



Complex Dispute Resolution Clauses in Contracts

EXECUTIVE SUMMARY

Dispute resolution clauses are often given less importance and are dealt with towards the end of contractual negotiations, or even dismissed as boilerplate clauses and given standard wording without due thought and consideration as to the implications on how any dispute is resolved and how the contractual rights and obligations of parties will be enforced.

The purpose of this article is to provide advice and guidance, namely to our clients in the finance and construction sectors, on complex dispute resolution clauses including “*hybrid*”, “*multi-tiered*” and “*carve out*” clauses to assist in identifying them, understanding how they work, and explain what issues may arise by their inclusion within contracts.

HYBRID CLAUSES

Hybrid clauses will arise in situations where one or more parties are given the opportunity to choose between arbitration and litigation.

The purpose of a hybrid clause is to allow the parties to choose the most appropriate forum of dispute resolution after a dispute has arisen. However, these clauses should be treated with caution as there are significant risks in including these types of clauses within a contract namely because they can give rise to enforcement issues and the likelihood of parallel proceedings.

Hybrid clauses may include sole option, asymmetrical or one-sided clauses.

Under a sole option clause, only one of the parties to the contract has the option to initiate court litigation or arbitration proceedings, and an asymmetrical or one-sided clause typically requires one party to a contract to sue in the courts of a specified jurisdiction only whilst allowing the other party (often a financial institution) to sue in any court with jurisdiction.

For example, in banking and finance transactions, it is often provided in the contract that one party has the option to choose litigation or arbitration as a forum of dispute resolution.

In the UAE for example, banking and finance documents sometimes include a unilateral option provision which purports to reserve to the lender, bank or investment fund, the right to choose litigation or arbitration, or sometimes litigation in a different forum to the local courts.

Typically, such clauses are drafted so that the financial institution has the exclusive right, at their own option, to choose between litigation and arbitration, with the other party to the contract having no say in the matter which gives the financial institution superior rights when it comes to the choice of forum for resolving the dispute.



A typical example of this is in a bank lending agreement which often provides for an agreement to arbitrate, with the option to the bank to sue in any competent jurisdiction along with a waiver of any *forum non conveniens* objection to the court.

An example hybrid clause is as follows:

“DISPUTE RESOLUTION

It is agreed that any controversy or claim arising out of or in connection with this Agreement, or the breach thereof, (including a dispute regarding the existence, validity or termination of this Agreement) shall be referred to and finally settled by arbitration administered by [the arbitral tribunal i.e. the DIFC-LCIA Arbitration Centre] under the Rules of the DIFC-LCIA Arbitration Centre (the “Rules”) which are deemed to be incorporated by reference to this clause. The arbitral tribunal shall consist of one arbitrator who shall be appointed in accordance with the Rules. The place of the arbitration shall be the DIFC and the language of the arbitration shall be in English.

Notwithstanding the above, at its sole option, it is agreed that a Financial Party, may choose, instead of arbitration, to submit any such claim before the courts of any competent jurisdiction. If arbitration has been commenced by Other Party at the time that Financial Party chooses to submit the matter to a court of competent jurisdiction, it is agreed that such arbitration shall be discontinued.”

In the UAE, the risk with such a provision arises from the practice of the UAE Courts to accept jurisdiction if a claim is brought by a party in connection with any agreement negotiated, signed or performed in whole or in part within the UAE. Therefore, in circumstances where there is an arbitration clause and a clause which provides for the Dubai International Financial Centre Courts (or any other Courts) to have jurisdiction, a UAE Court may disregard the arbitration provision agreed between the parties and consider itself to have jurisdiction.

When considering the UAE Courts attitude towards unilateral option clauses, it is important to consider how other jurisdictions have approached this. For example:

- In England and Wales, unilateral options are recognised as enforceable as a matter of law (*Mauritius Commercial Bank Ltd v Hestia Holdings Ltd and another [2013] EWHC 1328 (Comm)*);
- In Hong Kong and Singapore, unilateral option clauses have been held to be valid and enforceable (*China Merchants Heavy Industry Co Ltd v JGC Group [2001] HKLRD (Yrbk) 21*); and
- In France, some national courts have refused to recognise such clauses on the basis that they are one-sided.

Moreover, the main lines of attack by parties in other jurisdictions has been on the basis that such clauses are: (1) void for uncertainty; (2) void for unconscionability; and/or (3) void as a matter of public policy.

Notwithstanding, in our view, in the UAE a unilateral clause to arbitrate is likely to not be recognised by the UAE Courts as a valid arbitration agreement in circumstances where it is inconsistent with the obligation of good faith by creating an inequality of bargaining power between the parties.



MULTI-TIERED CLAUSES

A multi-tiered clause requires the parties to perform one or more steps of dispute resolution before proceeding to arbitration or litigation. It is a clause that provides for distinct stages involving separate procedures for dealing with and seeking to resolve disputes between the parties

For example, a multi-tiered clause may provide that the parties must use various methods to resolve the dispute (in the following order): (1) negotiate; (2) mediate; (3) arbitration.

Multi-tiered clauses are commonly found in complex construction contracts because they are often cost effective and efficient.

Whilst arbitration is generally recognised as an effective method of dispute resolution, in international commercial contracts, it can be time consuming and costly to the parties. Therefore, the aim and function of a multi-tiered dispute resolution clause is to reduce time and money by allowing for a period of amicable settlement. Further, the use of such clauses may preserve ongoing commercial relationships between the parties by providing the opportunity to resolve disputes in a less adversarial setting.

However, there are potential disadvantages in using such clauses because if, for example, the parties mediate and do not successfully resolve the dispute, then these costs are largely wasted and the parties still need to move to the next stage to reach a binding resolution. Therefore, in circumstances where one of the parties wants a swift resolution, such delay can prolong the eventual award which allows a party to further evade its contractual obligations.

In the UAE, multi-tiered dispute resolution clauses are a common feature of construction contracts, and the best-known international examples are clause 67 of the FIDIC 1987 Red Book and clause 20 of its 1999 Rainbow Suite of Contracts.

Under clause 67 of FIDIC 1987 Red Book, all disputes related to construction are to be referred to the Engineer in the first instance for a decision, which is final and binding upon the parties unless and until the dissatisfied party proceeds to arbitration. Clause 20 of 1999 Rainbow Suite of Contracts added a dedicated, impartial Dispute Adjudication Board (“DAB”) which could be standing or *ad hoc* and appointed when a dispute arose, and sought to offer the Contractor some certainty and lessen the risk in the event that a DAB and arbitration are necessary.

A multi-tiered clause should include an Alternative Dispute Resolution stage (“ADR”) (i.e. a stage for negotiation, mediation, informal discussions, expert determination, reference to dispute boards and/or any other procedure or mechanism agreed by the parties) and provide for arbitration or court proceedings if the ADR stage fails.

An example multi-tiered dispute resolution clause is as follows:

“DISPUTE RESOLUTION

If a dispute arises out of or in connection with this agreement (“Dispute”), then the parties shall follow the dispute resolution procedure set out below:

within [] days of service a written notice (“Notice”) from one party to the other party setting out the nature of the Dispute with full particulars together with evidence in support, both parties shall attempt in good faith to resolve the Dispute;

if the parties are unable to resolve the Dispute within [] days of service of the Notice, the parties agree to enter into mediation in good faith to settle the Dispute in accordance with the CEDR Model Mediation Procedure.



Unless otherwise agreed between the parties, within [] days of service of the Notice, the mediator shall be nominated by CEDR.

*To initiate the mediation, a party must serve notice in writing ("**Mediation Request**") to the other party to the Dispute requesting for the Dispute to be referred to mediation and unless otherwise agreed by the parties, the mediation shall commence no later than [] days after the date of the Mediation Request.*

Where mediation between the parties fails, the parties agree to refer the dispute to arbitration in accordance with the Rules of the DIFC-LCIA Arbitration Centre."

CARVE-OUT CLAUSES

In circumstances where there is likely to be a significant difference between the types of disputes that may arise under a particular contract, the parties may opt to choose a carve-out clause.

A carve-out clause will arise where precisely identified disputes are expressly stated and carved out from the main dispute resolution mechanism and are treated differently.

One of the main examples is an expert determination clause.

Expert determination is often applied to determine technical or valuation issues where the parties appoint an expert to apply their expertise on certain, defined issues under the contract. The types of disputes that are referred to expert determination often involve single issues and technical rather than legal questions.

Expert determination clauses operate wholly on a contractual basis and often provide that the expert's decision is final and binding, except in the event of certain circumstances (for example, fraud). For purely technical disputes they provide a cost-effective way of resolving issues without the time and cost involved in bringing court or arbitration proceedings, and unlike court proceedings which take place in the public domain, parties to an expert determination can maintain the privacy of their contractual relationship.

Further, if the parties agree to be bound by the expert's decision it is difficult to challenge it. Typically, the clause will specify the field of expertise from which the expert is to be chosen, provide that the parties must try to agree on the identity of the expert at the time the dispute arises and failing such agreement, confirm that an appropriate professional institution shall be appointed. It should also expressly state that the expert's decision is final and provide for a mechanism to deal with challenges to and enforcement of the expert's decision to avoid situations in which it is unclear which forum a party should go to if a party considers that the decision is not final and binding or simply refuses to recognise it. Where an expert determination clause is used, it is crucial that the clause expressly states that the expert is to act as an expert to avoid confusion with other methods of dispute resolution.

Other carve out clauses are those that submit certain types of disputes under a contract to arbitration and others to litigation. The concern with these types of clauses are that they can result in parallel proceedings, and therefore if used, it is important that they define the precise scope of the dispute to be submitted to the dispute resolution mechanism.

An example of a carve out clause can be found in the model ICC Operational Expert Determination by the ICC International Centre for Technical Expertise which provides as follows:

"The parties may at any time, without prejudice to any other proceedings, agree to submit any dispute arising out of or in connection with clause [x] of the present contract to administered expertise proceedings in accordance with the Rules of Expertise of the International Chamber of Commerce."



ANY OTHER CONSIDERATIONS?

Another key consideration is multiple contracts, for example, transactions that involve a suite of documents.

There should be consistency throughout the documents as to how the dispute should be resolved. However, whilst preferable, it is often either not possible or not the case. In such circumstances, in our experience, the issues that tend to arise are as follows:

- Uncertainty and the possibility of satellite litigation as the parties end up in court trying to determine which dispute resolution clause is applicable; and
- An increased risk of parallel proceedings - in circumstances where a dispute falls within the scope of different contracts, separate proceedings should be commenced in accordance with the dispute resolution provision within each agreement.

To minimise these risks, it is important for the parties and their legal representatives to consider the dispute resolution strategy at the transactional stage. The main problem, however, is trying to determine the type of dispute that may arise out of the contract(s), and it is therefore important to think carefully where you want any disputes to be heard and how you want them to be dealt with. Moreover, whichever forum for dispute resolution is chosen, the parties should also give due consideration to whether they need to provide an address for service, which is essentially a clause that provides that when a dispute arises, proceedings must be served at a particular address.

Robert Whitehead | Senior Associate
Hamdan Al Shamsi Lawyers & Legal Consultants

For any enquiry please click [here](#)

