

CONSTRUCTION LAW INTERNATIONAL

FROM THE IBA INTERNATIONAL CONSTRUCTION PROJECTS COMMITTEE OF THE
ENERGY ENVIRONMENT, NATURAL RESOURCES AND INFRASTRUCTURE LAW SECTION (SEERIL)

Vol 14 ISSUE 1

ISSN 1819-1371

NOVEMBER 2019



the global voice of
the legal profession

**IFRS 15 legal
implications**

**Dispute resolution
processes**

**Contract
repudiation**

The Swiss Federal Supreme Court stays arbitration proceedings because the parties skipped mandatory pre-arbitral steps



Introduction

The Swiss Federal Supreme Court (the ‘Supreme Court’) has revisited an earlier decision of 2014 on the consequences for arbitration proceedings seated in Switzerland if the parties have skipped mandatory pre-arbitral steps.

In a decision dated 7 July 2014 (4A_124/2014),¹ the Supreme Court held that the proceedings under the Dispute Adjudication Board (DAB) according to Clause 20 of the FIDIC conditions of 1999 were a mandatory pre-arbitral step. However, the ad hoc DAB had not been constituted for more than 18 months.

Juliette Asso

LALIVE, Geneva

Angela Casey

LALIVE, Zurich

Consequently, the Supreme Court did not allow the party challenging the arbitral tribunal's jurisdiction to rely on the argument that the DAB procedure was mandatory in the present case.²

In the more recent landmark decision, FSC 142 III 296, dated 16 March 2016 (4A_628/2015),³ the Supreme Court seized the opportunity to clarify one important aspect that had not been decided in the previously mentioned decision: the consequences to the arbitration proceedings if the parties have skipped mandatory pre-arbitral steps. In the 2016 decision, the Supreme Court ordered the arbitral tribunal to stay the arbitration proceedings, but it did not annul the award entirely because this would have made it necessary for the arbitration to be commenced again with a completely new arbitral tribunal.

In the 2016 decision, the Supreme Court ordered the arbitral tribunal to stay the arbitration proceedings, but it did not annul the award entirely.

Facts of the decision

Both parties to the arbitration are involved in the exploration and production of hydrocarbons in Algeria. The contract of association between the parties contained the following dispute resolution and arbitration clause:

'Any disagreement between the Parties as to the performance or the interpretation of this Contract, which cannot be settled by the parties, shall firstly be the object of an attempt at conciliation pursuant to the ADR (Alternative Disputes Resolution) Rules of the International Chamber of Commerce (ICC).

Any disagreement between the Parties as to the performance or the interpretation of this Contract, which is not resolved by way of conciliation, shall be decided in last instance by arbitration in accordance with the UNCITRAL arbitration rules by three (3) arbitrators appointed in conformity with such rules.

Applicable law shall be the law of [name of country omitted]. The place of arbitration shall be Geneva, Switzerland. The language of arbitration shall be French. However, English may be used if necessary.⁴

Following disagreements between the parties, the Respondent initiated conciliation

proceedings under the ICC Amicable Dispute Resolution Rules of 2001 (the 'ADR Rules').⁵

The appointed 'Neutral' (in the language of the ADR Rules) asked a series of questions pertaining to the conduct of the conciliation and proposed a meeting. The Respondent requested that the meeting took place by way of telephone conference, to which the Appellant agreed. The Respondent's counsel suggested using its conferencing system to facilitate the participation of the Respondent's representatives. The Appellant firmly opposed this suggestion, as the conference was scheduled between the parties' legal representatives only. Following this, the conciliation meeting was postponed, but subsequently never rescheduled.

After the Neutral inquired about the continuation of the conciliation, the Respondent filed a request for arbitration. On the same day, the Respondent sent a letter to the Neutral stating that the conciliation had failed due to the Appellant's behaviour.

During the first stage of the arbitration, the Appellant reserved the right to challenge the jurisdiction of the arbitral tribunal insisting that the mandatory pre-arbitral conciliation according to the ADR Rules had not been complied with. Following an exchange of submissions on the issue, the arbitral tribunal issued an interim award, according to which it accepted its jurisdiction.⁶

Subsequently, the Appellant filed a motion to set aside the interim award before the Supreme Court for the lack of the arbitral tribunal's jurisdiction *ratione temporis* according to Article 190(2)b of the Private International Law Act (PILA).

The Supreme Court's ruling

First, the Supreme Court had to assess whether or not the conciliation was mandatory. In confirmation of its earlier ruling pertaining to the FIDIC conditions,⁷ the Supreme Court held that conciliation is a mandatory pre-arbitral step if the parties have agreed to a structured institutional framework with a procedure that covers every step in the process, such as the ADR Rules of the ICC.⁸

The Supreme Court held that the Respondent did not comply with the mandatory conciliation. According to the ADR Rules, the parties may not withdraw from the conciliation procedure before the parties have met with the Neutral.⁹ The exchange of several letters and emails

concerning the coordination of a date for a meeting was not considered to be a sufficient attempt at conciliation.¹⁰

Second, the Supreme Court assessed whether the Appellant invoked the arbitral tribunal's failure to abide by the pre-arbitral steps in an abusive way as prohibited under Article 2(2) of the Swiss Civil Code.¹¹ The Supreme Court noted that the manifest abuse of a (procedural) right was not protected by the law. However, the Supreme Court did not consider the Appellant's behaviour as obstructionist. Rather, the Supreme Court accepted the Appellant's explanation that it was taken aback by the proposal that the Respondent's party representatives were going to take part in the telephone conference that was scheduled to start ten minutes later.¹²

Third, the Supreme Court answered the unsettled question on how such a breach of a mediation agreement should be sanctioned. It considered three alternatives:

- *To continue the arbitration proceedings and to sanction the party refusing to comply with the pre-arbitral steps with damages:* The Supreme Court considered this solution to be unsatisfactory because it would deprive the mediation proceedings of its purpose to reach a settlement. Further, the Supreme Court considered the difficulties in establishing the quantum of such a damage.¹³
- *To declare the claim inadmissible and close the arbitration proceedings:* The Supreme Court did not consider this appropriate either, as it would close the arbitral tribunal's mandate and the arbitral tribunal would have to be reconstituted. Furthermore, the proceedings would be prolonged, which would create additional costs to the detriment of both parties. Since conciliation procedures do not stop or interrupt the statute of limitations, there is also the potential danger that a claim could be rejected because, by the time the new request for arbitration has been filed, the action may be time barred.¹⁴
- *To set aside the interim award on jurisdiction and stay the arbitration proceedings until the conciliation procedure is concluded:* This practical approach was the preferred solution by the Supreme Court. It further set a time limit of multiple months to enable the parties to proceed with the conciliation proceedings.¹⁵

After the decision by the Supreme Court was rendered, the parties held the necessary

conciliation meetings but were unable to reach an amicable solution. The arbitration thus continued before the arbitral tribunal.¹⁶

Commentary and outlook

This landmark decision is particularly relevant for international construction contracts because they frequently contain multi-tier dispute resolution or escalation clauses, which set out that parties must resort to mediation, conciliation or dispute resolution boards before proceeding to arbitration.

The Supreme Court confirms that in arbitration proceedings conducted in Switzerland, the parties should carefully follow the dispute resolution clause and the required pre-arbitral steps to avoid an appeal of the arbitral tribunal's award on jurisdiction, which inevitably would prolong the proceedings.

At the earlier stage of the drafting of the dispute resolution clause, it is important to

The parties should carefully follow the dispute resolution clause and the required pre-arbitral steps to avoid an appeal of the arbitral tribunal's award on jurisdiction.

come up with realistic and practical steps that hold up in multiple scenarios. Later, when a party is already preparing for arbitration proceedings, the parties should carefully check whether any dispute resolution clauses could have been incorporated by reference in the arbitration clause, a practice that is widely accepted in Switzerland.

Considering this ruling of the Supreme Court, parties should not take for granted that they can instrumentalise the pre-arbitral proceedings to delay the arbitration. In its analysis, the Supreme Court emphasised that the Appellant, who made the objection against the arbitral tribunal's jurisdiction and requested the setting aside of the interim award, had sufficiently participated in the conciliation proceedings. It further held that the Appellant did not abuse any rights, although it refused to participate in the telephone conference after learning that the other side's party representatives would be present.

A few examples of institutions that contain pre-arbitral steps that could be included in

arbitration clauses for arbitrations seated in Switzerland are:

- FIDIC¹⁷ – the new editions of the FIDIC Red Book, Yellow Book and Silver Book came into force in December 2017. While the new FIDIC conditions are generally intended to increase clarity and certainty, they now also provide for standing dispute adjudication boards (formerly DAB, now the Dispute Avoidance/Adjudication Board (DAAB)). According to Clause 21, disputes need to be referred to the DAAB within 42 days.
- ICC Mediation Rules of 2014¹⁸ – the ICC Mediation Rules provide users with clear parameters for the conduct of the mediation proceedings but at the same time seek to maintain flexibility. The ICC also publishes several mediation clauses that parties can include in their contract.¹⁹
- Swiss Rules of Commercial Mediation²⁰ – the Swiss Rules of Commercial Mediation provide for a detailed procedure and offer a multitude of arbitration clauses.

Notes

- 1 See the decision of the Supreme Court, 4A_124/2014, dated 7 July 2014 (the decision was issued in French, but an English translation is available at www.swissarbitrationdecisions.com).
- 2 Adrian Bell, 'Swiss Court considers effect of FIDIC, clause 20 where no DAB has been constituted' *IBA Construction Law International*, Vol 9, Issue 4, December 2014, 4.
- 3 The decision was issued in French and is translated to English at www.swissarbitrationdecisions.com accessed 15 October 2019.
- 4 Decision of the Supreme Court, ATF 142 III 296, dated 6 March 2016, cons A.b.
- 5 *Ibid.*, cons A.c.
- 6 *Ibid.*, cons B.
- 7 Decision of the Supreme Court, 4A_124/2014, dated 7 July 2014, cons 3.4.3.3.
- 8 Decision of the Supreme Court, ATF 142 III 296, dated 6 March 2016, cons 2.4.1.2. The ICC ADR Rules of 2001 are available at <http://gipi.org/wp-content/uploads/icc-adr-rules.pdf>, accessed 15 October 2019, but have been replaced by the ICC Mediation Rules

of 2014; see paragraph 19 at <https://iccwbo.org/dispute-resolution-services/mediation/mediation-rules> accessed 15 October 2019.

- 9 *Ibid.*, cons 2.4.2.
- 10 *Ibid.*
- 11 *Ibid.*, cons 2.4.3.2.
- 12 *Ibid.*
- 13 *Ibid.*, cons 2.4.4.1.
- 14 *Ibid.*
- 15 *Ibid.*
- 16 After it was established that the conciliation procedure has not led to a settlement, the arbitral tribunal resumed with the proceedings and issued two procedural orders regarding the second phase of the arbitration. The Respondent, however, filed another motion before the Supreme Court to annul both procedural orders and to hold that the arbitral tribunal did not have jurisdiction *ratione temporis* between 22 May 2015 and 1 June 2016 (decision of the Supreme Court, 4A_524/2016, dated 20 September 2016). Within less than a week, the Supreme Court issued a ruling holding that a procedural order is not capable of an appeal (unless the arbitral tribunal implicitly ruled on its own jurisdiction). The Supreme Court further explained that the content of the procedural orders had corresponded with the scope the Supreme Court intended to give its earlier decision in the same case and thus rejected the appeal without any further ado.
- 17 See, for a detailed overview: Ben Mellors, 'Second editions of the FIDIC Rainbow Suite' *IBA Construction Law International*, Vol 13, Issue 1, March 2018, p 64 et seq.
- 18 See <https://iccwbo.org/dispute-resolution-services/mediation/mediation-rules> accessed 15 October 2019.
- 19 *Ibid.*
- 20 See www.swissarbitration.org/Mediation/Mediation-rules accessed 15 October 2019.

Juliette Asso is an associate at LALIVE in Geneva and can be contacted at jasso@lalive.law.

Angela Casey is an associate at LALIVE in Zurich and can be contacted at acasey@lalive.law.