Society of Construction Arbitrators
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Do pre-arbitral procedures work, are they necessary or are they simply killing construction arbitration as we used to know it?

Notes of the talk given on 6th May 2007

The Hong Kong Perspective

Introduction

To examine, briefly against the above questions, the procedures of Engineer's / Architect's Decision, Mediation, Adjudication, Dispute Resolution Adviser system and Dispute Review Board / Group, from a Hong Kong context

Engineer's/Architect's Decision is normally a condition precedent to commencing arbitration. This arrangement appears in Government contracts and many other civil engineering and building forms. The exception is the new HKIA HKIS Building Form of Contract dated April 2005.

Do they work? No, nearly always confirm the previous decision at a lower level, therefore disputes pass on to the next level of resolution.

Are they necessary? Yes, helpful to crystallize and define the scope of the dispute – though the procedure often leads to jurisdictional challenges at the arbitration stage.

Mediation is often included in a multi-tiered dispute resolution mechanism. Government, Airport Authority, KCRC and other forms, including the HKIA HKIS Building Form of Contract dated April 2005, contain mediation provisions.

An attempt at mediation is normally though not always a condition precedent, to proceeding to arbitration. "Attempt" will usually be defined in some way, often by a time limit or possibly two such limits. The first, time limit being a failure to respond to a mediation request and the second being a failure to resolve the dispute within a specified time limit. A failure in either case is deemed a failure of the mediation process and the dispute can pass on to arbitration.

Does it work? Yes, mediation enjoys a very high success rate in Hong Kong, at around 80% being the same as the internationally cited norm. The only hard evidence, as to statistics is from the ACP projects, where there was a 79% success rate at the mediation stage. Less than 10% of disputes on ACP proceeded to formal arbitration.

Is it necessary? Yes, mediation in the construction industry is well known and is long established (the first Hong Kong mediation training course was held before CEDR started its training) and mediation is present

in all standard forms of building and civil engineering contacts and sub-contracts. Mediation is less popular in private sector ad hoc contracts. Mediation is much faster than arbitration and very cost effective, when compared to arbitrations and is normally permitted to take place during the currency of the contract – although success rates before a contract is concluded may be lower than in a global wrap up situation, at the end of the contract. In contrast, most arbitrations still take place at the conclusion of the contract and involve costly after the fact determinations. Hong Kong construction mediations are normally a few days long and antidotal evidence suggests that mediation durations are longer than those in UK.

The judge in charge of the construction and arbitration list, with the full approval of the Chief Justice, has recently introduced, via a practice direction, a court attached mediation scheme, effective from 1st September 2006. Whilst the scheme is voluntary, an unreasonable refusal to attempt mediation may result in an adverse costs order at the end of the court proceedings. This scheme is expected to give a further boost to the use of mediation to resolve construction disputes. Powers exist in the practice direction to stay the litigation, specify a minimum level of participation in the mediation (if not agreed) and allow the judge to express a view on whether mediation might help resolve all or part of the dispute.

The volume of construction cases in the court system is low as resolution by arbitration is the norm. To date, there are three known referrals to mediation, under the scheme, although there is no obligation to report back on the success or otherwise of the mediation, there is one known mediation success.

Adjudication

Construction adjudication is almost non-existent. There was a contractual adjudication system in place for the ACP contracts but only a handful of adjudications took place. The Government is introducing adjudication as a voluntary procedure in a trial scheme. Decisions take 56 days but can be extended by a further 28 days. Whilst the decision of the adjudicator is final and binding if not challenged, within 90 days, if it is challenged, by way of a notice of arbitration, it loses its temporary enforceable nature.

Does it work? It is very unlikely to be used and if used will probably be ineffective. A further difficulty exists as to whether a non-challenged adjudicator's decision will be enforceable, as non-compliance would create a breach of contract dispute, which would then be arbitrated, as Section 6 of the Arbitration Ordinance, is the same as Article 8 of UNCITRAL Model Law and the courts would grant a stay to arbitration.

Is it necessary? Not really, there is little ground swell to introduce statutory or contractual adjudication, because mediation is so

successful. Furthermore, wage protection legislation exists, reducing the impact of financial difficulties encountered by contractor and sub-contractor disputes, there is no obvious adjudication champion in the fragmented construction industry (sub-contractors account for 62% of the gross value of work performed on all main contracts) and legislative time for such matters is short.

Dispute Resolution Adviser system is a hybrid system comprising, inter alia, project mediation, informal partnering, step negotiation**,** and short-form arbitration, where a project neutral, the DRA, is employed for the duration of the contract. The DRA will nip disagreements in the bud, advise the parties on the best means of resolving those disputes that do arise which cannot be mediated and if the suggested resolution technique fails and the top executives cannot resolve the dispute, with the aid of the DRA, there is a one day arbitration procedure to resolve the dispute. The system was introduced in 1992.

Does it work? Yes, it is highly successful on complex Government building construction contracts and has now been introduced by the Housing Authority into their construction projects and civil engineering projects for the Government. There is only one known short form arbitration, in 53 projects, up to November 2004. An analysis of the DRA system shows that projects containing a DRA are more likely to be completed on time, with DRA projects having time extensions at 7.2 % compared with 15.7% on non DRA jobs and cost savings of 2.2% on DRA jobs compared with 1.7% on non- DRA jobs, even allowing for the cost of the DRA (who is retained and paid equally by the employer and main contractor). Moreover, the DRA is only employed on complex or high value jobs, making the statistics even more impressive.

Is it necessary? Yes, on complex projects because the DRA system avoids disputes, provides excellent budget control and results in prompt settlements of final accounts and maintains relationships.

Dispute Review Board / Group, there is only one known usage in Hong Kong on the new airport.

Did it work? Not really, as there was only one dispute referred under the system, as this was liability only and resulted in subsequent arbitration, which ended up in litigation, which went to the Court of Appeal. Disputes were not resolved as intended, on a regular basis, and were subsequently resolved post airport opening by a variety of means and after the DRG was disbanded. Apparently the DRG had some success in leading to on account payments as the project progressed

Was it necessary? Probably not, as the DRA system works better and is cheaper being one person rather than a group of seven or a panel of three when a dispute arises and the DRA system has more flexibility.

Conclusion

Mediation and the DRA system have created two very effective pre-arbitral procedures in Hong Kong and have led to a substantial reduction in the number of disputes that might otherwise reach arbitration. However, in those disputes which are arbitrated, being mainly private sector building disputes, traditional adversarial, document and fact heavy arbitrations are the norm, with interlocutory battles being commonplace before the hearings, so in these areas construction arbitration, as we used to know it is live and well.

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