

Arbitration clauses – an overriding promise?

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Introduction

The existence of arbitration clauses in construction contracts is not uncommon. In the construction industry, the Malaysian Institute of Architects (PAM) form contract is widely used.

This article examines the impact of the Federal Court's recent decision in *Tindak Murni Sdn Bhd v Juang Setia Sdn Bhd* ([2020] MLJU 232), in which it had to decide whether an arbitration clause or a judgment in default which had already been obtained despite the existence of the arbitration clause took precedence.

Facts

Tindak Murni Sdn Bhd (the employer) entered into a building construction contract with Juang Setia Sdn Bhd (the contractor) for the construction of the remaining portions of a main access road, earthworks and infrastructure works. The underlying contract was a standard PAM form contract.

The architect issued a certificate of practical completion regarding the works. The contractor then initiated a civil suit against the employer over unpaid sums under several certificates of payment. This was done despite the clear and unambiguous arbitration clause in Clause 34 of the contract. The employer failed to appear within the requisite time period and the contractor consequently obtained a judgment in default of appearance (JID) on 1 March 2017.

The employer filed an application to set aside the JID based on disputes against the contractor's claim and the existence of the arbitration clause. The high court registrar was satisfied that "there was a defence on the merits in that there were disputes and/or triable issues justifying matter being heard on its merit" and thus allowed the JID to be set aside.

High court decision

Dissatisfied, the contractor appealed the decision of the high court registrar. The employer simultaneously filed an application for a stay of proceeding pending arbitration pursuant to Section 10 of the Arbitration Act 2005. The high court judge heard both the appeal and the application and held that the setting-aside order ought to stand because there was a defence on the merits. In addition, the high court judge found that there was a valid arbitration clause by which the parties had agreed to be bound. Therefore, pursuant to Section 10 of the Arbitration Act, a stay pending arbitration should be granted.

Court of Appeal decision

The contractor filed two appeals to the Court of Appeal in respect of the high court judge's decision to:

- uphold the setting aside of the JID; and
- allow the stay of proceedings pending arbitration.

The Court of Appeal first dealt with the first appeal and ruled that the high court judge's decision in this respect was wrong. In reaching this conclusion, the Court of Appeal approached the issue from a substantive law perspective (ie, that certificates of payment are final and conclusive in nature). As such, the Court of Appeal concluded that the JID was regular and consequently allowed both of the

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contractor's appeals.

Federal Court decision

The Federal Court found that pursuant to Section 10 of the Arbitration Act, the appeal regarding the stay warranted consideration ahead of the appeal regarding the JID.

Section 10 of the Arbitration Act reads as follows:

*A court **before which proceedings are brought in respect of a matter which is the subject of an arbitration agreement** shall, where a party makes an application before taking any other steps in the proceedings, stay those proceedings and refer the parties to arbitration unless it finds that the agreement is null and void, inoperative or incapable of being performed.* (Emphasis added.)

The Federal Court found as follows:

- Section 10 applies even when a JID has been obtained.
- The commencement of the civil suit by the contractor amounted to a breach of the arbitration clause. In this regard, unless and until such a breach is accepted by the employer, the contract remains valid.
- If the JID were allowed to stand, it would in effect undermine the parties' intentions when entering into the contract.
- The appeal regarding the stay was in substance a jurisdictional point which the court was bound to consider. This dictates that the form and substance, as well as the significance, of both appeals had to be considered in their totality. The Court of Appeal had failed to appreciate that these two appeals were "inextricably intertwined".

In its attempt to convince the Federal Court, the contractor, citing the relevant case law, submitted that its claim, which had arisen from certificates of payment, was beyond dispute and that there was thus no dispute which warranted referral to arbitration.

The Federal Court held that this argument could not stand. Under Section 10 of the Arbitration Act, there was no question of the court venturing into the realm of whether a dispute existed between the parties. The court's role is simply as set out in Section 10. A dispute is for the consideration and determination of the arbitral tribunal.

The Federal Court based its argument on the removal of Subsection (b) during the amendment to Section 10. Prior to its amendment, Section 10 read as follows:

(1) The court before which proceedings brought in respect of a matter which is the subject matter of an Arbitration Agreement shall, where party makes an application before taking any other step in the proceedings, stay those proceedings and refer the parties to arbitration unless it finds:-

*(a) That the agreement is null and void, inoperative or incapable of being performed;
or*

(b) That there is in fact no dispute between the parties with regard to the matters to be referred.

As such, the removal of Subsection (b) clearly signifies that the days where the courts could delve into whether a dispute exists are long gone.

In light of the above, the Federal Court ordered the Court of Appeal's order to be set aside and reinstated that of the high court judge.

Comment

The Federal Court's decision aligns with other appellate court decisions on Section 10 of the Arbitration Act, such as *TNB Fuel Services Sdn Bhd v China National Coal Group Corp* ([2013] 4 MLJ 857) and *Press Metal Sarawak Sdn Bhd v Etiqa Takaful Bhd* ([2016] 5 MLJ 417). Together, these decisions show that the courts will not review whether a dispute exists between parties, regardless of whether a judgment in default has been obtained, as illustrated by this case.

The upshot of the Federal Court's decision is that where parties have agreed to arbitrate, they will be bound by their agreement.

Evidently, the Malaysian courts recognise the importance of upholding the sanctity and freedom of contract and recognise such principles as a cardinal pillar of contract law. In a nutshell, a valid arbitration clause is an overriding promise.

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