

# INTERNATIONAL CONSTRUCTION DISPUTES IN TODAY'S ECONOMY

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Current trends in international construction dispute resolution, especially those emerging from the global economic downturn, are reshaping the dispute resolution process. One trend is the impact on construction arbitration of the increased use of non-arbitration alternative dispute resolution (ADR) mechanisms. The genesis of this trend is more efficient and less costly processes. A further trend is the rise (and possibly now retrenchment) of international construction disputes as “investment” claims in investor-state arbitrations. In addition, driven by two forces in the current global economy, the liquidity problem and the desire for project work, bonds are increasingly required and somewhat counterintuitively readily available. We consider that these issues are likely to lead increasingly to bond guarantors in construction projects becoming part of the dispute resolution process.

Accordingly, this article examines:

- The rise of ADR and its impact on arbitration.
- Construction disputes as “investment” disputes.
- Issues when negotiating and administering construction contracts, particularly the increased importance of bonds, time clauses and choice of law clauses.

## Rise of ADR and Its Impact on Arbitration

### Effect of the Economic Downturn

The current global economy is not making life easy for the construction industry (whether developer, owner, contractor, sureties or designer). Broadly, contractors and designers are currently facing fewer new opportunities. Anecdotal information indicates that the new opportunities are being chased by more bidders at prices below engineer estimates. Sureties, attempting to bolster their bottom lines, are extending bonding capacity, enabling contractors to expand the range of projects for which they can compete. Hungry for work, pricing is super-competitive, too often below responsible levels. The result, when problems arise, is the claims process. Owners, with budgets constrained by tight bonding policies, are hard pressed to respond other than to resist the claims.

The effects of the economic downturn on construction appear to be global. For example, 10% of the world's skyscraper construction is on hold (28 July 2009, [www.bdcnetwork.com/article/CA6673425.html](http://www.bdcnetwork.com/article/CA6673425.html)).

In relation to the Middle East:

- In April 2009, the Kuwait Finance Centre reported that more than “\$1 trillion of Gulf real estate projects are at risk of cancellation” (23 April 2009: <http://business.maktoob.com>).
- On 28 July 2009, it was being reported that “a third of UAE building projects worth more than \$300 billion are still on hold or cancelled”. This included 400 out of 1,150 civil construction projects (28 July 2009, <http://business.maktoob.com>). Even Tiger Woods’ golf course, Al Ruwaya in Dubai, is on hold (5 June 2009, <http://sports.espn.go.com/golf/news/story?id=4234770>).
- In Saudi Arabia, 80 projects worth around \$20 billion (about €13.7 billion) are on hold or cancelled (2 August 2009, <http://business.maktoob.com>).
- See also ConstructionWeekonline.com, quoting an Ulma Formworks general manager: “Payment has been disastrous. Everyone is delaying payment. It takes an inordinate amount of time to collect” (3 August 2009 “Let the Bidding Commence” <http://construction-weekonline.com>).

#### **Increased Number of Disputes**

It is in this economic environment that construction project parties find themselves embroiled in dispute resolution processes, whether ADR, arbitration or litigation. In an effort to secure an expeditious and less costly resolution, parties explore ADR mechanisms such as mediation, nonbinding mini-trials, expert recommendations, and dispute

boards. Not only is ADR occurring during or before the formal arbitral process, but the ADR ideal of resolving construction disputes in real time with cost and time savings is exerting pressure on arbitral institutions to adjust their rules to provide these benefits, and on arbitrators when deciding cases.

Recent indications are that in certain markets the number of construction issues ripening into construction disputes is increasing. There is little to suggest that the situation is likely to slow, much less retreat, in the short term. For example, it has been reported that in the Middle East Gulf region, the number of construction disputes has doubled since the start of 2009, and is predicted to double again by the end of 2009. The tenor in that region seems to be that among contractors patience is declining, perhaps because significant sums are allegedly owed. (reportedly at least \$2 billion (about €1.35 billion) alone in Dubai, 17 June 2009: Litigations rise as construction deals unravel, E O’Sullivan, [www.meed.com](http://www.meed.com)). Arabian Business.com reports the same trend: “What seems to be changing is a resolve to pursue claims and make a firmer stand for what they [contractors] consider to be their rightful entitlement. The number of disputes being referred to arbitration centres is on the increase” (25 July 2009, Construction Disputes and the economic crisis, David Dale, [www.arabianbusiness.com](http://www.arabianbusiness.com)).

In these circumstances, it is likely that there will be increased construction arbitration activity in the Gulf. Indeed, on 16 August 2009 it was reported that \$4.9 billion (about

€3.32 billion) worth of construction claims are estimated to be pending in Dubai, according to an official at the Dubai International Arbitration Centre (DIAC) (16 August 2009, [www.arabianbusiness.com/564910-dubai-construction-claims-total-49bn](http://www.arabianbusiness.com/564910-dubai-construction-claims-total-49bn)). Perhaps a sign of growing demand is the decision of the London Court of International Arbitration (LCIA) to open a Dubai presence.

Likewise, construction disputes seem to be increasing in other regions, such as the UK (see “Is the industry becoming more litigious? Current trends in construction disputes,” PLC Construction, <http://construction.practicallaw.com/blog/construction/plc/?p=68>). Further, a review of arbitration filings at global arbitral institutions, while not broken down by industry sector, generally seems to substantiate a rising trend towards more international disputes. (Singapore International Arbitration Centre, at [www.siac.org.sg/facts-statistics.htm](http://www.siac.org.sg/facts-statistics.htm)). For example:

- The LCIA caseload increased from 137 cases in 2007 to 213 cases in 2008.
- The American Arbitration Association’s (AAA’s) International Centre for Dispute Resolution caseload grew from 621 cases to 703 cases in 2007/08.
- The International Chamber of Commerce (ICC)’s overall caseload has increased from 599 cases in 2007 to 663 cases in 2008.
- The International Centre for Dispute Resolution’s (ICDR) construction caseload grew from 48

cases in 2006 and 55 cases in 2007, to 77 cases in 2008 (e-mail from Wayne Kessler at AAA, 13 August 2009). The AAA also reported that in 2007 there was an 11% increase in U.S. domestic construction cases being filed with its AAWeb-file service (AAA 2007 President's Letter and Financial Statement).

### Increased Interest in ADR

Over the last five years there has been in the construction industry increased interest in ADR methods, particularly:

- Mediation.
- Adjudication.
- Non-binding mini-trials.
- Expert determination.
- Dispute boards.

This interest in ADR has occurred for a number of reasons (including, for example, the combined contentious nature of construction projects and desire to preserve and maintain relationships; the desire of parties to define solutions) but it has been driven by the business fundamentals that, at its best, ADR offers to all project parties a way to get buildings built quicker and at less cost than would be the case if the project were exposed to a lengthy traditional dispute process. In this regard, significantly, arbitration can no longer be considered "alternative" dispute resolution. See, for example:

- "Arbitration: The 'New Litigation'" (Thomas J. Stipanowich, Pepperdine University School of Law Paper No. 2009/15 (June 2009)).
- "International Dispute Resolution" (Chapter 43, pages 1747 to

1749, *Construction Law Handbook*, Ness, McHugh and Thomson (2008)).

- "U.S. Project Disputes: Has the Time to Consider Adjudication Finally Arrived?" (Jaffe and McHugh, *AAA Dispute Resolution Journal*, May to July 2007).

The ultimate aim of these ADR mechanisms is to secure the cost effective resolution of construction disputes, where possible before the culmination of the projects. Dr. Helmut Köntges, counsel at the German based international contractor Hochtief, summed up the reasons for the rise of these new ADR structures ("International Dispute Adjudication—Contractors' Experiences," Dr. Helmut Köntges [2006] *Intl. Const. L.R.* 306) (Köntges):

"Under normal circumstances it should be in the interest of both parties to a contract to find an early resolution of a problem on site. Unresolved problems create uncertainties and risks to the detriment of both parties. If a contractor has to perform work and prefinance such works without knowing what he will recover in respect of his costs, then this will at the very least demotivate him and the project will suffer accordingly."

It is for these reasons that today there is so much interest in mediation, dispute boards and the use of adjudication similar to that in the UK. This interest will continue to increase as parties to construction projects look for cost-effective and speedy ways to resolve disputes. There is increasingly broad support for ADR (see, for example, "Why

International Dispute Settlement Institutions Should Offer Ad Hoc Dispute Board Rules," Volker Mahnken [2006] *Intl. Const. L.R.* 433 (Mahnken). "The Avoidance of Disputes by Contractors in Design and Construct Contracts," Dr. Donald Charrett [2008] *Intl. Const. L.R.* 427 (advocating adjudication, dispute boards and stop-clock arbitration (at 437)).

Further, the same forces and considerations that drove the creation of these ADR models have now gone to the next level: new contract forms that contain "no dispute" clauses. See, for example:

- "Alliancing in Delivery of Major Infrastructure Projects and Outsourcing Services I Australia—An Overview of Legal Issues" (Andrew Chew [2004] *Intl. Const. L.R.* 319). This references a typical pure alliance contract provision providing "The Project Alliance Participants embrace the fact that one of the prime advantages of alliancing is to avoid disputation and litigation. The contractual structure is designed to reinforce the fact that there are to be no disputes or litigation, the only exception being in the event of Wilful Default by a Project Alliance Participant" (at 340).
- "Pushing the Envelope—The Be Collaborative Contract" (Nicolas Brown [2004] *Intl. Const. L.R.* 153). This notes that since 2000, five partnering contract forms have been released that all "contractualise" partnering, and explains that the Be contract uses the collaborative concept as an explicit reference point in the

dispute resolution clause, providing that the overriding collaborative principle must be taken into account in any award (Article 1.7).

- In the U.S., this trend has led to ConsensusDoc forms (see [www.consensusdocs.org/index.html](http://www.consensusdocs.org/index.html)).

It remains to be seen whether these contracts will find more acceptance, especially in the current market conditions.

The industry has been conscientious in developing ADR processes, and appears to have become more efficient at resolving its disputes. Both Mahnken and Köntges state that the costs of dispute boards are far less than those of arbitration:

- Mahnken states they are about 0.3% to 0.5% on a €100 million (about \$146 million) contract (Mahnken, at 436 to 437).
- Köntges puts them at 2% of contract value, in contrast to 5% for arbitration. (Köntges, at 310).

What is most noticeable about Köntges' article is, however, not his thesis that dispute boards can effectively resolve disputes in a timely and cost effective way, but that of the 22 large and medium international projects he surveys over a six-year period, 15 of those projects had disputes that required an outside party to assist with resolution (Köntges, at 307 to 310).

This amounts to a dispute rate of 68% of projects, occurring even during the good times of 2006.

While it perhaps cannot be said that more effective ADR has encouraged more disputes, there does appear to be a relationship between the fact of

widespread disputes and their resolution by ADR. Bill Smith's study in Australia of construction industry participants is instructive, concluding that "disputes are widespread", "negotiation is by far the preferred method to resolve disputes", and most participants were "not satisfied with the time, cost, process and outcome of the dispute resolution methods they used" ("Scope for Improvement—A Survey of Pressure Points in Australia Construction and Infrastructure Projects," Bill Smith [2007] *Intl. Const. L.R.* 36 at 52).

#### **The Effect of ADR on Arbitration**

The growth of ADR mechanisms in the construction industry, and the cost and time savings behind them, is having an effect on construction arbitration, both domestic and international, and is changing arbitral rules and processes.

International arbitration remains, and is likely to remain, the default choice for deciding international project disputes, due to the UN Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (New York Convention) (at least until more countries decide to sign up to the Hague Convention on Choice of Court Agreements, which allows reciprocal recognition and enforcement of court judgments). However the arbitral process in construction disputes is not immune from the pressures that have spurred ADR development (see Joseph R. Profaizer, International Arbitration: "Now Getting Longer and More Costly," *The National Law Journal*, 29 July 2008, at [www.law.com/jsp/article.jsp?id=1202423321977](http://www.law.com/jsp/article.jsp?id=1202423321977)).

In certain jurisdictions, not least the U.S., domestic construction arbitration has come to be subject to significant critique for being slow and expensive. This critique is so much so that the American Institute of Architects construction forms removed arbitration as the default dispute resolution mechanism in its A201 form in 2007.

International arbitration is also being critiqued. For example, while unlike the courts in the U.S., none of the prominent international arbitral institutions require parties to engage in ADR before commencing arbitration, there have been voices calling for arbitral institutions and arbitrators to be more proactive in ADR processes (Mahnken. Also, "Arbitrator-Directed Arbitration: A Different Approach to ADR," Mark C. Friedlander [2006] *Intl Const. L.R.* 312).

The pressure on arbitral institutions to ensure more cost-, and particularly, time-effective, dispute resolution mechanisms, is being felt in arbitration circles. In "The International-isation of ADR," Donald L. Marston ([2005] *Intl Const. L.R.* 16) observed (at 17) that "The message is clear, business parties are interested in creative new approaches to assist them in avoiding or at least minimizing, disputes."

Arbitral institutions are beginning to respond. The ICC, for example, recently changed its arbitrator disclosure requirements. From 17 August 2009, any nominated arbitrator must complete a "Statement of Acceptance, Availability and Independence, in which the

arbitrator is to confirm that he or she expects to be able to make available the time and effort necessary for prompt and efficient conduct of the case. Arbitrators are also asked to indicate the number of cases in which they are already involved and any foreseeable competing demands upon their time in the following 12–18 months” ([www.iccwbo.org/court/arbitration/index.html?id=32208](http://www.iccwbo.org/court/arbitration/index.html?id=32208)). The aim is not merely to broaden the pool of ICC arbitrators, but to reduce the time it takes to set hearing dates and to issue awards.

This issue is not limited to the ICC. In International Centre for Settlement of Investment Disputes (ICSID) arbitrations, the time period between the end of the proceedings and the issue of awards is lengthy. For example, in *Bayindir v Pakistan* (ICSID Case No. ARB003/29), a case involving the investment rights arising out of termination of a road building contract, the case began on 15 April 2002, the hearing occurred in June 2008, post-hearing briefs were filed on 16 July 2008, and costs information was filed on 26 September 2008 (<http://icsid.worldbank.org/ICSID/FrontServlet>). The tribunal did not “close” the proceedings until nearly a year later on 5 August 2009. The award was issued on 27 August 2009.

In addition, arbitral institutions have adopted rule changes to seek to streamline arbitrations. For example in the U.S., the International Institute for Conflict Prevention and Resolution (CPR) issued rules for expedited arbitration in construction disputes. In the UK, the Society of

Construction Arbitrators has called for 100-day arbitrations ([www.arbitrators-society.org/news/100day.htm](http://www.arbitrators-society.org/news/100day.htm)). The ICC is now reconsidering its rules and it is likely that changes will be made that take into account the issues of timeliness and cost. And, on 1 October 2009 the AAA adopted new construction arbitration rules that further attempt to improve arbitral efficiency.

It may be stated that some in the industry who complain about the issues with arbitration do not take advantage in their contracts “of the many improvements in dispute resolution that are already in place” (see “New Rules for Expedited Construction Arbitration in the USA,” Jesse B. Grove [2007] *Intl. Const. L.R.* 136 at 141). However, the construction industry and the arbitral institutions would do well to see arbitration and ADR as processes that can be complimentary, to the advantage of industry participants and institutions.

### Construction as an Investment Dispute

Another significant trend in international construction disputes in recent years has been to bring disputes on construction projects involving State parties to the ICSID and other fora as “investment” disputes. A review of the ICSID website, searching on simply the word “construction”, reveals 34 cases involving various construction projects including a hotel, fertiliser factory, low-income housing units, airport terminal, highways, dams, office buildings and a mosque. International construction companies have at times constructed

elaborate corporate structures to create vehicles that allow them to obtain rights under Bilateral Investment Treaties (BIT), in order to obtain investment protections. These treaty protections stand separate and apart from any rights under the construction contract, and the disputes concern treaty violations, not contractual breaches.

While ICSID proceedings may provide a means to achieve a hearing outside a party opponent’s national courts, it is no panacea. Consider, for example, *Pantechniki S.A. Contractors & Engineers v Republic of Albania* (ICSID Case No. ARB/07/21, 30 July 2009). The case arose out of a road and bridge project in Albania which the claimant, a Greek contractor, won in an international tender. The contractor and Albania entered into two contracts on International Federation of Consulting Engineers (FIDIC) equivalent forms. The contracts contained an arbitration clause in relation to disputes. The contracts also contained a provision that placed risk of loss due to civil disturbances on Albania’s General Road Directorate.

In 1997 there was severe civil unrest in Albania. As noted by the Tribunal, “Disorder was everywhere” and there was significant looting and destruction of the claimant’s equipment. Work was interrupted on site by several days of rioting and the claimant had to abandon the site. The contractor claimed in May 1997 \$4,893,623.93 (about €3.3 million) in compensation. The resident engineer evaluated the claimant’s damages at \$3,123,199 (about €2.1 million). A special commission created by the

Albanian General Road Directorate further evaluated the claimant's loss at \$1,821,796 (about €1.2 million).

The Albanian Ministry of Public Works informed the Albanian Minister of Finance of the evaluation to pay this sum, but said it did not have funds to do so. The Minister of Finance stated it was not its obligation to pay, and that payment could only be made from a special fund of the Ministers' Council. Rather than invoking arbitration under the contract, the claimant sued in the Albanian courts, apparently after being informed that payment would be made if there was an enforceable court judgment requiring the government to pay. The Albanian court, however, dismissed the case on the basis that the risk of loss provision in the contract created liability without fault. The claimant decided not to pursue the claim to the Albanian Supreme Court and filed for ICSID arbitration.

The ICSID tribunal ruled against the claimant. The tribunal noted that "The Claimant suffered losses which it appeared contractually entitled to recover. The Government negotiated a reduced amount. It then refused to pay on grounds that are difficult to understand. Subsequently, Albanian courts denied the very validity of the underlying contract on equally obscure grounds. The claim does not fail for lack of inherent validity. It rather falters because the Treaty is unavailable to the Claimant in the circumstances."

The decision in *Pantehniki* may signal the start of a trend of retrenchment in which a much

closer scrutiny is taken by investment arbitration tribunals of claims arising out of construction projects. Though unconnected, *Pantehniki* was quickly followed by *Bayindir* (see above), where the ICSID Tribunal denied the contractor's claims for \$494.6 million (about €339 million) on the basis that the claims did not amount to a breach of treaty rights. As such, lawyers advising construction parties on claims may now have to be much more circumspect before recommending that a matter be taken forward as an investment case. Further, while ICSID jurisdiction has recently been granted in *Toto Construzioni Generali S.P.A v. The Republic of Lebanon* (ICSID Case No. ARB/07/12 (September 11, 2009)), that case, relating to a road construction project, contains many of the same construction elements as in *Bayindir*, and will perhaps face the same "it is a contract dispute" defence as asserted in *Bayindir*.

Instructive in this respect is ICC Award No 8677 which related to a Middle East contractor's claim against an Asian state. While mobilising, the contractor's country was invaded by a foreign state and the contractor lost a significant amount of equipment. The Tribunal held: "If a party cannot enforce a contract entitlement over which there is no, or no real, dispute through the arbitral process, there will be cases...in which there is no available remedy" (Extracts from "ICC Arbitral Awards in International Construction Disputes," *ICC Bulletin* Vol 19/No 2 2008 (2009) 71 at 73). The tribunal held for the claimant contractor.

Besides the risk of trying to shoe-horn contractual rights into an investment treaty framework, there are other factors that need to be considered before deciding to eschew contract-based dispute resolution. Investment cases are typically long affairs, with cases continuing often over five years before reaching decisions. In addition, there is a limited degree of ADR in these cases. Further, given that they involve public international law and countries, they play out with a degree of publicity. Also, investor-state cases can involve unrelated parties as amicus. As such, simply following the trend to investor-state arbitration with a construction dispute is not a course to be pursued without a careful balancing.

### Issues When Negotiating and Administering Construction Contracts

While of great importance, it is not the focus of this article to set out the issues that need to be considered when preparing a dispute resolution clause in an international contract. Instead, we highlight three issues:

- The importance of bonds.
- The significance of complying with time clauses.
- Ensuring the proper choice of law clause.

### Increased Importance of Bonds in Today's Construction Market

It is not surprising in the present economy that bonds and other security documents have taken on an increased significance. These documents are now playing a role beyond protecting against bankruptcy, non-payment and default in

performance by both contractors and owners. These bonds and guarantees provide an immediate source of funds with dispute resolution to follow.

Bonds written by compensated sureties rarely provide for immediate payment. Rather, they provide only an ultimate source of funds if the surety's principal is unable to pay and the beneficiary of the bond has taken the steps to perfect its rights. In contrast, a guarantee supported by an irrevocable letter of credit is seen as a readily available source of funds if the principal defaults. However here as elsewhere, the bond/letter of credit approach is not a failsafe.

A recent case in which we have been involved illustrates the point. The contractor provided a performance guarantee of 12.5% of the contract price. The guarantee provided that as a condition precedent to any draw against the guarantee by the owner, the owner would have paid the contractor the final payment milestone under the contract. This was done because it was considered that the performance guarantee should not be tied to payment issues, as it concerned performance of the facility being supplied, and also because the owner should not be able both to refuse payment and call on the guarantee, therefore potentially withholding over 20% of the contract sum. When the owner sought to call on the bond it was met with an injunction preventing the bank from paying against it, pending the outcome of arbitral proceedings.

Generally, the rule has been that first demand bonds are autonomous from

the underlying contract and the guarantor is not a party to the arbitration agreement. As such, as noted by Philip Dunham, arbitration tribunals have often found that they have no jurisdiction over a guarantor. ("The Use and Abuse of First Demand Guarantees in International Projects," Philip Durham [2008] *Intl. Const. L.R.* 273). However, this may change as bonds receive more scrutiny in the present economy and more negotiation, bringing into arbitration more bond issues and requests for arbitral injunctive relief. Certainly, if there is a connection between the bond and the underlying contract, such as where the bond incorporates the contract by reference, then arbitral rights are often found to arise against the guarantor.

In ICC Case No. 3896 the tribunal held that there was a connection between the guarantee and the underlying contract so that it could decide on whether a call on the bond had been abusive. The tribunal also found that the beneficiary's entitlement to receive the money was not absolute but tied to a breach of the underlying contract. It may be that in the current market, with parties more willing to negotiate bond terms, more bond issues will be resolved in the arbitral context.

#### **Time Clauses**

A common anti-arbitration argument, particularly in the U.S., is that arbitration awards are compromised decisions. The evidence from international arbitrations is to the contrary. Arbitrators decide cases based on the facts of the case and the parties' agreements applying the principle of *pacta sunt servanda*. Consistent with this general

approach, the ICC issued construction award extracts in the *ICC Bulletin* (Volume 19 No.2 2008 (2009)) reveal, if nothing else, that arbitrators apply contract terms containing time provisions rigorously (Extracts from "ICC Arbitral Awards in International Construction Disputes," *ICC Bulletin* Vol 19/No 2 2008 (2009) at 71 et seq. See also "International Construction Contract Disputes: Second Commentary on ICC Awards Dealing Primarily with FIDIC Contracts," Christopher R. Seppälä (*ICC Bulletin* Vol 19/No 2 2008 (2009), at 41).

For example, in ICC Case No. 11039 decided in 2002, concerning the *FIDIC White Book 2nd Edition* (1991), a Danish engineering company (Respondent) entered into a contract to provide technical assistance to a German construction company (Claimant) (*ICC Bulletin* Vol 19/No 2 2008 (2009), at 95 to 97). The Claimant filed for arbitration in relation to additional costs it incurred as a result of a bid bust in quantities for which it blamed the Respondent. The parties' agreement had a time bar provision, which provided that neither party would be liable for "any loss or damage" unless "a claim is formally made... before the expiry of the relevant period stated in Part II or such earlier date as may be prescribed by law." Part II set out a one-year period. The tribunal noted: "The reduction [to one year] of the period of limitation agreed to by two business parties with equal bargaining power cannot be deemed unreasonable or create an unreasonable balance between the parties."

As such, the tribunal held the Claimant's claim time barred.

Likewise, in ICC Case 10892 (concerning a sports stadium project in the Caribbean and the *FIDIC Red Book 4th Edition* 1987), the tribunal noted that the owner had violated Clause 63, which provided that: "the Employer may, after giving 14 days notice to the Contractor, enter upon the Site and the Works and terminate the employment of the Contractor..." (*ICC Bulletin* Vol 19/ No 2 2008 (2009), at 91 to 95). The tribunal stated: "Employer gave a 14-day notice of its intent to terminate the Contract (dated October 29, delivered on November 1, and terminated on November 15); but, it did not wait 14 days to enter the premises. Employer obtained an injunction on the date of its notice, ejected Contractor from the site the same day, and seized Contractor's equipment and records for its use" Partly due to this, and also the .absence of an engineer's recommendation to terminate the contractor, the tribunal found that the termination of the contractor was improper.

The compliance with time provisions by the engineer, and its impact on the parties to the contract is also important. At issue in ICC Case 10619 (involving a claim by an Italian contractor under a *FIDIC Red Book 4th Edition* (1987) contract with an African state regarding the construction of roads) was whether the German engineer's issuance of decisions more than the contractual 84 days after the claimant's request for them rendered the decisions void (*ICC Bulletin* Vol 19/No 2 2008 (2009), at 85 to 91). The delay was due to the fact that the principals

were negotiating settlement and the engineer deferred its decisions. The tribunal held in the absence of any evidence at this stage that both parties had, whether in express terms or impliedly, agreed that the engineer was not required to stick to the time condition in Article 67.1. The tribunal ruled the engineer had no authority to depart from the rule.

These cases show that compliance with time clauses is important and can have significant effects on the outcome of arbitral proceedings. Proper compliance with these clauses is even more important in today's market. Parties may be considering contractual action because they have either not received payments for work performed or they are facing a contractor who is having financial difficulty. Care must be taken to review time clauses such as FIDIC's Contract for Major Works, which has a 28 day notice provision for claims (Clause 20.1), and change order time requirements (Clause 61.3, NEC3 Engineering and Construction Contract, giving an eight week period).

Ultimately, time clauses are considered as part of freedom of contract and there is little basis to criticise tribunals for strictly enforcing time clauses. While there are constructive notice arguments that can be made at times, more often than not in international arbitration limited consideration will be granted to parties who fail to comply with specific time provisions of the contract.

In this context, see also "The Rise and Rise of Time Bar Clauses: The

Real Issue for Construction Arbitrators" (Hamish Lal [2007] *Intl. Const. L.R.* 118), stating "Construction arbitrators sitting in domestic and international arbitrations now have a vital role in deciding whether "time bar" clauses are effective as a complete defense to contractor's claims that are not submitted in accordance with express notice provisions."

#### **Choice of Law Clauses**

Differences in the law applicable to a contract can produce radically different results. This is a significant matter and one which is sometimes overlooked. For example, we recently finished an arbitration in a case involving a contract for engineering services in the U.S. where the parties had agreed on a Virginia choice of law clause, stating "This Agreement shall be governed by and construed in accordance with the laws of the Commonwealth of Virginia."

A dispute arose over payments and the other side asserted statutory claims under Maryland law, on the basis that some of the work was done in Maryland. The Maryland statute made a claim for treble damages possible. Under U.S. law, a choice of law clause will be given effect unless it has no "reasonable" relationship to the transaction. Our client had an office in Virginia. Further, if the choice of law clause was invalid, it was not clear that Maryland law applied as the contract provided explicitly that the work was to be performed in Tennessee, and our clients were ultimately based in Alaska. All of these states had different statutory schemes.

At the very least, the case illustrates the need to ensure that a choice of law clause is properly drafted and that it will be enforced as envisioned. This caution applies particularly in the international context. For example, depending on the contract provisions, there are significant choice-of-law issues involved in contracting in the Middle East concerning the enforceability of contract provisions under specific law. See, for example, "Turnkey Contracting Under the ICC Model Contract for Major Projects: A Middle Eastern Law Perspective" (Marwan Sakr, [2009] *Intl. Const. L.R.* 146), noting that some of the provisions of the ICC Model Turnkey Contract for major projects may not be enforceable in certain Arabic legal systems.

Further, contractors who execute different choice of law provisions in the subcontract than those contained in the prime contract can create divergent liability and recovery chains, which cannot be passed along the contractual chain back to back. Where no choice of law is selected in a subcontract agreement, the law of the subcontractor's principal place of business may apply, despite little other nexus to that forum. See "The Subcontractors' Direct Claim in International Business Law" (J. Florian Pulkowski [2004] *Intl. Const. L.R.* 31), and noting that where different laws apply to the prime contract and the subcontract, the law governing the main contract should determine

whether the subcontractor is entitled to bring the right of direct action against the owner (at 55). Note that in U.S. federal contracting the subcontractor has a right to direct action against the owner on a "pass through" basis, under the prime contractor's name.

Further, a lowest common denominator choice of law is not always best. For example, parties sometimes opt for Swiss law on the basis it is neutral. However, while for example this may seem to be a compromise for a Turkish party, be aware that the Turkish commercial code in large measure comes from the Swiss. As such, in that circumstance it is little compromise at all.

### Conclusions

The international construction industry remains one that spawns significant disputes in number and amount at issue. The incidence of such disputes may increase in the near term, due to the fallout from the problems in financial markets. However, construction entities and their advisors have become quite effective at promoting ADR mechanisms to resolve disputes quickly and efficiently.

It remains to be seen whether it will be possible to use these mechanisms effectively in the current economic climate, or whether the disputes will require reliance on the typical dispute resolution of arbitration. However, the rise of ADR is affecting arbitration and generating demand for more efficient, timely and less

expensive processes. The creative adaptations of other ADR approaches are likely to have a substantial impact on dispute resolution. Staying abreast of these developments is important both at the contract drafting stage and when disputes arise. Similarly important in the current economy is looking closely at bond and other guarantees, notice provisions and choice of law, all of which can have a significant impact on project outcomes.

