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## CHOICE OF DISPUTE RESOLUTION METHOD IN INTERNATIONAL CONSTRUCTION CONTRACTS:A DELPHI STUDY

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### ABSTRACT

*Disputes are common in international projects because of contractual, legal and cultural factors. Although international construction projects offer new avenues for construction services, there are still many challenges to moving into international markets. Contractors should be aware that, though the international contracts they will sign may be similar to their own local contracts; they will still include some major additional/modified clauses that address international issues. Because disputes in construction projects are inevitable, one of the very critical contract clauses in an international contract is the dispute resolution clause. The dispute resolution methods currently adopted in international projects are varying including arbitration, mediation, expert determination, adjudication, dispute resolution board and litigation. The problem in question is on how to select the most appropriate resolution method that can fit nicely in the nature of the dispute and the disputing parties' needs. The objectives of this paper are to use the Delphi technique to identify factors that have an effect on the choice of dispute resolution methods (DRM) in international construction contracts and to recommend specific DRM(s) to contractors based in India.*

**Key Words:** *Dispute Resolution, International Contracts*

### INTRODUCTION

The business of construction has changed a great deal resulting from the effects of growing globalization and competition. The fast-growing international trade and developments, such as the World Trade Organization agreements and the Asia-Pacific Economic Cooperation forum have provided new opportunities to the construction industry. Facilitated by sophisticated communication technologies, advanced project management, and by profits attraction, large-scale projects are no longer local events but international affairs involving parties of different nations (Chan, 1997; Ofori, 2000). International construction is the industry where companies from one country diversify and expand their market shares by performing work in other countries. For example, companies from advanced industrialized countries that perform work in newly industrialized or less developed countries. This provides the opportunity of utilizing the most up-to-date expertise, knowledge, and methods. Despite these benefits, many challenges and risks are associated with international contracts, such as differences in economic conditions, specifications and standards, legal frameworks, productivity, and culture (Dikmen and Birgonul 2006). Once international contractors decide to venture into international projects, they must be aware that international contracts will include major clauses that manage international issues, notably the dispute resolution clause. Companies that enter foreign markets must be cross-culturally competent and capable of managing projects in different cultural environments (Chan and Tse 2003). This paper is part of a study that investigates the choice of dispute resolution methods (DRMs) in international construction contracts. The objectives of the paper are to identify factors that affect the choice of DRMs in international construction contracts and to recommend specific DRM(s) to contractors based in India.

## DISPUTES IN INTERNATIONAL CONSTRUCTION PROJECTS

International construction projects have maintained high levels of quality control while employing premium materials and tools. Project developers have invested heavily in importing expert resource, outsourcing skilled labour and purchasing certified and modern machinery. It is the successful execution of project processes that ultimately influences costs, timelines, business relationships and overall recognition. International construction disputes primarily involve delays on interdependent construction phases due to mismanaged time, inefficient processes and unclear contract terms that all undermine the business relationship between contractors, consultants and clients. Project managers usually spend as much as 50% to 70% of their time resolving conflict and disputes. Construction professionals need more knowledge and skills to manage and resolve conflict and disputes efficient and effectively, and the project progress and quality of the product will be improved. There are some leading key complexities faced in the international construction projects:

- (1) Validity of instructions from client or consultants to contractors and engineers;
- (2) Misconceived understanding by clients regarding the deliverables or services promised by contractors. Clients can assume they are entitled to ask for further support or specifications than the contractor has agreed to or can do;
- (3) Weak management skills in the areas of legalities and dispute resolutions that prolong conflicts;
- (4) Cultural diversity that leads in many cases to poor communication and understanding among the different parties to the contract.

## DISPUTES RELATING TO CONTRACTUAL MATTERS

There are many studies with recommendations on avoiding disputes caused by contractual issues in general. The following are a few specific points relating to international projects in India. The parties should, before any agreements, assess how much risks are involved for working in India with its legal, cultural and political background. These risks should be explicitly reflected in the relevant contracts. Reliable sources with reports and statistics by the Indian officials for risk assessments will be helpful and a contingent plan for emergencies will be advisable. As to the drafting of contract terms, parties should specify exact terms, in particular for payment and performance standards and establishing a realistic timetable. India is a Civil Law country which relies heavily what have been written down in contracts and codified in legislation. There are many specific compliance requirements by various departments for Indian projects and a local administrator will help better to ensure every step is complied with. The parties should also pay attention to minor details, such as checking the consistency with the English version. Even though an internationally acceded standard form, such as the FIDIC, is used, different interpretations by various parties from the two legal systems, Common Law and Civil Law, may cause misunderstanding. In this regard, pay special attention to any change to the standard form of contract, such as penalty clause, added responsibility of contractors, and impact from local legislation and administrative rules. Prevention is always better than cure; the parties should spend some time going through the entire contract document in order to reduce chances of discrepancies and errors. As arbitration is the preferred method for resolving any dispute arising from international projects in India, the contract clauses should facilitate such preference. In India, for international projects, it is advisable to specify the arbitration to be administered through the Indian Council of Arbitration (ICA) or reputable international institutions.

Rules of International Commercial Arbitration of the Council have been effective from 1st January, 2014, which recommends a standard arbitration clause, as reproduced below, which may be included in any contract or agreement for resolution of any international commercial dispute/s without modification or modified as may be required or according to the parties' preferences:

**“Any dispute or difference whatsoever arising between the parties out of or relating to the construction, meaning, scope, operation or effect of this agreement or the validity or the**

**breach thereof shall be settled by arbitration in accordance with the Rules of International Commercial Arbitration of the Indian Council of Arbitration and the award made in pursuance thereof shall be binding on the parties.”**

## **DISPUTES RELATING TO CULTURE**

Culture describes the social system that a group of people create in which they share common rules, norms, values, beliefs, perspectives, practices and rituals (Chan and Tse 2003). In terms of an organization, Hofstede (1984) defines culture as the collective programming of the mind that distinguishes one group from the other. In the construction industry, culture is about “the characteristics of the industry, approaches to construction, competence of people, and the goals, values and strategies of the organizations they work in” (Kivrak et al. 2008).

Since culture is an intangible concept that can only be seen through people's behaviours, it is necessary to develop a means of making it more concrete. Culture can be identified in terms of constructs referred to as culture dimensions. The effect of cultural differences on organizational management cannot be ignored. In the 1950s and 1960s, it was thought that organizational management practices are universal regardless of the culture. However, evident cultural differences that exist among individuals defy this view point. Transfers of management theories without cultural sensitivity, such as the adaptation of American theories in Europe or Third World countries, have proven failures in many cases. Professionals involved with participants from different cultural backgrounds must comprehend others' expectations and beliefs to function effectively (Chan and Tse 2003). This cross-cultural comprehension seems to be limited in the construction industry (Hall and Jaggar 1997). A survey conducted in the United States by the CII and American Society of Civil Engineers revealed that one of the major concerns of construction professionals is the lack of understanding of foreign cultures, ethics, and languages. Cultural differences affect most, if not all, activities of a construction project. Many ethical and moral dilemmas arise from failure to properly manage cultural differences include expatriates' culture shock, unfamiliar local work styles, different negotiation styles, different professional standards and construction codes, and codes of conduct and ethical standards (bribery and corruption (Hall and Jaggar 1997).

## **DISPUTE RESOLUTION METHODS**

Different contractual factors, legal and economic factors, technical standards, procedures, trade customs, currencies, cultural backgrounds, and languages involved in international projects make projects more vulnerable to disputes. International construction disputes represent a significant number of disputes arbitrated in the international commercial arbitration accounting for almost 20 percent of all disputes referred to the International Chamber of Commerce (ICC) each year (Seifert 2005). The Construction Industry Institute (CII) defines dispute resolution as one of twelve contract aspects related to risk allocation. The importance of bringing the dispute to a conclusion as efficiently and cost effectively as possible cannot be overstated. Thus, choosing the most suitable DRM becomes crucial.

In the global arena, there are many DRMs such as litigation, arbitration, dispute review board (DRB), mediation, adjudication, mini-trial, and early neutral evaluation. While, many researchers described the different DRMs and their characteristics (Chan and Suen 2005; Yates and Smith 2007), a limited number of studies investigated the basis on which the decision to choose DRMs in the contract is made. Most studies recommended the need for a systematic approach to choose DRMs (Chan et al. 2006). Such a systematic approach becomes very crucial when dealing with projects that have different characteristics such as contracting parties of different cultures.

DRMs vary in terms of cost of the process, duration taken to resolve the dispute, and decision enforceability, among many other things (Chan and Suen 2005; Yates and Smith 2007; Gad et al.

2011). Thus, the choice of a DRM to state in a contract should not be arbitrary. Deep thought should be placed on why one method is chosen versus the other, especially if this choice entails an international dimension. The dispute resolution process can be designed to control or minimise both the risk of claims and the cost of disputes that may arise in such an international context.

## **DELPHY METHODOLOGY**

The Delphi technique was used to gain a deeper understanding on the factors that affect the choice of DRMs in international construction contracts and to investigate the effect on the choice of DRMs. The following sections introduce the Delphi technique and the design employed in this study, including details on the three rounds of questions sent to the experts.

### **Delphi Technique Background**

The Delphi technique was developed by the Rand Corporation in the early 1950s. It aims at achieving convergence of opinions among a panel of experts about real-world topics that are often intangible. Experts are selected to participate in series of structured surveys using multiple rounds. In each round, the researcher provides the experts with an anonymous summary of the results of the previous round seeking their input and re-evaluation of their responses to achieve group consensus. Thus, the objective is to minimize the variability of the experts' responses (Hsu and Sandford 2007; Hallowell and Gambatese 2010). The Delphi technique has several advantages. It allows researchers to have control over any bias in a well-structured process by using the qualified experts' opinions and allows for experts' interaction. It also is useful when it is hard to reach objective data, no empirical evidence is available, and experimental research is not adoption. However, if the technique is not properly designed and implemented, the quality of findings may be compromised.

### **Delphi Technique Design**

Hallowell and Gambatese (2010) developed guidelines for the implementation of the Delphi technique which are used in this study. These guidelines identify how experts are chosen, the number of experts in a panel, and optimum number of rounds. A list of 26 experts was generated based on the following criteria:

- projects practitioners who have more than ten-year experience of construction contracts management in international projects;
- practitioners who have more than five-year experience of dispute resolution mechanisms in international projects; and
- practitioners who have more than five-year experience of international construction projects policies in India.

Such 26 experts were contacted and asked to participate in the study, twelve of which agreed.

### **Delphi Round One**

The first round of the Delphi constituted two main sections. The first section sought information on the expert's experience to confirm that they met the criteria for participation in the study. The second section asked the experts to list all the factors they could think of that might affect the choice of DRMs in international construction contracts. The second question in this section asked the experts whether from their experience, they thought culture of the contracting parties had an effect on the choice of DRMs in an international construction contract. Experts were also asked to provide justification for their answers. Round one questions were sent to 12 experts and 11 responded.

### Delphi Round Two

In the second round, the factors generated from the first round were compiled. Results from the first round included the frequency of mentioning each factor and the percentage of experts who identified each factor. The experts were provided those factors and were asked to rate them in terms of their importance, using a Likert scale from 1 to 5, with 1 being not important to 5 very important. On rating those factors, the experts were asked to assume a specific scenario: they are consulting a India-based international contractor on the factors to consider when selecting DRM(s) in the international contract with the owner. Eleven experts were sent the second round, all of which responded.

### Delphi Round Three

The third round included two questions about the influence of culture. The first question gave the experts the opportunity to revise their responses from the first round regarding culture effect on the choice of DRMs in international contracts in attempt to reach consensus among all the experts. Experts were provided the justifications given by all the panel members to their responses. The second question asked the experts to rate the suitability of specific DRMs in India using a score from 10 (least favourable) to 100 (most favourable). Eleven experts were sent the third round; ten of which responded.

## RESULTS AND ANALYSIS

The following sections cover the results and analysis of the Delphi rounds of questions.

### Delphi Round One

In the first round, 11 experts generated 38 factors that affect the choice of DRMs in international construction contracts. Factors with similar meanings were grouped yielding a total of 20 different factors. For example, 'value of privacy' and 'confidentiality of the processes were grouped into 'confidentiality and privacy'. As for the second question, 10 experts agreed that culture affects the choice of DRMs in international construction contracts providing different reasons such as:

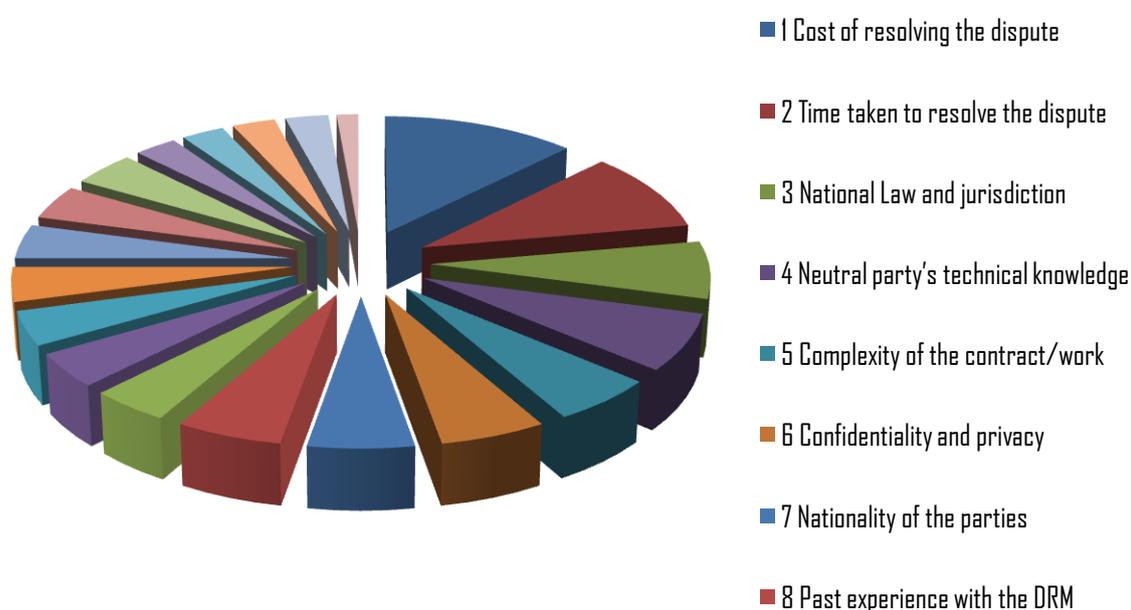
- Unfamiliarity with judicial system and with interpretation of contracts governed by local laws,
- Uncertainty about local courts' reliability,
- Preference of an international process for neutrality reasons (preference not to be governed by culture of the other contracting party),
- Unfamiliarity with the DRMs most popular in the country of operation,
- Different preferences of how disputes should be resolved; for instance, Asian cultures prefer a less formal process as a preliminary way to resolve disputes,
- Involvement of multinational parties from different political, legal, economic, and cultural backgrounds, and
- Communication problems are involved, such as language barriers.

Table 2. Factors affecting choice of DRM, sorted by frequency mentioned by experts (Round 1)

No.	Factor	Frequency mentioned
1	Cost of resolving the dispute	10
2	Time taken to resolve the dispute	8
3	National Law and jurisdiction	5
4	Neutral party's technical knowledge	5
5	Complexity of the contract/work	4
6	Confidentiality and privacy	4
7	Nationality of the parties	4

8	Past experience with the DRM	4
9	Binding outcome	3
10	Contract/funder/insurance requirements	3
11	Court system	3
12	Enforceability of decision	3
13	Flexibility of the process	3
14	Location of the project	3
15	Neutral party selection flexibility	3
16	Location of the hearings	2
17	Maintaining good long-term relationships	2
18	Nature and size of the dispute	2
19	Value of the contract	2
20	Duration of the contract	1

### Frequency mentioned



### Delphi Round Two

Table 3 shows the top five factors ranked in terms of average importance scores given by the experts. These five factors all had an average score greater than 5. The top rated factor was the 'enforceability of the decision' ( $M = 4.64$ ,  $SD = 0.674$ ) followed by 'national law and jurisdiction' ( $M = 4.45$ ,  $SD = 0.820$ ); both of which are related to the country of operation.

Table 3. Top 5 factors ranked in terms of importance (Round 2)

No.	Factor	Importance Average Score	Standard Deviation
1	Enforceability of decision	4.54	0.66
2	National Law and jurisdiction	4.45	0.80
3	Binding outcome	4.17	0.75
4	Time taken to resolve the dispute	4.10	0.75
5	Court system	4.07	1.21

### Delphi Round Three

By the third round, all experts reached a consensus that effect on the choice of DRMs. As for the most suitable DRMs to use in India, arbitration followed by negotiations then mediation got the highest average scores. The least recommended method being litigation.

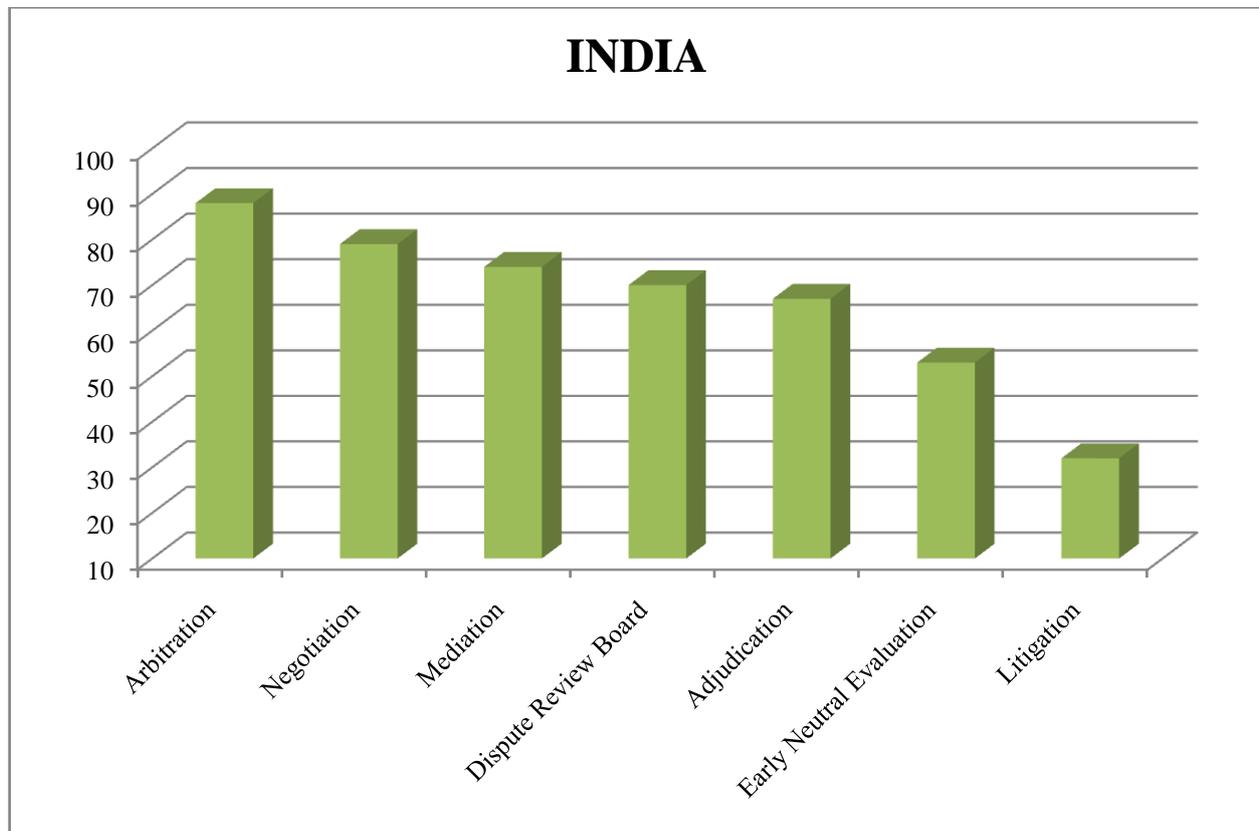


Figure 1. Comparison of scores given by experts for different DRMs (Round 3)

### CONCLUSIONS

This paper has two main objectives; to identify the factors that affect the choice of DRMs in international construction contracts and to recommend, for international contractors, specific DRMs to use for projects operated in India. Interviews with 11 international DRM experts identified 20 groups of factors that affect the choice of DRMs for international contracts. The top three factors rated by experts were enforceability of the decision followed by national law and jurisdiction.

Top five factors ranked in terms of average importance scores given by the experts. The top rated factor was the 'enforceability of the decision' followed by 'national law and jurisdiction'; both of which are related to the country of operation.

As for the recommended DRMs to use in India, by the last round, all experts agreed that culture has an effect on the choice of DRMs in international construction contracts. This implied that that the DRMs chosen by experts will be somehow different in various cultures. In India, experts recommended the choice of arbitration as the first method followed by negotiation and mediation. The least recommended was litigation.

This study provides recommendation on which DRMs based on the experiences of DRM experts who have been involved in resolving disputes with parties from different countries in India. It is of great importance to international contractors to understand that the DRM they choose to employ in the contract will have a great effect on the dispute resolution process and the resolution reached.

Thus, employing the optimum DRM that mitigates the risks that might occur is necessary for better project management.

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