International Construction Contract Disputes: Fourth Commentary on ICC Awards Dealing Primarily with FIDIC Contracts

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This commentary on five ICC arbitral awards from the years 2002, 2008 and 2010 analyses the decisions reached by ICC arbitral tribunals on a number of salient issues in international construction disputes. The issue examined in the first award is the extension of the arbitration agreement to the parent company of one of the signatories and, in particular, the piercing of the corporate veil as a transnational principle on the basis of which to operate such an extension. In the other four awards, the author examines issues relating to FIDIC Conditions of Contract, which are widely used in international construction contracts. In his discussion of the second award, the author considers questions relating to time bars for bringing claims under FIDIC Clause 67 and Sub-Clause 52.2. His discussion of the third award focuses on the relationship between the contractual Defects Liability Period and a statutory warranty period of longer duration in the country concerned. In relation to the fourth award, the author discusses claims relating to payments, including the effect of the Final Payment Certificate and the claimant's entitlement to claim for financing and overhead charges and exchange rate losses. Finally, in his discussion of the last award, the author examines whether the tribunal's reasoning over the Employer's right to set-off against certified sums due to the Contractor is consistent with the intention underlying the relevant FIDIC provisions and makes a recommendation for their future revision.

Ce commentaire de cinq sentences arbitrales de la CCI, rendues en 2002, 2008 et 2010, examine les décisions prises par des tribunaux arbitraux de la CCI sur plusieurs questions importantes survenues dans des litiges internationaux en matière de construction. La question traitée dans la première sentence est celle de l'extension des effets de la convention d’arbitrage à la société mère d'un des signataires et, plus particulièrement, de la levée du voile social comme un principe transnational permettant de fonder cette extension. Dans les quatre autres sentences, l’auteur examine des questions relatives aux conditions contractuelles FIDIC, qui sont largement utilisées dans des contrats internationaux de construction. Dans son analyse de la deuxième sentence, l’auteur aborde des questions portant sur les délais de forclusion auxquels sont soumises les réclamations faites conformément à la clause 67 et à la clause 52, alinéa 2, des conditions FIDIC. Son analyse de la troisième sentence vise le rapport entre le délai de garantie prévu au contrat et celui, plus long, fixé par la loi du pays en question. Concernant la quatrième sentence, l’auteur s’intéresse aux réclamations relatives aux paiements et notamment à l’effet du certificat final de paiement et au droit du demandeur d’être indemnisé de coûts de financement, de frais généraux et de pertes de change. Enfin, dans son analyse de la dernière sentence, l’auteur s’interroge sur la compatibilité entre, d’une part, le raisonnement du tribunal quant au droit de l’employeur à compenser sa dette de sommes certifiées envers l’entrepreneur avec sa créance à son égard et, d’autre part, l’intention sous-jacente des conditions FIDIC y afférentes et il recommande la révision de celles-ci.

El presente comentario acerca de cinco laudos arbitrales de la CCI de los años 2002, 2008 y 2010 analiza las decisiones adoptadas por los tribunales arbitrales de la CCI sobre varios asuntos importantes en controversias internacionales del sector de la construcción. En el primer laudo se examina la extensión de los efectos del acuerdo de arbitraje a la empresa matriz de uno de los signatarios y, en particular, el levantamiento del velo corporativo como un principio transnacional que permita fundamentar dicha extensión. En los cuatro laudos restantes, el autor analiza las cuestiones relativas a las condiciones contractuales de la FIDIC, que son ampliamente utilizadas en los contratos internacionales de...
Introduction


The various FIDIC Conditions of Contract are the best known and probably most widely used international standard forms of construction contract conditions. The first edition of the Red Book, published in 1957, was based on an English domestic standard form: the then current edition of the English Institution of Civil Engineers (‘ICE’) conditions. Even today, the official and authentic text of the Red Book is the version in the English language. However, in subsequent editions, the Red Book has become progressively more ‘international’ in style and content and today is widely used in civil law, as well as common law, jurisdictions.

The long time lag (ten to twenty years or more) between the moment a new edition of the FIDIC Conditions is introduced and the moment it comes into general use internationally and is then the subject of disputes that result in arbitral awards, as well as the time that needs to elapse before an award becomes eligible for publication by the ICC, mean that only one award in this issue deals with the latest suite of FIDIC construction contracts for major works published in 1999, consisting of the ‘Red’ (for civil engineering construction), ‘Yellow’ (for plant and design-build) and ‘Silver’ (for EPC/turnkey projects) Books (the ‘1999 FIDIC Books’). That award relates to the Test Edition of the Yellow Book published in 1998.

At the same time, the precedential value of awards dealing with older editions of the FIDIC Conditions, such as those which are the subject of this commentary, should not be underestimated for two important reasons. First, they continue to be in use in certain parts of the world (notably the Arabian Gulf) and, consequently, are likely to be the subject of disputes and arbitrations for years to come. Second, while the pre-arbitral procedure for the resolution of disputes by the Engineer under Clause 67 of the former editions of the Red Book was replaced in 1999 by the procedure for disputes to be submitted to a Dispute Adjudication Board (‘DAB’), the disputes clause in the 1999 FIDIC Books (Clause 20) is similar in principle to that in the older editions and thus awards relating to the resolution of disputes by the Engineer may well remain relevant to the procedure for the resolution of disputes by the DAB. A good example of this is the final award of 2010 in ICC Case 15282, discussed below. Hence, awards dealing with the earlier editions of the FIDIC Conditions may continue to be instructive in relation to the 1999 FIDIC Books.

A first series of extracts from ICC awards dealing with construction contracts referring to the FIDIC Conditions was published in Volume 2, No. 1, of this Bulletin in 1991. This was not accompanied by a commentary. A second series was published in Volume 9 Nos. 1 and 2 in 1998, a third in Volume 19 No. 2 in 2008 and a fourth in Volume 23 No. 2 in 2012, in each case accompanied by a commentary by the present author. They can all be found in the ICC Dispute Resolution Library (www.iccdr.com). ICC awards dealing with the FIDIC Conditions have also been published elsewhere. However, until recently (2008), this author had found only about forty published arbitral awards interpreting them, which is a matter for regret.

This fourth commentary will discuss the following five subjects and their corresponding awards:

A. Piercing the corporate veil of a Contractor to reach its parent company, ICC Case 14208/14236 (2008).

1 ‘FIDIC’ refers to the ‘Fédération Internationale des Ingénieurs Conseils’ or (in English) the International Federation of Consulting Engineers, which has its Secretariat in Geneva, Switzerland, see FIDIC’s website: www.fidic.org
2 The author gratefully acknowledges the assistance of Luka Kristovic Blazevic, an associate at White & Case LLP, Paris, in the preparation of this article.


A. Piercing the corporate veil of a Contractor to reach its parent company, ICC Case 14208/14236 (2008)

While this case did not involve a FIDIC form of construction contract, it addresses important issues that could arise under any international construction contract, including the FIDIC forms.

If, when entering into a construction contract, an Employer has any doubts about the solvency of the Contractor, the Employer will ordinarily require the Contractor to supply a guarantee from its parent company. This may, of course, not be its immediate parent but whichever company in its group is believed to have the requisite financial standing – a matter always requiring careful investigation. Each of the 1999 FIDIC Books contains, as an annex, an example form of parent company guarantee.

As international construction projects often take several years to complete, it is not unknown for an Employer that entered into a construction contract with a Contractor whose financial standing was good and therefore required no parent company guarantee to find some years later that it has a large, unsettled claim (e.g. for defective works) against a now insolvent Contractor? How is such a claim to be enforced?

While in most cases the Employer may be without an effective remedy, there has been a trend for international arbitrators to decide otherwise where the Contractor’s parent company has been involved in the conclusion, performance and/or termination of the construction contract and/or where the parent company appears by some action to have caused the Contractor’s insolvency or, as civil lawyers would say, to have abused its rights as regards its subsidiary, the Contractor. In these cases, the Employer may be able to claim that the arbitration clause in the construction contract should extend to the Contractor’s parent company and, thus, allow it to claim against the parent company directly in arbitration.

This was the matter at issue in ICC Case 14208/14236, where the Tribunal specifically addressed three important questions:

1. What law should apply to the issue of whether the arbitration clause in the construction contract should be extended to the Contractor’s parent company?

2. What theories might be applied to the issue of extending the arbitration clause to the parent company?

3. How might the theory of piercing the corporate veil be applied to find the parent company bound by the arbitration clause in its subsidiary’s construction contract?

1. What law should apply to the issue of whether the arbitration clause in the construction contract should be extended to the parent company?

The ICC Tribunal found that the issue of the extension of the arbitration clause should be governed:

- not by the substantive law governing the contract (as it would not be known whether the non-signatory parent company is bound by the contract, a law other than the law governing the contract must apply);
- not by the law of the place of arbitration (France) (although the extension of the arbitration agreement brings into question the jurisdiction of the arbitral tribunal, it is now outdated to consider that the law of the place of arbitration should apply as the law applicable to the proceedings);
- not by the law of the place of incorporation of the Contractor and its parent, which happened to be the same (as, although such law should apply to the internal affairs of a company, it should not apply where the rights of third parties external to the company are at issue, as here).
but instead by a transnational approach, consisting of transnational principles derived from prior ICC awards. In the words of the Tribunal, according to such awards arbitrators:

prefer to rely on a direct assessment of the facts and circumstances of each instance in order to determine the actual or supposed intention of the parties to be bound by the arbitration clause, or to sanction behavior considered abusive. Such an approach is certainly explained by the essentially factual nature of the issue... It... depends above all on a precise analysis of the facts of each case, which makes the question of deciding on the applicable law less essential.

2. What theories might be applied to the issue of the extension of the arbitration clause to the parent company?

The Tribunal then stated that, according to transnational principles, three theories could apply to the extension of the arbitration clause to the parent: (i) express consent, (ii) implied consent, and (iii) piercing of the corporate veil.

(i) Express consent

Under this theory, the arbitration clause may be extended to a third party, such as the parent, if the third party has expressly consented to the contract that includes the arbitration clause. The Tribunal found that there was no satisfactory evidence of express consent in this case.

(ii) Implied consent

Under this theory, an arbitration clause may be extended to a third party if the conduct of the third party in the conclusion, performance and the termination of the contract clearly demonstrates that it was the parties’ mutual intention that the third party should be a party to the contract and its arbitration clause. The Tribunal rejected this theory, too, because:

(a) there was no evidence of the Employer’s intention to make the parent a party to the contract; and

(b) although the parent had interfered in the performance of the contract, it had not been involved in its negotiation or its termination.

(iii) Piercing the corporate veil

As a matter of law, applying transnational norms, the Tribunal found that the corporate veil might be pierced where the following two conditions were satisfied:

(a) The dominant shareholder has complete control over the subsidiary, as evidenced in particular by:

- the insufficient capitalization of the subsidiary; and

- confusion in the administration, management and assets of the two companies.

(b) There is evidence of fraud (or intention to harm) or the abusive exercise of a right, known in French as abus de droit (for which no intention to harm is required), such as:

- for example when the control and effective management of the subsidiary by the parent company contribute to compromise the financial situation of the subsidiary and to make any action against the subsidiary illusory or at least doubtful or are used to promote and protect the parent company’s own interests at the costs of those who deal with the [subsidiary].

As discussed below, the Tribunal found the theory of piercing the corporate veil, based on the notion of the abusive exercise of a right, most relevant in this case.

3. How might the theory of piercing the corporate veil be applied to find the parent company bound by the arbitration clause in its subsidiary’s construction contract?

Having found no issue of fraud, the Tribunal stated that the issue was rather ‘whether [the Parent Company] had abused [the Contractor’s] corporate structure’. The Tribunal found that after the discovery of a defect in the Contractor’s work:

(a) the parent had transferred practically all of the Contractor’s assets to another company in the parent’s group of companies leading to a dramatic drop in the Contractor’s capitalization;

(b) after this transfer, the parent was in full control of the Contractor and managed and controlled performance of the construction contract;
(c) the Contractor had no independent office, telephone and fax number, human resources or legal and accounting department;

(d) there was confusion between the Contractor and the parent as regards employees and suppliers; and

(e) the Contractor appeared to have been maintained in existence for the sole purpose of performing the contract.

On the basis of the foregoing, the Tribunal concluded that the parent’s behavior was abusive because:

(a) it controlled and dominated its subsidiary, the Contractor, which was seriously undercapitalized and whose management was indistinguishable from that of the parent; and

(b) it abused ‘the corporate structure’ to protect its own interests because:

At the very moment when it appeared that [the Contractor] might incur substantial liability towards [the Employer], [the Parent Company] transferred all of [the Contractor]’s assets (except those relating to the [construction project]) to a subsidiary of [the Parent Company] in [country Y], the Contract remaining however in [the Contractor]’s name. Doing so, it abused the corporate structure to protect its own interests at the possible expense of [the Contractor]’s creditors ... In other words, [the Parent Company] has abused its control of [the Contractor] to transfer away from the company the bulk of its assets, but not the Contract, leaving [the Contractor] substantially undercapitalized, given the nature of its then-existing business and potential obligations. 15

In short, by transferring practically all of the Contractor’s assets to another subsidiary of the parent company after it was clear that the Contractor might have substantial liability to the Employer, the parent company was found to have abused the corporate structure of the parent company’s group.

Consequently, the Tribunal found this to be an appropriate case in which to pierce the Contractor’s corporate veil and extend to the parent company the arbitration clause contained in the Contractor’s construction contract.

In conclusion, in cases like the foregoing, the Contractor’s status as a separate legal entity will not shield a parent company from responsibility for the Contractor’s obligations and liabilities to the Employer. The Employer may be able to enforce them in international arbitration directly against the parent company.


This case presents three issues under the Red Book, Fourth Edition, as discussed below:

1. Was the Claimant’s claim in relation to design works time-barred under Clause 67?16

Whenever the disputes clause in a FIDIC contract is invoked (Clause 67 in the Red Book, Fourth Edition; Clause 20 in the 1999 FIDIC Books), the parties are advised to proceed with extreme caution as there is a risk that rights can be lost. That risk materialized here and rights were indeed lost.

Perhaps the key point to understand in Clause 67 is that, once a dispute has been referred to the Engineer for a decision pursuant to that Clause (or referred to the DAB under the 1999 FIDIC Books), time starts to run and can be stopped only by an amendment to the contract which, in the context of an international construction contract, is often unobtainable, as a practical matter, in the limited time available under the Clause.

Where the Engineer fails to give a decision but instead, as here, requests further information from the Contractor, a Contractor may be misled into thinking that, because the Engineer is the Employer’s representative for certain purposes, the time period(s) specified in the disputes clause is (are) necessarily suspended or relaxed. Yet this would be a mistake, as the Engineer has no power to amend the contract.

If the Engineer’s decision is not notified within 84 days of the dispute being referred to the Engineer, it is as if the Engineer had not given a decision, so if the Contractor wishes to preserve its right to refer the matter to arbitration, it must give notice of its intention to commence arbitration to the Employer, with a copy to the Engineer, within 70 days. This is what the Contractor failed to do here and, in a well-reasoned decision (not less so for having cited the present author!), the Tribunal concluded that the Contractor’s claim was time-barred. 17

The same principle applies under the 1999 FIDIC Books. If the DAB fails to give a decision within the designated 84-day period and the Contractor...
fails to preserve its rights within 28 days, the Contractor’s claim that is the subject of the dispute will be time-barred.\textsuperscript{18}

2. Was the Claimant’s claim for additional design work time-barred under Sub-Clause 52.2?\textsuperscript{19}

In this case, the Claimant had clearly failed to comply with the 14-day time limit provided for in Sub-Clause 52.2 and the 28-day time limit in Clause 53.

In the author’s view, the Tribunal was mistaken to interpret Sub-Clause 54.3 as affording it discretion to waive or relax the time limit in Sub-Clause 52.2. Sub-Clause 53.4 refers to a failure to comply with any of the provisions of ‘this Clause’ (i.e. Clause 53) and does not authorize the Tribunal to relax the time limit in Sub-Clause 52.2.

Rather than dismissing the Contractor’s claim outright as time-barred under Sub-Clause 52.2, which it could have done if it had taken a more strict approach, the Tribunal took a pragmatic approach and examined the documentary evidence produced by the Claimant to determine whether this was sufficient to support its claim. In doing so, the Tribunal referred to the definition of ‘contemporary records’ in the well-known Falkland Islands case, the most authoritative judicial decision on the subject.\textsuperscript{20}

The Tribunal found that the Claimant had failed to present ‘contemporary records’ to support its claim as required by Sub-Clause 54.3 and, on that basis, concluded that the Claimant had failed to meet its burden of proof and rejected the claim on that basis.\textsuperscript{21}

3. Was the Claimant’s claim for additional remuneration for the cost of more sophisticated valves time-barred under Clause 67?\textsuperscript{22}

The issue here was whether the Claimant notified the other party of its intention to commence arbitration in time, i.e. within 70 days of being notified of the Engineer’s decision. Specifically, the question was whether, under Sub-Clause 67.1, the notice of arbitration had simply to be sent to the other party (in this case it was sent by registered mail) or whether the other party had to have physically received the document within the specified 70-day period.

Although Sub-Clause 67.1 merely requires that on or before the 70th day after the day on which a party receives notice of the Engineer’s decision, that party must ‘give’ notice to the other party of its intention to commence arbitration, the Tribunal concluded, after examining the law of State X (including, specifically, the notion of ‘declaration of will’, which the Tribunal described as a ‘manifestation of will of a person made to the other person in circumstances where such declaration of will creates or influences the legal situation of that other person’\textsuperscript{23}), that the other party has to receive that notice within the 70-day period. Consequently, the Tribunal found the Claimant’s claim to be time-barred.

While the result seems somewhat harsh to this author (literally, ‘give’ suggests sending rather than receiving), and its relevance is possibly to be confined to countries having laws similar to those in State X, this case illustrates once again that where a time-bar may apply, parties are strongly advised to allow themselves plenty of margin, as the penalty for falling foul of a time-bar can be severe.


This case raises the issue of whether, under the contract concerned, which was based on the Red Book, Fourth Edition, the Respondent/Employer was required to release the second half of the retention money:

(a) upon the expiry of the 12-month Defects Liability Period specified in the contract, as argued by the Contractor/Claimant;\textsuperscript{24} or

(b) upon the expiry of the 60-month warranty period laid down in the Act of Public Works, which was a mandatory law of the state where the contract was being performed, as argued by the Respondent/Employer.\textsuperscript{25}

Under FIDIC Conditions, the Defects Liability Period usually lasts one year but for certain projects may extend to two years or even more. During this period the Contractor must not only complete any outstanding items of work as listed in the Taking-Over Certificate but also remedy any defects that may have appeared. The Contractor’s obligations in this respect are typically secured by the second half of the

\textsuperscript{19} §§ 159−202.
\textsuperscript{20} §§ 194.
\textsuperscript{21} §§ 202.
\textsuperscript{22} §§ 203−262.
\textsuperscript{23} §§ 251.
\textsuperscript{24} §§ 55−59.
\textsuperscript{25} §§ 72–80.
retention money\(^{26}\) (the first half of which is released when the Taking-Over Certificate is issued) and the performance security.\(^{27}\)

The expiry of the Defects Liability Period does not, of course, relieve the Contractor of further liability for defects. The Contractor remains liable to the Employer for any defects that may appear subsequently (commonly called ‘latent defects’) for the duration of the applicable statute of limitation.\(^{28}\) However, an important difference, from the Employer’s point of view, is that the Contractor’s responsibility to rectify latent defects is no longer secured by either the retention money or the performance security. As a consequence, unless the Contractor can be persuaded to rectify the defect voluntarily, the Employer would normally have to pursue the Contractor and/or its assets wherever they can be found in order to obtain relief.

In some civil law countries, local statutes or public policy may make the Contractor absolutely liable (i.e. liable without any need to prove fault) for a specified number of years after substantial completion of the works and the issuance of a Taking-Over Certificate. In France, this liability lasts for ten years, during which the Contractor is required to cover its liability by insurance. The Act of Public Works in State X appears to have contained a similar warranty or guaranty provision, although only for five years.

In international construction projects, there is sometimes confusion between the Defects Liability Period in a FIDIC form of contract and the mandatory statutory period. This may be due to a failure to distinguish between a contractual and a legal warranty period, or to a translation error or otherwise, leading (as in this case) to a dispute over the time for the release of the second half of the retention money, i.e. at the end of a one or two-year Defects Liability Period, or at the end of a much longer statutory warranty period.

In this case, the sole arbitrator resolved this issue sensibly by finding that there was no contradiction between, on the one hand, the Employer having to release the second half of the retention money after a 12-month Defects Liability Period and, on the other hand, the 60-month mandatory warranty period laid down in the Act of Public Works of State X. The arbitrator arrived at this conclusion by noting that, under the Act of Public Works, the only condition for releasing the retention money was that certain qualitative parameters had been satisfied (not the expiry of the 60-month warranty period provided for in the Act of Public Works or, indeed, any other time period) and the Contractor had satisfied those parameters.\(^{29}\) The Tribunal inferred that the Act of Public Works was less strict than the parties’ contractual agreement providing for release of the second half of the retention money upon the expiry of the Defects Liability Period and, consequently, was no obstacle to the application of that provision.\(^{30}\)


This case deals with the following issues under the Orange Book (1995):

1. Was the Employer bound by the Final Payment Certificate signed by the Employer’s Representative?

2. Could the Contractor recover from the two Respondents (a Ministry of State X and State X itself) financing charges for the period between the time the Ministry made deductions for certain taxes and the time of their subsequent refund?

3. Could the Contractor recover from the same State entities overhead charges and exchange rate losses (due to the devaluation of the currency of State X) over the same period, i.e. between the time of the deduction and the time of the refund?

1. **Effect of the Final Payment Certificate**

The Claimant/Contractor maintained that the Employer’s Representative had certified the Contractor’s claim for overheads, financing charges and exchange rate losses in the Final Payment Certificate issued pursuant to Sub-Clause 13.13 and that the Arbitral Tribunal was bound by what the Employer’s Representative had agreed in the Final Payment Certificate as this represented ‘a binding agreement between the Claimant and the … Respondent which must be given effect under Clause 13.13 of the FIDIC Conditions’.\(^{31}\)
While the arbitration clause in the FIDIC Orange Book (Sub-Clause 20.6) expressly provides that the arbitrators have full power to open up, review and revise any decision of the Dispute Adjudication Board, it does not provide – as is provided explicitly in the 1999 FIDIC Books – that they could also open up, review and revise any decision of the Employer’s Representative. Nevertheless, the sole arbitrator found that the Claimant had been unable to provide any written evidence that the Respondents had given express or implied authority to the Employer’s Representative to agree on what they regarded as non-contractual claims and accordingly found that he was not bound by the amounts stated in the Final Payment Certificate as being payable to the Claimant.32

2. Claim for financing charges

The sole arbitrator found that the Claimant was entitled to financing charges as the Claimant had been deprived of the use of the money deducted by the Respondents for taxes from the time of its deduction to the time its refund. On this basis, the sole arbitrator found that Sub-Clauses 11.1.5.6 (which defines ‘Cost’) and 13.16 (changes in legislation) were applicable and that the Claimant was entitled to financing charges for the amounts deducted and then refunded by the Respondents for taxes.33

3. Claim for overhead charges

The Claimant further claimed that it had incurred overhead charges at the rate of 7.67% as a result of the deduction and subsequent refund of money by the Respondents for taxes. The sole arbitrator stated the issue as follows:

In order for the Claimant to succeed in this claim, it will have to show the basis or entitlement under the Contract Conditions for this overhead claim, and how it had incurred this expenditure resulting from the monies that were deducted and refunded to it for the VAT and additional AIT (Advance Income Tax). In particular, the Claimant must be able to show that such expenditure as incurred by it constitutes ‘Cost’ as defined under Clause 11.1.5.6 of the FIDIC Conditions.34

There is a practice among some Contractors to assume that, because overheads are typically calculated as a percentage of turnover, they can be applied as an addition to any claim of the Contractor, regardless of its nature, as a successful claim will add to the turnover. However, this practice was not accepted in this case by the sole arbitrator, who questioned one of the Contractor’s witnesses as follows:

I just want to see what is the basis of your entitlement for the overhead. I can understand if your works have been delayed, you will incur overheads, for which you want to be paid. But where you are claiming for monies that have been withheld and you are claiming interest and exchange losses, I am just wondering what other losses would you have suffered?35

As the witness was unable to provide an answer, the sole arbitrator concluded that the Claimant had no real understanding of the basis for its overhead claim.36

The sole arbitrator found that the Contractor could not establish that it had suffered any loss that could be claimed as a ‘Cost’ under Sub-Clause 11.1.5.6, as the Contractor was already claiming for financing charges in respect of the money temporarily deducted and for the loss resulting from the fluctuation in exchange rates. Consequently, the sole arbitrator could not see how the Contractor could claim for overheads as a loss under either Sub-Clause 11.1.5.6 or Sub-Clause 13.3(a) to (g) and disallowed the claim.37

4. Claim for exchange rate loss

The Contractor also claimed for the loss resulting from the devaluation of the currency of State X against the Pound Sterling (the currency of the Contractor’s country) during the period between the deduction and refund of money by the Respondents for taxes. In response to this, the sole arbitrator stated that:

Although the Claimant’s argument appears to be cogent at first glance, I would have to ask what its position would be if in the intervening period the [State X currency] had strengthened in value vis-à-vis the Pound Sterling so that when the conversion from [State X currency] to Pound Sterling took place, the Claimant would have made an unexpected windfall gain in Pound Sterling.38

The sole arbitrator asked whether, in such an event, the Claimant would have given its windfall gain to the Respondents and strongly suspected not. He concluded that the Respondents likewise should not be penalized for the exchange rate loss of the Claimant.39

The Tribunal further found that it would be stretching the meaning of the term ‘Cost’ under Sub-Clause 11.1.5.6 of the Orange Book to regard a loss arising from exchange rate fluctuations as an expenditure of the Claimant. Consequently, the Tribunal denied this claim.40

The Tribunal’s reasoning on all these issues appears sound and calls for no further comment.

The decision in this case suggests that, at least under English substantive law, the Employer’s right of set-off remains intact under the 1999 FIDIC Books and is not excluded by their current wording.

In this case, the Claimants, two Contractors, sought an interim or provisional award in respect of certain unpaid certified sums due to one of them. In response, the Employer, the Respondent, asserted claims for liquidated damages for delay and argued that it was entitled to set off the amount of these claims against any amount due to the Claimants. The Claimants insisted that any right of set-off by the Respondent was effectively excluded by numerous provisions of the general conditions of the contract concerned – the Yellow Book (Test Edition, 1998). Among other things, the Claimants referred to Sub-Clause 2.5 of the general conditions dealing with the Employer’s claims as well as Sub-Clauses 14.6, 14.7, 20.4 and 20.6. Sub-Clause 2.5 sets out a procedure which the Employer is required to observe in relation to any claim that it might make against the Contractor.

While the Tribunal recognized that the Employer might have breached Sub-Clause 2.5, it held that nothing in that Sub-Clause or any of the other Sub-Clauses referred to amounted to an exclusion of the Employer’s right of set-off (under English law), which would have required words of sanction such as the following: ‘unless the Employer complies with this clause, it shall have no right to deduct or set-off…’. However, the Tribunal found that the contract contained no such provision.

Similarly, the Tribunal found that the requirement of Sub-Clause 20.6 to refer all disputes to a DAB did not exclude set-off rights. With respect to Sub-Clause 20.6, the Tribunal stated:

This does not require that a claim asserted as a set-off first be submitted to the DAB. It merely indicates that if a DAB’s decision does become final and binding, then the dispute might not be subject to arbitration. By its express terms (i.e., the reference to a DAB decision ‘if any’), Article 20.6 encompasses ‘disputes’ and therefore claims – as to which no DAB decisions [sic] has been made.

While, as mentioned above, the case concerned the Test Edition of the Yellow Book, the Tribunal’s comments appear to be relevant to the final version of the 1999 FIDIC Books generally as the relevant terms of the Test Edition of the Yellow Book were not significantly different from the corresponding terms in the final version of all of the 1999 FIDIC Books.

The present author finds this result surprising and, as a member of the FIDIC Update Task Group which prepared the 1999 FIDIC Books, believes it was not the intention of FIDIC that the Employer should be able to have rights of set-off against certified sums due to the Contractor. This decision may even be going too far in the eyes of English law as an English legal authority has recently stated, in relation to contractual rights of set-off, that: ‘Ultimately … the question is one of the parties’ intentions, as construed from the language of the contract itself and the known commercial background of the transaction.’

Arguably, the wording of the 1999 FIDIC Books, especially the mandatory language in Sub-Clause 2.5 dealing with Employer’s claims, should be interpreted as excluding set-off, in keeping with what the present author believes to have been FIDIC’s intention.

In light of this arbitral award, the author believes that FIDIC would be well advised to consider modifying its general conditions when preparing new editions of the 1999 FIDIC Books, in order to exclude expressly the Employer’s, or even each party’s, right of set-off.

41 § 60.
42 §§ 64 and 65.
43 § 65.
44 § 66.
45 § 66.
46 Footnote to § 71.
47 J. Bailey, Construction Law, Vol. 1 (Informa Law, 2011) at 539. The author is grateful to Anthony Lavers, a colleague in the London office of White & Case, for drawing his attention to this passage.
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