MULTI-TIER DISPUTE RESOLUTION CLAUSES: DRAFTERS BEWARE

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This article considers a tension at the heart of this approach: the desire on the one hand to give effect to what the parties agreed, and the difficulty on the other hand in giving what they have agreed objective and legally controllable substance. In that context it explores the recent Court of Appeal decision in *Kajima Construction & Anor v Children's Ark Partnership Limited* [2023] EWCA Civ 292. That decision has made clear that, whilst the courts will endeavour to uphold parties' agreements, there are limits.

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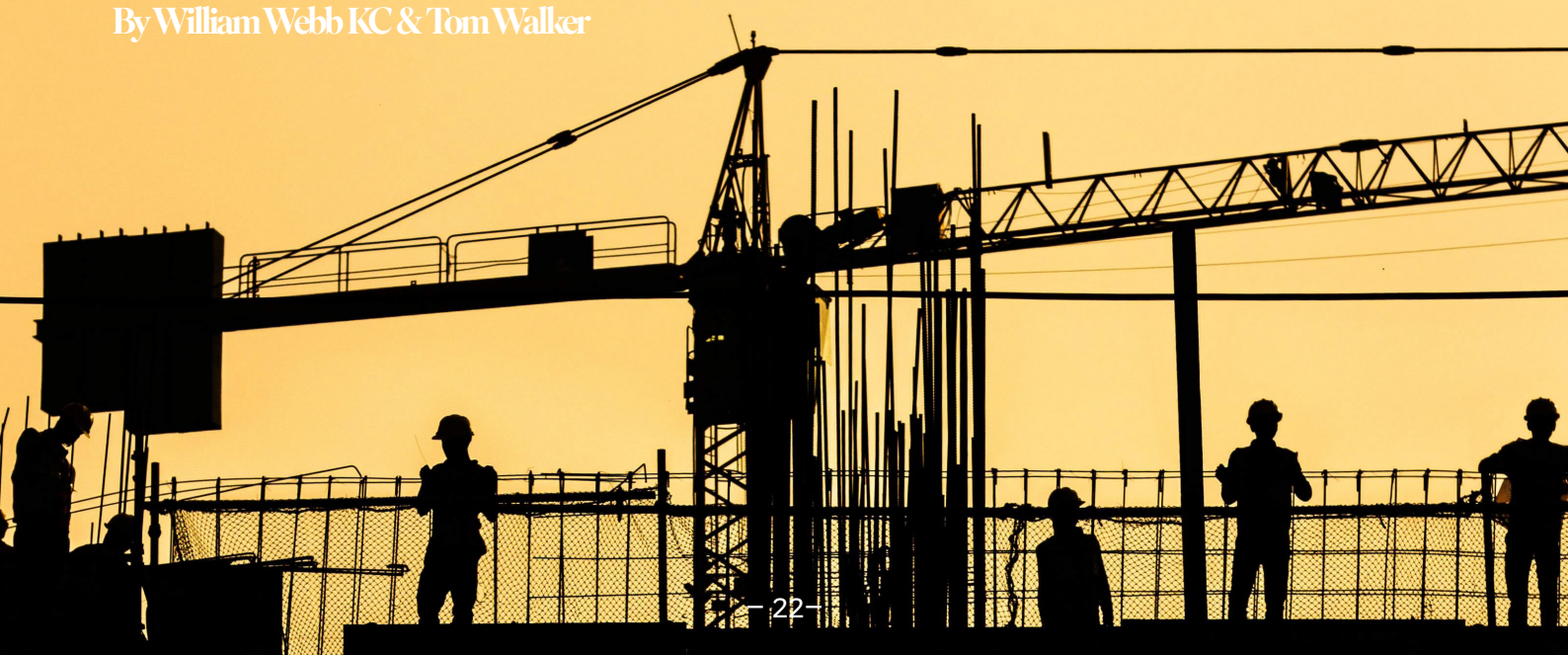

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Multi-tier dispute resolution clauses: Drafters beware

Multi-tier dispute resolution clauses are a familiar feature of construction contracts. They commonly provide that some stages of the dispute resolution mechanism are a condition precedent to starting formal proceedings. Where the condition involved a reference to an independent tribunal, such as an expert, a dispute board or an adjudicator, the courts have historically found little difficulty in upholding such a requirement by imposing a stay on the proceedings.

However, where the obligation is to engage in mediation or negotiation before proceeding to litigation or arbitration, the enforceability of such clauses has in the past been doubtful because they were said to do no more than express an aspiration to resolve the parties' dispute.

In more recent years the courts have taken a generally permissive approach; they have endeavoured to uphold the parties' agreement. However, the authorities also demonstrate a tension *"between the desire to give effect to what the parties agreed and the difficulty in giving what they have agreed objective and legally controllable substance" (Tang & Anor v Grant Thornton International Ltd & Ors* [2012] EWHC 3198 (Ch) at [56])). This tension was in stark display in the recent Court of Appeal decision in *Kajima Construction & Anor v Children's Ark Partnership Limited* [2023] EWCA Civ 292. This case illustrates that, whilst the courts will endeavour to uphold the parties' agreements, there are limits.

Historic hostility to agreements to negotiate

The enforceability of clauses providing that parties must first seek to negotiate or mediate before commencing proceedings was rendered doubtful by, in particular, two decisions: (1) *Courtney & Fairbairn Ltd v Tolaini Brothers (Hotels) Ltd* [1975] 1 WLR 297; and (2) *Walford v Miles* (1991) 62 P & CR 410.

The parties in Courtney & Fairbairn had agreed to *"negotiate fair and reasonable contract sums"* for building works. The Court of Appeal held that this was an unenforceable agreement. Lord Denning MR, giving the leading judgment, was concerned that it amounted to no more than an agreement to agree (at p301-2):

"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, is not a contract known to the law."

The view taken by the Court of Appeal in *Courtney & Fairbairn* was subsequently approved in *Walford v Miles*. This case concerned an agreement not to negotiate with any third party in respect of the prospective purchase of a photographic business (i.e. a 'lock-out' agreement). Mr and Mrs Miles had accepted an offer, subject to contract, to sell their photographic business to the Walford brothers. The price was to be 2 million pounds. In return for the Walfords obtaining a comfort letter from their bank indicating that it would finance the purchase, Mr and Mrs Miles agreed not to negotiate with other potential purchasers. Contrary to this agreement, they went on to sell the business to a third party. The Walfords made two claims for damages. The first was to recover the costs wasted on preparing contract documents. This was said to be £700. The second claim was for the loss of a bargain. Namely, the acquisition of the Miles' business for 2 million pounds when, according to the Walfords, it was worth 3 million pounds. In support of this argument, the Walfords argued that it was an implied term of the lock-out agreement that Mr Miles would continue to negotiate with them in good faith. There was also said to be a further implied term that the negotiations could only be terminated for an honest reason. Lord Ackner, with whom the other law lords agreed, gave this argument short shrift. A bare agreement to negotiate had no legal content. His reasons for this position were twofold. First, a duty to negotiate in good faith was said to be *"inherently repugnant to the adversarial position of the parties when involved in negotiations."* Secondly, such a duty was, in his view, *"unworkable in practice as it is inherently inconsistent with the position of a negotiating party"* (at [1992] 2 AC 128, 138C-H).

Walford v Miles has been the subject of sustained academic criticism (see, for example, A Mills and R Loveridge, *"The uncertain future of Walford v Miles"* [2011] LMCLQ 587). The principal complaint is that it offends a central aim of English commercial law, namely, to uphold parties' agreements.

This aim has been eloquently expressed by Sir Robert Goff (R Goff, *"Commercial Contracts and the Commercial Court"* [1984] LMCLQ 382, 391):

"Our only desire is to give sensible commercial effect to the transaction. We are there to help businessmen, not to hinder them: we are there to give effect to their transaction, not to frustrate them: we are there to oil the wheels of commerce, not to put a spanner in the works, or even grit in the oil."

It follows that the role of the court is to give effect to what the parties have agreed. The court should not *"throw its hands in the air and refuse to do so because the parties have not made its task easy" (Openwork Ltd v Forte* [2018] EWCA Civ 783 at [27]). Accordingly, where parties intend a clause to create a legal obligation, freedom of contract dictates that the court should endeavour to give legal effect to that intention. To hold that a clause is too uncertain to be unenforceable is, in Lord Denning's memorable words, *"a counsel of despair" (Nea Agrex SA v Baltic Shipping Co Ltd* [1976] 1 Q.B. 933, 943). It should be a last resort.

The permissive approach

Walford v Miles remains good law. However, in line with the criticism set out above, it has been treated as distinguishable in several subsequent cases. The thrust of these decisions is to confine *Walford v Miles* to situations in which there is a mere agreement to negotiate (i.e. where no process or standard is identified). These cases indicate a more permissive approach in which the courts endeavour to enforce the parties' agreement, provided certain minimum requirements are met.

Cable & Wireless Plc v IBM [2002] EWHC 2059 (Comm) is one such case. It considered a clause providing that:

"If the matter is not resolved through negotiation, the Parties shall attempt in good faith to resolve the dispute or claim through an Alternative Dispute Resolution (ADR) procedure as recommended to the parties by the Centre for Dispute Resolution. However, an ADR procedure which is being followed shall not prevent any Party or Local Party from issuing proceedings."

The court held that this clause was enforceable. In so doing, it emphasised the importance of upholding the parties' agreement. Distinguishing the case before it from *Walford v Miles*, the court emphasised that the parties had gone further than a mere agreement to negotiate. They had identified a specific process: *"Resort to*

CEDR and participation in its recommended procedure are, in my judgment, engagements of sufficient certainty for a court readily to ascertain whether they have been complied with" (at p1326). The court emphasised the importance of upholding the parties' agreement: "*English courts should nowadays not be astute to accentuate uncertainty (and therefore unenforceability) in the field of dispute resolution references"* (at p1326).

In *Holloway v Chancery Mead Ltd* [2007] EWHC 2495 (TCC) Ramsey J set out the minimum requirements for a dispute resolution clause to be enforceable (at [81]):

"It seems to me that considering the above authorities the principles to be derived are that the ADR clause must meet at least the following three requirements: 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 or at least a model of the process should be set out so that the detail of the process is sufficiently certain."

Similarly, in Tang Hildyard J stated (at [60]):

"In the context of a positive obligation to attempt to resolve a dispute or difference amicably before referring a matter to arbitration or bringing proceedings the test is whether the provision prescribes, without the need for further agreement, (a) a sufficiently certain and unequivocal commitment to commence a process (b) from which may be discerned what steps each party is required to take to put the process in place and which is (c) sufficiently clearly defined to enable the court to determine objectively (i) what under that process is the minimum required of the parties to the dispute in terms of their participation in it and (ii) when or how the process will be exhausted or properly terminable without breach."

Sulamérica Cia Nacional de Seuros SA and others v Enesa Engelharia SA and others [2012] EWCA Civ 638 provides a contrasting example of a clause being too uncertain, despite the court's best efforts to give it legal force. The Court of Appeal considered a clause requiring the parties to seek to resolve their dispute amicably by mediation prior to commencing arbitration. It noted that there was little doubt that the parties had intended to create an enforceable obligation. Accordingly, "*the court should be slow to hold they failed to do so"* (at [35]). Nonetheless, the clause was held to be too uncertain to be enforceable: "*... in order for any agreement to be effective in law it must define the parties' rights and obligations with sufficient certainty to enable it to be enforced"* (at [35]). Contrary to this, the clause in question provided no defined mediation process. Nor did it refer to the procedure of a specific mediation provider. Similarly, no provision was made for the process by which the mediation was to be undertaken. The clause was not apt to create an obligation to commence or participate in a mediation. At most, it imposed an obligation to invite the other side to join in an ad hoc mediation. However, the content of such a limited obligation would be too uncertain to be enforced (at [36]).

This line of authority was considered in *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd* [2014] EWHC 2104 (Comm). This case concerned a contract for the sale and purchase of iron ore. The contract's dispute resolution clause required the parties to "*first seek to resolve the dispute or claim by friendly discussion"* before commencing arbitration. Following a dispute between the parties, the seller commenced arbitration proceedings. The buyer contended that the arbitrators lacked jurisdiction on the basis that the condition precedent in the dispute resolution clause had not been complied with. There had been no attempt to resolve the dispute by friendly discussions. In response, the seller argued that the clause was too uncertain to be enforceable. Teare J rejected the seller's argument. In holding that the clause was enforceable, he noted (at [40]) that:

"[W]here commercial parties have entered into obligations they reasonably expect the courts to uphold those obligations. The decision in the Walford case arguably frustrates that expectation. For that reason there has been at least one clear indication that the decision in the Walford case may in appropriate circumstances be distinguished..."

Teare J distinguished the clause before him from the one considered in *Sulamérica*. In the absence of a named mediator or an agreed process whereby a mediator could be appointed, the agreement in *Sulamérica* was incomplete. However, an agreement to resolve a dispute by friendly discussions in good faith was not so incomplete (at [60]). Teare J concluded that (at [64]):

"...an obligation to seek to resolve a dispute by friendly discussions has an identifiable standard, namely, fair, honest and genuine discussions aimed at resolving a dispute. Difficulty of proving a breach in some cases should not be confused with a suggestion that a clause lacks certainty. In the context of a dispute resolution clause pursuant to which the parties have voluntarily accepted a restriction on their freedom not to negotiate it is not appropriate to suggest that the obligation is inconsistent with the position of a negotiating party.

Enforcement of such an agreement when found as part of a dispute resolution clause is in the public interest, first, because commercial men expect the court to enforce obligations which they have freely undertaken and, second, because the object of the agreement is to avoid what might otherwise be an expensive and time consuming arbitration."

Kajima Construction

Whilst the emphasis following *Walford v Miles* has been on upholding parties' agreements, the recent Court of Appeal decision in *Kajima Construction* highlights that there are limits.

Kajima Construction concerned a fire defects claim. On 10 June 2004 Children's Ark Partnership Limited (**"CAP"**) was engaged to design, build, and finance the redevelopment of the Royal Alexandra Hospital for Sick Children (**the "Project Agreement"**). CAP engaged Kajima Construction Europe (UK) Limited to design, construct, and commission the hospital (**the "Construction Contract"**). CAP subsequently entered into a deed of guarantee with the second appellant, Kajima Europe (collectively **"Kajima"**), by which the second appellant agreed to guarantee the due and punctual performance by Kajima Construction of each and all of its duties or obligations to CAP under the Construction Contract. Schedule 26 of the Construction Contract included a dispute resolution procedure in the following terms:

"3.1 Subject to paragraph 2 and 6 of this Schedule, all Disputes shall first be referred to the Liaison Committee for resolution. Any decision of the Liaison Committee shall be final and binding unless the parties otherwise agree.

3.2 Where a Dispute is a Construction Dispute the Liaison Committee will convene and seek to resolve the Dispute within ten (10) Business Days of the referral of the Dispute."

Schedule 26 did not itself define "Liaison Committee". This was instead defined in Schedule 1 as "...the committee referred to in clause 12 (Liaison Committee) of the Project Agreement". Clause 12 of the Project Agreement provided, in relevant part, as follows:

"12.1 The Trust and Project Co shall establish and maintain throughout the Project Term a joint liaison committee (the "Liaison Committee"), consisting of three (3) representatives of the Trust (one of whom shall be appointed Chairman) and three (3) representatives of Project Co which shall have the functions described below.

12.2 The functions of the Liaison Committee shall be:

...

(c) in certain circumstances, pursuant to Schedule 26 (Dispute Resolution Procedure), to provide a means of resolving disputes or disagreements between the parties amicably."

Following the Grenfell Tower tragedy in 2017, defects were identified in respect of the cladding and fire stopping works at the hospital. CAP issued proceedings on 21

December 2021. Kajima applied to strike out the claim on the basis that CAP had not complied with the dispute resolution clause.

At first instance Joanna Smith J dismissed the strike out application and granted CAP's cross-application for a stay. She held that, whilst the dispute resolution clause gave rise to a condition precedent, it was unenforceable.

Joanna Smith J's decision was upheld on appeal. Coulson LJ delivered the lead judgment and considered that various factors pointed to the dispute resolution procedure being unenforceable. In particular, the competing interpretations of the reference to *"the parties"* in paragraph 3.1 of Schedule 26 of the Construction Contract were both unworkable.

Kajima argued that *"the parties"* was a reference to the Trust and CAP, not Kajima. However, that would mean that Kajima had to take part in a process the result of which it would not be bound by. That made no commercial sense (at [50]). The alternative interpretation that it was a reference to CAP and Kajima produced a further set of difficulties. Kajima would be bound by the decision of the Liaison Committee, on which it had no representative, whose meetings it had no right to attend, whom it could not make representations to and whose documents it was not entitled to see. This could not possibly lead to the *"amicable settlement"* identified as an outcome of the provisions (at [51]). In the circumstances, the Court of Appeal saw the force in Kajima's submission that actual, or at least perceived, bias would be inherent in the process (at [52]). Accordingly, it concluded that the Liaison Committee was a fundamentally flawed body. It could neither resolve a dispute involving Kajima *"amicably"*, nor could it fairly provide a decision binding in any event (at [53]). It was *"pointless"* (at [50]).

The process prescribed by the dispute resolution procedure was also too uncertain. It was not at all clear when the condition precedent might be satisfied. For example, it was impossible to see what, if any, minimum participation was required. The Court of Appeal noted that if, as was suggested by Children's Ark, Kajima's minimum duty was non-existent or zero, that could hardly represent an effective dispute resolution process (at [56]). Further, whilst Schedule 26 required the Liaison Committee to try to resolve the dispute within ten days of referral, the Project Agreement allowed them 10 days' notice before they even had a meeting. Accordingly, the process could be over before it had even begun (at [57]).

Further, it was not possible to render the dispute resolution procedure enforceable by looking at the parts that could work in isolation.

It was necessary for the court to treat the process as a whole to see whether or not it was enforceable. It was not permissible to rely on some terms and disavow others in an attempt to produce an enforceable procedure (at [70] to [71]).

In reaching its conclusions, the Court of Appeal emphasised that, whilst the court must endeavour to enforce the agreement between the parties, it should not overstrain itself to do so, so as to arrive at an artificial result (at [70]). It also concluded that it was permissible for the court to have a *"weather eye to the utility"* of a dispute resolution procedure (at [74]).

It can, however, be noted that Popplewell LJ formed a somewhat different view to the majority of the Court of Appeal. He considered that there was a construction of the clause which would render it sufficiently certain to be effective and enforceable – namely that it was only the commencement of the DRP process which was required (at [130]) with a wide ranging appeal to business common sense being used to create an effective process thereafter (at [125-127]). However, this construction was not one which had been reached by the trial judge or advanced by Kajima. Therefore, it was not covered by the grounds of appeal such that Popplewell LJ ultimately considered himself constrained to concur with the majority in terms of the outcome (at [132]).

It could be said that Popplewell LJ's judgment is most in line with the general trend towards straining to enforce the parties' agreements wherever possible, no matter how poorly worded. However, it also highlights the difficulties with that approach in this particular context. Where a clause is a condition precedent to litigation, the parties need to be able to act in reliance upon a clause in order to preserve their legal rights. However, where the requirements of the clause are vague or absurd, it may be more appropriate for the courts to simply set the clause aside than seek to use business common sense to glean a meaning which may not have been foreseen by either party.

This may explain why the courts appear more willing to strike down as ineffective unclear conditions precedent to litigation than other contract terms, and may explain why the majority of the Court of Appeal in this case differed from Popplewell LJ's analysis.

Concluding thoughts

The trend since *Walford v Miles* has been for the courts to endeavour to enforce dispute resolution clauses. However, *Kajima Construction* has provided a salutary shot across the bows for contract drafters. The Court of Appeal has made clear that there are limits to how far the court will indulge the parties' agreement. The court will not *"overstrain itself"* to arrive at an artificial result. It will also have an eye to whether enforcing the clause would be pointless. Drafters are, therefore, well advised to not only provide a sufficiently detailed process, but also one that has a clear utility.