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ROLES AND RELATIONSHIPS WITHIN THE PROJECT: THE EMPLOYER

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THE FIDIC CONTRACTS CONFERENCE 2007

Introduction

1. The purpose of this paper is to provide a brief introduction to the FIDIC form of contract and then concentrate on three key parts of the FIDIC form from the employer's point of view, namely making claims, payment and termination.[1]

2. The Fédération Internationale des Ingénieurs-Conseils ("FIDIC") organisation was founded in 1913 by France, Belgium and Switzerland. The UK did not join until 1949. The first edition of the *Conditions of Contract (International) for Works of Civil Engineering Construction* was published in August 1957. A number of contract revisions and additions followed. This paper will concentrate on the most recent suite of contracts issued in 1999, primarily the Red Book.[2]

3. These contracts arose out of the task force established by FIDIC in 1994 to update their contracts in the light of developments in the international construction industry. The key considerations included:

   (i) The role of the engineer and in particular the requirement to act impartially in the circumstances of being employed and paid by the employer;

   (ii) The desirability for the standardisation of the FIDIC forms;

   (iii) The simplification of the FIDIC forms in light of the fact that the FIDIC conditions were issued in English but in very many instances were being utilised by those whose language background was other than English; and

   (iv) That the new books would be suitable for use in both common law and civil law jurisdictions.

4. This led to the publication of four new contracts in 1999:

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[1] Inevitably these are matters which will form part of the discussion throughout the whole day.
[2] Although this talk concentrates on the new FIDIC forms, it should be remembered that the FIDIC 4th Edition ("The Old Red Book") remains the contract of choice throughout much of the Middle East, particularly the UAE.

(i) Conditions of Contract for Construction for Building and Engineering Works Designed by the Employer: The Construction Contract (the new Red Book);

(ii) Conditions of Contract for Plant and Design-Build for Electrical and Mechanical Plant and for Building and Engineering Works, Designed by the Contractor: The Plant and Design/Build Contract (the new Yellow Book);

(iii) Conditions of Contract for EPC/Turnkey Projects: the EPC Turnkey Contract (the Silver Book); and

(iv) A short form of contract (the Green Book).

5. In keeping with the desire for standardisation, each of the new books includes General Conditions (numbering 20 in total they are perhaps best viewed as chapters covering the key project topics), together with guidance for the preparation of the Particular Conditions, and a Letter of Tender, Contract Agreement and Dispute Adjudication Agreements. Whilst the Red Book refers to works designed by the employer, it is appropriate for use where the works include some contractor-designed works whether civil, mechanical, electrical or construction work.

6. There have been two additional developments. The first was the development of an alternative version of the Red Book. This MDB version of the FIDIC Red Book evolved out of the fact that the word's banking community tended to adopt the FIDIC Conditions as part of their standard bidding documents. However, when doing this, the banks also introduced their own amendments. There were inevitable differences between these amendments and the banks realised there would be a benefit in having their own uniform conditions. This has resulted in a "harmonised edition" which was the product of preparation by the FIDIC Contracts Committee and by a group of participating banks.[3] The first harmonised edition of the 1999 Conditions was published in May 2005, only to be amended in March 2006. The clear aim is that all MDB-funded contracts will incorporate these amendments.

7. Second, on 13 September 2007, in Singapore, FIDIC launched their new DBO[4] form of contract.[5] The FIDIC DBO form has arisen out of recognition that for concession contracts in the transport and water/waste sectors, the market typically uses the existing FIDIC Yellow Book with operations and maintenance obligations tacked on. FIDIC has recognised that this is unsatisfactory and in a similar way with some of the contractual developments described above, in order to achieve uniformity and therefore a higher degree of certainty, the new form has been prepared to meet the demand. FIDIC therefore has adopted a different approach to that of the NEC who adopt a "One Size Fit's All" philosophy.

8. The DBO approach to contracting combines design, construction, and long-term operation and maintenance of a facility into one single contract awarded to a single contractor (who will

[3] The banks involved were the African Development Bank, Asian Development Bank, Black Sea Trade and Development Bank, Caribbean Development Bank, European Bank for Reconstruction and Development, Inter-American Development Bank, International Bank for Reconstruction and Development (the World Bank), Islamic Bank for Development, Nordic Development Fund.
[4] DBO meaning design-build-operate
[5] Or the Gold Book

usually be a joint venture or consortium containing all the skills required by the particular DBO arrangement).

9. The new contract will mirror the existing forms in that again it will only have 20 clauses. The three key factors that were taken into consideration in the drafting of the new form were:

   (i) Time – possibilities to overlap of some design and build activities;

   (ii) Cost – cost restraints, commitments, and other risks carried by the contractor; and

   (iii) Quality – as the contractor is responsible for 20 years' operation, it is in his interest to design and build quality plant with low operation and maintenance costs.

10. Given the increasing sophistication of the construction industry, it seems likely that this new DBO form will not be the last new FIDIC form.

Making a claim under the FIDIC form – the employer

11. The ability to make claims under any contract is always an area that requires careful consideration. Under the FIDIC form, it is noticeable that the Employer and Contractor are treated very differently.

Introduction – the claims mechanism

12. Sub-clause 2.5 of the FIDIC Conditions of Contract for Construction[6] provides that:

> *If the Employer considers himself to be entitled to any payment under any Clause of these Conditions or otherwise in connection with the Contract, and/or to any extension of the Defects Notification Period, the Employer or the Engineer shall give notice and particulars to the Contractor. However, notice is not required for payments due under Sub-Clause 4.19 [Electricity, Water and Gas], under Sub-Clause 4.20 [Employer's Equipment and Free-Issue Material], or for other services requested by the Contractor.*
>
> *The notice shall be given as soon as practicable after the Employer became aware of the event or circumstances giving rise to the claim. A notice relating to any extension of the Defects Notification Period shall be given before the expiry of such period.*
>
> *The particulars shall specify the Clause or other basis of the claim, and shall include substantiation of the amount and/or extension to which the Employer considers himself to be entitled in connection with the Contract. The Engineer shall then proceed in accordance with Sub-Clause 3.5 [Determinations] to agree or determine (i) the amount (if any) which the Employer is entitled to be paid by the Contractor, and/or (ii) the extension (if any) of the Defects Notification Period in accordance with Sub-Clause 11.3 [Extension of Defects Notification Period].*
>
> *This amount may be included as a deduction in the Contract Price and Payment Certificates. The Employer shall only be entitled to set off against or make any*

[6] The same wording is used for the Plant and Design-build Conditions.

deduction from an amount certified in a Payment Certificate, or to otherwise claim against the Contractor, in accordance with this Sub-Clause.

13. The final paragraph of the conditions for EPC/Turnkey projects reads slightly differently as follows:

The Employer may deduct this amount from any moneys due, or to become due, to the Contractor. The Employer shall only be entitled to setoff against or make any deduction from an amount due to the Contractor, or to otherwise claim against the Contractor, in accordance with this Sub-Clause or with sub-paragraph (a) and/or (b) or Sub-Clause 14.6 [interim payments].

14. The key features of this sub-clause are:

- If the Employer considers himself entitled to either any payment or an extension of the Defects Notification period under the Contract, the Employer or Engineer shall give notice and particulars to the Contractor.
- The notice relating to payment should be given as soon as practicable after the Employer has become aware of the event or circumstance which gives rise to the claim.
- Any notice relating to the extension of the Defects Notification Period should be given before the expiry of that period.
- The Employer must also provide substantiation including the basis of the claim and details of the relief sought.
- Once notice has been given, the Engineer shall make a determination in accordance with sub-clause 3.5.
- Any amount payable under sub-clause 2.5 may be included as a deduction in the Contract Price and Payment Certificates.
- The Employer cannot make any deduction by way of set-off or any other claim unless it is in accordance with the Engineer's determination.
- Notice is not required for payments due to the Employer for services under sub-clause 14.19 or equipment under sub-clause 4.20.

15. Sub-clause 2.5 is a new "Contractor-friendly" clause. I say this because it is designed to prevent an Employer from summarily withholding payment or unilaterally extending the Defects Notification Period. One particularly important feature can be found in the final paragraph which specifically confirms that the Employer no longer has a general right of setoff. The Employer can only set-off sums once the Engineer has agreed or certified any amount owing to the Contractor following a claim.

16. The Employer should remember that in accordance with sub-cause 14.7, he must pay any amount certified, even if he disagrees with the Engineer's decision. By sub-clause 14.8, were the Dispute Adjudication Board to decide that the Employer had not paid the amount due, the Contractor would be entitled to finance charges.

17. Sub-clause 2.5 imposes a specific notice procedure on any Employer who considers that it has any claims against the Contractor. Unless the Employer follows the procedure laid down by this sub-clause, he cannot withhold or otherwise deduct any sums due for payment to the Contractor. The notice must be in writing and delivered in accordance with the requirements of sub-clause 1.3. It is unclear as to whether the particulars are required to be provided at the same time as the notice is served. The sub-clause does not require that the particulars are provided at the same time as no time limit or frame is imposed on either.

18. The Employer must give notice "as soon as practicable" of him becoming aware of a situation which might entitle him to payment. Therefore unlike sub-clause 20.1, where a Contractor has 28 days to give notice, there is no strict time limit within which an Employer must make a claim, although any notice relating to the extension of the Defects Notification Period must of course be made before the current end of that period. In addition it is possible that the Applicable Law might just impose some kind of limit.

19. It might have been thought that one option would have been to suggest that the Employer should be bound by the same 28-day limit as the Contractor. Instead, sub-clause 2.5 provides a simpler claims mechanism with no time bar. However, the rationale for the difference in treatment is presumably that in the majority of, if not all, situations, the Contractor will be (or should be) in a better position to know what is happening on site and so will be much better placed to know if a claims situation is likely to arise than an Employer.

20. The particulars that the Employer must provide are details of the clause (or basis) under which the claim is made, together with details of the money-is-time relief sought. Details of any notices served by the Employer are also required by sub-clause 4.21(f) to form part of the regular progress reports.

21. Under sub-clause 3.5 of the Construction and Design-Build Conditions, the Engineer must first try and agree the claim. Under the EPC/Turnkey Conditions, the primary onus to agree or determine any claims lies with the Employer. If either party is not satisfied with the determination made by the Engineer under sub-clause 3.5, then the resulting dispute could be referred to the Dispute Adjudication Board under clause 20. An Employer would therefore be advised not to deduct the amount to which he is believed to be entitled, before any such determination of the Dispute Adjudication Board, as to do so would leave the Employer liable to a claim from the Contractor.

What does sub-clause 2.5 cover?

22. There are a number of different clauses throughout the Contract which provide the Employer with a right to claim payment from the Contractor. These include:-

Sub-clause 4.19 –	Electricity, water and gas
Sub-clause 4.20 -	Employer's equipment and free-issue material
Sub-clause 7.5 –	Rejection
Sub-clause 7.6 –	Remedial work
Sub-clause 8.1 –	Commencement of works
Sub-clause 8.6 –	Rate of progress
Sub-clause 8.7 -	Delay damages
Sub-clause 9.4 -	Failure to pass tests on completion
Sub-clause 10.2 -	Taking over of parts of the works
Sub-clause 11.3 -	Extension of defects notification period
Sub-clause 11.4 -	Failure to remedy defects
Sub-clause 13.7 -	Adjustments for changes in legislation
Sub-clause 15.3 -	Valuation at date of termination
Sub-clause 15.4 -	Payment after termination
Sub-clause 17.1 -	Indemnities
Sub-clause 18.1 -	General requirements for insurances
Sub-clause 18.2 -	Insurance for works and contractor's equipment

MDB Harmonised edition

23. There are, of course, two different versions of sub-clause 2.5. There are some slight differences between the FIDIC Standard Form and the version produced by the Multilateral Development Banks known as the MDB Harmonised edition. Some of these differences are minor. For example, the reference to Free-Issue Material has been changed to Free-Issue Materials.

24. However, a more significant change has been introduced to the sentence which details when the Employer must give notice which now reads as follows:

> *The notice shall be given as soon as practicable and no longer than 28 days after the Employer became aware, or should have become aware, of the event or circumstances giving rise to the claim. A notice relating to any extension of the Defects Notification Period shall be given before the expiry of such period.* [emphasis added]

25. The first impression given by the addition of the underlined words is that they serve to tighten up the period in which the Employer must notify any claim an impression reinforced by the apparent 28-day time limit. However, the new words introduce an additional subjective

reasonableness test. Whereas before, all that mattered was when the Employer actually became aware of the circumstances giving rise to a claim, now some consideration needs to be given to when the Employer should have realised that a claims situation had arisen.

26. However in reality, save for extreme cases, little has changed. There is still no time limit to serve as a condition precedent to deprive the Employer of the opportunity to make a claim.

27. The claims mechanism for the Contractor is somewhat different.[7] However, for the benefit of those reading this paper separately, sub-clause 20.1[8] states that:

> *If the Contractor considers himself to be entitled to any extension to the Time for Completion and/or any additional payment, under any Clause of these Conditions or otherwise in connection with the Contract, the Contractor shall give notice to the Engineer, describing the event or circumstance giving rise to the claim. The notice shall be given 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.* [emphasis added]
>
> *If the Contractor fails to give notice of a claim within such period of 28 days, the Time for Completion shall not be extended, the Contractor shall not be entitled to additional payment, and the Employer shall be discharged from all liability in connection with the claim. Otherwise, the following provisions of this Sub-Clause shall apply.*

28. The key features of sub-clause 20.1 are that:

- The Contractor must give notice to the Engineer of time or money claims, as soon as practicable and not later than 28 days after the date on which the Contractor became aware, or should have become aware, of the relevant event or circumstance.
- Any claim to time or money will be lost if there is no notice within the specified time limit.
- Supporting particulars should be served by the Contractor and the Contractor should also maintain such contemporary records as may be needed to substantiate claims.
- The Contractor should submit a fully particularised claim after 42 days.
- The Engineer is to respond, in principle at least, within 42 days.
- The claim shall be an interim claim. Further interim updated claims are to be submitted monthly. A final claim is to be submitted, unless agreed otherwise, within 28 days of the end of the claim event.
- Payment Certificates should reflect any sums acknowledged in respect of substantiated claims.

[7] And is being covered by other speakers.
[8] Clause 20.1 is identical in the Red, Yellow and Silver Books, except that in the Silver Book, the Employer performs the role of the Engineer.

- Contrary to the old FIDIC Books,[9] the notice to be served under sub-clause 20.1 relates to claims for an extension of time as well as claims for additional payment.

29. In other words, clause 20.1 is a condition precedent.

30. The rationale for the difference in treatment between the Employer and Contractor is that presumably in the majority of, if not all, situations, the Contractor will be (or should be) in a better position to know what is happening on site and so will be much better placed to know if a claims situation is likely to arise than an Employer. Nevertheless, sub-clause 2.5 is a clear step forward for the Contractor from the 1987 Old Red Book edition as one reason for the introduction of the clause was, as noted above, to prevent an Employer from unilaterally withholding payment.

Payment

31. As noted above, the restrictions of sub-clause 2.5 have been introduced to provide the Contractor with some protection from the Employer. From the Employer's point of view, the key clauses when it comes to payment are 13, which addresses variations, and 14, which specifically deals with the contract price and payment.

32. The amount the Contractor is going to be paid, and the timing of that payment is of fundamental importance to both Contractor and Employer alike. The manner in which the payment is made is traditionally dependent on the precise wording of the contract.[10] Under the code of Hammurabi[11] the rule was as follows: "*If a builder build a house for some one and complete it, he shall give him a fee of two shekels in money for each sar of surface."*

33. Thus the amount to be paid was clear and, given that the punishment for violating most of the provisions of the code was death, it might be presumed that most builders were paid, provided the house was constructed properly. However, unlike the FIDIC Form, the rule did not say when the payment had to be made.

34. Under sub-clause 14.3, the Employer has the right to expect detailed applications for payment from the Contractor. The Contractor must submit monthly applications, sixfold, containing the following information:

> *14.3 (a) the estimated contract value of the Works executed and the Contractor's Documents produced up to the end of the month (including Variations but excluding items described in sub-paragraphs (b) to (g) below);*
>
> *(b) any amounts to be added and deducted for changes in legislation and changes in cost, in accordance with Sub-Clause 13.7 [Adjustments for Changes in Legislations] and Sub-Clause 13.8 [Adjustments for Changes in Cost];*

[9] In the Orange Book (1995), Sub-Clause 20.1 only sets a notification deadline in respect of claims for additional payment. However, similar provisions in respect of time-related claims can be found at Sub-Clause 8.6.
[10] Although in the UK, section 109 of the 1998 Housing Grants Construction & Regeneration Act, now gives most contractors the right to payment by instalments.
[11] King Hammurabi ruled the kingdom of Babylon from 1792 to 1750 BC.

(c) any amount to be deducted for retention, calculated by applying the percentage of retention stated in the Appendix to Tender to the total of the above amounts, until the amount so retained by the Employer reaches the limit of Retention Money (if any) stated in the Appendix to Tender;

(d) any amounts to be added and deducted for the advance payment and repayments in accordance with Sub-Clause 14.2 [Advance Payment];

(e) any amounts to be added and deducted for Plant and Materials in accordance with Sub-Clause 14.5 [Plant and Materials intended for the Works];

(f) any other additions or deductions which may have become due under the Contract or otherwise, including those under Clause 20 [Claims, Disputes and Arbitration]; and

(g) the deduction of amounts certified in all previous Payment Certificates.

35. In addition, it is a precondition of payment that the application include a Progress Report submitted in accordance with sub-clause 4.21. The progress report is another new feature of the 1999 suite of contracts. The required format is very detailed and the EIC has described it as being "unnecessarily detailed"[12] and over prescriptive for most types of contract.

36. Whilst the importance of ensuring that the progress reports are accurate might seem obvious, His Honour Judge Wilcox in a recent case[13] involving a construction manager highlighted some of the potential difficulties for an Employer where that reporting is not accurate.

37. Under the terms of the particular contract, the construction manager was described as being the only person on the project with access to all of the information and the various programmes. He was the only available person who could make an accurate report to the Client at any one time, of both the current status of the Project and the likely effects, both on timing and on costs. He was at *"the centre of the information hub"* of the Project.

38. It is only with knowledge of the exact status of the Project on a regular basis that the construction manager can deal with problems that have arisen, and therefore anticipate potential problems that may arise, and make provisions to deal with these work fronts. That is not dissimilar from the status of the Contractor under FIDIC conditions.

39. An Employer will need accurate information of the likely completion date, and the costs, because this would affect his pre-commencement preparation and financing costs. Any change to the likely completion date would give an Employer the chance to adjust its operational dates. Judge Wilcox concluded:

> *Where a completion date was subject to change the competent Construction Manager had a clear obligation to accurately report any change from the original projected completion date, and the effect on costs.*

[12] *The EIC Contractor's Guide to the FIDIC Conditions of Contract for Construction*, which provides a useful and informative view from a Contractor's viewpoint of this contract.
[13] *Great Eastern Hotel Company Limited* v *John Laing Construction Ltd and Laing Construction Plc* - 99 Con LR 45

40. Under sub-clause 4.21(h) the Contractor has a similar obligation here. If the Employer and the Engineer are aware of the true position they might be able to bring their combined resources to improve the position on site and so assist the Contractor.

41. This is recognised by sub-clause 8.3, which requires the Contractor to give prompt notice of events or circumstances which may adversely delay the work or increase the contract price. Indeed sub-clause 4.21(f) requires that the Progress Reports also list out any notices served by either the Employer or Contractor pursuant to sub-clauses 2.5 and 20.1.

42. The Engineer, who, remember, by sub-clause 3.1(a) shall be deemed to act as the agent of the Employer,[14] then must make a fair determination of what is due to the Contractor. There is some slight confusion as to when an interim payment can be withheld. Under English jurisdictions, an Employer must check to ensure he gives the appropriate notice to comply with section 111 of the Housing Grants, Construction and Regeneration Act 1996. Sub-clause 14.6 specifically refers to two situations when the Employer can withhold payment:

    (i) the Employer has not received and approved the Performance Security; or

    (ii) the amount to be certified is less than the amount of the interim payment certificate as stated in the contract.

43. However, although the Employer must pay the amount certified, sub-clause 14.6, within sub-paragraphs (a) and (b), does set out other limited circumstances where payments may be withheld:

    (i) Where work is carried out which is not in accordance with the contract, the costs of rectification work may be withheld until the work is carried out; and

    (ii) If the Engineer notifies the Contractor that it is failing to perform any obligation in accordance with the Contract, then the value of this work may be withheld until the work has been carried out.

44. The Employer should note that the exception in sub-paragraph (b) is dependent on the appropriate notice being given by the Engineer. This is slightly confusing in that these seem to refer to failures to perform which are the very items an Employer would expect to withhold payment for but which at the same time are the very items which sub-clause 2.5 has been set up to deal with. In reality these should not, in any event, be a separate withholding issue. If work has been carried out which is contrary to the contract, it will presumably be valued at a reduced price, or even nil, by the Engineer.

45. When it comes to actual payment, the Employer must, with an interim payment, pay the sum certified by the Engineer within 56 days of the date of the Contractor's application. With the Final Payment, if the amount of the payment is agreed, the position is this:

[14] Thus confirming within the contract, what many had already suspected

(i) The Contractor receives the Performance Certificate (see sub-clause 11.9);

(ii) The Contractor then has 56 days to submit the draft Final Account (see sub-clause 14.11);

(iii) If the Final Payment Certificate is agreed, the Engineer has 28 days to issue a Final Payment Certificate (see sub-clause 14.13);

(iv) The Employer then has a further 56 days to make payment (see sub-clause 14.7(c));

(v) If the amount of payment is not agreed, then following sub-clause 14.11, the disagreement will be resolved in accordance with the principles of sub-clauses 3.5 and 20.4 and 5.

46. If the Employer fails to pay either on time or at all, then the Contractor has a right to interest under sub-clause 14.8, to give notice that it intends to suspend performance of its work under sub-clause 16.2 and ultimately to terminate under sub-clause 16.2.

Termination

47. The Employer should at all times remember that, in accordance with clause 16, a Contractor can only suspend performance in the following circumstances:

(i) If the Engineer fails to issue a timely interim certificate; or

(ii) If the Employer fails to provide financial information under sub-clause 2.4; or

(iii) If the Employer fails to pay any sums due.

48. Before the Contractor can suspend, it must give 21 days' notice. If the default is remedied, the Contractor must resume work as soon as possible. Where the suspension is valid, the Contractor is entitled to claim for delay or cost plus reasonable profit in accordance with clause 20.

49. The Employer should also bear in mind the circumstances listed under sub-clause 16.2 where the Contractor is entitled to terminate:

(i) The Employer fails to provide reasonable evidence of its financial arrangements;

(ii) The Engineer fails to issue a Payment Certificate on time;

(iii) The Employer fails to make due payment on time;

(iv) The Employer fails to perform its contractual obligations;

(v) The Employer fails to enter into the Contract Agreement or assigns its entire interest in the project;

(vi) There is a prolonged suspension in accordance with sub-clause 8.11;

(vii) The Employer goes into insolvency.

50. Termination by either party is a very serious step and one which is not to be taken lightly. Termination is likely to delay the completion and increase the costs of the project. Sub-clause 15.2 deals with the mechanism of termination and sets out the circumstances in which the Employer may terminate. In addition, the Employer may use sub-clause 15.5 to terminate at its "convenience".

51. It is important that determination provisions are precisely followed. If a dispute arises, those procedures particularly in relation to notices or time limits will usually be carefully considered and strictly applied. The case of *Brown & Docherty* v *Whangarei Country,*[15] provides a typical example of the principles that apply when considering termination clauses. Here Smellie J held that:

(i) Determination clauses must be interpreted strictly;

(ii) For a determination to be valid under the contract, the correct procedure must be complied with;

(iii) A professional consultant (such as an engineer or architect) must act fairly and impartially in the exercise of any discretion to issue a contractual certificate or notice that may be relied upon by the Employer as grounds for determination;

(iv) The Contractor must be given fair warning that continuation of his conduct may result in determination and he should not be lulled into assuming that he would be permitted to continue with the work; and

(v) A certificate or notice issued by the architect or engineer in reliance upon incorrect or irrelevant information or grounds (such as claims for additional payment and requests for further extensions of time) will be invalid.

52. The Employer must therefore take care to follow any notice requirements in the Contract. Who should the notice be served upon? Where should the notice be served? How should the notice be delivered? The purpose of this contractual provision is to ensure that one party knows what the other wishes to communicate. There is conflicting case law on the effect of serving the notice in the wrong way. In the case of *Central Provident Fund Board* v *Ho Bock Kee,*[16] the Court of Appeal in Singapore found that a notice was invalid on the grounds that it failed to comply with the contract, being both sent by the wrong body (the Superintending Officer and not the Chairman of the Board) and delivered by hand and not by registered post. However, in England, in the case of J.M. Hill v London Borough of Camden[17] the Court of Appeal took a different line when a notice was served by recorded delivery rather than registered post. Ormrod LJ said:

[15] [1988] 1 N.Z.L.R 33
[16] (1981) 17 BLR 21
[17] (1980) 18 BLR 35

Nothing is more distasteful to me than to construe a business contract in this formalistic sense … Everybody concerned knew perfectly well what was happening. No one was in the very slightest degree prejudiced by it … So that it is the most purely formal point.

53. More recently, again in England, Judge Gilliland, when looking at a JCT form of contract, said that actual delivery is simply *"transmission by an appropriate means so that it is actually received"* and that what was important was actual receipt.[18] Nevertheless, it is always better to follow the requirements of the contract. Different countries may have different legal approaches, and the costs of and time involved in asking the court to resolve any dispute that arises as a result of uncertainty might be considerable. With time limits, the 14-day period must be followed. If the notice is served a day early or late it may well not count. The consequence of a wrongful termination will be significant, typically amounting to a repudiatory breach of contract, which will leave the Employer vulnerable to a significant claim by the aggrieved Contractor.

54. Do not forget that the contractual right to termination exists in addition to the common law right to repudiation. In England, the Court Appeal in the case of *Lockland Builders* v *Rickwood* accepted that contractual and common law rights can sit side by side provided the defaulting party demonstrates an intention not to be bound by the Contract. [19] Hirst LJ adopted the general principle stated in *Chitty on Contracts*[20] that:

The fact that one party is contractually entitled to terminate the agreement in the event of a breach by the other party does not preclude that party from treating the agreement as discharged by reason of the other's repudiation or breach of condition, unless the agreement itself expressly or impliedly provides that it can only be terminated by exercise of the contractual right.

55. Nevertheless where, as here, the Contract contains an express termination clause, the Party seeking termination would be best advised to rely on that clause. It is likely to be the more practical and straightforward approach. Indeed, it was in recognition of this, that the Court of Appeal noted in the *Lockland* case that Mr Rickwood could have saved himself considerable time and expense by adopting the simple procedure available to him under condition 2 of the Contract.

56. One sub-clause of particular interest is the termination for convenience sub-clause, 15.5, which deals with the Employer's entitlement to termination. It says this:

The Employer shall be entitled to terminate the Contract, at any time for the Employer's convenience, by giving notice of such termination to the Contractor. The termination shall take effect 28 days after the later of the dates on which the Contractor receives this notice or the Employer returns the Performance Security. The Employer shall not terminate the Contract under this Sub-Clause in order to

[18] *Construction Partnership UK Ltd* v *Leek Developments Ltd*
[19] 77 BLR 38.
[20] Paragraph 22-044 – 27th Edition

execute the Works himself or to arrange for the Works to be executed by another contractor.

57. The key features of this sub-clause are that:

- The Employer may terminate at any time, absent Contractor default, upon 28 days' notice.
- If the Employer terminates on this basis, the works cannot be completed by another.
- The Contractor is entitled to be paid in accordance with sub-clauses 16.3 and 19.6.

58. Under the MDB version, the words *"or to avoid determination of the contract by the Contractor under clause 16.2"* have been added to prevent the Employer from stepping in to prevent the Contractor from operating its own right to terminate.

59. The most likely reason that an Employer will choose to operate this sub-clause will be an inability to fund and thereby finish the project. Those advising Employers should note the deliberate restraint on an Employer's ability to implement the sub-clause as he will be unable to finish the project either by himself or by engaging a new contractor. Thus the Employer, under this termination for convenience clause, cannot terminate if his intention is to remove the Contractor in order to find another to carrying out the project. In other words, the Employer must act in good faith towards the Contractor.

60. The question of termination for convenience clauses came before the English courts in the case of *Hadley Design Associates* v *The Lord Mayor and Citizens of the City of Westminster.*[21] Here Hadley had been appointed as consultant surveyor and architect in connection with work to a block of flats. Westminster, relying upon a provision in the contract entitling it to terminate on one month's notice, sought to bring the contract to an end. Note that Westminster gave three reasons for bringing the contract to an end. Residents of the estate had expressed dissatisfaction with the performance of Hadley; a separate firm had been appointed to provide maintenance services and Westminster wanted one firm to deal with all matters relating to the estate, and finally Westminster was required to follow a policy of compulsory competitive tendering which meant that the surveying and maintenance services needed to be market tested. However, under the contract, all they had to do was give notice.

61. Hadley responded by bringing a claim for loss of profit. Hadley argued that during a meeting that took place before the contract was signed, Westminster said it would only terminate the contract if Hadley was in default or Westminster was unable to complete the block of flats due to a lack of money. The Judge, on the facts, disagreed that there was such a collateral contract.

62. Hadley also suggested that the termination clause was unreasonable, for example by reference to the 1977 Unfair Contract Terms Act. Again, the Judge disagreed. Thus Westminster was able to terminate the contract without giving reasons.

63. More recently, in Australia, the Supreme Court of Victoria had to consider a termination for convenience power.

[21] [2003] All ER (D) 262

64. In *Kellogg Brown & Root Pty Ltd* v *Australian Aerospace Ltd,*[22] KBR sought an injunction restraining AAL from relying on a notice given pursuant to a termination for convenience clause. AAL had entered into a contract with the Australian Government to supply 46 helicopters. KBR had entered into a sub-contract for part of the work.

65. Clause 12.3 of the contract said this:

> *12.3.1 in addition to any other right it has under the Contract, AA may terminate the Contract or reduce the scope of the Contract by notifying the Contractor in writing.*
>
> *12.3.2 where the contract manager issues a notice under clause 12.3.1, the contractor shall:*
>
> *(a) stop work in accordance with the notice;*
> *(b) comply with any directions given to the contractor by AA; and*
> *(c) mitigate all loss, costs and expenses*
>
> *12.3.3 AA shall only be liable for:*
>
> *(a) payments under the payment provisions of the contract for work conducted for the effect of day to day termination;*
> *(b) any reasonable costs directly attributable to the termination; and*
> *(c) materials purchased and/or for purchase committed as at the date of the notice of termination*
>
> *12.3.4 The Contractor shall not be entitled to profit anticipated on any part of the Contract terminated*

66. The evidence before the court showed that the termination for convenience clause was a standard one and had been used in numerous contracts within the defence industry.

67. Differences had arisen between the parties over the performance of KBR and AAL had attempted to re-scope the work, i.e. reduce the scope of KBR's appointment. The negotiations between the parties were unsuccessful and AAL sought to terminate pursuant to clause 12.3 of the contract.

68. KBR said that the purported termination was a breach of the implied terms of the contract in that it denied KBR the substantial benefit of the contract, was not given in good faith, fairly and reasonably or for just cause, and it was given in respect of default which was the subject of a dispute resolution process which had been invoked. It was accepted by AAL that there was a serious question to be tried, namely whether a term of good faith and fair dealing could be implied into the contract and whether the notice of termination was given in breach of that term.

[22] [2007] VSC 200

69. There are a number of Australian cases which provide for the implication of a term of good faith.[23] None of these cases, nor the others cited before the court, concerned a termination for convenience clause.

70. It was, however, deposed that the principal reason for the inclusion of a termination for convenience clause was that the Commonwealth of Australia was able to terminate its contract with AAL in certain limited circumstances (perhaps when the political climate had changed) and this clause therefore ensured that in that event, AAL was in a position to terminate its sub-contracts.

71. The Judge, Hansen J, held that on the basis of the evidence before him, there was an arguable case. However, as this was an application for an injunction, the matters in evidence were not tested as they would be at a full trial. That said, the injunction was granted temporarily, at least preventing AAL from exercising the termination for convenience clause.

72. As noted above, the whole point of termination for convenience clauses is to allow a party to terminate the contract without having to prove default or insolvency. It can and presumably now will be argued that this Australian decision has created an element of uncertainty to this presumption. However, on the other hand, the implication of the principle of good faith, is a matter which must always be borne in mind in international contracts such as FIDIC.

73. That said, English law does not tend to recognise the obligation of good faith in a similar way to the Australian and many other jursidictions in relation to the exercise of contractual rights. Therefore, it is arguable whether the English courts would take a similar view at present. However, the discussion of such issues is particularly important when discussing international contracts such as FIDIC, because you will almost certainly be bound by the jurisdiction of the country where the work is being carried out.

74. In Australia the concept of good faith is being developed in the courts. Unlike England and Australia, many jurisdictions are governed by their own civil codes. Whilst these codes recognise contract autonomy and allow the parties to determine the terms and conditions of their contract, they will also insist that these conditions do not contravene any mandatory provision of the law or public policy. One such example is this concept of good faith.

75. Many civil codes provide that a contract must be performed in accordance with its contents, and in a manner consistent with the requirements of good faith. It is not always that easy to define what good faith might mean. The English courts have said this:

> *It is a principle of fundamental justice that if a promisor is himself the cause of the failure of performance, either of an obligation due to him or of a condition upon which his own liability depends, he cannot take advantage of the failure.*[24]

76. In France there is the concept of *abus de droit* (misuse of a right). Under the Egyptian Civil Code, for example, the exercise of a right is considered unlawful in the following cases:

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[23] For example, *Renard Constructions (ME) Pty Ltd* v *Minister for Public Works and Specific Brands Sport & Leisure Pty Ltd* v *Underworks Pty Ltd.*

[24] CIA Borcad & Panona SA v George Wimpey & Co [1980] 1 Lloyd Rep 598

- If the sole aim thereof is to harm another person;
- If the benefit it is desired to realize is out of proportion to the harm caused thereby to another person;
- If the benefit it is desired to realize is unlawful."[25]

77. Article 148 of the Egyptian Code further provides that:

> *a contract must be performed in accordance with its contents and in compliance with the requirements of good faith.*

78. However, in France, for example, contractual time bars have been given effect by the courts provided they appear to be reasonable under the circumstances.[26] Similarly, before Egyptian courts, an agreement to a contractual forfeiture of a right for the non-accomplishment of a certain action within a determined period of time might still be valid and binding.[27] Thus good faith is far from always the answer. Note the wording of the Egyptian Code. A contract must be performed in accordance not only with the requirements of good faith, but also in accordance with the contents of that contract.

79. In practice, much will therefore depend on the circumstances of the case and the conduct of both parties. For example, the contractual obligation to deliver timely notice of one's intention to claim additional time or money will normally be upheld, unless the particular circumstances of the case show that such conclusion would lead to a misuse of a right or a breach of the parties' good faith obligations. If therefore a Contractor is only a few days late in submitting its sub-clause 20.1 notice in respect of very substantial claims and the forfeiture of its contractual rights would result in serious financial difficulties, then one might reasonably be entitled to argue that it would be an *abus de droit* for the Employer to rely on Clause 20.1. Similarly, if the Employer has actual knowledge of the "event or circumstance giving rise to the claim", and/or suffers no substantial harm as a result of not receiving the Contractor's notice on time, then, having regard to its implied obligation of good faith, the Employer may not be able to rely on sub-clause 20.1 to defeat the Contractor's claims.

80. Similar considerations, of course, will apply to questions relating to termination.

5 October 2007

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[25] Article 5 of the Egyptian Civil Code. The prime author of the Egyptian Civil Code, Prof. Abdel-Razzak Al-Sanhuri had studied law in Lyon, France between 1921 and 1927, which might explain the influence of some of the concepts of the French Civil Code such as *abus de droit* on the Egyptian civil code.
[26] FIDIC, *An Analysis of International Construction Contracts*, edited by Robert Knutson (2005), p.84.
[27] See for example Article 750 of the Egyptian Civil Code on insurance contracts.