Can a party ignore FIDIC's DAB process and refer its dispute directly to arbitration?

Written by Taner Dedezade

If there is no DAB appointed by the parties to a FIDIC 1999 contract, may disputes be referred directly to arbitration under clause 20.8? This issue has troubled many in the industry – and has now been considered in English and Swiss courts.

Background to the issue

Regular users of FIDIC contracts will be aware that the 1999 Red Book makes provision for a 'standing' DAB and the 1999 Yellow and Silver Books make provision for an *'ad-hoc'* DAB. In the Red Book, the pro forma appendix to tender provides the default position that the standing DAB should be constituted 28 days after the commencement date. In the Yellow and Silver books, the DAB is to be appointed by the date 28 days after one party gives notice to the other of its intention to refer a dispute to a DAB.

It seems clear that it was intended by the drafters of all 1999 FIDIC books that a dispute, once crystallised, should be referred to the DAB prior to amicable settlement/arbitration under sub-clauses 20.5 and 20.6. However, in circumstances where this is not possible e.g. if a party refuses to sign the dispute adjudication agreement (DAA) and the DAB is not 'in place', it was also intended by the drafters that the parties could rely on Sub-Clause 20.8 to bypass that process.

In the author's experience, it is common for parties to enter into a 1999 Red Book contract but fail to constitute the DAB in the time set out in the appendix to tender. It is also common in projects involving a Yellow or Silver Book contract, to find that one party does not want to refer the matter to a DAB. That party might procrastinate in the DAB appointment process and, even if an appointment is eventually made by the appointing body under sub-clause 20.3, that party will then refuse to sign the DAA.

There are conflicting views on whether an appointment under sub-clause 20.3 renders the signature of a DAA unnecessary. The author's view has always been that only when the DAA is actually signed can a DAB be said to be 'in place'. If that view is correct then (absent any ability by a court to rectify a refusal to sign – see below) it follows that sub-clause 20.8 can be relied upon and the dispute referred directly to arbitration. This view is supported by the FIDIC Contracts Guide Commentary on sub-clause 20.8:

> *"There may be "no DAB in place" because of a Party's intransigence (e.g., in respect of the first paragraph of P&DB/EPCT 20.2), or because the DAB's appointment had expired in accordance with the last paragraph of Sub-Clause 20.2. If a dispute arises thereafter, either Party can initiate arbitration immediately (subject to the first paragraph of P&DB/EPCT 20.2), without having to reconvene a DAB for a decision and without attempting amicable settlement. However, the claimant should not disregard the possibility of settling the dispute amicably.*
>
> *Under P&DB or EPCT, the first paragraph of Sub-Clause 20.2 requires a DAB to be appointed within 28 days after a Party gives notice of intention to refer a dispute to a DAB, and Sub-Clause 20.3 should resolve any failure to agree the membership of the DAB. The Parties should thus comply with Sub-Clauses 20.2 and 20.3 before invoking Sub-Clause 20.8. If one Party prevents a DAB becoming 'in place', it would be in breach of contract. Sub-Clause 20.8 then provides a solution for the other Party, which is entitled to submit all disputes (and this breach) directly to arbitration."*

Tel: + 44 (0)20 8614 6200
Fax: + 44 (0)20 8614 6222
Email: info@corbett.co.uk
www.corbett.co.uk

If one party is simply not prepared to co-operate with what is intended to be a consensual DAB process, particularly in light of the difficulties that are now recognised with the enforcement of binding but not final DAB decisions, then it makes sense for the power in sub-clause 20.8 to be available and exercised.

The courts of both England and Switzerland have had to consider these issues recently and both courts proceeded on the basis that there is a tension between:

- the opening wording of sub-clause 20.2 which uses mandatory language for the parties to refer their dispute to the DAB; and
- the wording in sub-clause 20.8 which provides that if a DAB is not 'in place whether by expiry … or otherwise' the parties can bypass the DAB.

This tension is particularly apparent in the Yellow and Silver Books where the parties are to constitute an ad hoc DAB when a dispute has arisen. A literal reading of sub-clause 20.8, in isolation, however allows a party to bypass the DAB in favour of arbitration because necessarily no DAB will be 'in place' at that point.

The English case: Peterborough City Council ("the Council") v Enterprise Managed Services Limited ("EMS") [2014] EWHC 3193 (TCC) [1]

The parties entered into a FIDIC Silver Book 1999 contract with amendments to sub-clause 20.6 which provided that the English courts would be substituted for arbitration. The Council opted to bring court proceedings without referring the matter to the DAB, relying on sub-clause 20.8. EMS applied for a stay of the court proceedings relying on sub-clause 20.2. Mr Justice Edwards-Stuart granted the stay for the parties to resolve their dispute in accordance with the contractual machinery i.e. to enable the dispute to be referred to the DAB.

Counsel for EMS, Miss Anneliese Day QC, relied on the opening words of sub-clause 20.2 and pointed out that if the wording in sub-clause 20.8 were interpreted literally, it would render sub-clauses 20.2 to 20.5 redundant.

Counsel for the Council, Ms. Fiona Sinclair QC, relied on the words *"or otherwise"* in sub-clause 20.8 to argue that it could refer the matter to court in any circumstances where no DAB was 'in place'. Counsel argued that the source of the DAB's authority was the DAA (an important point that the judge agreed with); that without a *signed* DAA the DAB could not be 'in place'; that because the parties had failed to sign the DAA, the route to arbitration under sub-clause 20.8 was open. To support her position that the court should allow court proceedings under sub-clause 20.8 (as opposed to insisting on reference to a DAB under sub-clauses 20.2 to 20.4), Ms. Sinclair argued that, sub-clauses 20.2 to 20.4 were unenforceable anyway for lack of certainty as a result of the 'gap' identified in the FIDIC General Conditions by commentators.

The judge considered the difficulties that exist in relation to the enforceability of binding DAB decisions as raised by Ms Sinclair. They had been set out in two articles on the "gap". One was written by Professor Nael Bunni. The other was the present author's own article entitled *Mind the gap: Analysis of cases and principles concerning the ability of ICC tribunals to enforce binding DAB decisions under the 1999 FIDIC Conditions of contract* [2012] Int ALR 145). The judge summarised the issues set out in: *"Mind the gap"* as follows: *"limitations on the powers of the arbitrators…(in particular whether or not they could order specific performance), the type of award (interim, partial or final) that is or may be appropriate if the DAB's decision is to be enforced and the whole question of delay that would be involved in resorting to arbitration"*. The judge considered that although this *"may be arguable in the context of the standard FIDIC red books which include an arbitration clause, it loses force where the arbitration clause has been removed – as in the present case."* His rationale was that an English court has the power of specific performance and so would have no difficulty in using that power in relation to the enforcement of a DAB decision.

Tel: + 44 (0)20 8614 6200
Fax: + 44 (0)20 8614 6222
Email: info@corbett.co.uk
www.corbett.co.uk

The judge turned to the potential problem of a failure by the parties to agree on an adjudicator's fees for insertion in the DAA. He found that there was an implied term that the adjudicator would be entitled to his reasonable fees and expenses which the court could readily assess in default of agreement. In practice, however, it is usual for the DAB to propose its own fees. If one party considered that the fees were reasonable and the other thought they were excessive and therefore refused to sign the DAA, it is unlikely that the court could impose a lesser fee than that requested by the DAB because in those circumstances, it is likely that the DAB would simply refuse to act.

The judge dealt with the situation where one party refused to sign the DAA. He ruled that, again, the court could exercise its power of specific performance to compel the refusing party to sign. Indeed if all of the terms of the DAA were clear and accepted, and/or the court felt able to imply reasonable fees in the absence of agreement, the possibility of compelling a party to sign might be appropriate. However, in circumstances where, for example, the DAB wished to propose additional terms to its DAA (which is quite common in practice) and one party rejected those terms, it is questionable whether a judge would have the power to compel the parties to sign in the face of such disagreement.

It is interesting to note that the judge considered that the DAB is 'in place' from the moment that the member(s) of the DAB has/have been appointed, whether under sub-clause 20.2 or 20.3. He considered that *"the effect of incorporating the Appendix to the Conditions as the terms of the Dispute Adjudication Agreement was that all the relevant terms of that agreement would be in place save for agreement of the adjudicator's fees"*. The advantage of the judge's analysis is that if there is an interval (which might be substantial) between the date of appointment and the date on which a party ultimately signs the DAA (following an order by the Court that it is compelled to sign), any work carried out by the DAB in this period will be within its jurisdiction. Conversely, if the date when the DAB is 'in place' is the date of signature of the DAA, any work carried out in the interval before date of signature would arguably be a nullity.

The judge's construction fits the facts of the Peterborough case because he concluded that he *could* rectify the issues set out above (failure to agree terms/fees/refusal to sign). However, his construction would not necessarily be correct in circumstances where those issues could *not* be rectified by the court or by an arbitral tribunal. The judge correctly concluded that the source of the DAB's authority is the DAA. If specific performance is not a power available to the arbitral tribunal or if the nature of the issue is simply not amenable to the exercise of such a power, then the judge's analysis is questionable.

Swiss Federal Supreme Court Case dated 7 July 2014 (4A_124/2014) [2]

The Parties entered into a FIDIC 1999 contract – the court did not specify which Book. Following a dispute the parties spent some 15 months unsuccessfully trying to form a DAB despite some input from the President of FIDIC. It is difficult from the judgment to establish the precise sequence of events. In the end, one party refused to sign the DAA and issued arbitration proceedings. As a preliminary issue, the arbitral tribunal was asked to determine whether it had jurisdiction over the dispute referred to it. The tribunal, seated in Geneva, issued a partial award upholding jurisdiction. The losing party sought annulment of the partial award in the Swiss courts, under ss. 190-192 PILA, the Swiss law on international arbitration. The Swiss Federal Supreme Court published its redacted judgment in French on 20 August 2014. It rejected the application for annulment upholding the arbitral tribunal's partial award. We have relied on an unofficial translation of the judgement in preparing this case note.

Reasoning

The following points mentioned in the judgment are of interest:

- Reference to the DAB is mandatory subject to exceptions.

Tel: + 44 (0)20 8614 6200
Fax: + 44 (0)20 8614 6222
Email: info@corbett.co.uk
www.corbett.co.uk

- What was contemplated by sub-clause 20.8 was exceptional (for a standing DAB situation), namely there is a time-period for the duration of the DAB which then expires. In such circumstances, the DAB is no longer 'in place'.
- The strict interpretation of sub-clause 20.8 *"would ultimately turn the alternate dispute resolution mechanism devised by FIDIC into an empty shell"* (the same point made by counsel for EMS in the English case above).
- The intransigence of a party was an example of circumstances that justify omitting the DAB.
- *"Special circumstances, whether objective or not, must be reserved in which resorting to pre-arbitration DAB procedure could not be imposed upon the party wishing to submit the dispute with its contractual counterpart to arbitration. Considered from the opposite perspective, the exception is a case in point of the principle of good faith, which governs the procedural behaviour of the parties as well. Depending on the circumstances, the principle will therefore prevent one of them from objecting on the basis of the absence of a DAB decision. Yet, saying in advance and once and for all when it may be applied is impossible because the answer to the question depends upon the facts germane to the case at hand."*
- Under Clause 2, first paragraph, of the General Conditions of the DAA, the DAA takes effect when the project owner, the contractor and each member of the DAB have signed it. On the facts of this case, as the DAA had not been signed, the DAB was not 'in place'. In circumstances where a DAB is not 'in place', it is permissible to refer the dispute directly to arbitration under sub-clause 20.8.
- *"[I]t is indeed impossible to blame the Respondent for losing patience and finally skipping the DAB phase despite its mandatory nature in order to submit the matter to arbitration."*

It seems, therefore, that the Swiss court considered that sub-clause 20.8 was the exception rather than the rule. However, in the author's view, that fact should not present a particular hurdle to its operation. If one party is faced with intransigence of another in the setting up of a DAB, it should not be necessary for him to waste further time proving that he did all he could to refer the matter to the DAB. The Swiss court did not give any guidance as to how long a party has to try for before it can resort to 20.8. Certainly, there was no endorsement of the 28-day time limit in 20.2 (which permits a party to apply to FIDIC) as the moment when 20.8 applies. The author suggests that as soon as the other party's refusal to co-operate and therefore his breach of contract becomes clear, the first party should be free to refer the matter to arbitration. Necessarily at that point there will be no DAB 'in place' and so the mechanism in Sub-Clause 20.8 will be available. The Swiss court held that a refusal to sign the DAA meant there was no DAB 'in place' and so Sub-Clause 20.8 could be relied on. That decision must be correct even if the court left it unclear for how long such a refusal should last.

Conclusion

Both the English and the Swiss judgements support the existence of the DAB as the centre-piece for dispute resolution in the FIDIC contract. In England, the judge went so far as to treat the DAB process as a mandatory pre-condition to arbitration. The court felt able to rectify all the difficulties arising on the facts of that case by using its extensive powers to ensure that the DAB was 'in place'. However, on other facts, even if an English court were substituted for arbitration, it is questionable whether it will always be possible to rectify a lack of agreement and/or signatures of the DAA. It is difficult to see how arbitrators could do so. Accordingly, it seems to the author that those who are prevented from referring a dispute to DAB by an uncooperative party may go directly to arbitration by relying on sub-clause 20.8. Those who would prefer to skip the DAB stage may not do so without first attempting to set up a DAB.

In the second editions of the 1999 forms, FIDIC should consider making it clear that a

Tel: + 44 (0)20 8614 6200
Fax: + 44 (0)20 8614 6222
Email: info@corbett.co.uk
www.corbett.co.uk

failure by one party to sign the standard DAA with a DAB member agreed by the parties or appointed by FIDIC will not prevent the DAB giving valid decisions. To make this work, perhaps FIDIC could publish a range of fees deemed reasonable by any party signing a FIDIC contract. One way or another, the success of the DAB project depends on it being seen as a means of quick, straightforward and enforceable dispute resolution. We are not there yet.

[1] http://www.bailii.org/ew/cases/EWHC/TCC/2014/3193.html

[2] http://www.servat.unibe.ch/dfr/bger/140707_4A_124-2014.html

Article Author

Taner Dedezade

Email: taner.d@corbett.co.uk

Tel: + 44 (0)20 8614 6200
Fax: + 44 (0)20 8614 6222
Email: info@corbett.co.uk
www.corbett.co.uk