Legal Affairs Group Cheat Sheet
Methods of dispute resolution

intellect
REPRESENTING THE UK TECHNOLOGY INDUSTRY

Andrew Tibber and Georgina Shaw of Burges Salmon LLP consider the types of dispute resolution clauses frequently encountered in IT and other commercial contracts.

Introduction

Many IT and other commercial contracts will contain a dispute resolution clause, setting out a defined procedure for the contracting parties to follow in the event of a dispute. Although a dispute is something neither party wants nor expects when embarking on a new business venture, it is always a possibility that the contractual relationship will break down. It is therefore important for parties to consider whether a particular dispute resolution clause will meet their needs, resources and expectations in the event of a dispute and provide the best possible chance of a successful outcome.

This cheat sheet sets out some of the issues that parties should have in mind when considering the suitability of a dispute resolution clause into a contract, and goes on to explain the different forms of dispute resolution and what each method seeks to do.

Considerations

The following considerations may have an impact on which choice of dispute resolution method your contract provides for:

- Do you want to enter into a formal process with set stages of escalation, or would you prefer a more flexible approach?
- Do you want the final say in the outcome of settlement negotiations or are you prepared to submit to the binding decision of an independent third party?
- Do you need or want a speedy resolution to any dispute?
- What are the financial resources of the parties involved?
- Is confidentiality important to you?

You may want to consider different approaches for different types of dispute. For example the contract can be drafted to stipulate one method of dispute resolution for agreeing price reviews, and another for agreeing damages for delays in meeting agreed project milestones. Remember, however, that if the contract provides for a certain method of dispute resolution to be used in the event of a dispute arising, the Court can require parties to adhere to that method and not permit them to pursue separate legal proceedings. You need to be satisfied therefore that this would be acceptable in the event of a dispute.

Legal Affairs Group

The Legal Affairs Group consists of over 130 member companies including large prime contractors, small subcontractors, manufacturing and outsourcing service companies, and those that manufacture and outsource services. The group's membership also includes a number of Intellect's Affiliate Members from various Law Firms. The group meets to share expertise and experience with a view to informing and helping other members.

Cheat Sheet series

The Legal Affairs Cheat Sheets series has been designed to help answer various legal questions Intellect members may have.

They are available in hard copy, and can also be found on our website at **www.intellectuk.org/legalaffairs**

If you have any suggestions for future Cheat Sheets please contact
Theodora Kalessi
T 020 7331 2058
E theodora.kalessi@intellectuk.org

Legal Affairs Group Cheat Sheet
Methods of dispute resolution

intellect
REPRESENTING THE UK TECHNOLOGY INDUSTRY

Methods of Dispute Resolution

1. Litigation

The term litigation is generally used to refer to formal civil proceedings in Court, where a judge hears the arguments put forward by each party and imposes a legally binding decision on them (with scope for appeal).

If proceedings are defended, litigation can be slow and costly in comparison to other methods of dispute resolution. The basic rule in English law is that the party who loses in litigation is liable to pay a substantial proportion of the winning party's legal costs, and as litigation is expensive and inherently unpredictable, no matter how strong a case a party thinks it has, the potential cost exposure can be very high.

Moreover, statements of case and the judgment of the Court are available for scrutiny by the public unless litigants can show good cause why they should not be. If confidentiality is important to the parties, therefore, litigation may not be the best method of settling a dispute.

2. ADR

Alternative Dispute Resolution (ADR) can take many different forms, but is essentially the collective term for methods of resolving disputes outside of the normal trial process. Broadly, ADR provides for two different approaches, namely, where an independent third party brings the parties to a dispute together to try and encourage them to negotiate a settlement of the dispute, or where an independent third party is appointed to reach a decision on the issues in dispute. It is also possible to provide for more than one method of dispute resolution within a contract by way of a dispute escalation clause (discussed at 3. below).

a) Mediation

This is a consensual process where the parties appoint an independent third party who seeks to help the parties to a dispute to reach a negotiated settlement. The role of the appointed mediator is to identify the issues in dispute and explore the options for settlement, usually in the form of shuttlecock diplomacy between the parties. The mediator has no power to adjudicate or impose a decision, and so the parties are able to control the mediation process and to reject any proposed settlement with which they are not comfortable. The downside of this is that there is no guarantee that a meditation will successfully resolve the dispute.

The outcome of the mediation is confidential unless the parties agree otherwise and the process is flexible enough to allow the parties to agree settlement terms that no Court would grant (for example granting a licence in return for compromising a claim).

Moreover, the procedure is relatively cheap when compared to litigation, although there are costs involved in paying for the mediators' fees and the costs of preparing for the mediation (which are frequently attended by legal representatives).

Whether or not a contract provides expressly for mediation, parties should always consider this as an alternative to litigation as the Court can impose costs sanctions on anyone who issues proceedings having unreasonably refused a prior invitation to mediate.

b) Arbitration

Arbitration is a private form of dispute resolution conducted in accordance with set rules of procedure where an independent arbitrator imposes an award on the parties, in judicial fashion, in order to finalise the dispute. Although there is some flexibility in the procedure (for example in the requirements to disclose documents to each other), in general it is much like litigation with an exchange of statements of case and evidence, followed by a hearing at which one or more arbitrators make a final award that is contractually binding on the parties. The decision is usually final with limited or no scope to appeal. In England, the Arbitration Act 1996 sets out the circumstances in which the Court is prepared to hear a challenge to an arbitral award, namely on grounds of jurisdiction, serious irregularity or a point of law.

The advantages of arbitration as a method of dispute resolution are that it is usually quicker than litigation; the parties are able to choose their arbitrator by agreement; the hearing is held in private (unlike the court process) with only the parties and their representatives in attendance; and the parties are free to agree a mutually convenient date and venue for the arbitration.

Arbitration can also be particularly effective in resolving international disputes. In litigation, there can issues as to which jurisdiction applies and where a judgment is obtained in the national court of one party, the national court of the other party may not be prepared to recognise and enforce it. Arbitration awards, on the other hand, are readily recognised and enforced by the courts of countries, including China, that have signed up to international conventions such as the New York Convention.

However, it must be borne in mind that arbitration can often be more expensive than litigation as in addition to their own legal costs, the parties have to pay for the costs of the arbitrator (or arbitrators) and the arbitrator's expenses, which can include long-haul flight and hotel expenses.

c) Adjudication

Adjudication is used to provide a decision on disputes as they arise during the course of a contract. The decision of an adjudicator only has an “interim-binding effect,” which means that it is open to the parties to agree to alter the effect of the decision, or to refer the dispute to arbitration or litigation for a final, binding determination.

Adjudication is a statutory right that parties cannot contract out of. Adjudication is governed by the Housing Grants, Construction and Regeneration Act 1996 and is mandatory in relation to a domestic construction contract. Such contracts often contain provisions relating to IT and communications systems, and it is therefore possible that you may enter into a contract that is governed by this form of dispute resolution in the event of a dispute.

Adjudication has a proven record of success and is a quick and cost effective means of dealing with a dispute. A dispute can be decided within 28 days of the matter being referred to an arbitrator. Also, adjudication is usually cheaper than litigation (and arbitration) as there is a tight timetable meaning that preparation costs are lower.

However, this also has some disadvantages, as the short timescale can increase the risk of obtaining a rough and ready decision from an adjudicator on a complex dispute. Furthermore, the costs of adjudication are usually not recoverable from the other side.

Legal Affairs Group Cheat Sheet
Methods of dispute resolution

intellect
REPRESENTING THE UK TECHNOLOGY INDUSTRY

d) Expert Determination

Expert determination is an informal process with a proven track record of success in which an expert in the subject matter in dispute is appointed by the parties to determine a particular issue, which is usually of a technical nature. The process can be kept confidential.

Expert determination is particularly suited to disputes which centre around technical issues. As the expert's decision is legally binding there is only limited scope to challenge the determination. Therefore the parties should take care to ensure that they appoint an expert with the appropriate knowledge and expertise in the technical area in question.

However, sometimes the parties can agree that the expert's decision is advisory rather than binding. In that case, the expert's evaluation often then forms the basis of settlement.

The cost will vary according to the complexity of the issues but the appointment fee, expert's charges and costs will at least be quantified in advance and it is usual for the parties to split the cost of the expert's fees and other administrative expenses.

3. Dispute Escalation Clauses

The purpose of a dispute escalation clause is to provide contractual certainty as to what procedure contracting parties should follow in the event of a dispute, and when it is open to the parties to commence litigation. This type of clause can promote flexibility by enabling the parties to tailor the dispute resolution procedures adopted at each stage to suit the particular project in question. It can also encourage a negotiated settlement by making parties talk to each other first before they rush headlong into litigation. For example, the first step could provide for negotiation between project personnel; if unsuccessful, the dispute could then be referred to management and potentially senior management level, before being referred to an external, independent third party if necessary. It is important however that the clause should contain a binding method of dispute resolution (arbitration or litigation) as a last resort, regardless of the number of steps before reaching that stage.

Although a dispute escalation procedure can provide flexibility and may increase the chances of early settlement, it is important that the clause is carefully considered at the drafting stage. If the escalation procedure is unclear, this may lead to a dispute in relation to the meaning and effect of the clause itself, leading to wasted time and costs. An escalation of steps may also enable one party to unduly delay a resolution to the dispute further (which may in turn increase cost).

However, providing that the clause is drafted carefully and clearly, and is appropriate to the particular contract, a dispute escalation clause can be a very useful means of encouraging parties to resolve a dispute without recourse to litigation.

Conclusion

In summary, there are a variety of dispute resolution mechanisms to choose from, each with particular advantages and disadvantages that will make them more or less suitable for a particular type of contract.

Litigation should frequently be the last resort. It is advisable therefore for businesses to consider the other options that are available in advance of entering into contractual relations, and to choose the procedure that is likely to be best suited to the types of disputes that are likely to arise.

Andrew Tibber
Burges Salmon LLP
T 0117 902 7758
E andrew.tibber@burges-salmon.com

Georgina Shaw
Burges Salmon LLP
T 0117 307 6871
E georgina.shaw@burges-salmon.com