Oregon State Bar CLE Seminars

Mediation and Arbitration in Construction-Related Disputes

Getting Better Results with Mediation and Arbitration in Oregon Series

Cosponsored by the Alternative Dispute Resolution Section

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D. Gary Christensen, *Miller Nash LLP, Portland.* Mr. Christensen chairs the firm's construction industry team; he focuses his practice on commercial construction litigation, negotiation of design and construction contracts, insurance recovery, public contracting, and strategic options for construction projects. He helps clients build schools, medical facilities, affordable housing, distribution centers, resorts, and other large commercial and public projects, from planning, structuring, and negotiating contracting relationships to litigation of claims both during and after construction. He regularly negotiates design, construction, design-build, construction management, and related contracts and subcontracts. He also arbitrates and litigates delay, lien, payment, priority, and defect claims during and after construction. He is active in the Oregon State Bar, serving as an advisory member and past chair of the Construction Law Section and a member of the Business Litigation Section, Litigation Section, and Debtor-Creditor Section. Mr. Christensen is also a member of the Associated General Contractors Oregon-Columbia Chapter and the American Bar Association.

Chapter 20

ADR OF CONSTRUCTION DISPUTES

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§ 20.1 INTRODUCTION

Construction disputes are regularly resolved using methods other than litigation. However, the complex nature of most construction disputes, and longstanding construction industry practices, often require a more sophisticated and industry-specific approach to alternative dispute resolution (ADR) than traditional ADR methods. This chapter assumes that the reader is generally familiar with traditional ADR law and methods (as covered elsewhere in this practice manual). In addition to the material in this chapter, the reader should also review the discussion of ADR for construction disputes in *Construction Law* chapter 19 (OSB Legal Pubs 2019).

Treatment of construction disputes in this chapter focuses on resolution through ADR after a dispute or claim has arisen. For a discussion of drafting construction documents specifying ADR, see *Construction Law* chapter 19.

For ease of reference, claims and disputes involving the engineering, design, demolition, construction, etc., of buildings and other structures are referred to as "construction disputes."

§ 20.2 UNIQUE CHARACTERISTICS OF CONSTRUCTION ADR

As pertinent to ADR, construction disputes have several unique characteristics. First, construction disputes tend to involve complex technical issues. Factual questions involving engineering (civil and structural), geology, project management and scheduling, root cause and product failure analysis, and even plant selection may be at play in many types of construction disputes. For that reason, expert witnesses usually are required. Counsel and neutrals must have a solid understanding of how to

manage the participation of experts, particularly the mutual exchange of information generated by the experts (usually not present in other types of litigation).

Second, the parties in larger-scale commercial and multiunit residential construction disputes tend to be sophisticated, often have been through similar disputes before, and may already be relatively familiar with the litigation and ADR process.

Third, many construction disputes (especially those involving construction defects after a project has been completed) involve many parties. *See* § 20.3-1(d). This affects the logistics of a mediation or arbitration. Challenges in such cases range from the esoteric (how exactly will a settlement by one joint tortfeasor affect the liability of the other potentially liable parties?) to the practical (is there enough room for all participants in the arbitration or mediation venue . . . can certain parties be in the same room with one another . . . how should the hearing or mediation be organized and scheduled to maximize efficiency?).

Finally, construction-defect disputes usually involve sophisticated insurance coverage issues that significantly affect the ability and willingness of the actual parties to reach settlement. This adds insurance adjusters and multiple counsel per party to the already-large crowd of participants. All these issues can affect both the legal issues and process applied by the neutral running the ADR session.

§ 20.3 CHARACTERISTICS OF CONSTRUCTION DISPUTES

There are generally two types of construction disputes, whether on commercial or residential projects. Construction-defect claims typically arise after the project is completed when the project owner or a related party (e.g., property insurance carrier proceeding in subrogation) alleges that it was not built correctly and that the owner has suffered in some way (usually property damage or diminution in value, but sometimes including other forms of damages, such as personal injury from toxic mold caused by water intrusion). These claims frequently are framed in terms of both contract and tort, usually involve multiple parties at all tiers of the contracting chain, and almost always raise insurance coverage questions and

require the involvement of insurance carriers. Indeed the owner's or general contractor's goal is often to bring as many parties into the dispute as possible to increase the number of carriers and consequently the amount of money available for a potential settlement.

By contrast, "traditional" construction disputes tend to involve contractual issues arising during or shortly after the completion of construction, usually concerning cost, payments, scheduling and delay, or the scope of work—and very often involve all of them. These disputes generally are not about property damage, but rather about whether one party or the other was denied the benefit of the bargain struck in one of the many layers of contracts that are common in large construction projects.

Both kinds of disputes can be highly complex and almost always involve expert witnesses. Cases often involve both types of disputes—a claim by a contractor for nonpayment may often result in a construction-defect claim, and vice versa. Thus, it is common to have two very different kinds of claims proceeding in the same case. Structuring a mediation or arbitration proceeding that is adapted to the similarities and differences in each of these types of disputes is critical for a successful result.

§ 20.3-1 Construction Defect

§ 20.3-1(a) Insurance Coverage Questions

The most significant difference between a construction-defect dispute and a traditional dispute is the involvement of one or more insurance carriers, who may have differing degrees of responsibility for both their insured's cost of defense and for any ultimate liability. The carriers have significant impact on whether a party will agree to settle, because the carriers controls the money. Therefore, the dynamic among attorney, client, and carrier is very important. In Oregon, although the insurance carrier hires the attorney, the attorney owes a fiduciary duty to the insured client, regardless of the carrier's interest. This is referred to as a tripartite relationship. As long as there is a joint economic interest in the outcome, this type of common representation is acceptable. *See* OSB Formal Ethics Op No 2005-77 (rev 2016); OSB Formal Ethics Op No 2005-121 (rev 2016).

When the carriers for a single party disagree, or when the party disagrees with its carrier, the path to settlement becomes more complicated.

The most common conflict arises when the carrier has accepted a tender of defense based on the allegations in the complaint or claim, but has reserved its rights regarding its ultimate duty to indemnify its insured (usually because there is a question about when the claim arose or whether an exclusion in the insurance policy applies). The insured may end up having two or more lawyers: insurance defense counsel and coverage counsel. This can often result in one or more side negotiations within the context of the larger mediation or arbitration, partial settlement agreements that extricate a party but leave the carriers to resolve their disagreements in a separate forum, etc.

The complexities that can be presented in these circumstances make it critical for counsel to select a mediator who understands the nature and dynamics of these relationships and the potentially competing interests inherent in them. It often becomes necessary for the mediator to engage in discussions with one or more of these four parties—defense counsel, coverage counsel, insurance adjuster, and insured—independent of each other or in side groups in order to identify conflicts, potential roadblocks to insurance coverage, and potential avenues to resolution.

§ 20.3-1(b) Experts

Construction-defect cases are unlike many other disputes in Oregon because each party's expert witnesses usually are disclosed to the other side. In disputes involving residences, this is due partly to the requirement in ORS 701.565(3)(e) that the owner asserting a defect claim provide the respondent with "[a]ny report or other document evidencing the existence of the defects and any incidental damage" (allowing the contractor the opportunity to repair, pay compensation, or do nothing). Although the contractor is not similarly required to disclose its experts or provide the other side with an expert report, in practice most parties exchange reports and disclose experts by the time a case reaches mediation.

When contractual arbitration requirements apply, the exchange of expert information commonly is required by the rules of the arbitration service provider. For example, the procedural rules for arbitrations being administered by the Arbitration Service of Portland, Inc. (ASP) require the disclosure of expert witnesses and the exchange of expert reports. *See* ASP

Arb Rules r 19(A) (Arb Serv of Portland rev 2019). The ASP rules also presume the admissibility of a written expert report. *See* ASP Arb Rules r 22(B)(6). Similarly, the American Arbitration Association's (AAA) Construction Industry Arbitration Rules (Constr Indust Arb Rules), available at <www.adr.org/sites/default/files/document_repository/Construction_Arbitration_Rules_7May2018.pdf>, which are not as directive as ASP's, nevertheless presume the exchange of expert reports and contemplate a discussion between the parties and the arbitrator(s) "whether to establish a schedule for the parties to identify their experts and exchange expert reports." Constr Indust Arb Rules P-2(a)(xi) (Am Arb Ass'n 2015).

Depending on the complexity of the claims and the number of parties involved in the dispute, experts may attend the main mediation session with all the parties, or there may be a separate session involving only the experts (either with or without counsel) to discuss the empirical evidence of the claims, the causes and scope of property damage, the scope and cost of possible repairs, and the allocation of responsibility among the defending parties. In either circumstance, the information exchanged by the experts generally remains confidential pursuant to OEC 408, mediation confidentiality, and, usually, by an additional agreement among the parties that nothing shared, proposed, or admitted by any expert during mediation is binding and that it cannot be used as an admission at trial or hearing. The information exchanged between the experts thus tends to be relatively free and honest, and can be key to a successful settlement.

When a case reaches the arbitration stage, the use of experts is more like a traditional trial, except that the parties have usually exchanged expert reports by that stage, whether or not a formal ADR service is used, and there is unlikely to be a "trial by ambush," as can happen with other types of disputes.

§ 20.3-1(c) Differing Legal Standards

One challenge to ADR among multiple parties is that different legal standards may apply to different parties' conduct, and must be navigated by the parties and the neutral. For example, a single case may include a contractor's claim against an owner for nonpayment (contract law); the owner may counterclaim for construction defects (tort law) and add a third-

party claim against the design professional (professional liability). In contract claims, the primary issue is whether one or the other party breached its duty under the contract documents. If the claims involve negligent construction, a reasonable-contractor standard applies. If the owner asserts claims against its design professional, a professional standard of care arises. This can create challenges in attempting to allocate responsibility among the parties. It is conceivable that a contractor is not negligent and correctly adhered to the contract documents, and that the design professional did not breach the professional standard of care, but that the project does not ultimately perform as intended. That scenario is often argued in a proceeding that involves both designers and contractors.

§ 20.3-1(d) Multiple Parties

Construction-defect disputes almost always involve multiple parties in addition to the primary claimant and respondent. The residential-construction-defect notice statute (ORS 701.560–701.600) expressly contemplates this structure by providing for a "secondary notice of defect" whereby a prime contractor must notify its subcontractor whose work is at issue about the allegations of defective work and provide an opportunity for that subcontractor to participate in the response to the claim. ORS 701.570. Additionally, owners may elect to join their design professionals in a dispute involving questions about errors or omissions in the design process.

The sheer number of parties often affects the structure of the mediation or arbitration. In a construction mediation, the claimant often is in one room, the prime contractor is in another, and the subcontractors are grouped together in a third room (colloquially known as the "bullpen"). The mediator occupies yet another room. If one or two subcontractors have a greater involvement or risk in the dispute, they may also be in separate rooms. When the mediator is ready to talk to one of the many subcontractor representatives, that party is summoned out of the bullpen to have that discussion in private. This happens over and over as the mediator works to build a sufficient pot of money with which to settle the dispute. Sometimes, the mediation is staggered—for example, with all parties implicated in water intrusion being scheduled for one day, all parties implicated in structural problems on another day, etc.

Similarly, in a construction arbitration, the presence of multiple parties often affects how the hearing is structured. Usually, claims are asserted against other lower-tier parties in a manner similar to third-party practice in court. Subcontractor claims can sometimes be grouped together for the sake of an efficient hearing. If design professionals are involved, the parties and the arbitrator may decide to bifurcate those claims to minimize the difficulties presented by differing legal standards. And, as with mediation, the parties and neutral may decide to organize the hearing by subject matter, and so on.

§ 20.3-1(e) Common Insurance Coverage Issues

Oregon courts do not strictly adhere to a contract-versus-tort regime when determining whether damages are covered by insurance or whether a carrier has a duty to defend. Rather, the question is primarily whether the damages are purely economic or whether there are noneconomic damages (e.g., property damage or personal injury). Generally, a party's insurance policy will cover noneconomic damages, but not economic damages. To complicate matters further, Oregon courts have been modifying the traditional economic-loss doctrine in favor of a foreseeability standard in construction-defect cases. *See Harris v. Suniga*, 209 Or App 410, 149 P3d 224 (2006), *aff'd*, 344 Or 301 (2008); *Bunnell v. Dalton Constr., Inc*., 210 Or App 138, 149 P3d 1240 (2006), *rev den*, 344 Or 558 (2008). These issues are often key to determining whether and to what extent an insurance carrier will agree to provide funds with which to settle a defect claim.

§ 20.3-2 Traditional Claims

§ 20.3-2(a) Primarily Economic Damages

Traditional construction claims arise during construction and usually involve scope and payment issues.

Traditional construction disputes can arise for a variety of reasons that usually do not involve property damage or allegations of defective workmanship. Rather, these are disputes about nonpayment or underpayment; so-called "scope creep" (a dispute about whether certain work is within or outside the contract's scope of work); delay or acceleration

claims, by which one party is seeking compensation for costs that arise when a project runs longer than the agreed-upon schedule; and so on.

§ 20.3-2(b) Ongoing Business Relationships

Unlike in construction-defect disputes, in which the various parties' relationships and conflicts can be muted by the presence and involvement—and often the direction—of insurance carriers, the principals for the parties in a traditional dispute are often front and center throughout the dispute. The parties, rather than their insurance carriers, make decisions. The parties themselves often have multiple other projects ongoing together. Counsel and mediators are wise to understand the nature of these ongoing business relationships and to what extent they can be used as currency within the mediation.

§ 20.3-2(c) Unique Technical Issues

Traditional construction disputes often involve complex, technical, and scientific questions necessitating the use of expert witnesses. These have generated unique bodies of law. The areas of dispute usually fall into one of three broad categories: change-order pricing disputes, scope-of-work disputes, and disputes about time and the resulting cost.

§ 20.3-2(c)(1) Change Order Issues

Disputes involving change orders are often about the cost of a change after the parties have agreed on its scope but cannot agree on its cost. This type of dispute frequently arises when a contractor has partially performed work, only to be told to change it midstream. This means undoing work already completed, or adapting the new scope around the existing work, and factoring in the time impacts as well. Calculating the cost impacts of such a change can be difficult and imprecise.

§ 20.3-2(c)(2) Delay or Acceleration

Time-related disputes arise for a variety of reasons. The project may have been suspended because of permitting problems, weather, or labor strife, or because materials or equipment became unavailable, or because the project site conditions were different from what the parties anticipated, necessitating a change in excavation methods, and so on. Or an owner may wish to have the project completed earlier than originally set out in the

project schedule and direct the contractor to accelerate its production. Or the owner may believe the contractor is falling behind schedule and direct acceleration for that reason.

Time-related claims are among the most complex and difficult to unwind in a construction dispute. They usually require the use of a scheduling expert. Often, each party's expert uses different measurement criteria to assess the extent and cause of a delay. There may also be concurrent delay—when multiple parties were causing delay to the same aspect of the schedule. Any of these issues can take significant time in either a mediation or an arbitration.

§ 20.3-2(c)(3) Scope

Probably the most common types of traditional construction disputes are about scope of work. Is the disputed work included in the contract or is it an extra? That is the ultimate question. These disputes can arise between owner and contractor, and usually involve an omission in the drawings and specifications versus whether the disputed work was "reasonably inferable" from the existing plans.

Alternatively, scope disputes can arise between subcontractors and the prime contractor. Does the subcontract include the disputed work, or is it included within another subcontractor's scope of work? This is a common occurrence when the work of two trades (such as roofers and framers) overlaps. A subcontractor may argue that it excluded the disputed work from its bid, while the contractor argues that the work was included in the final subcontract documents. As with nearly every other kind of construction dispute (except perhaps for a simple refusal by one party to pay another), scope claims can be very technical and tend to require the use of expert witnesses.

§ 20.4 LEGAL AND CONTRACTUAL PREREQUISITES TO CONSTRUCTION ADR

§ 20.4-1 Contractor Licensure

A contractor cannot seek compensation for its services through arbitration, construction liens, bond claims, litigation, or other dispute-resolution methods unless that contractor was properly licensed and

endorsed by the Oregon Construction Contractors Board (CCB) continuously from the time of bidding or contract formation until completion of the project. ORS 701.131(1). The definition of *contractor* is broad and includes persons that one may not think of as construction contractors. ORS 701.005; OAR 812-002-0170. *See generally Construction Law* chs 1, 18, 19 (OSB Legal Pubs 2019). Lack of licensure is not a bar to the owner suing an unlicensed contractor.

PRACTICE TIP: An initial item of due diligence in a construction dispute is to verify with the CCB whether the lawyer's client (if a contractor) and each adverse or potentially adverse contractor has been continuously licensed and endorsed by the CCB throughout the project.

CAVEAT: Continuous licensure cannot be determined solely by checking the CCB's website. Upon request, the CCB will certify the full licensure history of a contractor, which will reveal any formal lapses. But a contractor might also fail to meet licensure or endorsement requirements at some time unknown to the CCB. For example, the contractor may have changed insurance carriers but had a gap between policies. The CCB may not be informed of the change or gap, so no formal lapse would be noted. Thus, discovery may properly focus on whether a contractor failed to meet its continuous licensure and endorsement requirements at the relevant times.

§ 20.4-2 Contractual Prerequisites to ADR

Increasingly, design and construction contracts condition formal ADR processes on the completion of informal mitigation processes designed to avoid formal proceedings. These commonly include (1) some hierarchical process in which the parties bump a dispute up to increasingly higher levels of each party's management for direct negotiation or (2) informal resolution by another party to the project, usually the architect. These processes can be successful in reaching practical, business-oriented solutions at minimal expense.

At the same time, these prerequisites can get in the way of dispute resolution if they are inappropriate or poorly drafted. For example,

construction-defect claims arising years after substantial completion may still need to be submitted to the architect before ADR may commence, even though the architect no longer serves (and is not paid to serve) in that role. The parties may waive inapt requirements.

Current editions of both the American Institute of Architects (AIA) and ConsensusDocs families of design and construction contracts contain versions of these informal prerequisite processes. *See generally Construction Law* ch 19 (OSB Legal Pubs 2019).

> PRACTICE TIP: The initial evaluation of contracts involved in construction disputes should include mapping the contractually required path for disputes to take. Skipping steps can result in costly motion practice and delay in ADR proceedings.

§ 20.4-3 CCB Complaint Prerequisites

Formerly, the CCB provided ADR services for construction disputes. That is no longer the case, except for limited mediation provided to homeowners and their contractors. Now, the CCB will accept claims against licensed contractors but will defer to litigation or arbitration for the parties to adjudicate the claims themselves.

A complaint to the CCB (1) is the only channel to reach the contractor's public registration bond and (2) is used to initiate the CCB's enforcement action that could affect the status of a contractor's license or endorsement. For claims against the contractor's licensure bond, the date of the CCB complaint filing is used to determine the priority of multiple claimants. *See generally Construction Law* chs 18, 19 (OSB Legal Pubs 2019).

Navigating the CCB complaint process successfully is intricate and can be complicated, depending on the nature of the claimant, the type of contractor, the nature of the work involved, the size and type of the project itself, and other factors. But that process cannot begin until the complainant (owner, upstream contractor, or laborer) provides the contractor with a written notice of intent to file the claim with the CCB, sent by certified mail at least 30 days before filing the complaint with the CCB. ORS 701.133(1). Proof of service is required with the complaint as a prerequisite to the CCB's ability to open a claim.

The limitation period within which to file a CCB complaint is much shorter than the statute of limitations for claims in court or arbitration, usually a year to 14 months. Complaints must be filed with the CCB on forms that it provides on its website: <www.oregon.gov/CCB/complaints/Pages/how-file-a-complaint.aspx>. OAR chapter 812 provides complaint-filing requirements. Filing deadlines may be tolled under limited circumstances. ORS 701.133(2).

PRACTICE TIP: The administrative rules regarding the CCB are set forth in OAR chapter 812, but they are amended often. Therefore, lawyers are advised to follow current rules and procedures carefully.

§ 20.4-4 Residential-Defect Notice Prerequisite

A homeowner (and certain landlords) must provide the contractor with the notice required by ORS 701.560 to 701.605 before proceeding with arbitration or litigation. The prime contractor must also deliver a secondary notice under that statute to each subcontractor whose work is implicated in the claim. All contractors have the right (but not the obligation) to inspect the residence to determine the claim's validity and prepare their responses. Only after complying with this requirement can formal arbitration, bond claims, or litigation ensue. This is not a bar to mediation, however.

PRACTICE TIP: The notice requirement in ORS 701.560 to 701.605 can be combined with the notice required before filing a CCB complaint. ORS 701.133(1). The notice periods may run concurrently.

NOTE: The residential-defect notice statute allows for limited tolling of any statute of limitations that may run during the notice period. *See* ORS 701.585.

§ 20.5 UNIQUE ISSUES IN ARBITRATION AND OTHER BINDING ADR

Binding ADR proceedings (including arbitration) may be prescribed in the parties' design or construction contract before claims arise, or in an arbitration or mediation agreement negotiated after disputes have arisen.

These are not mutually exclusive: contractual ADR terms often leave procedural processes and rules to be established by the parties' later agreement or by resort to the rules of a specified ADR service. Although the parties to a construction dispute may alter these requirements by mutual agreement at any time, the need to obtain consent from multiple parties may make obtaining such agreement challenging.

Binding ADR proceedings often are required by the terms of design and construction contracts. These terms should (but often do not) address critical issues for success of ADR. At a minimum, the terms should specify who is bound by the ADR clause (discussed further below in § 20.5-1), what kinds of disputes are or are not subject to the ADR proceeding, whether ADR is mandatory or permissive (e.g., a party or parties can unilaterally determine whether to invoke or veto ADR), whether the ADR process will result in a binding decision or award that can be entered as a judgment, and the scope of remedies that the ADR neutral may apply.

§ 20.5-1 Ensuring Joinder of Parties

Whether ADR can be successfully employed depends to a great degree on whether all the relevant parties can be brought to the same table. Construction disputes usually involve multiple parties of different "tiers" beyond the owner, developer, and general contractor. First-tier subcontractors are those who contract directly with the prime or general contractor; second-tier subcontractors or suppliers contract with the first tier; etc. In this chain, each tier has a contract with the party above it and the party below it (if any). Likewise, the architect, its engineers, and its other subconsultants have a similar tiered contracting chain, starting with the owner-architect contract.

> NOTE: These claims may be combined in the case of design-build contracts. *See generally Construction Law* ch 8 (OSB Legal Pubs 2019).

Because liability may be shared by a combination of these entities across the tiers, whatever ADR requirements bind the owner and general contractor should also bind the general with its first-tier and lower-tier subcontractors and suppliers. The same issue must be addressed in the architect contracting chain. Otherwise, there is a risk of multiple and

inefficient ADR proceedings, possibly yielding inconsistent results. This frustrates the efficient and complete resolution of claims.

This important coordination task ideally is accomplished by a "flow-down" clause in the original contract documents, which bind the lower-tier party to the terms and conditions of the upper-tier contracts, usually including the owner's contract with the general contractor (or architect). Flow-down terms require (1) that each lower-tier entity construct the project using the same design documents and specifications, as applied to the work of the specific lower-tier subcontractor (e.g., electrical subcontractor, drywall subcontractor); and (2) that all lower-tier entities, regardless of the scope of their respective work, follow all the same legal terms and conditions applicable to the entire project, including dispute-resolution provisions. Breaks in the flow-down chain can and do happen, resulting in arbitration between some tiers and litigation between others, inconsistent results, and incomplete or tortured final resolution of claims.

Likewise, with separate design and construction contracting chains, the terms and conditions of the architect's contract with the owner should be "coordinated" to have the same basic legal requirements as those between the owner and the contractor, to avoid a mismatch and multiple proceedings among all the parties on the project.

> PRACTICE TIP: When a dispute arises (if not before), the lawyer should examine not only the terms of the client's contract, but also the contracts of the tiers above and below it. A failure of flow-down terms or coordination of contracts, creating a mismatch in dispute-resolution terms, can have a real effect on the cost and time required to resolve the entire dispute, and these issues might be better resolved or dealt with early in the dispute process.
>
> NOTE: An advantage of using contract "families," such as ConsensusDocs or the AIA contract documents, is that these terms are already coordinated between the design- and construction-contract chains, and within those of the lower-tiered chains. But potential disadvantages of using standard form families should also be considered. *See generally Construction Law* ch 19 (OSB Legal Pubs 2019). In addition, standard documents are usually amended to fit

particular parties and projects, which may disrupt the coordination and flow-down terms. *See, e.g.*, AIA Document A201-2017, § 15.4.4; ConsensusDocs 200, § 12.6 (consolidation and joinder).

§ 20.5-2 Claims Subject to ADR

Design and construction contracts may or may not be written to address all claims that arise during the construction project. An arbitration clause, for example, may apply only to disputes arising before substantial completion or may not apply at all unless one party elects to employ arbitration.

§ 20.5-3 Rules to Be Applied

A design or construction contract may specify as much or as little of the ADR process as is required. It may address discovery limitations, evidence rules to be used (or not), confidentiality of proceedings, venue, and other important considerations. But most do this only by incorporation or reference to the published rules of an ADR service. *See generally Construction Law* ch 19 (OSB Legal Pubs 2019).

The rules of ADR services vary widely about important issues, such as discovery, and few are specifically keyed to construction disputes. The two most-used sets of rules that are specific to design and construction arbitration are the AAA Constr Indust Arb Rules and the JAMS Engineering and Construction Arbitration Rules and Procedures. The Constr Indust Arb Rules have four tracks: regular (R rules), fast track (F procedures), large and complex (L procedures), and arbitration by document submission (D procedures). (These two rule sets also provide for mediation, either separately or in conjunction with an arbitration proceeding.) These rules have been modified through the years, so the correct edition should be consulted.

CAVEAT: ADR clauses may be ambiguous about which version or edition of the specified rules applies to claims. On occasion, that can make a difference in the proceeding. The clause invoking the rules may point to those in force when the contract was formed or those in force when the dispute arises and a demand is made to arbitrate.

§ 20.5-4 Discovery

Discovery is of particular concern in construction disputes. Establishing delay, additional cost, the cause of defective work, and other aspects of construction claims is not possible without the contracts, schedules, cost reports, and project documentation generated by others also working on the project. Expert witnesses evaluating the schedules for delay claims, or the cost reports for additional-cost claims, require the data of others. ADR for construction disputes is most successful after the parties have a good handle on the potential evidence. Consequently, the ADR rules must permit sufficient discovery, although some rules do not.

§ 20.5-5 Venue

If not specified, the ADR proceeding's location will be established by the incorporated rules or the ADR service retained to administer the proceeding. Provisions in construction contracts that select non-Oregon venues for dispute resolution are void and unenforceable under Oregon law. ORS 701.640(1)(a). But the Federal Arbitration Act (FAA), 9 USC §§ 1–16, may supersede Oregon's venue law if it conflicts with the FAA and impedes implementation of the parties' arbitration agreement. *See* § 9.1-1.

The arbitration clause may define permissive venue or exclusive venue. Consequently, the language "venue for the hearing is in Marion County, Oregon," allows hearings to be conducted in Marion County but may not be held to require that hearings be conducted there. If exclusive venue is to be set in the agreement, the venue clause should specify, for example, "All hearings must be held in Portland, Oregon."

§ 20.5-6 Choice of Law

The choice of law for contracts for construction work to be performed primarily in Oregon is the law of Oregon. ORS 15.320(2); ORS 701.640(1)(a).

§ 20.5-7 Selecting an ADR Service Provider

Construction arbitration normally is conducted either by well-established arbitration service providers or by individual neutrals, chosen by the parties, who are familiar with the construction industry and its

claims. Whether to use a service provider or an individual neutral is largely based on the particular case's need for resources that individual neutrals may not be able to provide, such as administering voluminous, complex discovery and prehearing matters in arbitration, and on whether the parties can agree on a particular arbitrator (since service providers can select a neutral for parties who are unable to agree on one).

Arbitrators need not be associated with a particular arbitration service firm. Many individual arbitrators, mostly construction lawyers and former judges, know the construction industry and its laws and regularly arbitrate and mediate construction disputes. These arbitrators are much less costly than an ADR service, but do not provide prepublished, comprehensive arbitration rules and other administrative options that an arbitration service can provide. However, the arbitrator and parties can stipulate to follow published rules by standard providers like the AAA.

A number of Oregon and national firms provide ADR services for construction disputes. Each has its own fee schedule and rules. These rules may limit the compensation of the arbitrator or panel, and may provide for streamlined and less-costly discovery and prehearing processes. Local services that have historically provided arbitrators with experience in construction law include United States A&M of Oregon, Inc., and the Arbitration Service of Portland, Inc. On a national basis, JAMS and AAA have extensive experience in construction disputes. This is not an exhaustive list. The Oregon State Bar's ADR Section website maintains a list of useful links to various ADR websites, at <www.osbadr.wordpress.com>. For further discussion about choosing an arbitrator, see chapter 2.

Individual neutrals may have their own forms of contract, but usually an agreement needs to be reached with the principal parties and the neutral about ground rules, procedures, and standards. A private agreement typically incorporates the construction-dispute rules available from the AAA or JAMS, modified to fit the dispute. *See generally Construction Law* ch 19 (OSB Legal Pubs 2019).

When selecting an ADR service, the attorney and client should review the discovery and procedural rules of the service and the likely effect of those rules on the cost and efficiency of resolving the construction

dispute. The AAA, for example, has tiers of specific rules suited just for construction disputes. *See Construction Law* § 19.2-4. The services also usually provide the qualifications of their arbitrators with regard to construction disputes.

§ 20.6 UNIQUE ISSUES IN CONSTRUCTION MEDIATION

§ 20.6-1 Choice of Mediator

Individual mediators steeped in construction-claims experience usually mediate construction disputes. ADR services provide less value for mediation than they can for arbitration.

Individual neutrals may have their own forms of contract, but usually an agreement needs to be reached with the principal parties and the neutral about ground rules, procedures, and standards.

For further discussion about choosing a mediator, see chapter 2.

§ 20.6-2 Identification and Presence of Necessary Parties

Ensuring that the right parties with knowledge of the issues in dispute and with authority to settle are present at the mediation is one of the greatest challenges for counsel and mediators. This is particularly so in construction-defect disputes, in which multiple persons may fill these roles: the client/insured, the insurance adjuster(s), the experts, and sometimes the primary fact witnesses. The absence of one or more of these persons can present significant impediments to a successful mediation. Many mediators now require a commitment that parties with authority to settle be physically present at the mediation, or at a minimum available at all times by telephone. Even that accommodation can become problematic when an adjuster is located in a different time zone and the mediation runs long.

By contrast, in most "traditional" construction disputes the smaller number of parties, and (usually) absence of insurance coverage issues, may diminish the problem of getting the right parties to the mediation.

§ 20.6-3 Using Expert Witnesses

As discussed in § 20.2 and § 20.3-1(b), construction disputes create unique questions and challenges regarding the use of experts. These issues are highlighted when the parties elect to mediate their dispute.

§ 20.6-4 Separate Expert-Only Caucuses?

The parties and mediator must first decide whether to include experts in the mediation at all. Assuming that experts will be involved, the next question is how. Depending on the mediation's size, it may make sense for experts to meet in a separate session before the main mediation session, so that the technical issues that are in play can be fully vetted without getting in the way of the ultimate negotiation. Alternatively, it may make more sense simply to have experts present to address questions as they may arise during the course of the single session.

§ 20.6-5 Exchange of Expert Reports and the Effect of Oregon's Notice-of-Construction-Defect Law

While Oregon does not ordinarily allow one party to compel the discovery of an expert's identity or of that expert's opinions before trial, construction-defect cases are unique. ORS 701.565 requires that a complaining party provide a notice of the allegedly defective construction to the other party, with "[a]ny report or other document evidencing the existence of the defects and any incidental damage" as part of the notice. ORS 701.565(3)(e). Since the complaining party must almost always have an expert evaluation of the property that is the subject of the complaint to properly identify areas of defective construction and damage, that party must necessarily provide a copy of the expert's report to the other side. But the contractor that responds to the notice is not compelled to produce or provide its own expert report. So in the context of a mediation, the question often arises whether the contractors will make their experts available for the mediation, and further whether they will provide copies of their reports to the complainant.

As a practical matter, most defect cases—particularly those that are complex and involve significant dollars and risk—do involve the exchange of reports before the mediation. Without that information it becomes difficult for the parties to identify and understand the basis for the claims

or defenses, how to allocate responsibility, and how to evaluate the ultimate risks in the dispute.

§ 20.6-6 Presence of Insurance Adjusters

Construction-defect litigation usually involves insurance carriers, and therefore insurance adjusters. The logistical challenges to getting adjusters to attend are no different here than in other cases in which insurance dollars are in play. There are some unique aspects given the potentially available dollars, the length and complexity of construction-defect mediations, and the fact that insured parties are often active participants whose interest in the outcome may differ from that of their carriers. Some mediators require, as a condition of mediating the case, that adjusters be physically present at the mediation. Others are more sanguine about an adjuster's being available by phone. Again, that can create its own challenges if the mediation runs long.

§ 20.6-7 Indemnity and Insurance Coverage Issues

Coverage disputes are often a complicated subset of construction-defect mediations. If there is a question whether coverage exists, or whether there are sufficient limits to cover all the alleged damages, and so on, it may be necessary for a defending party to have independent counsel present to advise the insured on its rights between it and its carrier. The mediator must be able to assist in negotiations between the party and its carrier over issues like the amount that the carrier will contribute to settlement, the allocation of any settlement among multiple carriers for the same insured, whether to make an offer at all, whether and to what extent the insured will contribute to the settlement, the allocation of settlement between (covered) defect claims and (often uncovered) warranty and contract claims, etc.

§ 20.7 OTHER TYPES OF CONSTRUCTION ADR

§ 20.7-1 Disputes Review Boards and Project Neutrals

A disputes review board (DRB) is a dispute mechanism unique to the construction industry. It was originally developed by the American Society of Civil Engineers for use in large tunneling projects, and is still most often used on large, usually public, infrastructure projects.

At the start of a project, a DRB individual or panel is appointed, consisting of construction-industry experts. (A single individual may be chosen to act in this role, who is sometimes called the "project neutral.") The DRB stays in place throughout the project and issues nonbinding opinions on disputes that arise during its course. Submitting a dispute to the DRB is usually a contractual precondition to pursuing mediation, arbitration, or litigation. *See generally Construction Law* ch 19 (OSB Legal Pubs 2019).

The contract documents usually specify whether and to what extent a DRB decision may be used as evidence in subsequent litigation or arbitration. Often, the contract documents specify that the DRB decision is admissible in further proceedings. *See* ConsensusDocs 200, § 12.3. If the nonbinding DRB findings are admissible in litigation or arbitration, that fact creates additional pressure on the parties to accept the DRB decision and settle the dispute.

§ 20.7-2 Complex-Case Designation and Referee

Oregon generally requires all civil actions to be tried within one year from their commencement, but allows for designation of some actions as "complex cases," with extension of those deadlines and other advantages. UTCR 7.030. Some circuit courts specifically provide for complex construction litigation, either by rule or by practice. For example, Multnomah County's construction-litigation program is described at <www.courts.oregon.gov/courts/multnomah/go/Pages/civil.aspx>.

Construction cases designated "complex" may be assigned a neutral referee by the presiding court. The referee usually is empowered to determine discovery disputes and other nondispositive pretrial motions (subject to appeal to the circuit court) and may have substantial input (by direct contact with the court or otherwise) into the pretrial calendar. Referees will discuss ADR options with counsel and usually recommend and help coordinate mediation. At times, parties have enlisted the complex-case referee to also mediate the dispute, although this may not always be wise for strategic reasons unique to each case. At a minimum, the referee coordinates with the court and with any chosen mediator to plan case scheduling and, at times, to narrow the issues requiring decision.

§ 20.7-3 CCB Residential Mediation

The CCB processes complaints involving residential structures under ORS 701.145. A complainant must first file the appropriate breach-of-contract complaint form with the CCB. If the CCB accepts the complaint, it will notify the opposing party and begin an investigation. ORS 701.145(4). CCB staff will conduct an on-site or telephonic mediation of the dispute. If the CCB determines that the contract was breached or that work was performed negligently or improperly, the CCB may recommend a resolution of the complaint. ORS 701.145(4); OAR 812-004-1450 to 812-004-1490. For most homeowner complainants, the CCB investigator will attempt to assist the parties in settling their dispute before recommending complaint resolution. But if the CCB staff cannot resolve the complaint, the complainant must go to court or arbitration to adjudicate the dispute before the CCB will allow access to the contractor's licensure bond. ORS 701.145(5). *See generally Construction Law* ch 19 (OSB Legal Pubs 2019).

§ 20.7-4 Final-Offer or "Baseball" Arbitration

In cases where liability appears clear but the parties differ substantially on the appropriate amount of damages, they may agree to an arbitration model, derived from Major League Baseball salary disputes, in which each party presents its case along with its assessment of what judgment it believes the arbitrator should award; the arbitrator then is required to choose one or the other party's offers, without discretion to arrive at a different figure. This form of ADR encourages the parties to scrutinize their own claims to ensure that the position submitted to the arbitrator is as reasonable as it can be, to maximize the likelihood that the arbitrator will select it. *See* JAMS Eng'g and Constr Arb Rules & Procedures R 33 (2014) (optional rule for final-offer arbitration), *available at* <www.jamsadr.com/rules-construction-arbitration>. In some cases, the parties' self-editing of their own demands may provide a basis for settlement even before the arbitration concludes.

§ 20.7-5 Minitrial

The parties may agree to a process in which they present evidence in an abbreviated hearing, usually with one or no witness, before a neutral

who, following the presentation, encourages the parties to reach an agreement based on the information provided and, if they cannot, issues a nonbinding determination and then attempts to mediate the dispute.

§ 20.7-6 Bracketed "High-Low" Arbitration

The parties may agree in writing among themselves, either before or during arbitration, on minimum and maximum amounts of damages that may be awarded on each claim or on the claims in the aggregate. The arbitrator is not made aware of this agreement, unless the parties agree otherwise. If the arbitrator issues an award that falls within the high and low amounts agreed on, the award stands as it is. If it falls outside that range, however, the final award will reflect the agreed-upon minimum (if the award is lower) or maximum (if the award is higher) amount. *See* JAMS Eng'g and Constr Arb Rules & Procedures R 32 (2014) (optional rule for high-low or bracketed arbitration), *available at* <www.jamsadr.com/rules-construction-arbitration>.

§ 20.8 SCOPE AND DOCUMENTATION OF SETTLEMENTS

§ 20.8-1 Preparing Settlement Agreements

The settlement agreement prepared at the conclusion of a construction dispute's successful mediation is not unlike that document in any other dispute, except in some circumstances. For example, parties will often mediate before a project is substantially complete, meaning that they must continue to work together and the settlement must hold during the ongoing project. Or parties will agree to settle most but not all of their disputes and leave others open to be addressed later. The settlement must carefully articulate what is being settled and what is not. In the context of a construction agreement, that can be a very technical and difficult endeavor.

§ 20.8-2 The Mediator's Role in Documenting the Settlement

Parties often ask the mediator to act as the scrivener for a settlement agreement or to provide the agreement template, or both. There is a near consensus that a mediator acting as a scrivener is not practicing law and that there are no ethical implications in doing so. However, the mediator and parties in construction disputes should be cautious about having the mediator act as the scrivener, particularly if the settlement is not resolving

all known and unknown issues between the parties. When fewer than all possible disputes are being resolved, there is a heightened need for specificity of what is in and what is out of the agreement. The parties and their counsel are generally better equipped to articulate these technical details.

§ 20.8-3 The "Czar" Clause

The mediator is also often asked to act as the "czar" of the agreement in case a dispute arises about the document's interpretation or enforcement. In other words, the mediator "rules" on any such disputes, taking him or her out of the role of mediator and into a role more like that of an arbitrator. There are pros and cons to creating that role for the mediator. *See* § 6.5-1. When considering whether to include such a provision in the context of a construction dispute, however, counsel and the mediator should consider the nature of potential disputes. If ongoing work could result in future disputes governed by the agreement, or there is a technical aspect to potential disputes, a subject-matter expert, rather than the mediator, may be a more appropriate decision-maker. When a subject-matter expert is to be used in that role, it is important for the parties to jointly select someone they each trust to make binding decisions, and to obtain that person's agreement to act in that role before the agreement is finalized and executed.

§ 20.8-4 Addressing Releases and Prospective Waivers

Drafting release and waiver language can sometimes feel as though it is taking as long as the mediation itself. The scope of a release and waiver can be the "make or break" issue in a construction mediation. For example, in a simple payment dispute, the parties will usually agree that the claimant's payment claims are extinguished but that the party remains bound to its contractual obligations, including its duty to honor warranties, and to indemnify against future claims arising from its work. If that party demands a release of all claims in exchange for a compromise on a disputed payment, however, it can undermine the entire agreement. The same can happen if a dispute arises over one aspect of work but one party wants a release of claims related to all work.

These important substantive questions tend to be overlooked until late in the mediation process—often until the parties are attempting to draft the settlement documents after the primary dispute has been resolved. The

best way to avoid surprises that could undermine a settlement is for the parties to raise issues about the scope of potential releases early in the mediation process, so that this discussion becomes a part of the main negotiation.

§ 20.8-5 Indemnity and Warranty Obligations

The parties often argue over the scope of ongoing responsibilities after a settlement is reached. To what extent does a party owe a continuing obligation under a warranty if the warranted work was the subject of the dispute? To which parties (or third parties) does a settling party owe a duty of indemnity, and for how long? Because of the complicated nature of these future and sometimes esoteric obligations, the parties should be discussing the parameters of these obligations early in the process to avoid disputes during the document-drafting phase.

Appendix 20A Abbreviations

AAA ..... American Arbitration Association

ADR ..... alternative or appropriate dispute resolution (see § 1.1)

AIA..... The American Institute of Architects

CCB..... Construction Contractors Board

Constr Indust Arb Rules ..... AAA Construction Industry Arbitration Rules, <www.adr.org/sites/default/files/document_repository/Construction_Arbitration_Rules_7May2018.pdf>

DRB..... disputes review board

ADR for Design & Construction Disputes

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How do construction disputes differ?

- Multiple parties, different contract chains
- Lack of privity
- Insurance
- Sophisticated parties
- Standards of care
- Expert witnesses
- Multiple claims among parties
- Lien requirements and risks
- Payment and performance bonds

§ 20.2

Prerequisites to ADR

- CCB license “continuously”
- Contractual
- File with CCB for public bond recovery
- Residential defects: statutory notice to contractor

§ 20.4

Defects vs. traditional disputes

- Traditional: scope of work, delay, and payments
- Defect: after completion of work

§ 20.3

Traditional claims

- During project rejected change proposals or directives = “disputes”
- “Claims”
- Scope creep
- Delay and acceleration—difficulties of proof
- Underpayment or nonpayment
- Other considerations:
  - Claims often arise during construction
  - Ongoing business relationships of the parties
- ADR inconsistencies in contracts

Defect Claims

- Design or construction? Or both?
  - Expert retention
  - Preservation of evidence
  - Differing legal standards
- Insurance coverage
  - Property (builders risk) vs. commercial general liability (CGL)
  - Other insurance
- Multiple parties
- Binding dispute forums

§ 20.3-1

Mediation

- First things first:
  - When?
    - Contractual pre-condition to litigation?
  - Where?
    - Venue requirement?
  - How?
    - Agency administered (AAA? ASP? JAMS?)
    - Bilateral agreement?
  - Whom?
    - Choosing the right mediator
      - Evaluative vs. procedural
      - Experience
  - Pre-mediation briefs

Mediation

- Identifying all the issues early
  - Just about money?
  - Ongoing business relationships?
  - Need to "do" anything post-settlement?
  - Avoid surprise issues at the end of mediation!
- Participation
  - Who are the key people necessary?
    - Decision-maker(s)
    - Key fact witnesses
    - Risk managers?
    - Key subcontractors?
    - Experts?

Mediation

- Where
  - Project location?
  - Law office?
  - Courthouse?
  - Important factors:
    - Location of key documents/information
    - Convenience of all parties/participants
    - Cost
    - Size (ability to provide private space for parties to deliberate)

Mediation

- Experts
  - Separate expert caucus?
  - Exchange of information
    - Notice of defect vs. expert privilege
- Insurance
  - Necessary party in defect disputes
- Managing indemnity and coverage issues

Mediation

- Mediation process
  - Joint sessions vs. caucus
  - Communicating with the mediator
  - Presumed confidentiality vs. presumed information exchange
  - Mediation confidentiality (ORS 36.220)

Mediation

- Getting to the finish line
  - Scope of agreement
    - What is being release? What is being reserved?
    - Has everything been discussed and agreed to?
      - Avoid surprise issues, such as ongoing warranty, demand for indemnity, limitations/expansion of release language, etc., requirement for future work/service, etc.
  - Necessary parties
  - Importance of getting it on paper

Settlement considerations

- Identifying specifically what is resolved and what is not. A payment settlement should not broaden to include latent defects discovered later on.
- The mediator's role: A scrivener or a "czar" (or neither)?
- Resolving issues of collateral (e.g., lien release)
- Scope, mutuality, and carve-outs to releases
- Consent of sureties

Unique issues in arbitration - 1

- Contract may specify ground rules for arbitration
- Joinder of parties
- Claims subject to ADR
- Rules
  - FAA
  - State law (ORS 36)
  - Contract
  - Service

Unique issues in arbitration - 2

- Discovery
  - Physical evidence and the “site visit”
  - Experts and reports
- Referees
- Venue
- Choice of law
- Selecting an arbitration service or arbitrator

Other Forms of ADR

- DRB/CRB
- Complex cases/referees
- CCB mediation (residential only)
- Baseball arbitration
- Brackets
- Minitrial

Thank You

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