

Arbitration in Construction Industry in Malaysia

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ABSTRACT

Disputes in construction industry are normal and sometimes cannot be avoided. Disputes arise from the interpretation and/or application of any part of building or engineering contract documents that are ambiguous, unplanned and conflicting at any time during the execution of the contract. There are many methods/techniques have been introduced in order to resolve the disputes and arbitration is one of the popular recommended method. This study examines the concept of arbitration and its acceptance by the Malaysia construction industry. Questionnaires have been sent to the selected contractors to collect information, data and views regarding to arbitration process, procedures and award. The survey reveals that arbitration still fails to impress Malaysian contractors. Lengthy time and high expenses are the common reasons given. Improvement must be made in order to improve the efficiency and the effectiveness of arbitration. New techniques of dispute resolution can be introduced by taking into account the problems existing in the recent techniques available and come out with better techniques that can guaranty satisfaction to the users.

Introduction

Traditionally the words “construction” and “development” often, denote, in a narrow sense, the physical activities of construction and development and relate only parties as builders, contractors, architects, engineers and

developers. This is a shallow interpretation and inadequate reflection of the two words and it has, in fact, created a misconception of construction and development. The activities of construction spread well beyond the functions of merely building and contracting and the processes of development stretch far in excess of the scope of simply designing and developing [1].

Construction and development involve numerous parties, various processes, different phases and stages of work, and many inputs from both the public and private sectors. The level of success in carrying out such construction and development activities will depend heavily on the quality of the managerial, financial and organizational performance of the respective parties and above all the effective co-ordination of such activities and performances through teamwork approach [2].

Because of the rapid advancement in science and technology and the complicated system of governmental control, construction and development are becoming more and more complex [3]. As such a sophisticated approach is necessary to deal with the planning and management of such construction and development activities. This is particularly important in a developing country like Malaysia.

Under the circumstances, there is an urgent need to study, analyse and investigate into the prevailing conditions with a view to identify problems and formulate solutions and, if required, to carry out extensive researches to up-grade and improve method and strategy in the planning and implementation of development projects thus increasing the efficiency and productivity of the construction industry.

The activities generated in the construction industry will in turn generate or cause activities to generate in other industries thus producing a chain of economic activities affecting the Malaysian economy as a whole. The construction industry in Malaysia, like in other countries, can serve as a barometer indicating the nation's economic conditions. Brisk construction activities point generally to the direction that the nation's economy is booming and sluggish construction activities will mean that the country's economic condition is depressing. In fact in many advanced and developed countries, the construction industry had, been and is still being used as one of the means in regulating the economy of the state [2]. It is abundantly obvious that the importance of the construction industry in the overall economic well being of Malaysia cannot be over emphasized.

Disputes

The meaning of the word “dispute” according to the Oxford Dictionary is “controversy, debate, heated contention, quarrel or difference of opinion”. In discussing disputes that may arise from or connected with the execution of a building or engineering contract, the meaning of the word “dispute” for all intents and purposes should be construed within the confines of the contract. In Malaysia, the contract forms used are commonly in the JKR 203 series, the PAM form, the ICE form or the FIDIC form, whether amended or otherwise. The ICE form or the FIDIC forms, if used, are usually in their amended form to suit local conditions and requirements.

From the above it can be deduced that the word dispute when used within the context of a building or engineering contract means “the difference between the-employer (or the architect, engineer or superintending officer on his behalf) and the contractor on matters connected with or arising from the building or engineering contract which they have entered into as the employer and the contractor.

Disputes can arise from the interpretation and/or application of any part of the contract documents and at any time during the execution of the contract. If the contract documents are ambiguous, unplanned and conflicting they will most certainly lead to disputes [4]. Such situations can be further aggravated if numerous additions and or omissions are made to the contract and persons responsible for the administration of the contract on both sides are badly equipped to understand and apply the contract documents, (including instructions to tenderers, agreement and conditions of contract, specifications, drawings and bills of quantities and with annexure which form part of the contract). It can be said the seeds of disputes are sown right from the outset if the above-described situation exist in any contract. Where ambiguous or conflicting provisions do exist and disputes do arise, there is a need to ascertain if a dispute has arisen or whether the dispute can be amicably resolved before referring such disputes to arbitration [5].

Dispute Resolution Method

As mentioned by Whitfield [6], some conflict and dispute are unavoidable, proper management of conflict will ease the impact it has on the construction process, but resolution must follow quickly. Dispute can be resolve by either using informal such as negotiation and alternative

resolution methods (ADR) or formal resolution methods such as litigation and arbitration.

Arbitration

In the execution of building and engineering contracts differences and disputes often arise from or in connection with the contracts. In almost all such contracts a clause for settlement of disputes by arbitration is provided so that when such disputes arise, the matter can be dealt with accordingly [7].

Undoubtedly the main reason for the popularity of arbitration is the fact that the parties have greater confidence in a tribunal, when the subject matter of the dispute is almost entirely technical, if the tribunal itself is technically qualified and experienced in the same field. Due to the fact that the tribunal is so qualified, it will restrain the exuberance of the parties and their experts and will induce a large measure of caution in their evidence not always so apparent in ordinary legal proceedings. Further more, in building and engineering disputes where the dispute is one of the facts, documentation can be extremely heavy and the relative informality of arbitration proceedings can help to reduce the expenses of copying and preparing documentary evidence in the form usually required in courts.

On the other hand, the inexperience of arbitrators in sifting and weighing evidence can be a serious disadvantage, even in reaching findings of fact, than laymen usually realize, and, in the absence of a high degree of restraint and fairness by the parties' legal representatives, a lay arbitrator can be placed in a most difficult position if the rules of evidence or procedure are ignored by the parties during the hearing, since he is usually in no position to judge the validity of legal submissions or objections in procedural matters, and may be quite unaware of the failure and inability of a party to comply with proper evidentiary or procedural requirements, or of the inferences of fact or credit to be drawn therefrom [5]. In addition there is the difficulty in analyzing the underlying reasons for rules of substantive or procedural law, and can give way to impulses of sympathy or compromise producing anomalous and sometimes startling results.

However, arbitration proceedings have what is sometimes the extremely important advantages, from the point of view of one or other party, of privacy, and also a fair degree of finality after any award is made by an arbitrator, as it is relatively difficult to upset such an award

once it has been made, since an appeal is by way of case stated upon a point of law only, except in cases of fraud or professional negligence.

Research Methods

Method of Collection

A postal questionnaire is considered to be the appropriate method for the analysis survey. The postal questionnaire is selected in view of its clear advantages over other method such as interview that will take longer time to achieve the same size of sample. By using the postal survey, a wider geographical coverage is possible. Moreover, due to time and financial factors, postal questionnaire is the most suitable method to collect the data.

As the research required the feedback about arbitration in Malaysia, multistage sampling has been adopted to ensure the samples provide a good representation of the population and more sensible data could be collected. It is also designed to ensure easy understanding and answering. 120 questionnaires have been directed to the selected firm for data collection. According to Fellows *et al.* [8] the normal expected useable response rate is ranging from 25 % to 35 %. By assuming 30 % responses rate, 36 members of responses will be collected by sending 120 numbers of questionnaires, which will provide sufficient data for this research. Therefore, 120 numbers of questionnaires should meet the requirement mentioned above and within the time and financial resources available.

Response to Questionnaire

Out of the 120 questionnaires sent, 35 were completed properly, giving the response rate of 29.17 %. Three of the questionnaires received were uncompleted, therefore could not be included in the data analysis. Although the response of Malaysia construction industry was not very encouraging, it is fall within the expected response rate, which is 25 % to 35 % [8]. Out of 35 of the respondents, 14 (40 %) are not familiar and have no knowledge about arbitration provision in Malaysia. Only 21 (60 %) respondents are familiar and have knowledge in arbitration provision. The 14 unfamiliar respondents are not allowed to answer all the questions in the questionnaire since they have no knowledge about arbitration. They only answered until question 2 and precede to the last question, which

they will give their reasons on why they are not familiar in arbitration provision.

Data Analysis

All the collected data from the questionnaire are analysed in two steps or methods. There are Frequency & relative index (RI) and Correlation. Frequency analysis is used as a preliminary analysis. This method will show the frequency, the percent of total for each value, the valid percent and the cumulative percentage in the form of table and pie chart. All questions based on Likert's scale will be analysed by using Relative Index (RI) technique.

Result and Discussion

Arbitration Users

There are many parties involve in arbitration process. There are employers, main contractors, sub-contractors, suppliers, authorities and many others. Some of them have the experience with arbitration and some of them have no knowledge and experience. A representative will be appointed by each party to represent them in the arbitration proceeding. The representative can be a person with legal background such as lawyer or an industrial expert who have knowledge in the specific area of the disputes.

In this project, three main parties in construction industry are focused. There are employers, main contractors and sub-contractors. According to Table 1, main contractors are the most frequent users (0.77) of arbitration to resolve disputes followed by the employers (0.70) and sub-contractors (0.53). Main contractors are the key player in every construction project compare to sub-contractor. They handle the primary work and deal with many parties that involve in a construction work. This may expose them to greater chance of disputes. Many employers are not directly involved in construction work and only communicate through the main contractor regarding the progress of the work.

In comparison by size of organisation, large organisations use arbitration more frequent (0.82) compare to medium organisations (0.62) and small organisations (0.49). Stable financial is the main factor that influences their participation in arbitration. Arbitration proceeding is costly

and usually small firms such as sub-contractors can't afford it and prefer to settle dispute by informal manner. Furthermore, larger organisations deal with larger project and works, which will expose them to higher risk of disputes.

Table 1 also shows that parties with experience in arbitration are likely to use it again in future. Parties are repeat users (0.66), repeat vs. infrequent users (0.55) and both infrequent user (0.48). Arbitration involves many processes and experience is one of the necessities needed by the parties before commencing arbitration. When the parties are familiar with all the process and procedures related to arbitration, they would gain confident in using it again. For the parties that infrequent in using arbitration, they may have doubts whether this technique will be successful in resolving their dispute or in the other hand will make their problem even worst. This will discourage them to use arbitration and prefer to settle disputes in their own way.

In the case of representation of each party in arbitration, both parties frequently used legal representatives (0.73). They also have choice to choose industrial expert (0.63) to represent them, but legal representative are more preferred. Each party may also represent themselves (0.44) in the arbitration proceeding but it is very seldom as stated in Table 1. Legal representatives more preferred due to his expertise in laws and their familiarity in the arbitration proceedings. It is an additional advantage if the legal representatives have knowledge and familiar to the construction industry.

Parties that involves in the arbitration should consider the appointment of an arbitrator especially if it is their intention that he should be appropriately qualified to deal with the technicalities involved. They can choose arbitrator with legal background or construction industry background. 67 % of the respondents choose to have an arbitrator with construction industry background and 33 % of them choose arbitrator with legal background. Contrast with the appointment of representative, arbitrator with construction industry background is preferred by most of the respondents. This may due to his experience in construction industry and he will understand better regarding the construction disputes compare to arbitrator with legal background.

Arbitration Procedures

When engaging arbitration, there are procedures stated in standard form of contract and in the construction contract that need to be followed.

Table 1: Arbitration Users

	RI
<u>Contractual position</u>	
Employer	0.7
Main Contractor	0.77
Sub-contractor	0.53
<u>Size of organisation</u>	
Large	0.82
Medium	0.62
Small	0.49
<u>Experience of arbitration</u>	
Both parties are repeat users	0.66
Both parties infrequent users	0.48
Repeat user vs. infrequent users	0.55
<u>Representation of proceeding</u>	
Both parties legally represented	0.73
Both parties represented by industrial expert	0.63
Both parties self represented	0.44
Legally represented vs. expertly represented	0.47
Legally represented vs. self represented	0.41
Expertly represented vs. self represented	0.38

48 % of the respondents followed procedures provided in the standard form of contract and 52 % of them choose to follow procedures stated in construction contract when engaging arbitration.

In arbitration, the procedures are flexible and sometimes it is carried out by informal process. Parties involve have freedom to choose a suitable person to be arbitrator. Arbitration is a privacy process and will not involve court and not open to press or the public. But, arbitration has its procedures that should be followed properly by all parties involved to ensure smooth proceeding and to avoid any unwanted matters arise. From all the 21 respondents, 62 % of them describe procedures of arbitration as a legal and formal process and 24 % believe it is informal procedures. There are 14 % describe the procedures are inquisitive and no respondents choose adversarial.

In preparing for arbitration, each parties involve will try to prepare themselves for the proceeding. This includes trying to collect available evidence and information in order to support their claims or to defend

their points during the hearing and presentation of their evidence. There are 47 % of the respondent spend much time in preparing for the arbitration proceeding. 24 % of them do not spend much time and 29 % of them believe that only one party spend much time. All the parties involved should prepare themselves before entering arbitration. Co-operation and agreement between them is very important.

Table 2: Driving Force Behind Matter of Procedures

	RI
Both construction parties	0.7
One construction party	0.51
Arbitrator	0.52
Legal representative	0.52
Expert representative	0.5

In order to achieve the objectives of the arbitration and to settle the disputes in a proper manner, all the participants must work together. Construction parties, arbitrator and the representatives must play their role effectively and efficiently. They must learn to co-operate with one another to ensure all the arbitration procedures are followed as stated in their arbitration agreement. Table 2 indicate the driving force behind matter of arbitration procedures. From the feedback of the respondents, both construction parties (0.70) are the primary driving force in the arbitration process and they are supported by the arbitrator and the representatives of each party. Every person involve must show their roles and try to make the process going.

Arbitration Award

The next step which the arbitrator must take after he has closed the proceedings is to prepare his award in which he will embody his decisions. In making his award, the arbitrator's objective is to define clearly, ambiguously, justly and enforceable on what the parties are to do and when they are to do it in order to resolve the matters in disputes.

75 % of the respondents indicate that it takes more than 4 weeks before the award is given. 10 % of them specify that the process will take 3 to 4 weeks, 5 % state 2 weeks and none of them state 1 week. This is due to all the procedures that have to be followed before come

into conclusion. The hearing process may extend over several weeks and even month especially where the issues are complex. In some instance, one party may ask that the hearing be postponed. Presentation of the evidence may also take time. Arbitrator should take notes in a careful and meticulous manner of all the evidence given by the parties and their witnesses throughout the hearing.

There are many reasons contribute to the long period time taken for consideration of award after the commencement of the arbitration proceeding. Table 3 shows some of the main reasons that influence the process. Over complex procedures arbitration proceeding (0.72) is the main reason why the process of consideration of award is lengthy. Delay or non-compliance by one of the party (0.64) is the second highest reason chooses by the respondents followed by presentation of complex evidence (0.63) and delay or non-compliance by both parties (0.57).

In reaching the decision, arbitrator may take a while in order to make sure his decision and award will convince both parties and successfully settle the disputes. 51 % of the respondents indicate that arbitrator needs more than 4 weeks to reach his decision. 10 % of them specify 4 weeks, 19 % for 3 weeks and 10 % for 2 weeks and 1 week.

Arbitrator may need time in order to come out with the decision an award. His decision must be definite in its terms, so that there is no doubt as to what the parties are required to do. The award must be consistent with his findings and he must make sure that his decision is final so that nothing remains to be done.

Basically, arbitrator will make his decision according to law or maybe to other considerations, which include matters of opinion other than those related to law. The arbitrator may use his expert knowledge of the matters, but must not rely upon any special knowledge of the particular case without disclosing such knowledge to the parties. 57 % of the decision by arbitrator made according to law and 43 % according to other considerations.

Although the objective of arbitration is to produce and award which is just, final and enforceable, there are reasons why this objectives is not always achieved. There maybe accidental errors in, or omission from the award. It may have been procured improperly or it may contain errors of law. It can lead to biased and unjust decision by the arbitrator.

Almost all the respondents, with 86 % agree that arbitration award is fair and just. Only 14 % of them consider the award is unfair and unjust. None of them feel that the award is biased and unacceptable.

Table 3: Driving Force Behind Matter of Procedures

	RI
Over complex procedures	0.72
Delay/non-compliance by 1 party	0.64
Delay/non-compliance by both	0.57
Presentation of complex evidence	0.63
Simple & effective procedures	0.48
Full compliance by the parties	0.5
Presentation of simple evidence	0.5

General Opinion

One of the most important aspects in choosing a method to resolve dispute in construction industry is the expense. 81 % of them believed that arbitration is costly and expensive and 19 % believed that it is inexpensive.

The direct cost of arbitration mainly includes the arbitrator's fee, expenses for arbitrator travel and hearing room rental, the cost of site inspection or experts appointed to assist the arbitrator and legal fee. Among these fees, legal fee usually takes up most part of the whole cost. The parties have to appoint lawyers to deal with the dispute except very simple case, because the law is very complexity. Legal fee main depends on how much time the attorneys spend. The longer the procedure lasts, the more legal fee is charged [9]. At the same time, the disputes are often concern with professional knowledge; arbitrators have to appoint experts to assessment. The expense of employing these professionals is very high.

Unfamiliar Respondents

There are 14 of the respondents (40 %) are not familiar and have no knowledge and experience in arbitration. There are many reasons given by them to support their unfamiliarity regarding the arbitrations. The two most common reasons are "Never involved in any arbitration process" and "No exposure given regarding the arbitration process"

The familiarity of the respondents toward arbitration can be influenced by many factors for instance nature of job, contractor's class, number of year working and their participation in arbitration itself. Primary factor that influences their familiarity in arbitration is their own participation. When they participate, they will gain new knowledge and information regarding the process and becoming more familiar.

Conclusion

From the analysis carried out, it shows the frequent users of arbitration are the main-contractors and usually involve large construction companies. Large organisations tend to settle disputes in proper and formal manner and great sum of money always engage. Arbitration frequently used by repeat users. Once they involved in the process, they gain new knowledge and new experience regarding the arbitration process and become more familiar.

To represent each party in the arbitration proceeding, they can appoint a representative either with legal background or industrial/construction background. Appointment of arbitration is also similar. He can be the one with legal or industrial background. From the results of the analysis, it shows representatives with legal background are preferred but for arbitrator, person with construction background is favoured.

In arbitration procedures, construction contract is frequently used as a reference to arbitration. The procedures are described as being legal and formal by majority of the respondents. Before arbitration start, both parties involved spend much time to gather all information and evidence available in order to support their points and claims during the hearing.

In arbitration award, it usually takes a lengthy period of time from the beginning of the proceeding until the consideration of award. This may due to over complex procedures and evidences and non-compliance by parties involved. Arbitral decisions are frequently made according to law and sometimes other considerations can be helpful in making a just and fair decision.

40 % of the respondents of this survey are not familiar with arbitration. This is because they do not have knowledge and experience. According to their feedback, no involvement in arbitration and no exposure given to encourage them in using arbitration are the main reasons why they prefer to settle disputes by informal manner such as negotiation amongst themselves.

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