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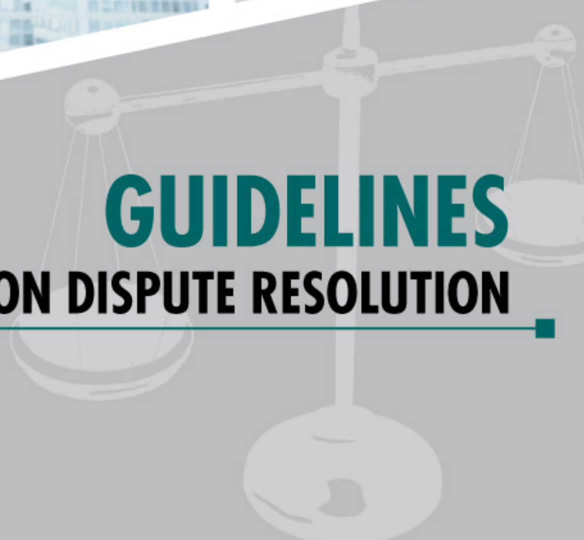

GUIDELINES
ON DISPUTE RESOLUTION

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Preface

The Construction Industry Council (CIC) is committed to seeking continuous improvement in all aspects of the construction industry in Hong Kong. To achieve this aim, the CIC forms Committees, Task Forces and other forums to review specific areas of work with the intention of producing Guidelines, Codes of Practice and Codes of Conduct to assist participants in the industry to strive for excellence.

The CIC appreciates that some improvements and practices can be implemented immediately whilst others may take more time to complete the adjustment. It is for this reason that three separate categories of communication have been adopted, the purpose of which is as follows:

Guidelines	These are intended to guide industry participants to adopt new standards, methodologies or practices. The CIC strongly recommends the adoption of these Guidelines by industry stakeholders where appropriate.
Codes of Practice	The CIC expects all industry participants to adopt the recommendations set out in such Codes as soon as practicable and to adhere to such standards or procedures therein at all times.
Codes of Conduct	The CIC encourages the upholding of professionalism and integrity within the industry through self discipline. The Codes of Conduct set out the relevant principles that all industry participants are expected to follow.

If you have attempted to follow this publication, we do urge you to share your feedback with us in order that we can further enhance them for the benefit of all concerned. On this basis the CIC Secretariat is in the process of developing a “feed-back” mechanism, whereby your views can be consolidated for such purposes. With our joint efforts, we believe our construction industry will develop further and will continue to prosper for years to come.

Terminology

In this document, unless the context otherwise requires:

1. "Adjudication."	The adjudicator will allow the parties to present their case and deal with that of the opponent whilst to a certain extent also using his own expertise to understand the issue and to resolve the dispute within a short time frame. It provides an alternative if a final result by way of expert determination is not preferred.
2. "Arbitration."	Domestic Arbitration under the Arbitration Ordinance (Cap. 341) is a legal process which results in an award being issued by an arbitrator. Arbitration awards are final and binding on the parties and can only be challenged in very exceptional circumstances.
3. "Dispute."	In the Guidelines, dispute means any disagreement which cannot be resolved through any dispute avoidance measures but which turns into an argument to be resolved through any of the dispute resolution methods.
4. "Dispute Resolution Advisor" (DRA)."	A DRA is a neutral person selected from a panel of construction professionals and paid for jointly by the employer and the contractor. A DRA works with them as well as the architect/engineer to encourage cooperation and joint problem solving and to encourage the resolution of disagreements at the site level and if not successful, at the senior level, to ensure that disagreements are resolved expeditiously and cost-effectively before they turn into formal disputes.
5. "Expert Determination."	An expert appointed by both parties in a dispute to quickly and cost-effectively form a view on the dispute. This decision is final and binding with little opportunity for being reviewed and challenged.
6. "Final Account."	A statement of account showing in detail the value of the work done in accordance with the contract, together with all further sums which the contractor considers to be due to him up to the date of the maintenance certificate.
7. "Independent Expert Certifier" (IEC)."	An IEC certifies a rate in lieu of the architect/engineer/quantity surveyor only if a dispute arises on the rate of variation works, facilitating the payment to the contractor for the relevant variation accordingly.
8. "Mediation."	A voluntary and non-binding dispute resolution process in which a neutral person (the mediator) helps the parties to reach a negotiated settlement.
9. "Short Form Arbitration."	A variation on arbitration with some of the procedures simplified. It is appropriate for smaller cases where there is little dispute on the facts and where the issues can be put to the arbitrator on a documents-only basis or with limited evidence.

1. Background

In April 2000, the Chief Executive of the Hong Kong Special Administrative Region appointed the Construction Industry Review Committee (CIRC) to comprehensively review the current state of the industry and to recommend improvement measures. One of the issues addressed in the review is dispute resolution.

The resolution of disputes can be expensive and time-consuming, sometimes causing significant negative impact on a company. Hence, it is preferable to address all claims and potential claims as early as possible to prevent them from developing into disputes. However, when there are circumstances where disputes are unavoidable they should firstly be handled in a constructive and collaborative way to reach early and effective settlements, while the traditional arbitration and litigation approaches should remain as last resort solutions.

a. What has been done?

The Provisional Construction Industry Coordination Board (PCICB) was formed in 2001 to implement the recommendations of the CIRC report before the formation of the Construction Industry Council (CIC). The PCICB started with the identification of various types of dispute resolution techniques and the promotion of proactive and collaborative approaches to the resolution of disputes relating to public projects.

b. What will be done?

With the successful implementation of alternative dispute resolution methods in public sector construction projects, the CIC will take on the promulgation and further exploration of alternative dispute resolution methods. The CIC aims to encourage the wider use of proactive and collaborative dispute resolution approaches in resolving claims and disputes in private sector construction projects.

Hence, the CIC has decided to prepare guidelines on dispute resolution (the Guidelines) with a view to ultimately enhancing the security of the payment of stakeholders in the construction industry.

c. Inside the Guidelines

The Guidelines aim to provide industry stakeholders, particularly private sector employers, with more information about the use of dispute avoidance measures and various dispute resolution methods for resolving different forms of disputes in their construction contracts.

The Guidelines recommend the use of dispute avoidance measures through the employment of dispute resolution advisors to resolve any disagreements whenever they arise.

If the disagreements cannot be resolved and ultimately turn into disputes, the Guidelines advocate the provision of different choices of dispute resolution methods in construction contracts to facilitate the resolution of disputes under different situations. The Guidelines also introduce a new concept of the adoption of an independent expert

certifier as one of the dispute resolution methods which will be further elaborated on later in the Guidelines.

Employers of construction projects interested in the recommended measures can consult the relevant professionals for assistance in the implementation of the measures in their construction contracts.

Depending on the feedback from the industry on the recommended measures in the Guidelines, the CIC may issue further guidelines relating to the recommended measures. The CIC will also work with industry stakeholders to improve the implementation of those measures to optimise their applications in construction projects for the betterment of the industry as a whole.

2. Introduction

Payment issues arise in many different circumstances but can be broadly categorised as those relating to interim payments, release of retention money and Final Account.

Hong Kong promotes a harmonious society and encourages the use of contracts within the construction sector. Yet, in the provision of dispute resolution mechanisms, most contracts provide for post-contract completion arbitration. This arrangement tends to create a hostile environment and prohibits parties from resolving their differences as soon as a dispute arises, resulting in the entrenchment of views and thereby damaging the spirit of partnership. This type of dispute resolution clause has long been abandoned in various other jurisdictions as they have been seen as unfair and detrimental to the cash flow of contractors, with a tendency to aggravate the relationship of the partners on the construction site. This arrangement is unsatisfactory for reasons elaborated on further below.

The Housing Authority has adopted the use of dispute resolution advisors (DRA) in their foundation and building contracts as a dispute avoidance measure. Some government projects have also introduced the use of DRA as a pilot scheme. These DRA contracts are usually accompanied by the right and obligation of the parties to immediately resolve their dispute using Short Form Arbitration, adjudication or mediation. The Housing Authority contracts stipulate Short Form Arbitration (unless the contracting parties agree to adopt full arbitration or other alternative dispute resolution methods) whilst other government projects give the right to request mediation or adjudication before the completion of the works. The last resort for resolving disputes in these contracts is still arbitration after the completion of the works.

The industry has discussed speedy dispute resolution in the past. It is time to change the prevailing mindset so that the industry will resort to immediate dispute resolution as and when disputes arise.

The parties involved in construction contracts are the employer, main contractor, domestic subcontractors, nominated subcontractors, suppliers and workers.

The Guidelines are intended to set out what is viewed by the industry as good practice in resolving disputes where it cannot be avoided by other measures such as the DRA. This is beneficial for all the parties involved and more importantly, will encourage the healthy and professional development of the construction industry, thereby improving and enhancing the public image of the construction industry as a whole.

3. Usual Problems and Consequences

a. Interim payment disputes

The types of disputes that commonly arise during the interim payment stages are numerous and can take several different forms. They are as follows:

1. Whether or not an instruction amounts to a variation;
2. The proper valuation of variation;
3. The amount of work done;
4. The quality of the works and whether the works should have been accepted as complete;
5. Whether an event amounts to an event that gives rise to the extension of time and if so the extent of the extension of time.

b. Final account and release of retention

What has remained unresolved at the interim payment stages naturally will have to be dealt with at the Final Account stage.

1. Questions of liquidated damages become particularly pertinent;
2. The quality of works is often raised at this stage which may entitle the employer to withhold further payments so as to compensate for the rectification cost for the defective works;
3. The duration taken to finalise the Final Account is unusually long;
4. Furthermore, in some construction contracts, the release of the second moiety of retention money is delayed as it turns on whether the works were defective because of the specifications or workmanship and who is therefore responsible for the rectification costs.

c. Payment to suppliers

At various stages of the works, either the main contractor or the employer may have purchased equipment or materials directly from suppliers. The suppliers would normally have a purchase contract with either post-contract completion arbitration or alternatively no dispute resolution mechanism at all. Disputes usually relate to whether or not certain equipment complies with the specifications and whether any changes that were ordered to be made is a variation, thereby entitling the supplier to additional payment beyond what it has contracted for. Goods have often been delivered before payment is fully made. Therefore, suppliers sometimes cannot recover the payments in time.

d. Consultants

Consultants include engineers, architects and quantity surveyors. In construction contracts, the consultants play an important role in ensuring that the works are constructed in accordance with its design and certifying for payment at the interim stages as well as to finalise the Final Account. Each of the disputes described above would include some sort of opinion or decision from the consultant either in the form of a certificate or in the form of a Decision under the contract. Consultants are sometimes placed in an invidious position as some employers may influence the views of the consultant or even direct that the certificates be issued in a separate way. The impartiality of the consultants is therefore sometimes challenged. Most of these challenges are probably unjustifiable but nonetheless, justice must not only be done but must be seen to be done. The proposals contained in these Guidelines will help to enhance and preserve the impartiality of the consultant whilst ensuring that the spirit of partnership remains intact and disputes resolved. It will also ultimately enable professionals to act as third party neutrals in unrelated contracts.

e. Abandonment of works

This has happened in Hong Kong as a result of non-payment from the main contractor to the subcontractor and the subcontractor to the sub-subcontractors and ultimately the workers. Whilst the direct victims are those who did not get paid, the employer nonetheless has to suffer the ultimate consequence of an abandoned project thereby resulting in additional time to completion as well as extra costs in engaging a replacement contractor to complete the outstanding works. Hence, whilst an employer may be very fair in ensuring payment to the main contractor, it should also ensure that there are proper mechanisms available downstream so that its projects would not ultimately be adversely impacted by the abandonment of works as a result of non-payment or delayed payment at the lower tiers.

f. Spirit of partnership destroyed

Employers have generally actively promoted partnerships in construction contracts. However, the lack of proper mechanisms to ensure the security of payment all the way downstream may create an animosity amongst the personnel of the subcontractors and main contractor, thereby indirectly affecting the spirit of partnership which the employer has worked so hard to bring about.

g. Need for subsequent rectification of works

While disputes relating to quality remain unresolved, the employer will not receive work of a satisfactory quality. Mechanisms must be identified to swiftly address questions of quality so that these quality issues are resolved during the works. The works should be as free from defects as possible at completion. This is not only beneficial to the construction industry but also the public.

4. Important Principles

a. Resolving disputes as they arise

It is always preferable to avoid disagreements which can eventually turn into disputes. There are dispute avoidance measures that can be adopted to resolve any disagreements as and when they arise. However, if the disagreements fail to be resolved and ultimately become disputes, employers, consultants and contractors should be encouraged to adopt a proactive approach to resolving claims and disputes as they arise, with sufficient high-level support and involvement to bring about a speedy resolution.

It is important to manage a dispute actively and positively to encourage early and effective settlement. Different procedures such as negotiation, alternative dispute resolution (e.g. mediation, independent expert certifier, expert determination and adjudication), arbitration and litigation may be resorted to, having regard to the circumstances of a particular dispute.

Such proactive and collaborative ways of dispute resolution should be encouraged through the adoption in contracts of provisions which facilitate the resolution of disputes by means of alternative dispute resolution techniques in addition to formal and binding adjudicative means which will remain a necessary, but last resort, solution.

b. Justice delayed is justice denied

The courts have long realised a fundamental principle – that justice delayed is justice denied. In light of the current standard forms of construction contracts, the delay would constitute the whole of the construction period (which usually lasts for years) and then the duration of the dispute resolution process itself, which may be another lengthy period.

In some other jurisdictions where arbitration has become a costly and lengthy process, a more rough and ready process such as adjudication has been introduced. Adjudication tends to provide more of a rough justice than the fine and detailed determination that one may obtain in arbitration. Yet, being a shorter and simpler process it has the benefit of ensuring cash flow and avoiding delayed justice.

Other forms of dispute resolution mechanisms such as mediation have also been adopted and indeed its use is being encouraged in Hong Kong. It has the benefit of creating a win-win result that the parties themselves devise and are content with. The limitation often found in mediation involving public sectors is the inability or unwillingness of the parties to make commercial decisions without some assessment of the strengths and weaknesses of their respective case. As a result, the process itself is not always short.

c. Cash flow is the lifeblood of a contractor

Another well recognised principle in the construction sector is that cash flow is the lifeblood of a contractor. Not only that; it is also the livelihood of the workers who are at the end of what one may call the "food chain." Yet it is the workers themselves who are at the front lines exerting sweat, toil and labour as well as their technical skills in constructing the works. The inability to receive prompt payment is something that the construction industry and the society of Hong Kong must address. As explained in the paper "Security of Payment for Hong Kong Construction Industry Workable Alternatives and Suggestions"[1], cash flow must be generated from the top of the food chain, namely from the employer to the main contractor, subcontractors and ultimately the workers. Any problems at the up-stream of this cash flow will ultimately impact others down the chain. Importantly, these problems will manifest themselves in a way that will severely damage the reputation of Hong Kong's construction industry. It is high time that steps were taken to improve the public image of the construction industry as a whole.

In the Guidelines, the focus is on ways to ensure prompt and timely payments in the context of security of payments from the employer all the way down to the labour-only subcontractors who are then responsible for payment to the workers. The protection afforded to workers for the receipt of wages is generally provided in the Employment Ordinance (Cap 57). As with all legislation, there may be room for improvement in light of the changing society; but that is a matter to be considered elsewhere. Nonetheless, this must not be overlooked when considering security of payment for the reasons set out above.

[1] by Teresa Cheng, Gary Soo, Mohan Kumaraswamy, Wu Jin

5. Various Forms of Dispute Avoidance and Dispute Resolution Mechanisms

a. Dispute avoidance measures

Whilst the focus of the Guidelines is not on dispute avoidance measures, they would be incomplete if they fail to mention two commonly adopted measures to avoid disputes. The first consists of partnering, often accompanied with a charter to be signed by all parties to the construction contracts (the CIC is currently studying the practicality of partnering in Hong Kong; the result will be announced separately). The other is the use of a DRA.

A DRA is a neutral person selected from a panel of construction professionals and paid for jointly by the employer and the contractor to work with the parties from the commencement of the contract to completion. Upon appointment, the DRA holds familiarisation meetings with the aim of developing the relationships between the personnel on site as well as building their support for the system. Regular site visits are used to facilitate the settlement of any disagreements that arise. The DRA employs proactive techniques to encourage cooperation and joint problem solving, encouraging the resolution of disagreements at site level and, if that is not successful, at the senior level in order to ensure that disagreements are resolved expeditiously and cost-effectively before they turn into formal disputes.

The Architectural Services Department was the first to incorporate the use of DRA in their contracts. Since then, the Housing Authority has also adopted the use of DRA. The Housing Authority's DRA addresses the differences that may arise from the main contractor as well as the nominated subcontractors. The DRA is to act as a go-between diffusing the differences between the parties before it crystallises into a dispute. If a dispute does arise, immediate Short Form Arbitration is available.

The various departments in the Development Bureau have set up a pilot scheme whereby DRA is used. With the DRA system, some projects give the right to the main contractor to request mediation or adjudication before the completion of the works. The post-completion arbitration clause is still retained for all of these contracts.

There are some views which suggest that the DRA should be more involved beyond just the main contractor level because any differences or problems are usually first identified at the lower tier subcontractor levels. Subject to further deliberations and discussions, the use of the DRA at these subcontractor levels may be useful.

The engagement of the DRA at the moment ends at the completion of the works or on the expiry of the maintenance period. In the Guidelines, it is proposed that the engagement of the DRA should be extended to the Final Account stage as he/she (collectively "he" herein and after) is best placed to try and bring the parties together in the outstanding issues that remain unresolved during the currency of the works. This may help to avoid any disputes altogether or at least reduce the number of disputes that may have to go to arbitration.

The benefit of the DRA is that he is truly impartial, being paid jointly by both the employer and the contractor and experienced in various techniques in avoiding and resolving disputes. The pool of the DRA may need to be increased to complement the policy if and when it is made that all projects will adopt the use of DRA.

It is only if these dispute avoidance measures are unsuccessful that the dispute resolution mechanisms would need to be addressed. Nonetheless, it is very important that the dispute resolution mechanisms be available and laid down in the contract so that the parties could immediately use them to resolve the dispute if and when avoidance measures fail.

b. Dispute resolution mechanism

The dispute resolution mechanism involves a spectrum of techniques which the parties can adopt to resolve their dispute. If the parties are unable to reach any settlement or agreement by way of negotiation or through the DRA, a third party neutral can be appointed to resolve the dispute.

The spectrum ranges from the least formal and most flexible form of mediation to the most formal with established procedures of arbitration. The more common forms that have been seen and used in construction disputes are: mediation, early expert evaluation, mini trial, adjudication, expert determination and arbitration. Whilst specific forms have been given names which are generally understood in the dispute resolution industry, it is always the process and rules for that particular form of dispute resolution that matters.[2]

There is no panacea for all. A particular dispute is only best resolved by a particular form of dispute resolution mechanism. Flexibility in devising the form of dispute resolution must be maintained in order to find the best method for the particular dispute. As a result, as will be seen below, one of the proposals involves mechanisms that are not generally well known but may nonetheless be considered suitable in light of the specific features and circumstances in Hong Kong.

It is beyond the scope of the Guidelines to provide the full details of each of these processes. In the Guidelines, the following five forms of dispute resolution mechanisms recommended for use are summarised in the table and flowchart below and examples will be used to illustrate how each would be suited to the particular type of dispute.

1. Arbitration
2. Expert Determination
3. Adjudication
4. Independent Expert Certifier (IEC)[3]
5. Mediation.

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[2] For instance, in Hong Kong, conciliation and mediation are treated as synonymous. In Taiwan, conciliation has been used to describe a form of a hybrid process compromising mediation and adjudication. There is also a hybrid process that is used in other civil law jurisdictions, Mainland China and Taiwan in particular, which has been described as arb-med.

[3] Independent Expert Certifier is a new concept introduced in the Guidelines which will be elaborated on in the following table and flowchart.

Various Forms of Dispute Avoidance and Dispute Resolution Mechanisms

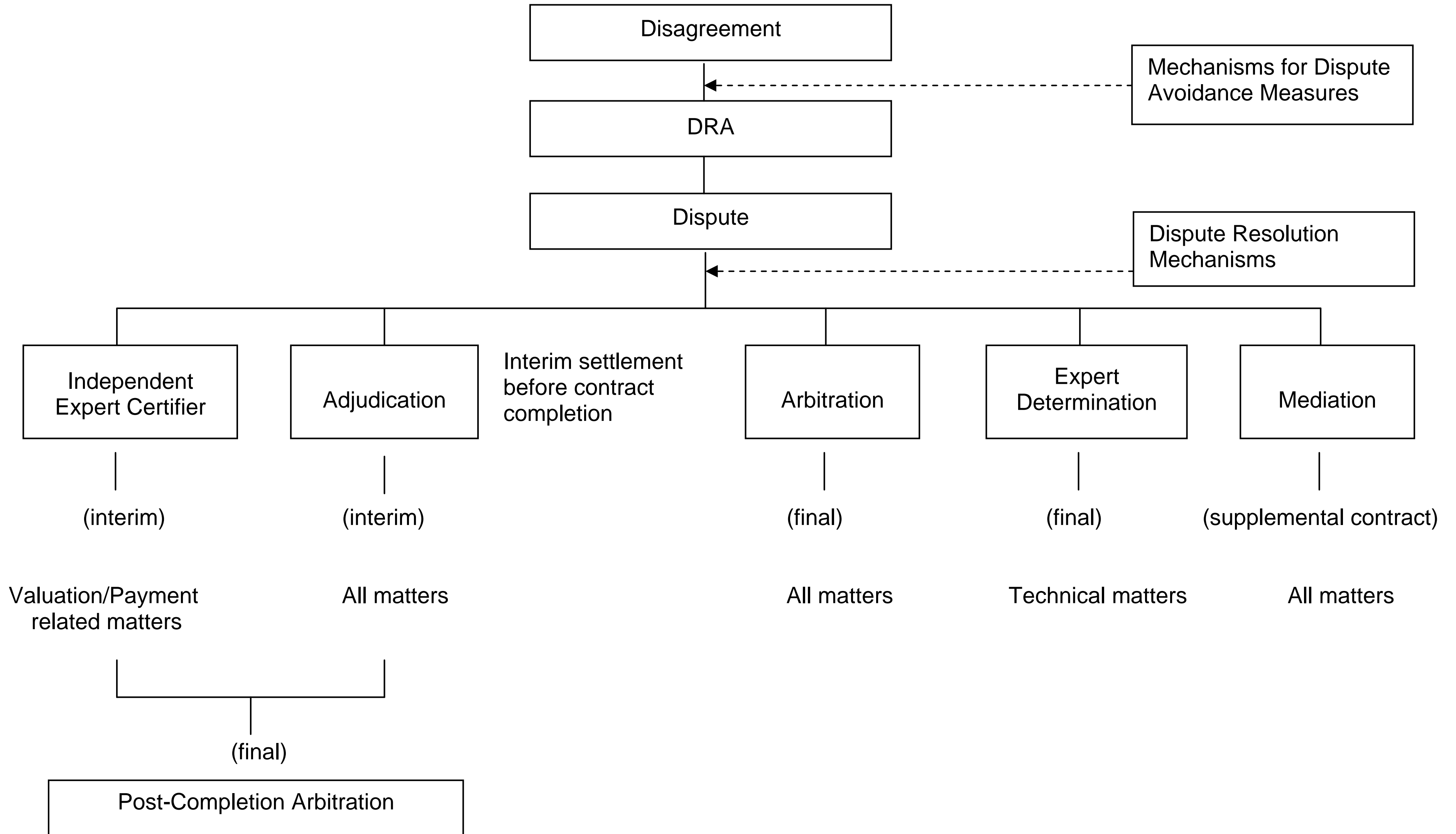
Arbitration	Expert Determination	Adjudication	Independent Expert Certifier (IEC)	Mediation
a) An arbitrator is appointed	a) Third party neutral is an expert in the relevant issue	a) An adjudicator is appointed	a) The IEC replaces the Architect, the Engineer or the Project Quantity Surveyor in certifying a rate if a dispute on the rate arises	a) A mediator is appointed
b) Rules of natural justice to be observed				b) The rules of natural justice do not apply
c) Parties have reasonable opportunity to present their case	b) Parties have right to present the case	b) Parties have right to present the case	b) Parties have right to present the case	c) The mediator can see a party in private
	c) Limited time for the process	c) Limited time for the process	c) Limited time for the certificate to be issued	d) Parties may stop the process by terminating the mediation
		d) Set procedures for the submission of documents and evidence so as to meet the time limit for the process		
	d) Expert entitled to use his own expertise to decide the issue		d) Certificate is not final or binding in the interim	
d) Construction arbitration conducted after the completion of the contracts usually involves an oral hearing		e) Hearing not always necessary		

Various Forms of Dispute Avoidance and Dispute Resolution Mechanisms

Arbitration	Expert Determination	Adjudication	Independent Expert Certifier (IEC)	Mediation
e) A final and binding award is produced	e) Expert renders a final determination	f) Adjudicator give a decision		e) No decision or opinion is rendered by the mediator
f) Right to challenge is limited to points of law	f) Very limited right to challenge	g) The decision is not final		
g) Award is enforceable in court as if it is a court judgment	g) Determination enforceable as a matter of contractual obligation	h) Decision enforceable as a matter of contractual obligation	e) Certificate is enforceable as a matter of contractual obligation	f) If successful it will result in a settlement agreement which is a contract supplemental to the construction contract
		i) Decision can be challenged and revised by subsequent arbitration	f) Certificate can be reviewed and revised by subsequent arbitration	g) If the mediation is unsuccessful another process will have to be used
h) Types of arbitration that can be adopted if it is to be commenced before completion of works include : • documents-only arbitration • look and sniff arbitration • Short Form Arbitration conducted under the Hong Kong International Arbitration Centre Short Form Arbitration Rules				

Various Forms of Dispute Avoidance and Dispute Resolution Mechanisms

Dispute Resolution Flowchart for Public Works



Various Forms of Dispute Avoidance and Dispute Resolution Mechanisms

It can be seen that the only process which will not definitively end the dispute, albeit temporarily, is mediation. Mediation presents many benefits, but if a definitive result is needed within a short time frame, it may not satisfy that requirement.

In order to ensure the dispute is resolved within a short time frame, a sequential process is not to be preferred. Mediation and negotiation can be conducted at the same time as any one of the other processes which would produce a definitive result. Consequently, different types of third party neutrals must be involved under different situations as follows:

An Independent Expert Certifier or Adjudicator will be involved if an interim decision is contemplated which can subsequently be reviewed by the post-completion arbitration;

Arbitrator or Expert for Determination will be involved if a final decision on the dispute is expected;

Mediator will be involved if a definitive decision is not required but the parties in dispute prefer to have the third party neutral to help out in the negotiation process.

It has to be stressed that the impartial role of architects/engineers/quantity surveyors in construction contracts remains unchanged after implementing the recommended dispute resolution mechanisms. A third party neutral as mentioned above will only be involved when there is a dispute which cannot be resolved between the employer and the contractor with the concerted effort of the architect/engineer/quantity surveyor.

None of these dispute resolution mechanisms will work unless there is consent from both parties. A right to request will not suffice. The process can only serve its purpose if it can be invoked immediately when the dispute arises. Only then can cash flow and a good working relationship be maintained, and the construction industry be allowed to develop in a healthy and professional manner.

6. Immediate Dispute Resolution

The practices in Hong Kong in relation to dispute resolution mechanisms in some contracts, though not all, have not been kept up-to-date. This is not conducive to the healthy development of a professional and responsible construction industry as a whole.

a. Arguments for and against post-contract completion arbitration only

The main arguments in favour of resolving the dispute only after the works have been completed are:

1. The attention and focus of the employer, consultants and contractors would not be diverted from completing the works in order to prepare evidence and submissions for the dispute resolution mechanisms;

2. Some issues such as the effect of a delaying event on the need or extent of the extension of time to be allotted cannot be known until the works are completed;

3. Unscrupulous and claim-conscious contractors may invoke a lot of mechanisms against the employer;

The first argument may be superficially attractive but fundamentally flawed. The reasons are as follows:

1. The continued proliferation of arguments through correspondence: Where a contractor perceives a right to make a claim and that claim is rejected, the dispute arises. Parties would then embark on exchanges of letters arguing their case. This will continue until the completion of works. The effort that should be devoted to the works is thereby diverted;

2. Continued preservation of evidence: Where a dispute remains unresolved and would only be decided after the completion of the works, both sides would continue to preserve the evidence either by keeping samples or alternatively by creating contemporaneous records so that their right to claim is not lost or deemed to have been waived;

3. Loss of memory: Apart from documentary or physical evidence, witnesses are often required. Memory does fail. Site staff who have the most direct evidence to offer in relation to what actually happened onsite often leave the job and either cannot be found or become unwilling to give evidence if they no longer work with that employer or contractor. As a result, the best evidence is somehow lost whilst secondary evidence may be overwhelmingly created so as to preserve the positions of both parties;

4. Views get entrenched: As is often the case with human nature, if a dispute remains unresolved, the views of the parties become entrenched and the impartiality of the consultants impugned. Site personnel may fail to maintain objectivity on other issues and lose appreciation of the other side’s viewpoint;

5. Partnership dissolved: As views become entrenched on one issue, relationships onsite turn sour, impacting other parts of the work which would not have been a problem had objectivity and equity been preserved. The trust between the parties will collapse and at the end of the day it is the project that ultimately suffers;

6. Imbalance of negotiating power: Injustice will result if the contractor lacks the right to an immediate resolution of the dispute, and the negotiating power of a contractor will be greatly reduced after the works are completed in light of the lack of legal protection such as liens in the United States;

In theory, people should be able to separate issues from personalities, but this is not always possible. As a result, it is exactly the preclusion of resolving the dispute immediately as and when it arises that will divert the focus and effort of the parties on the construction project away from the common goal, or what should have been the common goal, of building and completing the works on time and within budget. The first primary ground of preserving post-completion dispute resolution clauses is therefore, on a balance, unsustainable;

As to the second ground that is sometimes raised, the answer lies in some sort of interim decision that will put the issue at an end during the currency of the works so that the parties' attention could be reverted back to the construction works themselves rather than the preservation of evidence and position. If indeed a particular issue could not be finally resolved until the completion of the works, the interim decision, whatever form it takes, can then be reviewed and revised using a post-completion arbitration process;

The more realistic problem is the concern that unscrupulous and claim-conscious contractors and subcontractors may indiscriminately raise disputes and trigger the mechanism thereby creating a lot of unnecessary work for the other party in the construction contract. One has to distinguish between an unscrupulous claim-conscious contractor with a prudent rights-aware contractor. The need to prevent abuse by the former must be balanced against the need to protect the latter. One way may be to provide that costs incurred in these immediate dispute resolution mechanisms would have to be borne by each party themselves irrespective of the result save and except with the discretion of third party neutrals in special circumstances. For instance, claims which never ought to have been raised in the first place either because of complete lack of contractual basis or factual support may result in costs awarded against the party who raises the groundless claim;

The arrangement that each party bears their own costs have the advantage of encouraging the parties not to indulge in extensive and peripheral arguments but to try and find a way to solve the dispute speedily and cost-efficiently. Most if not all the mechanisms proposed in the Guidelines can be dealt with by the personnel on site with minimum help from head office staff. There may be situations whereby lawyers or contract advisors have to be involved but that should be rare if issues are dealt with one by one as opposed to the individual disputes being left to be dealt with in one go in a full blown arbitration after the completion of the works;

It is a matter of striking the right balance in light of the pros and cons of the matters discussed above. It is proposed that an immediate dispute resolution mechanism, with the right of the parties to review the interim decisions after completion of the works, would be the right balance to strike for the construction industry in Hong Kong;

Justice delayed is justice denied. Cash flow is the lifeblood of a contractor. Rough justice is better than no justice;

A post-completion dispute resolution mechanism conflicts with these principles and unnecessarily creates animosity between the partners in the project. It is inconsistent with the policy of developing a harmonious society in Hong Kong;

Post-completion arbitration should nonetheless be preserved to allow any interim decisions by other forms of dispute resolution mechanisms to be reopened so that the rough justice delivered can be revised to obtain a more detailed and final result.

b. Right to request for immediate dispute resolution mechanisms

It has been argued that employers currently have access to immediate dispute resolution mechanisms in that contracts provide avenues through which parties may request mediation or adjudication. Any party may have a right to request anything and it is otiose to stipulate that in a contract unless that right becomes an enforceable right such that the other side cannot refuse when the request is made. A "right to request" is not in fact a right as such, since it does not procure the desired result. There is no legislation that compels a party to agree to the other side's request unless expressly provided for in the contract. Dispute resolution is a consensual process based entirely on party autonomy. Even arbitrators cannot compel third parties to join in the proceedings without their consent and the consent of those already in the arbitration process.

In conclusion, it is misleading to argue that a right to request provides disputing parties with some sort of immediate dispute resolution mechanism. Immediate dispute resolution mechanisms must provide parties with a contractual right and obligation to participate in the dispute resolution process.

7. Examples of Use of Proposed Methods for Interim Payment Disputes

Disputes that arise during the interim payment stage must be resolved immediately in order to ensure that cash flow is maintained so that workers get paid and no subcontractors are held up by the inability to receive payment after work has been completed. This will ensure that the Employer receives the benefit it has contracted for.

Differences between parties are usually dealt with first by the Project Architect, Engineer or Project Quantity Surveyor. They act not only as an agent for the employer but also certifiers. There exists a general perception, albeit at times incorrect, that they lack impartiality and may be influenced by the employer. However, justice must not only be done but must be seen to be done. A consultant who is the agent of the employer and usually the designer of the project may be seen to lose objectivity when it comes to the certifying function that is invested in him, especially if it relates to design or specifications.

If the receiving party of the interim payment has to contend that the certifier's decision was wrong or influenced by the employer, unnecessary tensions will arise between the consultant and the contractor. The intervention of a third party neutral in the dissolution of such tension is beneficial to all. The consultants would be able to continue supervising the works and the third party neutral would be involved in resolving the dispute, either finally or as an interim decision binding on the parties up to the end of the contract.

By way of example, the following illustrate how a third party neutral can be of assistance.

a. Whether or not an instruction amounts to a variation

This is typically a contractual question that can be very quickly decided on paper. Oral evidence, if any, would be limited as instructions would usually be in written form or oral instructions could easily have been reduced into writing by the contractor. The question turns on the construction of the contract and the scope of works. As a result, there is no reason why this could not be resolved immediately when there is a dispute as to whether an instruction amounts to a variation entitling the contractor to additional payment.

This issue can be resolved by way of a third party neutral who is in a position to make a decision.

If it is thought that the matter ought to be dealt with by way of a final decision, Short Form Arbitration is the best method to use.

If for whatever reason the parties would like to revisit the question in due course, they can always adopt adjudication and engage an adjudicator who will make an interim decision that is binding on the parties during the currency of the works but may then be overruled by subsequent arbitration if either party is dissatisfied with the adjudicator's decision.

b. Valuation of variation

The most common form that is relevant to this type of dispute is the fixing of the rate. Arguments can arise as to how the principle of valuation of variation should be applied. So long as this argument is ongoing, contractors may not get paid at all or if they get paid, it is usually substantially less than what they contend is correct.

Examples of Use of Proposed Methods for Interim Payment Disputes

As the fixing of rates is very much a matter that is best resolved by experts in the industry, the following methods could be used:

1. An Independent Expert Certifier could be engaged to certify a rate in lieu of any certification by the Engineer, Architect or the Quantity Surveyor if a dispute arises regarding the rate. This fixing of rates by the IEC would then result in payment to the contractor for the relevant variation. The decision making period can be fixed at 14 days and both parties would have the prior opportunity to present their arguments to the IEC. The presentation of the argument will be no different from that to be presented to the contract certifier and there would be no need to engage outside parties, greatly reducing costs. The impartiality and independence of the IEC in making that decision whilst observing the rules of natural justice can be encapsulated in the rules for this process. The important feature is to limit the time by which the IEC can take to reach a decision;

2. Mediation within a set time frame can be used. But if that does not result in a settlement and hence a supplementary agreement, the issue remains unresolved;

3. Adjudication is another possible method by which the rates can be fixed.

c. Defective Works/acceptance of Works

Payment problems at the interim payment stages can occur when disputes arise regarding defective works as a result of poor workmanship or a lack of accordance with the specifications of the contract. At the moment, these issues cannot be resolved until the completion of the works, by which time much of the alleged defective works would usually have been covered up and either unnecessarily replaced or alternatively left in place subject to a payment deduction.

Samples would occasionally have been retained in the form of, for instance, borelogs or jars of excavated or fill material. The process in which the arbitrator examines these samples in order to decide whether they were in accordance with the specifications and hence whether payment ought to be made or deducted years after the completion of works is highly unsatisfactory and sometimes artificial. Of even greater concern are the safety implications of disputed works being subsequently left in place despite their truly defective nature.

It is therefore of utmost importance from all points of view that these disputes be resolved as and when the defective work is identified. As soon as the consultant realises or contends that the works are not in accordance with specifications, the parties should, through the DRA or themselves, first discuss the issues. If these cannot be resolved, a third party neutral with expertise in the particular area of works can be engaged to resolve the dispute.

1. A final result produced through expert determination is most apt for this type of dispute. The expert would be engaged by reason of his expertise in this area of work to decide whether or not the works were in accordance with the specifications so that first, if the works were in accordance with the specifications, payment should no longer be withheld or deducted; secondly, if the specifications were complied with but the continuation of works is nonetheless deemed unsafe, the specifications may be modified immediately so that the works completed at the end of the day are acceptable not only to the employer but also the contractor and the general public. Naturally, if the issue arose as a result of poor workmanship, rectification works may be carried out

immediately. The engagement of an expert to carry out the expert determination process is often used in technical disputes. This provides the benefit of relying on the expertise of that expert without any need to explain the details of the technical requirements. He is given the power to decide on the dispute based on his own expertise after listening to the views of both parties regarding the issue.

2. Adjudication provides an alternative if a final result by way of expert determination is not appropriate or preferred. The adjudicator will allow the parties to present their case and deal with that of the opponent whilst to a certain extent also using his own expertise to understand the issue and to resolve the dispute within a short time frame.

The outcome of the expert determination process is usually, as a matter of law, treated as final and cannot be overturned by the court save where there is fraud or bad faith on the part of the expert. However, if there is any reservation about that, adjudication may be used instead. This provides the parties with a means of recourse by post-completion arbitration should they be unsatisfied with the adjudicator's decision.

d. Quantity of work done

During the interim payment stages, there is often a difference between the parties in terms of the quantity of work for which payment is applied and the quantity of work for which payment is certified.

As this is a typical quantity surveying dispute, the following processes as already described above would be suitable:

1. Expert determination
2. Independent expert certifier
3. Adjudication.

e. Delay/extension of time

The issues that commonly arise in regards to questions of delay generally revolve around whether the particular event relied upon by the contractor falls within the extension of time clause, or whether that event has caused critical delay and if so, to what extent.

The first issue is one of a question of mixed law and fact. During the currency of the works, there is usually very little difference on the facts. Hence the question can then be answered by applying the agreed facts to the contract provisions. The method used can be one of arbitration. An arbitrator can probably deal with that by way of a documents-only arbitration or, if necessary, with the help of a very short hearing to receive evidence on any disputed facts or difficult legal arguments. Whether the event actually causes delay or not is another matter.

As to the second issue, that of critical delay and its extent, it is often said that it cannot be finally determined until the conclusion of the works. This can be addressed through the adoption of adjudication which provides a binding decision in the interim. The disputes between the parties can then be resolved immediately albeit on an interim basis. Arbitration is probably not the best method to be used given the nature of the dispute.

8. Final Account

The industry is concerned with the length of time required in most contracts for Final Accounts to be concluded. The issues relating to the Final Account are really the unresolved issues that arose during the interim payment stages. As a result, if the above proposals to deal with disputes during the interim stages are adopted, the outstanding issues at the Final Account stage would in future be greatly reduced.

At present, by reason of unreasonable post-completion arbitration clauses, issues at the Final Account stage cannot be resolved earlier during the course of the works. At the Final Account stage, payment for which there is no dispute may therefore be withheld as a result of separate disputed issues. This causes grave injustice and grievance to the contractors.

Swift dispute resolution mechanisms must therefore be adopted to address the current situation. Most standard form contracts provide avenues for the contractor to submit a Final Account in draft form within a specified period after the completion of works. There is, however, no stipulation as to when the employer must provide a response. As a result, negotiations between the parties on differences in the Final Account may take years to address and therefore significantly and adversely impact the timeliness of the payment that should be made.

To address issues with the Final Account pending the proper amendments that are to be made to the standard form contracts, the following is proposed:

1. Extension of the role of the DRA: The DRA is at the moment involved with a construction contract up to the completion of the works or upon the expiry of the maintenance period. It is clearly advisable to extend the involvement of the DRA to the Final Account stage for ongoing contracts. The DRA is familiar with the issues during the construction stage and his involvement will help the parties come to an agreement more quickly regarding longstanding disputed items;

2. Adjudication: Arbitration is of course available since by then the works will have been completed. However, as a matter of fact, arbitration involving Final Account issues cannot be resolved quickly. Hence it is necessary to find a more immediate and speedy form of dispute resolution to provide parties with an interim decision so that only those decisions that either party wishes to challenge would be taken further in a subsequent arbitration;

3. Arbitration: The arbitration process can still be a safety net for parties wishing to challenge the interim decision of the adjudicator.

9. Conclusion

In summary, it is recommended that dispute resolution mechanisms are adopted in the construction industry and, for those contracts adopting this approach, should be:

1. Available immediately as and when the dispute arises;

2. Contractually obliged as opposed to optional such that both parties would be obliged to participate when the process is invoked;

3. The process itself must be short in duration and inexpensive;

4. Sequential procedures are not to be preferred as that tends to proliferate the disputes between the parties as opposed to quickly resolving them;

5. There should be a right to review and revise any interim decisions by way of arbitration after the completion of the works;

6. The Guidelines have not looked at all forms of dispute resolution mechanisms that may be available such as mini trials, conciliation in the form of adjudication cum mediation or arb-med. Discussions on these other process can be found in various learned articles and textbooks and it is not appropriate to deal with all these other processes in the Guidelines. Suffice it to note that the emphasis is on immediate dispute resolution mechanisms.

10. Way Forward

In the long term:

1. The current dispute resolution clauses in standard form contracts should be reviewed and amended to ensure that immediate dispute resolution processes are available;

2. A DRA should be adopted for all new contracts so as to resolve any disagreements immediately before they evolve into disputes, and consideration should be given on how to expand the use of a DRA.

In the meantime, parties to construction contracts should have the right to immediately resolve their disputes by way of one of the following dispute resolution mechanisms[4]:

1. Mediation
2. Adjudication
3. Independent expert certifier
4. Expert determination
5. Arbitration.

Where a DRA has been used in existing government contracts, the engagement of the DRA should be extended into the Final Account stage.

It is recommended that successful experiences with the use of a DRA in government contracts be shared with private sector project developers with a view to encouraging the use of the same in private development projects.

The post-completion arbitration clause should be retained so as to provide the parties with recourse against the interim decisions of the adjudicator or IEC.

The parties should be free to choose any one of the five forms of dispute resolution mechanisms to resolve their dispute as and when it arises. This provides parties with flexibility in choosing whichever form is most suited to their dispute, and indeed to decide whether to use a final and binding method such as expert determination and arbitration or to use a process which provides an interim decision while reserving the right to refute the same by way of arbitration after the completion of the works. This is no panacea for all and the careful selection of the appropriate method for a particular dispute is crucial.

These dispute resolution mechanisms should be practised primarily by those directly involved in the construction industry. It is advisable to establish a pool of third party neutrals on the premises. This may necessitate the involvement of the learned societies and the Hong Kong International Arbitration Centre.

If this arrangement is adopted and successfully practised in Hong Kong, it will enhance the reputation of Hong Kong as a construction dispute resolution centre. The third party neutrals who have had experience in resolving construction disputes in Hong Kong may offer their services to construction contracts in other jurisdiction such as Mainland China.

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[4] Save for expert determination and arbitration, each of the above processes can, by agreement, be subject to be reviewed and re-opened in a subsequent arbitration so as to ensure that any interim decision that a party is not content with can be challenged.

Way Forward

In the long run, it will not only enhance Hong Kong's reputation, but enhance the skills of local construction professionals as well, enabling them to provide value-added services to the construction industry not only in Hong Kong, but throughout Asia.