JUDGMENT : MR JUSTICE CRESSWELL: QBD. Commercial Court. 13th February 2004.

1. There are before the court (1) the claimant's application for directions under section 18 of the Arbitration Act 1996 ("the 1996 Act") and (2) the defendant's cross-application to strike out the claim on the basis that there is no valid arbitration agreement. Thus, the issues in dispute are (1) whether the agreement to which I will refer contains an enforceable agreement to arbitrate; and (2), assuming that it does, what directions are appropriate for the appointment of an arbitrator.

2. The present dispute arises out of a Heads of Terms Agreement ("the Agreement") entered into between the claimant, Flight Training International Inc (trading as Granite Corporation) ("Flight Training"), and the defendant, International Fire Training Equipment Ltd ("IFTE") in January 1999 concerning the supply of a specialist anti-terrorist training facility, a mock-up of a Boeing 747, to the Saudi Royal Guard. I should record for completeness that the defendant has reserved its position as to the status of Flight Training and whether Flight Training International Inc in fact trades as Granite Corporation, but it is common ground that, for the purposes of the applications before the court, I should assume that the claimant is correctly identified.

3. Flight Training supplies training services in relation to, among other things, military aviation, VIP protection, special forces, emergency service high speed response and pursuit driving, aviation fire-fighting and airport disaster control. Flight Training's principal clients are government agencies in the Middle East. IFTE designs and manufactures systems for the training of fire fighters.

4. In July 1998, Flight Training was approached by the Saudi Royal Guard and invited to make proposals for training them in aircraft anti-terrorism and hostage rescue. Flight Training subsequently developed a training programme involving the use of a steel aircraft mock-up equipped with various training systems and devices. Flight Training does not manufacture steel aircraft mock-ups. In November 1998 Flight Training contacted IFTE to see whether they would be interested in working with Flight Training in supplying mock-ups to Middle Eastern countries for security training purposes.

5. On 7 January 1999, the parties concluded the Agreement. Its purpose was to*: "... establish an Agreement in order that [Flight Training] ... and [IFTE] can work together to be successful in procuring the prospect that [Flight Training] has brought to [IFTE] i.e. the supply of a specialist anti-terrorist training facility, being a 747 simulator, to the Saudi Royal Guard."*

6. The parties' main obligations under the Agreement are set out in Articles III to V. Flight Training's obligations included an obligation to introduce the client to IFTE. IFTE's obligations included obligations (a) to use best endeavours to promote the use of Flight Training for special operations and security training purposes; and (b) to pay Flight Training a commission of 30 per cent of the value of all orders received within the specified areas defined in Article XIII and resulting from efforts under the Agreement, such payment to be made promptly (i.e. within seven days) of receipt by IFTE. Further, by Article V the parties were regularly to keep each other informed of material events which could affect their interests under the Agreement.

7. Article XI is at the centre of the issues before the Court and provides:

"XI Settlement of Disputes

Disputes between [Flight Training] and [IFTE] on the performance of this Agreement, shall be submitted to the Advisory, Conciliation and Arbitration Services (ACAS) London. Legal fees and costs shall be paid by either party which does not prevail at mediation."

8. Following conclusion of the Agreement, disputes arose between the parties. The following account is intended to identify the broad nature of the dispute between the parties without making any findings as to what in fact happened.

9. According to Flight Training, Flight Training entered into dialogue with representatives of the Saudi Royal Guard, IBCOL Technical Services GmbH (a German entity) and with IFTE and on 26 April 1999 Flight Training made a presentation of its proposals to the senior offices of the Saudi Royal Guard at a London hotel, and also introduced IFTE to the Saudi Royal Guard/IBCOL. The costs of this exercise were paid by Flight Training. Direct negotiations then ensued between IFTE and IBCOL/the Saudi

Royal Guard, and in June 1999 IBCOL informed Flight Training that the Saudi Royal Guard had selected the Boeing 747 steel mock-up with the systems proposed during the April presentation.

10. According to Flight Training, in July 1999. IFTE ceased all communication with Flight Training. A meeting between the parties eventually took place in October 1999 at which IFTE informed Flight Training that they were no longer promoting Flight Training as a training provider and that IFTE were now providing these services. A written approach by Flight Training to IFTE in late October 1999 seeking the amicable resolution of the parties' positions went unanswered.

11. According to Flight Training, in January 2000 IBCOL advised Flight Training that a contract worth several tens of millions of dollars had been concluded for the completion of the training project, including the aircraft mock-up. Flight Training sought further information from IFTE but received no response. In October 2001, IFTE announced on its website that it had secured a multi-million pound security trainer contract "from Germany", details of which were not released. Flight Training believe this to be the contract for the supply of training services and the aircraft mock-up to the Saudi Royal Guard.

12. Following the announcement IFTE's website, Flight Training sent draft particulars of claim dated 5 December 2001 (Queen's Bench Division, Blackpool District Registry) to IFTE and discussions then took place between the parties but no resolution was achieved. I refer to the draft particulars of claim for their full terms and effect. In the event proceedings were not commenced.

13. In November 2002, Flight Training contacted ACAS pursuant to Article XI of the Agreement seeking its assistance to resolve the dispute. In a letter headed Granite Corporation a Flight Training International Company, Mr Whitehead wrote on 21 November: *"A dispute has arisen regarding the performance of the attached Heads of Terms Agreement between Granite Corporation and IFTE Ltd ... Article XI Settlement of Disputes, directs the parties to submit disputes to ACAS. Please advise the appropriate procedure for the settlement of this dispute through ACAS. If ACAS is not constituted or chartered to resolve commercial contract disputes and is, therefore, unable to assist, we need a formal document which will be acceptable to a court with appropriate jurisdiction, either in the UK or the US, confirming that Article XI Settlement of Disputes is unenforceable. Your assistance in providing such a certificate or affidavit, if appropriate, would be appreciated."*

14. On 26 November 2002, ACAS wrote back: *"I refer to your letter dated 21 November 2002 ... ACAS does not deal with the resolution of commercial disputes. We deal with employment relations and related matters, such as training. Clearly the circumstances you have outlined do not fall within that category."*

15. In December 2002, Flight Training commenced proceedings against IFTE in the United States Federal District Court for the Eastern District of Virginia. Flight Training's complaint included, in the alternative to claims for damages, a claim for an order that the Court designate and appoint an arbitrator or umpire who should act under the Agreement. The basis for this claim was as follows: *"... ACAS does not provide mediation services for commercial disputes. It provides such services only with respect to employment relations and related matters.*

17. In September 2002 FTI proposed to IFTE that the parties resolve the dispute between them or, if they cannot do so, present the matter to an alternative mediation service. IFTE refused ..."

16. IFTE challenged the United States' proceedings for want of personal jurisdiction. In support of their motion to dismiss, they served an affidavit sworn by Mr Michael Allman, the Director of Sales and Marketing of IFTE, in which he said*: "By its own terms, the Heads of Terms document was to be governed and construed under English law, and provided further for arbitration in London in the event of any disputes."*

17. IFTE's Reply Brief on its motion to dismiss also stated that the Agreement required the parties to arbitrate their disputes before a London arbitral tribunal. IFTE's jurisdiction challenge succeeded in June 2003.

18. Flight Training issued its claim form (arbitration) on 3 July 2003. Flight Training, in effect, asks the Court to appoint a sole arbitrator to determine Flight Training's claims for commission under the Agreement. Flight Training say that Article XI constitutes a valid arbitration agreement. IFTE says that it does not.

19. **The claimant's submissions** : Mr Richard Handyside for the claimant submitted as follows. Article XI of the Agreement is, on its true construction, an arbitration agreement for the purpose of the 1996 Act. The principles by which written contracts are construed were summarised by Lord Hoffmann in **Investors Compensation Scheme Ltd v. West Bromwich Building Society** [1998] 1 WLR 897 at pages 912-3. Lord Hoffmann's fourth and fifth principles are particularly relevant in this case. See also **Mannai Investments Co Ltd v. Eagle Star Life Assurance Co Ltd** [1997] AC 749, at pages 771A-C (Lord Steyn) and pages 774D-775G & 779F-H (Lord Hoffmann).

20. The subject of the Agreement is the provision of anti-terrorist facilities and training to a foreign government. Parties entering into such a contract would be likely to resolve disputes in private rather than in public. The Agreement is not a happily drafted document. This is particularly true of Article XI. Consideration of that Article clearly demonstrates that the parties did not intend to refer their disputes to "mediation" (in the sense of a facilitative dispute resolution process), but rather that they intended to submit their disputes for binding decision (i.e. arbitration) (by ACAS).

21. The second sentence of Article Xl provides that the party "*which does not prevail*" shall pay the costs and fees of the other party. The concept of a party "*prevailing*" has no application to a mediation. Mediation is a non-binding dispute resolution process in which a neutral person helps the parties to try to reach a mutually acceptable settlement. The mediator has no power to impose a settlement on the parties, nor is it his role to "decide" the merits of the case. Accordingly, the costs provision set out in the second sentence of Article XI makes no commercial sense in the context of a mediation. It does, however, make sense in the context of an arbitration, where the arbitrator decides the merits of the dispute and therefore is necessarily required to decide which party has prevailed. Moreover, agreements between parties as to costs are given effect to under sections 62 and following of the 1996 Act.

22. It would make no commercial sense for the parties to seek to agree in advance of any mediation which party should pay the fees and costs of it. Since the whole object of a mediation is to reach a mutually acceptable compromise, the costs of a mediation can -- if the parties so wish -- be taken into account in any settlement concluded at any mediation. The parties would obviously be free to depart from costs provision set out in Article XI when concluding a compromise at the mediation. What commercial purpose would be served in seeking to provide in the Agreement for who should bear the costs of the mediation?

23. There can be no guarantee that the parties to a mediation will reach agreement at it; and in circumstances where no compromise is reached, the costs provision in Article XI cannot work. The position is obviously different in an arbitration, where a decision as to the parties' rights is bound to be reached.

24. Article XI proceeds upon the assumption that submission of the dispute to ACAS will bring about the determination of the dispute. The Article makes no provision as to what is to happen, either to the dispute itself or to the costs of the "mediation", where no compromise is reached.

25. The first sentence of Article XI refers to the 'submission' of the dispute to ACAS. The concept of 'submission' is more apt in the context of judicial proceedings or an arbitration where the role of the judge or arbitrator is to decide the dispute and to make an enforceable award or order, than it is in the context of a consensual mediation process where the mediator has no power to impose any terms or outcome upon either party.

26. A reasonable person would have understood Article XI to require the parties to submit their disputes to arbitration. On its true construction, Article XI is an agreement to arbitrate.

27. As to the second sentence of Article XI a reasonable person would have understood mediation in that sentence to mean arbitration.

28. The defendant's submissions. Mr Toby Watkin for the defendant submitted as follows.

29. Clause XI constitutes an enforceable agreement to mediate disputes arising under the Agreement. Alternatively, if clause XI is not an effective mediation clause because ACAS do not provide a mediation service in relation to commercial disputes, the clause is nevertheless not an arbitration

clause within the meaning of sections 5 and 6 of the 1996 Act. As with any contractual clause, the Court should apply the normal canons of construction and attempt to find "what the parties using those words against the relevant background would reasonably have been understood to mean." **I.C.S. Ltd v. West Bromwich BS** [1998] 1 WLR 896 per Lord Hoffmann at 913.

30. In general, words within a clause should be given their natural and ordinary meaning and clauses should be read literally unless the literal meaning *"flouts business commonsense."*

31. Evidence of surrounding circumstances and trade meanings may be admitted for the purposes of ascertaining the meaning of a clause. However, the *"evidence of the negotiations of clauses or of the parties' subjective intentions"* cannot. Neither can the subsequent actions of the parties be a basis for ignoring the literal effect of a clause. **Prenn v. Simmons** [1971] 1 WLR 1381 per Lord Wilberforce at 1384. **North Eastern Railway v. Lord Hastings** [1900] AC 260 per Earl of Halsbury LC at 266.

32. Applying the normal rules of construction, the only *'reasonable meaning'* to be understood from the wording of clause XI is that the parties have expressed the intention to mediate disputes arising from the Heads of Agreement. This is the only construction which accords with the natural and ordinary meaning of the words and which prevents the clause from being internally inconsistent.

33. This construction is also consistent with 'business commonsense.' Mediation clauses are enforceable and widespread. They are consistent with modem business practice and the use of mediation is now required to be encouraged by the court. **Cable & Wireless PLC v. IBM United Kingdom Ltd** [2002] 2 All ER (Comm) 1041. Civil Procedure Rules 1998, Part 1.4(2)(e). **Dunnett v. Railtrack** [2002] 1 WLR 2434.

34. Having discerned the intention of the parties to mediate disputes, the Court should attempt to give effect to that intention, just as it would if they had expressed a clear intention to arbitrate.

35. The mere reference to a costs provision is not inconsistent with mediation.

36. The reference to ACAS within the clause is generally consistent with the manifest intention to mediate since ACAS provides, amongst other things, mediation services. However, ACAS do not provide such services in relation to commercial disputes of this nature. The construction for which the claimant contends, in reality, amounts to a correction of the clause to fit the claimant's subjective intention and interests. In the absence of a claim for rectification (which has not been made), the Court may only correct obvious drafting mistakes and only where: (a) it is clear that a correction is necessary (i.e. construction of the clause under the usual canons fails or "flouts business commonsense"); and (b) the nature of the necessary correction is clear. **Homburg v. Houtimport BV v. Agrosin Ltd** [2003] 2 WLR 711 Per Lord Steyn at para 23 & Lord Millett at para 193.

37. Neither requirement is fulfilled in the present case. As the defendant's case illustrates, it is not "necessary" that a correction be made to clause XI. The nature of the required correction is not clear, since the Court could *"correct"* clause XI either by strengthening the mediation clause, or by creating an arbitration clause. The clause provided for mediation (by ACAS) not arbitration.

38. **Analysis and Conclusions** : I analyse the position as follows.

(1) ACAS does not deal with the resolution of commercial disputes. ACAS deals with employment relations and related matters such as training. It is common ground that in relation to employment relations and related matters, ACAS provides three distinct services: (1) conciliation, (2) mediation, (3) arbitration. ACAS define:-- '*conciliating*' as the act of reconciling or bringing together the parties in a dispute with the aim of moving forward to a settlement acceptable to all sides; '*mediating*' as acting as an intermediary in talking to both sides -- the aim is for the parties to resolve the problem between themselves, but the mediator will make suggestions along the way; and ' arbitrating' as an independent arbitrator ... deciding the outcome of a dispute -- the decision may well be binding in law.

As to the services provided by ACAS, see further **Brown and Marriott, ADR Principles and Practice**, 1993 at page 213 et seq. For completeness I note that CPR Part 62 4.1(2) refers to "*ACAS (in a claim under the 1996 Act as applied with modifications by the ACAS Arbitration Scheme (England and Wales) Order 2001).*"

(2) The distinction between litigation, arbitration and Alternative Dispute Resolution, is reflected in the Admiralty and Commercial Courts Guide, August 2002, see in particular Chapter G, Alternative Dispute Resolution, G1.1: *"While emphasising its primary role as a forum for deciding commercial cases, the Commercial Court encourages parties to consider the use of ADR (such as but not confined to mediation and conciliation) as an alternative means of resolving disputes or particular issues."*

Brown and Marriott point out at page 18: *"Some ADR writers divide all dispute resolution processes (judicial and alternative) into three primary categories: negotiation, mediation and adjudication. Others extend them to up to six primary categories: negotiation, mediation, the judicial process, arbitration and the administrative and legal process. This effectively amounts to a subdivision of adjudication into its constituent parts."*

As to mediation or conciliation, it is stated at page 19: *"Mediation is a process by which disputing parties engage the assistance of a neutral third party to act as a mediator -- a facilitating intermediary -- who has no authority to make any binding decisions, but who uses various procedures, techniques and skills to help the parties resolve their dispute by negotiated agreement without adjudication. The mediator is a facilitator who may, in some models of mediation, also provide a non-binding evaluation of the merits of the dispute if required, but who cannot make any binding adjudicatory decisions. A conciliation is a term sometimes used interchangeably with mediation, and sometimes used to distinguish between one of these processes (often mediation) involving a more proactive mediator role, and the other (conciliation) involving a more facilitative mediator role; but there is no consistency in such usage."*

(3) Chapter 6 of **Mustill & Boyd, Commercial Arbitration** (2nd Ed. 1989) considers agreements to refer future disputes. At page 105 the following passage appears:

*"**3 Certainty***

As regards the third question, it must be shown that the terms of the agreement to arbitrate are sufficiently certain to be enforceable. Allegations of uncertainty may arise in various ways." ...

"(b) Abbreviated clauses. A similar question will arise, where the parties have agreed upon a term as to arbitration, but it is said that the term is too uncertain to be enforced. The courts will lean against frustrating the intention of the parties, and will try to give the clause a meaning. It is thus no objection that the clause is terse. Thus, 'Arbitration to be settled in London' is sufficiently clear to be enforced, and indeed it has been said that the single word ' Arbitration' will suffice."

See further the commentary in **Mustill & Boyd** to sections 5 and 6 of the 1996 Act in the 2001 Companion at pages 260 to 266.

In **David Wilson Homes Ltd v. Survey Services Ltd (In Liquidation) & Anr** [2001] BLR 267, the Court of Appeal considered the question whether a clause in an insurance policy which provided "any dispute or difference arising hereunder between the Assured and Insurers, shall be referred to a Queen's Counsel of the English Bar to be mutually agreed between the Insurers and the Assured, or, in the event of disagreement by the Chairman of the Bar Council" was an arbitration agreement within the Arbitration Act 1996. At paragraph 11, Longmore LJ said:

"11. For my part, I prefer the arguments of Mr Phillips. There is no need for a clause which deals with reference of disputes to say in terms that the disputes are to be referred to an 'arbitrator' or to ' arbitration'. The necessary attributes of an arbitration agreement are set out in the second edition of Mustill & Boyd, Commercial Arbitration at page 41. But, for present purposes, the important thing is that there should be an agreement to refer disputes to a person other than the court who is to resolve the dispute in a manner binding on the parties to the agreement. That is what this clause in my opinion does, and it is therefore an arbitration agreement within the meaning of section 6 of the Arbitration Act 1996. ...

15. In the present case, the parties cannot ... have intended a reference to a Queen's Counsel as an expert or for a non-binding opinion, because in that way no finality could be achieved. They must in my judgment have wanted a binding result, and the clause thus constitutes an arbitration agreement."

In **Cable & Wireless Plc v. IBM (UK) Ltd** [2002] 2 All ER (Comm) 1041, Colman J considered whether a contract to refer disputes to Alternative Dispute Resolution ("ADR") was enforceable. He held that the reference to ADR in the parties' agreement was analogous to an agreement to

arbitrate and therefore strong cause had to be shown before a court could be justified in declining to enforce such an agreement. Parties which entered into an ADR agreement wide enough to cover pure issues of construction had at best a weak basis for inviting the court to withhold enforcement. Moreover, since the defendant disputed the fundamental validity of the benchmarking report, the issue of construction might even not arise. There were therefore extremely strong case management reasons for allowing the reference to ADR to proceed. Accordingly, the appropriate course was to adjourn the proceedings for a declaration as to the construction of the agreement, pending the dispute being referred to ADR.

(4) In my judgment, clause XI does not incorporate an agreement to submit future disputes to arbitration. It refers disputes to a body which does not deal with the resolution of commercial disputes, but which, in the field of employment relations and related matters provides conciliation services, mediation services and arbitration services. I emphasise that these three sets of services are distinct (see (2) above). Clause XI specifically refers to ' mediation' in the second sentence. This provides a strong indication of an intention to select mediation out of the services provided by ACAS. Where a dispute resolution clause refers disputes to a body that provides conciliation, mediation and arbitration services and the only reference in the clause is to mediation, this provides a strong indication of an intention to select mediation as opposed to conciliation or arbitration services.

39. The effect of the second sentence of clause XI (Legal fees and costs shall be paid by either party which does not prevail at mediation") is to provide that, if one party prevails in the mediation, the fees and costs of the mediation are to be paid by the other party. Thus it would seem that the parties intended that if, for example, the result of the mediation was a mediated agreement (1) by the defendant to pay the claimant, say, $500,000, the defendant would pay the costs of the mediation; (2) by the claimant to withdraw the claim, the claimant would pay the costs of the mediation. I recognise that in practice it is likely that the parties might take this provision into account before agreeing to any mediated result, but nonetheless, the second sentence of clause 11 makes provision for where the costs of the mediation should fall if either side prevails.

40. The Commercial Court Guide at Appendix 7 (Draft ADR Order) at paragraph 6, puts the word "costs" in square brackets. This is intended as a reminder that consideration should be given to questions of costs of mediation when an ADR order is made. It is not surprising that in a provision expressly providing for mediation, the parties should attempt to provide as to what is to happen in relation to the costs of mediation.

41. For the reasons set out above, I do not consider that there is an agreement to refer the underlying dispute to arbitration as required by section 5 and section 6 of the 1996 Arbitration Act. The defendant's application succeeds. I order accordingly.

Mr Richard Handyside (Instructed by Messrs Lonsdales) appeared on behalf of the Claimant.
Mr Toby Watkins (Instructed by Messrs Mayer, Brown Rowe & May) appeared on behalf of the Defendant.