

FIDIC Construction Contracts and Arbitration: The Role of Dispute Adjudication Boards and the Importance of Governing Law

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An illustrative case study

FIDIC's standard forms of contract are widely used by parties of different nationalities as a contractual benchmark for the implementation of large scale construction projects worldwide. A special feature of FIDIC forms of contract is its built-in dispute resolution process through adjudication by a Dispute Adjudication Board (DAB).

One of the key perceived advantages of FIDIC forms of contract is that contracting parties are generally familiar with their standardized terms and value the legal certainty which their anticipated uniform application across jurisdictions offers. With respect to the DAB mechanism in particular, it is generally considered by market players as a success story in terms of promoting the efficient and cost effective resolution of disputes.

Nonetheless, a recent ICC award, the fourth of a series of ICC awards preceded by six DAB decisions during a 10-year old dispute regarding an infrastructure project in Romania, could cast doubts on the efficacy of the FIDIC DAB mechanism. This case also comes as a useful reminder that the effect of the governing law of the contract should not be underestimated, even in the FIDIC standardized contractual context.

The Key Matters in Dispute – Legal and Policy Issues in the Spotlight

The circumstances of the protracted dispute between the Contractor and the Employer were typical for similar construction projects. Delays in the project completion gave rise to a series of disputes involving the Contractor's claims for Extension of Time for Completion (EOT) and additional payment and respective Employer's counterclaims for delay damages. Following a longtime "battle" involving six DAB decisions, two ICC arbitrations, and numerous local court enforcement proceedings, the Parties resorted to a third ICC arbitration to resolve remaining open issues.

The key issue in dispute was whether the Contractor was entitled to claim back the major part of the delay damages imposed under the Contract^[fn]Sub-Clause 8.7 of the FIDIC Contract (FIDIC Conditions of Contract for Construction (First Ed. 1999 Red Book)).^[fn], considering that the Contractor had timely completed the major part of the Works, although no partial Taking Over certificates had been issued, as provided under the Contract^[fn]Sub-Clause 10.2 of the FIDIC Contract^[fn]. An important point is that various contractual aspects regarding extension of time, partial taking-over and delay damages had been previously addressed in a number of DAB decisions and other ICC arbitrations, raising issues of *res judicata* potentially barring contractual claims.

A set of interesting legal questions were raised in this case touching upon the interpretation of certain FIDIC contract provisions, including:

- Does the failure to issue a Notice of Dissatisfaction in relation to a DAB decision ruling on the date of the Taking-Over of the Works preclude the referral to arbitration of a claim for the pro rata reduction of delay damages to account for the use of parts of the Works Sub-Clauses 8.7. and 10.2 of the FIDIC Contract?
- Assuming that a party is contractually barred under FIDIC Contract provisions from bringing to arbitration a claim in the aforementioned context, would it nevertheless be entitled to invoke in arbitration the respective provisions of applicable law?

Perhaps more importantly, though, the fact that the Parties had to go through numerous dispute resolution proceedings, whereby practically none of the six DAB decisions issued were complied with voluntarily by the Parties, raises the broader policy question whether the FIDIC DAB procedure remains an effective tool for the timely and cost-effective resolution of construction disputes.

Key Facts of the Dispute in a Nutshell

The original Time for the Completion was in May 2007. During the Project Implementation various disputes arose between the Parties, including those in relation to delays in the execution of Works. The Contractor initiated the first ICC arbitration, claiming EOT and additional cost, in 2006, at a time when the Works were still in progress and no DAB was yet in place. The Parties later decided to suspend the first ICC arbitration proceedings and agreed to set up the DAB.

At that time, the Contractor's claims for EOT and additional cost were still pending, while the major part of the Works had been completed and used by the Employer. However, the Engineer refused to issue a Taking-Over Certificate pursuant to the Contract Sub-Clause 10.1 of the FIDIC Contract.

The Contractor referred, *inter alia*, the matter of issuance of the Taking-Over Certificate Sub Clause 10.1 of the FIDIC Contract to the DAB for adjudication. The DAB decided that the Taking-Over Certificate should be deemed issued as of January 2009. No Party submitted a Notice of Dissatisfaction against that DAB decision.

Nonetheless, the Contractor's initial claims for EOT and additional cost had still not been finally resolved and the first ICC proceedings were resumed. First a partial and then a final ICC award was issued in 2009, awarding a 7-month EOT for Employer's Risk Delay Events and compensation for additional cost.

In the meantime, the Parties referred to the DAB several other matters, including new claims of the Contractor for additional EOT and cost and counterclaims of the Employer for delay damages. Respective DAB decisions were issued, against which both Parties gave Notices of Dissatisfaction. A second ICC arbitration award was handed down in January 2014 awarding to the Contractor a further 9-month EOT and compensation for Employer's Delay Risk Events.

In July 2015, the Contractor initiated a third ICC arbitration claiming, *inter alia*, that the major part of the delay damages had been determined by the Engineer in the breach of the Contract and should be reduced proportionately to the value of the parts of the Works which had been completed and were being used by the Employer at the time of the (extended) Time for Completion see Sub-Clauses 8.7 and 10.2 of the FIDIC Contract. The matter of pro rata reduction of delay damages had been previously rejected by the DAB on procedural grounds, based on the fact that the date of the Taking-Over Certificate had been irrevocably fixed in a previous DAB decision ("**First DAB Decision**"), against which no Notice of Dissatisfaction had been given. Hence, that First DAB Decision had become final and binding for the Parties and the matter could not be revisited in the context of a posterior DAB decision ("**Second DAB Decision**"). Sub-Clause 20.4 of the FIDIC Contract.

The legal basis of the Contractor's claim in this third ICC referral was two-fold.

- First, as a matter of contract, the Contractor argued that the claim for a pro rata reduction of delay damages did not fall within the scope of the final and binding First DAB Decision but was a different claim premised on the provisions of the Contract.[fn]Sub-Clauses 10.2, 8.7 and 3.5 of the FIDIC Contract.[/fn]
- Second, as a matter of law, the Contractor's claim was independently founded on Romanian applicable law and, in specific Article 1070 of the Civil Code (1864) providing for the pro rata reduction of a contractual penalty in case of partial performance.

The Decision of the Sole Arbitrator

In January 2017, the arbitral award was issued. As regards the issue of delay damages, the Sole Arbitrator reached the following conclusions:

- The Sole Arbitrator rejected the Contractor's primary contractual claim, ruling that the application of the provisions of the Contract would involve reopening the final and binding First DAB Decision.[fn]Sub-Clause 10.2 of the FIDIC Contract.[/fn] The Sole Arbitrator considered that, in the given circumstances, the "matter in dispute" was in essence the same, given that both the Contractor's DAB referral and the First DAB Decision centered on a broad consideration of the provisions of the Contract.[fn]Sub-Clauses 10.1 and 10.2 of the FIDIC Contract.[/fn] Thus, the Contractor was barred from referring the matter to arbitration, given that it had not submitted a Notice of Dissatisfaction to the First DAB Decision.
- However, the Sole Arbitrator accepted the Contractor's secondary legal basis and reduced the delay damages amount by applying Article 1070 of the Romanian Civil Code. The Sole Arbitrator considered that the amount of delay damages provided for under the Contract was excessive under the given circumstances and should be reduced in light of the partial performance of the Contractor's obligations.

Interestingly, albeit ruling that the Contractor's contractual claim did not fall within Tribunal's jurisdiction, the Sole Arbitrator relied on the applicable law provisions as a means of granting the requested relief.

Lessons Learned

The manner in which the dispute was resolved in the recent ICC award offers an educative insight in the way arbitrators tend to apply FIDIC contractual provisions in combination with applicable law.

Lesson 1 – Parties should be cautious to adhere to the FIDIC dispute resolution provisions prior to referring disputes to arbitration.

In the case at hand, the Contractor was precluded from having its contractual claim be examined on its merits in arbitration because it had failed to give a Notice of Dissatisfaction to a DAB decision which had ruled on a matter closely connected with – but separate from – the issue in dispute. The bottom line: when in doubt about whether a matter falls within the scope of the DAB decision or not, it would be prudent to timely give a Notice of Dissatisfaction in order to be on the safe side.

Lesson 2 – The importance of applicable law should not be underestimated.

This case is a useful reminder of the importance of the governing law, even within the standardized FIDIC contractual context. The Sole Arbitrator partially granted the Contractor's claim for deduction of delay damages as a matter of law, even though it had previously ruled that the Contractor was contractually precluded from raising such a claim.

Other than the case specific lessons learned, this case raises concerns regarding the effectiveness of the FIDIC DAB procedure and its interplay with arbitration. Although the DAB decisions were swiftly issued at a relatively low cost, practically none of them was complied with voluntarily by the Parties. In fact, one of the Parties sought and partially succeeded in arbitration, invoking applicable law provisions, to essentially revise a final and binding DAB decision several years after the issue in dispute first arose. The lack of time limit under FIDIC for bringing claims to arbitration following a

DAB decision undermines the effectiveness and finality of the DAB process, resulting in time and cost inefficiencies, and may need to be revisited.

Conclusion

The FIDIC forms of contract are and will undoubtedly continue to be a very useful tool for parties of different nationalities seeking a familiar and business friendly contractual environment regulating construction projects. One of the most favorably commented aspect of FIDIC contracts relates to its dispute settlement process through the DAB. Far from negating the efficiency of this dispute resolution tool, this recent ICC award is a useful case study shedding light on legal issues typically encountered in this context and provides food for thought regarding ways of potentially enhancing the existing FIDIC dispute resolution mechanism.