Expanded note to EURIM on guidance for ADR in public sector ICT procurement and contract renegotiations – November 2010

> *This guidance note extends the preliminary note of June 2010 and aims to sets out basic principles of Alternative Dispute Resolution (ADR) good practice in public sector ICT procurement and contract renegotiations. In particular, it refers to mediation and mediation skills as a key aspect of dispute prevention, conflict management and collaborative leadership*

1 Introduction

As part of its public spending reductions the Government announced it wanted to save £1.7bn by delaying or stopping contracts. It would review how current PFI/PPP projects can be best managed to extract improved VfM or renegotiate contracts so they are more affordable.[1] The Government also put into effect a moratorium on ICT projects and public bodies were asked to collaborate to maximise procurement savings. [2]

The 'call to collaboration' will not be easy for everyone. Collaboration demands more effort and time and may not appear to square easily with the financial belt-tightening being asked of the Government. More so because experienced project and contracts managers know that the reality of a project often falls short of the optimism found when the contract has been agreed.

The Authority and the supplier may soon find themselves constantly monitoring each other to ensure they are fulfilling their contractual obligations. And with this may come the dangers of developing a blame culture: people pointing the finger at each other to avoid being punished or feeling humiliated, with the result that no new ideas are pursued or no personal initiative is taken because people don't want to risk making a mistake or telling it as it is.

Blame culture has no room for unexpected problems. Often, finding someone to blame interferes with the process of finding a practical resolution to a problem and even if someone is found to blame, it does not end there. The pursuit of some form of punishment (legal, political, commercial, personal) follows. But even if a mistake is punished it does not mean a lesson has been learned or value created.

While we can easily say "we all make mistakes", mistakes are almost always associated with negative emotions and excessively negative language. This is familiar territory for journalists and politicians:

> *"Failed £234m C-Nomis IT project-ministers not told full truth"* (Computer Weekly,12 March 2009)

[1] The Government says it has now identified the first group of projects following the review and will decide in January 2011 which of these projects to terminate or re-scope.
[2] National Audit Office and Audit Commission. (May 2010). *A review of collaborative procurement across the public sector.*

"MPs furious at another government IT cock-up" (Techworld, 22 Oct 2004)

"Disastrous £400m courts IT project slammed by MPs" (Silicon.com, 11 Nov 2003

"Passport fiasco cost taxpayers £12m" (BBC News, 27 Oct 1999).

Not surprisingly, such headlines do nothing to lower our level of anxiety and the threat we feel when we think about mistakes. In turn, it makes it hard to talk openly about mistakes or when things start to go wrong.

Rather than excessive vigilance on contract obligations, time must be spent on maintaining a stable working relationship to allow not only disputes and problems to be resolved in a timely way but also to allow day-to-day conflicts to be addressed in as open and a direct way as possible. Vigilance needs to be directed to patient problem-solving in most cases.

Building mediation (and other ADR provisions) into contracts at procurement stage or during contract renegotiations will be important to help achieve this Budgets will need to focus on service delivery, not legal battles ineffective and aggravating dispute resolution procedures. Perhaps more significantly, project managers and contract managers will need to step up a gear in their communication effectiveness when faced with challenging discussions. A 'capability gap' was one of the findings of the 2010 "Tough Talk" survey of 1000 UK workers commissioned by CEDR looking at the management of conflict at a time of severe public spending cuts. Some 87% of people said that levels of conflict had either remained the same or increased during the past 12 to 18 months and nearly 75% of public sector staff identified weaknesses in their organisation's ability to conduct difficult or challenging conversations. Tellingly, only 44% of managers believe they are equipped to handle workplace conflicts and organisations experience more instances of internal conflict – between management (32%) and staff (27%) – than with customers, partners and suppliers combined. For project managers and project leaders this means they will have to be more sensitive to individuals in their project or negotiation teams and their ability to deal with conflicts. It will also mean being aware of people's different communication preferences: some like to get stuck into the details while others only want the big picture.

So what steps can be taken to keep the working relationship between the Authority and the supplier and the project team in each organisation on track? There are two general aspects to consider: the first deals with dispute escalation mechanisms which should be considered during the procurement process for inclusion in ICT contracts. The second, and still neglected aspect, deals with skills development in negotiation and conflict management.

2 Dispute escalation mechanisms and mediation

Dispute escalation mechanisms usually start with problem resolution hierarchies and may include ad hoc or mandatory mediation and expert determination[3]. In addition it should include consideration of dispute boards and project mediation which have been used successfully in the construction industry and which are equally capable of being adopted for ICT projects.

All these mechanisms prompt considerations at procurement stage regarding:

- whether to use an ad hoc or institutional procedure
- whether the procedure is single-stage or multistage
- the timescales involved
- whether the procedure covers all or certain types of dispute
- the cost – which would also include setting financial thresholds, where possible, to reduce the risk of the cost of resolution exceeding the value of the dispute.

(Refer to www.cedr.com/about_us/library/documents.php**)**

One potential difficulty with tiered dispute resolution provisions is the length of time it can take to work through the various steps involved. Escalating negotiation clauses often involve second or possibly third stages, which can take weeks, or longer, to comply with. Where the parties end up in a dispute, they may have been negotiating the issue for some time before one party triggers the dispute resolution clause's formal process. On the other hand, the opportunity to resolve disputes at operational level may be lost if all disputes have to be elevated to senior executive level.

If mediation is available at any time it means there is a greater chance for productive discussions because the parties are actually ready to engage in mediation. On the other hand, a compulsory mediation stage close to the outset of a dispute may not give a party enough time to have a genuine understanding of its own factual and legal positions or the other party's.

If mandatory negotiation or mediation is included, it is wise to consider short time limits before the parties can move onto the next stage. If the negotiation is going well then the parties can always agree to extend the time period. The point is that if one party does not play ball, it cannot use failure to comply to stop the other party from moving to the next dispute resolution stage.

For PFI contracts, section 28 of HM Treasury's Standardisation of PFI Contracts (SoPC4) (as published in March 2007) suggests a three-stage dispute resolution process, encompassing direct negotiation between the authority and the contractor, expert determination and, ultimately, arbitration or the courts if either party is dissatisfied with the expert's decision. SoPC4 also says 'it may be appropriate in certain circumstances to substitute other forms of Alternative

[3] Expert determination is commonly used in complex, high value ICT projects for technical disputes. However, care needs to be taken when drafting a dispute resolution clause including expert determination regarding what 'technical' actually means.

Dispute Resolution' for the expert determination stage, and a footnote identifies mediation, conciliation and neutral evaluation as possible alternatives.

Certainly, the use of **ad hoc mediation** is familiar to the ICT industry either as an attempt to by-pass litigation or arbitration, or as part of litigation proceedings. CEDR has successfully mediated many ICT disputes with three out of four mediations
concluding in settlement. For example:

- A government department entered into a contract for the supply of software licences. The department understood that a trial period for software suitability and testing would precede final acceptance. During the trial, the software was deemed unsuitable and the supplier was told the contract would be terminated. The parties were in dispute over whether the department was entitled to terminate the contract without making any payment, whether payment was contingent upon successful completion of the trial and whether the software provided met the requirements of the brief. A second dispute related to the duration of a contract for the provision of consultancy support and software maintenance. A clause in both contracts directed the parties to arbitration in the event of a dispute. However, the parties agreed to try mediation first and, should no settlement result, would pursue arbitration. The dispute was resolved in a day, saving the cost of arbitration estimated at 5% of the contract value.

- A mortgage and loan company entered into a ten-year agreement with an ICT company to provide services for all its offices. Three years into the contract a dispute occurred over invoicing and payment. The ICT company claimed it had not been paid for its services while the mortgage and loan company claimed the ICT company was not invoicing correctly. The amount in dispute was £175million. The dispute settled after two days with mediation costs of £6800 per party.

- Parties entered into a contract to design, develop and customise an electronic network-based trading system in order for the claimant, a UK company, to run live auctions on the internet. The defendant was also to provide support and maintenance for the system. The claimant alleged that over a ten-month period the system malfunctioned four times. The claimant terminated the contract for material breach and claimed damages. The defendant and guarantors alleged the claimant was in repudiatory breach of the contract and counterclaimed damages. The damages claimed amounted to £2.15m. The dispute was settled in a day with mediation costs of £3500 per party.

In contrast with ad hoc mediation (or expert determination) where an impartial person is asked to intervene at the point where a dispute arises, dispute boards and project mediation allow persons to be appointed at, and involved from, the start of the project to ensure that they are not only familiar with the project but also in a position to deal with problems as they arise.

Where a contract provides for a dispute board it will be as part of a tiered dispute resolution clause. For example, a clause might provide for a dispute board to operate throughout the project, for some technical disputes or disputes with financial thresholds to be referable, in certain circumstances, to senior executives and/or independent experts, mediation and, finally, arbitration or court.

A dispute board creates an environment in which the parties are encouraged not to exaggerate any representations that they may make to each other because they will know that at some point the board members may be asked to intervene. Because the same board reviews all project disputes, the parties become accustomed to how the board will react and take that into consideration when negotiating with each other. In that way claims are avoided and many disputes are likely to settle before being put to the board. The regular on-site presence of the dispute board members is more likely to develop co-operative behaviour since neither party will want to be seen as the cause of a dispute in front of the dispute board members who will be the same people dealing with all disputes.

The effect of the dispute board has also been explained as a situation where site staff and operational managers, who work with each other every day, see the dispute board members as intruders who must be ganged up on so as not to poke their nose in the project's private business. Parties, therefore, quickly come to a compromise.

There are three main types of dispute board:

> **Dispute Review Boards** issue recommendations. If no party expresses dissatisfaction with the recommendation then the parties have to comply with the recommendation. If , however, a party is dissatisfied with the recommendation, it must say so within a specified period and may then resort to arbitration or the courts. Pending determination by the arbitration tribunal or the court, the parties are not required to comply with the recommendation.
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> **Dispute Adjudication Boards** issue decisions. The parties must comply with a decision as soon as they receive it. If a party expresses dissatisfaction within a specified period, it may turn to arbitration or the courts for final determination of the dispute but the parties are contractually bound to comply with the decision.
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> Members of a Dispute Adjudication Board must act in a judicial capacity because the decision interprets the rights and obligations of the parties to a contract. So, the board must not only consider the facts but also the applicable law and must follow the rules of natural justice. This means that unlike a mediator, the board cannot meet privately with each party in order to discuss matters which one party does not want the other to know. The board would risk basing its decision on information which had not been disclosed to the other party.

Dispute Management Boards are independent advisory boards which are attached to the project management team. They observe the early stages of the team's work and subsequently pay regular updating visits to the project site during the life of the project. The board will comprise a number of different specialists or experts and one or more of its members can often adopt the role of advising the project team on the best way forward to address problems identified by the board as a whole. Alternatively, it may adopt the role of a mediator, facilitating discussions between members of the project team aimed at producing a dispute settlement agreement.

When projects involve multi-contracting regimes or a series of projects on a substantial programme, maintaining a number of dispute boards may be difficult and there may be issues regarding continuity and general oversight of the programme as a whole. In these circumstances it may be appropriate to have a single dispute board to be in place for all projects with a common chairman for all boards throughout the various projects and who will be in a position to look at the dispute resolution landscape over the entire project programme. It may also be of benefit to have an independent ADR organisation convene the board, deal with their administrative aspects and be a continuing resource for the board and the parties

Like dispute boards, **project mediation** is set up at the start of a contract. However, the project mediator(s), in addition to having familiarity with technical and contractual aspects of the project has a team-building role, placing an emphasis on effective communication and nipping problems in the bud.

This communication role should not be undervalued. Research in the construction industry has shown that there is a substantial difference between low and high performing projects in terms of project sponsors'/owners' desire for communication and their perception of project performance. On high performing projects, project sponsors had a much greater desire for communication, but also a lower perception of project performance than that held by project managers. Conversely, on low performance projects, project sponsors had less of a desire for communication, but a higher perception of project performance than that held by the project manager.[4]

Also, research has shown that delays and disruptions have a much greater impact on cost overruns than project managers intuitively expect and that many technically focussed project managers equate fast exchange of information with effective communication.

Coming at it from a slightly different angle, traditional risk management approaches often leave out ways of dealing with human factors: that is, purely technical risk assessment misses out the main project risks which deal with the interfaces and inter/intra-relationships between parties. Communication

[4] Turner, J and Muller, R. *Project Communication and Emotions: Communication to Maintain the Client's Comfort Levels and Build Cooperation.* Paper presented to the research conference, Vienna, 29 October 2003.

breakdowns both cause and equally are caused by project problems. So while it is possible to point to problems arising out of any number of procurement, design and operational management activities, all these areas of activity have many human variables.

Under CEDR's *Model Project Mediation Protocol and Agreement*, project team members have access to one or two project mediators who visit the project site on a regular basis to discuss progress and to identify with the parties any actual or potential communication or technical problems. The visit will normally coincide with the regular project meetings. The project mediators may have discussions with the any member of the project team including consultants, sub-contractors and specialist suppliers collectively referred to as key suppliers. The key suppliers are joined into the project mediation agreement between the owner and contractor, referred to as the core parties.

Before the project starts, the project mediators arrange a workshop attended by all project decision-makers. The project mediators also receive core documentation to review during the course of the works and may be contacted at any time to discuss project concerns and to seek guidance. If required, the parties may enter into a formal mediation conducted by the project mediators.

(Refer to www. cedr.com/CEDR_Solve/services/project_mediation_form.php)

3 Collaboration and conflict management

While an understanding of available dispute escalation mechanisms is desirable so, too, is raising awareness of aspects of effective communication and negotiation which lie at their heart. This recognises that critical relationships cannot be built or maintained by formal mechanisms and lies at the core of collaborative leadership.

The simple idea of maintaining good working relationships for better business and project delivery has to some extent been lost in the grander concepts of partnering, collaborative contracting, integrated working, alliancing etc. which speak more to the joint intentions of the parties regarding the project than it does to the skills they need to adopt to work together to achieve those intentions. With this has come much technical (and still relevant) guidance and attempts to produce more user friendly forms of contract. This has been particularly true for the construction industry.[5]

For example, at the heart of **partnering** lies a commitment by executive managers to adopt a collaborative approach to a project. The approach is used to arrive at business objectives by looking to optimise each of the partner organisations' resources. So, one of the aims of partnering is to increase productivity and so generate more successful outcomes to contract performance. A written document is not necessary for partnering to be effective. However, it is generally the case

[5] See for example, OGC, *Excellence in Procurement Guide*, 2007; International Business Leaders Forum ,*The Partnering Toolbook*, 2003; Reading Construction Forum, *The Seven Pillars of Partnering,* 1998.

that partnering begins with setting out joint objectives in writing after the contract is signed. This is generally thought to be the most effective approach, but is not a fixed feature of partnering. Some form of 'partnering charter' or agreement is the usual end product of a partnering workshop. This sets out the ground rules for how everybody will work together. However, the partnering charter, unlike the main contract, is not usually binding. Usually, it is necessary to provide training in working as a partnering team if a contract partnering agreement is to be adopted successfully.

Even though a so-called "suitable" contract cannot be relied upon in its entirety to reduce the impact of negative conflict, certain **contracts** (again from the construction industry) place emphasis on **promoting collaborative working** and through regulating the relationships in a project. One important example is the New Engineering Contract 3rd Edition (NEC3) which is endorsed by the Office of Government Commerce for public sector construction procurement.[6] It includes the option of a partnering charter that can be used for some or all parties. It creates a multiparty partnering team where the parties cooperate to achieve each other's project interests. They contract separately and partner together, and they are required to establish a core group to make key decisions.

The guidance note to NEC3 says that key to its successful use is 'users adopting the desired cultural transition': a transition which involves changing from a hindsight-based decision-making and management approach to a forward-looking one encompassing collaborative relationships. As already mentioned in the introduction, that cultural transition may not be a seamless one.

Partnering, mediation and collaborative leadership all come down to some core themes and areas for skills development which can be applied to team-working or individual interactions. These call on project leaders and project teams to:

- Actively manage the tension between focusing on project delivery and on building relationships, and prepare for how you are going to handle conflict well in advance.

- Recognise that conflict is not a mark of failure : it comes with the territory and will involve holding difficult conversations about key aspects of the relationship. The question is whether you are confident you have the skills to do so.

- Be sensitive to any patterns of caution and blame which prevent reflection and communication, conceal problems and compromise organisational or project team learning. Also, recognise that process mistakes and outcome mistakes are different and are often confused. Process mistakes are where lack of information, lack of care or poor decisions have led to an undesired outcome. Some outcome mistakes are rational to the extent that thinking was right but the outcome was not. Other outcome mistakes are irrational in that they could have been avoided if the thinking was right.

[6] NEC3 has been used on the Channel Tunnel Rail Link, Heathrow T5 and is currently being used on the 2012 Olympics construction programme.

- Make sure that decision-making is as inclusive as possible and is informed by bottom-up information. A by-product of this is that a learning environment is more likely to occur in a setting which encourages greater involvement of individuals in decision making.

- Carrying out regular leadership or team reviews using an independent facilitator to help teams to benchmark their negotiation/communication effectiveness and to improve their performance and realism on project options. A single "partnering workshop" at the start of a project will rarely be enough to provide a solid foundation for a collaborative working approach and to encourage active listening and genuine curiosity. Project members must be prepared to reveal what they think about each other and give each other feedback. Differences are best brought into the open and acknowledged, even if they cannot always be resolved. A project can soon become unstuck when the focus of one collaborative partner turns to 'beating' the other rather than being effective itself, believing that differences should be fought over rather than explored. Linked to this may be the need for awareness-raising and training on the role of negotiation in effective conflict management to enable participants to prepare effectively for a negotiation and to recognise and use different negotiation approaches.

Conclusion

Problems and disputes are perhaps the last thing that an Authority and suppler want to think about after involving themselves in a lengthy and expensive bidding and negotiation process. But a number of factors demand a clear approach to conflict management, dispute resolution and ensuring people have the skills to negotiate through the inevitable commercial, technical and people problems which will arise.

The increasing complexity of projects bring more interfaces and specialised teams to manage. In long term projects the successful resolution of problems will often involve both the resolution of the problem and a reconsideration, or possibly a variation, to the contract to prevent similar problems occurring again. And the length and complexity of contracts themselves can be daunting, leaving plenty of scope for differences in interpretation to emerge. If there is great inequality amongst project or negotiation team members in their ability to deal with problems they may easily fall back on adversarial or blame behaviours, or turning the contract into an arena for combat destroying the collaborative effort.

All this means that mediation should not be seen as a damage limitation exercise or as a last-ditch attempt to save relationships. It needs to be integrated as part of the project leadership strategy and not left as an add-on. This involves project leaders adopting mediation techniques and approaches as much as it does in being open to employing impartial persons to help. Any collaborative relationship takes time to become established and to avoid complacency it must be managed continuously. It requires energy and drive to make it happen. In addition, risk management approaches need to consider ways of dealing with communication and

relationship issues in projects and not relying mainly on the implementation of a methodology focussing on the technical aspects of a project. Coaching project leaders to ensure they remain mindful of conflict as a key area for management may be as necessary as the coaching role of managers of our leading football teams!

CEDR and ADR guidance in the public sector

Over the last twenty years CEDR has been in contact with many Departments of State, their agencies and other public authorities in work dealing with policy making, contract drafting, the administration of schemes and consultation on and delivery of training courses. Among other activities this included developing specific mediation training for the Treasury Solicitor and Ministry of Justice and helping OGC draft its original dispute resolution guidance on ADR. OGC currently refers to CEDR's Model Mediation Procedure under Schedule 8.3 of its ICT guidance on dispute resolution procedures.[7]

CEDR produced an ADR Guide for Local Authorities in Public Private Partnerships in consultation with a number of key agencies, including Partnerships UK and 4ps (now Local Partnerships). The guide was endorsed by 4ps as "the key source of guidance" in the, then, latest version of the Local Government Supplement to the Standardisation of PFI Contracts.

More recently, CEDR advised the Department of Health on the development of a structured dispute resolution process and related contract clauses for inclusion within its standard contracts for community, acute, mental health and ambulance services. These clauses have now been adopted.

[7] OGC ICT Services Model Agreement, version 2.3.