An Owner's Guide to Avoiding the Pitfalls of Disputes Review Boards on Transportation Related Projects

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I. INTRODUCTION

Over the past twenty years, billions of dollars of public money has been committed and spent on the construction of major transportation projects, including subway systems, above-ground commuter rail projects, highways, freeways, and airports. As with any large construction project, substantial disputes frequently arise during the construction of transportation projects. These disputes can be quite complex and technical in nature with enormous amounts of money in controversy. The resolution of substantial construction disputes can be costly and may result in years of litigation. Dissatisfaction with the traditional litigation model of dispute resolution long ago triggered efforts to develop specialized forms of alternative disputes resolution ("ADR") for heavy construction projects.

A unique form of ADR known as disputes review boards ("DRBs") has gained increased acceptance on major transportation projects. While the DRB concept was initially promoted for underground projects, public

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owners have used DRBs on a wide variety of transportation projects ranging from construction at airports to the building of subways.[1] DRBs continue to be used on an ever increasing number of multi-billion dollar transportation projects. Industry publications report that DRBs demonstrate remarkable success in helping owners and contractors avoid costly litigation.[2] In the context of these encouraging results, however, owners (and contractors) need to be cognizant of lessons learned from the industry's now substantial experience with DRBs. Applying such lessons will ensure that DRBs remain an effective means of avoiding litigation on transportation and other construction projects.

At this juncture in the development and use of DRBs, certain pitfalls with the DRB process can be identified and addressed by owners. A recent California Court of Appeal decision concerning DRBs – the first published court decision in the country to address the operation of DRBs – demonstrates that the pitfalls associated with DRBs are not hypothetical and, in many instances, can be avoided with advance planning and careful drafting of the contract documents governing the DRB process.[3] This article identifies a number of potential pitfalls associated with DRBs and other issues that should be considered when drafting DRB related contract documents. All of these issues are discussed in the context of the attributes that distinguish DRBs from other forms of ADR and mediation. Better that owners embrace DRBs with "eyes wide open" than with "eyes wide shut."

II. The Unique Nature, Function and Purpose of Disputes Review Boards

Before discussing the various features of the DRB process, it should be noted that at least three sources of model DRB contractual provisions exist.[4] These model DRB contractual provisions include: model three

1. R. M. Matyas et al., Construction Dispute Review Board Manual 13-17 (1996) [hereinafter DRB Manual]; Technical Committee on Contracting Practices Of the Underground Technology Research Council, American Society Of Civil Engineers, Avoiding & Resolving Disputes During Construction 1 (1991) [hereinafter 1991 ASCE Guide].

2. DRB Manual, *supra* note 1, at 13-14; 1991 ASCE Guide, *supra* note 1, at 16; *see also* Brison S. Shipley, *Claims Avoidance & Management: DRBs On The Boston Central Artery/Tunnel Project Part 2,* Constr. Specifier, Nov. 1998, at 47.

3. *See* Los Angeles County Metro. Transp. Auth. v. Shea-Kiewit-Kenny, 59 Cal. App. 4th 676 (1997) [hereinafter MTA v. SKK]. The author represented the Metropolitan Transportation Authority in that action. The only other published judicial decision that even mentions DRBs is a short two page memorandum decision holding that, under the language of the applicable contract documents, a general contractor could not compel a subcontractor to utilize a DRB process established by the prime contract. General Ry. Signal Corp. v. L. K. Comstock & Co., 678 N.Y.S.2d 208 (N.Y. App. Div. 1998).

4. *See* DRB Manual, *supra* note 1, at 122-40; 1991 ASCE Guide, *supra* note 1, at 45-60;

party agreements between the owner, contractor, and the DRB (i.e., its three members); and model DRB specifications to be incorporated into the prime contract between the owner and the contractor.[5] These model contractual provisions should be consulted by the owner, the contractor, and their attorneys. Each of these sources contains commentary on DRBs and explanation of the DRB process. These sources also describe the conventional wisdom concerning DRBs.

In assessing the potential pitfalls of DRBs and the options available to avoid these problems, it is important to understand the nature, function, and primary purpose of DRBs. By specifying the features credited with the reported success of DRBs, the available options to avoid these pitfalls can be critically evaluated and the impact on the effectiveness of DRBs better assessed. Different commentators may attribute the success of DRBs more to one characteristic than another and may have varying opinions about the primary purpose of DRBs. Despite any divergence in viewpoints, an appreciation of these competing views of the nature, function and primary purpose of DRBs provides owners an analytical framework in which to make decisions about how to structure DRBs to avoid potential pitfalls.

A. The DRB Concept

A traditional DRB is a three person board of industry experts that assists the owner and contractor in resolving disputes.[6] The DRB conducts hearings on disputes and issues *non-binding* recommendations that are intended to help the parties reach a resolution without resort to litigation.[7] The DRB concept, while relatively simple and straightforward, has a number of significant features.

Composition Of A DRB. Typical DRB agreements provide that the owner and the contractor each appoint one member of the DRB and that the first two members nominate the third member, who ordinarily serves as the chairperson.[8] The party appointed members must be approved by the non-appointing party and both parties must approve the chairperson.[9] The conventional DRB wisdom is that this ensures that both the owner and contractor have confidence in the DRB as initially constituted.

Committee On Contracting Practices of the Underground Technology Research Council, American Society of Civil Engineers, Avoiding & Resolving Disputes in Underground Construction B8-20 (1989) [hereinafter 1989 ASCE Guide].

5. 1991 ASCE Guide, *supra* note 1, at 45-60; 1989 ASCE Guide, *supra* note 4, at B8-14.
6. 1991 ASCE Guide, *supra* note 1, at 1; 1989 ASCE Guide, *supra* note 4, at 2.
7. 1991 ASCE Guide, *supra* note 1, at 5; 1989 ASCE Guide, *supra* note 4, at 2.
8. 1991 ASCE Guide, *supra* note 1, at 44; 1989 ASCE Guide, *supra* note 4, at B9.
9. 1991 ASCE Guide, *supra* note 1, at 46; 1989 ASCE Guide, *supra* note 4, at B9.

Model DRB agreements specify that DRB members must have technical qualifications.[10] Each DRB member is to be experienced with the type of construction involved in the project.[11] Again, conventional DRB wisdom is that the parties will give greater weight to the recommendations of respected industry experts than to the views of those who lack such experience and stature.

While the owner and contractor each appoint one DRB member (with the approval of the other party), all DRB members are to be neutral and impartial.[12] The DRB members, regardless of which party appointed them, are *not* to act as advocates for either the owner or the contractor.[13] Conventional DRB wisdom holds that the impartiality (and the perception of impartiality) of each DRB member and the DRB as a whole is critical to the success of a DRB. This makes intuitive sense because the owner and contractor are less likely to give serious weight to the non-binding recommendations of a DRB when the impartiality of the DRB and its members is subject to doubt. Further, conventional DRB wisdom holds that the mere existence of a DRB reduces the number of disputes because owners and contractors will be much more judicious in pursuing claims knowing that a panel of respected experts will be reviewing disputes that are not resolved at the project level.

The three party agreement governing the DRB ordinarily specifies each party's contractual right to remove or terminate a DRB member.[14] The original industry model three party agreement promulgated in 1989 provided that DRB "members may be terminated for cause only by their original appointer; the OWNER may only terminate the OWNER-appointed member, the CONTRACTOR may only terminate the CONTRACTOR-appointed member, and the first two members must agree to terminate the third member."[15] The 1991 model agreement abandoned the cause standard for exercising the contractually specified right to remove a party-appointed DRB member in favor of an essentially "at will" standard: "BOARD members may be terminated for or without cause only by their original appointer; the OWNER may only terminate the OWNER-appointed member, the CONTRACTOR may only terminate the CONTRACTOR-appointed member, and the first two members must agree to terminate the third member."[16] The more recent model three party agreement retains the "for or without cause" standard for party

10. 1991 ASCE GUIDE, *supra* note 1, at 46-47; 1989 ASCE GUIDE, *supra* note 4, at B9.
11. 1991 ASCE GUIDE, *supra* note 1, at 46; 1989 ASCE GUIDE, *supra* note 4, at B9.
12. 1991 ASCE GUIDE, *supra* note 1, at 47; 1989 ASCE GUIDE, *supra* note 4, at B9.
13. 1991 ASCE GUIDE, *supra* note 1, at 47; 1989 ASCE GUIDE, *supra* note 4, at B9.
14. 1991 ASCE GUIDE, *supra* note 1, at 59; 1989 ASCE GUIDE, *supra* note 4, at B19.
15. 1989 ASCE GUIDE, *supra* note 4, at B19 (Three Party Agreement art. IX).
16. 1991 ASCE GUIDE, *supra* note 1, at 59 (Three Party Agreement art. IX).

appointees and provides that the two party appointed DRB members "or the Owner and Contractor must agree to terminate the third member."[17]

Notably absent from each of the three model agreements is an express contractual right on behalf of the owner or contractor to remove or terminate the other party's appointee. This creates a potential source of tension in the event one party loses confidence in the DRB and seeks to replace the DRB members. This aspect of the model agreements and the advisability of a modification permitting either party to remove any DRB member "for or without" cause is discussed below.

Familiarity With The Project Through Site Visits And Periodic Meetings. DRBs are meant to be constituted as soon after the execution of the contract and as early in the construction process as practical. The creation of a DRB is not intended to be deferred until disputes actually arise. Instead, the DRB is to be composed at the outset of the project. On many projects, however, there is some delay in constituting the DRB.

In addition to conducting hearings as particular disputes arise, DRBs (i) participate in periodic site visits and progress update meetings, and (ii) receive copies of project documents, including the contract documents, project schedules, and various progress reports. During the site visits, the DRB members tour the project with owner and contractor representatives and observe the progress of the construction. Usually on the same day as the site visits, the DRB conducts a progress update meeting in which the owner and contractor discuss the status of the project. In this way, the DRB members develop a familiarity with the project. Conventional wisdom is that the DRB's familiarity and firsthand knowledge of the project adds to the credibility of the DRB and the weight the parties will assign to recommendations issued by the DRB.

DRB Hearings And The Admissibility Of The DRB's Non-Binding Recommendations: If a dispute cannot be resolved at the project level, the parties may submit the matter to the DRB.[18] The DRB is to conduct a fair and impartial hearing.[19] Each party is to be given a reasonable time to prepare for the hearing in light of, among other things, the nature and complexity of the dispute.[20] Each party may make written submissions to the DRB and is to be afforded a full opportunity to present its position at the hearing.[21] However, the model DRB provisions do not provide either party with any formal right to engage in discovery in advance of

17. DRB MANUAL, *supra* note 1, at 138 (Three Party Agreement art. IX).
18. 1991 ASCE GUIDE, *supra* note 1, at 54.
19. 1991 ASCE GUIDE, *supra* note 1, at 47; 1989 ASCE GUIDE, *supra* note 4, at B9.
20. 1991 ASCE GUIDE, *supra* note 1, at 49; 1989 ASCE GUIDE, *supra* note 4, at B11.
21. 1991 ASCE GUIDE, *supra* note 1, at 50; 1989 ASCE GUIDE, *supra* note 4, at B11.

the hearing. By addressing issues as they arise and promoting early resolution of disputes, the conventional wisdom is that DRBs thereby reduce the friction and difficulties that might otherwise arise when issues are left unresolved and the owner and contractor become embroiled in litigation during the construction of a project.

After a hearing, the DRB prepares and provides to both parties written recommendations concerning the resolution of the dispute.[22] The recommendations of the DRB are *not* binding on the parties.[23] The parties ordinarily have fourteen days from receipt of the recommendations to respond by either accepting or rejecting the recommendations and the failure to respond in a timely fashion is deemed an acceptance.[24] Conventional DRB wisdom provides that, although the DRB recommendations are non-binding, the parties will nonetheless seriously consider the DRB recommendations whether favorable or unfavorable because: (i) the parties have faith and confidence in the neutrality and impartiality of the DRB members; (ii) the DRB members are themselves experienced in the type of construction involved on the project; (iii) the DRB members are familiar with the project; and (iv) the recommendations should themselves have some persuasive or logical force.

While DRB recommendations are not binding, the model DRB agreements provide that the DRB recommendations are admissible as evidence "to the extent permitted by law" in the event of subsequent litigation.[25] Conventional DRB wisdom is that, if the above enumerated factors are themselves insufficient to encourage a party to utilize the DRB's recommendations to resolve the dispute, the admissibility of the recommendations provides added incentive. The assumption is that an owner or contractor would be reluctant to proceed with litigation knowing that unfavorable recommendations of neutral and respected experts in the industry may be admissible and presented to the judge and/or jury.

B. Important Attributes Of A DRB

Based on the above discussion, a number of important characteristics of the DRB process can be identified that contribute to the success of DRBs in assisting owners and contractors in avoiding litigation.

22. 1991 ASCE Guide, *supra* note 1, at 50; 1989 ASCE Guide, *supra* note 4, at B12.

23. 1991 ASCE Guide, *supra* note 1, at 5; 1989 ASCE Guide, *supra* note 4, at 2.

24. *See, e.g.*, DRB Manual, *supra* note 1, at 132 (DRB Specifications §1.04 (I)).

25. The most recent model DRB specification states:

> If the Board's recommendation does not resolve the dispute, the written recommendation, including any minority report, will be admissible as evidence to the extent permitted by law in any subsequent dispute resolution proceeding or forum to establish (a) that a Dispute Review Board considered the Dispute, (b) the qualifications of the Board members, and (c) the Board's recommendation that resulted from the process.

DRB Manual, *supra* note 1, at 132 (Model Specifications § K1).

- *Confidence In The Neutrality And Impartiality Of The DRB And Its Members*: As a practical matter, a prerequisite to the success of the DRB process is that both the owner and the contractor have continuing confidence and faith in the neutrality and impartiality of the DRB and its members. Absent this, the chances of a successful DRB process are marginal at best. DRB recommendations are non-binding.[26] The reality is that, if the owner or contractor has lost confidence in the neutrality and impartiality of the DRB or its members, the disillusioned party cannot be expected to view the DRB's recommendations as a constructive tool to resolve the dispute.
- *Admissibility Of Recommendations*: The admissibility of DRB recommendations is intended to provide additional impetus to accept even unfavorable recommendations or to at least compel the parties to seriously consider the recommendations before initiating litigation. Of paramount importance, however, is that the owner and the contractor have confidence in the neutrality and impartiality of the DRB and its members. While there might be hypothetical circumstances where the admissibility of the recommendation might induce a disappointed party to accept the DRB recommendations, a loss of confidence in the neutrality and impartiality of the DRB and the process that produced the recommendations undermines the effective functioning of the DRB.
- *Qualifications Of DRB Members*: The expertise of DRB members and their familiarity with the type of construction involved in the project is quite important. The expertise of the DRB members and their technical background allows for disputes to be handled more expeditiously and without the need to educate a judge or jury who is unfamiliar with construction and engineering concepts. The unbiased assessment of a dispute by a group of respected experts undoubtedly would be given serious consideration by any responsible owner or contractor. The qualifications and stature of the DRB members is intended to reinforce the owner's and the contractor's confidence in the DRB and the weight accorded its recommendations.
- *Familiarity With The Project*: One of the intriguing aspects of a DRB is that its members develop familiarity with the project as the construction progresses. Familiarity with the project permits more efficient consideration of disputes. Of course, familiarity may breed contempt or a perception by either the owner or contractor that the other party has somehow ingratiated itself to one

26. 1991 ASCE GUIDE, *supra* note 1, at 5; 1989 ASCE GUIDE, *supra* note 4, at 2.

or more of the DRB members. DRB rules, however, are designed to minimize this risk by (i) ensuring that representatives of both the owner and contractor are present at site visits, project update meetings, and DRB hearings, and ii) prohibiting DRB members from providing advice or expressing opinions on the merits of disputes except in their written recommendations.[27]

- *Removal Of DRB Members*: All of the model agreements provide express contractual rights to remove a party's appointee to the DRB.[28] Although the standard for removal varies from "cause" to "for or without cause,"[29] removal of a DRB member may be necessary, for example, to restore the confidence of a party in the neutrality and impartiality of the DRB or a DRB member. The removal of one or more DRB members results in a loss of that member's (or the entire DRB's) familiarity and historical knowledge of the project. However, the right to remove a DRB member is not conditioned on the member's degree of familiarity with the project. The standard for removal does not become more difficult to satisfy as the DRB member's historical knowledge of the project increases.
- *Timely Resolution Of Disputes*: Another important attribute of DRBs is that they are intended to address disputes as they arise or as the parties fail to resolve the disputes at the project level. DRB conventional wisdom holds that this "real time" feature helps avoid the hardening of positions and the damage to the relationship between owner and contractor that may occur if an issue is allowed to fester.[30] Similarly, this feature is viewed as an advantage over litigation and other forms of traditional ADR like arbitration where disputes frequently are not addressed until several years after the occurrence of the relevant events by judges or arbitrators with no firsthand familiarity with the project.

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27. One of the industry DRB practice guides expressly admonishes against *ex parte* communications between DRB members and owner or contractor representatives:

> In order to avoid any suggestion of partiality, there should be no individual communication between Board members and employees of the contractor or owner during the life of the Board. Board communications with the owner or contractor, outside DRB meetings or hearings, should be handled only by the board chairman.

1991 ASCE GUIDE, *supra* note 1, at 8.

At the initial DRB kickoff meeting, the DRB and the owner and contractor ordinarily discuss procedural rules to be followed with respect to the DRB process. Most DRBs adopt a rule requiring that each party designate a DRB contact person and that the DRB chairperson coordinate administrative matters (e.g., scheduling of meetings, site visits, and hearings).

28. 1991 ASCE GUIDE, *supra* note 1, at 59; 1989 ASCE GUIDE, *supra* note 4, at B19.

29. 1991 ASCE GUIDE, *supra* note 1, at 59; 1989 ASCE GUIDE, *supra* note 4, at B19.

30. 1991 ASCE GUIDE, *supra* note 1, at 13.

Mindful of these key attributes of DRBs, owners can assess how modifying the DRB process to avoid potential pitfalls may compromise (or enhance) the effectiveness of a DRB in helping the parties avoid litigation.

C. The Primary Purpose Of The DRB: Assisting The Parties In Avoiding Disputes And Litigation

There should be no doubt as to the primary and essential purpose of a DRB - i.e., to help the parties avoid and resolve disputes without litigation. In short, the central purpose of the DRB process is to avoid litigation.

Unfortunately, either the owner or the contractor may develop a distorted view of the DRB process. For example, a contractor who believes the DRB is sympathetic to the contractor's plight and suspicious of the owner may consider the DRB as a means to generate recommendations for use in litigation and not as a means to resolve disputes and avoid litigation. This, of course, turns the purpose of the DRB on its head. The purpose of the DRB is not to generate evidence for use in litigation, but to avoid litigation. The admissibility of recommendations is simply one feature of the DRB process designed to encourage parties to accept DRB recommendations and to discourage parties from litigating marginal claims.

III. Owner Beware: DRB Pitfalls and Other Issues

A. Issues Concerning DRB Membership And Removal Of DRB Members

The first three issues and potential pitfalls of the DRB process involve the qualifications, appointment, and retention of DRB members. These issues should be of significant concern to owners and contractors because the effectiveness of a DRB is inextricably linked to the parties' mutual confidence in the neutrality and impartiality of the DRB and its members.

1. The preferred standard for removal of DRB members: A lesson from the MTA v. SKK *case*

A recent California Court of Appeal decision, *MTA v. SKK*,[31] addressed the standard for removing a party's appointee to the DRB.[32] That case contains a number of lessons and illustrates several potential pitfalls in the DRB process. Most notably, a DRB can be structured in a way to reduce the risk of owners and contractors becoming embroiled in

31. MTA v. SKK, 59 Cal. App. 4th 676 (1997).
32. *Id.* at 681.

collateral litigation over the composition of the DRB or termination of its members.[33] The best way avoid such litigation is for the DRB contract provisions to provide that a party's appointee may be terminated "for or without cause." This type of "at will" standard affords a party wide latitude in exercising its right to remove its appointee and virtually insulates the exercise of such a right from meaningful judicial review. Consequently, the likelihood of litigation (and certainly successful litigation) challenging removal of a party's appointee is significantly reduced.

The DRB provisions at issue in *MTA v. SKK* provided that the "DRB members can 'be terminated for cause only by their original appointer.'"[34] This is consistent with the standard for removal specified in the 1989 ASCE Guide.[35] When MTA gave notice of termination to its DRB appointee, the contractor objected asserting that MTA lacked cause and was proceeding in bad faith.[36] As a result of the contractor's attempt to block MTA's effort to replace its appointee to the DRB, MTA commenced a declaratory relief action seeking a judicial declaration validating the termination of its appointee.[37]

Because the contractor contested the existence of cause to terminate MTA's appointee and MTA's appointee refused to honor the notice of termination (or to resign under protest), the matter proceeded to trial.[38] As a result, MTA was required to develop and present all of the facts that justified the termination of its appointee.[39] The necessity of proving cause required that difficult and uncomfortable issues of misconduct be addressed while the contractor and the other DRB members defended the conduct of MTA's appointee. In the end, the trial court found that MTA's appointee had violated contractual provisions and industry standards governing his conduct as a DRB member and that such conduct constituted cause for removal.[40] This decision was affirmed by the court

33. *Id.* at 683, 683 n.3.

34. *Id.* at 679.

35. 1989 ASCE GUIDE, *supra* note 4, at B19 (Three Party Agreement ¶ IX).

36. MTA v. SKK, 59 Cal. App. 4th at 680-81.

37. *Id.* at 681.

38. *Id.* at 678.

39. *Id.* at 685, 687.

40. *Id.* at 685. The trial court found six types of violations, each of which independently satisfied the cause requirements, including: (i) improper prejudgment of issues concerning the MTA's termination of the contractor; (ii) improper prejudgment and *ex parte* communication in connection with a DRB hearing concerning the owner's removal of the contractor's general superintendent; (iii) statements at an industry function demonstrating bias against the MTA; (iv) improper *ex parte* communication with the contractor after the DRB member received notice of his termination; (v) failure to exhibit an appropriate temperament; and (iv) providing premature advice on incipient disputes during site visits and quarterly meetings. *Id.*; *see also* MTA v. SKK, No. BC 136559, slip op. at 6-10 (Cal. Super. Ct. Dec. 6, 1996) [hereinafter Statement of Decision].

of appeal.[41]

The contractor had alleged that MTA's decision to terminate its appointee was made in bad faith and was strategically motivated to disrupt the functioning of the DRB.[42] The contractor's argument centered on the fact that MTA's termination of its appointee occurred *after* the following events: (i) the contractor had itself been terminated for cause; (ii) the DRB had conducted a hearing concerning the termination of the contractor over the objection and in the absence of MTA; and (iii) the contractor thereafter sought to schedule additional DRB hearings on other pre-termination claims.[43] Contrary to the contractor's contention, the trial court specifically found that the owner had acted in good faith and this finding was again affirmed by the court of appeal.[44] The trial court, however, did not expressly address whether the contractor's conduct was itself strategically motivated to block the owner's efforts to replace its appointee and restore mutual confidence in the DRB. Regardless of the contractor's motivation, it is quite clear that the DRB process cannot function effectively where both parties do not share confidence in the DRB's neutrality and impartiality.

In light of the experience of *MTA v. SKK,* DRB agreements should allow for termination of a party's appointee "for or without cause." This will avoid disputes over a party's right to remove its appointee and collateral litigation over the exercise of that right. The "for cause" standard may require that reasons for removal be articulated. The very process of having to specify the misconduct constituting cause exacerbates the situation. An industry expert accused of misconduct (and the other DRB members) often may take issue with accusations of misconduct. The owner or contractor may be strategically motivated to defend the conduct of the DRB member accused of misconduct. This dynamic can only raise suspicions and further compromise the ability of the DRB to resume a useful function. A standard that allows removal "for or without cause" minimizes the opportunity and incentive for this type of strategic behavior. This "at will" type of standard also permits an amicable separation without the accusations and recriminations that accompany proof of "cause."

In this way, the "for or without cause" standard maximizes the potential success of the DRB. True, the replacement of DRB members sacrifices their project familiarity and historical knowledge. While there may be no way to replace firsthand knowledge, knowledge and familiarity

41. MTA v. SKK, 59 Cal. App. 4th at 687.

42. *Id.* at 683 n.3; Statement of Decision, *supra* note 40, at 10.

43. Carl F. Ingwalson, Jr., *Court Upholds Removal of DRB Panelist,* 21 CONST. DISPUTE & AVOIDANCE & RESOLUTION PUNCH LIST, May 1998, at 3.

44. MTA v. SKK, 59 Cal. App. 4th at 686-87; Statement of Decision, *supra* note 40, at 10.

with the project can be learned by an appropriate replacement DRB member. A loss of trust and confidence, however, may irrevocably compromise the ability of a DRB to function unless and until restored by replacing DRB members or by other means. For this reason, the DRB process should allow removal of a party's appointee "for or without cause."

Recent industry publications recognize that mutual confidence in the neutrality and impartiality of DRB members is of paramount importance.[45] Consistent with this recognition, the model three party agreements in both the 1991 ASCE Guide and the more recent 1996 DRB Manual provide for removal of party's appointee "for or without cause."[46] Indeed, the 1991 ASCE Guide advises that DRB members should voluntarily resign when a party has expressed a loss of confidence: "If, at any time, the Board believes that the process might work better with other Board members, it should offer to step aside. This necessity would arise if the Board senses that either the owner or the contractor has lost trust in their impartiality or judgment."[47] Similar advice is echoed in the 1996 DRB Manual: "If, at any time, it becomes apparent that either party has lost faith in a member of the board, that member should step aside. Regardless of the merits of the occasion, the credibility of the DRB concept should never be sacrificed to individual feelings."[48]

This advice – namely, that a DRB member should resign in the event a party loses confidence in that member – is not fully reflected in the 1991 and 1996 model DRB agreements. While those agreements do permit removal of a party's appointee "for or without cause," the agreements do not confer an express contractual right to remove the other party's appointee and provide that the owner and the contractor or the first two members must agree to terminate the third member.[49] In other words, there is no express contractual right to remove the other two members "for or without cause."

Due to the critical nature of mutual trust and confidence in the DRB and its members, owners should consider revising the language of the model agreements to permit the owner or the contractor to replace any of the DRB members "for or without cause." This will allow either party to more freely take the steps it deems necessary to restore mutual confidence in the DRB. The counter-argument is that permitting removal of

45. Ingwalson, *supra* note 42, at 4.

46. DRB MANUAL, *supra* note 1, at 138 (Three Party Agreement art. IX); 1991 ASCE GUIDE, *supra* note 1 at 59 (Three Party Agreement art. IX).

47. 1991 ASCE GUIDE, *supra* note 1, at 14-15.

48. DRB MANUAL, *supra* note 1, at 41.

49. DRB MANUAL, *supra* note 1, at 138 (Three Party Agreement, art. IX); 1991 ASCE GUIDE, *supra* note 1, at 59 (Three Party Agreement art. IX).

any DRB member "for or without cause" may have a revolving door effect on DRB membership and does nothing to deter strategic removal of DRB members. But this ignores the central tenant of the DRB process – mutual trust in each of the DRB members is essential to the effectiveness of a DRB. Accordingly, owners should consider permitting either party to remove any of the DRB members "for or without cause" and, at a minimum, this standard should be adopted for removal of a party's appointee.

2. Qualifications: Retired judge as chairperson

As the case of *MTA v. SKK* illustrates, a DRB's failure to maintain a sense of procedural fairness and regularity may seriously compromise the owner's or contractor's confidence in the DRB and its members.[50] Seemingly innocent statements or well intentioned efforts to expedite consideration of an issue may violate contractual provisions and suggest prejudgment of issues or bias in favor of one side. One of the lessons of *MTA v. SKK* is that process matters and adherence to the standards of conduct specified in DRB agreements is critical.[51]

Owners concerned about reducing the likelihood of procedural issues compromising the integrity of the DRB process should consider specifying that a retired judge or attorney with experience with construction litigation serve as the chairperson of the DRB. Certain of the issues that arose in *MTA v. SKK* involved issues of temperament and procedure.[52] Judges and attorneys receive specialized training in procedure and due process. An effective DRB depends on the preservation of the parties initial perception of the DRB's impartiality – a delicate task considering the generally informal nature of the DRB process and the sometimes heated tenor of DRB hearings. The best judges develop a judicial temperament well suited for adversarial settings and an attentiveness to procedural propriety that may help preserve the perception of the DRB's impartiality. Attorneys who are trained and experienced as arbitrators will display many of the same characteristics. The inclusion of a well qualified retired judge (or attorney) on the DRB panel may provide a valuable complement to engineers and other technically qualified DRB members.

This suggestion will undoubtedly face much criticism and resistance for a variety of reasons.[53] In viewing the critical attributes of a DRB,

50. MTA v. SKK, 59 Cal. App. 4th at 685-86.

51. Ingwalson, *supra* note 43, at 3 ("What the case does is highlight the need for DRB members to have strong ethical and process training. DRB panelists must adhere to the contract documents, maintain their integrity and avoid any appearance of bias.").

52. MTA v. SKK, 59 Cal. App. 4th at 685-86.

53. If the absence of a third DRB member with technical expertise is a real concern, a

however, the inclusion of a retired judge should not compromise the effectiveness of a DRB or cause the parties to unnecessarily "lawyer up" their submissions and presentations to the DRB. To the contrary, appointment of a well respected judge who understands and appreciates the difference between a court of law and the DRB process should enhance and help maintain the impartiality of the DRB. This change in the composition of the typical DRB therefore may increase the likelihood of acceptance of DRB recommendations and the avoidance of litigation.

3. Careful evaluation of DRB nominees is a must

One of the frequent pitfalls of the DRB process is that owners do not conduct due diligence or sufficient due diligence when considering a DRB nominee. Similarly, the owner's staff is frequently reluctant to reject a contractor's nominee.

An essential element of the DRB process is that the parties be satisfied with the appointees to the DRB. For that reason, both the owner and the contractor must approve each of the three DRB members.[54]

Owners must not be shy about rejecting a contractor's nominee. Frequently, an owner's project manager feels ambivalent and conflicted about the prospect of rejecting a contractor's nominee. The owner may believe that the contractor will misinterpret such a rejection as a sign of obstruction or lack of cooperation. The owner's staff may not want a conflict with the contractor over the DRB's composition to be the first conflict on the project or may fear that rejecting the contractor's nominee will precipitate a retaliatory rejection of the owner's nominee. In a completely different vein, the owner's staff may have prior experience with the nominee and may not want to reject the nomination for fear of insulting the DRB candidate.

Owners should feel no qualms about rejecting a DRB nominee. A rejection is not meant as an insult to the nominee and should not be misinterpreted by the contractor. Owners must recognize that accepting a nominee when questions exist as to the suitability of that member only heightens the likelihood of greater problems down the road. Owners should take heed of the following admonition:

> If a party is not comfortable with a nomination, it has the right to disapprove, and the appointing party should honor this right. Each party should make clear that it will not take offense if the other party rejects a nomination and will honor that commitment should the situation arise.[55]

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retired judge could be appointed as a non-voting fourth member of the DRB who would serve as the chairperson with respect to procedural matters and formal hearings.

54. 1991 ASCE GUIDE, *supra* note 1, at 46; 1989 ASCE GUIDE, *supra* note 4, at B9.

55. DRB MANUAL, *supra* note 1, at 43-44.

In terms of due diligence, owners should not hesitate to conduct a systematic assessment of a DRB nominee. Some owners interview the contractor's nominee and review the submitted disclosure statement and resume. Even more importantly, the owner's staff should inquire of individuals involved on other projects where the nominee served as a DRB member. Inquiry should be made of the role and demeanor of the nominee (e.g., did the nominee serve as the chairperson, did the nominee ask a lot of questions during DRB meetings and hearings, etc.), the confidence of both the owner and contractor in the neutrality and impartiality of the nominee, and how successful the DRB was in assisting the parties in avoiding litigation.

Another crucial piece of information ignored by most owners is prior DRB recommendations. Owners should request from DRB nominees copies of all prior DRB recommendations for prior DRBs on which they served. The recommendations themselves will provide significant insight into the effectiveness of the DRB member. For example, a review of prior recommendations will indicate whether the nominee has participated on DRBs that generate effective recommendations that will be useful in resolving disputes versus recommendations that are too bare bones or inflammatory.

Appropriate due diligence provides a basis for owners to evaluate whether to approve or reject a DRB nominee and thereby increases the likelihood of creating an effective DRB. Thus, an owner interested in a successful DRB should do its homework and be prepared to reject nominees as appropriate.

B. Limiting The Jurisdiction Of The DRB: Avoiding the Pitfall Of The Unrestrained DRB

1. Termination of the contractor and other issues that should be carved out of the DRB's jurisdiction

Owners need to consider whether the contract documents should provide unlimited DRB jurisdiction over disputes or whether there should be limitations on the type of disputes that may heard by a DRB. At least one issue should always be carved out of the DRB's jurisdiction – termination of the contractor.

Conventional DRB wisdom counsels against imposing limitations on the type of disputes a DRB may consider:

> In several instances, the scope of DRB activities has been limited to specific types of issues or minimum or maximum claim values. There should be no limitation on the issues which can be referred to the board. To impose such limits invites controversy over those subjects and calls into question the com-

mitment of the owner and the DRB concept itself.[56]

Although this advice makes good sense as a general matter, disputes over the termination of the contractor should be expressly excluded from the jurisdiction of the DRB.

There are a number of reasons that termination of a contractor should not be submitted to a DRB. Termination for default is a harsh remedy. Many industry participants immediately view an owner's exercise of this drastic measure with suspicion (if not disdain). For that reason alone, owners should consider carving out contractor terminations from the jurisdiction of a DRB.

Moreover, a termination for default ordinarily signals an irremediable breach in the relations between the owner and the contractor and almost invariably results in litigation. The stakes are incredibly high. Evidence must be carefully developed and marshalled. The nature of the typical termination dispute simply is ill-suited for the informality of the DRB process. If the parties believe that the DRB might be helpful in brokering a resolution or providing a constructive perspective, the parties always are free to ask the DRB to mediate the dispute; however, it simply is not advisable to make the DRB process mandatory in cases of termination.

To the extent owners see advantages to carving out other issues (e.g., owner directed replacement of contractor personnel), the excluded issues need to be carefully defined. Otherwise, there inevitably will be disputes over the jurisdiction of the DRB. The issue of contractor termination, however, can be clearly defined and should be carved out from the DRB's jurisdiction.[57]

2. *Termination of the contractor and survival of the DRB*

Owners should consider whether it is desirable for a DRB to survive after (i) completion of the project (whether defined as final payment, final completion, or some other point), or (ii) termination of either the contract or contractor.[58]

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56. DRB MANUAL, *supra* note 1, at 121.

57. To eliminate any jurisdictional debate, owners should consider expressly excluding from the DRB's jurisdiction all disputes concerning alleged violations of state or federal false claims acts. *See, e.g.*, Federal False Claims Act, 31 U.S.C. § 3729 (1983 & Supp. 1999); California False Claims Act, Cal. Gov't Code § 12651 (1992 & Supp. 1999).

58. The question of whether a DRB survives termination is a slightly different issue than whether the DRB should have jurisdiction over termination related disputes. The contractual provisions may carve out disputes over termination from the DRB's jurisdiction but the DRB may still have continuing jurisdiction over non-termination or pre-termination disputes. The survival issue addresses whether the DRB continues to function after the contractor's termination.

The most recent model three party agreement provides that the DRB "shall be active throughout the duration of the Contract" and "shall terminate its activities on completion of the Construction Contract after final payment has been made."[59] The corresponding model DRB specifications state: "The Board will be dissolved as of the date of final payment to the Contractor unless earlier terminated or dissolved by mutual agreement of the Owner and Contractor."[60]

A more restricted duration on the life of the DRB may be advisable. Good arguments can be made for structuring the DRB so that it does not survive termination of either the contract or the contractor and that all DRB activities conclude at that time. Under this approach, once the contract or contractor is terminated, the DRB would cease to function even as to pre-termination disputes.[61] When a contractor is terminated for cause, other pre-termination disputes take a back seat to the termination. Ordinarily, pre-termination disputes must be resolved as part of the resolution of the termination issue – whether through litigation or as part of a global settlement. In these circumstances, the utility of a DRB is questionable.

Additionally, some of the primary justifications for a DRB no longer exist after a contractor has been terminated. A DRB is intended to permit prompt resolution of disputes so that (i) the positions of parties do not become fixed in stone, (ii) good relations between owner and contractor are maintained during the course of construction, and (iii) construction of the project is not disrupted by the commencement of litigation. If a contractor has been terminated for cause, a DRB can do little to achieve these goals. Accordingly, it may make little sense to continue to use a DRB after the contractor has been terminated.

One option owners might consider is having the DRB terminate automatically upon the earlier of (i) final payment and (ii) termination of the contract or the contractor, unless both parties elect to reaffirm the DRB process and agree that the DRB should hear any unresolved disputes. If the DRB is to be effective after termination, both the owner and contractor need to remain committed to the DRB process. If they are unwilling to reaffirm the value of the DRB, then it is quite likely that one or the other party will seek to use the DRB to posture for litigation.

59. DRB MANUAL, *supra* note 1, at 136 (Three Party Agreement art. VII (A)).

60. *Id.* at 124 (DRB Specifications § 1.01 (F)(2)).

61. Some might criticize suggestions of curtailing the life of a DRB in the event of termination of the contractor because this might provide the owner with an incentive to engage in strategic conduct – i.e., terminating the contractor to bring the DRB to a standstill. Of course, if an owner were willing to take such an extreme step, there is little to no hope that the DRB could accomplish its purpose even if it were to survive.

C. Issues And Pitfalls Associated With DRB Hearings

1. Non-Admissibility of DRB recommendations as the preferred approach

Competing views exist as to whether DRB recommendations should be admissible in subsequent litigation. The committee responsible for preparing the 1991 model DRB provisions stated that it "strongly believes that the effectiveness of the DRB will be maximized, and the parties given greatest incentive to adopt the Board's recommendations, if they know in advance that the Board's decision and rationale will be received in evidence in the event the dispute is not resolved amicably."[62] Some maintain that DRB recommendations should be admissible because the DRB's "findings are likely to be accurate" to the extent they are "based on first hand observations."[63]

A number of arguments have been made against the admissibility of DRB recommendations.[64] Certain of those arguments focus on whether a court would even permit DRB recommendations to be admissible to the extent they are hearsay or the result of an ADR or settlement process.[65] If the (potential) admissibility of DRB recommendations is a true deterrent to litigation, then parties may treat the DRB proceeding itself as a trial and thereby undermine the efficiency and flexibility of the DRB process.[66]

Unfortunately, the empirical data has not been assembled and analyzed to determine whether DRBs experience greater success when the recommendations are admissible versus inadmissible. Owners on a number of projects have opted to drop the provisions in the model agreements providing for the admissibility of DRB recommendations. If the industry literature reporting the overwhelming and unqualified success of DRBs is to be credited and that literature does not distinguish between DRBs whose recommendations are admissible and those whose recommendations are inadmissible, a question certainly exists as to whether the admissibility provision is crucial to the successful operation of DRBs.

In the absence of any study on comparative success, *ad hoc* experience can be considered. The author has been involved in cases where: (i) contractors have initiated litigation despite unfavorable DRB recommendations, and (ii) owners have refused to accept unfavorable DRB recom-

62. 1991 ASCE Guide, *supra* note 1, at 12-13.

63. DRB Manual, *supra* note 1, at 38 (stating that the DRB recommendations can be no more reliable then the process that generated the recommendations – a process that does not allow for discovery).

64. *Id.* at 38-39.

65. *Id.* at 39.

66. *Id.*

mendations and defended their position in court. In all of these cases, the contractual language provided that the DRB recommendations were admissible to the extent permitted by law.

Based on these experiences, it appears that the admissibility of unfavorable DRB recommendations does little to deter initiation of litigation. This is especially so when substantial sums are at issue and the DRB does not "split the baby" but makes an "all" or "nothing" recommendation. The party who is in receipt of the unfavorable DRB recommendations is much more likely to adopt an attitude of "I'll take my chances in court because I can't fair any worse." In addition, the author has observed what appears to be strategic use of DRBs by certain contractors to obtain what the contractor hopes will be admissible DRB recommendations *for use in litigation* rather than utilizing the DRB process *to avoid litigation.*

In view of the foregoing, owners that use DRBs should consider deleting the model DRB specification language concerning the admissibility of DRB recommendations. This will minimize the incentive to engage in strategic use of the DRB to "set up" litigation. Rather, the parties will remain focused on the primary purpose of the DRB, which is to help avoid and resolve disputes without litigation.

2. *Conducting hearings in the absence of a party: A failed DRB process*

Another problematic issue that has arisen is whether DRB's can or should conduct hearings if the owner or the contractor refuses to attend.[67] As with the other DRB pitfalls, there is no one right solution to this problem. However, if an owner decides that a DRB should not be able to conduct a hearing in the absence of a party, language should be inserted into the DRB provisions to expressly limit the DRB's jurisdiction and eliminate any ambiguity. Otherwise, whether a DRB may conduct a hearing in the absence of a party who has been provided with notice of the hearing will turn on an interpretation of the language of the contracts at issue and the vagaries of the applicable state or federal law.

A number of arguments can be made in favor of self-executing DRBs – that is DRBs that can conduct duly scheduled hearings in the absence of a party who refuses to attend without the need to first secure a court order authorizing the hearing or compelling attendance. Some argue that the party who has requested the hearing loses the benefit of his bargain if the DRB does not conduct a hearing when requested to do so.[68] Of course, if the agreement expressly provides that the DRB may

67. Bart Bartholomew, *One Size Does Not Fit All*, DISPUTE REVIEW BOARD: FOUNDATION FORUM, Oct. 1998, at 6-7.

68. *Id.* at 6.

not conduct a hearing in the absence of a party or unless a court order is obtained, the party seeking the hearing has not been denied the benefit of the bargain.

Similarly, the argument has been made that the benefit of the bargain includes a party's right to secure DRB recommendations that may be admissible in subsequent litigation.[69] Again, neither party is denied "the benefit of the bargain" if the governing contracts specify that (i) a hearing may not be conducted in the absence of a party unless a prior court order has been secured, or (ii) the DRB recommendations are not admissible. Thus, a premium is placed on owners deciding how to structure the DRB at the time the agreements are being drafted and before the contract is awarded.

The arguments against DRB hearings in the absence of a party are similarly compelling. Every commentator recognizes that the DRB process is not functioning properly when one party refuses to attend a hearing.[70] If the DRB conducts a hearing in the absence of a party, the DRB process is almost assured of failure. The DRB process is fundamentally a mediative process. The effectiveness of the DRB in helping parties avoid litigation hinges upon the voluntary participation of the parties and the mutual confidence placed in the DRB by the owner and the contractor. A party typically cannot be expected to accept unfavorable DRB recommendations that are a product of a hearing conducted in that party's absence. A DRB that conducts a hearing over the objection of, and in the absence of, a party invariably compromises its appearance of neutrality in eyes of the objecting party. The only real solution is for the DRB to request that the party seeking the hearing obtain a court order compelling the hearing. This helps preserve the DRB's appearance of impartiality because it insulates the DRB from the appearance of choosing sides.

This is a thorny problem with no perfect solution. However, nothing meaningful is normally gained by proceeding with a DRB hearing in the absence of one of the parties. For this reason, it is recommended that DRB agreements specify that a hearing not be conducted in the absence of a party. At most, the agreement should provide that a DRB hearing may proceed in the absence of a party *only if* a prior court order compelling the hearing has been obtained.

3. *The information vacuum: How to minimize this pitfall by exercising an owners's audit rights*

The information vacuum is another potential pitfall of the DRB process that can be minimized with some advance planning. The model

69. *Id.*
70. *Id.*

DRB provisions do not expressly allow for discovery by the owner or the contractor in advance of a DRB hearing. The model DRB provisions do specify that the "Board members and the parties may ask questions, request clarification, or ask for additional data."[71] However, this provision does not provide a formal mechanism to gain discovery and does not directly address securing documents from third parties.

Owners frequently are at a significant information disadvantage with respect to many types of differing site condition claims and certain other claims that might be heard by a DRB. To effectively present its position (i.e., defend itself), the owner often needs to review documents from the contractor's file and the files of third parties. In many instances, such information is not voluntarily provided by contractors in advance of DRB hearings. If a contractor submits to the DRB selective pages from project diaries in support of a claim but does not make available the balance of such diaries, the owner (and the DRB) may never know whether the diaries contain information inconsistent with the contractor's position.

One simple solution for owners is to exercise their audit rights under the contract in advance of the hearing. The owner can request pertinent documents such as shifter and walker diaries, diaries of the project superintendent, scheduling and pricing information, the contractor's bid documents, and other documents typically unavailable prior to the hearing.

When drafting contract documents, owners therefore should make sure that the audit language is sufficiently broad to enable the owner to secure project documents in advance of DRB hearings. In addition, owners should make sure that their audit rights apply to subcontractors and suppliers. This will enable owners to secure pertinent information from these sources prior to DRB hearings. Any changes to clarify otherwise standard audit language should be made by the owner in consultation with its counsel. Effective use of audit rights will enable owners to be better prepared for significant DRB hearings and to avoid the pitfall of the information vacuum.

4. The danger of unintended acceptance of DRB recommendations

The model DRB specifications provide time restrictions for the owner and contractor to accept or reject the DRB's recommendations.[72] If an owner or contractor does not accept or reject the DRB recommendations within two weeks of their receipt, the failure to respond is deemed to be an acceptance.[73]

71. DRB MANUAL, *supra* note 1, at 131 (DRB Specifications § 1.04 (F)).

72. *Id.*

73. *See, e.g.*, DRB MANUAL, *supra* note 1, at 132 (DRB Specifications § 1.04(I)) (noting that the legal effect of a "deemed acceptance" on public entities may be subject to some debate

The time restrictions contained in the model DRB provisions may be impractical for many state and local agencies. Many local public entities must secure approval of a board before DRB recommendations can be accepted. Often times a public entity's board cannot be convened within fourteen days of receiving the recommendations. Consequently, the owner must somehow secure an extension to respond to the DRB recommendations or simply reject the DRB recommendations until the necessary board action can be taken.

Neither of these two options is entirely satisfactory. If the owner is late securing an extension, the contractor may argue an acceptance already has occurred by virtue of the owner's failure to timely respond. Further, the contractor may interpret requests for extensions as gamesmanship. Likewise, if the owner is put in the position of automatically having to reject the DRB recommendations because insufficient time exists for internal review of the recommendations, this too may be perceived as gamesmanship and strain the relationship between the contractor and owner.

To avoid such problems, the owner should realistically assess how much time will be required to act upon DRB recommendations. Model DRB provisions should be modified in the contract drafting process to allow sufficient time to make decisions to accept or reject DRB recommendations. Of course, owners should be mindful that one of the goals of the DRB process is to resolve disputes sooner rather than later. Public owners therefore should try to develop a streamlined process of review that enables a decision to accept or reject DRB recommendations to be made on an expedited basis.

In all events, an owner needs to make sure that its contract administrators and construction management personnel understand the applicable time limitations for accepting or rejecting the DRB's recommendations. The owner's staff needs to be aware that, even though the DRB recommendations are "non-binding," time limits exist to respond to the DRB recommendations. The unwary owner runs the risk of a "deemed acceptance."

IV. Conclusion

The DRB process continues to be incorporated into the bid documents on many major transportation projects. While the DRB process has garnered much praise for its effectiveness in helping parties avoid litigation, a number of potential pitfalls exist. The industry has developed and revised model agreements addressing some (but not all) of these is-

and for example, issues may exist as to whether certain public entities can be bound by a "deemed acceptance" in the absence of formal action by the public entity's board of directors).

sues. Owners interested in employing DRBs on large construction projects need to be cognizant of the associated pitfalls and the various modifications that can be made to model industry forms to mitigate these problems. With this information in hand and with "eyes wide open," owners can structure the contractual provisions governing the DRB process to avoid traps for the unwary and to enhance the success of both the DRB and the project as a whole.