

The Gap in Sub-Clause 20.7 of
The 1999 FIDIC Contracts for Major Works

by

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Introduction

Christopher Seppälä has always written and had published extremely useful articles on the FIDIC Contracts and his most recent article published by ICLR,¹ is no exception. The article dealt with and explained the complex and difficult provisions of the arbitration clause in the 1999 FIDIC contracts for major works. Mr. Seppälä also explained the thinking behind the various Sub-Clauses of Clause 20 of these contracts and as the Editors in Chief of ICLR mentioned in their Introduction, he identified many points which have to be borne in mind by the parties when operating that clause. Mr. Seppälä's articles are also thought provoking and prompt the reader to consider many practical aspects for the practicing engineer within the context of the topic.

This latest article prompts me to consider the gap that exists in the present Sub-Clause 20.7 of these contracts and the practical problems that might arise as a result, from the point of view of the practising engineer and perhaps the arbitrator who would have to resolve the consequent dispute. The gap I am referring to is that created when a DAB's decision has not become final & binding (i.e. where one of the Parties is dissatisfied with the decision), and the Party against whom the decision was made fails to comply with it. In such circumstances, there is no solution offered within Clause 20 other than simply treating the non-compliant party as being in breach of contract. However, as the remedy for such breach is damages that might be imposed at some future date, it is of little value in the immediate term and is in violation of the requirement in Sub-Clause 20.4 that the parties shall "*promptly give effect*" to the DAB's decision itself.² In this article, I attempt to highlight the extent of this gap and the hidden problems within Clause 20 in that connection.

A. The Gap in Clause 20

¹ Christopher R. Seppälä, "The Arbitration Clause in FIDIC Contracts for Major Works", ICLR Vol. 22, Part 1, January 2005.

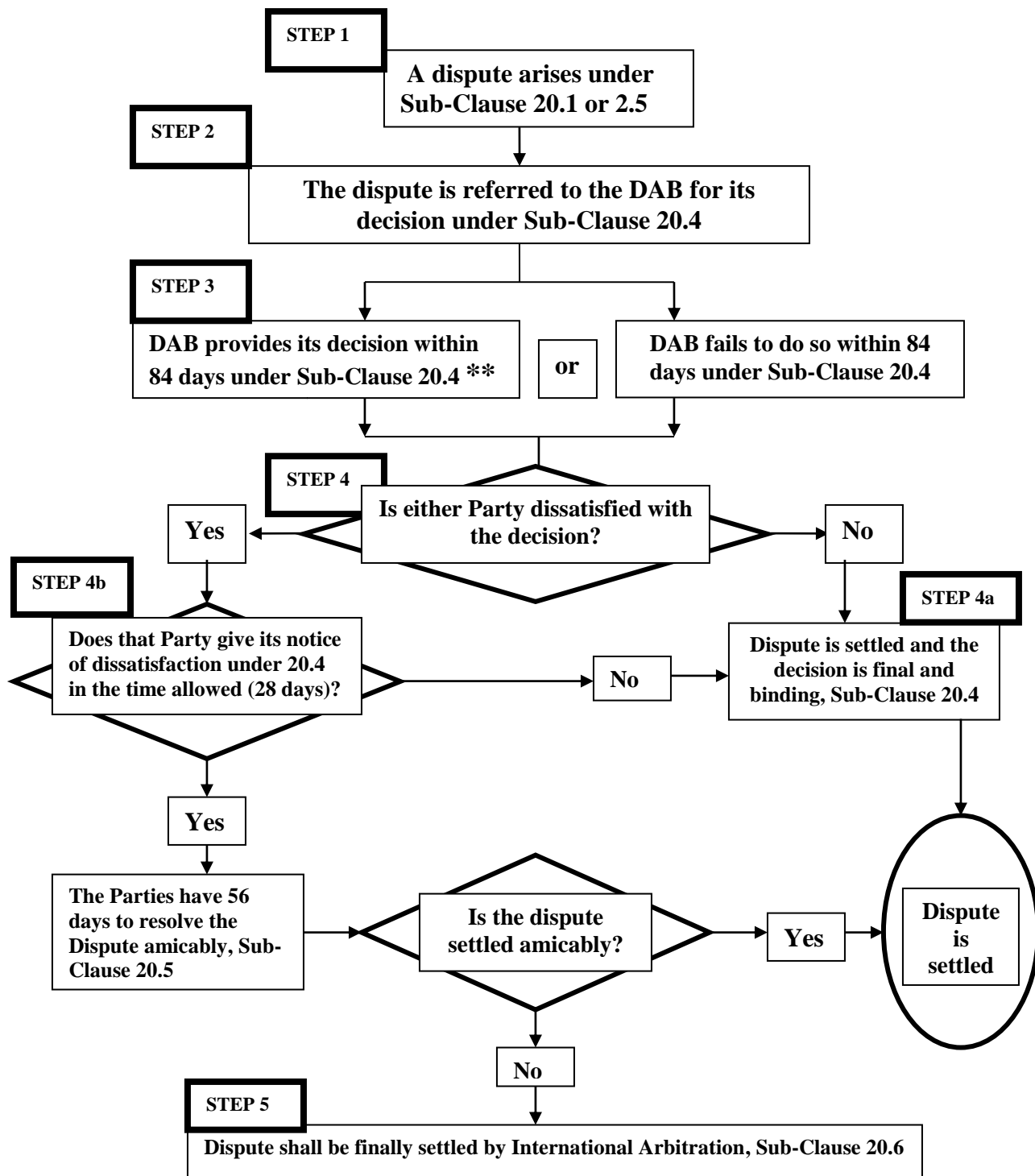
² The quoted words are taken from the fourth paragraph of Sub-Clause 20.4.

In order to understand how this gap could arise when Clause 20 is applied in practice, one has to start from the beginning of the procedure for dispute resolution as set out in that clause. Due to the fact that the dispute resolution procedure contained in Clause 20 of the 1999 FIDIC contracts for major works is a difficult and complex one, it is easier explained and better understood by using flow charts. Figure No. 1 shows the procedure itself and Figure No. 2 illustrates the compliance requirements contained in the fourth paragraph of Sub-Clause 20.4, which form the subject of this article. As can be seen from Figure No. 1, essentially, the procedure comprises only five steps that can be summarised as follows:³

1. Step 1: A dispute arises.
2. Step 2: The dispute is referred to the DAB in writing for its decision, under Sub-Clause 20.4.
3. Step 3: The DAB gives notice of its decision within 84 days or it fails to give a decision within that period.
4. Step 4: The Parties react to the decision of the DAB, which could be one of two possibilities:
 - (a) Both Parties are satisfied with that decision, the dispute is resolved and such decision becomes final and binding; or
 - (b) At least one of the Parties is dissatisfied with the decision of the DAB, or with its lack of decision, and thus notifies the other Party of its dissatisfaction within 28 days.⁴ In this case, the Parties are given 56 days to attempt resolving their dispute by amicable settlement, under Sub-Clause 20.5. If the attempt is successful, the dispute is resolved. If not, step 5 applies.
5. Step 5: If the attempt to amicably resolve the dispute fails, such dispute is to be finally settled by international arbitration, under Sub-Clause 20.6.

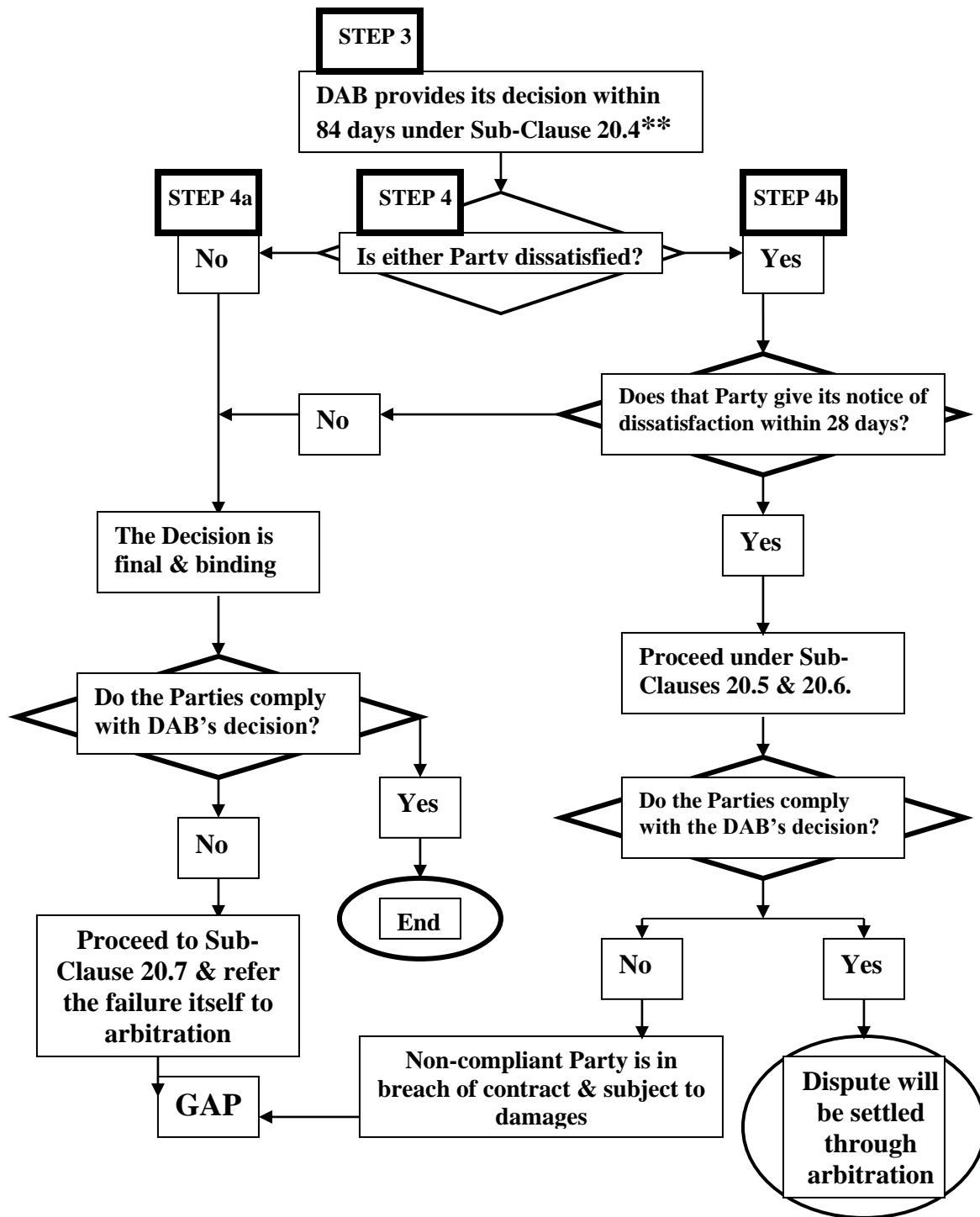
³ In his above-mentioned article, Mr. Seppälä divides the process into six steps. However, his steps 4 and 5 form in essence the two possible responses of the Parties to the decision of the DAB and only one response could apply, but not both. Therefore, these two steps are in reality two prongs of a single step.

⁴ If the notice of dissatisfaction is not given within the required 28 days, the decision of the DAB will become final and binding and the provisions relating to Step 4(a) will apply.



** The decision shall be binding on both Parties, who shall promptly give effect to it unless and until it shall be revised in an amicable settlement or an arbitral award, see 4th paragraph of Sub-Clause 20.4.

Figure No. 1. Dispute Resolution Procedure under Clause 20



** The decision shall be binding on both Parties, who shall promptly give effect to it unless and until it shall be revised in an amicable settlement or an arbitral award, see 4th paragraph of Sub-Clause 20.4.

Figure No. 2. Compliance with the Decision of the DAB under the 1999 FIDIC Major Contracts

It is important to note that irrespective of whether the dispute is resolved through steps 4(a) or 4(b), the decision of the DAB becomes binding on the Parties pursuant to the terms of Sub-Clause 20.4, which provides in its fourth paragraph the following wording: ***“The decision shall be binding on both Parties, who shall promptly give effect to it unless and until it shall be revised in an amicable settlement or an arbitral award as described below. ...”***

The effect of this provision on the decision of the DAB is known technically as a *“temporarily final & binding”* effect. The decision must be complied with by both parties, which is a characteristic feature of the FIDIC DAB procedure distinguishing it from the DRB procedure under other forms of contract. The decision becomes, in effect, a contractual obligation on both Parties such that non-compliance with it by either of them is a breach of contract and the Party in breach would be liable in damages. However, such liability for damages on its own is:

1. Insufficient to ensure that the decision of the DAB is complied with ***“promptly”***, since
 - (a) The dissatisfied party might feel so strongly against the decision that it might ignore it and continue its work, or the position it had adopted, in breach of the DAB’s decision, taking on board the risk that in the end, at some future date, it might be vindicated and found not to be liable in damages;
 - (b) The dissatisfied party might simply keep silent and not respond;
2. Unlikely to be an appropriate remedy in the circumstances of a dispute, since the dispute might require instantaneous attention such as the case where the DAB’s decision is in connection with allegations of defective design, material or workmanship under Sub-Clause 15.1;⁵ and
3. Not decisive enough to ensure the smooth running of a project or a contract to proper completion, since additional investigation, instruction or drawing might be quickly required.

Sub-Clause 20.7, in its present wording quoted below, resolves this problem in the event that a DAB’s decision is not complied with, but unfortunately it only deals with the situation when the decision of the DAB has become final and binding. Accordingly, as can be seen from Figure No. 2 above, the compliance by the Parties with the decision of the DAB where the decision has not become final and binding, i.e. where one of the Parties is dissatisfied with the decision, remains without a prompt and decisive mechanism to enforce it promptly. For completeness sake, the present wording of Sub-Clause 20.7 is as follows:

⁵ Failure to comply with a Notice to Correct under Sub-Clause 15.1 entitles the Employer to terminate the Contract under Sub-Clause 15.2 with all of its serious consequences.

“20.7 Failure to Comply with Dispute Adjudication Board’s Decision

In the event that:

- (a) neither Party has given notice of dissatisfaction within the period stated in Sub-Clause 20.4 [Obtaining Dispute Adjudication Board’s Decision],***
- (b) the DAB’s related decision (if any) has become final and binding, and***
- (c) a Party fails to comply with this decision,***

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]. Sub-Clause 20.4 [Obtaining Dispute Adjudication Board’s Decision] and Sub-Clause 20.5 [Amicable Settlement] shall not apply to this reference.”

The provisions that describe the situation where one Party is dissatisfied with the DAB’s decision are contained in the fifth and sixth paragraphs of Sub-Clause 20.4. They provide that the dissatisfied Party must give a notice to this effect to the other Party within 28 days of the DAB’s decision. These two paragraphs also provide that, except as stated elsewhere (Sub-Clauses 20.7 and 20.8), neither Party shall be entitled to proceed to arbitration of the dispute unless such notice of dissatisfaction has been given.

B. The Effect of the Compliance Requirements under Sub-Clause 20.4

There are three consequences to a properly given decision by the DAB under Sub-Clause 20.4 of the 1999 FIDIC contracts for major works. These are as follows:

1. The decision of the DAB affects the Parties’ rights and obligations and as such it is binding on the Parties who are required to ***“promptly give effect to it unless and until it shall be revised in an amicable settlement or an arbitral award”***, as described in Sub-Clauses 20.5 and 20.6 of the contract conditions.
2. Sub-clause 20.4 also stipulates that ***“If the DAB has given its decision and no notice of dissatisfaction has been given by either Party within 28 days after it received the DAB’s***

decision, then the decision shall become final and binding upon both Parties". (emphasis added.)

3. However, if a notice of dissatisfaction is given by either Party within 28 days after receiving the decision, setting out the matter in dispute and the reason(s) for dissatisfaction, then both Parties are required to attempt to settle their dispute amicably, as stipulated under Sub-Clause 20.5, before commencement of arbitration. Furthermore, as set out in Sub-Clause 20.6, unless settled amicably, any dispute in respect of which the DAB's decision has not become final and binding may be finally settled by international arbitration.

As a result of the first consequence, Sub-Clause 20.7 deals with the possibility of non-compliance with the DAB's decision. However, although the clear intention of Sub-Clause 20.4 is that the DAB's decision should be complied with promptly, unless and until it is revised in a subsequent forum (amicable settlement or arbitration), and irrespective of whether or not one of the Parties is dissatisfied with it, Sub-Clause 20.7 is worded in such a way that it only deals with the event where the Parties are satisfied with the decision. The draftsmen did not deal with circumstances where the parties are dissatisfied with the decision, leaving that situation without any prompt solution or elucidation, hence creating a gap. In doing so, it should be noted that this gap survives from the 1987 Red Book, 4th edition, as explained below.

C. The Gap has survived from the 1987 Red Book

The origin of this problem or this gap, as described above, goes back to Sub-Clause 67.4 of the 1987 Red Book, the Fourth Edition. Sub-Clause 67.4 was a new provision of the Fourth Edition at the time.⁶ It provided that failure of a party to comply with an Engineer's decision which had become final and binding under Clause 67 may itself be referred to arbitration. Such reference to arbitration was made directly under the provisions of Sub-Clause 67.3 and accordingly, a party's failure to comply with a final and binding decision of the Engineer need not first be referred either to the decision of the Engineer, or to an amicable settlement, under Sub-Clause 67.2.

⁶ See Section 19.8.1 of "The FIDIC Forms of Contract", Third Edition, Blackwell Publishing Limited, but expected to be published in April 2005.

However, there was a precondition placed on this right to refer the failure to comply with the Engineer's decision to arbitration: Sub-Clause 67.4 starts with the words *“Where neither the Employer nor the Contractor has given notice of intention to commence arbitration within the period stated in Sub-Clause 67.1 and the related decision has become final and binding, either party may ...”*. Further, Sub-Clause 67.1 unambiguously required the parties to comply with the Engineer's decision: *“... unless and until same shall be revised, as hereinafter provided, in an amicable settlement or an arbitral award”*.

So what of the scenario where a notice of intention to commence arbitration had been served, but it is too soon to have had an arbitral award, and one party is not complying with the Engineer's decision?

It would appear that the injured party in this scenario would have no right to refer such non-compliance to arbitration for enforcement of the Engineer's decision. While an arbitration may already have been commenced by virtue of the notice served, it will be based on the merits of the Engineer's decision which may take some time to determine, rather than the failure to comply with the decision which requires the arbitrator in that case to merely examine the Engineer's decision and to be satisfied that there has been a failure to comply with it. If, for example, the Engineer's decision involves a large sum of money to be paid to the contractor who is experiencing financial difficulties, then the employer's failure to make such payment promptly might mean the difference between the contractor on the one hand being able to afford to continue in the arbitration; and on the other hand being under such economic pressure that he is forced to concede to the employer.

Such a possibility cannot be acceptable in a standard form of contract. It is suggested here that the right to refer failure to comply with the Engineer's decision should be available regardless of whether a notice of intention to commence arbitration has been served and regardless of whether the Engineer's decision has become final and binding. In this way, the Engineer's decision can be confirmed through an arbitration which, if international, could then be enforced by virtue of any international convention on enforcement of foreign arbitral awards which might be applicable.

This gap under the 1987 Red Book did not cause major problems because the Engineer under that form of contract was required to act in the dual role of an agent of the employer and also as an independent and impartial decision maker. The Engineer could therefore correct an inappropriate situation through his intervention. No such action by the DAB is possible.

Therefore, in the 1999 FIDIC contracts for major works, the problem is aggravated and cannot be left without a prompt and decisive mechanism for its resolution.

**D. Is the referral to arbitration
an appeal from the DAB's decision or a new case?**

Before attempting to find a solution to this gap in Clause 20, it is appropriate to discuss the question of whether the referral to arbitration under Sub-Clauses 20.6 to 20.8 by a dissatisfied party is an appeal from the decision of the DAB or is it a totally new process initiated by that party to resolve the whole dispute from beginning to end. If it is the latter, the decision of the DAB is simply a matter of record and historical value and the appointed arbitral tribunal is expected to deal with the dispute in its entirety, including any claims and counterclaims and in the words of Article 18.1 of the ICC Rules of Arbitration *“in the light of their most recent submissions”*.⁷ If it is the former, the decision of the DAB has to be considered by the arbitral tribunal and analysed to establish whether or not it is correct in the circumstances of the case.

To answer the question posed above, one has to look to the individual wording of each of the three Sub-Clauses referred to above for guidance and assistance.

Starting with Sub-Clause 20.6, quoted below, we have in its 3rd paragraph a revealing wording in this connection. It provides that *“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, ...”*. Therefore, if the Parties could make new submissions before the arbitral tribunal, the case that would be presented to the arbitrators could essentially be a totally different case to that which had been examined by the DAB. Furthermore, whilst the second paragraph of Sub-Clause 20.6 permits the Engineer to be called as a witness and to give evidence before the arbitral tribunal, there is no mention of such possibility being afforded to the members of the DAB.

⁷ In a provocative address given by His Honour Judge Humphrey LLOYD at a conference organised by ICC and FIDIC in association with the Cairo Regional Centre for International Commercial Arbitration in Cairo on 9th and 10th April 2005, he asked the above-mentioned question and debated the two alternatives.

“20.6 Arbitration

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. Unless otherwise agreed by both Parties:

- (a) the dispute shall be finally settled under the Rules of Arbitration of the International Chamber of Commerce,***
- (b) the dispute shall be settled by three arbitrators appointed in accordance with these Rules, and***
- (c) the arbitration shall be conducted in the language for communications defined in Sub-Clause 1.4 [Law and Language].***

The arbitrator(s) shall have full power to open up, review and revise any certificate, determination, instruction, opinion or valuation of the Engineer, and also 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.

Arbitration may be commenced prior to or after completion of the Works. The obligations of the Parties, the Engineer and the DAB shall not be altered by reason of the arbitration being conducted during the progress of the Works.”

It is therefore suggested here that Sub-Clause 20.6 is not intended to be an appeal but a fresh submission that would lead to a new case and that the role of the arbitral tribunal is not an appellate role but a distinct role for a new case. Of course, the dissatisfied party could be either a loser in the DAB's decision or a winner having been successful to a lesser degree than it sought in its claim. In both cases, the dissatisfied party would be the party requiring a new trial of the

case, but in the meantime, compliance with the decision of the DAB, as provided for under Sub-Clause 20.4, should be implemented.

Turning now to Sub-Clause 20.7, we find that the wording is once again clear, but with a different intention. Its opening words, quoted above, clearly establish that the purpose of the Sub-Clause is to deal with *“the failure itself”* to comply with the decision of the DAB. Therefore, it is suggested here that Sub-Clause 20.7 represents a special form of appeal to an arbitral tribunal seeking to confirm through an arbitral award the requirement of compliance, as neither party had declared its dissatisfaction within the stipulated time of 28 days. Of course, an arbitral award has a better chance of enforcement than a DAB’s decision.

Sub-Clause 20.8 deals with the situation where there is no DAB in place and, therefore, it is outside the topic of this paper.

E. Two Suggested Solutions to the Problem of the Gap

If it is accepted that this gap in the 1999 FIDIC contracts for major works should be eliminated, then it is suggested that the solution to the problem could be one of two possibilities:

- (a) First, by implementing a number of changes to certain provisions of the contract to ensure that the DAB’s decision is *“promptly”* given effect to by utilising sanctions under Sub-Clause 15.2, *“Termination by Employer”*; Sub-Clause 16.1, *“Contractor’s Entitlement to Suspend Work”*; and Sub-Clause 16.2, *“Termination by Contractor”*. These sanctions would mean that the consequences of non-compliance could be serious for both the employer and the contractor. However, these are drastic measures; could be abused; and might produce more disputes than they resolve.
- (b) Secondly, and more simply, an effective solution would be to amend Sub-Clause 20.7 such that it caters for both steps 4(a) and 4(b) set out above; and to implement a minor modification to Sub-Clause 20.6 that would permit the change in the wording of Sub-Clause 20.7 to be implemented. In doing so, Sub-Clause 20.7 could be amended to remove the

restriction of **“final and binding”** in its wording so that it allows relief whether or not finality has materialised. The suggested amended wording would read as follows:⁸

“20.7 Failure to Comply with Dispute Adjudication Board’s Decision

In the event that a Party fails to comply with the Decision of the Dispute Adjudication Board, 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]. Sub-Clause 20.4 [Obtaining Dispute Adjudication Board’s Decision] and Sub-Clause 20.5 [Amicable Settlement] shall not apply to this reference.”

Following such amendment to Sub-Clause 20.7, the necessary modification to Sub-Clause 20.6 would be to add at the beginning the words **“Subject to the provisions of Sub-Clause 20.7”**, for two reasons, as follows:

1. To allow the Party who has given a notice of dissatisfaction to limit the arbitration proceedings to the failure to comply and thus negate the effect of the words **“shall have full power to open up an review ...”**, in Sub-Clause 20.6, from the powers of the Arbitrator; and
2. To bring into action the wording in the fifth and sixth paragraphs of Sub-Clause 20.4, which were quoted above, i.e. **“except as stated elsewhere neither Party shall be entitled to commence arbitration of the dispute unless such notice has been given”**. The added words also help to eliminate the restriction that would arise in the event that neither Party gives a notice of dissatisfaction, (so neither Party would be entitled to commence arbitration of a dispute pursuant to Sub-Clause 20.6).

In this way, the decision of the DAB could be transformed into an arbitral award, with all the enforcement prerequisites attached to such a document. This is done by treating the non-compliance as **“a dispute”** and through reference of such dispute to arbitration pursuant to Sub-

⁸ A similar solution was discussed and adopted during the deliberations of ICC’s drafting Committee for its recently published Dispute Board Rules, in force as from 1st September 2004. It is embodied in Article 5.4 of these Rules which provides **“If any Party fails to comply with a Decision when required to do so pursuant to this Article 5, the other Party may refer the failure itself to arbitration, if the Parties have so agreed, or, if not, to any court of competent jurisdiction”**.

Clause 20.7, the arbitrator(s) would have to be satisfied that the proper procedure had been followed by the DAB and then would issue a declaratory award requiring the non-compliant party to “*promptly give effect*”. In this way, the decision of the DAB would be transformed to an award that would have the support of the relevant legislative enactments relating to an arbitral award and would be enforced like any other award, subject to the application of the relevant legal system under which enforcement is sought.

F. Arbitration Pursuant to the proposed Sub-Clause 20.7

The second solution suggested above is based on the requirement that the Parties would have to comply with the intentions behind the provisions of the contract and in particular those under the fourth paragraph of Sub-Clause 20.4. Similarly, such solution is based on the assumption that the arbitral tribunal appointed pursuant to the provisions of Sub-Clause 20.7 would be capable of applying it. However, there are some questions that arise in this connection since the reference to arbitration under Sub-Clause 20.7 will be relating to the narrow issue of whether or not a party ought to have complied with the DAB’s decision, irrespective of its merits. For example, what would the situation be if the non-compliant party submitted in defence a challenge to the reasoning contained in the DAB’s decision? Indeed, what would the situation be if the non-compliant party submitted a counterclaim relating to the merits of the dispute? Will the arbitral tribunal decline jurisdiction, as these submissions ought properly to be made pursuant to arbitration under Sub-Clause 20.6 and not 20.7? Will the applicable law of the contract permit recognition of a provisional award rendered in consequence to arbitration under Sub-Clause 20.7? Will the arbitration rules adopted permit such a course of action?

The answer to these questions would depend not only on the applicable law of the contract, but on the arbitration rules to be applied and of course on the parties’ submissions. For example, Article 23(1) of the ICC Rules of Arbitration provides that “*Unless the parties have otherwise agreed, as soon as the file has been transmitted to it, the Arbitral Tribunal may, at the request of a party, order any interim or conservatory measure it deems appropriate*”. The words “*any interim or conservatory measure*” are wide enough to permit a provisional award to be rendered, subject of course to the provisions of the applicable law. Taking, for example, the 1996 English

Arbitration Act, Article 39(1) provides that *“The parties are free to agree that the tribunal shall have power to order on a provisional basis any relief which it would have power to grant in a final award”*. Article 39(4) then goes on to provide that *“Unless the parties agree to confer such power on the tribunal, the tribunal has no such power”*. Therefore, it would seem that in an ICC arbitration case under the 1996 English Arbitration Act, a tribunal would have the power to issue a provisional award under Sub-Clause 20.7 since the parties involved would have conferred that power on the tribunal through the adoption of the ICC Arbitration Rules.

One final point that should not be forgotten is the provision in the second sentence of Article 23(1) of the ICC Rules of Arbitration, particularly where large sums of money are to be paid under a provisional award. It requires that consideration should be given to the effect that the arbitral tribunal should make the granting of the award subject to an appropriate security to be furnished by the claimant party for obvious reasons.

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