

# THE COURTESY TRAP – FIDIC’S SUB-CLAUSE 20.5 – AMICABLE SETTLEMENT AND EMIRATES TRADING

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## I. INTRODUCTION

The “courtesy trap” was a phrase coined by Professor Tibor Varady.<sup>1</sup> The “trap”, as Professor Varady explains, is that a party can be delayed from resolving its dispute by litigation or arbitration by the requirement to pursue amicable settlement discussions and alternative dispute resolution (ADR) processes until all these steps fail. On the one hand it may be argued that these steps are cost effective methods of resolving disputes; on the other hand they can create both procedural and jurisdictional problems where one party is determined not to negotiate and wants to delay the commencement of the arbitration.

In the 1999 FIDIC forms of contract there are a number of obligations and/or condition precedents that require a party to give notice of a claim (sub-clauses 20.1 and 2.5), refer the claim to the engineer (sub-clauses 20.1 and 3.5) and then submit the dispute to a dispute adjudication board (“DAB”) (sub-clause 20.4). If either party gives a notice of dissatisfaction relating to the DAB’s decision then sub-clause 20.5 provides that:<sup>2</sup>

“Where notice of dissatisfaction has been given under sub-clause 20.4 above, both Parties shall attempt to settle the dispute amicably before the commencement of arbitration. However, unless both Parties agree otherwise, arbitration may be commenced on or after the fifty-sixth day after the day on which notice of dissatisfaction was given, even if no attempt at amicable settlement has been made.”

The issue that this article addresses is whether sub-clause 20.5 is a condition precedent to the commencement of an arbitration or whether it is an obligation, the breach of which will not affect the jurisdiction of the arbitral tribunal to resolve the dispute. The guidance section of the FIDIC Red Book 1999 does not assist. It merely states:

“Sub-clause 20.5 Amicable Settlement

The provisions of this sub-clause are intended to encourage the parties to settle a dispute amicably, without the need for arbitration: for example, by direct negotiation, conciliation, mediation, or other forms of alternative dispute resolution.<sup>3</sup> Amicable

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<sup>1</sup> Varady T, “The Courtesy Trap: Arbitration ‘If No Amicable Settlement Can Be Reached’”, *Journal of International Arbitration*, Volume 14 (1997) Number 4, pp 5–12.

<sup>2</sup> This provision is found in the Red, Yellow and Silver Books.

<sup>3</sup> For a thorough discourse of the various types of ADR procedure see *The FIDIC Forms of Contract*, 3rd Edition, Bunni N, Blackwell publishing, 2005 at pp 439 to 460.

settlement procedures often depend, for their success, on confidentiality and on both Parties' acceptance of the procedure. Therefore neither Party should seek to impose the procedure on the other Party."

FIDIC recognises that there is an apparent contradiction in the drafting of this clause. The FIDIC Guide states as follows:

"Although the first sentence of the sub-clause imposes an obligation to attempt amicable settlement, the second sentence specifies that, if a Party fails to make any attempt, the other Party cannot insist on it. This apparent contradiction is unavoidable, because of the impossibility of providing any meaningful method of imposing a requirement for the Parties to reach a consensual agreement of their differences."

The FIDIC drafters do not use language which suggests that sub-clause 20.5 is a condition precedent to the commencement of the arbitration. In sub-clause 20.1 the FIDIC drafters spelt out the consequences of not providing a 28-day notice; the clause stated that if the notice was not given then the contractor would not be entitled to an extension of time, to additional payment, "and the Employer shall be discharged from all liability in connection with the claim." As discussed below, in the 1990s, when sub-clause 20.5 was drafted, common law courts rarely found that this type of clause created a condition precedent; however, a number of recent cases now cast doubt on this conclusion. Sub-clause 20.5 creates two distinct obligations; the first is to attempt to settle the dispute amicably and the second is to wait 56 days from the date of the notice of dissatisfaction before commencing the arbitration.

## II. THE COMMENTARIES

The amicable settlement provision at sub-clause 20.5 of FIDIC 1999 contracts was based on clause 67.2 of the FIDIC 4th Edition (1987). Amicable settlement was a new provision in the FIDIC 4th form of contract. At the time it was noted that the clause could be criticised as it gave no guidance as to how the 56 days should be spent and therefore it was thought that this provision will "often merely represent an eight-week delay to the resolution of the dispute."<sup>4</sup> Edward Corbett explains that a failure by a party to attempt to settle the dispute amicably would appear not to be a breach of contract. However, as to the 56-day amicable settlement period, Corbett states that the right to commence arbitration: "... must be subject to clause 67.2 and the 56-day amicable settlement period provided for there."<sup>5</sup>

Glover and Hughes are emphatic in their view that sub-clause 20.5 is a condition precedent and state that: "An attempt to obtain an amiable settlement for a prescribed time of 56 days is also a condition precedent

<sup>4</sup> *FIDIC 4th A Practical Legal Guide*, Corbett E, Sweet and Maxwell, 1991 at p 450.

<sup>5</sup> *Ibid* at p 449.

to a referral to arbitration.”<sup>6</sup> The authors thereafter note that a party does not need to make an attempt at amicable settlement but do not explain how this is consistent with a condition precedent that an attempt must take place. It is therefore assumed that their reference to a condition precedent is to the need to wait for a 56-day period.

Baker, Mellors, Chalmers, Lavers<sup>7</sup> expressly disagree with the above view of Glover and Hughes<sup>8</sup> and state that “depending on the governing law, the mandatory language of the first sentence [of clause 20.5] may mean that there is a legal obligation to *attempt* to achieve a settlement before commencement of arbitration.” The authors’ view, however, is that arbitration may be validly commenced after the 56th day “... even if no attempt has been made for amicable settlement.”<sup>9</sup>

Robert Knutson, however, takes a different approach to the above commentators.<sup>10</sup> Knutson asks the question, what exactly is required by the parties when faced with this type of clause, and points out that:

“Agreements to negotiate are normally said not to be effective under English law. Amicable negotiations are not an inevitable precondition to arbitration as is sometimes seen because the sub-clause has a 56-day long stop after which arbitration may be commenced in any event.”

The inconsistencies in the FIDIC commentator’s views leave three questions unanswered:

- (a) Does a bare agreement to negotiate in good faith or attempt amicable settlement create an enforceable obligation?
- (b) Does a time limited obligation to negotiate create an enforceable obligation?
- (c) Should an amicable settlement clause (such as FIDIC’s sub-clause 20.5) be a condition precedent to arbitration?

### III. NON-BINDING GOOD FAITH NEGOTIATION CLAUSES – THE HISTORICAL POSITION

In the 1970s, the position under English law was well established and amicable settlement or good faith negotiation clauses were considered to be non-binding on the parties. In *Courtney & Fairburn Ltd v Tolaini Brothers (Hotels) Ltd* Lord Denning MR stated:<sup>11</sup>

<sup>6</sup> *Understanding the New FIDIC Red Book*: Glover J and Hughes S, Sweet and Maxwell, 2006 at p 391.

<sup>7</sup> *FIDIC Contracts: Law and Practice*, Baker, Mellors, Chalmers, Lavers, Informa, 2009 at p 542.

<sup>8</sup> *Ibid.*

<sup>9</sup> See also Klee L, *International Construction Contract Law*, Wiley Blackwell, 2015 at p 248, which states that “an obligatory attempt to settle a dispute amicably must be included as a rule.”

<sup>10</sup> *FIDIC: An Analysis of International Construction Contracts*, edited by Knutson R, Kluwer Law International, 2005 at p 76.

<sup>11</sup> [1975] 1 WLR 297 at 301–302; [1975] 1 All ER 716.

“If the law does not recognise a contract to enter into a contract (when there is a fundamental term yet to be agreed) it seems to me it cannot recognise a contract to negotiate. The reason is because it is too uncertain to have any binding force. No court could estimate the damages because no one can tell whether the negotiations would be successful or would fall through: or if successful, what the result would be. It seems to me that a contract to negotiate, like a contract to enter into a contract, it is not a contract known to the law.”

This was still the position in the early 1990s when the House of Lords revisited the issue. In *Walford v Miles*<sup>12</sup> Lord Ackner concluded that good faith negotiation clauses were not binding under English law and held:<sup>13</sup>

“The reason why an agreement to negotiate, like an agreement to agree, is unenforceable, is simply because it lacks the necessary certainty ... A duty to negotiate in good faith is as unworkable in practice as it is inherently inconsistent with the position of a negotiating party. It is here that the uncertainty lies. In my judgment, while negotiations are in existence either party is entitled to withdraw from those negotiations, at any time and for any reason. There can be thus no obligation to continue to negotiate until there is a ‘proper reason’ to withdraw. Accordingly a bare agreement to negotiate has no legal content.”

The position was no different in arbitration proceedings. Contractual clauses which sought to impose on parties an obligation to negotiate prior to arbitration were regularly disregarded. In *ICC Arbitration 10663* the tribunal considered an amicable settlement clause which provided:

“Any dispute between [the parties] shall be settled in the first place on an amicable basis. However, if not settled in such a manner, the dispute shall finally be settled under the Rules of Conciliation and Arbitration [ICC].”

It was asserted by the respondent that while this clause attempted to impose a mandatory obligation to settle disputes, the conditions which would make such a clause enforceable were not present – in particular the time necessary for the negotiations to take place were not stated. Further, the respondent argued that this provision should not be considered as a condition precedent. The arbitral tribunal agreed. The tribunal considered the situation where a dispute had arisen and the claimant then sought to prevent the respondent counterclaiming because the respondent had not gone through the amicable settlement process. It was decided that:

“When hostilities have begun, is there much point in entering into negotiations on the counterclaim? If the Fleet attacks, should the Air-Force go to the negotiating table?”<sup>14</sup>

<sup>12</sup> (HL) [1992] 2 AC 128; [1992] 2 WLR 174; [1992] 1 All ER 453.

<sup>13</sup> *Ibid* at 460.

<sup>14</sup> Cited in *Arbitration of Commercial Disputes, International and English Law and Practice*, Tweeddale & Tweeddale, OUP, 2005 at p 264. See also *ICC Case 16083* reported by Seppälä C, “Commentary on Recent ICC Arbitral Awards dealing with Dispute Adjudication Boards under FIDIC Contracts”, *ICC Dispute Resolution Bulletin*, 2015 Issue 1, where an arbitral tribunal held that a party had waived its right to insist on a party referring its counterclaims to a FIDIC DAB when that party had referred its claims straight to arbitration.

Similarly, in *Himpurna California Energy Ltd v PT (Persero) Perusahaan Listrik Negara*<sup>15</sup> the arbitral tribunal considered a “good faith negotiation” clause and stated that:

“Negotiations are certainly to be encouraged. The purpose of [the good faith provisions] cannot, however, be to obstruct either party’s fundamental right to seek a remedy for a claim under the [contract], once that party has given prior notice of such an intention, by obliging it to persevere with negotiations which in its view are proving fruitless.”

In the mid-1990s both amicable settlement clauses and mediation clauses were considered differently from clauses which required a party to take certain specified steps as a condition precedent to commencing arbitration. While the courts upheld clauses that required a formal procedure as a condition precedent to arbitration they did not uphold clauses which merely required the parties to attempt to settle their disputes. Therefore contracts which required a dispute to be first submitted to an engineer for an assessment,<sup>16</sup> or to adjudicator,<sup>17</sup> or to an expert,<sup>18</sup> were upheld. Where these steps were not taken then the arbitral tribunal could find that the arbitration has been commenced prematurely. In *The Channel Tunnel Group v Balfour Beatty Construction Ltd* Lord Mustill stated:<sup>19</sup>

“I believe that it is in accordance, not only with the presumption exemplified in the English cases cited above that those who make agreements for the resolution of disputes must show good reason for departing from them, but also with the interests of the orderly regulation of international commerce, that having promised to take their complaints to the experts and if necessary to the arbitrators, that is where the appellants should go.”

The courts of Australia were also beginning to uphold ADR clauses in the late 1990s. In *Aiton Australia Pty Ltd v Transfield Pty Ltd*<sup>20</sup> the Supreme Court stated it would uphold an ADR clause if it was drafted as a condition precedent. However, such clauses did not oust the jurisdiction of the courts but merely gave right to an entitlement to postpone a party’s right to use court proceedings. The court further stated that the procedures for ADR had to be sufficiently detailed to be meaningfully enforced.<sup>21</sup>

In *Partial Award of ICC Case No 6276 (1990)*<sup>22</sup> the parties’ contract contained a provision requiring disputes to be initially referred to an engineer for

<sup>15</sup> (2000) XXV Ybk Comm Arbn 12 (Final Award of 4 May 1999).

<sup>16</sup> *JT Mackley & Company Ltd v Gosport Marina Ltd* [2002] EWHC 1315 (TCC); [2002] BLR 367. In *Al-Waddan Hotel Ltd v Man Enterprise SAL (Offshore)* [2014] EWHC 4796 (TCC) at paragraphs 29 to 30 HHJ Raeside QC referred to it being trite law that the referral to an Engineer under clause 67.1 of FIDIC 4th Contract was a condition precedent to arbitration.

<sup>17</sup> *Cape Durasteel Ltd v Rosser and Russell Building Services Ltd* [1995] 46 Con LR 75, and *DGT Steel and Cladding Ltd v Cubitt Building and Interiors* [2007] EWHC 1584 (TCC); [2007] BLR 371; 116 Con LR 118.

<sup>18</sup> *Cott UK Ltd v FE Barber Ltd* [1997] 3 All ER 540.

<sup>19</sup> [1992] 2 Lloyd’s Rep 7; [1993] AC 334 at 352–353; [1992] QB 656; [1993] 2 WLR 262; [1992] 2 All ER 609.

<sup>20</sup> [1999] NSWSC 996; (1999) 153 FLR 236.

<sup>21</sup> *Elizabeth Bay Developments Pty Ltd v Boral Building Services Pty Ltd* (1995) 36 NSWLR 709.

<sup>22</sup> (2003) 14 ICC Ct Bull (No 1) 76–7.

its decision. In this case the employer failed to advise the contractor of the name of the engineer and the contractor therefore argued that the employer could no longer rely on this provision. The arbitral tribunal held that the reference to the engineer was a condition precedent and that the contractor, as a minimum, had to request the employer to appoint an engineer. Only if that request was met with a specific refusal could a referral to arbitration be made without the initial reference to the engineer.<sup>23</sup>

#### IV. A CHANGE IN POLICY – MEDIATION

In 2001 the Lord Chancellor stated that he wanted to keep the government out of the courts and reduce the legal aid budget. To this end he announced a pledge to use ADR processes, whereby disputes would be settled out of court. Mediation therefore became “the new buzzword.”<sup>24</sup> The statement of the Lord Chancellor was in line with a wholesale rethinking about litigation and the costs of litigation and arbitration, as identified in (a) the *Latham Report* of 1994; and (b) Lord Woolf’s *Access to Justice Report 1996*.

In 1997, in *Bernhard’s Rugby Landscapes Ltd v Stockley Park Consortium Ltd*,<sup>25</sup> HHJ Humphrey Lloyd QC recognised this change and stated that:

“There is now a tide running in favour of alternative forms of dispute resolution prior to recourse to litigation.”

Subsequently, in *Cott UK Ltd v FE Barber Ltd*<sup>26</sup> HHJ Humphrey Lloyd QC again stated:

“I take the view, therefore, that even where there is no arbitration clause, in the light of the observations of Lord Mustill in the *Channel Tunnel Group* case and in the light of the changing attitudes of our legal system, the court plainly has a jurisdiction to stay under its inherent jurisdiction, where the parties have chosen some alternative means of dispute resolution.”

It is evident from the above, that HHJ Humphrey Lloyd QC reflected in his judgment changes in policy and attitudes towards litigation.

In 2002 the courts had to address whether a clause requiring mediation as a first step in the dispute resolution process was sufficiently certain to be enforced. The case of *Cable & Wireless plc v IBM United Kingdom Ltd*<sup>27</sup> has been described as a “seminal case in the history of the courts’ attitude to contractual dispute resolution provisions.”<sup>28</sup> Colman J (as he then was)

<sup>23</sup> However, see *Man Enterprise SAL v Al-Waddan Hotel Ltd* [2013] EWHC 2356 (TCC); [2014] 1 Lloyd’s Rep 217 where it was held that the need to wait 84 days for an engineer’s decision was not a condition precedent where the employer had failed to re-appoint an engineer.

<sup>24</sup> Tweeddale A, “Alternative route to Mediation”, *Estates Gazette*, 5 January 2002.

<sup>25</sup> (1997) 82 BLR 39 at 57.

<sup>26</sup> [1997] 3 All ER 540.

<sup>27</sup> [2002] EWHC 2059 (Comm); [2003] BLR 89; [2002] 2 All ER (Comm) 1041; [2002] All ER (D) 277.

<sup>28</sup> Mackie K, “The Future for ADR Clauses After *Cable & Wireless v IBM*”, (2003) *Arb Int’l*, Volume 19, Number 3, p 345.

approached the question of whether a mediation clause was enforceable by reference to three criteria. His Lordship found that: (1) there was an intention to be bound by the clause; (2) that there was sufficient certainty in the procedure that the parties had agreed upon; and (3) that there were public policy considerations.<sup>29</sup> Colman J stated that:

“It is to be observed that the parties have not simply agreed to attempt in good faith to negotiate a settlement. In this case they have gone further than that by identifying a particular procedure, namely an ADR procedure ... There is an obvious lack of certainty in a mere undertaking to negotiate a contract or settlement agreement, just as there is in an agreement to strive to settle a dispute amicably, as in *Paul Smith Ltd v H&S International Holding Inc*, supra. That is because a court would have insufficient objective criteria to decide whether one or both parties were in compliance or breach of such a provision. No doubt, therefore, if in the present case the words of clause 41.2 had simply provided that the parties should ‘attempt in good faith to resolve the dispute or claim’, that would not have been enforceable.”

In *Holloway v Chancery Mead Ltd*<sup>30</sup> Ramsey J re-considered the criteria to be applied in order for an ADR clause to be upheld. His Lordship stated:

“First, that the process must be sufficiently certain in that there should not be the need for an agreement at any stage before matters can proceed. Secondly, the administrative processes for selecting a party to resolve the dispute and to pay that person should also be defined. Thirdly, the process or at least a model of the process should be set out so that the detail of the process is sufficiently certain.”

These criteria were subsequently considered and approved by the Court of Appeal in *Sulamerica CIA Nacional De Seguros SA v Enesa Engenharia SA*.<sup>31</sup> In the *Sulamerica* case the court found that the criteria had not been met and therefore refused to enforce the mediation agreement. A similar decision was given by Hildyard J in *Wah (Aka Alan Tang) v Grant Thornton International Ltd*.<sup>32</sup>

## V. EMIRATES TRADING – UPHOLDING GOOD FAITH NEGOTIATION CLAUSES

In *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd*<sup>33</sup> the English High Court re-considered the question whether amicable settlement clauses were binding. Clause 11.1 of the contract stated:

<sup>29</sup> Colman J stated:

“For the courts now to decline to enforce contractual references to ADR on the grounds of intrinsic uncertainty would be to fly in the face of public policy as expressed in the CPR and as reflected in the judgment of the Court of Appeal in *Dunnett v Railtrack*.”

<sup>30</sup> [2007] EWHC 2495 (TCC) at paragraph 84; [2008] 1 All ER (Comm) 653; 117 Con LR 30.

<sup>31</sup> (CA) [2012] EWCA Civ 638; [2012] Lloyd’s Rep IR 405; [2012] 1 Lloyd’s Rep 671; [2013] 1 WLR 102; [2012] 2 All ER (Comm) 795.

<sup>32</sup> [2012] EWHC 3198 (Ch).

<sup>33</sup> [2014] EWHC 2104 (Comm); [2014] 2 Lloyd’s Rep 457; [2015] 1 WLR 1145.

“11.1 In case of any dispute or claim arising out of or in connection with or under this LTC including on account of a breaches/defaults mentioned in 9.2, 9.3, Clauses 10.1(d) and/or 10.1(e) above, the Parties shall first seek to resolve the dispute or claim by friendly discussion. Any party may notify the other Party of its desire to enter into consultation to resolve a dispute or claim. If no solution can be arrived at between the Parties for a continuous period of 4 (four) weeks then the non-defaulting party can invoke the arbitration clause and refer the disputes to arbitration.”

Teare J referred to *Walford v Miles*<sup>34</sup> and *Wah v Grant Thornton*<sup>35</sup> and stated that in these cases the courts had found that an obligation to negotiate is regarded as being so uncertain as to render it impossible of performance. Teare J then questioned the rationale of these cases. His Lordship stated that:<sup>36</sup>

“However, where commercial parties have entered into obligations they reasonably expect the courts to uphold those obligations. The decision in *Walford v Miles* arguably frustrates that expectation. For that reason there has been at least one clear indication (though not in the context of a dispute resolution clause) that the decision in *Walford v Miles* may in appropriate circumstances be distinguished.”

Teare J then examined in depth the decision of Alsopp P in *United Group Rail Services v Rail Corporation New South Wales*.<sup>37</sup> This Australian case considered a contract for the design and build of rolling stock which contained a dispute resolution clause that provided that the parties should “meet and undertake genuine and good faith negotiation with a view to resolving the dispute”. Alsopp P distinguished the English court’s decision in *Walford v Miles*<sup>38</sup> stating that he did not find Lord Ackner’s reasoning persuasive. Alsopp P stated:<sup>39</sup>

“a promise to negotiate (that is to treat and discuss) genuinely and in good faith with a view to resolving claims to entitlement by reference to a known body of rights and obligations, in a manner that respects the respective contractual rights of the parties, giving due allowance for honest and genuinely held views about those pre-existing rights is not vague, illusory or uncertain.”

Alsopp P further held that such an approach met with public policy requirements, which promoted efficient dispute resolution and encouraged approaches by, and attitudes of, parties conducive to the resolution of disputes without expensive litigation or arbitration.<sup>40</sup> Teare J, in *Emirates Trading*, stated that he considered the reasoning of Alsopp P to be cogent and that it should be applied. His Lordship proceeded to state that in conducting negotiations there must be imported an obligation to seek to do so in good faith.<sup>41</sup> His Lordship then referred to *International Research*

<sup>34</sup> (HL) [1992] 2 AC 128; [1992] 2 WLR 174; [1992] 1 All ER 453.

<sup>35</sup> [2012] EWHC 3198 (Ch).

<sup>36</sup> *Ibid* at paragraph 40.

<sup>37</sup> (2009) 127 Con LR 202.

<sup>38</sup> [1992] 2 AC 128; [1992] 2 WLR 174; [1992] 1 All ER 453.

<sup>39</sup> (2009) 127 Con LR 202 at paragraph 74.

<sup>40</sup> *Ibid* at paragraph 80.

<sup>41</sup> *Ibid* at paragraph 51.

*Corp plc v Lufthansa Systems Asia Pacific Pte Ltd*<sup>42</sup> where the High Court of Singapore had to consider whether a clause which referred to arbitration disputes “which cannot be settled by mediation” provided a condition precedent to arbitration that was too uncertain to be enforceable. The Singapore High Court found the agreement was not too uncertain and was binding on the parties.

One of the main issues addressed in *Emirates Trading*<sup>43</sup> related to the four-week period in which the negotiations were to take place. The claimant’s counsel argued that the four-week period created a condition precedent to be satisfied before the arbitrators would have jurisdiction to hear and determine the claim. The condition precedent was “a requirement to engage in time limited negotiations” and that requirement was not fulfilled because there had not been “a continuous period of 4 weeks of consultations to resolve the claims” which were the subject of the notice of termination.<sup>44</sup> Teare J considered this provision important because the reference to a period of four continuous weeks ensures that a defaulting party cannot postpone the commencement of arbitration indefinitely. In conclusion Teare J held:<sup>45</sup>

“There is, it seems to me, much to be said for the view that a time limited obligation to seek to resolve a dispute in good faith should be enforceable. Such an agreement is not incomplete.”

Teare J then addressed the question of how to distinguish *Walford v Miles* and *Courtney & Fairbairn Ltd v Tolaini Brothers*. His Lordship stated that:<sup>46</sup>

“... these were not cases of a dispute resolution clause within a binding contract obliging the parties to seek to settle a dispute under that contract within a time limited period whereas the present case is. It can therefore be distinguished on the facts. Moreover, given the clear public policy in enforcing obligations in dispute resolution clauses which are designed to avoid the expense of litigation or arbitration that factual distinction is material.”

According to Teare J it is necessary for a time requirement to exist if a good faith negotiation clause is to be upheld. However, no reference was made in the *Emirates Trading* case to *Globe Motors Inc v TRW Lucasvarity Electric Steering Ltd*.<sup>47</sup> In this case Mackie J indicated that he would uphold a bare good faith negotiation clause (with no reference to reasonableness or a time-limited obligation).<sup>48</sup> Mackie J subsequently stated that: “The existence of an enforceable obligation is consistent with a duty to collaborate.”<sup>49</sup>

<sup>42</sup> [2012] SGHC 226.

<sup>43</sup> [2014] EWHC 2104 (Comm); [2014] 2 Lloyd’s Rep 457; [2015] 1 WLR 1145.

<sup>44</sup> *Ibid* at paragraph 4.

<sup>45</sup> *Ibid* at paragraph 52.

<sup>46</sup> *Ibid* at paragraph 59.

<sup>47</sup> [2012] EWHC 3134 (QB).

<sup>48</sup> *Ibid* at paragraph 22.

<sup>49</sup> *Globe Motors Inc v TRW Lucasvarity Electric Steering Ltd (Rev 1)* [2014] EWHC 3718 (Comm) at paragraph 270.

In the case of *Emirates Trading Agency LLC v Sociedade de Fomento Industrial Private Ltd*<sup>50</sup> there was a time-related amicable settlement clause in terms similar to that found in *Emirates Trading v Prime Mineral Exports*.<sup>51</sup> The arbitral tribunal found that the amicable settlement provision, which required the parties to negotiate for three months prior to commencing arbitration, was too uncertain to be enforceable as a matter of law. The arbitral tribunal concluded that it was not a condition precedent to the commencement of the arbitration. Emirates Trading challenged the jurisdiction of the arbitral tribunal appointed to resolve the parties' dispute because the three-month period for friendly discussions had not taken place. However, as Emirates Trading had not challenged the decision of the arbitral tribunal within the time limits required under the Arbitration Act 1996, the decision became binding on the parties and Popplewell J was therefore able to avoid expressing any view on the issue of whether the clause created a condition precedent.

## VI. CONCLUSIONS

### **Does a bare agreement to negotiate in good faith or attempt amicable settlement create an enforceable obligation?**

The majority of English authorities suggest that a bare agreement to negotiate in good faith is unenforceable. In *Wah v Grant Thornton*<sup>52</sup> Hildyard J stated that: "Agreements to agree and agreements to negotiate in good faith, without more, must be taken to be unenforceable." Teare J's view in *Emirates Trading*<sup>53</sup> was that a time limit was necessary in order to make the agreement to negotiate complete. However, the question may be asked why is a time limit necessary? In contracts for the sale of goods the question of what is a reasonable time for delivery of goods can be determined by the courts.<sup>54</sup> One may therefore question why a reasonable time cannot be implied into the agreement? If the courts wish to give effect to the parties' intentions then this may well be the next step.

There is also a fundamental difference between an agreement to agree and an agreement to negotiate. An agreement to agree prevents a contract coming into existence, whereas an agreement to negotiate is a stage in the dispute resolution process of a contract – *Aiton Australia Pty Ltd v Transfield Pty Ltd*.<sup>55</sup> Furthermore, the parties do not warrant by their agreement to negotiate that they will enter into a settlement agreement –

<sup>50</sup> [2015] EWHC 1452 (Comm).

<sup>51</sup> [2014] EWHC 2104 (Comm); [2014] 2 Lloyd's Rep 457; [2015] 1 WLR 1145.

<sup>52</sup> [2012] EWHC 3198 (Ch) at paragraph 57.

<sup>53</sup> [2014] EWHC 2104 (Comm); [2014] 2 Lloyd's Rep 457; [2015] 1 WLR 1145.

<sup>54</sup> Sale of Goods Act 1979 section 29(3).

<sup>55</sup> [1999] NSWSC 996; (1999) 153 FLR 236.

they simply warrant that they will attempt the process of settlement. Is this really so different from a best endeavours clause or a reasonable endeavours clause? Lord Wright in *Hillas & Co Ltd v Arcos Ltd*<sup>56</sup> gave the following opinion:

“If, however, what is meant is that the parties agree to negotiate in the hope of effecting a valid contract, the position is different. There is then no bargain except to negotiate, and negotiations may be fruitless and end without any contract ensuing: yet even then, in strict theory, there is a contract (if there is good consideration) to negotiate, though in the event of repudiation by one party the damages may be nominal, unless a jury think that the opportunity to negotiate was of some appreciable value to the injured party.”

The case is often cited and recently Carnworth LJ in the Court of Appeal stated that the case helped the claimant “to the extent that they show how little straw the Court may need, in particular commercial contexts, to make the bricks necessary for an enforceable contract.”<sup>57</sup> One then has to consider whether a court or arbitrator can fill a gap in a good faith negotiation clause by using the concept of reasonableness? Cases such as *Hillas v Arcos*<sup>58</sup> are to be compared with cases where the court finds that a form of words is too vague to be saved even with the use of the concept of reasonableness, see *Scammell (G) & Nephew Ltd v Ouston*<sup>59</sup> and *Durham Tees Valley Airport Ltd v BMI Baby Ltd*.<sup>60</sup> The distinction between these two situations is whether there exist objective criteria against which a court would be able to assess reasonableness on an objective basis. In *Globe Motors Inc v TRW Lucasvarity Electric Steering Ltd*<sup>61</sup> Mackie J upheld a bare agree to negotiate; however, his decision was based on the fact that the contract was for a long term with an express duty to collaborate. English case law on this point appears to be at odds with a number of other jurisdictions where bare agreements to negotiate are more frequently upheld.<sup>62</sup>

### **Does a time limited obligation to negotiate create an enforceable obligation?**

Teare J in *Emirates Trading* was of the opinion that the inclusion of a time limited obligation into a bare agreement to negotiate in good faith was enough to complete the agreement. However, if this decision is followed

<sup>56</sup> (HL) [1932] LI L Rep 359, 369.

<sup>57</sup> *iSOFT Group plc v Misys Holdings Ltd* (CA) [2003] EWCA Civ 229 at paragraph 26.

<sup>58</sup> (HL) [1932] LI L Rep 359, 369.

<sup>59</sup> [1941] AC 251; [1941] 1 All ER 14.

<sup>60</sup> [2009] EWHC 852 (Ch); [2009] 2 Lloyd’s Rep 246; [2009] 2 All ER (Comm) 1083; [2009] All ER (D) 233.

<sup>61</sup> [2012] EWHC 3134 (QB).

<sup>62</sup> See, for example, *International Research Corp plc v Lufthansa Systems Asia Pacific Pte Ltd* [2012] SGHC 226; and *HSBC Institutional Trust Services (Singapore) Ltd v Toshin Development Singapore Pte Ltd* [2012] SGCA 48; *HIM Portland LLC v DeVito Builders Inc* 317 F.3d 41,42 (1st Cir 2003) and *Weekley Homes Inc v Jennings* 936 SW 2d 16, 18 (Tex App 1996) and Berger, Klaus P, “Law and Practice of Escalation Clauses”, *Arbitration International*, Volume 22 Issue 1 (2006), at p 5.

then the result would be that a time limited good faith negotiation clause would be enforceable but a time limited mediation or other ADR clause may not. The test which the courts apply to decide whether an ADR clause is enforceable is whether (a) the form of process is certain; (b) there is a process for selecting a party to resolve the dispute; and (c) the detail of the procedure is certain. There now seems to be a move towards upholding amicable settlement clauses where there is a time related provision within it.

In a recent unreported arbitration, the arbitral tribunal held that the amicable settlement provisions at sub-clause 20.5 of a FIDIC contract were a condition precedent. The tribunal therefore concluded that it did not have jurisdiction to proceed with the arbitration in the absence of an attempt to settle the dispute.<sup>63</sup> The IBA Arbitration Guide for the Middle East similarly states that:

“Where mandatory pre-conditions to arbitration are not followed, a respondent may argue that the claim is inadmissible and that a constituted tribunal does not have jurisdiction to hear the dispute. Awards made notwithstanding a claimant’s failure to follow the pre-conditions may be annulled by the courts.”

In ICC Interim Award in Case 14431<sup>64</sup> the arbitral tribunal had to consider whether it should stay the arbitration proceedings to allow the ADR process to be undertaken or dismiss the claims. The seat of the arbitration was Switzerland. The arbitral tribunal referred to a number of leading jurists<sup>65</sup> who considered that a stay could be granted and held: “As both solutions are possible, it falls within the Arbitral Tribunal’s discretion to determine the adequate solution.” A similar situation occurred in an unreported arbitration in Dubai where the arbitral tribunal suspended the arbitration until the amicable settlement procedure had been undertaken.

Case law indicates that sub-clause 20.5 of the FIDIC contracts is often considered to be a condition precedent to arbitration and that if a party commences an arbitration without waiting 56 days, the arbitral tribunal may lack jurisdiction. However, for the reasons set out hereafter, I consider this conclusion to be open to doubt as a matter of English law. The decisions to uphold amicable settlement clauses are a result of policy decisions. There is no legislative basis for enforcing dispute resolution clauses otherwise than those which provide for arbitration.

<sup>63</sup> However, see contra *Emirates Trading Agency LLC v Sociedade de Fomento Industrial Private Ltd* (above).

<sup>64</sup> *ICC Dispute Resolution Bulletin* (2015) No 1 at page 35.

<sup>65</sup> Voser N, “Enforcement of Multi-tiered Dispute Resolution Clauses by National Courts and Arbitral Tribunals - the Civil Law Approach”, revised version of the paper presented at the IBA Conference in Durban, December 2002, p 7; Voser and Ettlinger, Swiss report to the 2001 IBA Conference in Cancún, in: *Arbitration and ADR, Enforcement of Multi-Tiered Dispute Resolution Clauses*, pp 23/24; and Poudret/Besson, *Comparative Law of International Arbitration*, 2nd Edition, London/Zurich 2007 (translated by Stephen V Berti and Annette Ponti), pp 12/13.

**Should an amicable settlement clause (such as FIDIC’s sub-clause 20.5) be a condition precedent to arbitration?**

Under English law the mere fact that the words “condition precedent” are not used is immaterial. Courts and arbitrators should look at the intent of the wording. There is authority that: “it is not essential that the very words ‘condition precedent’ be used ... Other words can be used, if they are clear”: *Eagle Star Insurance Company Ltd v Cresswell*.<sup>66</sup> In *Bremer Handelsgesellschaft MBH v Vanden Avenne Izegem PVBA*<sup>67</sup> the House of Lords stated that a notice provision was unlikely to be a condition precedent unless it prescribed a specific time for delivery of the notice and makes plain the consequences of the failure to serve the notice. The principles set out in *Bremer v Vanden* should equally apply to amicable settlement clauses; however, there is little case law on this issue. This gives rise to a distinction between obligations and conditions precedent.

Sub-clause 20.5 of the FIDIC 1999 contracts is not framed as a condition precedent in that it does not state the consequences of a failure to negotiate for a period of 56 days. Sub-clause 20.6 provides that:

“Unless settled amicably, any dispute in respect of which a DAB’s decision (if any) has not become final and binding may be settled by international arbitration.”

There is therefore nothing that sets out the consequences of the failure to comply and therefore the presumption should be that sub-clause 20.5 does not create a condition precedent. In *Emirates Trading*<sup>68</sup> Teare J referred to the good faith negotiation clause in that contract as a condition precedent to arbitration.<sup>69</sup> With respect to the learned judge, this conclusion may be doubted. The obligation to negotiate for a limited period of time is better described as a procedural obligation, the breach of which sounds in damages (if appropriate) or can be sanctioned by an adverse costs order. This accords with the dicta of Lord Wright in *Hillas v Arcos*.<sup>70</sup>

**The difference between arbitration and litigation**

The courts have an inherent jurisdiction to stay cases and refer them to ADR or require that the parties carry out a contractual obligation to negotiate. In *DGT Steel and Cladding Ltd v Cubitt Building and Interiors Ltd*<sup>71</sup> the court stayed the litigation where there was an agreement to adjudicate.

<sup>66</sup> (CA) [2004] EWCA Civ 602; [2004] Lloyd’s Rep IR 537, [2004] 2 All ER (Comm) 244.

<sup>67</sup> (HL) [1978] 2 Lloyd’s Rep 109.

<sup>68</sup> [2014] EWHC 2104 (Comm); [2014] 2 Lloyd’s Rep 457; [2015] 1 WLR 1145.

<sup>69</sup> *Ibid* at paragraph 73.

<sup>70</sup> (HL) [1932] LI L Rep 359, 369.

<sup>71</sup> [2007] EWHC 1584 (TCC); [2007] BLR 371; 116 Con LR 118 and *Cape Durasteel Ltd v Rosser and Russell Building Services Ltd* [1995] 46 Con LR 75.

Similarly in *Peterborough City Council v Enterprise Managed Services Ltd*<sup>72</sup> the court exercised its inherent jurisdiction and stayed the case because the parties had not gone through the adjudication and amicable settlement procedures imposed by the contract, which was a FIDIC Silver Book. However, arbitration is different. If the arbitral tribunal does not have jurisdiction because a condition precedent has not been met it cannot retrospectively be given jurisdiction by staying the arbitration and requiring the parties to comply with the ADR process. This would be a classic case of pulling oneself up by their own bootstraps. The position is, however, different in other jurisdictions as illustrated in the ICC Interim Award in Case 14431.<sup>73</sup>

As a matter of policy the courts should not uphold challenges to the jurisdiction of an arbitral tribunal where one party has failed to enter into good faith negotiations. While negotiations are to be encouraged it would, I suggest, be absurd if an arbitration award is overturned simply because the parties have failed to discuss their dispute, for example, over a two-week period. In the *Emirates Trading Agency v Sociedade de Fomento* case<sup>74</sup> the arbitral tribunal found that the time limited good faith negotiation clause was not a condition precedent to the commencement of arbitration. Popplewell J made no comment on this issue. If amicable settlement clauses or good faith negotiation clauses are to be treated as conditions precedent to arbitration then clear words are needed setting out the consequences of a failure to comply with the obligation.

### **Hindrance, prevention and refusal to negotiate**

A further question that arises is whether a party is entitled to commence an arbitration where one party refuses to enter into negotiations? The question of hindrance and prevention under a FIDIC 4th Edition contract was recently considered by the courts in *Al-Waddan Hotel Ltd v Man Enterprise SAL (Offshore)*.<sup>75</sup> In this case HHJ Mark Raeside QC was asked to consider whether an arbitral tribunal had jurisdiction where an engineer had failed to issue a decision under clause 67.1 of the contract. HHJ Mark Raeside QC referred to the *Panamena Europea Navigacion (Compania Limitada) v Frederick Leyland & Co Ltd*<sup>76</sup> case and stated that where a party intends:<sup>77</sup>

<sup>72</sup> [2014] EWHC 3193 (TCC); [2014] BLR 735.

<sup>73</sup> *ICC Dispute Resolution Bulletin* (2015) No 1 at page 35. See also *Hooper Baile Associated Ltd v Natcon Group Pty Ltd* [1992] 28 NSWLR 194 where Giles J in the New South Wales Supreme Court stayed arbitration proceedings until the conclusion of conciliation proceedings.

<sup>74</sup> [2015] EWHC 1452 (Comm). See also *ICC Cases 16155* and *18505* reported by Seppälä C, “Commentary on Recent ICC Arbitral Awards dealing with Dispute Adjudication Boards under FIDIC Contracts”, *ICC Dispute Resolution Bulletin*, 2015 Issue 1.

<sup>75</sup> [2014] EWHC 4796 (TCC).

<sup>76</sup> [1947] AC 428.

<sup>77</sup> [2014] EWHC 4796 (TCC) at paragraph 53.

“to rely on the non-performance of a condition precedent he must do nothing to prevent the condition from being performed, and if there is anything that must be done by him to render possible the performance of the condition, a failure by him to do what is required disentitles him from insisting on performance of the condition.”

He then rhetorically asked the question why one party could simply not wait until the time for issuing a decision had elapsed and then commence arbitration. The learned judge set out two situations where a condition precedent would no longer be binding. First, referring to *Shell UK Ltd v Lostock Garages Ltd*,<sup>78</sup> the learned judge stated that if there was a “clear” and “absolute” refusal to perform a contractual function then both parties can proceed with the certain knowledge that this contractual requirement no longer binds them. However, the position of one party must be absolute and unequivocal if a party sought to escape from a condition precedent. Secondly, a party could be excused where there was hindrance and prevention by the other party. In this case a failure to appoint a new engineer.

Applying these observations to a time limited amicable settlement clause it would appear that if the clause is a condition precedent then a party may avoid having to wait 56 days before commencing arbitration if the other party shows an absolute and clear intention not to engage in amicable settlement discussions.

### **Summary**

The English courts have recently elected to uphold good faith negotiation clauses coupled with a time limited obligation. This is a trend which follows behind Australia, Singapore and the US. Similarly, there appear to be more cases where arbitral tribunals are finding that they lack jurisdiction where the parties have not gone through an amicable settlement process, such as sub-clause 20.5 of FIDIC. Although there is a logic to the courts staying cases under their inherent jurisdiction where parties have not complied with the amicable settlement provisions the same logic does not apply to arbitrations. Most amicable settlement clauses such as sub-clause 20.5 are not drafted in the form of conditions precedent and to hold them as such can lead to a significant amount of wasted costs and delay in the resolution of disputes.

<sup>78</sup> [1976] 1 WLR 1187; [1977] 1 All ER 481.