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FIDIC Conditions of Contract and the Dispute Adjudication Procedure

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Legal Concerns

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A. INTRODUCTION

I have been asked to address certain matters of practical legal concern relating to the new FIDIC contracts. As time is limited, I would like to address just eight matters as follows:

A. The Parties (Sub-Clause 1.1.2)
B. Governing Law (Sub-Clause 1.4) and International Arbitration (Clause 20),
C. Performance Security (Sub-Clause 4.2),
D. Termination by Employer (Clause 15),
E. Suspension and Termination by Contractor (Clause 16),
F. Limitations of Liability (Sub-Clause 17.6),
G. *Force Majeure* and Release from Performance (Clause 19), and
H. Subcontracts under FIDIC

B. THE PARTIES TO THE CONTRACT (SUB-CLAUSE 1.1.2)

As you know, the parties to a FIDIC construction contract (the **"Contract")** are the "Employer" and the "Contractor". Neither the Engineer (who is hired and paid by the Employer) nor, for example, a Subcontractor (who is hired and paid by the Contractor) are parties to the Contract, although they may play important roles in any project.

However, there can be confusion about who is the Employer and who is the Contractor and this is the subject I want to address.

1. <u>The Employer</u>

In a FIDIC Red Book-type contract, the "Employer" is typically the party who had originally invited tenders for the project. Thus, the Employer is defined in the new Red Book as:

> "the person named as employer in the Appendix to Tender and the legal successors in title to this person." [Sub-Clause 1.1.2.2]

The Appendix to Tender identifying the Employer is sent out by the Employer with the form of tender and other documents when tenders are requested.

However, Employers and their consultants are sometimes not as careful as they should be in identifying with sufficient exactness who is the Employer. For example, in a matter in which I was involved - relating to a FIDIC Red Book contract - the Contractor began an arbitration against the Republic of (what I shall call) Ruritania, believing the Employer to be the Republic (or State) of Ruritania. However, after submitting the Request for Arbitration to the address of the Employer shown in the construction contract, the Answer came back from the National Water and Sewage Association of the Republic of Ruritania ("NWSA") saying that it was a separate legal entity from the Republic of Ruritania and that the Employer was the NWSA, a separate legal entity, and not the Republic of Ruritania. Examination of the contract documents showed that they referred to:

National Water and Sewage Association of the Republic of
Ruritania, abbreviated sometimes as "NWSA".

From this description alone, it is impossible for a lawyer (let alone, I suggest, an Engineer) to ascertain the important question of whether the Employer is:

(1) The Republic of Ruritania itself, or

(2) the NWSA, an entity that is separate and distinct from the Employer.

This was a very important issue for the Contractor as, whereas the NWSA had almost no financial resources of its own which could be available to pay an arbitration award, the obligations of the State of Ruritania were backed by the full resources of the state treasury of Ruritania. Accordingly, while an arbitration award against NWSA would be practically worthless, as NWSA had no money, an award against the Republic of Ruritania would have value, as it was backed by Ruritania's state treasury. Thus, the first dispute in the arbitration was who was the Employer, which should have been a totally unnecessary enquiry.

Accordingly, my advice to those of you who are preparing tender and contract documents is to ascertain exactly the identity of the legal entity or legal person which is the Employer. If there is any doubt about this - and it can sometimes be a complicated legal issue - then insist on receiving a written legal opinion about the question from a lawyer of the relevant country concerned. I would also advise consultants to insist on obtaining the particular law, decree or other legal document, or articles of association, pursuant to which the Employer was constituted. This will help you to identify the exact legal nature of the Employer.

2. The Contractor

As regards the Contractor, it will usually be either a single company or a contractual joint venture of two or more companies (that is, a joint venture which is not in corporate form). The legal status of the Contractor will normally have been checked by the Employer and its consultants at the pre-qualification or tender stage. If it is a contractual joint venture of two or more companies, then they will be deemed to be jointly and severally liable to the Employer for the performance of the Contract.[1]

However, as projects under FIDIC contracts often take several years to complete, a common problem which arises is that there may be changes in the company or companies forming the Contractor after it has been pre-qualified or has tendered. What changes are permitted and what are not?

The "Contractor" is defined in Sub-Clause 1.1.2.3 as the:

> "person(s) named as contractor in the Letter of Tender accepted by the Employer and the legal successors in title to the person(s)."

Therefore, there is no difficulty if the Contractor or a member of the Contractor merely changes its name or if its assets and liabilities are transferred to a legal successor as transfers to "legal successors in title" are expressly permitted. A legal successor would normally include, for example, an entity into which the Contractor (or a member of the Contractor) has merged and which has acquired all its rights and assumed all its obligations. But Sub-Clause 1.14 makes clear that other transfers are not permitted without the prior consent of the Employer. This Sub-Clause provides that in case the Contractor is a joint venture or other unincorporated grouping of two or more persons:

> "the Contractor shall not alter its composition or legal status without the prior consent of the Employer."

Thus, if the members of a joint venture do change and the Employer does not agree to the change, then the Employer may continue to hold the original members liable for the performance of the Contract.

C. <u>GOVERNING LAW (SUB-CLAUSE 1.4)</u>

Broadly, the FIDIC Conditions refer to laws in two senses:

(1) the governing law of the contract or the law by which the contract is to be interpreted, which is referred to in Sub-Clause 1.4, and

(2) the duty of the Contractor to comply with applicable Laws when performing the contract, which is referred to in Sub-Clause 1.13.

I will talk about **the governing law** of the contract, which is provided for in Sub-Clause 1.4.

What do I mean by governing law?

Essentially this refers to the national law according to which the contract will be interpreted or construed. It will deal with such questions as:

(1) whether to find the meaning of the contract one must look only at the face of the contract or whether, and under what circumstances, one may look at pre-contract documents, which may not be part of the contract, such as the invitation to tender documents, and to the post-contract conduct of the parties,

(2) what rights or obligations a contracting party may have in addition to those provided for by the express wording of the contract (e.g. a right to claim additional payment, or damages for breach of contract, or a right to terminate the contract, which is independent of the provisions on termination in the contract itself), and

(3) in exceptional cases, the governing law may actually override the provisions of the contract (e.g. the provision for liquidated damages for delay in Sub-Clause 8.7, or the provision for the rate of interest on delayed payments in Sub-Clause 14.8, might be held to be invalid if, for example, the amount of the liquidated damages specified, or the rate of interest specified, is considered to be excessive under the applicable governing law).[2]

As a practical matter in a FIDIC form of contract, the governing law:

(1) Will usually be **the law of the Employer's country** which generally will be where the site is located.

(2) The Employer's country will often be an economically undeveloped country or developing country (e.g. in Africa, Asia, Eastern Europe or the Middle East). Just as the country will often be economically undeveloped, **so the law of the country concerned may be sparse or undeveloped.**

(3) **The laws may not even be published** or, if published, may not be readily available. Incidentally, here Sub-Clause 2.2 of the new Books may be helpful as it provides that:

"The Employer shall (where he is in a position to do so)

> provide reasonable assistance to the Contractor at the request of the Contractor... by obtaining the Laws of the Country which are relevant to the Contract but are not readily available."

(4) There may be relatively **few competent and independent lawyers** in the country to advise about the local law.

The question therefore which I want to address is this:

(1) Does it matter to the Contractor or the Engineer that the law is that of an undeveloped or developing country?

(2) Does it matter that the country has very little law?

(3) Does it matter that the country's political regime is repressive or has a bad reputation internationally?

(4) Does it matter that the law in that country is Islamic law, civil law or common law?

(5) Finally, and this is the specific question I want to address, how does the governing law clause compare in importance to:

> **(a) a provision for international arbitration, and**
> **(b) to the place of arbitration?**

After many years of practice in the field of international construction disputes, my advice is that if a Contractor is signing a contract governed by a foreign law, then provided that:

(1) he obtains legal advice in advance about the implications of the foreign law for his contract including, in particular, any local public policy laws (e.g. tax, customs, foreign exchange, usury and similar laws) and takes appropriate precautions, and

(2) the contract contains **a satisfactory international arbitration clause and specifies a satisfactory place of arbitration, then it does not matter what the governing law is,**

whether developed or undeveloped, whether common law, civil law or Islamic law. Nor is the nature of the political regime in the country concerned generally important.

Why do I say that it does not matter? I say this for the following reasons:

(1) The FIDIC contracts are **detailed and comprehensive** documents which will regulate the vast majority of the situations likely to arise.

(2) While they have their origin in English forms of contract and so still have a common law orientation, they have been drafted so as to have **universal application,** so far as this is practically possible today.

(3) Under all legal systems, whether Islamic law, civil law or common law, **primary weight is given to the parties' written agreement,** subject only to the limited exception of public policy laws that your local legal advisor will tell you about.

(4) In construction disputes, decisions depend perhaps 90 to 95% on the facts (including technical issues) and only 5 to 10% on the law. **Consequently, compared to the facts and the terms of the contract, the law is not generally very important.**

(5) In my experience, the nature of the political regime is not very important, especially as most regimes that may not enjoy a good reputation (Libya, for example) **clearly distinguish business from politics.**

So, in the vast majority of cases, the terms of the FIDIC contracts will be given effect as written. If the other party does not comply with the words of the contract (that is, if it breaches the contract), it will be liable in damages under all legal systems.

It is perfectly true that laws in less well developed countries may not provide solutions to many or all of the complex contractual disputes that can arise on a large building, civil engineering or industrial project. But if the matter gets to arbitration, then it is perfectly legitimate for **a party to fill in the gaps** by **reference to the principles of an appropriate developed system of law.** This is accepted in the case of international construction disputes and international arbitration. For example:

(1) In the case of problems which are not clearly answered under Nigerian or Indian law,

one can look to English law from which these laws originate.

(2) In the case of problems under Kuwaiti, Lebanese, Libyan or Qatari law, one can look to Egyptian and French law.

(3) In the case of an issue over the validity of a "pay when paid" clause in a subcontract under Congolese law, both parties in an ICC case I was involved in referred to French and U.S. law.

(4) In the case of a dispute over the interpretation of a "price escalation" clause in a contract with a public body in Zaire which was governed by the law of Zaire, both parties in a case in which I was involved referred to Belgian and French administrative law.

In conclusion, as long as a Contractor takes the precaution of obtaining legal advice about the governing law before the contract is signed, I do not believe it matters much to a Contractor what the governing law is, even if it is a very undeveloped national law.

However, what is essential for a Contractor is that the contract contains a provision for international arbitration in an appropriate location, preferably in a neutral country with a modern arbitration law and which has ratified the 1958 New York Convention on the Recognition and Enforcement of Arbitral Awards. Otherwise, the contract may be unenforceable.

Before leaving the question of governing law, I would like to address one other question. Should the parties ever agree to provide for **no governing** law in the contract and to provide, instead, that disputes shall be resolved by reference to **principles of equity or fairness or *amiable composition?*** On first sight, this might appear like an attractive and reasonable solution.

FIDIC Sub-Clause 1.4 says "no" and, in general, my answer is "no". Such a solution will leave too much discretion to the arbitrators. They will have no standards to guide them, as may be provided by a reference to a governing law. Instead, the outcome of any dispute will be determined by their sense of fairness, which may not be your sense of fairness or even that of the other party. In fact, according to ICC statistics, in less than 5 per cent of ICC arbitrations are the arbitrators empowered to decide disputes by reference to fairness or ***amiable composition.*** [3]

D. PERFORMANCE SECURITY (SUB-CLAUSE 4.2)

FIDIC takes a neutral position on whether the performance security is in the form of:

(1) a surety bond issued by an insurance company, or
(2) "on-demand" guarantee issued by a bank.

Both forms are provided in Annexes C and D of the FIDIC Conditions. Both forms incorporate by reference the excellent Uniform Rules of the ICC (for Demand Guarantees or Contract Bonds) that I commend to your attention. In preparing these Rules, great effort was made to find a fair balance between the interests of Employers, Contractors and banks. They represent today the "state of the art" in the field of bonds and guarantees.

No one in this room, I suggest, should agree to the issue of a bond or guarantee in future without having examined and considered the use of these rules.

But while FIDIC provides for **both** of these forms, the reality of the international construction business is that **owners insist upon "on-demand" guarantees** issued by a bank in their own country and, to compete, Contractors have had no alternative but to provide them. Today, on-demand guarantees are the norm in international construction, whether Contractors like it or not.

Nevertheless, in the interests of being fair to both parties, Sub-Clause 4.2 (after providing that the Employer may only claim for amounts to which he is entitled) sets out conditions for call of the performance security as follows:

(1) failure by the Contractor to extend the performance security as required,
(2) failure by the Contractor to pay an amount due,
(3) failure by the Contractor to remedy a default within 42 days after a notice of default, and
(4) a ground for termination by the Employer under Sub-Clause 15.2.

But note that - as far as the on-demand guarantee is concerned - as these conditions are only in the construction contract they are only valid as between the Employer and the Contractor who sign that contract. They do not limit the issuing bank's obligation to pay in conformity with an on-demand guarantee. If the Employer disregards these conditions and calls the on-demand guarantee, then the bank will have to pay even though these conditions are disregarded. While the

Employer may be in breach of contract in disregarding these conditions, the money may have been paid by the bank to the Employer in the meantime.

The form of on-demand guarantee itself (Annex C) sets out as the only condition for payment that the Employer provide to the Bank a written statement stating:

(1) that the Contractor is in breach of his obligation(s) under the contract, and

(2) the respect in which the Contractor is in breach.

These are important conditions as they require the Employer to observe **a certain discipline** before calling an on-demand guarantee: **the Employer must state that the Contractor is in breach and the respect in which the Contractor is in breach.**

However, as far as the bank is concerned, once these conditions are satisfied, the bank has to pay **whether what the Employer says is correct or not.** Thus, the Contractor does not have a lot of protection. **Is there any solution for the Contractor? If so, what is it?**

First a comment and then a solution. My comment is that, while "on-demand" guarantees look very dangerous to the Contractor and are dangerous, in practice, it is in practice sometimes possible to delay, if not prevent, payment where the demand is not really justified.

Under the laws of most countries, a Contractor may only enjoin the payment of an ondemand guarantee where he can show **serious fraud** by the Employer, which is a difficult standard to meet.

However, in my experience:

(1) after having received a demand from the Employer, the bank which has issued the on-demand guarantee (who will usually be in the Employer's country) normally will not pay for a few days or even a week or longer unless a court order has been issued (among other things, the issuing bank will not pay without assurance that it will be made whole by the counter-guaranteeing bank, who will usually be in the Contractor's country),

(2) in most countries, one can apply to a court *ex parte* (that is, **without the presence of the other party)** for an initial temporary injunction against payment - this is obviously an

advantage for the claimant/Contractor as, in such a proceeding, there is no one at the court to contradict what the Contractor says,

(3) if the bank in the Employer's country which has issued the on-demand guarantee is the local branch of a foreign bank, one can also apply to a court *ex parte* in the country where such bank has its head office (which may be the Contractor's country) for a temporary injunction to restrain the bank (including its branch in the Employer's country) from making payment,

(4) when an on-demand guarantee has been wrongly called then, in practice, the Contractor often has a basis for at least arguing that there has been serious fraud even if he cannot prove as much, and

(5) even if the Contractor is unable to enjoin payment of the guarantee issued to the Employer in the Employer's country, he may be able to enjoin payment of the counter-guarantee in the Contractor's country and thereby delay or prevent payment of the guarantee itself by the issuing bank in the Employer's country.

Thus, in practice, in my experience, even in the absence of serious fraud by the Employer, a determined Contractor may be in a position to delay payment of an on-demand guarantee for weeks, if not months, where the demand is not really justified (although the demand may not be fraudulent).

Now let me suggest the solution. As we will be discussing tomorrow, the new FIDIC Conditions all provide for the settlement of disputes initially by a Dispute Adjudication Board, before arbitration. The decision of such board, which is provisionally binding on the parties (subject to arbitration), must be rendered within 84 days. Accordingly, to limit the risk of an abusive call of an on-demand guarantee, why **does it not make sense for the parties to agree that any call on the on-demand guarantee must be accompanied by a decision from the Dispute Adjudication Board stating that the Contractor is in breach of contract and the damages**

resulting from the breach, the Employer being entitled to claim under the bond for the amount of such damages?

For many years, Contractors have been fighting against on-demand guarantees. In the past, Contractors have proposed that, when the Employer calls on the on-demand guarantee, he should accompany his demand with an arbitral award or a court judgment. However, this was totally unrealistic as it would normally take years to obtain an arbitral award or a court judgment. No one could expect the Employer to wait that long. On the other hand, the decision of a Dispute Adjudication Board can be obtained merely in 84 days. Before allowing the Employer to seize the amount of an on-demand guarantee (which may be regarded as having some of the characteristics of a cash deposit with the Employer), it would not seem unreasonable to require the Employer to wait the 84 days necessary **to obtain a favorable decision from the DAB.**

Accordingly, I believe that the requirement of a favorable decision of a DAB (determining that there has been a breach and stating the damages for such breach) could be of real value in limiting the harsh one-sided effect of an on-demand guarantee.

While this suggestion is not contained explicitly in FIDIC's *Guide* to the new FIDIC books, I believe that this is one which can be adopted without very substantial change to the relevant FIDIC documentation. It should only be necessary to make payment of the on-demand guarantee conditional upon an appropriate decision of the DAB. This solution is something which FIDIC could consider for inclusion in future FIDIC contract documentation.

In conclusion, I suggest that the introduction into the new FIDIC forms of the provision for a Dispute Adjudication Board provides a mechanism to limit the drastic, one-sided nature of an on-demand guarantee and to make the operation of that guarantee fairer to the Contractor without undermining its utility to the Employer.

E. TERMINATION BY EMPLOYER (CLAUSE 15)

There are two features of this Clause I would like to mention here:

(1) In **Sub-Clause 15.2(b),** it is no longer provided that the Employer may terminate where the Contractor has **"repudiated"** the contract *(see* Sub-Clause 63.1 (a) of the old Red Book) as it was difficult for non-lawyers, as well as lawyers from civil law countries, to understand what this meant.

Accordingly, it is now provided that the Employer may terminate if the Contractor "abandons the Works or otherwise **plainly demonstrates the intention not to continue performance of his obligations under the contract".** This is how we have translated a complicated English legal word - "repudiate" - into common English for the benefit of international users.

(2) The Orange Book (Sub-Clause 2.4) had introduced the principle into the FIDIC contracts that the Employer was entitled to terminate the contract for the Employer's convenience at any time and simply pay the Contractor for work done.

A similar **termination for convenience** clause is now introduced into **Sub-Clause 15.5** of all the new Books.

However, you will note that the Sub-Clause contains a provision protecting the Contractor against abusive termination by the Employer as it states that the Employer shall not terminate the contract in order "to execute the Works himself or to arrange for the Works to be executed by another contractor".

In the case of **public** works contracts, it may be reasonable to have such a clause and such a provision is widespread in public procurement laws around the world, where it is justified on the ground that the Government should be entitled, in light of the changing needs of public policy and in the public interest, to discontinue or abandon a project without having to pay for work which will not be performed. Nevertheless, at least in the case of **private** works contracts, this Sub-Clause seems to me unfair to the Contractor and one-sided as it entitles the Employer to terminate the contract at any time without paying the Contractor the profit on the balance of the work to be done to which the Contractor should normally be entitled, as it was part of the original contract.

F. SUSPENSION AND TERMINATION BY CONTRACTOR (CLAUSE 16)

Clause 16 contains **several useful protections for the Contractor** as follows:

(1) **Sub-Clause 16.1** of the-Red Book-now provides that the Contractor has a right to **suspend** work **if the Engineer fails to certify payments** in accordance with Sub-Clause 14.6 or **if, the Employer fails to provide information about its financial arrangements to the Contractor pursuant to Sub-Clause 2.4.** In the previous edition of the Red Book (Sub-Clause 69.4), the Contractor could only suspend or reduce the rate of work if the Employer was not paying monthly payment certificates on time.

(2) In addition, in **Sub-Clause** 16.2, the Contractor is now entitled **to terminate the contract** in two additional circumstances:

- **first, if the Engineer fails to certify a relevant payment certificate within 56 days, and**

- **second, if the Contractor does not receive reasonable evidence within 42 days of the Employer's financial arrangements for the contract.**

These are, I think, both appropriate additions to the cases where the Contractor should be able to terminate the contract.

G. LIMITATION OF LIABILITY (SUB-CLAUSE 17.6)

One of the goals of the new edition of the FIDIC Contracts was to harmonize the old different FIDIC forms of contract as much as possible.

The old Red and Yellow Books were prepared by different committees and, as a consequence, these forms sometimes dealt with the same subject matter (e.g. *force majeure* or the resolution of disputes) in different ways, implying FIDIC had different policies about the same subject matter, which was not correct.

One of the objectives of FIDIC in having a single task group to prepare the entire new suite of contracts was precisely to ensure a complete harmony of the forms with one another.

I believe this goal has been achieved. It has been greatly aided by their having been a single draftsman - the late Peter Booen - to draft all of the forms with the aid of our Task Group.

However, in at least one instance I think - limitation of liability - I think we have gone too far and, consequently, we have sought to correct the misimpression that may have been created by the new Book in the ***Guide.***

The old Red and Yellow Books took radically different positions with respect to limitation of liability.

The old Red Book, you will recall, was for civil engineering construction (e.g. dams, roads, tunnels and the like) designed by or on behalf of the Employer.

On the other hand, the old Yellow Book was for electrical and mechanical works (e.g. turbines, gates and generators for a hydro-electrical station) generally designed by the Contractor.

The old Red Book contained no clause limiting the amount or the duration of the Contractor's liability whereas the Yellow Book contained extensive limitations on the Contractor's liability.

Basically, the old Yellow Book limited the Contractor's liability in four respects:

(1) By providing generally that **neither party would be liable to the other for loss of profit or any other indirect or consequential damage** (Sub-Clause 42.1);

(2) by **limiting the amount of the Contractor's liability to the sum stated in the contract** or, if no sum were stated, the Contract Price (Sub-Clause 42.2);

(3) by expressly **excluding the Contractor's liability for defects and other things after the Defects Liability Period,** as defined, except in the case of Gross

Misconduct, as defined (Sub-Clauses 30.12 and 42.3); and

(4) by providing that the **remedies** provided for in the contract (e.g. for breach of contract or negligence) were **exclusive** except in the case of Gross Misconduct, as defined, *see* Sub-Clause 42.4 of the Yellow Book.

The Orange Book, which was issued in 1995, partially adopted the solutions in the old Yellow Book (it adopted limitations (1) and (2) with some modifications).

What is the situation under the new Books? The striking feature is that (1) the **same** approach is taken by all three Books, and (2) this approach is **a sort of middle ground between the old Red and Yellow Books, as follows:**

(1) Neither party is liable to the other for loss of use of works, loss of profit or consequential damages (other than under indemnity clauses),

(2) Monetary limit placed on Contractor's liability subject to certain exceptions (if none stated, the limit is the Contract Price), and

(3) Limitations do not apply in the case of fraud, deliberate default or reckless misconduct.

It can well be argued that, in the case of a civil engineering works contract, like the Red Book, there should be no contractual limit on the Contractor's liability (there had been none under the old Red Book) whereas in the case of a contract for the supply of plant and equipment, a contractual limit may be justified. A contract for the supply of plant and equipment is different as, in the case of such a contract, there may be revolving equipment, like turbines in a hydro-electric station or rollers in the rolling mill of a steel plant, that operate 24 hours a day, which need to be operated in a particular way and which require regular servicing, change of spare parts and maintenance. In the case of such a contract, after a year or two of operation by the Employer, any defects that may appear may be as much due to the manner in which the equipment has been operated and maintained by the Employer as to the quality of the original equipment supplied by the Contractor.

While FIDIC has not recognized this distinction in the new Books (as it should have, I believe, in retrospect) FIDIC has now recognized this distinction in the FIDIC ***Guide*** where it is stated on page 279 that:

> "If the Works include major items of Plant, it is usually appropriate for the Contract to limit the duration of the Contractor's liability for such Plant; for example, to a stated number of years after the completion date stated in the Taking-Over Certificate. After a few years' operation, it becomes increasingly difficult to establish whether any alleged defects are attributable to the Plant's design, manufacture, manuals (**Note: these three items being possibly the Contractor's responsibility),** operation, maintenance (**Note: these latter two items being the Employer's responsibility)** or a combination of these and/or other matters." (Emphasis added)

Limits of this kind would appear particularly appropriate in the new Yellow and Silver Books.

Thus, if you are an equipment supplier under a Yellow or Silver Book contract, you will almost certainly want to seek to amend FIDIC's forms to provide for - at least as regards the equipment supply component of the contract - the much greater limitations on liability that are common or normal in your industry and are acknowledged in the *Guide.* An example of these which equipment suppliers have been happy with is that contained in the old Yellow Book.[4]

H. *FORCE MAJEURE* AND RELEASE FROM PERFORMANCE (CLAUSE 19)

Some commentators on the new forms appear to think that because *`force majeure" is* a foreign expression (in fact, a French expression) that it refers to some foreign **legal concept.** While the confusion is understandable, at least for non-lawyers, this is totally incorrect. *A* ***"force majeure"*** **clause as used in the FIDIC contracts and in international contract practice generally is typically nothing more than a clause designed to allow a party (usually, in practice, the Contractor) to be released or excused from performing a contract, either temporarily or permanently, when his performance is prevented by exceptional adverse events or circumstances, which such party could not reasonably have foreseen, arise.**

Moreover, the idea of *a force majeure* clause is not new to the FIDIC contracts, as it was contained (albeit in different forms) in both the Yellow and Orange Books.

As *a Force Majeure* clause is a new clause in the Red Book and may lead to misunderstanding, I would like to review it for you.[5]

I. **SUBCONTRACTS UNDER FIDIC**

Originally, there was no form of subcontract under any FIDIC form of main contract. As a federation of national associations of consulting engineers, FIDIC was concerned primarily, if not entirely, with construction contracts which consulting engineers were expected to administer. On the other hand, subcontracts could be considered to be within the sphere of responsibility of contractors and not consulting engineers.

But, in 1994, FIDIC did publish a form of subcontract for use with FIDIC Red Book.[6] To my knowledge, this may have been the first international standard form of subcontract ever published.

However, to date, sales of the FIDIC form of subcontract have been limited. It is not clear why, as the form of subcontract was well received.[7] This may have been because it was first published six years after the fourth edition and did not get much publicity, or because main contractors, at least, prefer to require the use of their own more one-sided forms of subcontract and are not interested in the "evenly balanced" form which FIDIC had provided.

As sales of the form of subcontract for use with the fourth edition of the Red Book have been limited, FDIC has not yet attempted to develop a form of subcontract for use with the new (1999) books. But, as people have continued to suggest FIDIC should develop a form of subcontract for the New Books, FIDIC has consulted the European International Contractors ("EIC") on the subject. However, EIC have opposed the idea. Accordingly, having only very limited resources, FIDIC has decided for the time being not to publish a form of subcontract for the new (1999) books.

How then as a practical matter should a party go about addressing the question of preparing a subcontract for the new forms? I have the following suggestions:

(1) The fourth edition of the Red Book and its accompanying form of subcontract may be used as a starting point.

(2) While there are a number of difficulties involved in drafting a subcontract, e.g. the

so-called "flow down" provisions whereby the Contractor's obligations to the Employer are, as between the Contractor and the Subcontractor, assigned to the Subcontractor, the two most difficult areas we found in drafting the FIDIC form of subcontract were:

(a) whether and, if so, to what extent, payment to the Subcontractor should depend on the Contractor having received a corresponding payment from the Employer, and

(b) whether any arbitration between the Contractor and Subcontractor under the subcontract should be joined with any arbitration between the Employer and the Contractor under the main contract and, if so, how this should be done.

As to the first point (point (a) above), our difficulty was deciding **the policy question** of to what extent payments to the Subcontractor should be made dependent upon the payments the Contractor received from the Employer. Once we had decided this policy question, the drafting was relatively easy.[8]

The second point (point (b) above) raised both policy and drafting issues. Our solution was to provide that, in general, any arbitration was to be between the Contractor and the Subcontractor only. However if, in the case of any given contract, the parties wished to consider providing that the Employer should also be a party to that arbitration (and if the Employer agreed, as he would have to), then we provided for a list of issues which would need to be addressed in order to draft an arbitration clause which would permit this result.

There is no time for me now to go further into these questions. Those who are interested to see how we dealt with these issues can consult the FIDIC form of Subcontract, which is available from FIDIC in Geneva, Switzerland,[9] and my article on the form which is attached as Annex B hereto. I would be happy to elaborate upon how these points were resolved during the question period if anyone would like me to do so.

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[1]Sub-Clause 1.1.4 of the new Books.

[2]See Clauses 15 and 16 of the new Books.

[3] In this paper, I have only discussed whether it is advisable to provide for a governing law or no governing law. There is also another possible solution, although rarely used until now in my experience. Instead of providing that the governing law is the law of a particular country, it is possible to provide that the contract shall be governed by some appropriate international rules or principles, such as the Principles of International Commercial Contracts established by UNIDROIT (International Institute for the Unification of Private Law), Rome, 1994, which are commonly referred to as the "UNIDROIT Principles". If the parties are looking for some truly international solution to the governing law question under a FIDIC contract, the UNIDROIT Principles provide an excellent starting-point.

[4]See Sub-Clause 30.12 and Clause 42 of the old Yellow Book.

[5] This subject is not elaborated further in this paper as it has already been discussed in the speaker's article *FIDIC's New Standard Forms of Contract - Force Majeure, Claims, Disputes and Other Clauses*, 2000 The International Construction Law Review ("ICLR") 235, a copy of which is attached as **Annex** A hereto.

[6] See the speaker's article *The New FIDIC International Civil Engineering Subcontract, 1995* ICLR *5*, a copy of which is attached as **Annex B** hereto.

[7] See, *e.g.*, the comments in Jeremy B. Winter, *The FIDIC Conditions of Subcontract and the UK FCEC "Blue Form " of Contract, 1997* ICLR 433.

[8]For more details on this, *see* the speaker's article attached as **Annex B hereto.**

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