FIDIC's Sub-Clause 20.5 – A Condition Precedent to Arbitration

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The 1999 FIDIC forms of contract contain a number of obligations and/or conditions precedent that require (a) a party to give notice of a claim (Sub-Clauses 20.1 and 2.5); (b) refer the claim to the Engineer (Sub-Clauses 20.1 and 3.5); and (c) 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[1]:

"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."

There has been some question whether the above clause creates two distinct obligations or whether it creates a single obligation. The two distinct obligations may be stated as: (1) an obligation to attempt to settle the dispute amicably; and (2) an obligation to wait 56 days before commencing arbitration. Those who consider Sub-Clause 20.5 as creating two obligations acknowledge that the obligation to negotiate is not a condition precedent to arbitration but assert that the obligation to wait 56 days is. Those who take the view that there is a single obligation consider that the 56-day period is simply part of the obligation to negotiate amicably and that as negotiation clauses are generally unenforceable so is the obligation to wait 56 days before commencing arbitration. This was shown in the recent case of *Emirates Trading Agency Llc v Sociedade de Fomento Industrial Private Ltd*[2] where the arbitral tribunal held that a time related amicable settlement clause did not create a condition precedent to arbitration and that the arbitral tribunal had jurisdiction even though one of the parties had commenced the arbitration prematurely.

A Condition Precedent

Sub-Clause 20.5 of the FIDIC forms is not drafted as a condition precedent. "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 & Ors*[3]. In *Bremer Handelsgesellschaft MBH v Vanden Avenne Izegem PVBA*[4] the House of Lords held 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.

Sub-Clause 20.5 of the FIDIC 1999 contracts does not state the consequences of a failure to negotiate for a period of 56 days; i.e. it does not state that any arbitration commenced before the 56-day period shall be void or invalid. It may therefore be argued that the presumption should be that Sub-Clause 20.5 does not create a condition precedent. 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 – see *Hillas v Arcos*[5]. If the FIDIC drafters had intended that Sub-Clause 20.5 should have the consequences of preventing a party from commencing arbitration, then this could have easily been spelt out by them in the same way as they spelt out the consequences of not issuing a Sub-Clause 20.1 notice.

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The alternative view, however, is that the intention is clear enough. As Edward Corbett explains[6], a failure by a party to attempt to settle the dispute amicably would appear not to be a breach of contract. However, the right to commence arbitration "...must be subject to clause 67.2 and the 56-day amicable settlement period provided for there." Like many other commentators, Edward Corbett considers the 56-day time period a distinct obligation and one which is intended to be binding on the parties. These commentators consider that this type of clause is no different to a clause which prevents arbitration from being commenced until after practical completion of the works or delivery of goods.

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. This was still the position in the early 1990s when in *Walford v Miles*[7] Lord Ackner concluded that good faith negotiation clauses were not binding under English law and held[8]:

"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.

Historically, amicable settlement clauses and mediation clauses have been held to be different from clauses which require 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[9], or to an adjudicator[10], or to an expert[11] have been upheld as conditions precedent to the commencement of the arbitration.

A Change in Attitude

The English courts in the late 1990s began to question the orthodoxy that mediations clause had "no legal content". In 1997, in *Bernhard's Rugby Landscapes v Stockley Park*[12], HHJ Lloyd QC recognised a change in attitude to ADR and stated that: "There is now a tide running in favour of alternative forms of dispute resolution prior to recourse to litigation." In 2002, Colman J. (as he then was) approached the question of whether a mediation clause was enforceable by reference to three criteria. His lordship found that: (1) there must be 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[13]. Similarly, in *Holloway & Anor v Chancery Mead Ltd*[14], Ramsey J re-affirmed that a mediation clause would be enforceable if certain criteria were met. This reasoning of Ramsey J has subsequently been approved by the Court of Appeal and is now considered the orthodox view.

In the recent case of *Emirates Trading Agency Llc v Prime Mineral Exports Private Ltd*[15] the English High Court re-considered the question whether amicable settlement clauses was a condition precedent. Clause 11.1 of the contract stated:

"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

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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." [emphasis added]

Teare J. examined in depth the decision of Alsopp P. in *United Group Rail Services v Rail Corporation New South Wales*[16]. 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. stated:[17]

"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.[18] Teare J., in *Emirates Trading*, applied the reasoning of Alsopp P. His lordship proceeded to state that in conducting negotiations there must be imported an obligation to seek to do so in good faith.[19]

One of the main issues addressed in *Emirates Trading*[20] related to the 4 week period in which the negotiations were to take place. The claimant's counsel argued that the 4 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[21]. Teare J. considered this provision important because the reference to a period of 4 continuous weeks ensures that a defaulting party cannot postpone the commencement of arbitration indefinitely. In conclusion Teare J. held:[22] "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." Having reviewed the good faith negotiation clause in detail, and in particular the use of the word shall, Teare J held[23]:

"I accept that the first part of clause 11.1 provides that before a party can refer a claim to arbitration there must be friendly discussions to resolve the claim. Such friendly discussions are a condition precedent to the right to refer a claim to arbitration."

Conclusion

It now seems to be settled that an English court would find that an amicable settlement clause, such Sub-Clause 20.5 of the FIDIC forms, is a condition precedent to the commencement of arbitration. The High Court in Emirates Trading was clear that a good faith negotiation clause coupled with a time limited obligation was a condition precedent, which needed to be complied with prior to the commencement of arbitration. The English courts are now in line with the courts in Australia, Singapore, the United States and many civil law countries. Similarly, there appears to be more and more arbitrations 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.

1 This provision is found in the Red, Yellow and Silver Books

2 [2015] EWHC 1452

3 [2004] EWCA Civ 602

4 [1978] 2 Lloyd's Rep 109

5 [1932] Lloyd's List LR 359, 369

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6 FIDIC 4th A Practical Legal Guide, Corbett E., Sweet and Maxwell (1991) at page 449.

7 [1992] 1 All ER 453

8 Ibid at 460

9 J T Mackley & Company Ltd v Gosport Marina Ltd [2002] EWHC 1315 (TCC) (03 July 2002). In Al-Waddan Hotel Ltd v Man Enterprise SAL (Offshore) [2015] EWHC 4796 at [29-30] 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.

10 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)

11 Cott UK Ltd. v. FE Barber Ltd. [1997] 3 All ER 540

12 82 BLR 39 at 57

13 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."

14 [2007] EWHC 2495 (TCC) at para 84

15 [2014] EWHC 2104

16 (2009) 127 Con LR 202

17 (2009) 127 Con LR 202 at [74]

18 Ibid at [80]

19 Ibid at [51]

20 [2014] EWHC 2104

21 Ibid at [4]

22 Ibid at [52]

23 Ibid at [26].

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