Experts and Arbitrators

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This paper points out the danger in the increasingly common practice of including in construction contracts a provision that any disputes will be determined by an expert acting as an expert and not as an arbitrator. The author recommends that the practice cease.

For the first three quarters of this century there was a widespread misconception that between an expert acting as an expert and an expert acting as an arbitrator there was a third category of expert who performed a 'quasi-judicial' role1. This category of expert was called a 'quasi-arbitrator'.

This misconception was exposed by the House of Lords in *Sutcliffe v. Thackrah* [1974] A.C. 727. There is no third category. The term 'quasi-arbitrator' should never be used in the context of construction contracts2. Generations of architects, engineers and lawyers have been incorrectly taught that there is such a thing as a 'quasi-arbitrator' and even to this day3 the term is sometimes used to describe a role of the Superintendent4.

What is most disturbing is that the ghost of the 'quasi-arbitrator' has risen to haunt the construction industry under a new guise. The new guise is 'Expert Appraisal'. A synonym is 'Independent Expert Determination'. Newton [1991] suggests the following definition:

> **Independent Expert Determination**
> This is a process where an independent expert in the required field is asked to give a determination with which the parties by contract beforehand agree to comply. It is expressly outside commercial arbitration legislation.

Smart [1989] gives a more limited definition, namely:

> **Expert Appraisal** - An acknowledged expert is given the documents and the submissions of both sides and produces a binding solution; for example, rental redeterminations, valuations of shares, fixing of hire charges for building equipment such as formwork. The appraiser may be a valuer, accountant, or quantity surveyor etc.

With the recent enthusiasm for Alternative Dispute Resolution [ADR],

'Expert Appraisal' is being promoted as an accepted mechanism for determining disputes5. There are several published 'rules' for the conduct of 'Expert Appraisal'6. Sir Laurence Street has prepared a standard form *Agreement for Determination of Dispute by Expert Appraisal*'7 under which the parties in dispute agree to accept as final and binding a determination of an independent consultant. Under this agreement, if the parties so request, the consultant [the Expert] is bound to give them a hearing at which the parties can be legally represented. The procedure has all the hallmarks of an arbitration except for two provisions, namely:

1. The Expert will "act as an expert and not as an arbitrator"; and
2. The Expert is not "bound to observe the rules of natural justice".

Some solicitors are recommending to clients that they omit the arbitration clause from their construction contracts and instead include a provision that any dispute will be determined by an independent expert agreed upon by the parties or appointed by a third party and that the decision of the expert will be made as an expert and not as an arbitrator. The clause provides that the decision of the expert will be final and binding.

Some solicitors then include rules for the conduct of the determination by the expert. The rules commonly cover the type of procedural matters covered by Sir Laurence Street's standard form. Sometimes there is a statement that the Commercial Arbitration Act will not apply. Sometimes there is specific provision that the expert must conduct the process in accordance with the requirements of procedural fairness.

What is generally overlooked is that whether the expert will be acting as an expert and not as an arbitrator does not depend upon the words used in the contract or the "rules" agreed upon by the parties but depends upon the functions which the expert is to perform. If the expert is actually conducting an arbitration the expert will be an arbitrator even though the parties and the expert have agreed that the process is not to be arbitration and that the expert will act as an expert and not as an arbitrator8.

The mere fact that the parties and the expert agree that the uniform Commercial Arbitration Act will not apply does not stop it from applying. The Act will apply if the agreement is an agreement to refer present or future disputes to arbitration9 even though the parties agree that it will not apply. While there are many provisions of the Act which provide that the provision only applies "unless the parties otherwise agree", there are some provisions that give the Supreme Court powers. Parties to a contract cannot deprive the Supreme Court of powers which are given to the Court by statute.

A typical contract disputes clause providing for Expert Appraisal includes:

> If a dispute arises out of or in connection with this Contract whether raised before or after Practical Completion, then either party may give the other a written notice identifying the particulars of the dispute and the dispute will be dealt with in the following manner:
> 1. The dispute will be determined by one independent expert agreed upon and appointed jointly by the parties, or failing agreement, appointed upon the application of either party by the President of the Institute of Arbitrators Australia.
> 2. The decision of the expert will be made as an expert and not as an arbitrator and will be final and binding on the parties.
> 3. The Expert must make the determination according to the law and must conduct the Process in accordance with the requirements of procedural fairness.

Usually, the contract will also contain "rules" for the conduct of the dispute resolution proceedings. The rules may cover a hearing, procedural matters, legal representation, interest, costs and the liability of the expert.

Such a dispute resolution clause is in fact an arbitration clause and the Commercial Arbitration Act will apply, despite a provision in the contract to the contrary. The failure of the parties to acknowledge and agree that the clause is an arbitration clause is likely to give rise to ambiguity and dispute.

A similar clause was the subject of *Aztec Mining Company Limited v. Leighton Contractors Pty. Ltd.* [1990] 1 Australian Dispute Resolution Journal. Murray J. in the Supreme Court of Western Australia considered a clause which provided that disputes would be submitted to an expert who "shall be deemed not to be an arbitrator but an expert and the law relating to arbitration shall not apply to the expert or the expert's determination or the procedures adopted by the expert".

The plaintiff sought a declaration that the clause was void and unenforceable for uncertainty. The application was refused. Murray J. said:

> I do not think it to be helpful in considering this aspect of the case, to consider whether or not the expert may be truly said to be acting as an arbitrator or in some quasi judicial capacity [although I would think in a general sense that that was the case] ...

With respect, there is no such 'quasi judicial capacity'. It is unfortunate that Murray J. raised the spectre. Had he not fallen into the error of believing that there is a third category of quasi- arbitrator part way between an arbitrator and an expert, it should have been apparent that the process agreed upon by the parties was arbitration.

Jacobs [1990] also countenances the possibility of a third category of expert between a valuer [certifier] and an arbitrator. At p.3653 Jacobs says:

> In determining whether a person rendering a valuation is performing an arbitral function or the function of a valuer, the possibility that such person may be acting as a quasi-arbitrator must be considered. The status and further, the immunity of a quasi-arbitrator has been recognised by English law since at least the 19th century: see *Palacath* at 164, and the authorities cited therein; *Pappa v Rose* [1871] LR 7 CP 32, affirmed LR 7 CP 525; *Tharsis Sulphur & Copper Co Ltd v Loftus* [1972] LR 8 CP 1, where there was a clause referring to an average adjuster.

Those cases are not authority for the proposition that English law recognises a third category of 'quasi-arbitrator'. They were adversely commented upon in *Sutcliffe v Thackrah* [1974] A.C. 72710. Viscount Dilhorne said:

> In every case whether a person, who is to fulfil functions in relation to a contract between two other people, has to act as an arbitrator or quasi-arbitrator depends on the terms of the contract and the decisions in *Pappa v Rose* in the Court of Common Pleas and in *Tharsis Sulphur & Copper Co v Loftus* were only correct if, in the true view of the contract, the broker in the former case and the average adjuster in the latter were appointed to act as arbitrators to resolve disputes between the parties to the contract which might arise or had arisen.

In *Sutcliffe*, both Lord Reid and Lord Salmon adopted the words of Buckley LJ in *Arenson v Arenson* [1973] Ch 346 at p. 370:

> where a third party undertakes the role of deciding as between two other parties a question, the determination of which requires the third party to hold the scales fairly between the opposing interests of the two parties, the third party is immune from an action for negligence in respect of anything done in that role.

The reason for the immunity is that the third party is an arbitrator. Lord Reid discussed the liability of a valuer and said:

> On the other hand, the valuer could be engaged by both parties as an arbitrator if there is a dispute about the value of certain property. The dispute would be submitted to him for decision and the parties would put their contentions before him. Then he would have to judge between them and have an arbitrator's immunity.

It seems that in Australia the only room for the expression 'quasi-arbitrator' would be where the uniform Commercial Arbitration Act does not apply. The Act does not apply to oral agreements to arbitrate. An arbitrator under an oral agreement might be referred to as a *quasi*-arbitrator. If parties do not intend to create legally binding legal relations then the adjudicator might be described as a *quasi*-arbitrator11. Otherwise the term should not be used.

With respect to Murray J. and Jacobs [1990], there is no room for an expert appointed pursuant to an Expert

Appraisal clause to be a quasi-arbitrator or to perform a quasi-judicial role. The expert is either an arbitrator or an expert. There is no half way. If the agreement for Expert Appraisal is in writing and the expert is performing the role of deciding a dispute then the procedure is almost certainly an arbitration and the the uniform Commercial Arbitration Act applies. If the expert is engaged to give a valuation only, the Act does not apply. The fact that the parties have agreed that they will abide by the valuation does not make the process an arbitration.

In *Aztec Mining* Murray J. said:

> ... the express provision ... that the law relating to arbitration shall not apply to the expert or his determination, makes it clear that the immunity from suit which will attach to a judge or arbitrator, which is said to be conferred in the arbitrator's case by the law which relates to arbitration, is removed

Murray J. quotes no authority for this surprising proposition. With respect, it is far from "clear" that the immunity is "removed". The agreement of the parties or even the agreement of the expert that the Act does not apply does not create a liability for negligence when the expert is acting as an arbitrator. Section 51 of the uniform Commercial Arbitration Act destroys the cause of action, if any, which might have existed on the part of an arbitrator. Section 51 is not expressed to be subject to the agreement of the parties or the arbitrator. Saying that section 51 does not apply does not create a cause of action. It is not the same as saying that notwithstanding that in law there is no liability, the arbitrator agrees to indemnify both parties against loss which may flow from the arbitrator acting negligently.

Murray J. compounds the confusion by later stating that in his view "it may well be the case that an expert appointed [under the dispute clause] has the necessary indicia of judicial function to support immunity". With respect, it would not be necessary to look for some "indicia of judicial function to support immunity" if Murray J. had not mistakenly formed the opinion that the immunity provided by legislation had been "removed".

There is a danger that the view of Murray J. will lend support to the myth that the law recognises Expert Appraisal as a form of quasi-arbitration, part way between arbitration and valuation [or certification]. The solution is not to put in contracts the Expert Appraisal clause and to confine Expert Appraisal to what is truly a valuation or certification by an expert.

References

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Smart, Mr. Justice, *Aspects of Construction Industry Contracts and Disputes,* [1989] 5 BCL7.

Footnotes

[1] The main basis for the misconception was a Court of Appeal decision *Chambers v. Goldthorpe* [1901] Q.B. 624. The Court considered the position of an architect who had to decide the amount due to a builder and issue a certificate. Smith M.R. said that the architect "undertook the duty towards both parties of holding the scales even and deciding between them impartially as to the amount payable by one to the other". He held that "... although the [architect] may not ... have been an arbitrator in the strict sense of the term, he was in the position of a person who had to exercise functions of a judicial character as between two parties, and therefore was not liable to an action for negligence in respect of what he did in the exercise of those functions." For the next 75 years, the architect, engineer or Superintendent administering a construction contract was described as a quasi-arbitrator. The misunderstanding is exemplified by Duncan Wallace [1970] p.161:

> There is little doubt that, in his capacity as certifier, ... the architect owes no duty of skill or care to his employer [or, for that matter, the contractor].

In *Sutcliffe v Thackrah* [1974] A.C. 727 the House of Lords overruled what Lord Reid called "this rather startling proposition" and held that the architect is not a quasi-arbitrator and has no immunity from liability for negligence.

Duncan Wallace [1979] p.64 then went to the opposite extreme and said:

> ... it would seem that ... contractors will be able to sue certifiers in tort for carelessness in issuing their certificates.

The Court of Appeal in *Pacific Associates Inc. v. Baxter* [1989] 2 All E. R. 159 has cast doubt on the right of contractors to sue the Superintendent in tort for acts or omissions in certifying. Duncan Wallace [1990] says that the following statement by Bokhary J. in *Leon Engineering v Ka Duk Investment Company* [1989] 47 Build. L.R. 143 represents "an accurate assessment, though on the most conservative basis, of the Pacific Associates *ratio decidendi*":

> The Principle which I extract from the Court of Appeal's decision in *Pacific Associates v. Baxter* is one which I would state in these terms: where, first, there is adequate machinery under the contract between the employer and a contractor to enforce the contractor's rights thereunder and, secondly there is no good reason at tender stage to suppose that such rights and machinery would not together provide the contractor with an adequate remedy, then, in general, a certifying architect or engineer does not owe to the contractor a duty in tort coterminus with the obligation in contract owed to the contractor by the employer.

That appears to be an accurate statement of the law as it presently stands in Australia.

[2] In *Sutcliffe v. Thackrah,* Lord Morris of Bort-y-Gest said:

> There may be circumstances in which what is in effect

> an arbitration is not one that is within the provisions of the Arbitration Act. The expression *quasi*-arbitrator should only be used in that connection.

[3] See *The Dual Roles of a Superintendent*, Straughan, C., [1991] 3 Australian Construction Law Bulletin 25.

[4] In Australia it is common to use the term 'Superintendent' to describe the person, whether an architect or engineer or other expert, who issues certificates under a construction contract.

[5] The problem is not confined to Australia. Bernstein, R. *Handbook of Arbitration Practice*, 1987 Sweet & Maxwell, London at p. 11 says:

> A contract may provide that disputes arising under it are to be resolved by some third person acting not as an arbitrator but as an expert. ... The procedure involved is not an arbitration, and the Arbitration Acts do not apply to it.

Bernstein fails to warn the reader that even though the parties purport to appoint the third person as an expert and not as an arbitrator, that is not conclusive as to whether the third person is in fact acting as an expert or as an arbitrator.
Kendall, John, *Expert Judgment*, [1990] 134 SJ 1430 promotes expert appraisal and says that "there is nothing to stop" parties agreeing on a third person acting as an expert and not as an arbitrator in substitution for litigation or arbitration about the issue. While there is nothing to stop parties purporting to appoint a third party as an expert and not as an arbitrator, the question of whether the person is in fact an expert or an arbitrator does not depend solely on the fact that the parties have agreed that the person is an expert and not an arbitrator. Kendall also fails to give a warning that despite the agreement of the parties the third person may in fact be an arbitrator.

[6] E.g. Freehill, Hollingdale and Page [1988] *Agreement to the Use of Expert Determination Process.*

[7] The form is reproduced in [1989] 8 Australian Construction Law Newsletter 17.

[8] Jacobs [1990] in Chapter 12 reviews some of the cases on the distinction between an arbitrator and an expert. Perhaps the case which most exhaustively considers the authorities is one which Jacobs does not mention. It is *Sports Maska Inc. v. Zittrer* [1988] 1 S.C.R. 564 where the Canadian Supreme Court reviews not only Canadian law but also United States law, English law and French law on the distinction between arbitration and expert appraisal. There appear to have been 35 authors and over 50 cases cited. It is interesting to see how similar the law is in these jurisdictions. Some of the more relevant statements from the unanimous decision are at pp. 603-4:

> The language used by the parties may indicate their intent to submit a dispute either to arbitration or to an expert opinion.... However, the courts are not bound by the terms chosen deliberately or otherwise by the parties, as these terms may well not correspond to the true intent appearing from other criteria.
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> One of the principal aspects that emerges from an analysis of the Code of Civil Procedure, academic opinion and the case law is the similarity that must exist between arbitration and the judicial process. The greater the similarity, the greater the likelihood that the reference to a third party will be chacterised as arbitration. The facts that the parties have the right to be heard, to argue, to present testimonial or documentary evidence, that lawyers are present at the hearing and that the third party delivers an arbitration award with reasons establish a closer likeness to the adversarial process than the expert opinion and tend to establish that the parties meant to submit to arbitration, but contrary to what was argued by the respondents, that criterion is not exclusive to arbitration.
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> The function assigned to the third party is indicative of the status conferred on him by the parties. If the third party has to decide between opposing arguments presented by the parties on a given point, we are much closer to arbitration. If however, the parties call on a third party solely to supply a necessary component of the contract, it is less certain that they intended to submit the present dispute to the third party, but rather tried to ensure that such a dispute did not arise, unless there are other criteria to the contrary. In the same vein, is the third party called on to make a decision in the light of his personal knowledge or must he choose among the various positions put forward by the parties concerned? In the first case, the situation will probably be one of an expert opinion, while in the second it will probably be an arbitration.

It appears that an Australian court would probably come to a similar conclusion.
Expert Appraisal - Challenging an Award, Davenport, P.J. [1990] 28 Law Society Journal 49, [1989] 6 Australian Construction Law Newsletter 12, also considers a number of cases on the distinction between an expert and an arbitrator and the relevance of the distinction. In particular, *Capricorn Inks Pty. Ltd. v. Lawter International [Australasia] Pty.Ltd.* [1989] 1 Qd. R.8. is discussed.

[9] See definition of "arbitration agreement" in section 4 of the Act. Different considerations apply when it is an international arbitration. This paper is concerned only with 'domestic arbitration' as defined in section 40[7] of the NSW Commercial Arbitration Act 1984.

[10] They are also considered in *Sport Maska Inc. v. Zittrer* [1988] 1 SCR 564 at 587.

[11] In formulating *Rules for Independent Appraisal* [see 1984 Building and Construction Council Reports no.103] and for *Hiring a Judge* [see *For your next dispute, try hiring a judge*, 58 Engineers Australia, July 1986 p. 18] the writer avoided the use of the term 'quasi-arbitrator' although the term could be properly applied to those procedures because the decision of the Appraiser or "Judge" is not binding and the Commercial Arbitration Act does not apply.