

MULTI-STEP DISPUTE RESOLUTION CLAUSES

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I. INTRODUCTION

It is increasingly common for parties who agree to include an arbitration clause in a contract to establish an obligation to negotiate before commencing arbitration proceedings. These obligations are referred to as “escalation clauses,” “multi-tier clauses,” or “multi-step alternative dispute resolution clauses.”¹

In essence, if a party wishes to start arbitration proceedings, it must first negotiate with the other party in order to try to reach an amicable solution to the dispute² (hence the reason why these clauses are said to have a “filtering” effect).

These clauses come in many forms. Some are extremely simple (e.g., when the parties undertake, before starting arbitration, to “use their best efforts to reach an agreement”), whereas others are more complex and establish a maximum term for the negotiations, name the individuals who will participate in the negotiation (e.g., the CEO, General Manager), and others even state the number of meetings that must be held.³

¹ D. JASON FILE, “*United States: Multistep Dispute Resolution Clauses*”, 3 MEDIATION COMMITTEE NEWSLETTER 1 (IBA Legal Practice Division), July 2007, at p. 36.

² DAVID ST JOHN SUTTON, JUDITH GILL & MATTHEW GEARING, RUSSELL ON ARBITRATION (2007), at p. 48

³ See FILE, *supra* note 1, at p. 33.

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The purpose of the multi-tier clause is clear: to require the aggrieved party to inform the other party of the existence of a controversy, providing an opportunity for the situation to be resolved outside arbitration, thereby avoiding the financial costs and delays involved in the arbitration process.⁴ Failing this, the clause may also serve to provide the respondent with an opportunity to prepare its defense better if a negotiated solution cannot be reached.⁵

In short, these clauses allow the parties to reflect on the facts that gave rise to the dispute and explore the possibilities of reaching an amicable resolution.

These clauses could have significant importance for the parties at a later stage: the parties entering into an agreement that includes an obligation to negotiate may have a strong interest in being able to resolve their disputes without having to resort to arbitration. It is clear that the time, expenses and reputational burdens associated with arbitration far exceed the costs of negotiation. Consequently, the parties should be mindful about the inclusion of a negotiation clause in the agreement.

Negotiation clauses raise many questions. What are the effects of disregarding the clause? Does the arbitral tribunal have jurisdiction if the clause has been breached? Can the breach be remedied? Can a party be compelled to comply with the clause? Can an arbitral award be set aside for failure to comply with the clause? The remainder of this article seeks to provide answers to these and other questions.

Finally, it is important to mention that although Spanish legal scholars and case law have examined similar concepts (such as the failure to exhaust administrative remedies, which is referred to in former article 533.7 of the Spanish Code of Civil Procedure of 1881, and the mandatory labor conciliation under article 63 of the Labor Procedure Act), these issues have not been explored in an arbitration context. However, there has been an intense debate on this

⁴ See Judgment of March 16, 1989, rendered by the Spanish Constitutional Court (RTC 1989/60), in which the Spanish Constitutional Court analyzed the purpose of the requirement to exhaust administrative remedies, which is somewhat analogous to the negotiation clause.

⁵ See Judgment of June 9, 1988, Spanish Supreme Court [Tribunal Supremo] (RJ 1988/5259), a decision that also refers to the exhaustion of administrative remedies.

issue in the courts and among legal scholars in the United States, giving rise to a number of contradictory decisions, which will be discussed below.

II. NATURE OF THE MULTI-STEP DISPUTE RESOLUTION CLAUSE

The multi-step dispute resolution clause can be considered as: (a) a condition precedent to the commencement of arbitration, (b) a procedural requirement for arbitration, or (c) a procedural step that ought to be followed for a party's own benefit ("*carga procesal*").

The legal nature of the clause has relevant consequences on matters such as whether the clause may be enforced or whether a breach may be remedied, so this preliminary question must be resolved before reaching any conclusions regarding these issues.

On one side of the debate are those who believe that the clause bars recourse to arbitration until the negotiation process has been complied with, and is therefore a type of condition precedent. This position is particularly popular among U.S. courts when the parties clearly desire to establish the obligation as such. The clause has similarly been considered to be a *pactum de non petendo*, a temporary waiver of the right to commence arbitration until negotiation has ended.⁶

In *HIM Portland LLC v. DeVito Builders Inc.*,⁷ the First Circuit Court of Appeals held that:

.. [u]nder the plain language of the contract, the arbitration provision is not triggered until one of the parties requests mediation. Consequently, because neither party ever attempted to mediate this dispute, neither party can be compelled to submit to arbitration.

Likewise, in *Weekly Homes Inc. v. Jennings*,⁸ the Texas Court of Appeals held that:

The trial court correctly interpreted the contractual language to require satisfaction of the provisions of the mandatory negotiation clause as a condition precedent to arbitration, and correctly determined that this

⁶ See KLAUS P. BERGER, "Law and Practice of Escalation Clauses," 22 ARBITRATION INTERNATIONAL 1 (2006), at p. 5.

⁷ *HIM Portland LLC v. DeVito Builders Inc.*, 317 F.3d 41,42 (1st Cir. 2003).

⁸ *Weekly Homes Inc. v. Jennings*, 936 SW 2d 16, 18 (Tex. App. 1996).

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arbitrability issue was one for the courts to determine, not the arbitration. Although the arbitration clause begins with broad language that generally grants jurisdiction to the arbitrator to determine the issue of arbitrability, express language in the contract restricts the breadth of that clause. The arbitration provision that makes arbitrable “any dispute or question arising under the provisions of this agreement” is qualified by the clause “which has not been resolved under the mandatory negotiation provision”.

Indeed, some U.S. courts have held that the negotiation clause must be considered a condition precedent in those cases in which the parties have expressly defined it as such.⁹

In my opinion, this interpretation is correct in the specific situations described above. However, in general terms, when the parties establish a multi-tier dispute resolution system that includes an obligation to negotiate before arbitration, but does not expressly provide that the obligation suspends the effect of the subsequent stages (e.g., the arbitration proceedings), a breach of the obligation to negotiate should not prevent a party from commencing the following stages to resolve the conflict. A different interpretation would lead directly to court proceedings (as the arbitration clause would not be triggered because the condition necessary to trigger it had not been met). This is precisely what the parties were attempting to avoid. For this reason, the effects of a breach of the negotiation clause should be considered within the arbitral proceedings itself. As Born sharply explains, “... even where an agreement provides for arbitration only after a lengthy process of other dispute resolution mechanisms, it stills remains an arbitration agreement. Arbitration delayed is not, so to speak, not arbitration.”¹⁰

In other words, suspending the effects of the multi-tier resolution dispute process because of a simple failure to negotiate, would invalidate the entire dispute resolution structure created by the parties in order to avoid going to court in the first place. Thus, by simply failing to initiate the negotiation phase (or refusing to engage in a negotiation requested by the other party), a

⁹ See SUTTON, GILL & GEARING, *supra* note 2, at p. 48. The Court held likewise in *Kemiron Atlantic Inc. v. Aguakem Int'l Inc.*: “The parties agreed to conditions precedent and, by placing those conditions in the contract, the parties clearly intended to make arbitration a dispute resolution mechanism of last resort ... [therefore,] [b]ecause neither party requested mediation, the arbitration provision has not been activated and the FAA does not apply.” *Kemiron Atlantic Inc. v. Aguakem Int'l Inc.*, 290 F.3d 1287, 1291 (11th Cir. 2002).

¹⁰ GARY B. BORN, *INTERNATIONAL COMMERCIAL ARBITRATION* (3d ed., 2009), at p. 241.

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party could avoid arbitration and take the case to court.¹¹ This is the conclusion of the Court in *Dave Greytak Enters Inc. v. Mazda Motors of America Inc.*¹²:

The good-faith-negotiation provision, when considered in its entirety and in context, was intended basically as the first step of a more comprehensive procedural scheme and obligation -imposed upon both parties- “to seek prompt and expeditious non-judicial resolution of disputes between them.” The highly detailed nonjudicial dispute resolution procedures ... begin with management review, progressing to a stipulation as to the facts and issues in dispute, moving to third-party resolution and, finally, to binding arbitration. Those procedures and their sequence, make it evident that litigation was intended as a last resort, and not ... the beginning point, of the dispute resolution process.

It seems therefore, that the negotiation clause would be better characterized as a procedural arbitration requirement, i.e., a set of requirements which affect the right to obtain a decision on the merits (and not a condition precedent).¹³ Indeed, breach of the negotiation clause would not prevent the commencement of arbitration. In the words of the Zurich Court of Cassation,¹⁴ the “obligation to mediate was a substantive obligation which did not prevent procedural commencement of arbitration.” In *Int’l Ass’n of Bridge v. EFCO Corp. and Constr. Products Inc.*,¹⁵ the Eighth Circuit Court of Appeals stated: “compliance with the procedural arbitration requirements in an arbitration agreement is not a bar to the commencement of arbitration, but instead is a substantive issue for the arbitrators to examine.” But this would mean that until the breach is remedied (we will examine later on the remedial issue), it would not be possible to issue a decision on the merits because an essential requirement to render a final award would be lacking. Although, in my opinion, it would not prevent an interlocutory ruling on this issue.

¹¹ *Ibid.*

¹² *Dave Greytak Enters Inc. v. Mazda Motors of America Inc.*, 622 A.2d 14, 23 (Del. Ch. 1992).

¹³ See MIGUEL ÁNGEL FERNÁNDEZ-BALLESTEROS, DERECHO PROCESAL PRÁCTICO [PRACTICAL PROCEDURAL LAW] VOL. 1 (1993), at p. 407.

¹⁴ Judgment of March 15, 1999, Kassationsgericht [Zurich Court of Cassation], cited in 20 ASA BULLETIN (2002), at pp. 373-376.

¹⁵ *International Association of Bridge v. EFCO Corp. and Construction Products, Inc.*, 359 F 3d 954, 957 (8th Cir. 2004).

It would also be possible to classify the obligation as a merely procedural step to be taken for the party's own benefit (i.e., an action that must be taken to avoid negative effects in the arbitration).¹⁶ The party interested in resolving the controversy is not required to commence negotiations prior to commencing arbitration, but a breach of the clause, unless rectified, would reduce that party's chances of obtaining a favorable decision on the merits.

In other words, regardless of whether it is considered a procedural arbitration requirement or just a procedural step, the failure to comply with it does not close the door to arbitration, but it would prevent reaching a decision on the merits (with a different outcome if it is considered to be a condition precedent). This conclusion, as we will see, has a significant impact on the jurisdiction of the arbitral tribunal and the enforceability of the negotiation clause.

It should also be mentioned that some scholars consider that the obligation to negotiate should be considered a purely substantive obligation, not a procedural one,¹⁷ pursuant to which a breach is remedied just like the breach of any other material obligation: paying damages. This interpretation is incorrect, in my opinion, not only because the negotiation clause forms part of the parties' dispute resolution scheme (and is therefore clearly a procedural issue), but also because the breach would go unpunished if the only consequence were damages. In practical terms it is unlikely that damages for the absence of negotiation would be determined.

III. REQUIREMENTS FOR ENFORCING THE NEGOTIATION CLAUSE

Using the Guaspian¹⁸ classification scheme, a series of requirements must be met in order to implement a negotiation clause, as briefly discussed below:

¹⁶ See JAMES P. GOLDSCHMIDT, *PRINCIPIOS GENERALES DEL PROCESO* [GENERAL PRINCIPLES OF PROCEDURE] VOL I (1961), p. 49 *et seq.*

¹⁷ See FRIDOLIN WALTHER, "E-confidence in e-commerce durch Alternative Dispute Resolution", *AKTUELLE JURISTISCHE PRAXIS* (JULY 2001), at p. 762.

¹⁸ JAIME GUASP DELGADO, Chaired Professor of Procedural Law, and author of, among other works: *COMENTARIOS A LA LEY DE ENJUICIAMIENTO CIVIL* [COMMENTS ON THE CIVIL PROCEDURE ACT] (1943); *EL ARBITRAJE EN DERECHO ESPAÑOL* [ARBITRATION UNDER SPANISH LAW] (1956), and *DERECHO PROCESAL CIVIL* [CIVIL PROCEDURAL LAW] (1956) (with ALONSO P. ARAGONESES, 6th ed. 2006).

1. Subjective requirements

Logically, a request to negotiate must be made by the party that has established the existence of the controversy and seeks to commence the dispute resolution procedure agreed to by the parties. If each side (the requesting party and the recipient of the request) is made up of only one person or entity, then no significant problems should arise.

If there are multiple parties on each side, all the parties who wish to resolve the dispute (if there is a plurality on the requesting side) must commence the procedure with all parties on the other side of the dispute.

This is important if one of the parties is an unincorporated association, such as a consortium or a temporary joint venture (*unión temporal de empresas*). If the requesting party is an unincorporated association, in principle, all the members of the association must make the request (either directly or through a duly authorized officer or representative).

There may however be instances in which only one of the members of a consortium desires to request negotiation, on its own behalf, if the claim is specific to that member. This is possible because it is generally established that when the performance of one of the members of a consortium is individualized and severable from the others, nothing prevents that member from making an individual claim.¹⁹

When an unincorporated association is requested to commence negotiation, the request must be addressed to all the members of the association, unless liability is joint and several or liability is specific to the member to which the request is made. The most prudent course of action, in any event, would be to address the request to all the members of the association.

The request must be made by a representative of the company and addressed to a duly authorized representative of the other party. However, it is normally sufficient for the request to be sent to the bodies or individuals with whom contact has been maintained during

¹⁹ Cf. *Impreglio SpA v. Pakistan*, Opinion on jurisdiction, April 22, 2005 (ICSID case ARB/03/3, Ref. ICC 133, 2005); see Comment by JOHN P. GAFFNEY; and *Lesi SpA and Astaldi SpA v. Algeria* (ICSID case ARB/05/3, Ref. ICC 354, 2008), both published in *Investment Claims*, Oxford University Press (2009). See also YVES DERAÏNS, *The limits of the arbitration agreement in contracts involving more than two parties*, 14 ICC INTERNATIONAL COURT OF ARBITRATION BULLETIN (Special Supp. 2003), p. 25 *et seq.*

performance of the agreement. In a partial award in ICC case No. 6276,²⁰ the tribunal so ruled in response to an objection raised by the respondent arguing that the recipient of the request for negotiation could not validly represent the company:

The defendant is in no position to dispute at present before the Tribunal the validity, which it has not disputed in the past, of the relations of the claimant with various municipal organs which moreover contacted it themselves and gave it instructions.

This conclusion is perfectly reasonable because, if a party has acted through particular representatives throughout the performance of an agreement, then such party cannot later deny that they have the capacity and standing to act in the negotiation process (much less to simply receive the request to commence negotiation).

2. Formal requirements

Requirements as to form are generally established in the negotiation clause. It is possible, however, for the clause to be silent in this regard. In such a case, it seems logical that the request be made in writing to inform the receiving party of the exact nature of the dispute (and to be able to prove compliance with the obligation to negotiate). Nothing prevents the request from being oral, but this would raise significant problems of proof that negotiation was commenced, which could perhaps be resolved through affidavits or written statements from the individuals who participated in the negotiation process. In any event, in international practice, parties avoid the use of a verbal request alone and almost always make a written request.

3. Time limits for the request

The request must be presented within a reasonable period of time after the dispute arises.²¹ This is not just because good faith so requires (to present notice long after the facts giving rise

²⁰ ICC case No. 6276, Partial Award of January 29, 1990, printed in D. JIMÉNEZ FIGUERES, “*Multi-Tiered Dispute Resolution Clauses in ICC Arbitration*”, 14 ICC INTERNATIONAL COURT OF ARBITRATION BULLETIN 1 (2003), at p. 77.

²¹ Cf. FIDIC Conditions of Contract for Construction, - General Conditions -, clauses 20.1-20.8, INTERNATIONAL FEDERATION OF CONSULTING ENGINEERS, MULTILATERAL DEVELOPMENT BANK HARMONISED EDITION, March 2006, at pp. 65-69.

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to the notice would evidence a lack of good faith), but also because it will be much easier for all of the parties involved to collect the necessary evidence and files needed to attempt to settle the dispute.

Many clauses establish a specific time period during which a party may request negotiation, after which arbitration is the only course of action. This situation often occurs in construction contracts, which typically establish a negotiation (or mediation) process led by the chief architect of the project. This process would make no sense after the project has been completed or final payment has been made.

This is precisely the case that the court considered in *Tekmen & Co. v. Southern Builders Inc.* (SBI).²² Tekmen had executed a contract with SBI to build a hotel in Rehoboth Beach. The work was completed in 2000, but in 2001, Tekmen discovered a series of structural defects and filed suit against SBI. The dispute resolution clause read as follows:

Claims, including those alleging an error or omission by the Architect but excluding those arising under Paragraphs 10.3 through 10.5, shall be referred initially to the Architect for decision. An initial decision by the Architect shall be required as a condition precedent to mediation, arbitration or litigation of all Claims between the Contractor and Owner arising prior to the date final payment is due, unless 30 days have passed after the claim has been referred to the Architect with no decision having been rendered by the Architect ...

In essence, Tekmen argued that since the project had already been completed, there was no need to commence the procedure with the architect, and since that procedure was a condition precedent to arbitration, the only recourse was a lawsuit before judicial courts.

The Delaware Superior Court held that the fact that it was no longer possible to commence the procedure with the architect did not extinguish or invalidate the requirement to submit to arbitration:

... the duty to submit the claim to arbitration did not end upon final payment. There is a distinction between the interpretation of clauses requiring that no

²² *Tekmen & Co. v. Southern Builders Inc.*, C.A. No. 04C-03-007 RFS (Del. Super. Ct. 2005).

demand for arbitration be made after the date of final payment and those requiring merely that the existing claim be submitted to the architect as a condition precedent up until the date of final payment. This case falls into the latter category. Where submission of the claims to the architect is a condition precedent to arbitration, a party's duty to arbitrate is not extinguished merely because the condition precedent is finite in time.

Finally, as regards the deadline for making the request, sometimes the arbitration commences before the negotiation period has expired. This problem will be addressed below, when the effects of a breach of the negotiation clause are analyzed. At this stage, suffice it to say that if the request for arbitration is presented after there is conclusive proof that it is impossible to reach a negotiated resolution to the controversy, then the requirement for arbitrability must be considered met. Any other position would merely delay resolution of the dispute, an outcome devoid of any legitimate interest.

4. Requirements as to content

As mentioned previously, there are many types of negotiation clauses. Some are vague or general (“the parties shall negotiate in good faith prior to ...”), while others are more detailed, establishing the maximum term for the negotiation, the individuals who must attend the negotiations (CEO, General Manager, etc.), and even the number of meetings that must be held. Logically, compliance with detailed negotiation clauses requires abidance with the terms established by the parties.

Sometimes, however, these requirements are only partially met. For example, when the negotiations are supposed to be held between “senior representatives” of the parties, and a mere representative attends on behalf of one party. Another frequent problem is the failure to exhaust the prescribed negotiation term. The first situation arose in an ICC arbitration case in 1999.²³ The respondent argued that the arbitrability requirement had not been met because, despite the fact that the negotiation clause provided for negotiations to be held between “senior management representatives,” the claimant had been represented by a mere attorney-in-fact who did not meet this requirement. The sole arbitrator rejected the argument, and stated that if the respondent believed that the level of the participants in the negotiation was

²³ See ICC case No. 9977, Final Award of June 22, 1999, printed in JIMÉNEZ FIGUERES, *supra* note 20, at pp. 84-85.

insufficient, it should have objected at the time so that the problem could be resolved. In the words of the Tribunal:

A prior process like the one set forth in the Agreement, rather implies an attitude and behaviour of the parties inspired in a true and honest purpose of reaching an agreement. Henceforth, if one of the parties considers in good faith that its counterpart is not authentically committed to foster the possibilities of settling the dispute, for instance, because of the quality of its representative, it is expected that the former would express so during the process. So that, the counterpart might be able to put a prompt remedy to said objection.

[...]

(iii) [Respondent]'s allegation objecting the characteristics of [Claimant] representative involved in the process is a post factual argument. If [Respondent] was truly committed to settle the controversy and considered the characteristics of the [Claimant]'s representative as an obstacle in doing so, it would be expected that [Respondent] should have raised such point at that time. It did not occur.

The negotiation requirement should be considered properly fulfilled, even though the term established by the parties for negotiation has not expired, when it is clear that the parties' positions are so opposed that it would be virtually impossible to reach a negotiated solution. Under these circumstances, there is no justification to order the parties to negotiate until the agreed deadline. As Jiménez Figueres explains²⁴:

The importance of good will in amicable dispute resolution may in the past sometimes have led arbitrators to believe that refusing to allow a request for arbitration when it was quite obvious that the parties were too divided to entertain an amicable settlement may not have been in the parties' best interests.

Finally, it is important to mention situations in which a formal milestone must be reached before the negotiation phase may be considered concluded. For example, when a party must send a letter stating its conclusion that an agreement cannot be reached. In those cases, the requirement must be met before the terms of the negotiation clause may be considered properly fulfilled. Some arbitration tribunals²⁵ have nevertheless held that, despite the

²⁴ JIMÉNEZ FIGUERES, *supra* note 20, at p. 72 .

²⁵ ICC case No. 9984, Preliminary Award of June 7, 1999, printed in JIMÉNEZ FIGUERES, *supra* note 20, at p. 87.

existence of the requirement, if one party sends a communication to the other stating that it will deem the negotiation to have ended if agreement is not reached by a certain date, such ending milestone (the letter stating that there is no possibility of reaching an agreement) should be deemed to have been met:

Fixing in advance in a letter a date by which the attempt to amicably settle the dispute would be held as having failed in this absence of a settlement was an acceptable substitute to sending a letter notifying Respondents of such failure.

The tribunal's interpretation is, in my opinion, correct because once the deadline established in the letter had elapsed, it was clear that the negotiation could not continue and the dispute could only be resolved by advancing to the next stage. Setting a milestone that allows the negotiation to be considered concluded is important to avoid the effects of obstructionist attitudes and delay tactics by the party that does not really wish to negotiate.

5. Requirements to prove compliance with the obligation to negotiate

As mentioned above, the request to negotiate is generally made in writing. This is typically a simple letter or document that refers to the subject-matter of the dispute and the claim being made and requests a meeting to commence negotiations. In these cases, proof of compliance with the obligation is straightforward.

Logically, one must prove not only that the negotiation was initiated but also that it actually took place. Given that negotiation usually involves the exchange of letters, emails and proposals, demonstrating this fact should not be difficult. However, the parties may have agreed that the negotiations must be kept confidential, or simply that their proposals should not be produced in the arbitral proceedings. In these cases, affidavits or written statements from the individuals involved²⁶ would be sufficient proof. However, if the parties have agreed to keep the negotiations confidential, there should be evidence of the confidentiality agreement. This will demonstrate to the tribunal why the evidentiary documents cannot be submitted.

²⁶ See ICC case No. 9977, Final Award of June 22, 1999, printed in JIMÉNEZ FIGUERES, *supra* note 20, at pp. 84-85.

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Respondents have on occasion also claimed that the obligation to negotiate was not met because the opposing party failed to negotiate in good faith, but arbitration tribunals generally refuse to examine whether the good faith requirement was met, limiting themselves to a review of whether the formal negotiation requirements were complied with.²⁷

Finally, if a party receiving a request to negotiate refuses to do so, and fails to provide a reasonable justification, the requirement will also be considered to have been met. This was the ruling in *Biloune (Syria) and Marine Drive Company Ltd. (Ghana) v. Ghana Investment Centre and Government of Ghana*:²⁸ “The Tribunal holds that the legal and contractual prerequisites to arbitration —failure of attempts at amicable settlement— were satisfied by the Claimant’s efforts and the Respondent’s inaction.”

The tribunal’s decision is sound because the purpose of the negotiation clause is to exhaust the possibility of amicably resolving the controversy. If that cannot be achieved due to the inaction of one of the parties, then the next stage of conflict resolution procedure should begin. Otherwise, the obstructionist party would be unduly rewarded.

IV. COMMENCEMENT OF ARBITRATION WITHOUT FULFILLING THE OBLIGATION TO NEGOTIATE

The commonly held view²⁹ is that arbitrators should decide on the consequences of a breach of the negotiation clause.³⁰ As discussed above, except for a U.S. court decision holding that

²⁷ See ICC case No. 7422, Interim Award of June 28, 1996, printed in JIMÉNEZ FIGUERES, *supra* note 20, at pp. 78-79.

²⁸ *Biloune (Syria) and Marine Drive Company Ltd. (Ghana) v. Ghana Investment Centre and Government of Ghana* (UNCITRAL), Award on Jurisdiction and Liability, 27 October 1989, 95, ILR, 184, XIX YEARBOOK COMMERCIAL ARBITRATION 11 (1994), at p. 18.

²⁹ See ALEXANDER JOLLES, “Consequences of Multi-tier Arbitration Clauses: Issues of Enforcement”, 72 ARBITRATION 4 (2006), at p. 335.

³⁰ See JAN PAULSSON “Jurisdiction and admissibility,” GLOBAL REFLECTIONS ON INTERNATIONAL LAW, COMMERCE AND DISPUTE RESOLUTION (2005), at pp. 601-617.

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the arbitral tribunal lacked jurisdiction because a condition precedent had not been met,³¹ the consensus is that this issue should be decided by the arbitration tribunal.³²

Once this preliminary matter has been explained, the next question is whether a breach of the obligation to negotiate may be decided by the arbitrators *sua sponte*.

In my opinion, there is little doubt that the respondent must raise the failure to meet this arbitrability condition or requirement as an objection which impedes the continuation of the arbitration proceedings. Indeed, arbitration is based on the will of the parties. Therefore, if a party capable of raising the objection fails to do so, one must conclude that both parties agree to eliminate the requirement. There would thus be tacit consent to amend the dispute resolution clause.

If a party raises the objection, then the tribunal may choose (after confirming that the obligation to negotiate was not met) to either immediately dismiss the proceedings or to suspend them and require the parties to negotiate.

A review of available arbitration decisions shows that arbitration tribunals generally dismiss the arbitration, finding that an essential procedural requirement to proceed with the arbitration has not been met and that the request for arbitration is therefore premature. In the famous *Channel Tunnel* matter,³³ Lord Mustill expressed the likely reason:

Those who make agreements for the resolution of disputes must show good cause for departing from them ... Having promised to take their complaints to the experts and if necessary to the arbitrators, this is where the appellants should go. The fact that the appellants now find their chosen method too slow to suit their purposes is to my way of thinking quite beside the point.

³¹ The majority believes the opposite: “issues concerning the procedure for triggering arbitration ... are matters for arbitration, not initial judicial determination.” *SBC Interactive Inc. v. Corp. Media Partners*, 714 A.2d 758, 759 (Del. 1998). See also *Pettinaro Constr. Co. v. Harry C. Partridge, Jr. & Sons*, 408 A.2d 963 (Del. Ch. 1979) (“The proper method of initiating arbitration under the contract is a matter for the decision of the arbitrator”).

³² See BORN, *supra* note 10, at p. 842.

³³ *Channel Tunnel Group Ltd v. Balfour Beatty Construction Ltd.*, ICC case No. 6276 (1993), 2 WLR 262 at p. 276 *et seq.*

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A prime example of a decision that follows this reasoning is ICC case No. 6276, Partial Award of January 29, 1990.³⁴ The parties had agreed to a three-stage dispute resolution procedure: first, amicable negotiation; then submission of the controversy to the decision of an engineer; and finally arbitration. The parties initiated negotiations, which did not succeed, and then they turned immediately to arbitration, without submitting the controversy to an engineer. The respondent objected that the dispute resolution clause was being breached, and the tribunal agreed, dismissing the arbitration in these terms:

The Tribunal has thus reached the conclusion that the claimant has not satisfied the prerequisite set forth in article 65 of the General conditions of contracts. Consequently, the request for arbitration concerning the 1981 contract, which is certainly not impossible for the future, is at present premature. It therefore behoves the claimant formally to demand from the defendant the designation of an engineer to whom to submit the present dispute before it comes before the Tribunal.

Although this may be common practice, it is not necessarily proper. If there is a dispute between the parties (which clearly exists when the arbitration stage is initiated), then negotiation will probably not lead to a happy ending. Dismissal will only cause recommencement of the arbitration and the appointment of a new arbitral tribunal, which results in a waste of precious time that could be used to resolve the conflict.

A more prudent choice, in the best interests of the parties, would be to suspend the arbitration proceedings, send the parties to negotiation and to resume the proceedings if the negotiations fail.³⁵ This would clearly require specific guidelines for the parties regarding the time limit for the negotiations and the conditions under which they must be carried out (unless the negotiation clause already contains those terms).³⁶

³⁴ ICC case No. 6276, Partial Award of January 29, 1990, printed in JIMÉNEZ FIGUERES, *supra* note 20, at p. 78.

³⁵ Cf. UNCITRAL Model Law on International Commercial Conciliation, art. 13, UN Doc. A/57/71, 2002, Annex I, at p. 6: “Resort to arbitral or judicial proceedings: Where the parties have agreed to conciliate and have expressly undertaken not to initiate during a specified period of time or until a specified event has occurred arbitral or judicial proceedings with respect to an existing or future dispute, such an undertaking shall be given effect by the arbitral tribunal or the court until the terms of the undertaking have been complied with, except to the extent necessary for a party, in its opinion, to preserve its rights. Initiation of such proceedings is not of itself to be regarded as a waiver of the agreement to conciliate or as a termination of the conciliation proceedings.”

³⁶ See BORN, *supra* note 10, at p. 843 and JOLLES, *supra* note 29, at p. 337.

The parties will of course be negotiating under the pressure of an arbitration that has already commenced, but on balance, this solution is preferable to dismissal. If the tribunal decides to dismiss the case, then obviously nothing prevents the party from complying with the negotiation requirement and filing for arbitration again.³⁷

On the other hand, if the tribunal believes that the parties' attitudes are so acrimonious that it would be impossible for them to reach an agreement, the tribunal may reject the defense and continue with the arbitration. This was the ruling in ICC case No. 8445:³⁸

The arbitrators are of the opinion that a clause calling for attempts to settle a dispute amicable ... should not be applied to oblige the parties to engage in fruitless negotiations or to delay an orderly resolution of the dispute.

V. VACATING THE ARBITRAL AWARD DUE TO BREACH OF THE NEGOTIATION CLAUSE

It has been argued that a breach of the negotiation clause invalidates the arbitral award. In essence, those who support this view maintain that because the negotiation clause is a condition precedent, the arbitral tribunal that rendered the award lacks jurisdiction (or, if one prefers, there was no mandate from the parties). Thus, its decision is void from the outset. This is precisely what the tribunal held in *White v. Kampner* (“the parties were required to participate in the mandatory negotiation sessions prior to arbitration”).³⁹

If the negotiation clause is characterized as a procedural arbitration requirement, or even as a mere procedural step (which appears to be the proper classification of these clauses), and not as a condition precedent, then the arbitration tribunal has jurisdiction to determine whether the negotiation requirement has been met, and its decision should not be invalidated because the negotiation process was not carried out.

³⁷ See BORN, *supra* note 10, at p. 846.

³⁸ ICC case No. 8445, Final Award of 1996, XXVI YEARBOOK OF COMMERCIAL ARBITRATION (2001), at pp. 167-180

³⁹ 641 A.2d 1381, 1387 (Conn. 1994). See also *Handelsmaatschappij Vekoma BV (Netherlands) v. Maran Coal Corp. (US)*, Swiss Federal Court (Bundesgericht), Civil Division I (August 17, 1995).

VI. ENFORCEABILITY OF THE NEGOTIATION CLAUSE AND ANTI-SUIT INJUNCTIONS

The issue of the enforceability of the negotiation clause has been raised mainly before U.S. courts. Their response has generally been that enforcement may be ordered only when the obligation to negotiate includes a series of parameters in order to determine whether the clause has truly been fulfilled.⁴⁰

Similarly, when the negotiation clause is vague, imprecise or generic, courts consider the clause to be unenforceable.⁴¹

Courts are more willing to enforce the clause when it is clearly drafted as a condition precedent to the subsequent stages of the dispute resolution scheme.⁴² However, when a court believes that a party's desire to enforce the negotiation clause is based on that party's spurious interest in delaying resolution of the dispute, the court has rejected enforcement.⁴³

The anti-suit injunction, which parties sometimes request in order to suspend an arbitration proceeding initiated before compliance with the negotiation clause, is also connected to enforceability of the negotiation clause.

It is worth mentioning in this regard *Commerce Bank NA v. DiMaria Construction Inc.* (April 17, 1997),⁴⁴ where the New Jersey Superior Court rejected the respondent's petition to suspend the arbitration, ruling that the issue of compliance with the negotiation clause had to

⁴⁰ In *Mocca Lounge Inc. v. Misak*, 99 AD. 2d 761 (2d Dept. N.Y.S. 1983) the court held that it was possible to enforce a negotiation clause: "As one New York court observed, it is possible to enforce a definite and certain duty to negotiate in good faith, but even when called upon to construe a clause in a contract expressly providing that a party is to apply his best efforts, a clear set of guidelines against which to measure a party's best efforts is essential to the enforcement of such a clause."

⁴¹ See *Candid Prod. Inc. v. International Skating Union*, 530 F.Supp. 1330 (S.D.N.Y. 1982) ("[A]n agreement to negotiate in good faith is unenforceable because it is even more vague than an agreement to agree; an agreement to negotiate in good faith is amorphous and nebulous, since it implicates so many factors that are themselves indefinite and uncertain that the intent of the parties can only be fathomed by conjecture and surmise.")

⁴² *White v. Kampner*, 641, A.2d, 1385 (Conn. 1994) (cited in FILE, *supra* note 1, at p. 36).

⁴³ *Southland Coop. v. Keating*, 465, US1 (U.S. S. Ct. 1984).

⁴⁴ *Commerce Bank v. DiMaria Construction*, 300 (N.J. Super. 9 1997).

be decided by the arbitrators (“... the trial court correctly construed the general arbitration clause in the contracts between Commerce and DiMaria to require the arbitrators to decide whether DiMaria was foreclosed for arbitrating because it did not file a claim with the architect or demand arbitration within twenty-one days of termination of the contracts”). However, these anti-suit injunctions have occasionally been granted when one party has refused to participate in the required negotiation process.⁴⁵

VII. CONCLUSION

Negotiation clauses play –and have played– an important role in the dispute resolution process. They should be considered procedural arbitration requirements that must be met before the parties can seek a decision on the merits. Thus, failure to comply with the clause should not bar access to arbitration. The arbitrators, and not the court, should determine the effects of non-compliance. Generally, the case should be dismissed, although it is more reasonable to simply suspend the proceedings until the requirement has been met. Enforcement of the negotiation clause is possible when the terms of performance are well defined, but not when the clause is reduced to generic or imprecise statements. In any event, these clauses serve an important role in “filtering” or “weeding out” conflicts that may arise, but do not avoid difficulties in certain cases that a practitioner should be aware of and anticipate.

⁴⁵ See JOLLES, *supra* note 29, at p. 332.