

COVID-19: PRESSURE POINTS: FIDIC CONTRACTS - IS FM THE RIGHT ANSWER? (GLOBAL/UK)

15 April 2020 | Global/UK

Legal Briefings - By **Emma Schaafsma and Kate O'Callaghan**

Many of the international construction projects that we have been advising on since February this year have been impacted to varying extents and at different times by a range of COVID-19 related matters, including personnel on sick or isolation leave, governmental or local authority travel restrictions including tighter visa requirements and quarantine rules, factory closures, border closures and export restrictions. Some contractors have repatriated site personnel back to their home country out of fears for their health and safety, whether in accordance with their government's recommendations or simply following their corporate health and safety policies.

Invariably the focus is initially on whether force majeure relief applies. Under English law, force majeure is a creature of contract, not law, so the application of relief will depend on the precise wording of the contract as applied to the facts.

Where contracts are based on the FIDIC forms, however, while the temptation may be to head straight for the Force Majeure clause at Sub-Clause 19¹ (termed "Exceptional Events" at SC18 in the 2017 edition), there are a number of other likely candidates that also need to be considered. They all provide varying degrees of protection, but only Force Majeure entitles a party to terminate the Contract for prolonged Force Majeure. It is therefore important to undertake a careful analysis of the facts and the contract terms to ensure that claims are legally sound.

UNFORESEEABLE SHORTAGES IN THE AVAILABILITY OF PERSONNEL OR GOODS CAUSED BY EPIDEMIC OR GOVERNMENTAL ACTIONS

SC8.4(d)² in the Red and Yellow Books permit an extension of time (“**EOT**”), but not Cost, where Taking Over is delayed by “*Unforeseeable shortages in the availability of personnel or Goods caused by epidemic or governmental actions*”. Importantly, this relief is only available where the shortages cause delay to completion, i.e. critical delays to the Works.

COVID-19 has been declared a pandemic and therefore should be caught within “epidemic”. Similarly, the restrictive measures and border controls imposed by many governments should be caught within “*governmental actions*”. “Goods” includes all equipment, materials and plant intended to form part of the Permanent Works, and all Temporary Works (SC1.1.5.2)³. There is no country restriction as to where the epidemic took place, or as to which government took the action that caused the shortages.

Note that “Unforeseeable” is defined in the Red and Yellow Books as “*not reasonably foreseeable by an experienced contractor by the date for submission of the Tender*” (SC1.1.6.8)⁴. Of course, whether this unforeseeable requirement will be satisfied will depend on when the Contract was entered into and other relevant facts.

This relief is not available in Silver 1999, but in Silver 2017 it is available for Unforeseeable shortages in the availability of Employer-Supplied Materials.⁵

DELAYS CAUSED BY LOCAL AUTHORITIES

While SC 8.4(d) relates to governmental actions regardless of jurisdiction, SC8.5⁶ provides relief in the event of delays caused by public authorities in the project Country. If the Contractor has diligently followed the procedures laid down by the “*relevant legally constituted public authorities in the Country*”, and those authorities delay or disrupt the Contractor’s work, provided the delay or disruption was not reasonably foreseeable at the time of submitting the Tender, and that those delays caused a critical delay to the Works, the Contractor will be entitled to an EOT.

The Guide⁷ acknowledges that there is no mention of the financial consequences, explaining that this is because it “*would depend upon the particular circumstances*”. However, it is not clear what circumstances would enable the Contractor to be compensated in such event.

If the Contractor can demonstrate that, for example, new quarantine rules or revised work permit requirements imposed by the authorities were so restrictive that they caused actual critical delay to the Works, for example if supervisors essential to the progress of the Work on Site were not permitted to travel or access Site, then it might look to claim relief under SC8.4(d).

CHANGES IN LAW

SC13.7⁸ permits the Contractor an EOT and adjustment in the Contract Price to compensate Cost incurred as a result of a change in the Laws of the Country made after the Base Date that affect the Contractor’s performance of its contractual obligations.

“Laws” are defined as “*all national (or state) legislation, statutes, ordinances and other laws, and regulations and by-laws of any legally constituted public authority*” (SC1.1.6.5)⁹. Legal advice should be obtained to confirm whether specific governmental decrees, directives, recommendations and guidance might fall within the scope of this term.

FORCE MAJEURE

SC19.1 sets out a definition of “Force Majeure” that requires fulfilment of 5 criteria that together provide for a restrictive application. The event or circumstance has to be “*exceptional*”¹⁰, and beyond the party’s control (note that this does not refer to ‘reasonable control’). It must not be substantially attributable to the other party and not something that the party could have provided against before entering into the contract. Importantly, once the event occurred, the party could not have reasonably overcome or avoided, thereby imposing an obligation to take reasonable steps to try to avoid the event from impacting performance.

Even where all those criteria can be met, the event has to actually prevent performance of any contractual obligations (SC19.2¹¹), as opposed to, for example, making performance slower, less efficient, or more expensive. The wording “*prevented from performing any of its obligations*” in SC19.2 permits what is commonly referred to as ‘partial force majeure’.

SC19.2 concludes with a statement that Force Majeure shall not apply to either party’s obligation to make payments to the other.

SC19.1 sets out at (i) to (v) a non-exhaustive list of the types of events that could constitute Force Majeure, so long as the above criteria can be met. While this is an illustrative list¹² it is nonetheless relevant, as discussed further below, in terms of when Cost can be claimed.

So long as 1) a Party is prevented from performing any of its obligations as a result of Force Majeure, and 2) the notice requirement has been satisfied (being 14 days of becoming aware, or should have become aware, of the event constituting Force Majeure, SC19.4¹³), it will be entitled to:

- (both Parties) relief from performance of the affected obligations for as long as the Force Majeure prevents it from performing them (SC19.2);
- (Contractor) an EOT if completion will be delayed because the Contractor has been prevented from performing any of its obligations by reason of Force Majeure (SC19.4 (a))¹⁴;
- (Contractor) Cost if the event is “*of the kind described*” in the list of events at SC19.1 (i) to (iv) (which the Guide notes are all manmade events¹⁵) and for three of those, if it occurs in the Country (SC19.4 (b))¹⁶; and

- (either Party) terminate the contract on 7 days' notice if the execution of "*substantially the whole of the Works*" is prevented for a continuous period of 84 days, or multiple periods totalling more than 140 days due to the same Force Majeure event (SC19.6)¹⁷. This latter element may well become relevant should it transpire that later waves of COVID-19 virus cause further disruption to supply chains and workforces. SC19.6 then sets out sums payable on termination, including demobilisation costs, and notably do not include profit.

Both Parties are required "*at all times*" to use "*all reasonable endeavours*" to minimise any delay in the performance of the Contract as a result of Force Majeure (SC19.2)¹⁸. Legal advice will be required to understand the extent to which steps need to be taken in order to satisfy such an endeavours obligation. The Parties must give notice when they are no longer affected by the Force Majeure.

Finally, SC19.5 provides that the Contractor takes the risk of subcontracts providing broader or additional force majeure relief than this contract¹⁹. Therefore, if a subcontractor is entitled to force majeure relief in circumstances that would not otherwise be afforded to the Contractor under SC19, the subcontractor's failure would put the Contractor in breach of the head Contract.

With regard to the Silver Book in particular (which as noted above does not contain EOT relief for Unforeseeable shortages in Goods and personnel arising from epidemics and governmental actions and only provides relief for changes in local Laws), Contractors may look to obtain Force Majeure relief for delays caused by overseas governmental orders and decrees (e.g. closing borders and imposing export and travel restrictions due to COVID-19). Employers would no doubt argue that, given the limited scope of SC13.4, the risk of delays arising from such overseas laws lies with the Contractor and should not be permitted to fall within the scope of Force Majeure. The arguments could be finely balanced in certain circumstances.

RELEASE FROM PERFORMANCE UNDER THE LAW

SC19.7 completes the set of relief events by dealing with two extreme situations, irrespective of whether they also amount to Force Majeure: where an event or circumstance makes it impossible or unlawful for a Party to perform, or if under the applicable law entitles the Parties to be released from further performance (under English law this would be the doctrine of frustration). The Parties will then be discharged from further performance, but without prejudice to rights in respect of prior breaches, and the Contractor would be entitled to be paid the same as if the Contract had been terminated for prolonged suspension under SC19.6.

MORE THAN ONE POSSIBLE RELIEF?

It is not inconceivable that an analysis of the facts in question might lead to the conclusion that the event could be covered by more than one clause. For example, where the government of the Country of Site has issued an order or decree that prevents Goods from reaching Site and therefore causing critical delay to the Work, depending on the facts, this might fall under SC8.4(d) (Unforeseen shortages of Goods and personnel) of FIDIC Red and Yellow Books and SC13.4 (Adjustments for Changes in Legislation) if the government action in question constitutes a “Law”. Similarly, given that both SC13.4 and SC8.5 (in all Books) deal with actions by public authorities it may be that the circumstances are such that both could equally apply. Note, however, that SC13.4 can provide financial relief regardless of whether the change in Law has resulted in a critical delay to completion of the Works.

THE IMPORTANCE OF GETTING IT RIGHT

While it would not be possible to recover the same cost or loss under more than one clause, due to the rules against double recovery, the prudent course of action would be to submit a notice of claim that cites each possible clause in the alternative, clearly setting out the facts and the legal basis for claiming under each.

In doing so, however, it is important to bear in mind that the notice requirements for claiming Force Majeure relief in SC19.2 are different to the notice requirements (in SC20.1)²⁰ for claiming under the other clauses mentioned here. In particular, the time period for submitting Force Majeure notices is 14 days from becoming (or should have been) aware of the event, whereas notices of claim are to be issued within 28 days under SC20.1. These notice provisions are all drafted as conditions precedent to being entitled to relief, so it is imperative to ensure that they are submitted in time and with as much detail as possible to demonstrate that not only an event has occurred which justifies seeking relief under the particular clause(s) but also how has, or it is anticipated to, impact performance, and then follow up with updates and particulars of claim as mandated in the relevant provisions.

Even more critical is for the claimant to be certain that the event in question amounts to Force Majeure before looking to invoke SC19.6 and terminating for prolonged Force Majeure. If it is later found that Force Majeure relief did not apply then the termination could itself entitle the other party to terminate (the Employer under SC15.2(b)²¹ or the Contractor under SC16.2(c)²²), or otherwise be considered a repudiatory breach of contract (under English law), and seek damages for wrongful termination.

1. References to Sub-Clauses (“**SC**”) in this note are to the 1999 Edition of the FIDIC Conditions of Contract for Construction for Building and Engineering Works Designed by the Employer (“**Red Book**”), Conditions of Contract for Plant and Design-Build (“**Yellow Book**”), and Conditions of Contract for EPC/Turnkey Projects (“**Silver Book**”). As the SCs in the 2017 Edition of the same forms are broadly similar to those in the 1999 Edition, we only note where there are material differences in the 2017 forms.

2. SC8.5(d) 2017 Edition
3. SC1.1.44 Red and Yellow Books 2017 Edition; SC1.1.39 Silver Book 2017 Edition
4. SC1.1.85 Red Book 2017 Edition; SC1.1.87 Yellow Book 2017 Edition; SC1.1.77 Silver Book 2017 Edition. "Unforeseeable" is defined by reference to the Base Date rather than the date of submission of the Tender.
5. SC8.5(c) Silver Book 2017 Edition
6. SC8.6 2017 Edition
7. FIDIC Contracts Guide to the Construction, Plant and Design-Build and EPC/Turnkey Contracts 1999 Editions (1st Edition, 2000) (the "**Guide**")
8. SC13.6 2017 Edition
9. SC1.1.49 Red and Yellow Books 2017 Edition; SC1.1.43 Silver Book 2017 Edition
10. Oddly, SC18.1 in the 2017 Edition does not state that exceptionality is a criteria, perhaps relying on the defined term itself "*Exceptional Events*" to imply this criteria.
11. SC18.2 2017 Edition
12. As noted in the Guide
13. SC18.2 2017 Edition
14. SC18.4(a) 2017 Edition
15. The Guide p295
16. SC18.4(b) 2017 Edition
17. SC18.5 2017 Edition
18. SC18.3 2017 Edition
19. Not included in the 2017 Edition
20. SC20 of the 2017 Edition contains different notice requirements
21. SC15.2.1(b) 2017 Edition
22. SC16.2.1(e) Red and Yellow, SC16.2.1(d) Silver Book 2017 Edition

KEY CONTACTS

If you have any questions, or would like to know how this might affect your business, phone, or email these key contacts.



**EMMA SCHAAFSMA
(KRATOCHVILOVA)**
PARTNER, LONDON

+44 207 466 2597
Emma.Kratochvilova@hsf.com

LEGAL NOTICE

The contents of this publication are for reference purposes only and may not be current as at the date of accessing this publication. They do not constitute legal advice and should not be relied upon as such. Specific legal advice about your specific circumstances should always be sought separately before taking any action based on this publication.

© Herbert Smith Freehills 2020

SUBSCRIBE TO STAY UP-TO-DATE WITH LATEST THINKING, BLOGS, EVENTS, AND MORE

Close

© HERBERT SMITH FREEHILLS LLP 2020