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Construction Disputes in Major Infrastructure Projects: Guidance from the United Kingdom as Canada moves to Statutory Dispute Adjudication

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Statutes Commented On: *Construction Lien Amendment Act, 2017* (Ontario); *Housing Grants, Construction and Regeneration Act 1996* (England)

Introduction

In the delivery of infrastructure projects, construction disputes give rise to delays and potential cost overruns. This is especially true for major projects in the energy and natural resources sector where the number of parties, cross-jurisdictional components, challenging locations and the scale of the construction works are all contributing factors to a fertile dispute environment. As a result, a specialist dispute resolution mechanism is needed that facilitates the expedited resolution of disputes in parallel to the continuation of the construction works. Statutory dispute adjudication provides parties with that specialist mechanism. It allows for a fast, project-accompanying alternative dispute resolution mechanism that results in an interim binding decision by an independent adjudicator. The intention of dispute adjudication is to de-escalate a dispute. The parties enter into mandatory negotiation of their dispute with the benefit of the adjudicator's decision. Following the lead of the United Kingdom and elsewhere, Canada has recently taken steps towards introducing statutory dispute adjudication for the construction industry in this country. This post sheds light on those developments, outlines the key features of statutory dispute adjudication, and reflects upon what Canada can anticipate based upon the experience of the United Kingdom.

Current Developments in Canada

Following the introduction of dispute adjudication in the United Kingdom in the *Housing Grants, Construction and Regeneration Act 1996* (the "UK Construction Act"), a number of common law jurisdictions introduced statutory dispute adjudication for the construction industry, including Australia, New Zealand and the Republic of Ireland.

In Canada, two significant developments on dispute adjudication are currently ongoing. In Ontario, a comprehensive report ("Ontario Report") presented in April 2016 on the status of the construction industry entitled "Striking the Balance: Expert Review of Ontario's Construction Lien Act" made 101 recommendations for improvements in the construction industry. These included recommendations to introduce a formal statutory dispute adjudication mechanism as well as a prompt payment regime. In response to the report, the Attorney General of Ontario introduced Bill 142, *An Act to Amend the Construction Lien Act* on May 31, 2017. On December 5, 2017, Bill 142 was passed unanimously by the Ontario Legislature as the *Construction Lien*

Amendment Act 2017, and the Act received Royal Assent on December 12, 2017. Section 1 of the 2017 Act will rename the Ontario *Construction Lien Act*, RSO 1990, c C.30 as the *Construction Act.* The provisions on prompt payment (Part I.1) and construction dispute interim adjudication (Part II.1) are expected to come into force on October 1, 2019.

Secondly, Federal Bill S-224, *Canada Prompt Payment Act: respecting payments made under construction contracts*, passed third reading in the Senate on May 4, 2017. If it comes into force, this Act will introduce statutory dispute adjudication at the federal level.

Ontario Bill 142, An Act to Amend the Construction Lien Act

The Ontario Report was commissioned by the Ministry of the Attorney General and the Ministry of Economic Development, Employment and Infrastructure and prepared by construction law experts Bruce Reynolds and Sharon Vogel. The report was delivered in April 2016. Based on its recommendations, Bill 142 proposed amendments to the province's *Construction Lien Act*.

The introduction of dispute adjudication in Ontario's new *Construction Act* was a direct result of the Ontario Report, which had endorsed the mechanism as a "targeted interim binding dispute resolution method" (Chapter 9, part 4: Analysis and Recommendations). As discussed below, one of the central issues with dispute adjudication is the enforceability of an adjudicator's decision. The report endorsed the interim binding effect of an adjudicator's decision until final determination of the dispute by either litigation or arbitration (or when the dispute is settled between the parties). These recommendations are reflected in Part II.1 of the *Construction Lien Amendment Act 2017*, specifically in section 13.20.

The Ontario Report also discussed the concept of "security of payment" in Chapter 8. As discussed further below, this mechanism is also known as "prompt payment" and has been popular in comparative jurisdictions which follow statutory dispute adjudication in construction contracting. Part I.1 of the *Construction Lien Amendment Act 2017* sets out the provisions on prompt payment. The objective is to facilitate cash flow among the contractual parties to a construction contract. The regime effectively creates an "unlocking" of potential payment delays and resultant disputes.

Federal Bill S-224, Canada Prompt Payment Act

As noted, federal Bill S-224, *Canada Prompt Payment Act: respecting payments made under construction contracts* passed its third reading in the Senate on May 4, 2017. As the bill was initiated in the Senate, it is now before the House of Commons for its first reading. The proposed legislation relates to construction contracts between a "government institution" and a "contractor/subcontractor" only. This may encompass both a department or ministry of state of the Government of Canada and any parent Crown corporation or wholly owned subsidiary of a Crown corporation. Bill S-224 has two critical objectives, namely to strengthen the stability of the construction industry and to lessen the financial risks faced by contractors and subcontractors.

The Objective of Dispute Adjudication

Dispute adjudication is rooted in the concept of alternative dispute resolution. Adjudication allows parties to resolve disputes according to a mutually agreed contractual dispute resolution mechanism that does not, without an escalation of the dispute, resort to resolution by litigation or arbitration. Contractual parties to major infrastructure projects depend on an independent, impartial, expedited and flexible dispute resolution mechanism that does not cause the project works to be delayed or result in an escalation of project costs. Dispute adjudication operates as a project-accompanying mechanism, which manages and resolves project disputes "in-time", in other words, in parallel to the continued construction of the project.

Four clear interconnected considerations drive dispute adjudication. The process avoids an escalation of the dispute, maintains the commercial relations between the parties, balances the commercial interests of the parties, and reduces insolvency risk by unlocking payment and cash flow issues. Only when the initial dispute neutralising process of adjudication fails does the mechanism operate as an expedited dispute resolution mechanism, by way of an escalation of the dispute for final resolution by either litigation or arbitration.

Dispute adjudication operates so that only the most serious and complex of disputes are escalated to litigation or arbitration. A dispute is literally "filtered", which maintains the commercial relationship between the contractual parties of the project as the dispute is "contained" from the wider project works, which can continue without significant delay. Dispute adjudication achieves its objective of dispute avoidance and dispute de-escalation in two ways. First, dispute adjudication front-loads the avoidance and potential resolution of the parties' dispute. By including provisions on mandatory discussions and amicable settlement between the parties, a potential dispute may be negotiated off the agenda before it develops into a protracted dispute. This is the dispute avoidance strategy of dispute adjudication. Secondly, dispute adjudication seeks to resolve a dispute in-time to the ongoing project completion. The dispute resolution mechanism and the completion of the construction works therefore operate in parallel and the mechanism exerts pressure on the parties to resolve their dispute with a collaborative focus on the overall construction project.

The Interim Binding Decision

Parties to construction projects require a dispute mechanism that resolves disputes quickly and efficiently. A decision of an adjudicator therefore has interim binding effect, which is an essential aspect of dispute adjudication. An interim binding decision facilitates negotiations between the parties with the benefit of an adjudicator's decision, in order to prevent an existing dispute from escalating to either litigation or arbitration. Dispute adjudication is dependent on a strict contractual dispute resolution process, set out in a multi-tiered dispute resolution clause that contains provisions on dispute escalation (examined in detail below). This dispute escalation mechanism, of which adjudication forms an integral part, ensures that only the most serious and protracted disputes are finally resolved with the aid of litigation or arbitration as the dispute resolution mechanism of last resort.

Preliminary Assessment of Dispute Adjudication

An in-time dispute resolution mechanism is essential to the operation of the construction industry. This is especially relevant to large-scale and long-term construction contracts that may involve a large number of parties. The complexities of the project works, the scale of investment and the duration of long term projects underline the importance of an effective dispute management process that allows projects to continue in parallel to the expedited resolution of disputes. The collaborative nature of the construction industry, especially on large-scale projects, is that it is simply not within any of the project parties' interest to interrupt the project works in order to resolve disputes off site by either time-consuming litigation or arbitration.

Herein lies the key advantage of dispute adjudication. Disputes are managed and disposed of in real time, project relationships are maintained and project schedules are not delayed. Project costs are also controlled. Dispute adjudication is therefore driven by a desire to provide the contractual parties with a quick and practical resolution of their dispute. The interim decision of the adjudication allows subsequent management decisions to be taken with the benefit of an impartial initial adjudication of the dispute.

As a consequence of the expedited resolution of disputes by way of adjudication, there is a risk that adjudication may result in allegations of rough justice. But as the English courts have consistently held, the adjudication system can only properly function in practice when some of the inherent breaches of the rules of natural justice "are disregarded" (*Balfour Beatty Construction Limited v Lambeth London Borough Council*, [2002] BLR 288) and the expediency of the adjudication mechanism is kept in mind by all involved parties.

Statutory Dispute Adjudication in the United Kingdom

The United Kingdom courts, in particular the dedicated Technology and Construction Court bench of the High Court of England and Wales, have developed a deep jurisprudence on the complexities of statutory dispute adjudication pursuant to the UK Construction Act regime. An analysis of this jurisprudence provides guidance on how the statutory dispute adjudication regimes in Canada may be framed and subsequently interpreted. Below is an overview of the key judicial pronouncements on the essential aspects and challenges of dispute adjudication pursuant to the UK Construction Act.

The Concept of a "Dispute"

For the purposes of the UK Construction Act, dispute includes "any difference" arising under a construction contract as related to a construction operation, including questions on termination of such a contract. A dispute may be referred to adjudication at any time and the case law has confirmed that the concept of dispute or difference should be given an "inclusive interpretation" (*Bovis Lend Lease Ltd v The Trustees of the London Clinic*, [2009] EWHC 64 (TCC)). For example, a refusal of a claim for payment will typically give rise to a dispute pursuant to the English statutory regime.

Evidence in Support of a Dispute

In *Jacques (t/a C&E Jacques Partnership) v Ensign Contractors Ltd*, [2009] EWHC 3383 (TCC) at para 21, the court emphasized the distinctive aspects of adjudication, namely that the right answer is subordinate to the expediency with which an answer must be obtained. This is a deeply enshrined position in the law of adjudication. As a consequence, an adjudicator enjoys a wide discretion on the admissibility of evidence and only the most exceptional circumstances will amount to a breach of natural justice.

Expediency in Reaching a Decision

Pursuant to the statutory regime of the UK Construction Act, the adjudicator is to reach its decision within a 28-day period (s 108(2)(a)-(c)). A longer period can be agreed upon between the parties. The Act prescribes that a construction contract must include mandatory provisions so that a decision of the adjudicator shall be binding "until the dispute is finally determined" (s 108(3)) by either legal proceedings, arbitration or settlement between the parties. To facilitate amicable settlement between the parties, they can accept the decision of the adjudicator as the final determination of their dispute.

The Adjudicator's Decision

The statutory regime of the UK Construction Act prescribes that the adjudicator shall decide the matters in dispute and may take into account any matter which the parties agree should be within the scope of the adjudication. The adjudicator may also take into account matters under the contract which the adjudicator considers to be "necessarily connected with the dispute" (*The Scheme for Construction Contracts (England and Wales) Regulations 1998*, SI 649/1998). Pursuant to the regulations, the parties are required to comply with the adjudicator's decision "immediately on delivery of the decision". It is mandatory for the parties to comply with the decision of the adjudicator until the dispute is finally determined by either litigation, arbitration or by agreement between the parties. To foster agreement between the parties, they may accept the adjudicator's decision as finally determining their dispute.

Enforcing the Adjudicator's Decision

An enforceable decision of an adjudicator is "only binding until the dispute is finally determined by litigation, arbitration or agreement" (*Bouygues UK Ltd v Dahl-Jensen UK Ltd*, ([2000] BLR 49 (TCC)). In *Bouygues* the court set out the steps for enforcing an adjudicator's decision. The first step is to determine the dispute or disputes that were referred to the adjudicator. The second step is to see whether the adjudicator made a mistake and how that mistake should be characterized. In the context of a mistake, courts should keep in mind that the expedited nature of the adjudication process means that mistakes will inevitably occur.

Challenging the Adjudicator's Decision

The English courts have confirmed that a challenge to the decision of an adjudicator is difficult to reconcile with the expedited and summary nature of adjudication, a factor that is underlined

when one recalls that adjudication is an "intervening provisional stage" of dispute escalation (*Dorchester Hotel Ltd v Vivid Interiors Ltd*, [2009] WL 634882*).* The most important factor for a court to consider in a challenge is whether the adjudicator had the ability to determine the adjudication with fairness. The leading English authority on this point is *Carillion Construction Ltd v Devonport Royal Dockyard Ltd*, [2005] EWHC (Civ) 1358 where the Court of Appeal confirmed that an adjudicator is bound to adhere to the stringent principles of natural justice. Natural justice, as per *Carillion Construction Ltd*, requires the avoidance of bias and the granting to each party of a fair hearing.

Challenges on grounds of alleged breaches of natural justice should be limited to the most serious of cases only (*Cantillon Ltd v Urvasco Ltd*, [2008] EWHC 282 (TCC)), as the adjudication process cannot accommodate an excessive concern for "procedural niceties" (*Balfour Beatty Construction Company Ltd v The Camden Borough of Lambeth*, [2002] BLR 288). The correct procedure is to challenge the decision at the enforcement stage by way of litigation or arbitration, as adjudication is not the final determination of the parties' dispute.

Procedural Issues with Statutory Dispute Adjudication

The statutory dispute adjudication process pursuant to the UK Construction Act is by no means a perfect one. A number of attributes of the streamlined adjudication mechanism, such as the expediency of the process, have been exploited by parties who have attempted to move dispute adjudication closer to the procedurally intensive process of litigation or arbitration. This has resulted in a number of legal and procedural influences that go contrary to the "rough and ready" resolution of a construction dispute pursuant to statutory adjudication. These include:

Adjudication by Ambush

One of the key issues that has troubled the English courts is the ease with which an adjudication can be commenced under the United Kingdom statutory dispute adjudication regime. The mechanism provides the parties with relative flexibility in commencing an adjudication (by way of a notice to adjudicate). This has given rise to the concept of "adjudication by ambush", which was raised as a defence in *Bovis Lend Lease Ltd v The Trustees of the London Clinic*, [2009] EWHC 64 (TCC). On the facts, the Clinic attempted to argue that Bovis had over 16 months to prepare its case for adjudication, whereas it was given an initial two weeks only to respond to new claims and evidence.

The decision held that the UK Construction Act enables parties to refer any aspect of a dispute to adjudication at any time and that the only threshold requirement is that a dispute must have crystallized. Adjudication by ambush does not, therefore, give rise to an automatic allegation of procedural unfairness. The question for the adjudicator to decide is whether, based on the evidence submitted, he or she is able to deliver a decision within the prescribed statutory timeframe.

In *Dorchester Hotel Ltd v Vivid Interiors Ltd*, a similar restrictive interpretation was taken. In this decision, the court rejected Dorchester's argument that it had suffered procedural unfairness and

a breach of natural justice because of the limited time available over the Christmas holiday period to consider a large volume of evidence that was included with the referral to adjudication.

Serial Adjudications

Serial adjudications involve an adjudication which may already have been dealt with by previous adjudicators tasked to determine the same or a substantially identical dispute. Policy grounds strongly dictate against serial adjudications. For example, in *Carillion Construction Limited v Stephen Andrew Smith*, [2011] EWHC 2910 (TCC), it was held that a party to a construction contract has no right to expect that an essentially identical dispute may be referred to adjudication more than once. *Carillion* remains the leading authority in English law on how to determine if the same or substantially the same dispute has previously been referred to or resolved in an earlier adjudication.

A Late Adjudicator's Decision

A late adjudicator's decision is problematic because it is contrary to the expediency of adjudication. A late decision upsets the natural flow of the dispute adjudication procedure. Despite this, the law in England is not clear on the consequences of a late decision by an adjudicator, with two conflicting decisions handed down by the Technology and Construction Court.

In *Simons Construction Ltd v Aardvark Developments Ltd*, [2003] WL 22358283 (TCC), the adjudicator had issued a draft decision to the parties, before delivering a final decision outside the prescribed statutory time limit. There was no change in substance between the decisions. The court concluded that a final decision rendered late by the adjudicator may be valid, provided that the parties consented to the delay and the late decision of the adjudicator did not terminate the adjudication agreement on grounds of delay.

In the subsequent decision of *AC Yule & Son Ltd v Speedwell Roofing & Cladding Ltd*, [2007] WL 2187002 (TCC), a contrary conclusion was reached. The decision emphasized that the statutory time period was strict and focused its attention on the conduct of the parties in their interactions with the adjudicator. According to the court, there was a clear obligation on the parties to respond "plainly and promptly" to any request of the adjudicator.

Failure to Make Payment Pursuant to an Adjudicator's Decision

When dispute adjudication was introduced in the UK Construction Act, the English courts were divided on whether a failure to make proper payment pursuant to an adjudicator's decision could give rise to a separate cause of action. Subsequent jurisprudence of the English courts has clarified this important practical point. In *Jim Ennis Construction Limited v Premier Asphalt Limited*, [2009] EWHC 1906 (TCC), it was held that a new cause of action does arise, in order to compel the losing party to comply with a payment obligation which is similar to an action in debt.

Recovery of Payment Obligations Pursuant to an Adjudicator's Decision

The statutory scheme under the UK Construction Act is also silent on the recovery of money paid by a party pursuant to the decision of an adjudicator. In an important decision in 2015, the Supreme Court of the United Kingdom clarified the status of such payments in *Aspects Contracts (Asbestos) Ltd v Higgins Construction Plc*, [2015] UKSC 38. The court concluded that it was an artificial construction to treat a claim to recover sums paid based on an alleged breach of contract. The court held that a necessary consequence of the statutory adjudication regime is that it implies into the parties' contractual relationship a directly enforceable right to recover an overpayment made by a party pursuant to a decision of the adjudicator.

A Strict Interpretation of Mandatory Dispute Adjudication

Attempts to move dispute adjudication closer to the established areas of litigation or arbitration will mean a loss of the underlying rough and ready focus of dispute adjudication. Dispute adjudication depends on the expedited resolution of a dispute by way of an interim binding decision, without the luxuries of "procedural niceties". Two key arguments therefore support the conclusion that a mandatory dispute adjudication mechanism, as proposed for Canada, must be interpreted strictly.

The "Prompt Payment" Argument

Dispute adjudication is intrinsically linked to prompt payment obligations in construction contracting. The decision of the adjudicator formalises the payment obligation and forms part of what is called a "security of payment mechanism". This mechanism facilitates the timely payment for construction works and is designed to support construction contractors and sub-contractors, who are typically the financially weaker party. The mechanism isolates the risk of an insolvent party to the construction contract from accumulating additional debts, delaying payment and thereby 'infecting' the contractual payment chain. Commercial risks are passed onto the stronger contractual party. Any disputed payment obligation is determined by way of dispute adjudication, resulting in the payment obligation being formalized in an interim binding adjudication decision.

This security of payment process operates as follows: Pay now, argue later. The contractor will be in possession of the payment until the point when the other party (usually the employer) has successfully challenged the adjudicator's decision on the "prompt payment" obligation by way of an escalation of the dispute to litigation or arbitration. This ensures that the contractor maintains cash flow and is able to complete the construction works. The emphasis on the "prompt" resolution of payment disputes and the formalising of a payment obligation in the adjudicator's decision is another compelling argument in favour of a strict interpretation of any mandatory dispute adjudication mechanism.

The Dispute Escalation Argument

The provisions on dispute adjudication in construction contracts are usually encased within a multi-tiered dispute escalation clause. Essentially, a dispute is pushed along the escalation scale

and typically, complex long-term construction contracts provide for a two- or three-stage dispute escalation clause, typically negotiations, adjudication, mediation, litigation or arbitration. Litigation or arbitration are the dispute layer of "last-resort".

A key issue with dispute escalation clauses lies in the enforceability of the escalation steps. A strict interpretation mandates that the parties must be held to adhere to the provisions of their previously agreed bargain and that an active dispute resolution method, for example adjudication, has the power to bind a higher dispute method. A "higher" arbitral tribunal would therefore be forced to stay the resolution of the dispute until such time as the adjudication step has been completed. For example (albeit in a non-construction law context) in *International Research Corporation v Lufthansa Systems Asia Pacific*, [2013] SGCA 55, the Court of Appeal of Singapore held that where parties have contracted for a specific dispute resolution procedure as a condition precedent to litigation or arbitration, that procedure must be fulfilled. A similar position was taken in the decision of *Peterborough City Council v Enterprise Managed Services Ltd*, [2014] EWHC 3193 (TCC), where the English High Court confirmed that the parties could not "leapfrog" the dispute adjudication procedure to undertake direct recourse to litigation of the dispute. The emphasis on escalation and the mandatory provision on amicable settlement by the court confirmed that the adjudication process is, first and foremost, designed to de-escalate disputes between the parties.

The decision in *Peterborough* is an important reminder that adjudication serves the primary purpose of dispute avoidance. The parties are locked in dialogue and negotiation throughout the process. Two processes are operating simultaneously. Firstly, an active dialogue between the parties is facilitated. Secondly, a time-limited challenge period to the decision of the adjudicator ensures that the parties do not endlessly negotiate, thus ensuring procedural efficiency. Upon completion of the adjudication step, the dispute is escalated to the next dispute layer. In order to bypass any dispute escalation process, an exceptional and outright procedural impossibility would have to exist. Such an exception should be reserved for all but the most serious instances of impossibility so as to justify a direct recourse to the final dispute layer of litigation or arbitration.

In any discussion of dispute adjudication, it is important to remember that the entire process is based upon the mandatory collaborative resolution of the parties' dispute with the assistance of an interim binding decision of the adjudicator. The dispute escalation clause is a contractual clause. If the parties were permitted to avoid the mandatory escalation provisions, the integrity of the entire dispute escalation process would break down. As the Australian decision of *Hooper Bailie Associated Ltd v Natcon Group Pty Ltd*, (1992) 28 NSWLR 194, held, the rigorous enforcement of an escalation clause is required to safeguard the parties' participation in a process "from which cooperation and consent may come".

Concluding Recommendations

The imminent adoption of statutory dispute adjudication in Canada will no doubt benefit from a comprehensive body of comparative judicial interpretations on statutory dispute adjudication. As this post anticipates, dispute adjudication will play an increasingly important role in the de-escalation and avoidance of disputes in the Canadian construction industry, especially in the

timely delivery of major infrastructure projects. On this basis, the following principles and recommendations endorse dispute adjudication in Canada:

1. The number of parties, cross-jurisdictional factors and challenging geographical locations of typical energy and natural resources infrastructure projects require an expedited, flexible and party-driven dispute resolution mechanism.
2. The dispute resolution mechanism must be in-time and on-site in order to focus the parties' attention on the overall goal of delivering the project in time, at cost and in a collaborative manner.
3. Dispute adjudication should be included within a dispute escalation clause that typically entails mediation, litigation or arbitration. This will provide the parties with the requisite assurances that adjudication is a not a weak form of alternative dispute resolution, thereby reducing the temptation to bypass the adjudication process and to escalate the dispute directly to litigation or arbitration. At the same time, the terminal dispute layer of litigation or arbitration provides the parties with the requisite level of final resolution of their dispute.
4. A strict enforcement of the mandatory dispute adjudication provisions ensures that the parties take the mechanism seriously and adhere to their contractual bargain. Negotiation and settlement pursuant to a decision of an adjudicator is an important step in dispute adjudication, from which resolution of the dispute by way of cooperation may arise.

As Canada develops its dispute adjudication framework, other important lessons from the United Kingdom regime include the fact that "procedural niceties" cannot be accommodated in an expedited adjudication mechanism. Arguably, dispute adjudication is not a perfect process. But once one acknowledges the rough and ready nature of dispute adjudication, temptations to introduce procedural luxuries common to other forms of dispute resolution will fall away.

With this in mind, the prospect of successfully establishing dispute adjudication in Canada looks likely. At the moment Ontario leads the way. This is a welcome development for the resolution of construction disputes in the delivery of major infrastructure projects, especially for the energy and natural resources sector.

This post is an abridged version of my forthcoming contribution to the Canadian Institute of Resources Law's 'Resources' publication entitled "De-Escalating Construction Disputes in Major Infrastructure Delivery: Lessons from the United Kingdom as Canada Moves to Statutory Dispute Adjudication".

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