

---

---

# THE INTERNATIONAL CONSTRUCTION LAW REVIEW

---

---

## CONTENTS

Introduction

---

### Articles

FIDIC's New Standard Forms of Contract—Force Majeure, Claims,  
Disputes and Other Clauses CHRISTOPHER R SEPPALA

---

Correspondents' Reports

---

Book Reviews

---

|L|L|P|

# FIDIC'S NEW STANDARD FORMS OF CONTRACT— FORCE MAJEURE, CLAIMS, DISPUTES AND OTHER CLAUSES

CHRISTOPHER R SEPPALA

*Legal Adviser, FIDIC Task Group for updating the FIDIC International Conditions of Contract, partner, White & Case LLP, Paris*

This article is divided into two parts. Part I discusses FIDIC's three new Books for major works<sup>1</sup> in relation to:

1. Contractor's risk and "Employer's Risk"<sup>2</sup>;
2. indemnities;
3. limitation of liability;
4. the new *force majeure* Clause; and
5. grounds and procedure for termination of the contract by the Employer and the Contractor.

Part II looks at:

1. the new procedures for claims of the Contractor and the Employer;
2. the procedure for the settlement of disputes by the Dispute Adjudication Board (DAB); and
3. very briefly, international arbitration.

## ***Part I: Risks, Force Majeure and Termination***

### CONTRACTOR'S RISK AND "EMPLOYER'S RISK" (ALLOCATION OF RESPONSIBILITY FOR DAMAGE TO THE WORKS) (Sub-Clauses 17.2 to 17.4)

The basic allocation of risk between the Contractor and the Employer for damage to the Works before takeover is dealt with in Sub-Clauses 17.2 to 17.4 of the new Books. The principles are essentially unchanged from those in the old Red and Orange Books. These principles (it will be recalled) are as follows:

1. The Contractor is required to take full responsibility for the care of the Works, materials and Plant from the Commencement Date until the Taking-Over Certificate is issued for the Works.

<sup>1</sup> The new Construction Contract (Conditions of Contract for Construction), Plant Contract (Conditions of Contract for Plant and Design-Build) and EPC Contract (Conditions of Contract for EPC/Turnkey Projects).

<sup>2</sup> The terms used with initial capitals in this article refer to defined terms in the new Books for major works.

2. If any loss or damage happens to the Works or materials and Plant, other than due to "Employer's Risk" (as defined), the Contractor must "rectify" this loss or damage at the Contractor's cost.
3. "Employer's Risks" are generally events or circumstances over which neither party will have any control (e.g. war, hostilities and the like) or events or circumstances caused by the Employer, directly or indirectly.

Under the new Books, the Contractor's responsibility before takeover now extends not merely to the Works, materials and Plant but, in addition, to:

1. "Goods": a new defined term in the new Books—which would include Contractor's Equipment, whether on or off the Site; and
2. "Contractor's Documents": also a new term—which would include computer software and documents of a technical nature supplied by the Contractor.

The Employer's Risks in the new Construction Contract and Plant Contract, which are defined in Sub-Clause 17.3, are similar to those in the old Red and Orange Books:

Employer's Risks	Comment
(a) "war, hostilities (whether war be declared or not), invasion ..."	May happen anywhere in the world, e.g. if a war in Eastern Europe causes losses or damages to the Contractor's Equipment or to Plant for use on a Site in China, then that is an Employer's Risk and the Contractor is entitled to recovery for the same.
(b) "rebellion, terrorism, revolution ...", and (c) "riot, commotion or disorder ...", and (d) "munitions of war, explosive materials, ionising radiation or contamination by radio-activity ..."	These are now all expressly limited to the country of the Works. (Note: "munitions of war" and "explosive materials" are <i>new</i> Employer's Risks since the test editions.)
(e) "pressure waves caused by aircraft ..."	No geographic limit. (Arguably, this could also have been limited to the country of the Works, but this was not done.)
(f) "use or occupation by the Employer ...", and (g) "design ... by the Employer's Personnel ..."	Basically, here talking of fault of the Employer. No geographic limit.
(h) "operation of the forces of nature which is Unforeseeable"	Again, no geographic limit.

The list of the Employer's Risks in the EPC Contract is more limited. It only includes paragraphs (a) through (e). Thus, use or occupation of the Works by the Employer (paragraph (f)), design of the Works by the Employer's Personnel (paragraph (g)) and "Unforeseeable" operations of the forces of nature (paragraph (h)), are not recognised as Employer's Risks in the EPC Contract, in keeping with the risk allocation philosophy of that Book, under which more risk is allocated to the Contractor.

As was the case under the old Red and Orange Books, if the Works suffer loss or damage *due to an Employer's Risk*, the Contractor must rectify this loss or damage to the extent required by the Employer or the Engineer. Where the Employer or the Engineer requires rectification and the Contractor suffers delay and/or incurs additional cost, the Contractor may be entitled to an extension of time and to the cost of rectification (Sub-Clause 17.4).

Where the Contractor rectifies Works which have been lost or damaged as the result of an Employer's Risk, is the Contractor entitled to recover profit in addition to the cost of rectification? In the past, FIDIC has taken different positions on this:

1. Under the old Red Book (Sub-Clause 20.3), the Contractor was entitled in *all* cases of Employer's Risks to "an addition to the Contract Price in accordance with Clause 52", implying he is entitled to profit.
2. However, under the Orange Book (Sub-Clause 17.4), the contractor was entitled in *all* cases only to cost, implying he is *not* entitled to profit.

The new Books take an intermediate position. In general, the Contractor is only entitled to recover his cost, but in the case of paragraph (f) (use or occupation by the Employer), and paragraph (g) (design by the Employer), the Contractor is entitled to "reasonable profit" as well. The theory here is that these are cases where the Employer is, in effect, in breach of contract and, therefore, the Contractor should be entitled to recover his profit, whereas in the other cases the Employer is not at fault and, therefore, there should be some sharing of risk by the Contractor, by his giving up an entitlement to profit.

As paragraphs (f) and (g) are not contained in the list of Employer's Risks in the EPC Contract, the issue of entitlement to profit does not arise at all in relation to that Book.

### INDEMNITIES (Sub-Clause 17.1)

Under the old Red Book, not only was the Contractor responsible for the care of the Works, from the Commencement Date until takeover, but he was also to a certain extent responsible for things that arose out of or as a consequence of his execution of the Works or remedying of any defects therein. Thus, if the Employer were subject to losses or claims for:

- (a) death or injury to any person; or
- (b) loss or damage to any property (other than the Works);

arising out of, or as a consequence of, the performance of the Contractor's duties, the Contractor was required to indemnify the Employer against such claims or losses (Sub-Clause 22.1) subject to certain exceptions (Sub-Clause 22.2). The Orange Book contains a somewhat similar indemnity (Sub-Clause 17.1).

Under the new Books, the Contractor continues to be responsible for losses or claims that arise out of, or as a consequence of, the Contractor's design (if any) and execution of the Works and remedying defects. However, while the Contractor must indemnify the Employer for losses or claims for bodily injury, disease or death of any person, regardless of whether or not the Contractor was negligent (unless positively caused by the Employer or his agents) recognising the Contractor's overriding control over Site operations, the Contractor is only liable to indemnify the Employer for property damage where the Contractor has been negligent or committed a breach of contract (Sub-Clause 17.1(b)).

The policy adopted by FIDIC in the new Books is in line with the policy in the major UK and other standard forms.<sup>3</sup>

#### LIMITATION OF LIABILITY (Sub-Clause 17.6)

There is no Clause providing for limitation of the Contractor's liability in the old Red Book, perhaps because the Contractor would be engaged in little or no design under that Book and, therefore, his exposure to liability was considered more limited. On the other hand, perhaps partly because the design and manufacture of electrical and mechanical works was considered to expose the Contractor to greater risk of liability, the old Yellow Book went to great lengths to limit the Contractor's liability.

The old Yellow Book limited the Contractor's liability in three main 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 Contractor's liability to the sum stated in the contract or, if no sum were stated, the Contract Price (Sub-Clause 42.2); and
3. by expressly excluding the Contractor's liability for defects and other things after the expiry of the Defects Liability Period, as defined, except in the case of Gross Misconduct, as defined (Sub-Clauses 30.12 and 42.3).<sup>4</sup>

Like the Yellow Book, the Orange Book excluded the Contractor's liability

<sup>3</sup> See, *Hudson's Building and Engineering Contracts* (1995), Vol II, p 1437.

<sup>4</sup> The Yellow Book had also provided 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.

for loss of use, loss of profit and indirect or consequential damage, subject to certain exceptions.<sup>5</sup> In addition, like the Yellow Book, the Orange Book placed a specific monetary limit on the Contractor's total liability to the Employer. Such liability was said to be limited to the Contract Price, subject to the same exceptions<sup>6</sup> (Sub-Clause 17.6).

However, like the Red Book and unlike the Yellow Book, the Orange Book did not exclude the Contractor's liability for defects and other things after the expiry of the Defects Liability Period (after the "Contract Period" in the Orange Book). Consequently, the Contractor would remain liable for defects until expiry of the relevant statute of limitations.

### **What has changed now in the new Books for major works?**

First, there is now a provision (Sub-Clause 17.6) limiting the Contractor's liability in *all* the new books, including the new Construction Contract. Like the Orange Book Clause, the new Clause:

1. excludes the Contractor's (and Employer's) liability for, among other things, loss of use of the Works, loss of profit, loss of any contract and for indirect or consequential damage which may be suffered by the other party; and
2. places a monetary limit on the Contractor's total liability subject to certain exceptions.

The second change is that, unlike the Orange Book, the new Clause does not specify, propose or recommend any particular monetary limit on the Contractor's liability in the General Conditions. It was not deemed to be desirable to put a limit in the General Conditions, as the limit which might be appropriate would vary widely depending, among other things, on the nature and importance of the Works to be constructed, the risks involved and the extent of the Contractor's obligations, e.g. whether he is designing the Works on a turnkey basis or not. Accordingly, the General Conditions now provide, like the old Yellow Book, that only if nothing is said in the Particular Conditions about the amount of this limit will the limit be effectively the "Contract Price" or, in the new Plant and EPC Contracts, the "Accepted Contract Amount".

The third change (from the Orange Book) is that liquidated damages for

<sup>5</sup> See Sub-Clause 17.6. These exceptions to the exclusion of the Contractor's liability included:

- (a) electricity, water, gas and other services purchased from the Employer (Sub-Clause 4.19);
- (b) charges for machinery and equipment supplied by the Employer (Sub-Clause 4.20);
- (c) the Contractor's indemnification of the Employer for infringement of industrial propriety rights (Sub-Clause 5.9);
- (d) liquidated damages for delay (Sub-Clause 8.6); and
- (e) liquidated damages for failure to pass tests after completion (Sub-Clause 11.4).

In addition, the Contractor's liability was said not to be excluded in the case of fraud, wilful misconduct or illegal or unlawful acts, nor in certain other cases (where the contract "impose(s) a greater liability" or in cases of acts "contrary to the most elementary rules of diligence ...").

<sup>6</sup> See footnote 8.

delay and liquidated damages for failing to pass tests after completion are no longer excluded from the liability cap or limit. On the other hand, the Contractor's general indemnification of the Employer (Sub-Clause 17.1) is now excluded, just as the Contractor's indemnification of the Employer for infringement of intellectual and industrial property rights (Sub-Clause 17.5) is excluded, as was the case in the Orange Book (Sub-Clause 17.6).

The only other qualification on the provision in the new Books limiting the Contractor's liability is that it will not apply:

"in any case of fraud, deliberate default or reckless misconduct by the defaulting party."

Finally, it should be noted that, like the earlier Books (except the old Yellow Book), none of the new Books excludes the Contractor's liability for defects after the Defect Notification Period. On the contrary, they provide that the Contractor's liability for defects shall continue (see Sub-Clause 11.10).

Therefore, the Contractor will remain liable for defects for the period of the relevant statute of limitation unless he can negotiate a limit on his liability in the case of a given contract.

### THE NEW FORCE MAJEURE CLAUSE AND RELEASE FROM PERFORMANCE (Clause 19)

A *force majeure* Clause is an increasingly common feature of international contracts. Typically, under such a Clause, where a party has been prevented from performing a contract by an event beyond its control, it will be excused for its delay in performing the contract, or, in an extreme case, it may be excused from having to perform the contract at all. In some cases, such party can recover any additional costs it had incurred as the result of the *force majeure* event as well.

In keeping with international practice, a *force majeure* Clause, Clause 19, has now been introduced into all of the new Books for major works.

While the old Red Book contained no *force majeure* Clause, as such, by virtue of a combination of Clause 44, dealing with extensions of time, and Clause 65, dealing with Special Risks (including war), the Contractor had, under the old Red Book, some of the relief (at least) provided by a typical *force majeure* Clause.

Both the old Yellow Book (Clause 44) and the Orange Book (Clause 19) contain a *force majeure* Clause. While the *force majeure* Clause in the Yellow Book seems satisfactory, in this author's view, the *force majeure* Clause in the Orange Book is deficient:

1. Under the Orange Book, to constitute *force majeure*, the event must be "impossible or illegal", which is much too restrictive. If an event must

be either impossible or illegal, there are very few circumstances in which the *force majeure* Clause in the Orange Book can apply.

It is only if one interprets the word "impossible" in the Orange Book broadly to refer to what is *commercially* impossible (e.g. cases where the cost of doing the work has increased by a multiple of 10 or 12 or where labour or materials have become extraordinarily scarce) that this Clause can really provide practical relief. But as Clause 19 of the Orange Book does not refer to what is *commercially* impossible but only to what is "impossible", this may imply something absolutely impossible.

2. A related problem is that Sub-Clauses 19.3 and 19.4 of the Orange Book provide that where an event occurs which either the Contractor or the Employer considers to constitute *force majeure*, the Employer or the Contractor "shall endeavour to continue to perform [their] obligations as far as reasonably practical". However, as performance of their obligations had (under the Orange Book) to be "illegal or impossible" to constitute *force majeure*, it was not clear how the Employer and the Contractor could be expected to continue to perform their obligations "as far as reasonably practical" when, obviously, they could not be expected to do something illegal or impossible.

Sub-Clauses 19.3 and 19.4 of the Orange Book only appear to be understandable in this respect in cases of *partial* illegality or impossibility, that is, where a party can perform some, but not all, of his obligations.

In the *force majeure* Clause in the new Books (Clause 19), a solution has been sought to overcome these difficulties. The new Clause may be broken down into the following parts:

- i. a relatively broad definition of "*force majeure*" (Sub-Clause 19.1);
- ii. *force majeure* must "prevent" a party from performing "any of" its obligations (thereby expressly acknowledging the possibility of *partial force majeure*) (Sub-Clause 19.2);
- iii. when this happens, the party affected must give notice within 14 days after the party became aware, or should have become aware, of the event or circumstance said to constitute *force majeure* (otherwise, the party may have no right to claim *force majeure*) (Sub-Clause 19.2);
- iv. where any *force majeure* Clause in a sub-contract gives relief on broader grounds than those provided for under Clause 19,<sup>7</sup> these broader grounds will not afford the Contractor relief under Clause 19 (Sub-Clause 19.5);

<sup>7</sup> Where *force majeure* (as defined in Sub-Clause 19.1) affects a subcontractor of the Contractor, this would normally be interpreted as affecting the Contractor as well, see Duncan Wallace, *Construction Contracts: Principles and Policies in Tort and Contract* (1996), Sweet & Maxwell, London, Vol 2, pp 425–429.



- v. where the Contractor is prevented from performing any obligations by *force majeure*, it may claim an extension of time and, in the case of war and related risks (Sub-Clause 19.1 (i) to (iv)), its additional costs arising "by reason of such *force majeure*" (Sub-Clause 19.4);
- vi. if execution of substantially all the Works in progress is prevented for a continuous period of 84 days, or for multiple periods which total more than 140 days, by *force majeure*, either party may, after notice to the other, terminate the contract, in which event the Contractor will be paid for work done only (Sub-Clause 19.6); and
- vii. a party must give notice when it ceases to be affected by *force majeure* (Sub-Clause 19.3).

The *force majeure* Clause further provides (Sub-Clause 19.7) that notwithstanding any other provision of the contract (including Sub-Clauses 19.1 to 19.6), if performance of the contract becomes illegal (e.g. as may happen should the site become a war zone) or impossible (e.g. as may happen where the site is totally destroyed by an earthquake or flood), or the parties are released from performance under the applicable law (e.g. under the common law doctrine of frustration or the civil law doctrine of *force majeure* as provided for in the applicable civil code),<sup>8</sup> then upon notice by either party to the other party, the parties are discharged from further performance of the contract, implying that the contract comes to an end forthwith. It is unnecessary to wait 84 days. Where the contract is terminated on this basis, the Contractor is paid the same amount as he would be paid if the contract were terminated for *force majeure* (as defined in Sub-Clause 19.1).

#### GROUND AND PROCEDURE FOR TERMINATION OF THE CONTRACT BY THE EMPLOYER AND THE CONTRACTOR (Clauses 15 and 16)

Following the pattern established by the Orange Book, the new Books for major works contain a Clause 15 dealing with "Termination by the Employer" (referred to in the Orange Book as "Default of Employer") and a Clause 16 dealing with "Suspension and Termination by Contractor" (referred to in the Orange Book as "Default by Employer"). Essentially, these Clauses set out the grounds which will entitle the Employer to terminate the contract or entitle the Contractor to suspend or terminate the contract.

<sup>8</sup> *Force majeure* as it may be provided for in the civil code of a civil law country is to be clearly distinguished from *force majeure* as it may be provided for in a *force majeure* clause drafted by parties for inclusion in a given contract. *Force majeure* as provided for in the civil code of a civil law country will almost invariably be much narrower in scope than *force majeure* as defined in the *force majeure* clause of a given contract. Indeed, *force majeure* as provided for in, for example, the French Civil Code is far narrower in scope than the doctrine of frustration under English law, see Nicholas, *The French Law of Contract*, 2nd edn (1992), Clarendon Press, Oxford, p 202.

### Termination by the Employer (Clause 15)

Both the old Red Book (Clause 63) and the old Yellow Book (Clause 45) contain provisions allowing the Employer to terminate the contract (or, in the case of the Red Book, to terminate "the employment of the Contractor") in the case of specified defaults by the Contractor, e.g. acts of bankruptcy, repudiation or where the Contractor without reasonable excuse fails to proceed with the works (Clause 63 of the Red Book). But in the Orange Book, an additional ground for termination was introduced. Sub-Clause 2.4 of the Orange Book provided that the Employer could terminate the contract at any time for the Employer's convenience upon 56 days prior notice to the Contractor. If the Employer did so, the Contractor would be paid for work done under Sub-Clause 19.6. The Contractor would not be paid the profit of which he would be deprived on the balance of the contract which he could no longer complete.

In order to ensure that this Clause was not abused by Employers, who might otherwise terminate a contract early merely in order to arrange for the work to be done by someone else at less cost, Sub-Clause 2.4 in the Orange Book provided that, after termination, the Works could not be recommended for a period of six years without the Contractor's consent.

Like the earlier Books, the three new Books for major works provide that the Employer may "terminate the Contract" for specified defaults by the Contractor (Sub-Clause 15.2). Unlike the old Red Book (Sub-Clause 63.1) and Orange Book (Sub-Clause 15.2), the Employer no longer terminates the "employment of the Contractor" but terminates the contract.

As will be recalled, under the old Red Book, where the Contractor had committed an event of default, the Employer had to give 14 days notice before he could "terminate the Contractor's employment" (Sub-Clause 63.1). While the same notice period generally applies under the new Books, it is also provided there that the Employer may terminate the contract "immediately" in a case where the Contractor becomes bankrupt or commits bribery (Sub-Clause 15.2). No prior notice is required.

In addition, a "termination for convenience" Clause has now been introduced into all the new Books for major works, except that now, more logically, it is to be found at the end of the contract, near the other termination provisions, in Sub-Clause 15.5, and not in Sub-Clause 2.4, as in the Orange Book.

This termination for convenience Clause is basically the same as the Orange Book Clause, except that instead of barring the Employer from engaging another contractor from doing the work for six years, it simply 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."

As with the Orange Book Clause, in the case of a termination for convenience, the Contractor is only entitled to be paid for work done and is

not entitled to his profit on the balance of the contract of which he is deprived of the right to complete.

### **Suspension or termination by the Contractor (Clause 16)**

The fourth edition of the Red Book was the first FIDIC form to provide that where the Contractor was not being paid amounts to which he was entitled (e.g. certified amounts) in due time, he had the right to suspend work or reduce the rate of his work. A provision to this effect is contained in Sub-Clause 69.4 of the (old) Red Book and Sub-Clause 16.1 of the Orange Book.

This was an excellent addition as, without it, at least in many common law countries, it was unclear what the Contractor could do when he was not being paid amounts to which he was clearly entitled. He usually had only two alternatives:

1. to continue working; or
2. if the non-payment was serious enough to justify termination of the contract, then, to terminate the contract;

and, in either case, to invoke the disputes Clause and, if necessary, begin arbitration. In common law countries, at least, if the Contractor was not being paid, he normally had no right to slow down or suspend work.<sup>9</sup> If he slowed down or suspended work, the Contractor would himself be in breach of contract, in which case the Employer might be justified in terminating the contract for breach.

Accordingly, at least in the common law countries, the introduction of this suspension provision provided the Contractor with a valuable remedy when he was not being paid.

The new Books have improved on this situation still more. The new Clause—Sub-Clause 16.1—provides that the Contractor may suspend work not only where the Employer fails, for example, to pay a certificate<sup>10</sup> but also:

1. in the case of the new Construction Contract, where the Engineer fails to certify a payment certificate when he should do so; and
2. where the Employer fails to provide reasonable evidence that financial arrangements have been made and are being maintained to enable the Employer to pay the Contract Price in accordance with the contract payment schedule (Sub-Clauses 16.1, 14.6 and 2.4).

These are, it seems, two very desirable additions in the new Books.

<sup>9</sup> In Civil Law countries, by virtue of the doctrine known in French law as *l'exception d'inexécution* (or *exceptio non adimpleti contractus*), the situation would be different although, even in Civil Law countries, this doctrine would not necessarily apply in the case of an "administrative" contract, such as a contract with the State or other public body.

<sup>10</sup> Under Sub-Clause 14.7 of the Construction Contract.

The new Books also add these two points as further grounds for termination of the contract by the Contractor. Thus, Sub-Clause 16.2 provides that the Contractor may terminate the contract:

1. where the Contractor does not receive reasonable evidence of the Employer's financial arrangements within 42 days after giving a notice to suspend on this account; and
2. in the case of the new Construction Contract, where the Engineer fails, within 56 days after receiving a payment application and supporting documents, to issue the relevant payment certificate.

FIDIC has been criticised in the past for not acknowledging, in its contracts, the situation where the Engineer himself fails to perform his duty and, therefore, for not providing the Contractor with a remedy in this situation.

In Clause 16, FIDIC has, to its credit, gone some way to redress this situation.

Under the old Red Book, where the Employer had committed an event of default, the Contractor had always to give 14 days' notice before he could terminate his "employment" (Sub-Clause 69.1). While the same notice period continues generally to apply under the new Books, nevertheless the Contractor may now terminate the contract immediately, in the case of an act of bankruptcy of the Employer<sup>11</sup> or a prolonged suspension ordered by the Employer (Sub-Clause 16.2). There is no reason why the Contractor should have to wait for a notice period to expire before being able to terminate in these two circumstances.

## *Part II: Claims, Resolution of Disputes and the Dispute Adjudication Board*

### THE NEW PROCEDURES FOR CLAIMS OF THE CONTRACTOR AND THE EMPLOYER (Sub-Clauses 20.1 and 2.5)

Both the old Red Book (Clause 53) and the Orange Book (Clause 20.1) contain special Clauses dealing with the procedure for claims by the Contractor.<sup>12</sup>

In the new Books for major works, the Sub-Clause dealing with Contractor's claims (Sub-Clause 20.1) is more developed and detailed than in the old Red Book and Orange Book. Not only does this Sub-Clause regulate claims for additional payment, as in the past, but it also very sensibly regulates claims for extension of time, as there appeared no good reason not to have the same procedure apply to claims for time and claims for money.

<sup>11</sup> Subject, like all provisions of the contract, to the mandatory requirements, if any, of applicable law.

<sup>12</sup> See C Seppala, "Contractor's Claims Under The FIDIC Civil Engineering Contract", 4th edn (1987) in Vol 19 of the *International Business Lawyer* at 395 and 457 (September and October 1991).

In addition, for the first time, a new Sub-Clause has been introduced dealing with the procedure which is to apply to Employer's claims (Sub-Clause 2.5).

There follows a discussion of these two Sub-Clauses: first, Sub-Clause 20.1 dealing with Contractor's claims and, second, Sub-Clause 2.5 dealing with Employer's claims.

### **Claims of the Contractor (Sub-Clause 20.1)**

Basically, in the case of Contractor's claims, the new Sub-Clause (Sub-Clause 20.1) provides for the following procedure:

1. If the Contractor considers himself to be entitled to an extension of the Time for Completion and/or additional payment under any Clause of the Conditions or otherwise, the Contractor must give notice to the Engineer or the Employer (depending on the contract concerned) as soon as practicable and "not later than 28 days after the Contractor became aware, or should have become aware, of the event or circumstance" giving rise to the claim.  
If the Contractor fails to do so, the Time for Completion will not be extended and the Contractor shall not be entitled to additional payment (Sub-Clause 20.1).  
A similar sanction was contained in the Orange Book where the Contractor failed to give a notice of a claim for additional payment (Sub-Clause 20.1). On the other hand, under the Red Book, where the Contractor failed to comply with the provisions for notices of claim the Contractor's entitlement to payment was limited to the amount which could be verified by contemporary records (Sub-Clause 53.4).
2. When the Contractor gives such a notice under the new Sub-Clause, he is required, as in the case of the old Red Book and Orange Book, to keep such contemporary records as may be necessary to substantiate his claim and the Engineer or Employer (depending on the contract) is authorised to monitor the Contractor's record-keeping and/or instruct the Contractor to keep additional contemporary records (Sub-Clause 20.1).
3. Within 42 days after the Contractor became aware, or should have become aware, of the event or circumstance giving rise to the claim (or within such other period as the Engineer or Employer may approve), the Contractor is required to send to the Engineer or Employer a fully detailed claim which includes full supporting particulars of the basis of the claim and of the extension of time and/or additional payment claimed. If the event or circumstance giving rise to the claim has a continuing effect, further procedures need to be complied with (see Sub-Clause 20.1(a), (b) and (c)).
4. Within 42 days after receiving a claim or any further particulars supporting a previous claim, or within such other period as may be

proposed by the Engineer or the Employer and approved by the Contractor, the Engineer or Employer *must* respond "with approval, or with disapproval and detailed comments". He may also request any necessary further particulars "but shall nevertheless give his response on the principles of the claim within such time".

This is the first time a FIDIC contract has required the Engineer or the Employer to respond to the claim of a Contractor within a given time period.

5. The requirements of Sub-Clause 20.1 are expressly stated to be "in addition to those of any other Sub-Clause which may apply to a claim". Thus, the Contractor must comply with the claims procedure provided for in Sub-Clause 20.1 in addition to the requirements of any other Clause in the contract which the Contractor may be relying upon to assert a claim.
6. Sub-Clause 20.1 further provides that:

"If the Contractor fails to comply with this or another Sub-Clause in relation to any claim, any extension of time and/or additional payment shall take account of the extent (if any) to which the failure has prevented or prejudiced proper investigation of the claim ..." [emphasis added].

This (point 6 above) is a relaxation of the requirement in the test editions. The test editions had provided that, if the Contractor had failed to comply with Sub-Clause 20.1, the Time for Completion would not be extended and the Contractor would not be entitled to additional payment.

After much reflection, the conclusion of the FIDIC Task Group was that there must be a notice of claim within 28 days for there to be a valid claim. If a Contractor has a claim for additional money or time, an Employer is entitled to know about this with reasonable promptness. Twenty-eight (28) days appeared to be a reasonable period. Most Contractors who work on international projects are large companies having a staff that is fully capable of recognising a claim situation when it arises. Consequently, if the Contractor indeed has a *bona fide* claim, there would seem to be no good reason why an experienced Contractor should not be required, under pain of forfeiture, to give a notice of claim within 28 days (or four weeks) of the event or circumstance giving rise to the claim.

It should be emphasised that the Contractor has merely to give a bare notice of claim within 28 days. This means that the Employer must be put on notice that he may have to pay the Contractor additional money or grant him an extension of time by reason of a specified event or circumstance: a one- or two-sentence letter from the Contractor may do. There is no need for the Contractor to provide particulars within 28 days.

On the other hand, it appeared to the Task Group to be less essential for the Contractor to have to comply with the other claim procedures in Sub-Clause 20.1 and elsewhere in the Contract. Therefore, a failure of the Contractor to comply with these should not be fatal to the claim. Rather, if the Contractor failed to comply with these procedures, the Contractor's

claim should be reduced by the damage, if any, which this may have caused to the Employer. This was the rationale for the new final paragraph of Sub-Clause 20.1 which provides that:

"If the Contractor fails to comply with this or another Sub-Clause in relation to any claim, any extension of time and/or additional payment shall take account of the extent (if any) to which the failure has prevented or prejudiced proper investigation of the claim. ..."

### **Claims of the Employer (Sub-Clause 2.5)**

As mentioned above, not only do the new Books provide a procedure that applies to Contractor's claims, they also provide one that applies to Employer's claims. The procedure for Employer's claims is to be found in Sub-Clause 2.5. Sub-Clause 2.5 of the new Construction Contract provides that:

"If the Employer considers himself to be entitled to any payment under any Clause of these Conditions or otherwise . . . , and/or to any extension of the Defects Notification Period, the Employer or the Engineer shall give notice and particulars to the Contractor."

The Sub-Clause requires the Employer to give notice of his claim "as soon as practicable" and a notice relating to the extension of the Defects Notification Period must be given before the expiry of such period (which period will normally be one year).

The particulars (given in the notice) must specify the Clause or other basis of the claim and include substantiation of the amount and/or extension to which the Employer considers himself to be entitled. The Engineer (or the Employer himself) is then required to proceed to make a "fair" determination on the Employer's claim under Sub-Clause 3.5. It is expressly provided that any amount due to the Employer may be included as a deduction in the Contract Price and Payment Certificates (Sub-Clause 2.5, last paragraph).

It is now clear in the definitive Books—this was not clear in the test editions—that the Employer may only set off against or make any deduction from an amount certified in a Payment Certificate, or otherwise claim against the Contractor, by complying with the procedure laid down in Sub-Clause 2.5 (see that last sentence of Sub-Clause 2.5). This is the first time that the FIDIC contracts have explicitly protected the Contractor against such unilateral actions by the Employer.

### **THE DISPUTE ADJUDICATION BOARD<sup>13</sup> (Clause 20)**

The old Red and Yellow Books provided for administration of the contract by the Engineer, who was required to act impartially. They also required that disputes be referred to the Engineer for decision, as a precondition to arbitration.

<sup>13</sup> See, C Seppala, "The New FIDIC Provision for a Dispute Adjudication Board" [1997] ICLR 443.

However, in the Orange Book, published in 1995, there was no longer an Engineer, only an Employer's Representative. Under the Orange Book, disputes had to be referred to an independent dispute adjudication board or "DAB" as a precondition to arbitration. In 1996 and 1997, FIDIC published Supplements to the Red and Yellow Books in which provision was made for a DAB to be available to replace the Engineer in determining disputes under those contracts.

Under the General Conditions of all of the new Books, provision is made for disputes to be adjudicated by a DAB. However, the particular conditions of the new Construction and Plant Contracts, which provide that they will be administered by an Engineer, offer the option for the Engineer to act as the DAB. In the EPC Contract, there is no Engineer. Therefore disputes under that Book must be handled by a specially appointed DAB.

The system of a DAB, which is advocated by FIDIC, should be distinguished from the Dispute Review Board ("DRB") advocated by the World Bank. The basic difference between the two systems is that the DAB renders a decision that is immediately binding on the parties whether one of them is dissatisfied with the decision or not. On the other hand, the DRB or Dispute Review Board merely issues a recommendation and, if a party is dissatisfied with the recommendation, he is not under any obligation to implement that recommendation.

### **Standing versus ad hoc DAB**

In the case of the test editions, all three Books had provided that disputes had to be referred to a standing DAB. The DAB was a standing board in the sense that it would be formed at the signature of the contract and would remain in place continuously until the works had been completed. Typically, this would mean that the DAB would be in place for a period of years, the exact length depending on the duration of the particular project.

However, upon reflection, the FIDIC Task Group concluded that, at least in the case of the new Plant and EPC Contracts, it would be more appropriate (and, probably, less expensive for the parties) to provide in the General Conditions for an *ad hoc* DAB, that is, a DAB which would only need to be constituted if and when a dispute or disputes arise(s) and which would normally cease to operate once a decision on such dispute or disputes had been issued. The main reason for a standing DAB is to deal with disputes on or related to the construction site. But, when the contract provides mainly for the design and manufacture of electrical or mechanical equipment in a factory rather than construction work on the site (as is true of many projects for which the new Plant and EPC Contracts would be used), the incidence of disputes should be much less and, hence, it is much more difficult to justify the time and expense of maintaining a standing DAB in such a case. Accordingly, FIDIC has opted for an *ad hoc* DAB in the General Conditions for these types of contracts.

An *ad hoc* DAB, which is only appointed when a dispute arises, also has the



advantage of allowing the parties the possibility of choosing an expert or experts with particular expertise in the area of the dispute or disputes which have arisen. This advantage would not be available in the case of a standing DAB.

However, where a Plant or EPC Contract is used for a project that will involve a lot of construction work on site, then the Guidance Notes in the new Books provide that a standing DAB may be more appropriate instead of an *ad hoc* DAB as provided for in the General Conditions of those contracts.

Under the new Books, a standing DAB, is now only provided for in the General Conditions of the Construction Contract. A standing DAB appears more justified in a contract for civil engineering works as, in the case of such a contract, there would normally be work on site (with the attendant risks this typically will involve) from the Commencement Date (or shortly thereafter) until at least Takeover.

However, again, where the new Construction Contract is used for a project that will involve more equipment supply than construction work on site, the new Construction Contract provides that an *ad hoc* DAB may be more appropriate instead of a standing DAB as provided for in the General Conditions of the Construction Contract.

### **Formation and Remuneration of DAB**

The number of members of the DAB may be one or three. Whether one or three persons are preferable will depend, among other things, on the size of the project, its duration and the field or fields of expertise likely to be required. Where the estimated Contract Price exceeds US\$ 25 million, FIDIC suggests three members.

As a general rule, the members should be engineers or other construction professionals with experience in the type of work involved and in the interpretation of contract documents. However, members may include lawyers e.g. the Chairman of the "Panel" used for the settlement of disputes under the Channel Tunnel contract was a lawyer.

Whether the number is one or three, each member should ordinarily be agreed by both parties. The purpose of this requirement is to ensure that the entire Board has the confidence of the parties.

Each member must be and remain throughout the contract period independent of the parties and, when called upon to make a decision, is required to act impartially.

The Employer and the Contractor are each responsible for one-half of the DAB's remuneration. However, in the interests of efficient administration, the DAB members are required to submit their invoices to the Contractor for payment who will then recover half the cost from the Employer through the payment provisions of the contract.

In the case of a standing DAB, the DAB is required to be kept regularly informed of the progress of the Works and to visit the site regularly e.g. at least three times in any year. The Employer and the Contractor must provide

each member of the DAB with a copy of all contract documents and papers that he may request.

The DAB has wide discretion as to how it should proceed in arriving at a decision. The DAB would normally be expected to conduct a hearing and may request written submissions from both parties prior to the hearing. Subject to the time restrictions within which it is required to operate, the DAB should ensure that each party has a reasonable opportunity to present its case in relation to the dispute referred to the DAB for decision. The DAB's decision should set out briefly the matter in dispute, the relevant facts, the principles (including contractual provisions) to be applied and the basis for its decision.

### Settlement of disputes by the DAB

In the case of an *ad hoc* DAB, as provided for under the new Plant and EPC Contracts, the sequence of events in the procedure for the settlement of disputes is as follows:

1. A Party gives notice of its intention to refer a dispute to the DAB (Sub-Clause 20.2);
2. Within 28 days thereafter, the parties must jointly appoint a DAB (Sub-Clause 20.2).

If the parties fail to do so, then the procedure for appointing a DAB where there has been a default applies (Sub-Clause 20.3) in order to permit the DAB to be constituted;

3. After a DAB has been appointed, a party may refer a dispute to the DAB for its decision. The DAB has 84 days in which to give its decision which must be reasoned and is binding on the parties. If a party is dissatisfied with the decision it must give a notice of dissatisfaction to the other party within 28 days after receiving the decision (Sub-Clause 20.4);
4. Where either party has given such a notice of dissatisfaction, the parties are required to attempt to settle the dispute amicably for 56 days (Sub-Clause 20.5); and
5. After the expiration of such 56 day period (and assuming no amicable settlement), each party is free to initiate arbitration as to the specific dispute (Sub-Clause 20.6).

As mentioned above, in the case of the Construction Contract, the DAB is a standing or permanent one. In this case, the DAB must be jointly appointed by the parties within 28 days of the Commencement Date. If the parties fail to do so, then the procedure for appointing a DAB where there has been a default applies (Sub-Clause 20.3) in order that the DAB can be constituted.

Once the standing DAB is in place, the procedure for the referral of disputes to the DAB, for the DAB to settle them and for requiring arbitration, is basically the same as for an *ad hoc* DAB described above.