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PRE-ARBITRAL PROCESS - AN OBLIGATION OR A FORMALITY?

Authored By- Akash Chatterjee & Moulinath Moitra

Abstract

Arbitration has grown in importance tremendously over the years centering its focus in commercial and business matters especially. While the process is really effective and yields good results too as compared to the long haul of litigation, there is a proper system that needs to be followed. The matter of concern for this particular research is the pre-arbitral stage of any dispute. The pre-arbitral stage is interpreted differently by courts and it assumes particular significance in shaping conformity to it. This paper analyses the validity of obeying and not obeying the same and analyses two different perspectives on the same.

KEYWORDS-

Pre-arbitral

Arbitration

Case laws

Conformity

Mandatory

Discretionary.

MERE FORMALITY PERSPECTIVE-

Various decisions in the case of *VISA International Limited v. Continental Resources (USA) Limited*¹ have shown how the Court interprets intention of parties to decide on such pre-arbitration agreements. In the present case the intention of having a sound communication and exchange of perspectives has been duly carried out by the recorded communication between them.

¹VISA International Limited v. Continental Resources (USA) Limited [2008] Arbitration Petition No. 16 of 2007

*Quick Heal Technologies Limited v. NCS Computech Private Limited*² was an important step in determining the nature of these agreements as in this case, the court held that arbitration initiation was not pre-mature due to noncompliance of pre-arbitration proceedings because the prior correspondence between the related parties had left no scope for an amicable settlement and the disputes needed to be settled.

The analysis of the nature of the proceedings depend on a case-to-case basis and in the present situation, correspondence between the parties had been quite regular till the moment cooperation failed and the resolution of disputes could have been no longer continued with agreements. In such cases where arbitration becomes rather inevitable towards dispute resolution, the pre-arbitral escalation gets reduced to a mere formality.

Deciphering the nature of dispute against the factual matrix got highlighted in the decision of the Supreme Court in *M/S Imz Corporate Pvt Ltd vs Msd Telematics Pvt Ltd*³, wherein the Court observed that the conduct of the parties was such that relegating them to the pre-arbitration stage and complying with the same would be a mere empty formality and having ignored that can in no way prejudice the arbitration proceeding.

The primary objective of such procedural formalities depends on the scope of arriving at a mutually agreed solution and preventing the escalation of the dispute further. It is almost as if exploring the last available options to encourage greater cooperation and avoid the last resort to arbitration. Hence the nature of the same is not a mandatory condition but a general advisory. Since the entire process depends on the will and intention of the parties, hence its application can also differ from case to case and the nature of the present dispute very clearly eliminates any cooperative settlement to be arrived at, thereby depending on arbitration finally.

The traditional jurisprudential attitude towards pre-arbitration clauses has been one of non-mandatory as evident in cases like *Sulamerica Cia Nacional de Seguros SA v Enesa Engenharia SA*⁴, *Wah v Grant Thornton International Ltd*⁵, clearly due to the lack of certainty in them.

² Quick Heal Technologies Limited v. NCS Computech Private Limited [2020]Arbitration Petition No.43 of 2018

³ M/S Imz Corporate Pvt Ltd vs Msd Telematics Pvt Ltd ARB.P. 204/2021

⁴ Sulamerica Cia Nacional de Seguros SA v Enesa Engenharia SA 2012 EWCA Civ 638

⁵ Wah v Grant Thornton International Ltd 2012 EWHC 3198 (Ch)

In the case of *Walford v Miles*⁶, it was adjudicated by the House of Lords that the lack of certainty in the negotiation agreement made it unenforceable. The reasoning stemmed from want of grounds to make a particular agreement enforceable and to reasonable calculate time and delay in going through the process as well.

This case became a much-cited authority with increasing reliance being placed on the agreements' certainty to construe its mandatory obligation. It is evident in cases like *Courtney & Fairbairn Ltd. v Tolaini Brothers*⁷ and *Dhanani v Crasnianski*⁸ as well as in *Shaker v Vistajet*⁹.

The extent to which such negotiations can be carried on and the degree of applicability has been quite controversial in various judgements, with one leading case of *Cable & Wireless v IBM*¹⁰ in which the bonafide attempt of parties to solve disputes in good faith, their efforts through authorized representatives was recognized as well.

In the case of *Emirates Trading Agency LLC v. Prime Mineral Exports Private Limited*¹¹ one important aspect was pointed out which was phrased as – “friendly discussions”, to which the parties were required to resort to.

The abovementioned authorities clearly enable a proper construction of a pre-arbitral clause -

- Sought to provide for a reinforcing cooperative mechanism.
- Encouraged mutual resolution of the disputes and a proper communication between the parties
- Aimed at keeping channels of dispute resolution open between the parties.

Another important perspective was provided by the ruling in the case of, *S Kumar Construction Co and Anr. vs. Municipal Corporation of Greater Bombay*¹² where two conditions were held to satisfy the test of whether the pre-arbitration process is mandatory, namely –

- The nature of drafting language in the contract
- Facts of the case in which the same would be applicable.

⁶ Walford v Miles 1992 2 AC 128

⁷ Courtney & Fairbairn Ltd. v Tolaini Brothers [1975] 1 WLR 297

⁸ Dhanani v Crasnianski [2011] EWHC 926 (Comm)

⁹ Shaker v Vistajet [2012] EWHC 1329 (Comm)

¹⁰ Cable & Wireless v IBM [2002] EWHC 2059 (Comm), [2002] CLC 1319

¹¹ Emirates Trading Agency LLC v. Prime Mineral Exports Private Limited [2014] EWHC 2104 (Comm)

¹² S Kumar Construction Co and Anr. vs. Municipal Corporation of Greater Bombay (APPEAL NO.914 OF 2003 in ARBITRATION PETITION NO.286 OF 1996)

In the light of this judgement, a discretionary and advisory clause of pre-arbitration can be attributed to a clause due to the following points-

- Lack of clarity on the methods
- Lack of certainty of the time period for compliance
- Absence of a pre-condition or a prerequisite being expressly mandatory
- Remedies or provisions for noncompliance of pre-arbitration escalation not specified as well.

The need to expedite the process and settle a remedy is one of the most important reasons to choose arbitration. In the case of *Shin-Etsu Chemical Co. Ltd. v. M/s. Aksh Optifibre Ltd.*¹³ it was held that the purpose of the process would be defeated if the expedited arbitration action will not be commenced and there would be a long haul even before beginning with the same.

The importance of the intention of the parties has to be ascertained as guided by the Supreme Court in the case of *Visa International Ltd v. Continental Resources (USA) Ltd*¹⁴, and in the present case the escalation procedure and the correspondence is evident enough to show the inclination towards reaching arbitration stage by both the parties.

With reference to the same issue, Supreme Court has also dealt the case of *Zhejiang Bonly Elevator Guide Rail Manufacture Co. Ltd. Vs. Jada Elevator Components*¹⁵, where intention of the parties to settle differences was evident through the nature of correspondence between them.

The most relevant judicial ruling, however came up in the case of *Rajiv Vyas v. Johnwin Manavalan*¹⁶, wherein it was held that a condition precedent to arbitration if not fulfilled would not per se invalidate the proceedings thereof.

Hence, it is established that the nature of pre-arbitration escalation procedure is non mandatory and its application is decided according to the case ad its importance lies with the intention of the parties aligned with the dispute.

¹³ *Shin-Etsu Chemical Co. Ltd. v. M/s. Aksh Optifibre Ltd.* AIR 2005 S.C. 3766

¹⁴ *Visa International Ltd v. Continental Resources (USA) Ltd* (2009) 2 SCC 55

¹⁵ *Zhejiang Bonly Elevator Guide Rail Manufacture Co. Ltd. Vs. Jada Elevator Components* (2018) 9 SCC 774

¹⁶ *Rajiv Vyas v. Johnwin Manavalan* (2010) 6 Mh.L.J. 483

This view has been further reiterated in the case of *Tulip Hotels Pvt Limited v. Trade Wings Limited*¹⁷ where a mere disagreement in participating in condition precedent to arbitration was held not to impact the validity of arbitration proceedings.

The view in *Ravindra Kumar Verma vs M/S. Bptp Ltd. & Anr*¹⁸ has been quite direct; that the nature of pre-arbitration agreements are directory and they cannot be interpreted as mandatory.

In the case of *M/s Haldiram Manufacturing Company Pvt. Ltd v. M/s DLF Commercial Complexes Ltd*¹⁹, the mandatory nature of pre-arbitral steps was highlighted, and this decision as subsequently overruled as well in the cases of *Siemens Ltd. vs. Jindal India Thermal Power Ltd*²⁰ and *Sarvesh Security Services Pvt Ltd vs Managing Director, DSIIDC*²¹ which further stated the entire process to be optional as well.

The ambiguity around whether or not pre-arbitral clauses are mandatory was settled by the case of *Holloway v Chancery Mead Limited*²² in which three clear conditions were laid down

- The process must be sufficiently certain such that it rules out an chances of agreement in commencing it.
- The administration of the process should be definite and a model approach must be specified
- Process of selecting appropriate persons and paying them must also be described in the agreement.

In the case of *Sul America v Enesa Engenharis*²³, the dispute was regarding a pre-arbitral obligation which stated that the parties should resort to mediation. The court held such a clause to be non -mandatory because there was no definite clarity as to the rights of the parties in the process concerned.

In the cases of *Sikand Construction Co. v. SBI*²⁴ and *Saraswati Construction Co. v. East*

¹⁷ Tulip Hotels, Pvt Limited v. Trade Wings Limited 2010 2 ArbLr 286

¹⁸ Ravindra Kumar Verma vs M/S. Bptp Ltd. & Anr C.M.(M) No.1021/2014

¹⁹ M/s Haldiram Manufacturing Company Pvt. Ltd v. M/s DLF Commercial Complexes Ltd IA No. 3363/2011 in CS(OS) 2288/2010

²⁰ Siemens Ltd. vs. Jindal India Thermal Power Ltd ARB.P. 243/2017

²¹ Sarvesh Security Services Pvt Ltd vs Managing Director, DSIIDC ARB.P. 181/2014

²² Holloway v Chancery Mead Limited 2007 EWHC 2495 (TCC)

²³ Sul America v Enesa Engenharis [2012] 1 Lloyd's Reports 671

²⁴ Sikand Construction Co. v. SBI 1978 SCC OnLine Del 180 : ILR (1979) 1 Del 364

*Delhi Coop. Group Housing Society Ltd*²⁵ it was clarified that the nature of pre-arbitral steps are not a mandatory requirement that has to be followed.

THE OTHER PERSPECTIVE –

In the light of growing demand for arbitration as a dispute resolution mechanism, the mutual cooperation of the parties becomes the most fundamental aspect in the adjudication mechanism. Whereas in this case, the actions of the employer in deliberately ignoring the pre-arbitration stage cannot be excused.

The recent English case of *Republic of Sierra Leone v. SL Mining Limited*²⁶ discussed a related principle of law-

- The matter of dispute related to a multitier dispute resolution and the non-observance of pre-arbitration procedures.
- This led to challenging of the arbitral award and the Court inspected into the arbitration agreement.
- It was a matter of admissibility as decided by the Court.
- The same has also been clarified by cases like *-BG Group v. Republic of Argentina*²⁷ and *BBA v. BAZ*²⁸ and *BTN v BTP*²⁹, a Singapore case.

Further in the case of *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd*³⁰, the importance of pre-arbitration dispute resolution strategies as agreed to be resorted to have been given high importance. It was also determined to be well enforceable.

The case of *NWA & ors v NVF & Ors*³¹ also holds that the compliance with pre-arbitral proceedings is a matter of admissibility and that has to be taken into account before beginning the arbitration procedure.

If in any well-defined pre-arbitration dispute escalation has been laid down and the failure to comply with the same should be taken into account before the arbitration process begins.

English Courts have interpreted on this issue in yet another situation of *Ohpen Operations v Invesco*³²-

²⁵ *Saraswati Construction Co. v. East Delhi Coop. Group Housing Society Ltd* 1994 scc online del 563

²⁶ *Republic of Sierra Leone v. SL Mining Limited* (2021) EWHC 286 (Comm)

²⁷ *BG Group v. Republic of Argentina* 134 S.Ct. 1198 (2002)

²⁸ *BBA v. BAZ* (2020) 2 SLR 453

²⁹ *BTN v BTP* 2020 SGCA 105

³⁰ *Emirates Trading Agency LLC v Prime Mineral Exports Private Ltd* . 2014 EWHC 2104 (Comm)

³¹ *NWA & ors v NVF & Ors* 2021 EWHC 2666 (Comm)

³² *Ohpen Operations v Invesco* 3 2019 EWHC 2246 (TCC)

- In this particular disputed contract, there was a pre-arbitration stage - a mediation stage as a mandatory escalation procedure to be adhered to in order to proceed to the arbitration stage.
- The observations in this case were made on some of the following legal principles –
 - Expression of condition precedent clearly in the contract
 - Agreement creating an obligation resorting to alternative dispute resolution.
 - The process does not have to be necessarily formal but must be clear and certain, objectively oriented and involving any third party or mediator or any other mechanism to fulfil the purpose aimed.
- Applying these principles in the case, the arbitration proceedings were stayed, as the pre-arbitration agreement was obligation and had to be construed along with the contract itself, the dispute resolution created a condition precedent even though the exact terminology was not used, and in essence had to be carried out.
- The provisions were clear enough to be mandatorily enforced and interpreted and hence avoiding it was held to be a breach.

In the case of *Emirates Trading Agency LLC v Prime Mineral Exports Pte Ltd (Emirates)*³³, it was held that any noncompliance with the pre-arbitration conditions which form a part of arbitration agreements can render the jurisdiction of the arbitration tribunal questionable as they are mandatory in nature.

It has been an accepted viewpoint that the nature of such agreements varies from contract-to-contract basis and have to be interpreted accordingly as well. The specific words and the way of drafting the clauses provides necessary guidance to the Court to decide on the applicability and nature of the same.³⁴

The case of *Wah v Grant Thornton*³⁵, analysed the criteria for compliance –

- It is a positive obligation aiming at an amicable resolution of the dispute.
- Sufficiently certain and an unequivocal commitment towards a process
- The process should be able to guide the prescribed steps which a party is required to take or carry out

³³ *Emirates Trading Agency LLC v Prime Mineral Exports Pte Ltd (Emirates)* EWHC 2014 (Comm),

³⁴ Jan Paulsson, “Jurisdiction and Admissibility” in *Global Reflections on International Law, Commerce and Dispute Resolution, Liber Amicorum in honour of Robert Briner* [2005] [601].

³⁵ *Wah v Grant Thornton* 2012 EWHC 3198 (Ch)

- A degree of minimum involvement and the extent to which such process would continue should also be specified in the same.

In the case of *Cable & Wireless PLC v IBM United Kingdom Ltd*³⁶, it was stated that any dispute resolution mechanism through ADR techniques in a contract is mandatorily enforceable and hence an obligation.

A pre-arbitral dispute needs to be mandatorily followed when -

- The nature of drafting the clause is one bearing the essence of a precondition.
- Is sufficiently precise and conforms to judgements declaring such escalation to be a necessary precondition to arbitration.
- Imposes an obligation on the parties to obey the same just like the other clauses of the contract.

In *Burlington Resources Inc. v Republic of Ecuador*³⁷ it was settled that when a particular valid precondition is laid down, the non-observance of the same disputed the jurisdiction of the tribunal.

Pre-arbitration necessities are typically a question of admissibility and affects the nature of claims forwarded in the dispute. The jurisdiction of the tribunal maybe settled with the necessary contract, but the question of admissibility has to determine whether the tribunal can at all adjudicate and admit the argument on claims and the entire process thereof.³⁸

On adjudicating a non-compliance, the nature and need for a remedy becomes an important question regarding which it has been widely accepted that either the defect of noncompliance be cured – by allowing the parties to correct the procedure or dismiss the claim in its entirety.³⁹

The Contractor humbly draws the attention of the tribunal to the nature of adjudicated judicial rulings and carefully consider the noncompliance breach in the present case before adjudicating the matter further.

In *Oriental Insurance Company v. M/s Narbheram Power and Steel*⁴⁰ and in case of *United*

³⁶ Cable & Wireless PLC v IBM United Kingdom Ltd 2002 EWHC 2058 (Comm)

³⁷ Oriental Insurance Company v. M/s Narbheram Power and Steel ICSID Case No. ARB/08/5

³⁸ Gary Born, International Commercial Arbitration (2014) 935

³⁹ Alexander Jolles, Consequences of Multi-tier Arbitration Clauses: Issues of Enforcement [2006] 72 Arbitration, 337.

⁴⁰ Oriental Insurance Company v. M/s Narbheram Power and Steel CIVIL APPEAL NO. 2268 OF 2018

*India Insurance Co. v. Hyundai Engineering and Construction Co*⁴¹, it has been emphasised that arbitration clause has to be strictly construed in the agreement, and the clauses have to be understood with respect to how do they express the intention of the parties in arbitration.

In *Distilleries Private Limited v. Demerara Distillers Limited*, the agreement required the parties to solve the disputes first through a mediation. One of the parties had skipped the stage and directly proceeded towards arbitration, Here Supreme Court held it to be premature for want of adequate compliance with necessary processes.

In a recent High Court case - *Sanjay Iron and Steel Limited v. Steel Authority of India*⁴², where a particular pre-condition of conciliation was agreed to by the parties and set out as a pre-arbitral step, that could not be avoided for reasons of expenditure.

The aforementioned case laws set out a standard of importance that is affixed on a precondition to arbitration, by way of emphasising the vital significance of agreement and consensus on the same. The entire arbitration way is a dispute resolution and goal-oriented mechanism that strives to expedite the process and hence such tiers of the process must be duly respected and obliged.

In *Nirman Sindia vs Indal Electromelts Ltd*⁴³, it was held that when the parties decide to resort to a particular mode of dispute resolution, they are under an obligation to obey the same and that skipping a stage of the same cannot be allowed.

The mandatory interpretation of the pre-arbitral escalation gained impetus from the judgement in the case of *International Research Corp PLC v. Lufthansa Systems Asia Pacific Pte Ltd and Another*⁴⁴, where it was decided that the compliance of pre-arbitral dispute resolution was mandatory and any failure of the same could oust the jurisdiction of the tribunal.

The contractual aspect of obeying a laid down and consented precondition was highlighted in the case of *S.B.P. & Co vs Patel Engineering Ltd. & Anr*⁴⁵, where it was held that the parties sign and agree on mutual terms to go through a specific procedure which they cannot refrain from in the matter of disputes.

⁴¹ United India Insurance Co. v. Hyundai Engineering and Construction Co CIVIL APPEAL NO. 8146 OF 2018,

⁴² Sanjay Iron and Steel Limited v. Steel Authority of India ARB.P. 408/2021

⁴³ Nirman Sindia vs Indal Electromelts Ltd AIR 1999 Ker 440

⁴⁴ PLC v. Lufthansa Systems Asia Pacific Pte Ltd and Another 2013 SGCA 55

⁴⁵ S.B.P. & Co vs Patel Engineering Ltd. & Anr Appeal (civil) 4168 of 2003

In the leading case of *M.K Shah Engineers & Contractors v. State of M.P.*⁴⁶, it was settled by the Supreme Court that the pre-arbitration procedures are mandatory compliance and the parties cannot skip or bypass them.

The increasing need for arbitration mechanism has opened up different tiers of the process leading up to arbitration as the final stage. This is exceptionally important in the construction contracts having high degrees of technicality and knowhow and requiring involvement of management, administrative personnel to work out dispute resolution among them.⁴⁷

Studies have shown how the presence of a mediator in aiding both the parties to reach mutually agreed settlement has helped in the dispute resolution mechanism.⁴⁸

In the case of *Simpark Infrastructure (P) Ltd. v. Jaipur Municipal Corpn*⁴⁹, it was held that the amicable solution finding was a condition precedent to arbitration and the process has to be followed in order.



⁴⁶ M.K Shah Engineers & Contractors v. State of M.P (1999) 2 SCC 594

⁴⁷ James H. Carter, Issues Arising from Integrated Dispute Resolution Clauses: Part I, in New Horizons in International Commercial Arbitration and Beyond, ICCA Congress Series No. 12, 446 [A.J. van den Berg (Ed.), 2005].

⁴⁸ Martin Hunter, The Freshfields Guide to Arbitration and ADR: Clauses in International Contracts, Kluwer Law and Taxation Publishers, 1993, 64.

⁴⁹ Simpark Infrastructure (P) Ltd. v. Jaipur Municipal Corpn 2012 SCC Online Raj 3833