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Including Non-Signatory Subcontractors in Arbitration Clauses in Construction Contracts

Contracts / September 16, 2020

Arbitration is an increasingly popular forum for the resolution of construction disputes. It often provides a more predictable procedural process specially designed for the industry in light of construction-specific rules and mediation procedures enacted by alternative dispute resolution providers, such as the American Arbitration Association (AAA). Of course, there are pros and cons to private arbitration proceedings administered by AAA and other organizations, including, among other things, those discussed in last week's post about the increased up-front costs incurred to initiate an arbitration proceeding and paying the fees and expenses associated with a single arbitrator or multiple arbitrator panel. On the other hand, construction arbitrators are generally highly-qualified and experienced construction attorneys and industry professionals capable of resolving complex and highly-technical disputes Given the complexity of construction disputes this is often advantageous and preferable to a state court judge or jury of laypersons with little or no construction experience.

When planning a construction project, construction professionals should anticipate claims or controversies and make an informed decision up front about the ideal forum for resolving these disputes when they inevitably arise. Whether arbitration or litigation is preferred depends on a number of time and expense factors, as discussed above. However, if arbitration is preferred, then "consistency is key" in order to bring all claims and controversies into an arbitration involving many contractors and subcontractors (and their subcontractors and vendors) and to avoid piecemeal dispute resolution outside of arbitration.

The arbitration clause in construction contracts defines the scope of the claims, controversies, and disputes arising from construction projects and directly influences the parties that are bound by an agreement to arbitrate. The contracting parties should express a clear intent to arbitrate, and must also consider other parties who do not actually sign the construction contract but are nevertheless contemplated by the terms of the operative agreement. In Texas, a non-signatory to an agreement to arbitrate within a construction contract—including a subcontractor, for example—may be compelled to arbitration under legal theories establishing the non-signing subcontractor's agency with and for another contractor, or as an alter ego of a general contractor that is in essence the same entity as between the general contractor and subcontractor (which is, generally, difficult to prove absent fraud).

At the outset of beginning a construction project, contracting parties can contemplate and capture non-signatories to the main construction contract through incorporating by reference the respective party's signed subcontract agreements or even reference to the subcontractors themselves. Generally, contracting parties seeking to arbitrate their disputes must establish both a valid agreement to arbitrate and that their claims fall within that agreement's scope. *See Jody James Farms, JV v. Altman Grp., Inc.*, 547 S.W.3d 624, 629 (Tex. 2018) (citing *In re Kellogg Brown & Root, Inc.*, 166 S.W.3d 732, 739 (Tex. 2005)). If the goal is to keep construction disputes wholly confined in the arbitration forum, the arbitration clause must be given special focus. That is, the owner/developer and its general contractor, and all subcontractors and second-tier or below subcontractors, should be expressly contemplated by and accounted for in the arbitration clause. The parties to the prime construction contract should endeavor to reference all of their respective signed subcontract agreements, to

the extent they exist, as well as develop the arbitration clause to capture all disputes arising from the construction project and include joinder or consolidation with the arbitration proceeding of any other person or entity that is necessary to resolve the claim, controversy, or dispute, or that is substantially involved in or affected by the same. In doing so, the contracting parties can better avoid bringing piecemeal, fact-intensive litigation against subcontractors.

It is often penny-wise and pound-foolish not to consult with an experienced attorney when drafting a construction contract on any project of significance. A well-drafted arbitration provision can later save significant time and expense in an effort to avoid costly multi-party (and potentially multi-forum) litigation. The KRCL Construction Team has significant experience guiding clients through the contract formation process. The cost of preparing an enforceable arbitration provision costs pennies on the dollar as compared to potential extensive discovery and prolonged litigation in state or federal court.

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