When an agreement to arbitrate is not an agreement to arbitrate

by DOUG JONES

JUST how much control over the means of resolving disputes do the parties to construction contracts really have?

And how much faith can be placed in past court decisions on this — including consistent court decisions on whether the courts may be excluded and alternative forms of dispute resolution used instead?

The answer, at least according to the Queensland Supreme Court, now seems to be: it all depends.

For several years it has been generally understood, on the basis of decisions by the High Court and others, that construction contract dispute resolution clauses which give "either party" the right to elect to refer disputes to arbitration or litigation are "agreements in writing to refer present or future disputes to arbitration", and are thus valid and enforceable "arbitration agreements" for the purposes of the Commercial Arbitration Act.

This means both parties are bound by Commercial Arbitration Act provisions under which, if one of the parties has commenced court proceedings, the other party may have these proceedings stayed if it is willing to have the matter arbitrated and there is no other reason why the dispute cannot be arbitrated.

In the 1995 High Court case PMT Partners v Australian National Parks and Wildlife Service, for example, the court decided that the words "agreement ... to refer present or future disputes to arbitration" are quite wide enough to encompass agreements binding the parties to have their dispute arbitrated if an election is made or some event occurs or one condition is satisfied, even if only one of the parties has the right to elect or only one of the parties is able to control the event or satisfy the condition.

Similarly, in the 1999 Manningham City Council case the Victorian Court of Appeal decided that section 13 of the Building Works Contract JCC-D 1994 is a binding arbitration agreement, even though the right it gives to "either party" to refer a dispute "to arbitration or litigation" depends on an election's being made.

Now, however, an apparently inconsistent decision by the Queensland Supreme Court has held that clause 47 of the Australian Standard construction contract AS2124–1992 is not a binding arbitration agreement.

This case, Mulgrave Central Mill Co Ltd v Hagglunds Drives Pty Ltd, is likely to cause some confusion in an area of law which, until now, has been considered reasonably certain.

The plaintiff, Mulgrave Central Mill, commenced court proceedings following a failure of equipment supplied by Hagglunds.

Hagglunds responded by giving notice that it was referring the dispute to arbitration and by applying for a stay in the court proceedings on the basis that the contract contained a binding arbitration agreement.

Reasonable

The contract nominated alternative 1 of AS2124–1992's clause 47.2:

"In the event that the dispute can not be so resolved [by the parties conferring], or if at any time either party considers that the other party is not making reasonable efforts to resolve the dispute, either party may, by notice in writing delivered by hand or sent by certified mail to the other party, refer such dispute to arbitration or litigation."

So the primary issue was whether this clause 47 amounted to an "arbitration agreement" of the kind contemplated by the Commercial Arbitration Act.

Hagglunds argued that clause 47 of AS2124–1992 has the same effect as section 13 of JCC-D 1994, and relied on the Manningham City Council decision in support of its argument that the litigation should be stayed.

But the Queensland Supreme Court decided that Manningham was distinguishable, because section 13 of JCC-D 1994 contains a "significant" addition not found in clause 47 of AS2124–1992.

Sections 13.03 and 13.04 of JCC-D 1994 provide:

13.03 In the event that the dispute cannot be resolved in accordance with the provisions of Clause 13.02 [private negotiation], or if at any time either party considers that the other party is not making reasonable efforts to resolve the dispute, either party may, by further notice in writing which shall be delivered by hand or sent by certified mail to the other party, refer such dispute to arbitration or litigation. The service of such further notice under this Clause 13.03 shall also be a condition precedent to the commencement of any arbitration or litigation proceedings in respect of such dispute.

13.04 At the time of giving the notice referred to in Clause 13.03, the party who wishes the dispute to be referred to arbitration shall provide to the other party evidence that he has deposited with the Chapter of the Royal Australian Institute of Architects or the Master Builders' Association, in each case of the State, Territory or place in which the Site is located, the sum of one thousand dollars ($1000.00) by way of security for costs of the arbitration proceedings. Subject to compliance with the provisions of Clause 13.03 and the foregoing provisions of this Clause 13.04, such dispute or difference (unless meanwhile settled) shall be and is hereby referred to arbitration pursuant to the succeeding provisions of this Section 13.

The last sentence of clause 13.04 was considered significant by the court, although the precise significance of these words remains somewhat obscure.

Justice White observed, "Such an intention to have disputes resolved exclusively by arbitration, if the preconditions are satisfied, cannot be found in clause 47 of AS2124," and concluded that clause 47 did not demonstrate the parties' intention to agree that a unilateral election to refer a dispute to arbitration would be binding on both parties.

The decision of Mulgrave Central Mill, which is now being appealed, is difficult to reconcile with the cases of PMT Partners and Manningham, so the law in Queensland is far from clear.

It is unclear whether courts in other jurisdictions, outside Queensland, will follow or be influenced by the decision.

Enforceability

What is clear, however, is that parties which have contracted using the AS2124 form of contract, or contracts with similarly worded dispute resolution clauses, now cannot be certain that their agreement includes a binding arbitration agreement.

It is not just the question of whether court proceedings can be stayed that is at stake. There is now uncertainty about the validity of arbitration proceedings commenced in accordance clause 47 of AS2124 (or similarly worded clauses) and the enforceability of arbitral awards delivered in these arbitrations.

So if you wish to use AS2124-1992 or another form of contract with a similarly worded dispute resolution clause, and you want to ensure that the contract includes an arbitration agreement which is definitely enforceable under the Commercial Arbitration Act, amendments to clause 47 are equally definitely in order.

The amendments themselves, while necessary, will not need to be complex. The more difficult task will be to anticipate the next move of the courts! ■

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Fixing shoddy work is not enough

LAWYERS warn building and construction companies that the price of shoddy workmanship can be much higher than just the cost of "putting things right".

Stewart Nankervis, a construction lawyer with international law firm Minter Ellison, says that the courts consider that merely rectifying defective work is sometimes inappropriate and is not always an adequate way of compensating owners.

Nankervis points to a recent court case in which the builder and engineers of a block of residential and commercial units were sued by the owner for defective work which caused severe water and structural damage.

"Even though the builder carried out remedial work, a subsequent expert's report found that the building still had major defects," Nankervis says.

"The owners argued successfully that the damage and associated disruption had caused them a loss of amenity and, more importantly, that the defects had reduced their property's resale value. The builder was ordered to pay the owners compensation in addition to rectifying the defects," he says.

The decision, handed down by the Northern Territory Supreme Court, was in line with a landmark ruling made by a court in the House of Lords in 1995. That case involved a swimming pool that had not been dug to the depth specified in the contract.

"The UK court found that the cost of remedying the fault would be disproportionately high compared with the small 'loss of value' sustained by the owner," Nankervis says.

"Nevertheless, the owner received more than nominal damages for loss of amenity – described as 'disappointment of expectation' – which the court considered was more adequate and appropriate compensation than would have been arrived at by calculating mere loss of value.

"Unfortunately, there is no fixed rule of law that people can rely on when measuring damages of this sort.

"On its own, remedying the fault may not always be the end of such matters. Builders and their insurers should be aware that if work is subsequently found to be defective, their liability might extend further than rectification.

"However, the courts' view is that owners should be fairly and adequately compensated for the loss or injury they have sustained. The decision a judge reaches in a particular case will depend on the circumstances in which the defects occurred and what harm they caused," he says. ■