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Judgment in Default Cannot Act as a Bar to Arbitration

In **Tindak Murni Sdn Bhd v Juang Setia Sdn Bhd**¹, the Federal Court addressed the issue of whether a judgment in default in Court can be sustained when the plaintiff who obtained the judgment in default is bound by a valid arbitration agreement and the defendant has raised disputes to be ventilated via arbitration pursuant to the arbitration clause.

After considering the nature and application of section 10 of the **Arbitration Act 2005**, the Federal Court, in the grounds of judgment delivered by Nallini Pathmanathan FCJ, held that the judgment in default cannot act as a bar to arbitration. The Federal Court then set aside the judgment in default and granted a stay pending arbitration for parties to refer their disputes to arbitration.

Background

The Appellant, (“Employer”), entered into a building construction contract (“Contract”) with the Respondent (“Contractor”) on 1 June 2015. Disputes arose between the parties resulting in the Contractor initiating a civil suit. The suit was initiated notwithstanding the clear and unambiguous provision, that is Clause 34 of the Contract, which required parties to refer any dispute or difference arising between them in relation to any matter arising in connection with the Contract to arbitration. The dispute related to the alleged failure by the Employer to make payment of a sum totalling RM1,702,870.37 due to the Contractor. This resulted in the Contractor issuing a notice of determination to the Employer, giving the Employer seven days to remedy the breach of the agreement.

As there was no response from the Employer, the Contractor issued a notice of termination pursuant to Clause 26.1(i) of the Contract and filed the civil suit. The claim was for the sum alleged to be owing to it under three interim certificates amounting to RM 2,684,924.55 being the value of works done. No appearance was filed within the requisite time period allowed, as a consequence of which the Contractor obtained a judgment in default against the Employer on 1 March 2017.

On 10 April 2017, the Employer filed a notice of application to set aside the judgment in default, on the basis that the Employer had valid disputes against the Contractor’s claims; and that parties should refer the disputes to arbitration pursuant to the arbitration clause. After the Registrar of the High Court set aside the judgment in default on 31 July 2017 on the basis that there was a defence on the merits, the Employer filed an application under section 10 of the **Arbitration Act 2005** to stay the Court proceedings pending arbitration premised on the arbitration clause. The Contractor appealed to the Judge in Chambers against the decision of the Registrar to set aside the judgment in default.

The Decision of the High Court:

The High Court needed to decide on two applications:

- 1) the Contractor's appeal against the Registrar's decision to set aside the judgment in default; and
- 2) the Employer's application for stay of proceedings pending arbitration pursuant to section 10 of the **Arbitration Act 2005**.

The High Court dismissed the appeal against the setting aside of the judgment in default and allowed the Employer's application for a stay pending arbitration on 14 November 2017. In so determining, the High Court held that:

- 1) there was a defence on the merits as there were issues or disputes of fact that required resolution at trial; and
- 2) there was a valid arbitration clause that parties agreed to be bound by. Applying section 10 of the **Arbitration Act 2005**, as there was nothing to show that the arbitration agreement between the parties was null and void, inapplicable or inoperative, the court proceedings were therefore stayed pending referral of the dispute to arbitration².

Aggrieved by the decision of the High Court, the Contractor filed two appeals to the Court of Appeal against the decision of the High Court, one in respect of the Judge upholding the Registrar's decision to set aside the judgment in default and the other against the grant of the stay pending arbitration.

The decision of the Court of Appeal

The Court of Appeal allowed both the Contractor's appeals. However, it, in essence, only dealt with the setting aside of the judgment in default. The Court of Appeal approached the appeals by starting with the appeal relating to the setting aside of the judgment in default. Only after that was the stay appeal considered. In relation to the appeal against the setting aside of the judgment in default, the Court of Appeal determined that there were no merits in the defence, and therefore held that the High Court had erred in setting the judgment in default aside.

The Court of Appeal then allowed the Contractor's appeal, restoring the judgment in default. Having concluded that the judgment in default was erroneously set aside, the only possible conclusion the Court of Appeal could come to was that the stay be dismissed. It did not consider or address the merits of the application for a stay pending arbitration³.

The Employer then appealed against both the Court of Appeal's decisions to the Federal Court.

The decision of the Federal Court

The two questions of law posed to the Federal Court were as follows:

- 1) can a judgment in default in Court be sustained when the plaintiff who obtained the judgment in default is bound by valid arbitration agreement/clause and the defendant has raised disputes to be ventilated via Arbitration pursuant to the Arbitration Clause; and
- 2) should the Court in hearing an application to set aside the Judgment in Default where a valid Arbitration Clause is binding on parties consider the "*merits*" or "*existence*" of the disputes raised by the defendant?⁴ In allowing the appeal, the Federal Court answered both questions in the negative⁵.

At the outset, the Federal Court noted that the approach adopted by the Court of Appeal, namely to consider the two appeals sequentially and in isolation, was flawed⁶.

Unlike the Court of Appeal, the Federal Court held that the starting point for an analysis of the issues in the appeals was the consideration of the arbitration clause in the governing contract so as to ascertain whether it comprises a valid agreement to arbitrate, as opposed to considering the merits of the defence. This is pursuant to section 10 of the **Arbitration Act 2005** which makes it clear that the first step is to ascertain whether there is in fact an agreement to arbitrate in respect of the dispute in question⁷. The Federal Court was satisfied that Clause 34 of the building contract comprised an arbitration agreement and it therefore followed that unless the arbitration agreement in Clause 34 was null, void, inoperable or incapable of being performed, all disputes arising under the governing contract were to be referred to arbitration⁸.

The next issue that the Federal Court considered was whether the position was any different where one of the contracting parties had obtained judgment in default in court proceedings, notwithstanding the arbitration clause⁹. The Federal Court answered the question in the negative for four reasons.

Firstly, the Federal Court held that section 10 remains applicable notwithstanding the judgment in default. Secondly, the Federal Court took the view that by initiating court proceedings, the Contractor had effectively breached the arbitration agreement and as such the Contractor cannot rely on its own breach to seek to impugn or subordinate the agreement to arbitrate. Thirdly, if the Contractor's breach of the agreement to arbitrate was condoned, it would effectively render the arbitration agreement nugatory and the intention of the parties at the point in time when the contract was concluded would be effectively undermined. Lastly, the Employee's application to stay the Court proceedings pending arbitration raised a jurisdictional point, namely whether the dispute ought to be dealt with by way of litigation or arbitration, but the Court of Appeal did not address this essential issue. This was a relevant consideration even when determining the appeal relating to the setting aside of the judgment in default because the existence of a jurisdictional issue afforded a defence on the merits¹⁰.

In response to the Contractor's submission that there was no dispute that warranted referral to arbitration, the Federal Court made two points. Firstly, under the present section 10 of the **Arbitration Act 2005**, the Court is not required to consider whether or not a "*dispute*" subsists between the parties. This was contrasted with the language of section 10 of the **Arbitration Act 2005** prior to the amendment in 2011 which expressly required the Court to consider whether there was any dispute between the parties before granting a stay pending arbitration. Secondly, after considering parties' respective positions, the Federal Court, in any event, was convinced that there was in fact a dispute subsisting between the parties to be determined by way of arbitration¹¹.

Interestingly, the Federal Court dedicated a whole section in the Grounds of Judgment to reiterate the duty of advocates and solicitors to provide honest and complete submissions to the Court. This was a response to

- 1) the Contractor's failure to bring the attention of the Court to a clause in the Contract which would defeat its argument that the disputes in question were intended to be "*carved out*" from the arbitration clause; and
- 2) the Employee's attempt to randomly cite a passage in an English judgment without sufficient explanation on, *inter alia*, the nature of the case and the context in which the statement relied upon was made.

The Federal Court reminded that suppression, or deliberately presenting a legal position that does not fully disclose the facts or the law, is a "*grave dereliction of the responsibilities of an advocate and solicitor*". The Federal Court emphasised that advocate and solicitors are duty bound not to suppress

facts or law which are either against their client’s case, or does not support it, because of their overriding duty to the court, and ultimately the administration of justice as a whole¹².

Finally, the Federal Court concluded the grounds of judgment by ruling that the Court of Appeal had erred in law in arriving at the decision it did and that the two questions of law must be answered in the negative¹³.

Conclusion

In this case, the Federal Court clarifies the interplay between an arbitration clause and a judgment in default. The Federal Court’s decision is unequivocal. By answering both questions of law in the negative, the Federal Court has made it clear that parties will not be allowed to defeat or circumvent an arbitration clause by obtaining a judgment in default. In other words, a judgment in default obtained notwithstanding the existence of an arbitration clause will be set aside as of right without the need to consider the merits or existence of any disputes between the parties.

This decision also reinforces the pro-Arbitration approach taken by the Malaysian Court and the Malaysian Court’s efforts to always give effect to a valid and binding arbitration agreement between the parties.

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¹ Civil Application No. 03-2-11/2018 (B) (The judgment is dated 17 February 2020).

² Paragraph [22] of the Grounds of Judgment.

³ Paragraph [23] to [28] of the Grounds of Judgment.

⁴ Paragraph [4] of the Grounds of Judgment.

⁵ Paragraph [5] of the Grounds of Judgment.

⁶ Paragraph [28] of the Grounds of Judgment.

⁷ Paragraph [37] to [39] of the Grounds of Judgment.

⁸ Paragraph [40] to [46] of the Grounds of Judgment.

⁹ Paragraph [47] of the Grounds of Judgment.

¹⁰ Paragraph [48] of the Grounds of Judgment.

¹¹ Paragraph [53] of the Grounds of Judgment.

¹² Paragraph [54] to [58] of the Grounds of Judgment.

¹³ Paragraph [72] to [75] of the Grounds of Judgment.



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