CONSTRUCTION : BULLETIN

The Importance of Mediation

Mediation is a way of resolving disputes by appointing a neutral third party mediator to facilitate communication between the parties, with a view to agreeing a settlement. The courts strongly emphasise the importance of trying to resolve disputes in mediation before pursuing a claim in the courts. As part of their strategy of trying to encourage alternative dispute resolution, the courts are willing to impose cost sanctions on parties who refuse to participate in mediation.

However, a party which considers it has a very strong case in a dispute may consider that mediation is a pointless and unnecessary waste of costs. In such circumstances, is mediation still a requirement? This issue was considered by the courts in the recent case of *Northop Grumman Mission Systems Europe Limited v BAE Systems (Al Diriyah) Limited.*

Background

In December 2010, BAE Systems (Al Diriyah) Limited ("BAE") entered into a software licensing agreement with Northop Grumman Mission Systems Europe Limited ("NGM"). After about a year, BAE purported to terminate the agreement under a termination for convenience clause. A dispute arose between the parties about whether or not BAE had been entitled to terminate for convenience.

NGM's position was that BAE was not entitled to terminate for convenience and therefore NGM was entitled to circa £2.6m in damages for wrongful termination. BAE's position was that it was entitled to terminate for convenience and was therefore only required to pay NGM its costs arising out of the termination, but NGM had not incurred any costs. Whichever party won depended entirely on whether a termination for convenience clause was incorporated into the licence agreement.

NGM made several written proposals to mediate but BAE repeatedly refused, primarily on the ground that NGM had failed to provide details of its costs arising from the termination and therefore BAE did not consider there was any chance of holding a meaningful mediation, particularly when BAE considered it had a very good prospect of defending NGM's claim.

In October 2013 NGM commenced legal proceedings against BAE. On 20 January 2014 BAE made a without prejudice offer that the proceedings should be brought to an end and that no payment would be paid to NGM, with each party paying their own costs. NGM rejected this offer and the case continued to trial.

The court's judgment

The court ruled in favour of BAE and NGM's claim for damages failed. Consequently, NGM was liable to pay BAE's legal costs.

NGM argued that BAE's legal costs should be reduced by 50% to take into account BAE's unreasonable refusal to take part in mediation to resolve the dispute. BAE argued that it had acted reasonably in refusing to mediate because of its belief that its defence was watertight.

When is it reasonable to refuse to mediate?

Previous case law has established six factors to consider when deciding whether a refusal to mediate was

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reasonable. The court considered each of these factors in turn.

1. Nature of the dispute

In certain circumstances, the courts acknowledge that particular types of dispute may not be suitable for mediation, particularly where the dispute relates to an issue of contractual interpretation which the parties simply cannot agree on.

However, although this was a case which turned on the interpretation of a contract, the court nevertheless considered that a skilled mediator would have been able to assist the parties in finding a solution to the dispute.

2. Merits of the case

It may be appropriate for a party to refuse to mediate where they reasonably consider that they have a strong case. BAE had believed that their case was strong, and were ultimately shown to be correct in this belief.

However, this factor alone did not mean that BAE was entitled to refuse to mediate. The court stated that parties should not ignore the "*positive effect that mediation can have in resolving disputes even if the claims have no merit*". In this case, BAE's reasonable view about the strength of its case was "*a factor which provides some but limited justification for not mediating*". The strength of BAE's case was not in itself sufficient for BAE to have refused mediation.

3. Extent to which other settlement methods were attempted

It may be possible to establish that mediation was not appropriate in cases where the parties have failed in their attempts to settle the case by other methods.

The court noted that in this case there was some attempt to settle the dispute by other means. There had been a without prejudice meeting between the parties' respective legal teams fairly early on in the dispute and BAE had also made a without prejudice offer which NGM ultimately rejected.

However, even though other attempts at settlement had not been successful, the court did not consider that this provided adequate justification for refusing to mediate.

4. Costs of mediation

Where the costs of mediation will be disproportionate to the cost of the dispute and/or to the costs of taking the dispute to trial, it may be appropriate to decline to mediate. However, that was not the case here. The costs of mediation (for both parties) would probably have been in the region of £40,000, whereas the parties had collectively incurred costs of approximately £500,000 in taking the dispute to trial.

5. Prejudicial delay

If engaging in mediation will cause a delay which might prejudice the case, it may be reasonable to refuse mediation. However, this was not a relevant factor in this case, as mediation could easily have been conducted without causing any delay to the legal proceedings.

6. Prospects of successful mediation

If the likely prospects of success of mediation are slim, it may be appropriate to refrain from mediating. However, this is a difficult ground to establish, because a great many cases settle in mediation, even where the parties appear to be entrenched in their positions.

The court, considered this to be a "classic case" where a mediator could have succeeded in bringing the parties together. The court also stated that the parties' entrenched positions are not a relevant factor when considering the likelihood of settling in mediation, because it is important to bear in mind that a skilled mediator would be able to find possibilities, solutions and options which may not have been considered by the parties prior to mediating.

Conclusion

The court concluded that, despite BAE holding a reasonable and rational belief that it had a strong case, its failure to mediate was unreasonable. Accordingly, the court was entitled to penalise BAE by reducing the costs recoverable from NGM.

However, because NGM had also acted unreasonably in failing to accept BAE's sensible without prejudice offer of settlement, the court decided that BAE's unreasonable conduct cancelled out NGM's unreasonable conduct, with the effect that BAE's legal costs should ultimately not be reduced.

Analysis

This case makes it clear that having a cast iron defence (or claim) does not necessarily give a party grounds to refuse to participate in mediation. In light of this case, we would suggest that the parties to a dispute should participate in mediation in all but the most exceptional of cases. Failure to do so could result in a costs sanction being imposed by the court. This could have serious financial consequences, particularly in construction disputes, where legal costs are often significant.

Although the parties to a dispute may consider that mediation is effectively being forced on them and is simply a procedural step that must be taken to avoid cost sanctions, it is important to remember that mediation is often successful and can be a very cost effective way of settling a dispute. Anyone involved with a mediation should try to keep an open mind and engage properly with the process in order to avoid wasting what may be a valuable opportunity to settle the dispute.

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