PERSERO II: "PAY NOW, ARGUE LATER" IN THE CONTEXT OF DAB DECISIONS – WHAT APPROACH BEST ADVANCES THE PURPOSE OF THE FIDIC'S SECURITY OF PAYMENT REGIME?

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1. INTRODUCTION

It is now firmly established in international arbitration circles that binding but not final decisions made by a Dispute Adjudication Board ("DAB") can be enforced by the winning party if the other party fails to comply with the decision in breach of sub-clause 20.4 of the FIDIC Conditions of Contract. The Singapore High Court has recently confirmed this in *PT Perusahaan Gas Negara (Persero) TBK v CRW Joint Operation (Indonesia)*[2] ("*Persero II*") and this is a welcome decision in this regard.

What is not clear, however, is what the winning party is meant to do in practice in order to enforce those binding but not final DAB decisions. The High Court in *Persero II* examines two possible approaches:

- "*The two-dispute approach*", whereby the winning party refers solely to arbitration the narrow dispute relating to the other party's failure to comply with the DAB decision, being a separate dispute in its own right, ie a breach of sub-clause 20.4, distinct from the underlying dispute; or
- "*The one-dispute approach*", whereby the winning party refers to arbitration both the other party's failure to comply with the DAB decision *and* the merits underlying the DAB decision at the same time, on the basis that the recalcitrant party's breach of sub-clause 20.4 is "simply another aspect of that primary dispute"[3].

Christopher Seppälä – legal advisor for the FIDIC Contracts Committee – in his detailed commentary of the *Persero II* decision[4] – endorses the conclusion of the High Court that "the one-dispute approach best advances the objective of the Red Book's security of payment regime"[5].

For reasons that follow, the author respectfully disagrees with that conclusion, as this one-dispute approach would unnecessarily complicate

[1] The views expressed herein are entirely those of the author and not necessarily those of the firm. The author is grateful to Estee Tan, Associate at Pinsent Masons LLP, for her comments on this paper.

[2] Judgment of the High Court of Singapore dated 16 July 2014 (the "2014 High Court decision" or the "*Persero II* decision") [2014] SGHC 146.

[3] 2014 High Court decision, paragraph 60.

[4] Christopher Seppälä "Singapore contributes to a better understanding of the FIDIC Disputes Clause: the second *Persero* case" [2014] ICLR 4.

[5] 2014 High Court decision, paragraph 176.

the enforcement of DAB decisions by forcing a party who may be satisfied with a DAB decision to take the onerous and time-consuming step of bringing an arbitration on the merits of the underlying dispute when, ultimately, all that party wants to do is to obtain a prompt payment of the sums awarded by the DAB.

Mr Seppälä suggests that: "While requiring the merits to be submitted to the same arbitration is less than ideal, this should not necessarily be a major inconvenience", echoing the High Court's view that "this is a minor disadvantage"[6]. The author submits that such an approach would not only be a major inconvenience to the winning party, but it would ultimately defeat the purpose of the DAB regime, which, when treated as a security of payment regime, is primarily designed to facilitate the cash flow of contractors in the construction industry as acknowledged by the High Court in *Persero II*[7].

This article examines why the winning party should be entitled to refer the failure itself to arbitration without having the burden of bringing the underlying dispute to arbitration concurrently. In the authors' view, this approach – described by the High Court as the "the two-dispute approach" – best advances the FIDIC's security of payment regime by requiring the employer to pay immediately, whilst allowing the employer to the underlying merits of that payment obligation contest (either in the same arbitration by bringing a counterclaim or in a separate arbitration) at a later stage, should it wish to do so. That two-dispute approach is also consistent with FIDIC's express policy objectives in relation to the enforcement of DAB decisions,[8] which the High Court has unfortunately not taken into account in its decision.

2. BACKGROUND: PERSERO I

The facts of the earlier case between the same parties PT Perusahaan Gas Negara (Persero) TBK ("PGN") and CRW Joint Operation ("CRW") ("*Persero I*"[9]) have already been covered in a number of articles published in ICLR[10].

[6] 2014 High Court decision, paragraph 75.

[7] 2014 High Court decision, paragraph 23.

[8] Namely, the implications of sub-clause 20.7 of the 1999 Red Book, sub-clause 20.9 of the latest Conditions of Contract for Design, Build and Operate Projects (the "Gold Book") issued in 2008 and the FIDIC Guidance Memorandum issued by the FIDIC Contracts Committee in April 2013 (the "2013 FIDIC Guidance"). See below.

[9] *PT Perusahaan Gas Negara (Persero) TBK v CRW Joint Operation (Indonesia)* [2010] SGHC 202 (the "2010 High Court decision") and *CRW Joint Operation (Indonesia) v PT Perusahaan Gas Negara (Persero) TBK* [2011] SGCA 33.

[10] See, eg, from the author Frédéric Gillion, "Enforcement of DAB decisions under the 1999 FIDIC Conditions of Contract – a recent development: *CRW Joint Operation (Indonesia) v PT Perusahaan Gas Negara (Persero) TBK*" [2011] ICLR 388; Christopher Seppälä, "How not to Interpret the FIDIC Disputes Clause: The Singapore Court of Appeal judgment in *Persero*" [2012] ICLR 4.

In summary, the parties' contract incorporated the FIDIC Conditions of Contract for Construction, First edition, 1999 (the "1999 Red Book"), with some amendments (the "Contract"). A dispute arose regarding certain variations in respect of which CRW sought additional payment. The dispute was referred to the DAB, following which a number of decisions were given by the DAB. One of the decisions ordered PGN to pay CRW a sum in excess of US$17 million. PGN issued a notice of its dissatisfaction pursuant to sub-clause 20.4 of the Contract, and subsequently refused to comply with the DAB's decision.

CRW filed a request for arbitration with the ICC International Court of Arbitration in 2009 which was limited to PGN's non-payment of the sum set out in the DAB's decision. Critically, CRW had not referred to the DAB the dispute which arose as a consequence of PGN's failure to comply with the DAB's decision.

The arbitral tribunal (the "2009 tribunal") found in CRW's favour and held in a final award that PGN was bound to pay CRW the sum US$17 million which had been awarded by the DAB.

PGN then applied to set aside the 2009 tribunal's award in Singapore, the seat of the arbitration.

In *Persero I*, the High Court and the Court of Appeal found in PGN's favour and held – although on different grounds – that the award should be set aside. These grounds were essentially the following:

(a) Ground 1: The dispute that CRW referred to arbitration – namely PGN's failure to comply with the DAB's decision – is a separate dispute and as such should initially have been referred to the DAB for a decision under sub-clause 20.4, which CRW did not do in the *Persero I* case[11]. The High Court in *Persero I* considered that consequently, the 2009 tribunal had exceeded its jurisdiction in making that award; and

(b) Ground 2: The arbitral proceedings were commenced pursuant to sub-clause 20.6 of the FIDIC Conditions of Contract – which requires, according to the High Court in *Persero I*, "a review of the correctness of the DAB decision" – and had to be distinguished from proceedings brought under sub-clause 20.7. The Court of Appeal reached a similar conclusion by relying on the fact that the

[11] The 2010 High Court relied in particular on the first sentence of sub-clause 20.6 which provides that:

"Unless settled amicably, any dispute in respect of which the DAB's decision (if any) has not become final and binding shall be finally settled by international arbitration". This is also clear from the penultimate paragraph of sub-clause 20.4 which provides that: "Except as stated in sub-clause 20.7 [*Failure to Comply with Dispute Adjudication Board's Decision*] and sub-clause 20.8 [*Expiry of Dispute Adjudication Board's Appointment*] neither Party shall be entitled to commence arbitration of a dispute unless a notice of dissatisfaction has been given in accordance with this sub-clause."

2009 tribunal had not exercised its discretion to open up, review and revise the DAB decision, which in turn meant that the award was not issued in accordance with sub-clause 20.6;[12]

(c) Ground 3: The Court of Appeal further held that there had been a breach of natural justice in that case as the 2009 tribunal had refused to open up and review the DAB decision when asked by PGN, and that, as a result, PGN had been denied a proper opportunity to present its case comprehensively on the DAB's decision.

Most commentators who have examined *Persero I*, including the author and Mr Seppälä, have agreed that the High Court and the Court of Appeal in *Persero I* erred in their interpretation of sub-clauses 20.6 and 20.7 in respect of Ground 2.

As for Ground 1, which is directly relevant to the present discussion about the one or two dispute approach developed in *Persero II*, a number of commentators[13] have, based on their actual experience of enforcing DAB decisions in arbitration, expressed support for the two-dispute dispute approach adopted by the High Court in *Persero I* and its conclusion that a separate referral to the DAB was required in respect of a party's failure to comply with a binding but not final DAB decision, given the current wording of sub-clause 20.7.

Mr Seppälä, on the other hand, was and, judging from his recent article, remains of the view that Ground 1 was questionable and that the Court of Appeal was right not to adopt it in its judgment in *Persero I*. Mr Seppälä commented at the time: "*As a practical matter, is a dispute over the enforcement of a DAB's decision to be distinguished from one over the merits of that decision? Can they not as easily be characterized as just one dispute?*"[14]

These are more or less the same questions which the judge considered necessary to answer in *Persero II*.

[12] The Court of Appeal relied on the fact that the Terms of Reference stated that the arbitration was commenced pursuant to sub-clause 20.6, which, according to the Court of Appeal, conferred to the arbitral tribunal "an unfettered discretion to reopen and review each and every finding by the Adjudication." This was on the basis that sub-clause 20.6 provides that: "The arbitrator(s) shall have full power to open up, review and revise (…) any decision of the DAB (…)." In *Persero I*, the arbitral tribunal declined to do so, on the basis that PGN had not filed a counterclaim. For further discussion on this, see the author's previous article on *Persero I* [2011] ICLR 403, and Seppälä, "How not to Interpret the FIDIC Disputes Clause: The Singapore Court of Appeal judgment in *Persero*" [2012] ICLR 4.

[13] See, eg, Oana Soimulescu and David Brown, "Enforcement of binding DAB decisions: A fresh approach to clause 20 of the 1999 FIDIC Conditions of Contract" [2012] ICLR 19, 24-25; Taner Dedezade, "The legal justification for the 'enforcement' of a 'binding' DAB decision under the FIDIC 1999 Red Book" (2012) 7(1) *CLInt* 13, 17; David Brown and Oana Soimulescu, "Enforcement of binding but not final DAB decisions: the impact of ICC Case 16948/GZ" (2012) 7(3) *CLInt* 7, 10; and Gerlando Butera, "Untangling the Enforcement of DAB Decisions" [2014] ICLR 36, 54 and 57.

[14] Christopher Seppälä, "How not to Interpret the FIDIC Disputes Clause: The Singapore Court of Appeal judgment in *Persero*" [2012] ICLR 4.

3. THE SINGAPORE HIGH COURT DECISION IN *PERSERO II*

Following *Persero I*, CRW presumably decided, to be on the safe side, to return to the DAB with a separate and narrow referral specifically on PGN's failure to comply with the DAB's decision. When it came to enforce that second DAB decision, CRW however followed the view expressed by the Court of Appeal in *Persero I* that "the practical response is for the successful party in the DAB proceedings to secure an interim or partial award from the arbitral tribunal in respect of the DAB decision pending the consideration of the merits of the parties' dispute(s) in the same arbitration"[15].

Accordingly, CRW commenced a second arbitration in 2011 with a new tribunal (the "2011 tribunal") to whom it referred both the underlying dispute (referred to in *Persero II* as the "primary dispute") and the losing party's failure to comply with the DAB decision (the "secondary dispute").

At an early stage in the proceedings, the 2011 tribunal rendered an interim or partial award in CRW's favour directing PGN to comply with the DAB decision in accordance with sub-clause 20.4 by paying the sum due to CRW immediately, pending the final resolution of the underlying dispute.

CRW then sought to enforce that interim or partial award against PGN. PGN in turn applied to the Singapore High Court to set aside that partial or interim award and the order sought by CRW to enforce the award.

Since CRW had strictly followed the Court of Appeal's interpretation of the steps that ought to be taken under the contract to enforce the DAB decision, it is no surprise that PGN's application to set aside that partial or interim award was dismissed by the 2014 High Court in *Persero II*.

The 2014 High Court indeed held that the arbitration award was entirely consistent with the Contract and with the manner in which that Contract had been interpreted by the Court of Appeal in *Persero I*.

In reaching its conclusion, the High Court in *Persero II* examined the DAB regime contained in sub-clauses 20.4 to 20.7 of the 1999 Red Book – referred to by the High Court as "a security of payment regime" – and its "central purpose", namely: "to facilitate the cash flow of contractors in the construction industry" by requiring the employer to pay immediately, whilst allowing the employer to argue later about the underlying merits of that payment obligation.

The author entirely agrees with Mr Seppälä that this was the right approach and also with Mr Seppälä's conclusion that "when interpreting those sub-clauses, one must look not merely to their words or phrases in isolation (as some tribunals and commentators appear to have done), but

[15] Court of Appeal decision, paragraph 66.

rather to the purpose of that regime, interpreting the words in light of that purpose."

The problem is that by seeking to conceptualise the security for payment regime with this one/two-dispute approach, the 2014 High Court ended up completely ignoring the intentions of FIDIC in relation to the enforcement of the DAB decisions, but also more fundamentally, it overlooked the true difficulties which will necessarily arise as a result of adopting the one-dispute approach.

The author submits, as explained further below, that by forcing a contractor to bring an arbitration not only for the employer's failure to comply with the DAB decision but also on the merits of the underlying dispute, this one-dispute approach ultimately defeats the purpose of the FIDIC's security of payment regime, summarised by the aphorism "pay now, argue later".

4. HOW THE "PAY NOW, ARGUE LATER" PRINCIPLE HAS BEEN IMPLEMENTED IN JURISDICTIONS WITH A STATUTORY ADJUDICATION REGIME

The "pay now, argue later" principle is at the heart of all statutory adjudication schemes which have been spreading around the world in recent years.

Adjudication was first introduced in the UK in May 1998 as a result of the Housing Grants, Construction and Regeneration Act 1996 ("HGCRA"). This statutory adjudication scheme provides that anyone entering into a construction contract (with some exceptions defined by the 1996 Act) has the unilateral right to call in an adjudicator to resolve any dispute in order to obtain a decision within 28 days.

The underlying principle behind the introduction of the compulsory statutory adjudication system in the UK was to recognise that cash-flow is the lifeblood of the construction industry. It follows the recommendation in the Latham Report[16] to tip the scales in favour of contractors, even if that was at the temporary expense of those who had to pay. This is perhaps best summarised in this passage by the Minister for Construction Planning and Energy Efficiency, Robert B Jones, when HGCRA was debated in the House of Commons:

> "The Bill promotes a clear system of dispute resolution called adjudication. The industry is clear about what it means by that: it wants a mechanism that produces a fast and impartial resolution of a dispute and allows the contract to continue. The industry does not want the decision necessarily to be the final one. It wants to ensure

[16] A review conducted by Sir Michael Latham of procurement and contractual arrangements in the UK, funded by the Department of the Environment together with four industry organisations and two groups representing clients. The Latham Report was published in July 1994.

> that disputes are tested at the time, on the spot and are resolved quickly to the party's satisfaction[17]."

Lord Ackner also usefully highlighted the intent of the HGCRA during the debate at the report stage in the House of Lords by reference to the "pay now, argue later" principle:

> "What I have always understood to be required by the adjudication process was a quick enforceable interim decision which lasted until practical completion when, if not acceptable, it would be the subject of arbitration or litigation. That was a highly satisfactory process. It came under the rubric of 'pay now argue later' which was a sensible way of dealing expeditiously and relatively inexpensively with disputes that might hold up the conclusion of important contracts."

Other common law jurisdictions have followed this model[18] though sometimes limiting the statutory regime to payment disputes, as is the case in Singapore[19].

A common feature in each of these statutory adjudication schemes is that construction disputes can be dealt with quickly and economically and, more importantly, the courts will enforce the adjudicator's decisions quickly by granting a summary judgment. This is for example the case in Singapore where the adjudicator's determination can be enforced, with leave of the court, in the same manner as a judgment or an order of the court. This is also the case in the UK where it is well established after 16 years of practice (and in excess of 30,000 adjudicator's decisions) that the courts will give effect to the "pay now, argue later" principle by enforcing adjudicator's decisions through summary judgments.

It is, in the author's opinion, the possibility for a contractor to enforce the adjudicator's decision quickly by applying for a summary judgment – without the judge looking into the underlying merits of that decision at that stage – that best achieves the "pay now" objective and thereby ensures that the security of payment regime functions correctly. Lord Justice Chadwick confirmed in the Court of Appeal case *Carillion Construction Ltd v Devonport Royal Dockyard Ltd*[20] that "in the overwhelming majority of cases, the proper course for the party who is unsuccessful in adjudication under the scheme must be to pay the amount that he has been ordered to pay by the adjudicator."

[17] *Hansard*, 7 May 1996, column 52.

[18] For example, New Zealand adopted the Security of Payment Act, and each of the States in Australia has also introduced adjudication. Singapore and Malaysia introduced a similar process in 2005 and 2012 respectively.

[19] In Singapore, statutory adjudication was introduced by the Building and Construction Industry Security of Payment Act. This Act was enacted in 2005 to facilitate payments for construction work done or for related goods or services supplied in the building and construction industry. It Act states that any party who has carried out construction work or supplied related goods or services in the building and construction industry under a contract made in writing has a statutory right to receive progress payment, even in the absence of such provision in the contract.

[20] [2006] BLR 15, paragraphs 85 to 87, a case referred to by Christopher Seppälä in "Singapore contributes to a better understanding of the FIDIC Disputes Clause: the second *Persero* case" [2014] ICLR 000.

Recent statistics[21] also confirm that approximately 85 per cent of adjudicator's decisions rendered in the UK are either complied with or lead to a settlement of the dispute without the need to enforce them. As for the remaining 15 per cent of adjudicators' decisions that need to be enforced through summary judgment, the Court of Appeal in England and Wales has consistently confirmed over the years the strict approach to enforcement adopted by the Technology and Construction Court ("TCC") and the very limited grounds on which adjudicators' decisions may be challenged (essentially lack of jurisdiction and breach of natural justice).

Unfortunately, no recent statistics are currently available in respect of DAB decisions, but in the author's experience, DAB decisions are more often than not ignored by employers, essentially because they currently see little or no risk in having the DAB decision quickly enforced against it.

There is very little evidence to suggest that the one-dispute approach recommended by the 2014 High Court will change that trend, since it requires the contractor to commence an arbitration on the merits of the underlying dispute if the contractors wishes to enforce its substantive right under sub-clause 20.4 to obtain immediate payment of any amount awarded by the DAB in its decision. This approach is, as explained below, entirely inconsistent with the essential features of the FIDIC's security of payment regime.

5. THE FIDIC'S SECURITY OF PAYMENT REGIME

In reality, the DAB regime included in the FIDIC 1999 Red Book goes beyond a simple security of payment regime, as in principle any dispute arising between the parties in connection with the contract or the execution of the works may be referred to the DAB for its decision[22].

The use of the expression "security of payment regime" by the 2014 High Court to describe the FIDIC's DAB regime was driven by the fact that adjudication in Singapore is limited to payment disputes. The 2014 High Court acknowledged this in its decision[23] but explained that, for convenience of exposition, it would use the "security of payment" terminology in its decision. The author will do the same here.

[21] The 2011 TCC Report indicates that 18 per cent of the 815 claims brought to the TCC (London and regional centres) between October 2010 and September 2011 are attributable to adjudication. This amounts to a maximum of 147 cases out of a total of approximately 1,000 adjudication cases (representing therefore 15 per cent of all adjudication cases) over that period according to the Glasgow Caledonia University.

[22] Sub-clause 20.4 of the 1999 Red Book provides: "If a dispute (of any kind whatsoever) arises between the Parties in connection with, or arising out of, the Contract or the execution of the Works, including any dispute as to any certificate, determination, instruction, opinion or valuation of the Engineer, then (…) either party may refer the dispute in writing to the DAB for its decision (…)".

[23] 2014 High Court decision, paragraph 32.

The reality is that the FIDIC's DAB regime[24] is closer to the adjudication system which is currently in place in other jurisdictions such as the UK (where all types of construction disputes may be referred to adjudication[25]). This has sometimes resulted in what was described by His Honour Judge Coulson in *William Verry (Glazing Systems) Ltd v Furlong Homes Ltd* [2005] as "kitchen sink adjudications", namely final account claims involving disputes about measured works, variations, valuations, extensions of time, loss and expense, defects and retention.

However, even then, the primary purpose of the adjudication regime remains ultimately to facilitate the cash flow of contractors by producing a fast and impartial resolution of a dispute and an enforceable interim decision which, if not acceptable, would be the subject of arbitration or litigation under the principle of "pay now, argue later".

This principle of "pay now, argue later" which underlies a security of payment regime is described in some detail by the 2014 High Court decision which considers that, as a result, that regime must have three essential features:

> "(a) First, it establishes a quick and relatively inexpensive procedure by which a contractor can secure from a neutral body a binding interim adjudication of its right to receive a disputed payment.
> (b) Second, it gives a successful contractor a quick and relatively inexpensive way of compelling a recalcitrant employer to comply with the interim adjudication.
> (c) Third, it ensures that the interim adjudication does not in any way preclude the parties from, in the fullness of time, arriving at a resolution of their payment dispute on its merits and with finality."

The first and second features are described by the 2014 High Court as comprising the "pay now" element, whilst the third feature enables the "argue later" element.

This description of the "pay now, argue later" principle by the 2014 High Court is, as seen above, entirely consistent with the description given by the House of Lords of that same principle when statutory adjudication was introduced in the UK.

The 2014 High Court then considered that "[t]here is a clear contractual intent in the Red Book's security of payment regime to implement the[se] three essential features (…) and to compel an obligor to pay now and argue later"[26]. The 2014 High Court importantly added the following:

> "The DAB is the neutral body empowered to make the interim adjudication. Clause 20.4[4] obliges an employer who has failed before the DAB to pay now. Most importantly for present purposes, clause 20.4[4] gives the contractor a correlative right to be paid now, without waiting for the final dispute to be resolved with finality. This is a substantive contractual right in and of itself. It is this right which forms the foundation of the secondary dispute. Clauses 20.6[2] and 20.6[3] permit the parties to

[24] Obviously putting aside the dispute avoidance role of the DAB in the 1999 Red Book.
[25] This is in fact acknowledged by the 2014 High Court at paragraph 32.
[26] 2014 High Court decision, paragraph 33.

> argue later. Clause 20.4[7] makes the DAB decision final if neither party gives notice of dissatisfaction within 28 days."[27]

The 2014 High Court summarised there, correctly in the author's view, the mechanism under the 1999 Red Book which allows the contractor to enforce its substantive contractual right under sub-clause 20.4 obtain immediately any amount awarded by the DAB in its decision.

6. WHY THE TWO-DISPUTE APPROACH BEST ADVANCES THE FIDIC'S SECURITY OF PAYMENT REGIME

The 2014 High Court rightly considered that "the central issue" of the case was whether CRW was "entitled to enforce the DAB decision by an interim award, which is final and binding without determining the merits."[28]

Having noted that the employer's failure to comply with a DAB decision is a breach of a substantive contractual right, namely a breach of sub-clause 20.4, it would have been logical for the 2014 High Court to conclude, in response to that "central issue", that a successful party is indeed entitled to enforce the DAB decision by bringing solely the "secondary dispute" to arbitration. That approach (described by the 2014 High Court as the "two-dispute" approach) is, as seen above, entirely consistent with the practice of enforcing adjudicators' decisions in jurisdictions which have introduced statutory adjudication.

Interestingly, the 2014 High Court initially reached that conclusion when it stated:

> "The two-dispute approach best advances the 'pay now' objective of the Red Book's security of payment regime. It gives the contractor a quick and relatively inexpensive way of compelling a recalcitrant employer to comply with the DAB's interim adjudication (see [2525(b)] above). This approach permits the contractor to refer to an arbitral tribunal the secondary dispute alone, for the tribunal to resolve separately and with finality, without requiring the contractor to incur the time and cost involved in having the primary dispute also resolved on the merits. Further, because the two-dispute approach separates clearly the two disputes, the arbitral tribunals' decision on the *secondary* dispute alone does not compromise the employer's ability in a future arbitration to 'argue later' over the primary dispute."[29]

The 2014 High Court seems however to have changed its mind during the course of its lengthy analysis and eventually dismissed the "two-dispute" approach, after having identified two shortcomings in the drafting of sub-clauses 20.4 to 20.7[30]. Those shortcomings are, the court said, exposed by the following "subsidiary questions":

[27] 2014 High Court decision, paragraph 33.

[28] 2014 High Court decision, paragraph 15 quoting paragraph 27 of PGN's Written Submissions dated 4 October 2013.

[29] 2014 High Court decision, paragraph 40.

[30] 2014 High Court decision, paragraph 35.

> "(a) Do the conditions precedent to arbitration continue to apply where the contractor wishes to refer the *secondary* dispute to arbitration under clause 20.6?
> (b) When the contractor seeks merely to resolve the *secondary* dispute, what limits are there, if any, on the power of the tribunal to open up the DAB decision under clause 20.6[2] and on the liberty of the parties to attack the DAB decision under clause 20.6[3]?"[31]

In focusing on those subsidiary questions, the 2014 High Court lost sight of the primary purpose of the FIDIC's security of payment regime when it concluded – wrongly in the author's view – that:

(a) the "two-dispute" approach "causes insoluble difficulties with both the "pay now" and the "argue later" aspects of the Red Book's security of payment regime"[32] and is therefore inconsistent with these features of security of payment regime;[33] and
(b) the "one-dispute" approach (namely a referral to arbitration of both the secondary dispute and the underlying merits of the primary dispute) must therefore be preferred as it "permits the drafting of the Red Book's dispute-resolution regime to be reconciled with its contractual intent to create a working security of payment regime"[34].

This is explained further below by examining the shortcomings in the drafting of sub-clauses 20.4 to 20.7, the consequences of which, the author submits, have been misunderstood or exaggerated by the 2014 High Court.

Do the conditions precedent to arbitration continue to apply where the contractor wishes to refer the *secondary* dispute to arbitration under clause 20.6?

The answer to that question is "yes" given the current wording of sub-clause 20.7.

The 2014 High court correctly noted that the 1999 Red Book "provides no shortcut to arbitration of the secondary dispute which is equivalent to clause 20.7", which means in practice the following:

> "a contractor holding a non-final DAB decision and wishing to arbitrate the secondary dispute must comply with the three conditions precedent to arbitration. That in turn means referring the secondary dispute to the DAB (clause 20.4[1]), waiting up to 84 days for the DAB to render its decision on the secondary dispute (clause 20.4[4]), plus another 28 days for the DAB decision on the secondary dispute to become final (clause 20.4[7]) or, if either party issues a notice of dissatisfaction within time, a further 56 days while the recalcitrant employer refuses to discuss amicable settlement

[31] 2014 High Court decision, paragraph 36.
[32] 2014 High Court decision, paragraph 44.
[33] 2014 High Court decision, paragraphs 48, 54 and 55.
[34] 2014 High Court decision, paragraph 58.

> of the secondary dispute (clause 20.5[1]). All of this delay is in addition to the time which has already elapsed while complying with the three conditions precedent in respect of the *primary* dispute."

The author already explained in respect of the *Persero I* case[35] that:

> "because the losing party's failure to comply with the DAB decision gives rise to a fresh cause of action – namely a breach of sub-clause 20.4 (which requires the decision to be given effect promptly) – and is a new and separate dispute from the original dispute referred to the DAB (…) [p]ursuant to sub-clauses 20.4 to 20.6 (and subject to the exception of sub-clause 20.8 – DAB no longer in place), any such dispute will have to be referred first to the DAB for its decision, and following the giving of a notice of dissatisfaction, the parties will have to comply with the amicable settlement procedure before the dispute may be referred to arbitration. Failing this, the losing party may object to the jurisdiction of the arbitral tribunal on the basis that the pre-conditions to arbitration have not been fulfilled (…)".

and that:

> "Although a second set of DAB proceedings may appear to be pointless, this is, the author suggests, the result of a lacuna in the drafting of sub-clause 20.7 of the 1999 FIDIC Books."

The author also indicated in the same article that this lacuna or shortcoming in the drafting of sub-clause 20.7 had now been addressed in the 2008 Gold Book, by making clear in its sub-clause 20.9 that a party may refer directly to arbitration the other party's failure to comply with any decision of the DAB "whether binding or "final and binding".

Without an amendment of sub-clause 20.7 to that effect (which the 2013 FIDIC Guidance recommends[36]), a second referral to the DAB is admittedly a necessary evil[37].

The effect of that second referral should not however be exaggerated. This referral is relatively easy to prepare, since the successful party would only need to ask the DAB to find that the other party failed to give effect to the earlier DAB decision and to order that recalcitrant party to pay immediately the amount awarded by the DAB in that earlier decision plus any interest due on that sum. The author submits that, from his experience, the DAB is likely to deal with such a referral on a document only basis (therefore limiting any legal costs involved) and to render its decision before 84 days.

[35] Frédéric Gillion, "Enforcement of DAB decisions under the 1999 FIDIC Conditions of Contract – a recent development: *CRW Joint Operation (Indonesia) v PT Perusahaan Gas Negara (Persero) TBK*" [2011] ICLR 401–402.

[36] By replacing sub-clause 20.7 in its entirety with: "In the event that a Party fails to comply with any decision of the DAB, whether binding or final and binding, then the other Party may, without prejudice to any other rights it may have, refer the failure itself to arbitration under sub-clause 20.6 [Arbitration] for summary or other expedited relief, as may be appropriate. Sub-clause 20.4 [Obtaining Dispute Adjudication Board's Decision] and sub-clause 20.5 [Amicable Settlement] shall not apply to this reference."

[37] It is worth mentioning that two recent court decisions in Switzerland (Swiss Federal Supreme Court Case dated 7 July 2014 (4A 124/2014) and in England (*Peterborough City Council v Enterprise Managed Services Ltd* [2014] EWHC 3193 (TCC); [2014] BLR 735) have confirmed the mandatory nature of the reference to the DAB prior to referring a dispute to arbitration (or courts in the English case).

The 2014 High Court's conclusion that: "[t]his delay upon delay is directly opposed to the intent of any security of payment regime to give the contractor a quick means of compelling the employer to 'pay now'"[38] is therefore totally misguided and denotes a misunderstanding as to how the enforcement of DAB decisions currently works in practice under the 1999 Suite of FIDIC Contracts.

The same misunderstanding is apparent from the 2014 High Court's suggestion that "a contractor who attempts to pursue, as a separate dispute, a secondary dispute which arises from a non-final DAB decision finds itself enmeshed in an infinite recursive loop"[39], on the basis that: "[t]he result of adopting the two-dispute approach (…) is to compel the contractor to secure an infinite series of DAB decisions, each of which is not complied with, but none of which gets the contractor any closer actually to commencing an arbitration to compel the employer to 'pay now'."[40]

Mr Seppälä quotes that passage of the 2014 High Court decision in his article but unfortunately does not provide his understanding of what the 2014 High Court actually meant by that.

There is *no* "infinite recursive loop". Once the winning party has obtained its second DAB decision in respect of the other party's failure to comply with the earlier DAB decision, it can then refer that narrow dispute to arbitration (provided of course that the pre-requisites for arbitration set forth in sub-clauses 20.4 and 20.5 have been satisfied) and seek an award for the amount awarded by the DAB and interest.

As the author recognised elsewhere,[41] such reference is unlikely to result in a simple arbitration (if any arbitration proceedings could ever be simple). This is because in practice, when faced with a claim for the immediate payment of the sum awarded by the DAB, the losing party will most certainly seek to broaden the scope of the arbitration by filing a counterclaim asking the arbitral tribunal to decide the merits of the original dispute and/or to open up, review and revise the first DAB decision.

Even if the losing party does so, it remains advantageous for the winning party to refer only that secondary dispute to arbitration. This is because:

(a) The winning party will be able to refer quickly to arbitration its claim for immediate payment of the sum awarded by the DAB without having to spend significant time and money to prove once more its entitlement to receive payment of the amount awarded to it in the initial DAB decision;

[38] 2014 High Court decision, paragraph 45.
[39] 2014 High Court decision, paragraph 46.
[40] 2014 High Court decision, paragraph 47.
[41] Frédéric Gillion, "Enforcement of DAB decisions under the 1999 FIDIC Conditions of Contract – a recent development: *CRW Joint Operation (Indonesia) v PT Perusahaan Gas Negara (Persero) TBK*" [2011] ICLR 403–404.

(b) It reverses the parties' role in the arbitration in relation to the underlying dispute which was the subject of the first DAB decision. The losing party, by bringing its counterclaim, will have to establish that the first DAB decision was incorrect and that the winning party was not entitled to the money awarded by the DAB; and

(c) An arbitral tribunal may be more inclined to make an interim or partial award in respect of the winning party's claim at an early stage of the arbitration proceedings if it becomes clear that a long time will be required for the losing party to establish its case regarding the merits of the DAB decision. Any such award, provided of course that it is not ignored by the losing party, would put the winning party in a favourable financial position and also a strong bargaining position in any amicable settlement discussions.

This two-dispute approach is therefore, the author submits, entirely consistent with the "pay now, argue later" principle and best advances the FIDIC's security of payment regime.

Does the 2014 High Court's second "subsidiary question" affect that conclusion?

When the contractor seeks merely to resolve the *secondary* dispute, what limits are there, if any, on the power of the tribunal to open up the DAB decision under clause 20.6[2] and on the liberty of the parties to attack the DAB decision under clause 20.6[3]?[42]

What lies behind that second "subsidiary question" appears to be the situation in which PGN found itself during the 2009 arbitration when it asked the Tribunal in its Answer to CRW's Request for Arbitration "to open up, review and revise the [Adjudicator's] decision", pursuant to sub-clause 20.6, but the 2009 Tribunal declined to do so on the basis that PGN had not filed a counterclaim.

The 2014 High Court considered that in that situation or in a situation where the employer does not even invite the tribunal to inquire into the primary dispute, there is a risk that, under the Singapore law of the "doctrine of abuse of process" (or "extended doctrine *of res judicata*"), that the employer might be precluded from "arguing later" about the merits

[42] The second and third paragraphs of sub-clause 20.6 provide as follows:

"The arbitrator(s) shall have full power to open up, review and revise any certificate, determination, instruction, opinion or valuation of the Engineer, and any decision of the DAB, relevant to the dispute. Nothing shall disqualify the Engineer from being called as a witness and giving evidence before the arbitrator(s) on any matter whatsoever relevant to the dispute.

Neither Party shall be limited in the proceedings before the arbitrator(s) to the evidence or arguments previously put before the DAB to obtain its decision, or to the reasons for dissatisfaction given in its notice of dissatisfaction. Any decision of the DAB shall be admissible in evidence in the arbitration."

of the primary dispute[43]. The 2014 High Court then suggested that the employer's right to argue later was, as a result, "illusory" given that "[f]or all practical purposes, the employer *must* raise the primary dispute as a cross-claim or counterclaim in that arbitration and the tribunal *must* permit it to do so. Otherwise, the contractor can successfully submit that the employer is precluded from "arguing later".

The author is not qualified to comment upon the laws of Singapore, but it seems that there would be no res judicata in a situation where all that the tribunal determines is the contractor's entitlement to be paid an amount awarded by the DAB. This would not make the DAB decision somehow final and binding. The employer should therefore still in principle be entitled to argue later about the merits of the underlying dispute even though an award has been rendered in respect of the employer's failure to pay the amount awarded by the DAB. In any event, in practice, the employer will raise a counterclaim by asking the arbitral tribunal to decide the merits of the primary dispute and/or to open up, review and revise the first DAB decision, and the tribunal will also in all likelihood permit it to do so. The 2014 High Court's concern therefore seems to be a non-issue, or at best a remote risk which would not justify in itself the adoption of the "one-dispute" approach recommended by the 2014 High Court for the enforcement of DAB decisions.

7. WHY THE "ONE-DISPUTE" APPROACH IS AN UNDESIRABLE APPROACH FOR A SECURITY OF PAYMENT REGIME

The one-dispute approach (namely a referral by the contractor to arbitration at the same time of both the secondary dispute and the underlying merits of the primary dispute) suffers from major disadvantages which make it an undesirable approach for a security of payment regime.

A first disadvantage was touched upon by the author in a previous article in relation to *Persero I*[44] which stated the following:

> "The main problem with Option 4 [the 'one-dispute' approach in *Persero II*] is the fact that the arbitration will inevitably focus more on the merits of the underlying dispute which was the subject of the first DAB decision than the fact that the DAB decision has been ignored by the losing party.
>
> In practice, unless the arbitral tribunal orders a bifurcation of the winning party's claims at the outset, all of its claims will be pleaded at the same time and the first opportunity which the winning party may have to request a partial award in respect of the losing party's failure to comply with the DAB decision is likely to be many months after the filing of its request for arbitration.
>
> Considerations such as 'lack of urgency' may then be raised by the losing party to resist the making of a partial award ahead of the hearing of the underlying dispute,

[43] 2014 High Court decision, paragraphs 53(a) and 54.

[44] Frédéric Gillion, "Enforcement of DAB decisions under the 1999 FIDIC Conditions of Contract – a recent development: *CRW Joint Operation (Indonesia) v PT Perusahaan Gas Negara (Persero) TBK*" [2011] ICLR 405.

> especially if that hearing is only months away. The losing party may also argue that the winning party will in any event be adequately compensated by an award of interest on the sums awarded by the DAB. Why can't the winning party then wait a few more months for the final hearing and a final award on the underlying dispute?"

Second and more fundamentally, as mentioned earlier in this paper, the one-dispute approach forces the contractor who may be satisfied with the DAB decision to take the onerous and time-consuming step of bringing an arbitration on the merits of the underlying dispute, when ultimately all that party wants is to obtain a prompt payment of the sums awarded by the DAB. This is a major disadvantage which is completely downplayed by the 2014 High Court as follows:

> "The one-dispute approach carries only one disadvantage to set against all of these advantages. It forces a contractor who holds a non-final DAB decision to take the initiative in putting the primary dispute before the tribunal even though it typically has no interest in resolving it. But this is a minor disadvantage. If the contractor secures an interim award in its favour on the secondary dispute, it will cease to be a claimant in all but name. The carriage of the remainder of the arbitration will inevitably shift to the employer. This disadvantage is a minor anomaly compared to the substantive and substantial drawbacks of adopting the two-dispute approach."[45]

Mr Seppälä does not go quite as far as this: whilst he recognises that "requiring the merits to be submitted to the same arbitration is less than ideal", he is of the view that "this should not necessarily be a major inconvenience".

The reality is that, on a typical construction dispute which involves issues relating to measured works, variations, and extensions of time, having to bring to arbitration those issues with the necessary witness and expert evidence (assuming this is submitted with the contractor's brief/memorial, as it is now often required by tribunals) is likely to take months and cost a significant amount of money. This is directly inconsistent with the primary purpose of a security of payment regime as explained above. The author also does not consider that the contractor will somehow after the issue of an interim award during the course of the proceedings cease to be a claimant in all but name. The burden of proving the contractor's entitlement will remain with it as a claimant in the arbitration.

Thirdly, the one-dispute approach proceeds on the basis that the employer's failure to comply with a DAB decision in breach of sub-clause 20.4 is "simply another aspect"[46] of the primary dispute and that accordingly "[t]hat breach and the secondary dispute it gives rise to, is not a separate 'dispute'"[47]. The 2014 High Court is therefore of the view that "there is no need to refer the secondary dispute to the DAB for decision before arbitrating it under clause 20.6". Although this may be right in theory, a winning party would be ill-advised to adopt this approach in the author's view. This is because,

[45] 2014 High Court decision, paragraph 75.
[46] 2014 High Court decision, paragraph 60.
[47] 2014 High Court decision, paragraph 60.

given the current wording of sub-clause 20.7 – which, as recognised by the 2014 High Court itself, "adopts and endorses the two-dispute approach and is wholly inconsistent with the one-dispute approach"[48] – the recalcitrant party is likely to raise jurisdictional objections, precisely on the basis that the secondary dispute is a separate dispute that should have been referred to the DAB for a decision. That recalcitrant party is likely to rely on the wording of sub-clause 20.7, but also the explicit intentions of the FIDIC which the 2014 High Court has completely ignored in its decision.

And this is the final point. By seeking to conceptualise the security for payment regime with this one/two-dispute approach, the 2014 High Court ended up completely ignoring the intentions of FIDIC in relation to the enforcement of the DAB decisions, in particular:

(a) The implications of sub-clause 20.7 of the 1999 Red Book, as recognised by the 2014 High Court itself:[49]

> "I am therefore driven to the conclusion that the only way to make the Red Book's security of payment regime workable, at least for non-final DAB decisions, is to ignore the implications of clause 20.7. That solution, although undoubtedly unsatisfactory, removes the most significant obstacle to adopting the one-dispute approach, which is clause 20.7's adoption of the two-dispute approach."

(b) Sub-clause 20.9 of the 2008 Gold Book which provides that:

> "In the event that a Party fails to comply with any decision of the DAB, whether binding or final and binding, then the other Party may, without prejudice to any other rights it may have, refer the failure itself to arbitration under sub-clause 20.8 [Arbitration] for summary or other expedited relied, as may be appropriate …"

and

(c) The 2013 FIDIC Guidance[50].

Admittedly, unlike the 2014 High Court, Mr Seppälä does refer to the "clarifying change" introduced by the 2008 Gold Book and also to the 2013 FIDIC Guidance,[51] but without acknowledging that the one-dispute approach developed by the 2014 High Court is completely contradicted by the explicit intentions of FIDIC in relation to the enforcement of the DAB decisions that are binding and not yet final.

The intentions of FIDIC in this regard are clearly set out in its Guidance of April 2013 and are beyond any doubt in support of the two-dispute approach:

> "in the case of failure to comply with these [DAB] decisions, the failure itself should be capable of being referred to arbitration under sub-clause 20.6 [Arbitration],

[48] 2014 High Court decision, paragraph 64.

[49] 2014 High Court decision, paragraph 70.

[50] FIDIC Guidance Memorandum for Users of the 1999 Conditions of Contract dated 1st April 2013 "designed to make explicit the intentions of FIDIC in relation to the enforcement of the DAB decisions that are binding and not yet final".

[51] Christopher Seppälä, "Singapore contributes to a better understanding of the FIDIC Disputes Clause: the second *Persero* case" [2014] ICLR 4.

> without sub-clause 20.4 [Obtaining Dispute Adjudication Board's Decision] and sub-clause 20.5 [Amicable Settlement] being applicable to the reference. This intention has been made manifest in the FIDIC Conditions of Contract for Design, Build and Operate Projects, 2008 ('Gold Book') by the equivalent sub-clause 20.9."

8. CONCLUSION

The current drafting of sub-clause 20.4 to 20.7 undoubtedly lacks clarity in respect of the way binding but not final DAB decisions should be enforced.

It is therefore encouraging to see the Singapore High Court promoting the principle of "pay now: argue later" in the context of binding but not final DAB decisions and upholding an arbitral award which orders the employer to pay amounts awarded by the DAB without a final determination of the underlying dispute.

The problem is that in doing so, the 2014 High Court sought to come up with a simple approach that would avoid having a second referral specifically on the failure of the recalcitrant party to comply with the DAB decision. That "simple approach" – the one-dispute approach – is in fact a far more complex and onerous approach for the contractor as it forces the contractor "to take the initiative in putting the primary dispute before the tribunal even though it typically has no interest in resolving it"[52].

That one-dispute approach is directly inconsistent with the FIDIC's explicit intentions in relation to the enforcement of the DAB decisions, but also, importantly, contradicts the primary purpose of the FIDIC's security of payment regime, which is for the employer to "pay now and argue later".

The author submits that the two-dispute approach, although not ideal with this second referral to the DAB, best advances the "pay now" features of this security of payment scheme whilst not compromising the employer's ability to "argue later" over the primary dispute whether in the same arbitration by raising a counterclaim or in a separate arbitration.

[52] 2014 High Court decision, paragraph 75.