for official court proceedings. With the help of third party facilitator, the process leads to a negotiated settlement which is then recorded as binding and enforceable. This is an innovative approach which typically has a very high success rate.

No matter what technique is used, some disputes will happen. Should this be the case, the need for an experienced team with the right skills to help the dispute see its course quickly and as cost effectively as possible is key. In this way disputes can be kept to a minimum, which will help to reduce delay, lower project costs, and ultimate keep the construction industry doing what it does best – building a better world for us all.

Methodology

This research was conducted by the EC Harris Contract Solutions and ARCADIS Construction Claims Consulting experts and is based on construction disputes handled by the teams during 2012.

About us

EC Harris, an ARCADIS company

EC Harris is a leading global built asset consultancy. As an ARCADIS company, EC Harris has access to approximately 22,000 professionals worldwide operating in over 70 countries, 300 offices and generating in excess of €2.5billion in revenue. Working across a wide range of market sectors, EC Harris helps clients make the most from the money they spend on their built assets. For further information, visit www.echarris.com

Contract Solutions and Construction Claims Services

EC Harris's specialist Contract Solutions and ARCADIS' Construction Claims Services teams help clients avoid, mitigate and resolve disputes. The team is based around the globe and encompasses one of the industry's largest pool of procurement, contract, risk management and also quantum, delay, project management, engineering defects and building surveying experts. The team provides procurement, contract and dispute avoidance and management strategies, management expertise as well as dispute resolution and expert witness services. This is delivered through a blend of technical expertise, commercialism, sector insight and the use of live project data, combined with a multi-disciplined and professional focus.

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