Efficiency in Mediation

Solving a Complex Cross-border Energy Infrastructure Dispute in the Shadow of Three Moving Regulatory Regimes

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This article discusses a recent case in which two energy companies used mediation to completely restructure a long-term contractual package for a large joint investment. The success of the mediation can be attributed to the applicability of appropriate mediation techniques to build a win-win solution to the dispute.

The basis of the dispute was unforeseen changes in the economic, regulatory and political circumstances of a large cross-border power purchase agreement (PPA) governing the operation of a thermal power station.¹ This facility had been built in Eastern Europe with Western European finance, while the host company agreed to purchase the electricity on a long-term, fixed-price contract for domestic distribution. Since the contract began, a decline in national demand and market liberalization had resulted in excess electricity supply. The joint facility's exclusive contractual use was thus seen as extremely onerous by the host country party while the financing party insisted on proper fulfillment of its twenty-year PPA in order to recover its initial investment and earn the planned return. The value of the dispute approached US$ 1 billion.

Prior to mediation, the parties had negotiated for three years without achieving a settlement. Arbitration seemed the most likely next step. The estimated cost of arbitration was US$ 3 million, with a timescale of perhaps three years.

With enforcement proceedings and the public policy issues involved, this would have meant more than five years to achieve full resolution of the dispute. There were also several other companies involved—transporters, traders, suppliers—and the rapidly moving, disjointed regulatory regimes of the two countries and the EU to be taken into account.

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For further information on this subject, see Special Issue of Mediation of OGEL (2-2003), at www.gasandoil.com/ogel; T. Walde, Pro-active Mediation of International Business and Investment Disputes Involving Long-term Contracts: From Zero-sum Litigation to Efficient Dispute Management, 5 Business Law International 99-110 (2004).

¹ For reasons of confidentiality, details of the parties and the contract are withheld.
Both parties agreed to appoint a mediator. A crucial element was the facilitative role of one of the external leading counsel of one party, who was an advocate of trying the mediation process. A mediator was chosen by public tender from leading international financial, accounting, management consulting and engineering companies, each proposing a "sole mediator" with a backup expert team to manage the process, reach a mediation agreement and see the process through. The challenge was to develop a realistic appraisal of the dispute from the existing framework of multiple personal, institutional, culturally biased and false perceptions.

At the beginning of the mediation, the parties were reluctant to open discussions on the dispute. With gradual pressure for information and interviews of management, senior executives and experts in both parties and of other relevant players in the dispute, more details about the dispute emerged and internal divisions in each side became apparent. The mediator facilitated an improved understanding by both parties of the legal and regulatory environment and the expected near-term changes. This understanding of contractual changes underlined the possible fragility of an agreement based on the existing framework, showing that such an agreement would sacrifice the potential to optimize the joint facility as contractual changes came into effect. This realization modified the valuation of the arbitration option, exposing the risk of a fixed arbitration result for both parties.

Following the initial appraisal, a confidential assessment of each party's position was presented and discussed. A joint history gradually evolved and was formalized, having the effect of giving a more realistic view of the dispute. It also had the effect of revising both parties' standpoint of being correct, smarter and more competent than the other party. This process and the agreed joint history statement form an essential element in the external role of the mediator, as it is almost impossible for a realistic assessment of a dispute to develop within an organization. A distorted view is not an exception but the normal result of the way a dispute with an outside organization is processed, perceived and managed within an organization.

Professor Dieter Flader—an inter-cultural communications specialist—has provided a description of how the mediation process can improve perceptions. Once a dispute starts, a restriction of social intelligence on both sides occurs, firstly with a very reduced view of the other party's case, and the energy of the competing sides is drawn towards winning the case at the cost of the opponent. While co-operative elements of the dispute are available to both parties to enable a solution, both parties become blind to them and concentrate on a vicious circle of attributing blame. The mediator then has an opportunity of bringing social intelligence back to the dispute in a non-reduced form by following the principle of substitution. This means, essentially, that what the parties can no longer do by themselves alone is done in favour of both by the mediator. In this dispute, the parties had

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