

Court concludes 'Friendly Discussions' clause is enforceable November 2014

In a departure from previous case law indicating that "agreements to negotiate in good faith" are unenforceable, the English High Court in *Emirates Trading Agency LLC v Prime Mineral Exports Private Limited (2014)* held that a contractual clause requiring the parties to engage in "friendly discussion" before commencing arbitration proceedings was enforceable.

"Friendly negotiation" clauses are often found in JV agreements and other commercial agreements in mainland China, and this case provides guidance as to how such clauses might be interpreted in Hong Kong.

This case marks a departure from the way in which the English court previously dealt with agreements to negotiate in good faith. On the facts, the Judge was able to distinguish this case from the leading English authority in this area, *Walford v Miles*, and preferred to follow the decision of the Australian court in *United Group Rail Services*; that such agreements to engage in friendly discussion are enforceable.

However, where the Australian case limited the scope of the good faith negotiations arising out of such clauses to an assessment of the parties' rights and obligation under the contract, the English Court averred that the negotiations could go further to include considerations of the parties' wider commercial interests, stating that good faith connoted both honesty and the observance of reasonable commercial standards of fair dealing and that where a party clearly fails to honour such standards, judges and arbitrators will have no particular difficulty in recognising and identifying such failures.

The Court further stated that while a bare agreement to agree is unenforceable, an obligation to resolve a dispute in good faith within a specified period of time should be enforceable, because it is not necessarily incomplete since no essential term is lacking. Just because breaches of such agreements would be difficult to police or prove, it does not mean the clause lacks real content or merit. There would also be conceivable cases where a party, despite the existence of this type of clause, could refuse to negotiate and seek to commence arbitral proceedings.

Teare J also noted public policy reasons for encouraging parties to resolve their disputes by making such clauses enforceable, as it can potentially avoid expensive and time-consuming proceedings in litigation or arbitration. Moreover, where commercial parties enter into obligations, they reasonably expect the court to uphold those obligations. Deeming such clauses as unenforceable frustrates the

expectation that courts will generally give effect to parties' bargains.

On the facts of this case, however, the courts found that the condition precedent had been satisfied and dismissed the application accordingly, upholding the jurisdiction of the arbitrators in the arbitration proceedings.

Comment

This decision is in line with general developments towards more efficient resolution of disputes and alternative dispute resolution clauses.

Parties providing undertakings in agreements to negotiate in good faith to settle disputes before entering arbitration proceedings, should, therefore, be sensitive to the fact that courts may now view these clauses as a condition precedent which must be satisfied before the matter can be taken further.

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