CIARAN FAHY
ARBITRATOR, CONCILIATOR, MEDIATOR

66 EGLINTON ROAD
DONNYBROOK
DUBLIN 4

Lecture to

Structure and Construction Division

Engineers Ireland

on

Dispute Resolution in Construction - Future Trends

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Ciaran Fahy BE MBA Eur Ing CEng FIEI FCIArb RConsEI Tel: (01) 218 5699 Fax: (01) 218 5698 Email: cfahy@cfahy.ie

1. I was asked by Ken Woods, of the Structures & Construction Division in Engineers Ireland, in June of this year to give a lecture on a topic of my choice within the Dispute Resolution area generally. I was delighted to accept and suggested that I might speak on the writing of Arbitration Awards, an area where I have some experience, a good deal of interest and fairly strong views. That offer was politely but nonetheless firmly declined and consequently I am here this evening to speak about Dispute Resolution in the broadest sense as applied to the Construction Industry in this country. I want to trace the historical evolution of the processes used, the very significant changes which have occurred in recent years or are likely to occur very shortly and finally to offer some views on what is likely to happen over the coming years.

2. I want to stress at the outset that any views expressed this evening are my own personal ones and I am not speaking as a representative of any organisation with which I am associated. My talk is set out in a paper and is available either through myself or Ken Woods.

3. This is a period of unprecedented change in the Irish Construction Industry with a number of events which, in Civil Engineering terms, could be described as having a return period of 50 years or more:

    - The introduction of new Government Contracts, developed by the Department of Finance, in 2007. This new suite of contracts displaced the IEI and RIAI Forms of Contract for civil engineering and building work which were used in the Public Sector for some 50 years.
    - The Arbitration Act 2010 which replaced the Arbitration Act 1954.
    - The imminent passage of the Construction Contracts Bill 2010 which is intended to introduce Statutory Adjudication into all Construction Contracts.

    Taken together these three events represent a once in a generation or possibly a once in a lifetime change in the Construction Industry and they are coinciding with one of the most dramatic reductions in output which has ever occurred in the industry. The output of the Construction Industry peaked at some ú39bn in 2007 and since then has reduced very dramatically so that it is now of the order of ú8bn or ú9bn. Unfortunately contractors are also struggling with a burden of bad debt due from developers while the industry is also beset with below cost tendering.

4. Historically construction disputes were dealt with by Arbitration and all of the earlier general conditions of contract contained an Arbitration Clause - for example the First Edition of the Institution of Civil Engineers of Ireland, a forerunner of Engineers Ireland, Conditions of Contract in 1959 and the RIAI Form of Contract produced in 1977. Some time ago I came across a 1939 ESB Conditions of Contract for the supply and erection of mechanical and electrical plant and it included a fairly standard Arbitration Clause referring *"any question, dispute, or difference whatsoever"* to Arbitration with the Arbitrator being appointed by the Minister of Industry and Commerce where the parties could not agree.

5. This use of Arbitration continued until the early 1990s when a two stepped Dispute Resolution process was first used comprising Conciliation followed by Arbitration. This was based on amicable settlement procedures by FIDIC, in 1987, as an obligatory preliminary step before Arbitration. Conciliation first appeared in the IEI Fourth Edition Conditions of Contract, produced in 1995, and the process was described in an IEI Procedure produced in the same year. This Procedure drew on the FIDIC approach as well as the Institution of Civil Engineers (ICE) Procedure and the UNICTRAL Conciliation Rules. The 1995 IEI Procedure was subsequently revised and continues to this day as the Engineers Ireland Conciliation Procedure 2000. The RIAI followed suit in 1996 and published its own Conciliation Procedure which is also still in use.

6. The Guide to the Engineers Ireland Conciliation Procedure 2000 states that it is *"essentially an assisted negotiation"* and goes on to say *"The aim of Conciliation is to reach an agreed solution. If for any reason such an agreed solution does not prove possible, then the Conciliator is required to make a Recommendation as to how, in his opinion, the matter should be settled."* The process is carried out on a confidential and without prejudice basis and since its introduction has enjoyed a wide measure of success leading to rapid and inexpensive, at least in comparison to Arbitration, resolution of many disputes.

7. Statutory Adjudication was introduced into the UK generally in May 1998 on the basis of Part II of the Housing Grants, Construction and Regeneration Act 1996 and this was extended into Northern Ireland in June 1999. The effect of this was to provide for any dispute at any time in a Construction Contract to be referred by any party to Adjudication with the Adjudicator's Determination to be binding but not generally final.

The Act contains a requirement that the Adjudicator make the Determination within 28 days of referral of the dispute although this timeframe may be extended in certain circumstances.

8. Since its introduction in 1998, Adjudication has been widely used in the UK and has led to a marked decline in Arbitration and other dispute resolution methods; despite the lack of finality, relatively few AdjudicatorsôDeterminations are subsequently referred to Arbitration or litigation. Since 1998, Adjudication has spread to Australia, New Zealand and also a number of countries in South East Asia. The approach adopted is very similar to the UK model except that in some of the Australian States its use is restricted to payment disputes.

9. The Construction Contracts Bill 2010 will introduce Adjudication into this country for Construction Contracts and I will deal in some detail with the Bill later in this talk. Adjudication is already used in this country on a contractual rather than a statutory basis and for example some of the NRA Contracts included Adjudication with Arbitration.

10. Dispute Boards, based on FIDIC practice, have been used successfully on large infrastructural projects, such as the LUAS, for some time. Essentially a Dispute Board comprises one or more persons appointed for the duration of a project, which maintains regular contact with the project and is available to deal with disputes as and when they arise. Depending on the constitution of the board, it may make a temporarily binding determination similar to that of an Adjudicator or the board may make a recommendation which the parties are free to reject.

11. Mediation and Expert Determination are also used in the Construction Industry although not widely. Expert Determination leads to a final and binding decision made by a third party neutral, normally an Expert in the area of the dispute, and the attraction is that it is seen as less formal, and consequently quicker and cheaper, than Arbitration while delivering a similar final outcome.

12. The use of Mediation in Construction has grown in recent years despite the fact that it is included in only one contract ï the CIF Subcontract for use with the Public Works Contracts. In simple terms it is negotiation between the parties carried out with the assistance of a third party neutral, the Mediator, and to that extent it resembles Conciliation except that there is no Recommendation where the parties cannot agree. Its great advantage is that it is not only the quickest and cheapest of the Dispute

Resolution processes but it is also the least damaging to the partiesôrelationship and for that reason it is increasingly used in commercial disputes generally. However it has been used successfully in recent times on some large-scale construction disputes ï for example the M 50.

13. In 2004 the Government decided to reform Public Sector Construction Procurement and since then has developed a Capital Works Management Framework to deliver on that objective. This is a comprehensive suite of documents specifically to achieve the following objectives:

- *"Greater cost certainty at Contract Award Stage;*
- *Better value for money at all stages during project delivery, particularly at handover stage; and*
- *More efficient end user delivery."*

14. The achievement of these objectives requires *"A comprehensive definition of the client's requirements*òpre-tender in order :

- *"To ensure as far as practical that the accepted tender prices and the final outturn costs are the same; and*
- *To allocate risk so that there is optimal transfer of risk to the Contractor."*

15. To my mind the Capital Works Management Framework is a most impressive suite of documents and represents a significant achievement by the Department of Finance which promoted it. In particular the documents are:

- Clearly and directly written in a modern style to facilitate easy comprehension.
- Freely available on the website which also facilitates amendment of the documents.
- Provided with extensive guidance notes covering all aspects of the documents.

16. The Capital Works Management Framework currently contains eleven different Forms of Contract for Public Works as well as two standard Conditions of Engagement for Consultancy Services. The more significant Forms of Contract cover building and civil engineering work separately both where the works is designed by the Employer and also where it is designed by the Contractor. In addition there is a Form of Contract to

cover minor building and civil engineering works, generally up to a value of ú5m, as well as a Short Form of Contract generally taken to cover building and civil engineering work up to a value of ú0.5m.

17. In terms of Dispute Resolution the suite of documents provides for Arbitration in all of the Forms of Contract as well as the Conditions of Engagement apart from the Short Form of Contract. Where Arbitration is used it is to be carried out under *"Public Works and Services Arbitration Rules, 2008"*.

18. Conciliation is provided as the first step in most, but not all, of the documents referred to above although in my view the use of the word is inexact. Conciliation is provided for in Clause 15 of the Short Form of Contract but there is no mention of a Recommendation and consequently it is in effect Mediation. In the Main Contracts Conciliation is provided for and fully described in Clause 13; however the process as described is closer to Adjudication than the traditional version of Conciliation.

19. The Clause 13 Procedure provides for the appointment of a Conciliator who is *"competent to adjudicate upon the dispute and independent of the parties."* The Conciliator is required to *"consult with the parties in an attempt to resolve the dispute by agreement"* and is given broad scope in the conduct of the Procedure.

20. The intention is that the dispute is to be resolved by agreement within 42 days of the Conciliatorôs appointment or a longer period agreed by the parties but where agreement is not achieved the Conciliator is required to give a written Recommendation based on *"the parties' rights and obligations under the contract"*. The parties have 42 days to consider the Recommendation and they may reject it but in doing so are required to *"State the matters in dispute and the reasons for dissatisfaction."*

21. If neither party rejects the Recommendation it becomes conclusive and binding; however in the case of rejection any payment recommended by the Conciliator is binding in the interim provided the party receiving payment:

    - Refers the dispute to Arbitration and;
    - Provides a bond covering the full extent of the payment;

    Finally, if the amount determined in Arbitration is less than the amount paid as a result of the Recommendation the party which has received the money must refund the balance together with interest.

22. Thus Clause 13 Conciliation, as provided in the Public Works Contracts, differs significantly from traditional IEI Conciliation, and is much closer to Adjudication. However it differs significantly from Adjudication in that:

- It is a much longer process;
- while it provides for payment of the monetary element of the Recommendation the conditions attached to it are such that I cannot see that a Contractor could obtain the use of the money recommended by a Conciliator.

23. I do not intend to deal with the Arbitration Rules for the Public Sector Contracts even though they contain some interesting features. However on 28 July 2011 a relatively small and unheralded change was made to the Tender and Schedule which is likely to have a very significant bearing on Arbitration under these Contracts. The effect of the change is that, as permitted by the Arbitration Act 2010, the parties to the contract must pay their own costs. However the amendment goes further and it provides that, where a sealed offer is made which is not exceeded by the Arbitratorôs Award, the Contractor will be liable for the costs of both parties; interestingly the corollary does not apply and, even if the sealed offer is exceeded, the Contractor must pay his own costs.

24. The Arbitration Act 2010 is based on international practice in commercial disputes but it applies equally to all Arbitrations commenced in this country after June 2010. The Act incorporates the UNICTRAL Model Law into Irish law with some relatively straightforward additional provisions and in my view it is a very good modern piece of legislation. I do not intend to go into in any great detail but I wish to point out the following features:

- It provides for limited court intervention. Art 5.
- It provides for the Arbitrator to decide on a challenge, Art 13, and on Jurisdiction, Art 16.
- It provides for the Arbitrator to decide all procedural matters subject to what the parties may agree. Art 19.
- It provides that the Arbitrator shall terminate the Proceedings if the Claimant fails to set out its claim. Art 25.
- It provides for reasoned Awards. Art 31.

- There is no appeal against an Award on the basis of an error in law, Art 34. Equally there is no appeal from a High Court decision.

- The parties may agree on the allocation of costs as part of the Arbitration Agreement in S. 21. This is a complete reversal of S. 30 of the 1954 Act.

25. Engineers Ireland has developed two Arbitrations Procedures specifically intended for use with the Arbitration Act 2010 and these, together with a Mediation Procedure, were launched by Judge Peter Kelly of the High Court in July this year and all are freely available at http://www.engineersireland.ie/services/dispute-resolution/ for use by anybody in a commercial dispute. The Procedures are specifically written in a modern idiom and are intended to have general application, in other words they are not confined to construction disputes, and over time they will be modified, and hopefully improved, based on experience of their use.

26. The Engineers Ireland Arbitration Procedure 2011 is suitable for multi party disputes, with one or more Arbitrators and for all disputes regardless of complexity or the amount at stake. The emphasis in the document is on the fair, expeditious, efficient and cost effective resolution of disputes and it places an onus on the Arbitrator to establish and maintain a timetable and generally conduct the proceedings to achieve these objectives. It attempts to streamline the process by moving away from litigation style pleadings towards a more comprehensive statement of each party's case to be complemented subsequently by written statements containing the evidence of each witness. The Arbitrator is given broad discretion as regards the Hearing in order to minimise the time and finally the Procedure deals with such issues as confidentiality, disclosure and the presentation of evidence generally.

27. The 100 Day Arbitration Procedure is intended for claims involving two parties and a sole Arbitrator where what is at issue is somewhat less both in terms of money and complexity. The Procedure allows for a claim and a counterclaim and it requires the Arbitrator to make an award dealing with all the substantive issues within 100 calendar days of the completion of the Arbitral appointment. The Procedure provides that where there is a counterclaim this must be set out at the same time as the claim and both of these are then run concurrently. A claim, a defence or a counterclaim must be set out fully together with backup information.

28. The Arbitrator is not allowed to extend the 100 Day timetable but is given full discretion as regards the allocation of the time; prior to acceptance of the

appointment the Arbitrator must confirm availability to meet the timetable and subsequently must consult with the parties as regards the allocation of time. The Arbitrator has broad discretion as regards the hearing ranging from whether or not to hold a hearing, fixing the length of the hearing, allocation of the time and also the manner in which evidence is to be presented.

29. The Arbitrator must make an interim award dealing with all issues, apart from costs, within 100 calendar days but may hold it until payment of any outstanding fees. If the Arbitrator does not make the Award within the time either party may terminate the proceedings and in such circumstances the Arbitrator is not entitled to any fees. However if neither party exercises the option to terminate a late Award is still valid and has full force.

30. The Construction Contracts Bill 2010 was introduced into the Seanad on 12 May last year as a Private Members Bill by Senator Feargal Quinn at the instigation of Seán Gallagher and it has been supported by the CIF. The Bill has been passed by the Seanad and it is now to be brought before the Dail with the support of the Government. The Bill as it currently stands contains 11 Sections and of these S. 3 to S. 5 deal with payment issues while S. 6 to S. 9 deal with Adjudication. The key points in relation to Adjudication are as follows:

- It is to be limited to *"any dispute relating to payment arising under the Construction Contract".*
- The parties have 5 days to agree on an Adjudicator.
- Once the appointment has been made the Claimant has 7 days to refer the dispute to the Adjudicator.
- The Adjudicator has 28 days from referral to make a decision. This period may be extended in certain circumstances.
- The Adjudicatorõs decision is binding unless the matter is referred to Arbitration.
- There is to be a Panel of Adjudicators, including a person to chair it, established by the Minister. The person who chairs the Panel will appoint an adjudicator where the parties cannot agree.
- It is envisaged the Minister will produce *"a Code of Practice governing the conduct of Adjudications*ò- in other words a Procedure.

31. In September of this year the Government published a Regulatory Impact Analysis (RIA) on the Bill and this considered the need for the legislation and its likely impact if passed into law together with a number of possible changes which could be made. The RIA was broadly positive to the Bill as currently drafted although it accepted that a change was required in relation to Contract thresholds currently in S. 2 of the Bill. It was also supportive of the idea of a National Panel of Adjudicators although noting that this was likely to *"involve a small administrative cost... in relation to appointing a Panel Chairperson to continuously maintain a Panel of Approved Adjudicators and to make nominations from the Panel from time to time. There would also be additional costs in relation to providing a secretary for the Chairperson and also for ongoing accommodation requirements and for advertisements costs etc."*

32. The RIA also considered the issue of nonbinding Adjudication under the heading ñ*Safeguarding of Public Monies"*. The concern considered is that Adjudication might *"expose the State to pay for Awards which were awarded by an Adjudicator and which were subsequently overturned by Arbitration."* This is obviously an issue troubling the Department of Finance and the RIA went on to say *"An alternative that could be considered would be have a two pillared approach, with differing arrangements for Public and Private Contracts. Adjudication would be binding for both Public and Private sectors. However the Public Sector would preserve the arrangements already in place in Public Works Contracts that require such Awards granted under the current Conciliation process to be covered by a Bond in the event that the Conciliator's decision is being challenged and is subsequently overturned in Arbitration. In such cases this could provide the necessary protection for the taxpayer."*

33. Up to this point I have attempted to set out the evolution of Dispute Resolution in the Irish Construction Industry and show where it is today. I would now like to turn my attention to what I believe is likely to happen in the coming years and also to comment on what I think should happen. I propose to do so by considering in turn the likely future roles of Adjudication, then Arbitration and finally Conciliation and Mediation.

34. I think there is little doubt that Adjudication will come into effect in this country in the near future but the real question is what form such Adjudication will take. As matters stand the current Bill is meaningless and S. 6 to S. 9 inclusive of it could be omitted since the simple fact is that unless it is binding, pending final resolution, Adjudication

is of no value. That point appears to me so obvious that I expect Adjudication, when it is introduced, will in fact be binding. I also believe the description of payment disputes in the Bill is insufficiently precise so that over time adjudication in practice will tend to be applied to all disputes rather than confined to payment issues.

35. I agree with the proposal for a National Panel of Adjudicators as set out in S. 8 of the current Bill although in my view it needs to be carefully handled in order to avoid becoming something of a political football. I support a National Panel because the alternative is a range of bodies offering the service with parties shopping from one to another to get the best Adjudicator, i.e. the most likely to favour their side, while the size of the country does not warrant several Panels of Adjudicators.

36. Currently Adjudication referrals through nominating bodies in the UK are running at somewhere between 1,500 and 2,000 per annum which means that on a pro rata base we should anticipate between 100 and 150 cases per annum in this country. On that basis it seems to me that a Panel of somewhere between 30 and 50 people should be more than adequate and I believe it should be composed of persons with significant experience of construction allied to training and qualifications in Dispute Resolution work. The suggestion in the Bill that a Barrister or a Solicitor, without any experience, should be suitable for inclusion on the Panel seems to me risible.

37. I further believe that any such Panel should be funded by taking a relatively small percentage of the Adjudicatorôs fee to cover costs. This approach is adopted in Australia and quite apart from covering the costs of the Panel it would also have the significant advantage of ensuring payment of the Adjudicator which, I understand from several Adjudicators, is a problem in the UK.

38. The really big issue in relation to Adjudication is the two pillared approach, floated in the RIA, namely that a different regime would apply to Public and Private contracts. This would mean that on any Public Sector job the Main Contractor would be liable to pay 100% of any amount recommended in Adjudication to any of its subcontractors while the same Main Contractor would have produce a 100% Bond to receive payment of any amount recommended by an Adjudicator against the Employer. The reality, as I see it, is that the Main Contractor would have to lodge the money in order to obtain the necessary surety; the effect of this is the Main Contractor would not gain the use of any money recommended and consequently would be put at a significant disadvantage.

39. In my view the two pillared approach is inherently unfair and divisive; it is also a convoluted and poorly thought out approach attempting at all costs to safeguard the interests of one group without any consideration of broader objectives or the need to improve efficiency in the industry. That is not to say that I do not have sympathy for the Department of Finance position - I do and I recognise the difficulty of attempting to recover money paid out which is subsequently determined not to be owed. However, in the broader national interest, I believe it absolutely essential that Public and Private Contracts be treated in the same manner in the Construction Contracts Bill.

40. One of the effects of Adjudication is that it shifts the balance of advantage away from the paying party towards the claiming one and a requirement for a 100% bond against any amount in an adjudicatorôs decision would negate that shift. I see no obvious reason why the amount demanded should be 100% which is very much in excess of what would be covered in a performance bond even though in fairness they are not entirely comparable situations. Personally I do not advocate the bonding of payments made following an adjudicatorôs decision but it seems to me that if such an approach is insisted upon it should be applied equally to Public and Private contracts and the percentage involved should be significantly less than 100%.

41. I have a concern about Adjudication of large claims and I find it difficult to believe that such a short process, in theory 28 days, could adequately deal with say a multimillion Euro claim on a complex Civil Engineering project. Several proponents of Adjudication, and there are many, have attempted to reassure me that whatever it says on paper it tends to work in reality ï mainly by increasing the duration. I remain sceptical and I wonder if a more appropriate solution would not be the regular use of Dispute Boards on large projects whether building or civil engineering; such a standing adjudicator would be much more likely to make a realistic assessment of disputes within a short timeframe given the ongoing contact and familiarity with the project.

42. In my view Arbitration as a process in this country, and indeed in others, is in decline and the significant growth of other Dispute Resolution methods is a testament to its shortcomings. In simple terms Arbitration is perceived, in my view rightly, as too slow and consequently too expensive. It is by no means uncommon to find an Arbitration on a one year construction job takes up to two years or to find the costs associated

with an Arbitration are a multiple of the Award and even sometimes the amounts claimed. To me, that is simply unacceptable.

43. However I believe the situation I have described above derives mainly from a lack of expertise and also a lack of creativity on the part of those involved rather than an inherent problem with the process itself. I have frequently heard it said the pool of Arbitrators in this country is very limited and outside of a few individuals the quality is at best uneven. In my view that is true but it is not the full truth of the situation since I believe the lack of expertise extends across the full range of people involved in Arbitration and in particular it seems to me to apply to lawyers where, with a few notable exceptions, the level of knowledge or understanding is limited at best.

44. In order to rectify this I believe that two approaches are required. Firstly the Professional Bodies involved in this area should recognise the need to provide ongoing training at an increasingly high level not only to those who are, or who wish to be, Arbitrators but also to those who see themselves engaged in Arbitration work. I also think those who are involved in Arbitration need to be more creative in their approach and in that context I believe the two new Procedures published by Engineers Ireland are significant. To me, a dispute involving a relatively small sum of money, and by that I mean anything up to ú250,000, should, as a matter of course, be dealt with under a fast track procedure such as the Engineers Ireland 100 Day Procedure.

45. I also see obvious scope to combine a fast track Arbitration Procedure with Adjudication. The supporters of Adjudication point to a very high success rate even though acknowledging that it is in reality rough justice. To my mind the high success rate is hardly surprising when the only alternative to accepting an unsatisfactory Adjudicatorôs determination is to embark either on a visit to the Courts or on an Arbitration which might take anything up to two years. As I understand it Adjudicatorôs decisions are not confidential and consequently may be produced in any subsequent proceedings. Consequently I believe there is a case to be made for combining Adjudication with something like the 100 Day Arbitration Procedure which would in effect operate as a rapid appeal and might lessen concerns about payment following an Adjudicatorôs decision. That would deal with the Department of Finance concerns about the need to safeguard public money and could easily be introduced into the Bill by changing S. 6(12) to read: ñ*The decision of the adjudicator shall be temporarily binding……. except where it is agreed either party may refer the decision*

to arbitration according to a procedure where the arbitrator is required to decide on the substantive matters within 100 days of appointment".

46. A further difficulty to be faced by Arbitration in Public Sector Contracts is the new cost provisions recently introduced by the Department of Finance. These have aroused a good deal of controversy, in my view understandably so, since the provisions are inequitable and a blatant abuse of power. I can see some logic in parties paying their own costs particularly in a fast track Arbitration where the costs are likely to be relatively modest; however as a general approach it seems to be wrong that a party which has been vindicated, by an Arbitrator's Award, in pursuing a claim should be denied the costs of doing so. Finally the one sided approach whereby the Contractor, but not the Department of Finance, is at risk of paying the other side's costs is simply outrageous.

47. This approach to costs and indeed the general approach to Clause 13 Conciliation and the suggestion that it should be incorporated into Adjudication highlights an inherent lack of balance in the Department of Finance. I think that is unfortunate and ultimately it will undermine the very significant achievement of the new Public Sector Contracts. I also believe this unbalanced approach is against the national interest since it will tend to damage what is an important industry and will impede rather than encourage the move to efficiency within that industry. I have no doubt that ultimately such an approach will change but it will require political will to do so and the issue is how long this will take and how much damage will be caused before the change occurs.

48. I find it difficult to see much of a future for the traditional form of Conciliation in the new world we are facing. In many ways that is a pity because Conciliation as a process has served the industry well and I believe that is generally recognised. It is an extremely flexible process and in the hands of a skilled practitioner can range, depending on the circumstances of the dispute, from a process which is essentially Mediation right through to Arbitration Lite, to the advantages of the parties.

49. On the other hand I believe there will be an increasing tendency to use Mediation even in a world which is likely to be dominated by some version of Adjudication. There are indications that trend has started in the UK while in this country Mediation is being used increasingly in commercial disputes generally.

50. In conclusion I would simply like to say that while there are areas of serious concern particularly in relation to Arbitration and to Adjudication as currently proposed, I believe that with flexibility and an emphasis on efficiency and fairness, I see no reason why the Construction Industry should not achieve a modern and efficient approach to the resolution of disputes. I see that as in the national interest and I think we should all commit ourselves to it.