Course Introduction

The construction industry is one that has a special role in our country's (better yet, in every developing country's) quest for development. We can say that there is no development sector into which construction does not enter. The construction industry plays a key role in building economic infrastructure like roads, railways etc; in expanding social infrastructure like schools, hospitals, etc; and in expanding factories. As one facet of improving people's lives is the building and renovation of residences, construction plays a great role in this regard as well. To bring about fast growth in any economic sector, a strong and efficient construction industry is called for.

In developing countries, the construction sector generally operates with severe limitations, and is unable to meet local demands. Several complex activities, agencies and inputs have to interact before deriving any products or outputs of this sector. Building materials and a multitude of things such as, contractors, equipment, machinery, skills etc have to be assembled to produce an output. Thus, the construction industry is characterized by complex relationships between various parties which call for law. Construction is a process that consists of the building or assembling of infrastructure and thus involves a certain property on which the construction is to be undertaken. A construction project must fit into the legal framework governing the property, which include governmental regulations on the use of property, and obligations that are created in the process of construction. However there are no well coherent and codified laws or pertinent reading materials, particularly in our country, on the ebullient matter of the construction law.

Construction is high-risk venture. Each project is unique and has its own specific design to be constructed on a particular site within a definite timeframe, cost, materials, equipment and labor. Successful construction requires flawless functioning of the project stakeholders comprising the client, the design team, the construction team, and various trades, manufacturers, suppliers in a professional and timely manner. In spite of the client and the contractor as the contract parties, other project players are involved in the construction process. Due to the different culture, interest and organizational structure of each of them, some parties represent a risk source to other parties.

The construction process is governed by complicated contracts involving complex relationships in several tiers. There are many risks involved in construction projects. These risks could be attributed to a number of reasons, which include the nature of the construction process, the complexity and time-consuming design and construction activities, and the involvement of a multitude of people from different organizations with different skills and interests. Hence, a great deal of effort is required to co-ordinate the wide range of activities that are undertaken.

To this end, this teaching material tries to address the various issues involved in construction law. It starts with by introducing the reader to the construction industry that exists at international as well as at national levels thus giving its historical perspective. It, then, looks at different issues that need to be handled before any person can enter into a construction contract. After familiarizing the reader with the meaning, scope, types and parties of construction contracts, the material deals with the ever-evolving construction law theories including the different international and national legal regimes as well

as policy considerations that are applicable to construction contracts. Because of the complex relationship that is created by construction contracts, disputes are bound to arise. Accordingly, the material finally deals with the different means of dispute settlement in construction disputes.

CHAPTER ONE
THE CONSTRUCTION INDUSTRY

Introduction

The Construction Industry can be described as the sum of all economic activities related to civil and building works: their conception, planning, execution, and maintenance. Such works normally comprise capital investment in the form of roads, railways, airports, ports and maritime structures, dams, power generating stations, irrigation schemes, health centers and hospitals, educational institutions, warehouses, factories, offices and residential premises. Construction is widely acknowledged as the most important single constituent in a developing country's investment program. Because of such a high contribution, the construction industry has a major influence on the economic growth of a country.

The contribution of the industrial sector to the overall economic development of a country is significant. One of the main indicators of socio-economic and technological development of a country is the level of the progress scored in this sector. In this respect, the present industrial development level of Ethiopia, compared to other developing countries, is low. Industry plays a leading role in the realization of the Agricultural Development Lead Industrialization Strategy of the country. This is because of its economic and technological contribution in supplying inputs such as raw materials, machinery, hand tools, spare parts, components, construction materials as well as in expanding infrastructure and providing materials and technical services for agriculture, and other economic

sectors. In addition to this, the sector has got a decisive role in the economic development process of the country in strengthening linkages, interdependence and in attaining a balanced regional development

However, in the construction sector, no significant activity is observed other than the limited research activities on construction materials. Generally, the major scientific and technological problems of this sector are low capability, low capacity in designing and supervising large construction projects, less attention to improve and develop indigenous construction technology and the application of labour intensive construction technique, inadequate local production of hand tools with acceptable quality, lack of well developed design standard codes and non-conducive system of collection, and use and dissemination of information. Therefore, at present, engineering and consultancy, and technology transfer and development capabilities that enable the reduction of dependence and promote self reliance through time are not well established in the industrial sector .

This chapter is aimed at familiarizing students with the concept of the construction industry and that of the construction contracts. The first part of this chapter deals with to familiarizing students with the meaning and historical background of the construction industry. If them discusses, the different activities that need to be undertaken before entering into a construction contract. After that if focuses on formalities that professionals in the construction need to full file before they deal with construction contracts. To this end, this chapter looks into the requirements for licensing and registration of contractors, architects and civil engineers. After dealing with these preliminary issues, the chapter deals with the main theme of the course: construction contracts, introducing readers with the meaning

and scope of The construction contracts.

Unit Objectives:

At the end of this Chapter, students should be able to:

- Recite the history of the construction industry both at international and national leves;
- Appreciate the role of the construction industry in development;
- Identify the different activities that need to be undertaken before starting any construction project;
- Realize the need for licensing and registration of requirements;
- Differentiate the criteria for licensing and registration of different parties;
- Relate construction contracts with ordinary contracts, and
- Delineate the scope of construction contracts

1.1. Historical Background of the Construction Industry

Before looking into the historical background of the construction industry, it is necessary to look at what exactly constitutes the construction industry. In trying to define the construction industry, it may not be easy to come up with a universal definition. This is because of the fact that the definitions bestowed to the phrase in different societies tend to contain different aspects pertinent to that society. Of the definitions given, the definition given to the phrase by Australian Bureau of Statistics to its construction industry survey seems appropriate and widely applicable. Accordingly, the construction industry is described as including:

"*all units mainly engaged in constructing buildings*

> *(including the on-site assembly and erection of prefabricated buildings), roads, railroads, aerodromes, irrigation projects, harbor or river works, gas, sewerage or storm water drains or mains, electricity or other transmission lines or towers, pipelines, oil refineries or other specified civil engineering projects. In general, units mainly engaged in the repair of buildings or other structures are also included…. as are those engaged in the alteration or renovation of buildings, preparation of mine sites, demolition or excavation.*

Construction has been an aspect of life since the beginning of human existence. The first buildings were huts and shelters constructed by hand or with simple tools. As cities grew during the Bronze Age, a class of professional craftsmen like bricklayers and carpenters appeared. Occasionally, slaves were used for construction work. In the 19th century, steam-powered machinery appeared, and later on diesel and electric powered vehicles such as cranes, excavators and bulldozers. Traditional construction, might be considered as having properly, commenced between 4000 and 2000 BC in Ancient Egypt and Mesopotamia when humans started to abandon a nomadic existence, that caused a the construction of shelter. The construction of Pyramids in Egypt (2700-2500 BC) might be considered the first instance of large structure construction. Other ancient historic constructions include the Parthenon by Iktinos in Ancient Greece (447-438 BC), the Apian Way by Roman engineers (312 BC), and the Great Wall of China by General Ming T'ien under orders from Ch'in Emperor Shih Huang Ti (c. 220 BC). Similarly, the Romans developed civil structures throughout their empire including aqueducts, insulae,

harbors, bridges, dams and roads.[1]

Population growth and urbanization led to an increasing need for shelter developments, and focused attention on the importance of local building materials and techniques. Accordingly, the construction industry in many parts of the world started to grow with an increasing demand.[2] In line with this, construction companies are growing at a fast pace all over the world. With this growth of the construction industry and subsequent growth of construction companies, contractual relationships related to construction are increasing. Thus, there is a dire need for a coherent and efficient law to deal with such contractual relationships.

Coming to our country, the growth and increasing demand for the construction industry has followed a similar pattern as observed in the trend of the world. Currently, construction is one of the sectors leading the way towards modernization and industrialization in Ethiopia. The construction sector in Ethiopia, generally in the world, contributes to the realization of about fifty percent of the total capital. Being the second largest employer in the country, it's also an engine for technology, innovation and overall development.[3]

In the past history of Ethiopia, the construction industry was not considered as an independent sector of the national economy. It was rather considered as incapable of generating national wealth. As a

[1] "Civil Engineering" [Available Online], available at www.Wikipedia.org

[2] Building Materials and Construction Technology: Annotated UN Habitat Bibliography

[3] Ethiopian Roads Authority, Ethiopia: Domestic Construction Industry Study, 2000

result, no comprehensive strategy for its development was considered. This, in turn, has led to the undesirable features of the current construction sector. These features include lack of clear developmental objectives for the industry; inadequate co-ordination of planning between the industry and infrastructure programs in the various sectors of the economy heavy dependence on foreign resources such as materials, equipment and expertise representation of the role players in the construction sector by inadequate and ineffective organizations inadequate numbers of suitably qualified and experienced personnel at all levels that include engineers, technicians, mechanics, operators and foremen, etc. inadequate relevant local construction regulations and standards, and inadequate consideration given to the use of local resources (including community participation in labor-based works).[4]

Ethiopia witnessed a decline in the performance of almost all sectors of the economy during the various periods of government prior to 1991. The post-world war period in Ethiopia registered significant changes from the time of Emperor Haile Selasie (1941-1974) to that of the Derg (1974-1991) culminating in the events of 1991 which resulted in the formation of the Transitional Government of Ethiopia (hereinafter TGE). Even though various market based economic reforms have been introduced to the various industries of the country, including the construction industry, since the downfall of the Derg regime in 1992, the domestic construction industry has still faced several hindering factors in its development.[5]

In the New Economic Policy statement issued in 1992, the TGE made clear its intention to transform the stagnant command economy

[4] Ibid

[5] Ibid

inherited from its predecessors into a functioning market-based economy. This transformation is sought to be achieved through an Agricultural Development Led-Industrialization (hereinafter ADLI) strategy for the country which is supported by similar strategies in education, health and transport sectors. However, even if the country is well endowed with natural resources with 60% of its total land area estimated to be potentially arable, its road density is amongst the lowest in Africa nations and other developing countries. Furthermore, the existing road network has deteriorated to the extent that only eleven percent of paved roads and nineteen percent of gravel roads are in good condition, making it the worst in comparison with other developing countries. It is evident from the above that the success of the ADLI strategy and the consequent economic recovery and development of the country is highly dependent on the restoration of the country's road infrastructure.[6]

With the above considerations in mind, the construction industry is being given special focus in the policies of the country. The construction industry is one of the three sectors of the economy identified by the Ethiopia Government for special consideration to foster the country's economic development. However, the general state of the domestic construction industry in Ethiopia is still characterized by inadequate capital base, old and limited numbers of equipment, low levels of equipment availability and utilization, deficiencies in technical, managerial, financial and entrepreneurial skills, limited experience and participation of the private sectors in construction and consultation works, and insufficient and ineffective use of labor-based road construction and maintenance technology.[7]

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[6] Ibid

[7] Industry Policy of the Federal Democratic Republic of Ethiopia

The construction industry in Ethiopia is a sector that opens the door for the growth of many additional industries. Building works require high input. For instance, they require different metal products, clay works, and cement and cement products, etc. As such, the growth of these industries will surely follow the growth of the construction industry. Similarly, when the construction and renovation of housing increase, the demand for household furniture increased; thereby, indirectly, opening the door for the growth of the furniture industry. All in all, the construction industry is a sector that can entertain big micro companies, that is widely labor based. All these being taken into consideration, the industry policy of the Federal Democratic Republic of Ethiopia has sought to pay special attention to the construction industry of the country.[8]

1.2 Meaning and Scope of Construction Law

Coming up with a precise definition of a construction contract is a rather difficult task. However, different authors have tried to formulate a universally accepted definition of construction contracts. Generally speaking, a construction contract is one type of ordinary contracts; its only different from ordinary contracts in that it deals with the construction of various infrastructure. A major distinguishing feature between construction contracts and ordinary contracts is that the latter is bilateral, affecting only two parties, whereas the former involves more than two parties.

The different definitions given by the different authors are considerably similar. For instance, Hudson defines a construction contract as "an agreement under which a person, called variously the builder or contractor, undertakes for reward to carry out for another person, variously referred to as the building owner of employer, works

[8] Ibid

of a building or civil engineering character."[9] Similarly, Keating defines a construction contract as "any contract where one person agrees for valuable consideration to carry out building or engineering works for another."[10]

According to the General Conditions of the Contract for Construction, a construction contract represents:

> *The entire and integrated agreement between the parties hereto and supersedes prior negotiations, representations or agreements, either written or oral. The contract may be amended or modified only by modification. The contract documents shall not be construed to create a contractual relationship of any kind (1) between the architect and contractor, (2) between the owner and sub-contractor or (3) between any persons or entities other than the owner and contractor. The architect shall, however, be entitled to performance and enforcement of obligations under the contract intended to facilitate performance of the architect's duties.*[11]

Article 2610 of the Civil Code of Ethiopia defines a construction contract as "a contract of work and labor is a contract whereby one a party, the contractor, undertakes to produce a given result, under his own responsibility, in consideration of a remuneration that the other party, the client, undertakes to pay him."[12]

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[9] Hudson

[10] Keating

[11] General Conditions for the Contract of Construction

[12] Article, 2610, Civil Code

Article 2876 goes further to elaborate that a contract whereby one of the parties undertakes to deliver to the other party a house, a flat or another building which does not yet exist, is a contract of work and labor relating to immovable.[13]

From this, it can be understood that a construction contract, wether in our country or in any other country, covers the relationship between the parties to the contract. It, therefore, stipulates the rights and obligations of each party and addresses the issue of remuneration and payment that is rightfully due to a party.

1.3 Pre-Contract Preparatory Works

Before a person (be it physical or legal) signs a construction contract, there are certain pre-contract preparatory works that need to be undertaken. These pre-contract preparatory works include soil tests, site surveys, securing of building permits as well as consideration of various rights of different parties. Soil tests and site surveys are needed before a person can plan a suitable design for the construction he/she intends to undertake. In addition to these, it is necessary to get a building permit from an authorized organ of the government of the country where the construction takes place, before starting any type of construction whatsoever. Moreover, a person needs to consider the various rights of different parties so that the construction he/she considers to undertake will, in no way, infringe upon other's rights.

Soil testing is usually required for securing of building permits. While conducting soil tests, the soil engineers conduct a thorough investigation into the soil’s interaction with the construction that is sought to take place. Soil tests will help to identify and clean up

[13] Article 2876, Civil Code

contaminated areas within the proposed construction site prior to the construction. The soil engineers investigate the site for the construction, analyze the site as well as the subsurface conditions and make recommendations for work to take place. Once the soil testing is successfully undertaken, the builder moves on to request a building permit from the authorized agency of the area (country) where in which the construction takes place. A building permit is a document you receive from a local building department actually allowing persons to do the construction they seek to undertake. In order to secure a building permit, a builder is expected to submit plans, sign-offs from the architect and engineer, and soil reports showing the condition of the construction site. In our country, a builder wishing to undertake a construction in a certain sub-city has to secure a building permit from the sub-city administration where the construction work is to be undertaken.

Once a builder secures a building permit for the construction, he/she wishes to undertake, he/she proceeds to have the construction site surveyed. The American Congress on Surveying and Mapping defines surveying as

> *the science and art of making all essential measurements to determine the relative position of points and/or physical and cultural details above, on, or beneath the surface of the earth, and to depict them in a usable form, or to establish the position of points and/or details.*[14]

Land surveying includes the study and inspection of legal instruments and data analysis in support of planning, designing and establishing of property. Accordingly, land surveying includes services such as

[14] American Congress on Surveying and Mapping

mapping and construction layout surveys. Construction layout surveys refer to the process of establishing and marking the position and detailed layout of the new structures of building constructions.

1.4. Licensing and Registration of Contractors, Architects and Civil Engineering Consults

Before contractors, architects and engineers undertake any construction work, they need to be licensed and registered. The requirements for licensing and registration may vary from country to country or from one legal system to the other. In this section, we will look at the requirements for licensing and registration of the above mentioned individuals in the context of The Ethiopian laws.

The present rationale for licensing of contractors in Ethiopia is to ensure that applicants for a project have the necessary capacity and capability. For contracts works in other countries and for multilateral donor projects, this requirement is met through the prequalification process for each tender. This requires information on the current status and past performances of the contractor. The current procedure of registration and issuance of graded licenses rely on ownership of relevant equipment and number of staff. These criteria for licensing and registration relate neither to past performance nor to the contractor’s (architect's, engineer's or consultant's) ability to lease or hire equipment; thus making it difficult for contractors, with sound technical and financial performance in other fields, to enter new markets.

1.4.1 Contractors

All contractors desiring to carry out construction works are required

to register with the Ministry of Works and Urban Development (hereinafter referred to as MoWUD) in accordance with the Guidelines for the Registration of Construction Professionals and Contractors (hereinafter referred to as the Guidelines). According to Part 3 of the guidelines, all contractors registering under the guidelines are required to register first with the Ministry of Trade in accordance with the Commercial Code of Ethiopia and related directives of the MoWUD.[15] It is after securing a registration certificate from the Ministry of Trade that an application for registration with the MoWUD can be entertained. Accordingly, every contractor has to submit a photocopy of such a certificate to the MoWUD before being licensed as a contractor.

Every contractor has the option of submitting an application for registration as a contractor in any one of the following categories:

1) **General Contractors:** These are contractors who are qualified to undertake a variety of construction works such as buildings, roads, railways, bridges, etc.
2) **Building Contractors:** These are contractors who are qualified to undertake building construction and related works.
3) **Road Contractors:** These are contractors who are qualified to undertake construction of roads and other related civil engineering works.
4) **Specialized Contractors:** These are contractors who are qualified to undertake construction activities in specialized trades such as electro mechanical installation works, painting and decorations, sanitary installation works, wood and metal works and landscaping and other related activities.[16]

[15]Article 3.1, Guidelines for the Registration of Construction Professionals and Contractors (hereinafter Guidelines)

[16] Ibid

The criteria for registration of a contractor in any of the categories listed above differ based on the grade to which the contractor is applying. There are 10 grades which are categorized accordingly based on the construction cost of the project That the contractor is seeking to undertake. General Contractors, Building Contractors and Road Contractors can register in the ten grades based on the following criteria.

Grade 1 - Construction cost of Birr above 20,000,000
Grade 2 - Construction Cost of Birr up to 20,000,000
Grade 3 - Construction cost of Birr up to 15,000,000
Grade 4 - Construction cost of Birr up to 10,000,000
Grade 5 - Construction cost of Birr up to 5,000,000
Grade 6 - Construction cost of Birr up to 2,500,000
Grade 7 - Construction cost of Birr up to 1,000,000
Grade 8 - Construction cost of Birr up to 500,000
Grade 9 - Construction cost of Birr up to 250,000
Grade 10 - Construction cost of Birr up to 100,000

As far as Specialized Contractors are concerned, they can register in the ten grades based on the cost of the construction or installation of the specialized trades.

Grade 5 - Construction (Installation) cost of Birr up to 5,000,000
Grade 6 - Construction (Installation) cost of Birr up to 2,500,000
Grade 7 - Construction (Installation) cost of Birr up to 1,000,000
Grade 8 - Construction (Installation) cost of Birr up to 500,000
Grade 9 - Construction (Installation) cost of Birr up to 250,000
Grade 10 - Construction (Installation) cost of Birr up to 100,000[17]

[17] Ibid

Once a contractor who wishes to register in any of the ten grades fulfills the criteria of the cost required, he/she has to have certain experience and qualification as well as staff requirements that he/she needs to fulfill. While registered a contractor is used , the work permit license under the name of the Technical Manager (the names of both the owner and the Technical Manager will be listed on the identification to be issued). For all categories of contractors, Grades 1 and 2, the general or technical manager should be a registered as Professional Engineer IV; for Grades 3 and 4, the general or technical manager has to be a registered as Associate Engineer IV or a Professional Engineer III; for Grade 5, the general or technical manager has to be a registered as Professional Engineer or Associate Engineer III; for Grade 6, he/she shall be a registered as Associate Engineer or Professional Engineer I; for Grades 7 and 8, he/she shall be a registered Engineering Aid or Construction Superintendent with eighteen years of relevant experience; and for Grades 9 and 10, the applicant can either be a Graduate Engineering Aide with four years of construction experience or a Graduate Associate Engineer with at least two years of construction experience or any person able to read, understand and interpret blue prints with at least seven years of practical experience in construction works.[18]

After fulfilling the experience and qualification requirements, a contractor has to fulfill staff requirement before he/she can be registered as a contractor. The staff requirements vary from grade to grade and sometimes from category to category. The staff requirements for the different categories of contractors of different grades can be seen from the following chart.[19]

[18] Article 3.2, Guidelines

[19] Ibid (However, for Building Contractors from Grades 1 up to 4, the

General Contractors, Grades 1 and 2 – two Professional Engineers IV or above

One Associate Engineer IV or above
One Associate Engineer III or above
One Engineering Aide III or above
Two Engineering Aides II or above

General Contractors, Grades 3 and 4 - One Professional Engineer III or above

One Associate Engineer III or above
One Associate Engineer II or above
One Engineering Aide II or above
One Engineering Aides I or above

General Contractors, Grade 5 - One Professional Engineer II or above

One Associate Engineer II or above
One Associate Engineer I or above
Two Engineering Aides I or above

Building and Road Contractors, Grades 1 and 2 - One Professional Engineer IV or above

Two Associate Engineers IV or above
Three Engineering Aides II or above

Building and Road Contractors, Grades 3 and 4 - One Professional Engineer III or above

One Associate Engineer III or

Professional Engineers can be substituted by Professional Architects)

above
One Engineering Aide II or above
One Engineering Aide I or above

Building and Road Contractors, Grade 5 - One Associate Engineer II or above
One Engineering Aide I or above

General, Building and Road Contractors, Grade 6 - One Associate Engineer II or above
One Graduate Engineering Aide or above

General, Building and Road Contractors, Grade 7 - One Engineering Aide I or above
One Graduate Engineering Aide or above

General, Building and Road Contractors, Grade 8 - One Engineering Aide I or above

Once a contractor fulfills the above mentioned requirements and pays the registration fee set by the Guidelines, he/she is expected to submit a record of past performances and an audited statement of accounts along with the number, type and capacity of the equipments he/she intends to use. There are various equipment requirements set by the Guidelines for the registration of different categories of contractors in different grades. Categories and grades to which a contractor is

registered may be varied, upon the application of the contractor, by decision of the Registration Committee after having examined the financial, experience and staff and other resources or quality of performance of the contractor. This decision of the Committee, however, is subject to the approval of the Minister of Works and Urban Development.[20] Contractors may apply for grade and category change only once in a fiscal year provided that they are able to meet fully all the requirements set by the Guidelines.

Once a contractor is registered as such, the registration shall be valid for a period of one calendar year beginning form the year of such registration. At the end of the one year's period, each contractor is expected to be renewed every calendar year thereafter. The renewal of registration is only be effected only after the person seeking the renewal complies with the requirement of registration set forth by the Guidelines. If the renewal year has lapsed, the contractor has the option of having the registration renewed within three years of the expiry date upon payment of the arrears plus a fifty percent of the renewal fee for the period within which the registration has not been renewed. Any registration that is not renewed within three years of its expiry date shall be deemed to be cancelled automatically.[21]

1.4.2 Architects and Engineers

Architects and engineers may be registered as professional architects and engineers, graduate architects and associate engineers, engineering aides and associate engineering aides after having fulfilled the registration requirements set forth in Part II of the Guidelines. Moreover, the applicants must also fulfill registration fees

[20] Article 3.5, Guidelines

[21] Article 1.9, Guidelines

specified under the Guidelines.

For registration as professional architects and engineers, applicants must hold at least a B.Sc degree or the equivalent in architecture or engineering from a recognized university or a similar institution. The applicant must also submit satisfactory evidence of at least four years of relevant and progressive design and supervision experience acquired after graduation. Moreover, the applicant may be engaged in the preparation of design documents and in the supervision of construction works for projects sponsored by his/her employer. For registration as graduate architects and engineers, the applicants must hold at least a B.Sc degree or the equivalent in architecture or engineering from a recognized University or a similar institution. The applicant must also have up to four years of relevant experience in the field for which he/she is applying. Moreover, the applicant may be engaged in the preparation of design documents and in the supervision of construction works for projects sponsored by his/her employer.[22]

For registration as associate engineers, the applicants must hold a diploma or the equivalent in an approved course in construction from a recognized university, or a similar institution. The applicant must also submit satisfactory evidence of at least six years of relevant experience acquired after graduation in construction or supervision works of projects. Moreover, the applicant may be engaged in construction superintendence or supervision for projects sponsored by his/her employer. Similarly, for registration as Graduate Associate Engineers, the applicants must hold a diploma in building engineering or the equivalent in an approved course in construction from a recognized university, or a similar institution. The applicant must also

[22] Part II, Articles 1 and 2, Guidelines

submit satisfactory evidence of at least six years of relevant experience in the fields of construction or supervision works of all projects. Moreover, the applicant may be engaged, either on part-time bases or full time, in construction or project supervision.[23]

For registration as engineering aide, an applicant must hold a technical school certificate or the equivalent from a recognized university, or a similar institution. The applicant must also submit satisfactory evidence of at least six year's of relevant experience in the fields of construction acquired after obtaining such certificate or the equivalent qualification. Moreover, the applicant may be engaged in drafting and in surveying works. Similarly, for registration as associate engineering aide, the applicants must hold a technical school certificate or the equivalent in an approved course in construction from a recognized university or a similar institution. The applicant may also be engaged, either part time or full time bases, in drafting and surveying works of projects.[24]

1.4.3. Consulting Offices

Applicants may also submit applications for registering as consulting offices under consulting architects and engineers, consulting architects, general consulting engineers, or specialized consulting engineers. Consultants registering in office for consulting architects and engineers may participate in the preparation of total design documents for building and civil projects befitting their categories. Those consultants registered in the Office for Consulting Architects may participate in the preparation and design of building projects befitting their categories. Those consultants registered in the Office

[23] Articles 3 and 4, Ibid

[24] Articles 5 and 6, Ibid

for General Consulting Engineers may participate in the preparation of all engineering design works befitting their category. On the other hand, applications for registration in the Office of Specialized Consulting Engineers may be submitted in the specific fields of engineering like structural, road, sanitary and mechanical, foundational, electrical, quantity surveying, and surveying. Consultants registered in any of the above specialized fields may participate in the preparation of design projects befitting their categories.[25]

All applicants wishing to register in any of the consulting offices have to submit satisfactory evidence that the owner[26] or manager at the consulting office being applied for is a registered practicing architect or engineer[27] along with satisfactory evidence that the firm or organization has the finance, equipment, and office and office facilities required for the consulting office applied for. Moreover, the applying offices are required to submit satisfactory evidence showing that the firm or organization has the minimum number of registered staff set out by the Guidelines as well as a certificate of registration

[25] Part IV, Article 1, Guidelines

[26] Note that the owner him/herself may be the manager

[27] Practicing architects and engineers are those applicants who have satisfactory and progressive evidence in design and supervision in relation to their educational background as well as 8 years of work experience (the experience required may be reduced if the applicant holds higher qualifications than a B.Sc). In addition applicants are required to register with the Ministry of Domestic Trade in accordance with the Commercial Code. They must also show satisfactory evidence that they have a working place and the necessary equipments and facilities for performing in the services that they are applying for.

from the Ministry of Domestic Trade in accordance with the Commercial Code of Ethiopia. [28]

Summary

Construction has a history that is as old as human existence. In our country, as well as elsewhere in the world, the construction industry is one that has significant contribution to the development of the economy of a country. It is an industry that is growing at the fastest rate with increasing demands. With its high contribution to the economic sector of Ethiopia, the construction industry is one that is paid due emphasis by the Industry Policy of the country. Thus, the construction industry is one that needs to be regulated by the proper legal regimes requiring 'Construction Law'. Construction law governs the relationship of persons with regards to construction contracts. Construction contracts are types of ordinary contracts that deal with the construction of various types of infrastructure.

A person who wishes to undertake a certain construction work must necessarily sign a construction contract. However, construction contracts are not the only things one needs to worry about. There are certain pre-contract preparatory works that need to be undertaken before the construction work can actually be undertaken. The pre-contract preparatory works include soil tests, quantity surveys, securing of a building permit and consideration of the rights of others. In addition to all these, the parties that enter into construction contract with a person wishing to have a certain infrastructure built (the employer), for example, an architect, a contractor, sub-contractors, engineers and consulting offices need to get licensed and registered according to the laws of the country in which they are

[28] Part IV, Article 3, Guidelines

operating. In Ethiopia, though there is no formal law that governs the licensing and registration of these professionals, there is a guideline set by the Ministry of Works and Urban Development on issuing licenses and registering the professionals. This, in a way, is in contradiction to the importance bestowed upon the industry by the country Industry Policy. There have to be applicable laws to govern this sector economic sector. Currently, there is a move by the government to enact a Construction Law that covers this and many other issues that relate to the construction industry. Though this law is at the draft stage and is currently being discussed by the House of Peoples' Representatives, hopefully

Review Questions

1. What are the requirements for registration of contractors according to the Commercial Code of Ethiopia?
2. In the registration requirements for the different professionals involved, relevant experience in the field of construction and other related works is stated as one requirement. What does relevant experience pertain to mean?
3. What does the phrase "befitting their category" pertain to in the registration of consulting offices?
4. What is the importance of undertaking pre-contract preparatory works?

CHAPTER TWO
FORMATION OF CONSTRUCTION CONTRACTS

Introduction

The construction industry is regulated by various legislative enactments that are enacted from time to time. This is essential in light of the fact that the industry is so dynamic, that the system has to cope up with it. Basically, the construction industry is treated in two different domains: The **Civil Construction Laws**, and the **Government Construction Laws**.

The division is simply based on the employer or owner who seeks the building project is to be completed. The former refers to when a private individual or company employer enters into a contract with a contractor. The latter refers to the government department, as an employer wants to have the construction carried out on behalf of the government for the public interest. Thus, whether the construction contract involves a private civil/business-to-business engagement or a government-to-business engenders a separate set of rights and obligations in the construction contract. Hence, we shall firs deal firstly with the formation of the civil construction contracts and, them with the formation processes used for the government construction contracts.

One area of concern for the employer regarding a construction contract is how to finance his/ her/its project. The followings are the major of ways in which construction project can be financed;

1. Self-financing through the owner's own resources;
2. Borrowing from a lending agency and

3) Financing through involvement of the public and /or the constructor of the project.

Such public/ private partnership contracts are mainly Build-Operate-Transfer (BOT) agreement, and Build-Own-Operate-Transfer (BOOT) agreement. Other fairly known models include Build-Lease-Transfer (BLT), Rehabilitate-Operate-Transfer (ROT), Lease-Rehabilitate-Operate (LRO), etc.

These situations require three elements. First, a feasible and viable project is required. Second, there must be a willing government to grant a concession agreement which empowers a concessionaire (grantee) the right to operate and benefit from the constructed project by that concession. Finally, there must be funding agencies who are willing to take the financial risk of undertaking the project. On the expiry of the concession period, the project reverts to the authorities which granted the concession.

Such arrangements involve the grant of a concession (sometimes authorization or licensing) by a properly empowered governmental authority (the grantor) to a special purpose company (the concessionaire). Under the concession, the concessionaire would agree to finance, build, and control and operate a facility for a limited time[29] after which responsibility for the facility is transferred to the government, usually free of charge.

Unit Objectives:

[29] Art.3227 of the Civil Code puts the ceiling for Sixty years. Otherwise it is up to the governmental body and the concessionaire to fix by way of negotiation the concession period in the absence of which will be 7 years.

At the end of this Chapter, students should:

- Be able to understand the basic principles underlying Work on Goods Contracts and Construction Contracts,
- Understand the differences between Government construction contracts and civil construction contracts, in the process of contract formation.
- Be able to efficiently manage the various contract documents, and
- specifically determine the respective rights and obligations of the parties in the construction contracts and Works on Goods.

2.1 Work on Goods[30] and Construction Contracts

To understand the distinguishing features of works-on-goods and construction contracts, it is better to look at Finsen's statements. He works is worth reproducing here:[31]

The conventional building contract, in which the contractor undertakes to supply all the labour and materials and to erect and complete the building is a contract for the letting and hiring of work- ***locatio conductio operis****- and is one of the species of entire contract, also known as synallagmatic, reciprocal or bilateral contracts, i.e., one in which each party undertakes obligations*

[30] The Authors are not comfortable with the heading 'contract of work and labor' given to the legal situation that is treated under the provisions. Thus, we prefer to give it the naming the European legal scholars use for the same legal situations.

[31] Eyvind Finsen, *The Building Contract: A commentary on the JBCC Agreements*, 2nd ed, (Juta and Co Ltd: Cape Town, 2005), p. 16 (Hereinafter 'Finsen').

towards the other, and neither is entitled to enforce the contract unless he has performed or is prepared to perform his own obligations. Such performance may be simultaneous or sequential, i.e., one after the other. A contract of sale is a typical contract in which the parties perform simultaneously, while a building contract is a typical example of one in which one party performs his complete obligation before the other is requiredtot perform his side of the bargain- the contractor builds, and once the work is complete, the employer is obliged to pay for it.[32]

Thus, a contractor who claims payment before he has completed the work in all respects may find his claim is countered by the doctrine of *exceptio non adimpleti contractus*- a response that, in effect, says 'regardless what I may eventually be obliged to pay you, I am not obliged to pay you one cent until you have finished your work'.

According to Finsen,[33] in *locatio conduction operis*, the *locator*- the person who does the work- is an independent contractor and not an employee of the *conductor*- the person for whom he performs the work- and he is free to perform it in his own manner and time, provided that he completes it by the agreed time. He is free to carry out his work in whatever manner he chooses in order to fulfill his side of the bargain. He can work whatever hours he likes can and employ whomsoever he wishes. He can, if it suits him, perform the work at very slow pace for the first half of the contract period and then put on a great spurt of speed to finish the work within the agreed time.

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[32] Finsen says, "This is the common-law position which is invariably modified contractually", and that unless the parties have agreed to vary the common law, the contractor has to perform entirely before he becomes entitled to payment by the employer.

[33] IBID

Unless there are specific conditions to the contrary contained in the agreement, the employer cannot complain if the builder does any of these things. His only concern should be that he gets the building properly constructed with sound materials not later than the end of the agreed contract period.

The locator accepts the risk of loss or damage to the work until it is completed and delivered to the conductor. He is delictually liable for any loss or injury to third parties that may be caused by his execution of the works. The *conductor* is not normally vicariously liable for any damage that the *locator* may cause to such a third party. The *locator* may employ workmen to assist him in carrying out his contractual obligations, and he may subcontract portions of the work to subcontractors with or, at times, without the authorization of the employer. Therefore, in the absence of special agreement, he is not entitled to any payment until he has completed the work and delivered it to the *conductor*.

Work-on-Goods may generally be referred to as the contract of work that results in a new chattel or goods and works of repair on an existing chattels or goods, with the necessary materials or parts thereof supplied by the workmen or the client or jointly by the workmen and the client. On the other hand, from perhaps a very rudimentary definition, a construction contract is meant that contract for the supply of materials or the carrying out of work or any combination of the two, upon the land of another and which will become fixed to and part of that land.

What makes, among other things, the formation of a building or civil engineering construction contracts is that while it is and has been possible to depict what the employer, builder, client, or owner wants

in his/ her construction project through 'plan, scheme or other documents'[34] such as drawings, bill quantities, schedule of rates, designs (structural, architectural, electrical, sanitary, etc), it has been difficult in the effort of bringing the parties' mind to meet, where numerous plans and specifications are involved. In the nature of things, these authors admit it is impossible to draft a building contract with its numerous plans and specifications, which will be mathematically exact. This is why the Civil Code provides two types of descriptions in which the work to be done. It may have sufficient description or general description. Art. 3206 provides thus:

Art. 3021. — Work to be done. — 1. Sufficient description

(1) The work to be done may be described by means of a plan, scheme or other document.

(2) The contractor shall in such case comply with the indications given in such documents.

Art. 3022. — 2. General description

(1) Where the work to be done has been described in a general manner, the contract shall be construed in a restrictive manner as regards the importance of such work.

(2) Prior to undertaking a work, the contractor shall, whenever this appears reasonable, satisfy himself that the client agrees to the work to be undertaken.

On top of this, one needs to keep in mind all the proclamations, regulations, directives that may be issued both at the Federal and State legislator levels and that can directly have an impact on the negotiating balance of the contracting parties. What makes this proclamations, regulations, and directives more slippery is that they

[34] Art. 3021 of the Ethiopian Civil Code (ECC)

are not only scattered in many pieces of legislative enactments, but they are also to be comprehend difficult time.[35]

Moreover writer correctly depicted it:

"Construction Contract documents often consist of hundreds, if not thousands, of pages of General and Special Conditions and addenda to those conditions that eliminate, change, or add important language. Government and quasi-government agency rules and regulations are incorporated into the contracts. Furthermore, there are technical specifications describing materials, construction methods, and requirements. To this are added 50 to 100 or more plans detailing the building and its many services. To complicate matters, the plans and specifications are often changed before bid time by addenda that sometimes describe plan changes by word rather than by revised drawings. It is impossible to avoid contradictory and erroneous information in this mass of documents."

In an ideal construction contract, all the terms are expected to be clear, unambiguous, and sufficient. As indicated above, however, a lot is left to be desired in the construction industry. In a construction contract, if parties dislike the outcome of their negotiation, we think, they would be quick to resort to Art.1714 of the Civil Code to get it avoided for the absence of clarity in their contractual obligations. More often than not, the contractual terms are dubious; documents contradict with one another; the details of the contract are differently depicted in the plan (design), differently written in the bill of quantities, etc. There may be a time for complex projects where the architect puts the architectural design; the Civil Engineer supplements it with the structural design; the Electrical Engineer,

[35] These may include federal and state public procurement proclamations, regulations, directives, national building codes, standard conditions of contract, urban planning regulations, etc.

Sanitary Engineer, and the Quantity surveyor do their respective assignments on the project; all of them working separately and independently. In such a situation, each profession must read one another carefully and meticulously.[36] Thus, one needs to carefully observe, at least, the consistency in the architectural design, structural design, sanitary design, electrical design, the bill of quantities, the specification, etc.

As it is clear from the above provisions, the parties should discuss and negotiate over all the terms and conditions of the contract. If there are disagreements on one or more issues of the terms of the contract, the contract is not yet completed. Exceptionally, however, parties may conclude contracts without having reached a consensus over all the issues in the negotiation. You may ask, however, as to what will happen to those terms that the parties have not reached a consensus? Or where do we strike the balance between **conclusion of a contract** without reaching an agreement over some of the terms and **the non-conclusion** for failing to agree over some of the terms of

[36] In our country, all the afore-mentioned professionals can form up a firm together. For example **Grade I: Consulting Engineers and Architects (designs a project whose estimate value exceeds Birr 30,000,000)** need to fulfill the following staff requirements in addition to the capital, office area, and office facilities requirements: two practicing professionals, three professional architects, two professional structural engineers, one professional electrical engineer, four associate graduate engineers, three graduate architects, seven engineering aides, three secretaries or its equivalent staffing strength. If the estimate value of the project is as stated above, then, only a professional architect does the architectural design (Ar); a professional structural engineer does the structural design (St); a professional sanitary engineer does the sanitary design (Sn). A professional electrical engineer, and a associate engineer do the electrical design (El) and quantity surveying respectively. See the directives issued by MoWUD, Office of Architectural and Engineering Consultants for determining the minimum requirements for the various categories (Issuing year: not indicated).

negotiation? It should be clear that those terms that the parties have not reached an agreement should be the ones that are **determinable** in the near future or according to the circumstances. Thus, as indicated under Article 1695(3) of the Civil Code, the law can remedy the deficiency in the agreement of the parties; 'trade usages' or customs can also give the solution.

It is necessary, therefore, that there must be a definitive offer and acceptance to avoid the risk that is recurring in the construction industry. Every set of contract documents must define what is to be constructed, and explain where, when and how they work is to be executed. Here, of particular importance in the Works on Goods contracts is the fact that 'silence may amount to acceptance' as per Article 2612. Art.2612 states thus:

Art. 2612. — Implied acceptance.

(1) Where a person has publicly offered to execute a certain task or where the carrying out of this task is within his professional duties, a contract of work and labour shall be formed where such person, having received an offer, does not immediately refuse to carry out the task which has been ordered.

(2) The same shall apply where a person is appointed by the public authorities to carry out a certain task and does not immediately refuse to do so.

One needs to note, therefore, that an immediate refusal is necessary to reject an offer made by the client in the formation of Work on Goods contracts.

At this juncture, it is also good to note that, by virtue of Article 2611 of the Civil Code, Articles 2610-2631 are applicable for Works on Goods contracts. However, these provisions are also applicable for

building contracts “where total cost of the building to be done does not exceed Birr 500.”[37]

Whilst Article 2611 of the Civil Code states that the provisions on Work on Goods contracts are applicable for buildings whose contract price does not exceed Birr 500, Article 3019(2) of the Civil Code provides that Arts.2610-2631 are applicable for building contracts of whatsoever price so long as they are not inconsistent with the Building Contracts Law under Articles 3019-3040 of the Civil Code. The afore-mentioned provisions are, thus, reproduced herein under *verbatim*:

Art. 2611. — Building undertakings.

(1) The provisions applicable to contracts of work and labour relating to an immovable are laid down in the title of this Code regarding "Contracts Relating to Immovables" (Art. 3019-3040).

(2) The provisions of this Chapter shal,l however apply where the total cost of the building to be done does not exceed five hundred Ethiopian dollars.

Art. 3019. — Applicable provisions.

(1) The provisions of this Chapter shall apply to contracts of work and labour relating to work to be done in connection with the ***building, repair or installation of immovables.***

(2) The provisions relating to contracts of work and labour laid down in the Title of this Code relating to "Contracts for the performance of services" shall also apply where they are not inconsistent with those of this Chapter (Art. 2610-2631).

Note, for example, the application of the warranty against defects and non-conformity provisions in Art.2622 of the Civil Code. Whilst legal

[37] Art.2611(2) of the Civil Code.

warranties against defects and non-conformity for the Work on Goods contracts is to be treated under the Sales Law provisions for warranties against defects and non-conformity, it is separately dealt with when it comes to the warranty against defect in the construction contracts.

Furthermore, a reading of Art.2616 of the Civil Code makes it clear that Works on Goods contracts are distinguished from a contract of employment in that the provision states that the contractor remains not only independent of the employer or client but also free to "carry out the task as he wishes" and is bound to comply only with the rules of the profession in addition to those orders from the client he specifically committed himself to respect at the time of contracting. In other words, the law has the presumption that the contractor is the 'master of his Art'. Corollary to it, therefore, the contractor should draw the attention of the client to any matter which he considers night may create a problem. As it has been said in the French legal system:

> *"He must not carry out with his eyes shut that which has been ordered nor without making reservations must he undertake work in accordance with drawings which he considers contain a mistake."* [38]

The same approach seems to have been adopted in our legal system where the contractor has the duty to exert his reasonable skill and experience to check or examine the materials and tools that are supplied by the client and, if found defective, he has to immediately give notice of the defect to the client for a decision whether to use

[38] P.D.V Marsh, *Comparative Contract Law: England, France, Germany*, (Gower Publishing; London, 1994), p.185.

them or not. In other words, he may not follow blindly the order of the client.

In a similar fashion, the following analogy can be used to the construction contracts as it is used in France in that:

… the contractor should examine the materials and, if he has doubts as to their suitability, then he must warn the employer with reasons for his reservations and obtain a definitive decision from him. If the employer were to confirm the instruction then the employer would assume the total responsibility. However, the contractor should still not follow the employer's instructions if to do so would mean constructing a building the solidity of which in his professional opinion would be seriously in doubt. To do so would put the contractor at fault."[39]

2.2 Public Construction Contracts: The Procurement Law

Government contract placing is not left to the whim of the individual power holders at the various hierarchies of the government structure. What officials of the Government do with the public expenditure should be transparent, and those wielding the power should be accountable to the general public for each and every activity that they do and have it done on behalf of the public. The Constitution of the Federal Democratic Republic of Ethiopia, under Article 12, titled as 'the Conduct and Accountability of Government', provides thus:

> *The Conduct of affairs of Government shall be transparent.*
>
> *Any public official or an elected representative is accountable for any failure in official duties.*

[39] IBID, p.184

A Nigerian writer Yemi Akensaye-George explains what the term 'accountability' as follows to:[40]

The obligation of public officers and institutions to submit their activities to scrutiny by the members of the public and by the organs and institutions of government authorized by the Constitution to carry out such scrutiny. It is concerned with the establishment of procedures and institutions that will deter and detect wrongdoings. A government is accountable if its activities are exposed to the searchlight of public scrutiny, including that of the opposition. Transparency is a key element of accountability. It simply means that public officials and institutions must be answerable and accessible to the press and to the general public. The government must be ready to answer questions and supply information about its activities to establish a government organ that, inter alia, sees to it that the Procurement laws are properly and legally implemented by each and every 'procuring entity' the public unless in the interest of the public to withhold such information.

Thus, on the one hand, to promote transparency in the process of government contract formation and, on the other hand, to make officials involved in public procurement processes be accountable, and thereby curb wide and expansive corrupt practices in their territories, governments have been trying hard to come up with the best possible modern procurement rules. Ethiopia, has issued a modestly modern procurement proclamation to which all government bodies should comply with in the process of their procurement needs for the supply of goods, services, and construction works. The proclamation is

[40] Yemi Akinseye-George, Legal System, Corruption, and Governance in Nigeria, (New Century Law Publishers: Lagos, 2000), p.67

referred to as “The determining procedures of public procurement and establishing its supervisory agency Proclamation No.430/2005”. (We will be referring henceforth to the Proclamation as “The Federal Procurement Proclamation”). Thus, the Proclamation both sets up the procurement procedures in all federal government bodies and establishes a Federal body that supervises the proper implementation of the procurement procedures. As per Art.5(1) of the Proclamation, the Ministry of Finance and Economic Development (MoFED) issued Procurement Directives that further strengthen and clarify the procurement laws. (We will be referring to it as “the Federal Procurement Directives”). The Federal Public Procurement Law defines procurement as “…the purchasing, hiring or obtaining by any other contractual means of **goods, works and services.”** It further defines ‘public procurement as “…procurement by procuring entities using public funds”. The procuring entities are defined to mean “… public body, which is partly or wholly financed by federal government budget, higher education institutions and public institutions of like nature”.

Perhaps this discussion might have been proper in a different forum. But the fact that procurement corruptions are rampant in Ethiopia and it is particularly severe in the procurement of construction contracts or public works contracts it is worth to give it proper place here.

Under the Proclamation, will the exception of the situation where the Minister for MoFED, in consultation with the pertinent body, decides to procure goods, services and works other than those procedures given under it for **national security or national defense interests**, all procurement needs of the Federal Government at all levels should comply with the prescribed methods of procurement.

This is basically to ensure the applicability of some basic principles that have developed in the procurement processes: which include:

- Transparency;
- Fairness;
- Market competitiveness;
- Non-discrimination;
- The best value for money;
- Economies of scale;
- Efficiency;
- Economy, and;
- Effectiveness.

Briefly, the Procurement Proclamation, thus, provides for some definitions of basic terminologies including 'public works', the public accessibility of the legal texts on procurement, the establishment, responsibilities and powers of the Federal Public Procurement Agency (FPPA), some basic procurement rules, the list of procurement methods and the conditions for applying them, the procedures that should be followed in applying them, complaint handling and, finally, the procurement crimes and their concomitant punishments.

Most importantly, therefore, the Law provides the following as the procurement methods to be complied with:

- The Open Bidding (tendering): national and international;
- The Restricted Bidding (tendering): national and international;
- The Request for Proposal (RFP);
- The Request for Quotations (RFQ) or the oft-cited "*Pro Forma*";
- The Two-Stage Bidding (Tendering);

- The Direct Procurement, and,;
- The Micro Procurement (Low-Value Procurements);

The specially-permitted procurement procedure to be employed for protecting the 'interest of national security or national defense; when the Minister of MoFED, in consultation with the relevant public bodies permit it with the caveat that even then, it should 'serve the interest of economy and efficiency'.[41]

Space constraints do not permit an extensive consideration of the aforementioned procurement methods, but the gist of the provisions is worth mentioning here.

We should start by mentioning, in passing, that the Ethiopian Procurement system is two-tiered; the Federal Procurement system, and the State Procurement system. This is to say that there can be nine state procurement laws and one that of the federal government. This is, of course, assuming that the self-governing Federal Capital City of Addis Ababa and the Federal Enclave City of Diredawa are yet to see whether they can enact their own procurement laws. It depends on how much legislative power the Federal Government is willing to slate to the cities.

Coming back to the Procurement of public works contracts, therefore, one can easily gather that the Federal Public Procurement Proclamation, the Federal Public Procurement Directives, and the Federal Standard Bidding Document for the Procurement of Works as enacted by the HOPR, MoFED, and the Federal Public Procurement Agency (FPPA) are respectively, in order of importance applicable to all the Federal public works contracts procurement processes.

[41] Art. 3(2) of the Federal Public Procurement Proclamation No.430/2005.

For the States, this is different. Let us take the following, for instance; the Procurement Proclamation of the State of Tigray, No. 123/99, *Negarit Gazetta Tigray*, 15th Year, No.8, Feb.10, 1999 E.C; Procurement Directives No. 1/1995 of the State of Tigray, issued by the Bureau of Finance and Economic Development (BoFED), Mekelle, Tigray. We can also mention the Amhara State Public Procurement Procedure Proclamation (issued on March 22, 2006) and the Southern NNP Public Procurement Procedure Proclamation issued on March 23, 2006.

Open tendering is the preferred procedure of procurement. Under open tendering, the procuring entity (hereinafter 'PE') must prepare an invitation to tender as well as tender documents. The invitation to tender must be brought to the attention of those who may wish to submit tenders by advertisement in newspapers that have wide circulation within the country.

Other procurement methods include:

- The restricted Tendering, which is available if the costs of open tendering would be disproportionate to the value of the contract and the value of the contract is below the prescribed maximum.[42] Restricted Tendering is also available if there are only a limited number of suppliers. Restricted Tendering is similar to "open tendering" except that the invitation to tender is given only to selected persons.
- The "Direct procurement" which is available if there is only one supplier or if there is an urgent need, or if the procurement is for goods or services in addition to those

[42] Birr 1,000,000 for the Procurement of Works and Birr 250,000 for Goods and Services. See Art.7 of the Federal Public Procurement Directives

already supplied under another contract. In this procedure, a Government's department negotiates directly with the supplier.

- The "Request for Proposals" which is available to procure services that are advisory or are of a predominantly intellectual nature.[43] In this procedure, the procuring entity invites expressions of interest by publication of an advertisement in the press. The Procuring entity determines which persons who express interest are qualified to be invited to submit proposals. The proposals that submitted are evaluated and the procuring entity negotiates a contract, subject to limitations which are set out with the person whose proposals is successful.
- The "Request for Quotations" (*pro forma*), which is available to procure goods that are readily available and for which there is an established market. In this procedure the procuring entity prepares a request for quotations and gives it to selected persons. The successful quotation is the one with the lowest price that meets the requirements in the request for quotations.
- The "Micro (Low-value) Procurements" is available only for procurement if the estimated values of the goods, works, or services are at or below the prescribed maximum.[44]

Thus, we can see that government procurement contracts for works are effected through tendering.[45] Once the tender proceedings are

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[43] Art.46 of the Federal Public Procurement Proclamation No.430/2005

[44] Art.10 of the Federal Public Procurement Directives

[45] As we have indicated earlier, students are referred to the Proclamations and Directives in the Federal Government and the States for further readings and studies.

carried out, and the lowest bidder or the 'most economically advantageous tender (MEAT)' is selected, the contract is concluded. Sykes has described it correctly every contract may consist of a collection of individual, mutually dependent documents such as:[46]

- the contract agreement
- the letter of acceptance[47];
- the tender;
- the conditions of contract;
- the specifications;
- the drawings, and;
- the bill of quantities ;

Quite often, the inconsistencies and contradictions in the documents forming up the construction contracts are pervasive. To avoid these intricacies, the parties need to set the order of priority. For example, the PPA Standard Bidding Document for the Procurement of Works (2006) puts the order of the priority of the contractual documents as follows:[48]

- Agreement;
- Letter of Acceptance;
- Contractor's Bid;
- Special Conditions of Contract;
- General Conditions of Contract;
- Specifications;
- Drawings;

[46] John Sykes, Construction Claims, (Sweet and Maxwell: London, 1999), p.66, hereinafter 'Sykes'

[47] Particularly more important in Government Construction contracts as the acceptance of the bid offer and the communication of the award winner is carried out through the letter.

[48] Art.2.3 of the Standard Bidding Document for the Procurement of Works issued by the PPA (January 2006).

- Bill of Quantities or Activity Schedule, and;
- Any other document listed in the Special Conditions of Contract as forming part of the Contract.

Summary

It has been tried to explain the difference between Work on Goods contracts and Construction contracts, on the one hand, and the difference between civil construction contracts and public works contracts, on the other hand. Works-on-Goods contracts have the nature of construction contracts. In fact, construction contracts law of Ethiopia heavily relies on the provisions governing the Works-on-Goods contracts.

It is also good to note, in light of the pervasive infrastructure projects by the Government in Ethiopia, that civil construction works and public works contracts are differently treated. This difference is not only manifested in the different treatment accorded to the public works contracts under the Civil Code/ Administrative contracts provisions, but also significantly in the manner of the formation of the contracts. The strict regulations in the process of awarding public works contracts and in the selection procedures of the rightful contractor should be reckoned here. This is aimed at maximizing the taxpayers' money and creating integrity as well as corruption-free acquisition of government property. Thus, the procedure is ideally devised to meet the objectives of transparency in government functions obtaining the best value for money, non-discriminatory, competitive, and fair environment in the process of the formation of government contracts in general and construction contracts in particular.

The procurement methods are described briefly to give some highlights to students. It should be noted that the documents in the formation of construction contracts are bulky and drafting a construction contracts needs the investment of careful and wise arrangement of the terms used and the documents adopted.

Review Questions

The Ethiopian Shipping Lines enters into a contract with a domestic company named 1. Fast Works PLC for the construction of a medium-sized Ro/Ro type of ship that

the Shipping Liner wants to use for transporting containers from the Port of Djibouti to the Port of Eden in Yemen. If you were to draft the contract, would you classify it as a construction contract or as a Work on Goods contract? Why? Would it make a difference for you if the contract were for a ship repair contract?

2. In terms of the Civil Code provisions governing the Civil Construction Contracts and Work on Goods contracts, where do

they differ? and where do they overlap?

3. Why is the formation process of Government Construction Contracts different in its method and seriousness from the Civil Construction contracts?
4. What do we mean by ‘Entire Contracts’? Look at the construction contract as an entire contract: If you were the contractor, do you think it is fair? If you were the employer, do you think it is fair?

CHAPTER THREE
THE ROLE-PLAYERS IN CONSTRUCTION CONTRACTS AND TYPES OF CONSTRUCTION CONTRACTS

Introduction

A construction contract, unlike ordinary contracts, is one that involves not two but, multiple parties. The process of concluding a construction contract has many complicated tiers as it takes a long period of time to conclude and to perform. Accordingly, there are different parties to be involved in a construction contract. A typical construction project involves at least five parties; the employer, the architect, the civil engineer, the quantity surveyor, and sub-contractors. The different parties usually sign different contracts with one another. The major contract, the one that deals with the project as a whole, is mostly signed between the employer and the engineer, being a prime contractor. The architect and others may sign independent contracts with the employer; whereas, the sub-contractors mostly enter into agreement with the prime contractor.

It has been established that a contract is the basis for the relationship between the different parties involved in a construction contract. Before signing a construction contract, it is essential to know the types and choices of contracts so as to protect oneself. In any construction contract, the cost of the project consists of the cost for labor materials and the builder's profit. The different types of construction contracts vary primarily in regard to who has to pay for cost over runs and who keeps the savings if the project costs less than that of the estimated one.

This chapter introduces readers to the different parties that are involved in the conclusion of construction contracts along with their respective obligations. It, then, moves on to familiarize readers with the major types of construction contracts that are widely applicable in different parts of the world, including our country.

Unit Objectives:

At the end of this chapter, students should be able to:

- Identify the different parties involved in a construction contract;
- Identify the obligations of each party involved in a construction contract;
- Appreciate the basis for the different types of construction contracts, and
- Identify the major types of construction contracts.

3.1 Parties and Their Respective Obligations

We have seen above that there are various parties involved in a construction contract and that each party has his/her own respective obligations. Here, we will look at the parties and their respective obligations in a more elaborate manner. In the strict sense of the term the parties involved in a construction contract are the employer and the contractor. The others are not normally included in the contract. However, they have to be addressed as they are part of the project and may even be included in separate contracts.

Finsen writes

> *The parties to a building contract are, on the one hand, the person who wishes to have a building built for himself, who is generally referred to in building contracts as the employer, and, on the other hand, the builder who carries out the work, generally referred to as the contractor. Architects, quantity surveyors, engineering consultants, etc. are not parties to a contract in that they do not acquire legal rights or obligations, but they are nevertheless charged with many duties as agents of the employer and have their own contracts with the client.*[49]

3.1.1 The Employer (Client)

The employer is the person for whom the project (construction) is being undertaken.[50] This person may be variably referred to as 'client, project owner, or developer'.[51] Employers may be divided into two categories: those who erect buildings for their own ownership and use, whether they intend to inhabit and use the buildings themselves or let them to others, and those whose intention is to sell the buildings as soon as they can, possibly even during the construction phase, so that they can recoup their capital with a profit, and embark on further

[49] Finsen

[50] Michael Gunta, Ye Construction Wool Gidetawoch, Ethiopian Bar Review, Vol. 1, No. 1, 2006, PP. 131-145 [Hereinafter referred to as Michael Gunta]

[51] Though different terminologies, or phrases or terms have the same definition and may be used interchangeably the term 'employer' has been chosen as a point of reference for this text as it has a wider applicability.

building projects.

The primary obligation of the employer is to pay the contractor for the work carried out. To this end, almost all types of construction contracts are required to make provisions for the payment of contractors. In addition to payment, the employer has further obligations which arise from the very nature of construction contracts. In order to complete the contract, the contractor requires the full cooperation of the employer. Accordingly, the employer is expected to cooperate whenever the work that the contractor is undertaking requires the employer's cooperation. On another note, the employer is expected to refrain from hindering or wrongfully interfering with the performance of the contract.[52] On projects involving multiple contractors, the owner has an implied duty to coordinate the contractors' work so as to avoid substantial interference between the contractors thus causing unreasonable delays.

On a more implied note, the employer is obliged to give possession of the site in a reasonable time so as to allow the contractor to complete the work by the tie sent in the contract. Accordingly, the contractor is entitled to sufficient degree of possession so at to permit execution of the work unimpeded by others. To this effect, the Standard Building Contract with Quantities state that "… on the Date of Possession, possession of the site shall be given to the contractor … who shall … proceed regularly and diligently … to complete the same on or before the completion date."[53] If the employer delays the giving of possession, then that will be considered as an entitlement for the

[52] John Adriaanse, Construction Contract Law, 2nd Edition, Palgrave Macmillan, 2007 (Hereinafter Adriaanse)

[53] Clause 2.4, Standard Building Contract with Quantities, 2005 Edition (Hereinafter, SBC)

contractor not only to an extension of time to complete the work, but also to compensation for any loss and/or expense suffered as a result of the delay.[54] The owner also has an implicit duty not to actively interfere with the contractor’s progress as well as the implied duty to share all known material information that would be useful for the contractor to properly bid and execute its work.

3.1.2 The Architect

The architect is the person who is employed by the employer so as to design the project and oversee that the construction is being undertaken as per the contract.[55] He/she, thus, designs the plans and specifications for the construction. An architect is a person who designs buildings and superintends of their erection. He is both an advisor, and an agent of his client. Only persons registered as an architect in terms of the Architects' Act 1970 may hold themselves out as an architect. An architect is required to be familiar with all the statutory, or other legal requirements, or limitations on the design of his client's building and to ensure that his design complies with them (Finsen, 1999; Murdoch, 1996; Van Deventer, 1993).

Usually, the architect enters into a contract with the employer as an agent of the employer. Accordingly, he/she has the duty to act fairly and professionally as the agent of the employer. The employer and the architect enter into an understanding that where the latter has to apply his/her professional skill he/she will act fairly and in an unbiased manner in applying the terms of the contract.

3.1.3 The Civil Engineer

[54] Clauses 2.24 and 2.29, SBC

[55] Michael Gunta

The structural design of contemporary buildings, and the design of their mechanical and electrical installations, has become so sophisticated and complex that it is beyond the technical knowledge and experience of architects, and is, therefore undertaken by engineers trained and experienced in this type of work. Like the other members of the professional team, the engineer who is normally signed an agreement with the employer of the building, and is liable to his client for any negligence in the execution of his professional duties.[56]

Construction engineers have a lot of responsibilities. Analyzing reports is the main part of their job description. They must analyze maps, drawings, blueprints, aerial photography and other topographical information. It is the construction engineer's job to make sure that everything is conducted correctly. Accordingly, they have to see the safety of all the workers undertaking the construction works. In addition to safety, the construction engineer has to make sure that the site stays clean and sanitary. Surveying the land while construction is in progress is also the construction engineer's responsibility. Construction engineers have to make sure that there are no impediments in the way of the structure's planned location and must move any that might exist. They also must estimate costs and keep the project under budget. Construction engineers have to test soils and materials used for adequate strength. Finally, construction engineers have to provide construction information including repairs and cost changes to the managers of the construction work.

To this end, construction engineers have many activities that they must do every day. Those activities include drafting, decision making,

[56] Finsen

computer interaction, communication, documentation, creative thinking, organizing, information collecting, estimating and analyzing. Construction engineers use drafting to design structures and show it to on others how to build them. They have to analyze information and make the best decision and solve problems. Computers are important tools used by construction engineers. They use them to write programs and solve equations. Communication is used everyday to interact with co-workers and supervisors. Documentation is used to record important information that needs to be passed on to The management. Most documenting is done electronically. Creative thinking is used to come up with new ideas and to solve problems. Construction engineers have to be organized to accomplish goals and prioritize jobs. They have to gather information on the task at hand before they can start a project. This will help them to ensure that the job is completed correctly. In order to keep a project under budget, construction engineers have to estimate costs of materials and workers. Finally, they have to analyze data to find answers to problems that they encounter on the job site.

3.1.4 The Quantity Surveyor

The quantity surveyor is a person who calculates the quantity of labor and materials that are required to erect the building and compiles this information in a document known as a bill of quantities, which is used by tenderers as a basis for estimating the cost of the project and formulating their tenders. As an agent of the client, the quantity surveyor prepares preliminary estimates of cost, advises on the value of interim payment certificates, evaluates claims for extras and determines the proper value of the final account. In recent years the quantity surveyors have been able to advise a client on a project’s future running and maintenance costs and the income it may be

expected to generate by way of rentals. During the course of the contract, he predicts the employer's cash flow in respect of monthly payments to the contractor, and continuously informs the employer about on variations to the contract price caused either by cost fluctuations or changes to the design, or specification. The profession of quantity surveying is governed by the South African Council for Quantity Surveyors, a statutory body established in terms of the Quantity Surveyors' Act 1970, which supervises the education of the quantity surveyors, registration of administers their deals with infringements of the rules of professional conduct.[57]

The quantity surveyors play a key role in the organization and financial management of the construction projects. In essence, they manage projects to ensure that they are built on time and budget. Their job is to manage costs effectively and to ensure that they get the best value from contractors and suppliers. This involves obtaining tenders, arranging contracts, and managing costs for the client while the works are being undertaken. It is also their job to negotiate with the client’s representatives on payments and the final settlement.

3.1.5. Sub-Contractors

Subcontractors are persons employed by the contractor so as to undertake part of the construction work.[58] The contractor has to first secure the consent of the employer before he/she can hire any sub-contractors. Essentially the typical standard form for subcontracting is designed to achieve a mirror image of the main contractual provisions. As the trend towards subcontracting developed, employers saw the opportunity of getting the best of both worlds, and the

[57] Ibid

[58] Michael Gunta

nominated subcontract was introduced which enabled the employer to have the benefit of a principal contractor to control the entire building operation while yet being able themselves to choose specific subcontractors to undertake specific work.[59]

Although the construction contract is made between the employer and the contractor, subcontractors are the ones that do most of the work. As a general rule, the contractor is the one liable for the work carried out by the sub contractor. In the words of HHJ Lloyd,

> *On virtually all building contracts of any magnitude, the role of the contractor is to sue his management know-how not only to procure the requisite skills but also to know whether and to what extent they are being provided adequately to meet the requirements of the contract.*

3.2 Types of Construction Contracts and Risk Allocation

Before signing on a construction contract, it is essential to know the types and choices of the contracts we have so as to protect ourselves. In any construction contract, the cost of the project consists of the costs labor materials as and as the builder’s profit and overhead. The different types of construction contracts vary primarily with regard to who takes the risks involved, which party has to pay for the cost over runs and who keeps the savings if the project costs are less than that of the estimate one.

3.2.1 Lump Sum Contracts

A lump sum, sometimes called stipulated sum, contract is the most

[59] Finsen

basic form of construction contract. Keating defines a lump sum contract as a contract to complete the work for a lump sum, i.e. whereby the contract promises to build X project for Y dollars.[60] In this type of contract, the supplier (contractor) agrees to provide specified services for a specific price. The receiver (employer) agrees to pay the price upon the completion of the work, or according to a negotiated payment schedule. Lump sum contracts require complete plans and specifications setting forth detailed directions to enable the contractor carry them out. In developing a lump sum bid, the builder estimates the costs of labor and materials and adds to it a standard amount for overhead and the desired amount of profit.[61]

Most builders estimate profit and overhead to total about 12-16 percent of the project cost. This amount may be increased based on the builder's assessment of risks. If the actual costs of labor and materials are higher than the builder's estimate, the profit is be reduced. If the actual costs are lower, the builder gets more profit. Either way, the cost to the owner is the same. In practice, however, costs that exceed the estimates may lead to disputes over the scope of work or attempts to substitute less expensive materials for those specified.

Lump sum contract envisages an entire contract and a fixed price contract. It is an entire contract in that the contract, basically, is one where the contractor’s obligation to carry out the work is based on a condition precedent to the liability of the employer to pay. On another note, it is a fixed price contract in which where the contractor takes the risk of the work becoming more extensive than that of the

[60] Keating

[61] Michael Gunta

estimated previously.[62] Thus, a lump sum contract is an entire contract that implies that the contractor must finalize the work in accordance with the contract before he/she entitled to the payment agreed upon. Similarly, there is an implied obligation upon the employer to satisfy the specifications in all its aspects so that the contractor can properly and timely undertake his/her work.

3.2.2 Re-Measurement Contracts

Re-measurement contracts, in contrast to the lump sum contracts, are contracts in which the price to be paid for the whole work is to be ascertained by measurement in detail of the various parts of the work and the valuation thereof by reference to a schedule of prices included in the contract. Keating defines such type of contracts as one where the amount of work, when completed, is to be measured and valued according to a schedule, or formula, or at cost plus a fixed fee, or a percentage of the cost, or at a reasonable price.[63]

This type of contract is usually entered into when the extent and scope of the work to be done is not known at the time of entering into the contract. Therefore, in this type of contract, it is usually immaterial whether any particular piece of work that the contractor is required to do is included in the contract or not. This is because the contractor is entitled to payment for the piece of work at a stipulated rate, whenever applicable, or at a reasonable market price whenever the stipulated rate is not applicable. However, where the schedule of rates incorporated in the contract specifies a piece of work and its rate, it raises a question of construction with regards to whether that particular piece of work is impliedly included in that item being

[62] Building Contracts

[63] Keating

incidental or contingent. If so, it would not be classified as extra work to be paid separately.[64]

Re-measurement contracts imply that price is agreed for each piece of work and the quantities are counted or measured either as the work proceeds, or at the end of the completion of a particular item. Profit rate is included in the rate settled, or separately as a percentage agreed upon.[65]

3.2.3 Cost-Reimbursable Contracts.

In a cost reimbursable contract the contractor's profit is set at a fixed amount. If actual costs are lower than that of the estimated, the owner keeps the savings. If actual costs are higher than that of the estimated, the owner must pay the additional amount. The great advantage of a cost reimbursable contract is that, generally speaking, the project will result in the building that was envisioned, even if costs run high. The contractor is less likely to cut corners, or argues, for less expensive materials since his profit is not in jeopardy. By the same token, the contractor has little incentive to keep the owner's costs down.

Under this arrangement, the contractor is reimbursed for the actual cost of labor and materials, plus charges fee (typically an agreed-upon lump or percentage of the total costs) for overhead and profit. This arrangement seldom begins with a blank slate regarding specifications and costs. Rather, the consumer and contractor create a list of specifications and an estimated budget that matches to the specifications. Although the contractor under this arrangement will

[64] Building Contracts

[65] Ibid

have to keep copious records of its costs, most residential consumers in a cost-plus arrangement suffer from overspending. One way to prevent breaking the budget is to set a guaranteed maximum price. However, even the maximum price will not alleviate problems.

This type of contract is advantageous in the fact that, where the employer wants to have open reign to select materials and workmanship as the project proceeds, this arrangement can be extremely flexible and accommodating. This contract also typically requires the contractor to obtain competitive bids from subcontractors, and translating (in theory) it in to lower construction cost. It is disadvantageous since this type of contracts are usually used where the scope of work is uncertain, and the costs can quickly get way out of control. Even under the maximum price, poor control in materials selection and on-the-fly design modification can quickly consume budget, leaving line items on the project starved for capital. This, in turn, requires either a diminution in quality in certain aspects of the project, and /or the total elimination of aspects of the project, and /or the need for an additive change order to increase project funding.

Summary

One distinguishing feature of construction contracts from ordinary contracts is that the former include, not two but, multiple parties. The different parties to a construction contract are the employer (client) and contractors, on the one hand architects, civil engineers, quantity surveyors, and/or sub-contractors, on the other hand. The different parties usually sign a different contract with one another. All these parties have different obligations prescribed by the laws of the county in which they are licensed and registered as professionals. In addition

to these obligations, these professionals have various rights that are protected by law. In Ethiopia, as there is no law at present to govern construction relations, the applicable provisions of our Civil Code are applied in determining the rights and obligations of these professionals in their contractual relations relating to the building undertakings.

As already stated, a construction contract is an essential feature of any construction work that is sought to be undertaken. Accordingly, a person needs to know what type of construction contract he/she ought to sign so as to protect oneself better. The different types of construction contracts that are available vary primarily in light of risk allocation. The most commonly used types of construction contracts, including in Ethiopia, are lump-sum contracts, re-measurement contracts, and cost-reimbursable contracts. Lump-sum contract is a type of contract that is specifically addressed by the Ethiopian Civil Code whereas the others have got recognition in one way or the other.

Review Questions

1. Should failure to hand over possession of the site by the employer be considered as breach of contractual obligations?
2. What are the differentiating factors between the different types of construction contracts?
3. How do the construction contracts different from that of the administrative contracts?
4. What are the advantages and disadvantages of each type of construction contract?

CHAPTER FOUR
BASIC CONCEPTS AND THEORIES IN CONSTRUCTION LAW IN ETHIOPIA

Introduction

Our country is undertaking massive infrastructural expansions. Roads, bridges, multi-storey buildings, tunnels, hydroelectric dams, irrigation dams, ring roads, light rail transits (LRT) and railways are being, or set to be constructed here and there. These undertakings are basically funded either by the Government coffer or international grants solicited from international donors. Efforts are being made to fulfill the infrastructural needs of country. Whilst private building constructions and investments on various projects abound in Ethiopia currently, huge amount of the Government budget is also allocated for these massive public projects.

In carrying out such massive projects, the Government enters into construction contracts. The contract administration of these colossal projects is not immune from various claims and disputes. In resolving the disputes, the Government is confronted with the public interest *vis-à-vis* private interest dilemma in trying to the balance in protecting the public interest, the private interest.

It's hoped that you have already studied 'Government Contracts Law' before taking this Course. It is, proper to highlight the basic tenets of the Ethiopia Government (Administrative) Contracts Law so as to enable students to link it with the Public Construction Contracts Law.

In Ethiopia, Administrative Contracts Law is governed under the Civil Code provisions of Articles 3131-3306 (Title XIX). These rules, peculiarly that put under the Civil Code provisions, were introducted to the Ethiopian legal system by the Prof. David in 1960. These provisions establish that all contracts concluded by the administrative bodies or authorities are not necessarily administrative contracts. It is set that the administrative bodies can choose either to apply the administrative contracts law regime or the private contracts law regime. Some contracts that are concluded by the administrative bodies have, however, been classified by law to be as 'administrative contract'. These are Public Service Concession Contracts, Contracts of Public Works, and Government Supply Contracts. The applicability of the administrative contracts law regime in Civil Code has been defined under Article 3131. That provides:

> (*1) Contracts concluded by the State or other administrative authorities shall be governed by the provisions of this Code which relate to contracts in general or special contracts.*
>
> *(2) The provisions of this Title shall supplement or replace such provisions where the contract is in the nature of an* ***administrative contract.*** [Emphasis supplied].

Unit Objectives

At the end of this chapter, students should be able to:

- Clearly differentiate administrative contracts from construction contracts;
- Identify the different theories applicable to construction law;
- Analyze the conceptual bases of construction law;
- Assess the applicability of the different theories and concepts to

the Ethiopian context;

- Differentiate 'assignment' from 'sub-contracting; and
- Identify the conditions and effect of variation with regards to construction contracts

4.1 Key Concepts in Government Construction Contracts

4.1.1 The Theory of *l'imprévision*

The doctrine of *l'imprevision* is translated in the Civil Code as 'unforeseen circumstances'. This doctrine is treated under Article 3183-3189 of the Civil Code. As stated earlier, the Administrative (Government) Contracts Law that is incorporated in the Ethiopian Civil Code of Ethiopia is a consolidation of the case law of the French *Conseil d'Etat*. The theory of *l'imprevision* was masterminded by the French *Counsel d'Etat*. This is in stark contrast to that of the French Civil Courts that are, to date, reluctant to accept the concept in the Civil and Commercial law regimes.

Similarly, in Ethiopia, the theory is not applicable in the commercial and civil contracts law. Article 1764 states;

Art. 1764. - Modification of the balance of a contract.

(1) A contract shall remain in force notwithstanding that the conditions of its performance have changed and the obligations assumed by a party have become more onerous than he foresaw.

(2) The effect of such changes may be regulated by the parties, and not by the court, in the original contract or in a new agreement.

As you can understand from the above-mentioned Civil Code Provision, the court may not intervene in a situation where the conditions of contractual performance are changed, and the performance of the contract has become more onerous or burdensome. Thus, judicial variation (revision) of contractual provisions, once entered into with the full consent of the parties, cannot be materialized at the request of either party except in few exceptional circumstances enumerated under Articles 1766, 1767, and 1768. The above provision reflects the view that a contract remains unaffected by difficulties and unforeseen events if its performance still remains possible.

Indeed, a party should perform his/her contractual obligations. If he/she fails to discharge his/her obligation, the party is liable to breach of contract or to non-performance of the contractual obligation. Eventually, the other party may claim either forced (specific) performance, or cancellation, or cancel it on his own or damages (compensations), or opt for proportionate reduction. If, however, the failure of performance was not due to his own fault and is prevented from performing by circumstances whose occurrence the parties cannot reasonably envisage, then the parties' legal position will depend on the extent and severity of the supervening event. If, for example, a factual or legal nature makes the performance of the contract impossible, such as when the goods contracted for supply are destroyed due to lightning, or the factory producing *reinforced bars* is accidentally burnt, then the case may fall under the defense of the doctrine of impossibility or *force majeure.* This means that the non-performing party will not in such a situation be liable to non-

performance to the other party in so-far-as he/ she has exerted a reasonable effort and diligence to perform the obligations under the contract.

But let us suppose that the unforeseen change of circumstances does not exactly render it impossible for the debtor to perform the contract, but makes it so much more difficult or so vastly more expensive that the two sides of the contract are now quite out of proportion. What happens if one party can easily perform his contractual obligation, whilst the other party can perform it but under a strained situation where he/she can benefit nothing?

Let us say the contactor has to supply on its own all the necessary construction materials to the construction of a G+5 building contracted on the basis of the Lump sum contract. Now, after the construction had begun, the price of cement and reinforcing bars increased altogether 50-fold in the five months time for a reason that is completely unknown to the parties and what economists have called it 'hoarding'.

Should the contractor continue performing it on the price of the agreed Lump sum contract or require revision of the price? Why?
Is it fair for the court to refuse to grant any remedy at all to the contractor?
If it is not fair, what is the rationale of the Article 1764?
If it is not fair once again, should it be likewise for Government contracting?
It would have been of some help if the price of item rose due to an increase in customs duties.[66]

[66] Article 2319 of the Civil Code of Ethiopia

Let us see now how this situation may be dealt with under the Administrative Contracts Law regime. By way of summery, Articles 3183-89 of the Civil Code define the doctrine of *l'imprevision* as follows:

- There must be (a) new circumstance(s);
- The circumstances impose additional obligations (disturb the expected equilibrium of the contract);
- The new circumstances were beyond the extreme limits of expectations by the parties, and
- Despite the altered circumstances, there is material possibility to perform.

The following should be added to elaborate the concept of 'new circumstances' under item no.1:

- The unforeseen supervening event was beyond the reasonable envisioning at the contracting time (this is to say it did not exist at the time of contracting); or,
- It is an unforeseeable consequence of an existing event; or
- It is an unforeseeable extension of an existing event.

In addition to the afore mentioned legal provisions, Articles 3286-3287 provide the following statements on unforeseen difficulties:

Art. 3286. — Unforeseen difficulties. — 1. Principle.

(1) Where, in the performance of his contract, the contractor encounters material difficulties of an absolutely abnormal nature, unforeseeable at the time of the conclusion of the contract, he may require that the contract be revised.

(2) The administrative authorities with whom he has contracted shall in such case assume at their charge a part of the exceptional expenses due to such unforeseen difficulties, unless

they prefer to cancel the contract.

(3) The provisions of this Title relating to cases of unforeseen events shall apply in such case (Art. 3183-3189).

Art. 3287. — 2. Duty to consult administrative authorities.

(1) Where the difficulty compels the contractor to perform a supplementary work not mentioned in the contract, the contractor may initiate such work only after having obtained a requisition order from the administrative authorities enjoining him to perform such work.

(2) However, where the work is absolutely necessary for the performance of the contract and it is of an urgent nature, the contractor may and shall initiate it even in the absence of a requisition order.

(3) In such case, he shall be entitled to compensation in accordance with the provisions of this Code relating to the voluntary management of another person's affairs (Art. 2257-2265).

Thus, an unforeseeable difficulties increased fuel of prices in a situation were the fuel was a major element of the cost of the contractor that could entitle the contractor for an indemnification on the basis of the doctrine of *imprevision*.

4.1.2 The Theory of *fait du prince* (Act of Government)

Whereas *imprévision* concerns situations arising from unforeseen circumstances necessarily unrelated to the behavior of the parties, the doctrine of '*fait du prince*' is involved when the economic basis of the contract is upset by the act of government department itself. According to this doctrine, unless the governmental act some general legislation affecting all citizens equally, the contractor is be entitled to

a monetary indemnity or to increase the charge to the consumer.

4.1.3 The Non-applicability of the Doctrine of *exceptio non adimpleti contractus*

One of the basic objectives of a public service is enshrined under this doctrine. The public service does not have to be interrupted at any cost by the contractor; continuity of the service for the public interest must be ensured so that the public and the Government will be able to function smoothly without disruption.

Art.3177. _ Exceptio non adempleti contractus[67]

> *The non-performance by the administrative authorities of their obligations shall not entitle the other party to fail to perform his obligations unless it makes impossible the performance of such obligations.*
>
> *In other cases, the other party may not avail himself of the failure by administrative authorities to perform their contractual obligations in order to suspend the performance of the contract.*

The objective of the doctrine is that the public service is to continue

[67] The principle was re-written by George Krzeczunowicz under the title 'Revised Translations for Administrative Contracts Class' (Unpublished), and the Authors believe that it reflects the correct view of the legislature and is hereby reproduced:Art.3177. _ Exception of nonperformed contractThe nonperformance by an administrative body of its obligations entitles the contractant to fail to perform his own obligations only where it makes his performance impossible.In other cases, the contractant may not invoke nonperformance by the administrative body in order to suspend his own performance of the contract.

providing its services to the public and the contractor will be indemnified fully afterwards. Thus, contractors involved in Government Construction Contracts, properly qualified as an administrative contract, cannot stop the work or raise the defense of '*exeptio non adimpleti contractus'.*

The defense is not applicable in the civil contracts where it is an established principle that:[68]

...when, in the case of a bilateral contract, correlative obligations are due for performance, either of the contracting parties may abstain from the performance of his obligations, if the other party does not perform his obligations.

4.1.4 The Doctrine of Specific Performance

Specific performance is defined as: "...a process whereby the creditor obtains as nearly as possible the actual subject matter of his bargain, as opposed to compensation in money for failing to obtain it". Thus, when a court decrees specific performance, it orders the party who has broken the contract to perform, on penalty of being held in contempt of court if he does not.[69]

In Ethiopia, specific performance is a contractual remedy that is exceptionally awarded to the party seeking for it. Art.1776 of the Civil Code, thus, generally govern the applicability of the doctrine in the Ethiopian Contracts law regime. Art.1776 of the Civil Code states thus:

Art. 1776. - Specific performance

Specific performance of a contract shall not be ordered unless it is

[68] Art.161 of the Egyptian Civil Code as cited by Borham Atallah, p. 33

[69] Richard Posner, Perspectives on

of special interest to the party requiring it and the contract can be enforced without affecting the personal liberty of the debtor.

A promisee of a contractual obligation can claim specific performance only if two conditions are satisfied:

- The obtaining of the very 'thing' contracted for is of essential interest to the promisee, and
- If granted, specific performance should not affect the **personal liberty** of the promisor.

The Sales Law provisions of the Civil Code (Arts. 2329-2335) also provide for the preconditions that should be fulfilled so as to claim for specific performance where Compensatory Sale is not obtainable for the seller or Purchase-in-Replacement is not possible for the buyer. Art.2892 of the Civil Code also gives specific performance; a separate treatment as it relates to the sale of immovable property.

In an Administrative Contracts Law context, Art.3194 of the Civil Code provides thus:

Art.3194. _Compulsory performance of contracts

The court may not order the administrative authorities to perform their obligation.

It may, however, make an order for the payment of damages unless the administrative authorities prefer to perform their obligations.

Unless otherwise provided by law, it may also cancel such measures as have been taken by the administrative authorities in violation of their contractual undertakings.

From the above provisions, therefore, courts cannot order specific

performance against a Government Department for the performance of its contractual obligations. The law opts for the imposition of compensatory damages being awarded to the aggrieved contractor. The Government Department, however, may still opt for the performance of the contractual obligations when and if the Government Department finds it that the compensation to be awarded to the contractor is more harmful to the Department than discharging its contractual obligations.

The Court, however, misinterpreted the provision in the case *re HighWay v Solel Boneh Ltd.*
Although by Art.3194(1) of the Civil Code, a court may not order administrative authorities to specifically perform their obligations, a court is not thereby precluded from ordering specific performance of an agreement to submit disputes to arbitration.

Thus, while the above mentioned provision does not seem to permit any exceptional readings into it, the Court ruled that specific performance can be ordered against Government Departments notwithstanding Art.3194(1) of the Civil Code.

4.1.5 The Theory of I*mmixion*

Variations[70] in construction contracts are permitted by law and are common in practice. The theory of immixion amounts to an unacceptable interference of the employer or his agent in the performance of the contractor's obligations. The degree or threshold of the variation orders may depend largely on the type and breadth of the construction project. Nevertheless, it may amount to abuse by the employer, especially when the employer's interference disrupted the

[70] See the discussion below in Chapter Four.

organization of the contractor as compared to the normal expectation that an experienced contractor would have had at the time of contracting.

The following provisions in the Government Construction Contracts provide to what extent variation may be permitted. Articles 3284-85 provide thus:

Art. 3284. — 2. New works.

(1) The administrative authorities may, against payment of an additional remuneration, require the contractor to perform works which were not mentioned in the contract.

(2) They may not, however, require him to perform a work which by its object would be totally different to the work mentioned in the contract or which would have no relation to such work.

(3) Nor may they require him to perform a work under conditions entirely different to those which have been mentioned in the contract.

Art. 3285. — Rights of the contractor.

(1) Unless otherwise provided in the contract, the contractor may cancel the contract where the increase or reduction of the works as a whole required by the administrative authorities involves a variation of more than one-sixth of the cost mentioned in the contract.

(2) In the case of reduction of the works as a whole, he shall be entitled to a compensation equal to the loss suffered by him and profit of which he is deprived by reason of the variation of the contract.

(3) The court may limit the amount of compensation for deprivation of profit where it appears that the variation is due to extraneous

circumstances and not to the default of the authorities having made the contract.

4.2 Public Policy Considerations

4.2.1 *Quantum Meruit*, Substantial Performance or Strict performance to the Letter

In the previous chapters, we indicated that the employer is not obliged to pay to the contractor unless and until the latter performs his contractual obligations. Now, the question still remaining is: "When do we say that the contractor has performed his contractual obligations to satisfy the employer so that the contractor can be entitled for the payment?"

Historically**,** the sanctity of contracts has always been observed. No encouragement has ever been given to that loose and dangerous doctrine which allows a person to violate his most solemn engagements. However, it is also true that slight omissions and inadvertences may sometimes very innocently occur. The question is that "Should the employer be compelled to pay what the work was reasonably worth on *quantum meruit* when he takes possession of the building although the terms of the contract have not been fulfilled?"

A strict application of the doctrine of *quantum meruit* would force upon the employer a building, no matter how far it is deviated from the plans and specifications. On the other hand, one can easily gather the disadvantages to the contractor if he is absolutely denied of the right to claim some compensation for the investment he made on the building. Thus, it has been long a perplexing issue in the construction industry whether any legal system can strike the balance between the

two interests.

Some argue,[71] for example, that if the contractor had, in good faith, attempted to fulfill his contract, and had succeeded, except as to a few minor details, he should not be compelled to lose the contract price; it is his duty to remedy the defects or to make some allowances for such defects. Thus, [72] full performance of an entire contract was a condition precedent to claim thereon and that the doctrine of substantial performance has been recognized where the contractor acted in good faith and where the deviations from the plans and specifications were comparatively few and unimportant. Therefore, recovery was prevented either because the plaintiff willfully and negligently failed to perform, or abandoned the contract entirely.[73] In a leading American case, for example, the court said:

> *It is now the rule, that where a builder has in good faith intended to comply with the contract, and has substantially complied with it, although there may be slight defects caused by inadvertences or unintentional omissions, he may recover the contract price, less the damage on account of such defects.*

Thus, in many jurisdictions, the law tolerates slight or unsubstantial deviations. The problem is, however, the term ‘substantial performance’ may not be clear. Hence a critical question:

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[71] Frank McKinney, Substantial Performance in Building and construction Contracts, 28Bench and Bar 61, 1912.

[72] IBID

[73] IBID, at 62

Does it depend upon the **cost** necessary to remedy the defects in relation to the total cost of the building, or upon the **number of defects**, or upon the **character** of the defects?

There is no clear-cut answer to this question. It is said, however, "… *the rule of substantial performance should not be extended beyond the purpose in view when the relaxation of strict performance was adopted. This relaxation of the strict performance was founded upon justice and made applicable to cases where the contractor honestly intended to perform*." [74]

With this understanding, the 'substantial performance' doctrine has effectively downplayed the applicability of 'the strict performance to the letter' doctrine.

In Ethiopia, the object of construction contracts can be classified as one of 'to do' obligations. Let us see the following provision to make it clear.

Art. 1712. - Obligation to give, to do or not to do.

(1)A party may undertake to procure to the other party a right on a thing or to do or not to do something.

(2) The party who undertakes ***to do something may undertake to procure to the other party a specified advantage*** *or to do his best to procure such advantage*. [Emphasis supplied].

Thus, as it is clear from the provision, obligations are <u>to give, to do, and not to do</u>. Let's see some example.

Example 1: A sales contract of a car. The owner of the car delivers the car and transfers or procures to the buyer the right of ownership

[74] IBID, at 64

of the car.

Example 2: An advocate will enter into a contract with his client **to do his best in representing** him in the court to defend him if it is a criminal case.

Example 3: A doctor will enter into a contract with a patient to do his best to cure him/her.

Example 4: In a transfer of technology contract, the licensee obligates himself to refrain from copying the technology of licensor. The licensee also promises to the licensor not to sell products outside of the agreed territory.

Example 5: A contractor enters into a contract with a client (employer) to do the construction work; complete it and deliver it to the client.

This can easily be gathered from Article 2610 of the Civil Code on Contract of work and labor or properly termed as 'Work on Goods' contracts.

Art. 2610. — Definition.

> *A contract of work and labour is a contract whereby one party, the contractor,* ***undertakes to produce a given result****, under his own responsibility, in consideration of a remuneration that the other party, the client, undertakes to pay him* [Emphasis is added].

As we have tried to indicate earlier, construction contracts are types of synallagmatic or reciprocal or bilateral contracts for which one party can validly raise the defense of '*exceptio non adimpleti*

contractus',[75] The employer, for example, is entitled to the response states, 'Regardless of what I may eventually be obliged to pay you, I am not be obliged to pay you one cent until you have finished your work'.[76] Such types of contracts are also called 'Entire Contracts'. An Entire Contract can, thus, be defined as:[77]

…the complete fulfillment of the promise by either party is a condition precedent to the right to call for the fulfillment of the promise by the other.

Thus, the rule on *Quantum meruit*[78] does only apply in certain situations as precisely given by Bunni:[79]

A contract agreement exists but either:

- A precise price has not been agreed; or
  conditions agreed as a basis for not charging for a certain work do not eventually materialize; or
- an original contract has been replaced by another and payment is sought for work done under this new contract.
- Some times for one reason or another, a contract not exists. According to Nael Bunni, this situation could

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[75] The doctrine cannot, however, be invoked by a contractor or Consulting Engineer, or any contracting party for that matter, in the Administrative contracts law regime as discussed above under 4.1.3 of this Material.

[76] Eyvind Finsen, p.17

[77] IBID,p.16

[78] *Quantum meruit* is the basis for a claim or a remedy sought for the payment of a reasonable remuneration for work done or services rendered.

[79] Nael Bunni, FIDIC Red Book, p.64

arise where:[80]

- There has never been a contract; or
- a contract could have existed but is discharged and no new contract is substituted; or
- There is a presumption of the existence of a contract but this is later found to be without legal validity.

Therefore, we can conclude that whilst the contractor is not entitled to claim on *Quantum meruit* basis where we have a validly concluded construction contract, and that he/ she is only entitled for payment from the employer when he/she produces a given result (complete the work), the rule of Strict Performance to the Letter is not the preferred option for the obvious injustice that may be inflicted upon the contractor. Thus, in the absence of agreement to the contrary, only the rule of substantial performance of construction contracts puts the contractor on the podium to claim the payment from the Employer.

4.2.2 Liquidated Damages

Regulating, in advance, the potential damages that either of the contracting party may suffer, as the consequence of the other party's failure to perform its contractual obligations, is the order of the day in the construction industry. The contracting parties address this by incorporating a 'the Liquidated Damages Clause' to that effect. It is believed that the Liquidated Damages Doctrine is used widely in Common Law Countries. Nowadays, however, the Doctrine has received a welcoming arm in the construction contracts including in

[80] IBID

the Civil Law Countries. In Ethiopia, for example, it is now fully being put in use in all government construction contracts. The Doctrine might have made its entry into the Ethiopian Construction Laws via the FIDIC (Red Book) Form.

Nevertheless, it does not mean that the Civil Law Countries do not have a counterpart doctrine whereby the contracting parties to a contract regulate the amount of damages that will accrue to either of the parties should the other party fail to perform its contractual obligations. It is governed by the Penalty Clause.

Thus, let us see what the two doctrines look like. A certain author defined 'Liquidated Damages' as:

> *... a sum fixed up in advance, which is a fair and genuine pre-estimate of the probable loss that is likely to result from the breach.*

The same author, 'Penalty' as follows :

> *... a sum fixed up in advance, which is extravagant and unconscionable in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.*

Prof. Kuchaal states that courts in England usually allow 'liquidated damages' stipulated in the contract without any regard to the actual loss sustained. He also adds that " Penalty clauses, however, are treated as invalid and the courts in that case calculate damages according to the ordinary principles and allow only reasonable compensation." India gives its own treatment to the concepts. Kuchaal states further that the Indian law does away with the

distinction between the two concepts. In India, courts are not bound to treat the sum fixed in the contract either by way of liquidated damages, or penalty as the sum payable as damages for the non-performance. He says that, "… courts are required to allow reasonable compensation so as to cover the actual loss sustained, not exceeding the amount so named in the contract." In other words, the courts will only grant reasonable compensation (to the claimant) that does not exceed the amount fixed in the contract by the parties, be it by way of penalty or genuine predetermination of the damages for non-performance.

It is worth mentioning that the provision for liquidated damages excludes the employer's right to claim additional damages even if it can show that the damage it has actually suffered exceeds the provision for liquidated damages in the contract. Therefore, it is important that the sum fixed for liquidated damages accurately reflect the extent of loss the employer will suffer if there is a delay in the performance of the contract. Rees, a construction Lawyer, advises that, " If liquidated damages are not considered to be a genuine pre-estimate of the loss which would be suffered by the employer, they run the risk of being struck out as constituting a 'penalty' for breach of contract, which is contrary to English public policy."

In our country, whilst the penalty clause is regulated under the Civil Code Articles 1889-1894, there is no rule, directly or indirectly, regulating the doctrine of liquidated damages clauses. As it has been indicated earlier, the doctrine of Liquidated Damages Clause is generally recognized and applied in the Common Law System. Recent developments in Ethiopia, however, witness that in all major Government Construction Contracts, the liquidated damages clause is incorporated. Therefore, the doctrine is particularly relevant and

merits due attention.

It is believed that this is because, of two reasons Firstly, the applicability of the FIDIC Red Book (1987) in the major international construction contracts in Ethiopia is evident, if not, inevitable. Secondly, through the MoWUD Standard Conditions of Contract for the Construction of Civil Work Projects (May 19940, all Government Construction Contracts, include the liquidated damages clause. Thus, in practice, as the contractor is obliged to produce 10% of the contract price as a performance bond to the Procuring Entity, then, for each day of delay on the part of the contractor in completing the work, 0.1% of the contract price is meted out against the contractor as a penalty until the penalty amounts to 10% of the contract price; that being the Performance Bond. Thus, when the penalty amounts to 10% of the contract price, the employer terminates the contract in addition to the appropriation of the performance bond.

Thus, the question that may follow is:

How should we treat it?

Should we treat it in the way that it is treated in the Common Law Countries?

Should the Ethiopian Courts let the parties use them interchangeably?

In Ethiopia, it is evident that parties provide for an extremely exaggerated amount of penalty if one of the parties fails to discharge its contractual obligations. Be this as it may, should the courts nullify a liquidated damages clause that slaps an exaggerated amount of money as damages to the non-performing party, considering it as contrary to Ethiopian public policy?

As it can be easily gathered from the Civil Code Article 1889 cum 1892, penalty clauses are not consistent with the idea of applying the liquidated damages clause, in Common Law as a genuine pre-estimate of the loss that may be suffered by the creditor. Articles 1889 and 1892 provide thus:

Art. 1889. — Penalty.

The parties may fix the amount of damages which will be due, should a party fail to discharge his obligations or to discharge them completely and in due time.

Art. 1892. — Actual damage.

(l) The penalty shall be due notwithstanding that no actual damage was caused to the creditor.

(2) Damages may not be claimed above the amount of the penalty unless non-performance is due to the debtor's intention to cause damage or to his gross negligence or grave fault.

Article 1893 of the Civil Code is also worth mentioning here in light of the discussion above.

Art. 1893. — Variation of penalty.

The agreed amount of the penalty due for non-performance may not be reduced by the court unless partial performance has taken place.

It should be clear, thus, that penalty clauses are not supposed to be ‘genuine pre-estimates of a potential loss’ as it is strongly demanded of the liquidated damages clause. Thus, even if it is an extremely exaggerated amount, the courts will give deference to it regardless of whether the creditor has suffered any or none of the damage. In fact,

Article 1892 (2) provides that the creditor can claim above and more than the amount that is fixed in the liquidated damages clause when and if the creditor can show that non-performance was due to:

- the debtor's intention to cause damage or
- the debtor's gross negligence, or
- the debtor's grave fault.

This shows that the amount fixed in the penalty clause may be exceeded if the non-performance is due to the afore mentioned causes. This is also contrary to the view that is held for liquidated damages in the Common Law Countries.

Thus, the only remedy for the non-performing party to avoid the payment of the amount of money so fixed in the penalty clause is to invalidate it on the grounds of vitiation of consent, lesion, etc. Article 1894 of the Civil Code, however, establishes the 'severability or separability' doctrine of the penalty clause and the main contract. This is to say that the fact that the penalty clause is invalidated does not mean that the main contract is necessarily invalid. Thus, the debtor may seek for invalidating grounds (mistake, fraud, duress, motive (cause), lesion, etc) only for the 'penalty clause' while the main contract is maintained valid. The vice versa is not, however, true. That is, if the main contract is invalidated for any ground, the penalty clause is necessarily invalid. Note that, in contrast with the penalty clause, an arbitral clause inserted in the main contract remains valid even if the main contract is invalidated for any ground. This will enable the contracting parties to an invalidated contract to appoint an arbitrator/ arbitral tribunal that will determine; for example, the modality for the contracting parties' reinstatement to the position they had, had the contract not been concluded. This is called the doctrine of Severability or Separability of Arbitral Clauses.

It is, thus, proper to give due attention to what a ‘liquidated damages clause’ is and how it works in the Common Law countries.

Therefore, the following Journal article on the ‘Enforceability of Liquidated damages’ is attached herewith as it is easily amenable to understand the doctrine ,and it is easy to compare and contrast it with that of the ‘Penalty Clause’ of ours.

Delayed Performance In Construction Contracts – Enforceability Of Liquidated Damage Clauses

HAROLD WARD
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THE VAST majority of construction contracts provide for liquidated damages should the contractor fail to complete the project within some specified period of time. In those instances where completion is delayed, it is reasonably certain that the owner or contractee will assert some claim for damages pursuant to the liquidated damage clause or, alternatively, seek to avoid the impact of the clause and recover alleged actual damages. It then becomes important to evaluate the enforceability of the clause—if it is enforceable the parties are bound by the sums stipulated; if unenforceable, the contractee, though free to recoup his actual damage, is saddled with the frequently difficult task of proving the amount.[1]



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In the field of construction contracts, it is almost universally true that, assuming compliance with the other essentials of a valid clause, reasonable per diem damages for each day of delay will be upheld in view of the uncertainty of computing actual damage.[2]

A determination of the enforceability of the clause requires an inquiry into three basic areas:

[1]This has been said to be either the rental value of the property or the value of its use; Psaty & Fuhrman v. Housing Authority of City of Providence, 76 R.I. 87, 68 A.2d 32, 10 A.L.R.2d 789 (1949); Lindberg v. Brandt, 350 Ill.App. 317, 112 N.E.2d 746 (1953); Morgan-National Woodworking Co. v. Cline, 324 Mass. 15, 84 N.E.2d 460 (1949); where there has been complete abandonment by the contractor most courts hold the correct measure of damage to be the additional cost of completion under the terms of the contract; Henderson v. Oakes-Waterman Builders, 44 Cal.App.2d 615, 112 P.2d 662 (1941); Thorne v. White, Mun.Ct. App.D.C., 103 A.2d 579 (1954); George Thompson & Son Co. v. Holzter-Cabot Electric Co., 184 Ill.App. 475 (1914); Schmidt Bros. Constr. Co. v. Raymond Y.M.C.A., 180 Iowa 1306, 163 N.W. 458 (1917); Cassinelli v. Stacy, 238 Ky. 827, 38 S.W.2d 980 (1931); Allen v. Wills, 4 La. Ann. 97 (1849); Di Mare v. Capaldi, 336 Mass. 497, 146 N.E.2d 517 (1957); Januska v. Mullins, 329 Mich. 606, 46 N.W.2d 398 (1951); Noonan v. Independence Indemn. Co., 328 Mo. 706, 41 S.W.2d 162, 76 A.L.R. 931 (1931); Von Dorn v. Mengedobt, 41 Neb. 525, 59 N.W. 800 (1894); Anderson v. Shattuck, 76 N.H. 240, 81 Atl. 781 (1911); Damato v. Leone Constr. Co., 41 N.J. Super. 366, 125 A.2d 302 (1956); Juell v. New Amsterdam Cas. Co., 223 App. Div. 612, 229 N.Y.Supp. 190 (1928); Eckes v. Luce, 70 Okla. 67, 173 Pac. 219 (1917); Mechanics' Trust Co. v. Fidelity & Cas. Co., 304 Pa. 526, 156 Atl. 146 (1931); Pelletier v. Masse, 49 R.I. 408, 143 Atl. 609 (1928); St. John v. Bratton, 25 Tenn.App. 64, 150 S.W.2d 727 (1941); Super-Cold Southwest Co. v. Green & Romans, Tex.Civ.App., 196 S.W.2d 340 (1946). Some courts, however, have announced the rule to be the difference in value of the structure between its incompleted and its completed state; Walstrom v. Oliver-Watts Constr. Co., 161 Ala. 608, 50 So. 46 (1909); Routt v. Dils, 40 Colo. 50, 90 Pac. 67 (1907).

[2]American Bank & Trust Co. v. Langston, 180 Ark. 643, 22 S.W.2d 381 (1929); Commercial Inv. Co. v. Herman, 98 N.J.Eq. 589, 131 Atl. 223 (1925); Star Sand Co. v. City of Portland, 96 Ore. 323, 189 Pac. 217 (1920); Wells v. City of Philadelphia, 270 Pa. 42, 112 Atl. 867 (1921); City of Bristol v. Bostwick, 146 Tenn. 205, 240 S.W. 774 (1922); Central Oil Development Co. v. Sinclair Oil & Gas Co., Civ. App., 253 S.W. 328 (1923); Wright v. A. G. McAdams Lumber Co., Civ.App., 218 S.W. 571 (1920); Parke v. Pence Springs Co., 94 W.Va. 382, 118 S.E. 508 (1923); Keachie v. Starkweather Drainage Dist., 168 Wis. 298, 170 N.W. 236 (1919); Grant Marble Co. v. Marshall & Ilsley Bank, 166 Wis. 547, 165 N.W. 14 (1917); Wise v. U.S., 249 U.S. 361, 39 S.Ct. 303, 63 L.Ed. 647 (1919); Indemnity Ins. Co. of North America v. City of Harrison, 186 Ark. 590, 54 S.W.2d 692 (1932); Weiss v. United States Fid. & Guar. Co., 300 Ill. 11, 132 N.E. 749 (1921); Edward E. Gustin & Co. v. Nebraska Bldg. & Inv. Co., 110 Neb. 241, 193 N.W. 269 (1923); Manufacturers Cas. Ins. Co. v. Sho-Me Power Corp., D.C., Mo., 157 F.Supp. 681 (1957); Wilson v. Peak, 210 La. 969, 28 So.2d 677 (1946); Lee v. Bergesen, 58 Wash.2d 462, 364 P.2d 18 (1961).

1. Was the clause valid when adopted by the parties?
   A. Was the contractee reasonably certain to incur some actual damage in the event of delayed performance?
   B. At the time of executing the contract, were actual damages difficult if not impossible to assess?
   C. Is the stipulated sum reasonable in amount, or is it more in the nature of a penalty?
2. Did the delayed performance actually cause harm to the contractee?
3. Are the circumstances of the delay such as to nullify the clause?
   A. Was the delay due at least in part to the contractee?
   B. Was the delay due to the contractor having abandoned the project?

A fairly comprehensive summary of much of the foregoing is to be found in *United States v. Kanter*, 137 F.2d 828 (8th Cir. 1943), where the court announced at page 830:

> Where, as the parties here have agreed is the fact, proof of actual damage for delay in performance of a contract is impracticable or difficult, courts look with favor upon reasonable agreements for liquidated damages made by the parties with full understanding of the situation confronting them; and such contract provisions are uniformly enforced as the parties have written them. [Cases cited] Where, however, the amount stipulated in the contract as liquidated damages for the failure of performance bears no relation to the actual damage which may reasonably be anticipated from such a failure, courts decline to enforce the terms of the stipulation. [Cases cited] Contracts falling in this latter category are regarded by the courts as contracts for unenforceable penalties. Where the contract for liquidated damages is reasonable in character, it is valid and enforceable although the party complaining of a failure of performance neglects or is unable to prove actual damages by reason of a breach of contract. [Cases cited] But it is also established that where one seeking to enforce a provision for liquidated damages is responsible for the failure of performance, or has contributed in part to it, the provision will not be enforced. Where both parties are in default, courts will not attempt to apportion the delay due to each party in the absence of a contract provision requiring such apportionment.

1. Was The Clause Valid When Adopted By The Parties?

The determination of whether the clause is a legitimate effort to assess liquidated damages or a proscribed attempt to impose a penalty is generally held to be an issue of law to be resolved by the court.[3] As said in *Yarbrough Realty Co. v. Barar*, 37 Ala. App. 342, 67 So.2d 853 (1953):

> It is virtually the unanimous rule of all jurisdictions that whether a stipulation is for liquidated damages or for a penalty is a question of law for the court. McCormick on Damages, Section 175; 15 Am. Jur., Section 242.

However, a few decisions suggest that where the intent of the parties is doubtful, a jury question is presented.[4]

An excellent discussion of the standards followed generally by the courts in evaluating the nature of the clause as one for true liquidated damages or as a prohibited penalty is found in *Pembroke v. Caudill*, 160 Fla. 948, 37 So.2d 538, 6 A.L.R.2d 1395 (1948):

> The real purpose in permitting a stipulation for damages to stand as compensation for a breach being "to render certain and definite that which appears to be uncertain and not easily susceptible of proof" [Cases cited], the fact that a stipulation denominates a sum to be paid for breach of a contract as "liquidated damages" or as a "penalty" will not in and of itself be conclusive. The courts will

[3]Trans World Airlines, Inc. v. Travelers Indemn. Co., 262 F.2d 321 (1959); Canadian Min. Co. v. Creekmore, 226 Ark. 980, 295 S.W.2d 357 (1956); Pembroke v. Caudill, 160 Fla. 948, 37 So.2d 538 (1948); Wade & Dunton v. Gordon, 144 Md. 49, 64 A.2d 422 (1949); H. J. McGrath Co. v. Wisner, 189 Md. 260, 55 A.2d 793 (1947); Sofio v. Glissman, 156 Neb. 610, 57 N.W.2d 176 (1953); Mid-Continent Life Ins. Co. v. Goforth, 193 Okla. 314, 143 P.2d 154 (1943); Suiter v. Davis, Civ.App., 286 S.W.2d 200 (1955).

[4]Smith v. Nevin, 82 Ga.App. 432, 61 S.E.2d 430 (1950); McMurray v. Faust, 224 Ia. 50, 276 N.W. 95 (1937); Geiger v. Cawley, 146 Mich. 550, 109 N.W. 1064 (1906); Psaty & Fuhrman v. Housing Authority of City of Providence, 76 R.I. 87, 68 A.2d 32, 10 A.L.R.2d 789 (1949).

always look to the nature of the contract, the terms and purposes of the whole instrument, the natural and ordinary consequences of a breach and the peculiar circumstances attending each case, to determine its real character and purpose.

* * * there appears to run throughout the * * * cases * * * the following controlling principle: Where compensation for injury resulting from a breach of contract is reasonably susceptible of measurement by some adequate and approved legal standard, a stipulation providing for the payment of an amount which may easily be excessive with reference to the terms, nature, and purpose of the contract, making it a matter held in terrorem over either party, should be construed as a penalty, even though it be specifically designated as liquidated damages. [Cases cited] Where the actual damages contemplated when the contract was made are in their nature uncertain and may so depend upon extrinsic considerations and circumstances as to be incapable of ascertainment with any reasonable degree of exactness, and the fixed sum stipulated to be paid is not disproportionate to the probable injury likely to result from a breach of the contract, effect should be given to the stipulation as one for liquidated damages, without regard to its designation or the amount of injury actually suffered as the result of the breach.

* * * the guiding principle * * * should be that of "just compensation" for injury resulting from the breach of the contract, and the controlling object should be to place the injured party in as advantageous position as he would have occupied had his contract not been broken.

There appear to be few decisions discussing which party has the burden of proof in adjudicating the nature of the clause, and those that do are in conflict. Some assert that the party seeking to rely upon the clause has the burden of establishing the impracticability of proving actual damages.[5] Other authorities hold that the burden of establishing the clause as a penalty is upon the party urging it to be so.[6]

2. Did The Delayed Performance Actually Cause Harm To The Contractee?

This presents a question as to which the courts are irreconcilably split. As a matter of pure logic, it would seem that those courts holding that absence of damage is no defense are conceptually correct, since the validity of the clause is to be determined with reference to the situation of the parties at the time it was agreed upon and must not be analyzed with the benefit of hindsight.[7]

Accordingly, under this view, if it appeared reasonable and probable at the time of contracting that delayed performance would visit some harm upon the contractee and the parties made an obvious attempt to reasonably assess damages only and not a penalty, the clause is enforceable notwithstanding the subsequent windfall nature of the result as to the contractee. And many courts have so held. Thus, in *McCarthy v. Tally*, 46 Cal.2d 577, 297 P.2d 981 (1956) the court stated:

> We hold that in order to recover on a contract provision for liquidated damages the plaintiff must plead and prove that at the time the contract was entered into damages in the event of breach would be impracticable or extremely difficult of an ascertainment; that the sum agreed upon represented a reasonable endeavor to ascertain what such damages would be; and that a breach of the contract had occurred. In other words, no actual damage is necessary in order to recover under a liquidated damage provision provided that the case is, in other respects, a proper one * * *.[8]

[5]Better Food Markets v. American Dist. Teleg. Co., 40 Cal.2d 179, 253 P.2d 10, A.L.R. 580 (1953); Rice v. Schmid, 18 Cal.2d 382, 115 P.2d 498 (1941); Dyer Bros. Golden West Iron Wks. v. Central Iron Wks., 182 Cal. 588, 189 Pac. 445 (1920).

[6]Manufacturers Cas. Ins. Co. v. Sho-Me Power Corp. (W.D.Mo., 1957) 157 F.Supp. 681; Wilt v. Waterfield, 273 S.W.2d 290 (1954); Lu-Mi-Nus Signs v. Jefferson Shoe Stores, 257 Ill. App. 150 (1930).

[7]Manufacturers Cas. Ins. Co. v. Sho-Me Power Corp., supra, note 6; Better Food Markets Inc. v. American Dist. Tel. Co., 40 Cal.2d 179, 253 P.2d 10, 42 A.L.R.2d 580 (1953).

[8]See also: Stewart-McGhee Constr. Co. v. Caddo Parish School Board, 115 So. 458 (1927); Byron Jackson v. United States, 35 F.Supp. 665 (S.D., Cal., 1940); Stephens v. Essex County Park Commission (3rd Cir. 1906) 143 Fed. 844; United States v. Bethlehem Steel Co., 205 U.S. 105, 27 S.Ct.Rep. 450, 51 L.Ed. 731 (1907); Walsh v. Methodist Episcopal

However, the foregoing view would appear to be wholly out of harmony with the sole purpose of liquidated damages as being no more than "just compensation" for the injury sustained (*Pembroke,* supra), and for that reason many jurisdictions have refused to apply the clause if the contractee cannot show some actual damage.[9] Thus, in *Northwest Fixture Co. v. Kilbourne & Clark Co.,* 128 Fed. 256 (9th Cir. 1904) the court stated at page 261:

> It is clear that no damages were recoverable by the appellant for the breach—if breach there were—of the contract. Conceding the rule to be that, in order to recover a sum as liquidated damages, it is unnecessary to prove actual damage, it is also true that no provision in a contract for the payment of a fixed sum as damages, whether stipulated for as a penalty or as liquidated damages, will be enforced in a case where the court can see that no damages have been sustained. It is the general rule that, where the sum named in the contract to be paid on a breach thereof is evidently wholly disproportionate to the damage actually sustained, or where it is shown that no actual damage has been sustained by the parties to have intended to stipulate for a mere penalty to secure performance. * * * Gay Manufacturing Co. v. Camp. 65 F. 794, * * *; Wilcus v. Kling, 87 Ill. 107.

It would seem, therefore, that to permit recovery of liquidated damages where the contractee has clearly suffered no actual damage is to violate the principle underlying awards for breach of contract; *i.e.,* to put the injured party in as good a position as he would have been had the bargain been fulfilled; *Pembroke,* supra; Restatement, Contracts, Section 329 (1932).

3. Are The Circumstances Of The Delay Such As To Nullify The Clause?

It is well-settled that where the delay is the exclusive responsibility of the contractee, the liquidated damage clause is nullified.[10] However, the courts are hope-

[9]Northwest Fixture Co. v. Kilbourne & Clark Co., 62 C.C.A. 638, 128 Fed. 256 (1904); Rispin v. Midnight Oil Co., 291 Fed. 481, 34 A.L.R. 1331 (1923); Gay Mfg. Co. v. Camp, 13 C.C.A. 137, 25 U.S.App. 134, 65 Fed. 794 (1895); Muldoon v. Lynch, 66 Cal. 536, 6 Pac. 417 (1885); Miller v. Macfarlane, 97 Conn. 299, 116 Atl. 335 (1922); Schoolnick v. Gold, 89 Conn. 110, 93 Atl. 124 (1915); Rabinowitz v. Apter, 90 Conn. 1, 96 Atl. 157 (1915); Banta v. Stamford Motor Co., 89 Conn. 51 92 Atl. 665 (1914); Smith v. Newell, 37 Fla. 147, 20 So. 249 (1896); Radloff v. Haase, 196 Ill. 365, 63 N.E. 729 (1902); Willson v. Baltimore, 83 Md. 203, 55 Am.St.Rep. 339, 34 Atl. 774 (1896); Ward v. Haren, 183 Mo.App. 569, 167 S.W. 1064 (1914); Jackson County Light, Heat & P. Co. v. Independence, 188 Mo.App. 157, 175 S.W. 86 (1915); Jersey City v. Flynn, 74 N.J.Eq. 104, 70 Atl. 497 (1908); McCann v. Albany, 11 App.Div. 378, 42 N.Y.Supp. 94 (1896); Dunn v. Morgenthau, 73 App.Div. 147, 76 N.Y.Supp. 827 (1902); Rubin v. John C. Gabler Co., 111 N.Y.Supp. 124, 127 App.Div. 275 (1908); Fehlinger v. Boos, 118 N.Y.Supp. 167 (1908); Graham v. Lebanon, 240 Pa. 337, 87 Atl. 567 (1913); Pierce v. Jung, 10 Wis. 30 (1859); United States v. Henke Constr. Co. (W.D., Mo., 1945) 67 F.Supp. 123; Kelly v. McDonald, 276 Pac. 404 (1929); Brooks v. City of Wichita, 114 Fed. 297 (1902); Wood v. Niagara Falls Paper Co., 121 Fed. 818 (1903); Fidelity & Deposit Co. of Maryland v. Jones, 75 S.W.2d 1057 (1934); Hathaway v. Lynn, 43 N.W. 956 (1889). Church, South, Tex.Civ.App. 173 S.W. 241 (1915); Elliott Mach. Co. v. United States, 43 Ct.Cl. 232 (1908); Brown Iron Co. v. Norwood, Tex.Civ.App. 69 S.W. 253 (1902); Omohundro v. Ottenheimer, 198 Ark. 137, 127 S.W.2d 642 (1939); Robbins v. Plant, 174 Ark. 639, 297 S.W. 1027, 59 A.L.R. 1128 (1927); Kelly v. McDonald, 98 Cal.App. 121, 276 Pac. 404, 406 (1929); Bowman v. Maryland Cas. Co., 88 Cal. App. 481, 263 Pac. 826 (1928); Lu-Mi-Nus Signs v. Jefferson Shoe Stores, 257 Ill.App. 150 (1930); Alexander Hamilton Institute v. Calkins, 112 N.J.Law 170, 170 Atl. 54 (1934); Norris v. McMechen, 238 N.Y.Supp. 181, 135 Misc. 361 (1930); Atwood v. Fagan, 63 Tex.Civ.App. 659, 134 S.W. 765 (1911); Jones v. Kelley, Tex.Civ.App. 91 S.W.2d 969 (1936); United States v. United States Fid. & Guar. Co., D.C. Pa., 35 F.Supp. 959 (1940); United States for Use and Benefit of Lichter v. Henke Constr. Co., 67 F. Supp. 123, aff'd C.C.A. 157 F.2d 13 (1945); United States v. Le Roy Dyal Co., C.A.N.J., 186 F.2d 460, cert. denied, 341 U.S. 926, 71 S.Ct. 797 (1950); Tate v. Le Master, 231 S.C. 429, 99 S.E.2d 39 (1957); Smith v. Lane, Civ.App. 236 S.W.2d 214 (1950).

[10]Williams v. Rosenbaum, 57 Wash. 94 (1910); Beattie Mfg. v. Heinz, 120 Mo.App. 465 (1906); Van Buren v. Digges, 11 How. 461, 13 L.Ed. 771 (1850); District of Columbia v. Camden Iron Works, 181 U.S. 453, 45 L.Ed. 948, 21 S.Ct. 680 (1901); Atlantic City v. Warren Bros. Co., (3rd Cir. 1915) 226 Fed. 372; King Iron Bridge & Mfg. Co. v. St. Louis, 43 Fed. 768, 10 L.R.A. 826 (1890); Erickson v. United States, 107 Fed. 204 (1901); Champlain Constr. Co. v. O'Brien, 117 Fed. 271 (1902); Consolidated Engineering Co. v. United States, 35 F.Supp. 980 (appeal dismissed in 1941), 123 F.2d 1015 (1940); Ittner v. United States, 43 Ct.Cl. 336 (1908); Austin Co. v. United States, 58 Ct.Cl. 98 (1923); Boyd v. Bargagliotti, 12 Cal.App. 228, 107 Pac. 150 (1909); Marsh v. Kauff, 74 Ill. 189 (1874); F. J. Lewis Mfg. Co. v. Cobe, 180 Ill.App. 466 (1913); Humphrey v. Flaherty, 98 Kan. 634, 158 Pac. 1112 (1916); Haffner & Taylor v. Perloff, 174 La. 687, 141 So. 377 (1932); Wallis v. Wenham, 204 Mass. 83, 90 N.E. 396, 17 Ann.Cas. 644 (1910); Scheible v. Klenk, 171 Mich. 1, 137 N.W. 106 (1912); Maurer v. School Dist., 186 Mich. 223, 152 N.W. 999 (1915); Eldridge v. Fuhr, 59 Mo.App. 44 (1894); Beattie Mfg. Co. v. Heinz, 120 Mo.App. 465, 97 S.W. 188 (1906); Weeks v.

lessly in conflict as to these questions: (a) What is the effect where the delay is due *in part* to the contractee? (b) What is the effect where the delay results from the contractor having completely abandoned the project?

Where the delay is in part occasioned by the contractee, the distinct majority view is that the clause is unenforceable, since the court will not undertake to apportion the loss in view of the impracticalities of the situation.[11]

One of the leading decisions expounding this view is *United States v. United Engineering & Contracting Co.,* 234 U.S. 236, 34 S.Ct. 843, 58 L.Ed. 1294 (1913), where the court announced:

> We think the better rule is that when the contractor has agreed to do a piece of work within a given time and the parties have stipulated a fixed sum as liquidated damages not wholly disproportionate to the loss for each day's delay, in order to enforce such payment the other party must not prevent the performance of the contract within the stipulated time, and that where such is the case, and thereafter the work is completed, though delayed by the fault of the contractor, the rule of the original contract cannot be insisted upon, and liquidated damages measured thereby are waived.

The minority view permits apportionment if possible.[12] However, two of the leading cases in this school seem to have made the issue turn solely on whether the evidence could feasibly present a jury question; see *Wallis v. Wenham,* 204 Mass. 83, 90 N.E. 396 (1910); *Bedford-Carthage Stone Co. v. Ramey,* 34 S.W.2d 387 (1930).

It should be noted that in this particular area, as in so many others in the field of contract law, the courts generally give effect to a provision of the contract whereby the parties clearly intended to provide for the problem that has arisen and to achieve a disposition in a manner other than through application of some general principle of contract law. Thus, irrespective of the causes of the delay, if the agreement requires that the contractor give notice of any delay or make application for extension of time, this is generally held to be a valid condition precedent that must be

[11]United States v. United Engineering & Contracting Co., 234 U.S. 236, 34 S.Ct. 843, 58 L.Ed. 1294 (1913); E. Guastavino Co. v. United States, 50 Ct. Cl. 115 (1915); Austin Co. v. United States, 58 Ct.Cl. 98 (1923); Standard Steel Car Co. v. United States, 67 Ct.Cl. 445 (1929); Greenfield Tap & Die Corp. v. United States, 68 Ct.Cl. 61 (1929); Newcomb v. United States, 68 Ct.Cl. 246 (1929); Levering & G. Co. v. United States, 73 Ct.Cl. 566 (1932); H.W. Zweig Co. v. United States, 92 Ct.Cl. 472 (1941); Champlain Constr. Co. v. O'Brien, 117 Fed. 271 (1902); Jefferson Hotel Co. v. Brumbaugh, 168 Fed. 867 (1909); Caldwell & Drake v. Schmulbach, 175 Fed. 429 (1909); Gogo v. Los Angeles Flood Control Dist., 45 Cal.App.2d 334, 114 P.2d 65 (1941); Early v. Tussing, 182 Mich. 314, 148 N.W. 678 (1914); Maurer v. School Dist., 186 Mich. 223, 152 N.W. 999 (1915); Mosler Safe Co. v. Maiden Lane Safe Deposit Co., 199 N.Y. 479, 93 N.E. 81 (1910); Dady v. New York, 10 N.Y.Supp. 819 (1890); Wills v. Webster, 37 N.Y.Supp. 354 (1896); Thilemann v. New York, 81 N.Y.Supp. 773 (1903); Holland Torpedo Boat Co. v. Nixon, 115 N.Y.Supp. 573 (1908); Argyle v. Plunkett, 162 N.Y.Supp. 242 (1916); Small v. Burke, 86 N.Y.Supp. 1066 (1904); Smith v. Tahlequah, 117 Okla. 204, 245 Pac. 994 (1926); American Engineering Co. v. United States, D.C.Pa., 24 F. Supp. 449 (1938); Wharton Green & Co. v. United States, 86 Ct.Cl. 100 (1937); Monks et al Ex'rs v. United States, 79 Ct.Cl. 302 (1934); Sun Shipbuilding & Dry Dock Co. v. United States, 76 Ct.Cl. 154 (1932); Bethlehem Steel Co. v. United States, 75 Ct. Cl. 845 (1932); Carroll v. United States, 68 Ct.Cl. 500 (1929); Camden Iron Works v. United States, 51 Ct. Cl. 9 (1915); Wyant v. United States, 46 Ct.Cl. 205 (1911); Germain Lumber Co. v. United States, D.C. Pa., 56 F.Supp. 1001 (1944); Joseph A. Holpuch Co. v. United States, 104 Ct.Cl. 254 (1945).

[12]Coal & Iron R. Co. v. Reherd, 204 F. 859 (1913); Texas & St. L.R. Co. v. Rust, 19 F. 239 (1883); American Engineering Co. v. United States, 24 F.Supp. 449 (1938); Snead & Co. Iron Works v. Merchants Loan & T. Co., 225 Ill. 442, 80 N.E. 237 (1907); Herbert v. Weil, 115 La. 424, 39 (1905); Haughery v. Thiberge, 24 La.Ann. 442 (1872); Wallis v. Wenham, 204 Mass. 83, 90 N.E. 396 (1910); Jobst v. Hayden Bros., 84 Neb. 735, 121 N.W. 957 (1909); Small v. Burke, 86 N.Y.Supp. 1066, 92 App.Div. 338 (1904); Pittsburgh Iron & S. Engineering Co. v. National Tube Works Co., 184 Pa. 251, 39 Atl. 76 (1898); Wright v. Meyer, 25 S.W. 1122 (1894); Wilkens v. Wilkerson, 41 S.W. 178 (1897); Neblett v. McGraw, 41 Tex.Civ.App. 239, 91 S.W. 309 (1905); Bedford-Carthage Stone Co. v. Ramey, 34 S.W.2d 387 (1930); Williams v. Ronsebaum, 57 Wash. 94, 106 P. 493 (1910); Wiley v. Hart, 74 Wash. 142, 132 P. 1015 (1913).

complied with before the contractor may escape the effect of the liquidated damage clause upon the ground that the contractee occasioned the delay.[13]

Illustratively, in *Trauts Realty Corp. v. Casualty Co. of America,* 166 N.Y.Supp. 807 (1917), the surety on the contractor's bond sought to defend against application of the damage clause on the basis that the contractee delayed the beginning of the work. The court, however, held this was no defense because of the failure to adhere to the contract requirement that in case of any delay the contractor was required to apply to the architect for an extension of time.

Nevertheless, a few decisions may be found which refuse to give effect to any such agreement and simply apply the majority rule. In *Smith v. Tahlequah,* 117 Okla. 204, 245 Pac. 994 (1926), the court, rejecting the need for compliance with such a provision, announced:

> * * * The provision of the contract heretofore quoted requiring notice and providing the method to be adopted to secure an extension of time and, etc., is of no avail to the defendant in his plea for liquidated damages, * * *
>
> The right to recover liquidated damages being once abrogated cannot be renewed or revised except by subsequent agreement.

And one court has gone so far as to hold that there will be no apportionment in instances of mutual delay despite the fact that the contract so provides.[14]

Finally, we come to perhaps the most perplexing of all the issues in this area: Does complete abandonment of the job by the contractor abrogate the clause for liquidated damages, or will it be enforced without regard to the fact of abandonment?

On this issue too, the courts are absolutely divided. The majority view—and the older one—is that complete abandonment by the contractor nullifies the clause and the contractee must prove actual damages.[15] The rationale of this view is perhaps best expressed in *Village of Canton v. Globe Indemnity Co.,* 195 N.Y.Supp. 445 (1922):

> The authorities quite uniformly hold, as far as I am advised, that a provision for liquidated damages in a building contract such as we are here considering should be construed and applied only to delayed, and not to abandoned, performance. * * *
>
> The contract herein provides that, on abandonment thereof by the contractor, the plaintiff may itself at its option complete the work at the expense of the contractor. This provision, by the terms of the bond, is made subject to the prior right of the surety to do the same thing. It seems anomalous that an owner should be allowed liquidated damages for delays in the completion of the contract which the owner itself completed, even though, as is probably true in this case, the plaintiff proceeded with the due diligence. * * * The provision for liqui-

[13]Chapman Decorative Co. v. Security Mut. Life Ins. Co., 149 Fed. 189 (1906); Carroll v. United States, 68 Ct.Cl. 500 (1929); Wait v. Stanton, 104 Ark. 9, 147 S.W. 446 (1912); United States v. Cunningham, 75 App.D.C. 95, 125 F.2d 28 (1941); Wm. P. Jungclaus Co. v. Ratti, 67 Ind.App. 84, 118 N.E. 966 (1918); Equitable Real Estate Co. v. National Surety Co., 133 La. 448, 63 So. 104 (1913); Ward v. Haren, 139 Mo.App. 8, 119 S.W. 446 (1909); Feeney v. Bardsley, 66 N.J.L. 239, 49 Atl. 443 (1901); Trauts Realty Corp. v. Casualty Co. of America, 166 N.Y. Supp. 807 (1917); Curry v. Olmstead, 26 R.I. 462, 59 Atl. 392 (1905); J. G. Wagner Co. v. Cawker, 112 Wis. 532, 88 N.W. 599 (1902); David v. La Crosse Hospital Ass'n, 121 Wis. 579, 99 N.W. 351 (1904).

[14]Caldwell & Drake v. Schmulbach, 175 Fed. 429 (1909).

[15]Moore v. Board of Regents, (Mo. 1908) 115 S.W. 6, 12-13; Gallagher v. Baird, 54 App.Div. 398, 66 N.Y.Supp. 759 (1900); Shields v. John Shields Constr. Co. (at Chancery N.J. 1913), 86 Atl. 958; Joint School Dist. No. 4 v. Bailey-Marsh Co. (Wis. 1923) 194 N.W. 171, 174; Moore v. School Dist. No. 2, 215 Mo. 705, 115 S.W. 6 (1909); Gillette v. Young, 45 Colo. 562, 101 Pac. 766 (1909); C.J. 794, § 135; Sinnott v. Schumacher (Dist.Ct.App., 1st Dist., Cal. 1919) 187 Pac. 105, 108; Mason v. Continental Supply Co. (Okla. 1924), 225 Pac. 381, 383; Garey v. City of Pasco, (Wash. 1962), 154 Pac. 433, 435; Bacitalupi v. Phoenix Bldgs. & Constr. Co. (Ct.App., 1st Dist.Cal. 1910) 1 So.Pac. 892, 894; City of Newhaven v. National Steam Economizer Co. (Conn. 1907) 64 Atl. 959, 962; Fidelity & Deposit Co. v. Robertson (Ala. 1903) 34 So. 933, 942-944; Mosses v. Autuomo (Fla. 1908) 47 So. 925, 926; Murphy v. United States Fid. & Guar. Co., (S.Ct., App. Div. 1905) 91 N.Y.Supp. 582 (aff'd without opinion, 184 N.Y.Supp. 73, 76 N.E. 1101); C. T. Willard Co. v. City of New York (S.Ct. 1913) 142 N.Y.Supp. 11; Clark v. Fleischmann Vehicle Co. (S.Ct., N.Y. 1921) 187 N.Y.Supp. 807; Village of Canton v. Globe Indemnity Co. (S.Ct. 1922) 195 N.Y.W. 445; Board of Education in City of New York v. Sandman (S.Ct. 1941), 234 N.Y.Supp. 665; The Lennon v. Smith (Ct.App., N.Y., 2nd Div. 1891), 27 N.E. 243.

> dated damages must be construed, not in the light of the fact that there has been no "unnecessary delay" by the plaintiff, but in light of possibilities permitted by such construction. There would be a constant temptation to an owner in such a case not to hasten the work to completion.

Frequently, the courts following this view decline to enforce the clause on the simple ground that complete abandonment was simply not contemplated by the parties when they agreed upon the damage clause. Thus in *Gallagher v. Baird,* 66 N.Y.Supp. 759 (1900), the court held at page 762:

> It is said that the liquidated damages for which the contract made provision furnished the measure of damage. But this clause relates to delay in completion of the contract. Its language so shows:
>
> > "In case the said party of the first part shall fail to fully and entirely * * * complete within the time hereinbefore limited for such completion and delivery * * * the said party of the first part shall and will pay to the said party of the second part the sum of fifty dollars for each and every day that the said party of the first part shall be in default."
>
> It is manifest that this clause contemplated a completion of the contract, with damages for delay. There was no completion or attempt to complete, but an utter abandonment, and such clause was not intended to cover such a case, nor was provision made in the contract for such a contingency.

The minority view, however, enforces the clause notwithstanding total abandonment by the contractor. One of the leading cases in this field—at least the one most frequently cited by the exponents of this school—is an opinion by the United States Court of Appeals, Ninth Circuit. (The decision was later reversed by the Supreme Court because the Court of Appeals failed to follow California law, the Supreme Court holding that the federal court was bound by past pronouncements of the state's intermediate appellate courts and that the absence of a ruling by the state supreme court was immaterial.) In *Six Companies v. Joint Highway Dis. No. 13,* 110 F.2d 620 (9th Cir. 1940) (reversed 311 U.S. 180, 61 S.Ct. 186):

> Appellants contend that the clause does not apply to the delay in completion after abandonment by the contractor. * * * Fairly construed, [the stipulation for liquidated damages] means that the period for which the damages are to be computed comprises the time between the agreed date of completion of the "work" and its actual completion, whether by the contractor or by the district. It is not for delay in completion of the contract but for delay in the completion of the work that the damages are provided. The clause does not in terms or by implication empower the contractor to put an end to the accrual of the liquidated damages by the mere process of refusing to go ahead after the time for completion has passed.

In *City of Reading v. United States Fid. & Guar. Co.,* 19 F.Supp. 350 (E.D. Pa., 1937), involving abandonment of the construction of a water supply tunnel, the court stated:

> The remaining question is whether the City is entitled to additional damages for delay. It has apparently claimed them upon the basis of the penalty of $50 per day for delay contained in Rae's Contract. We may admit that a stipulation of this kind may not be applied in respect of the full period of delayed construction, since some of the delay may well be due to acts of the owner of default of the second contractor and for these the defaulting contractor shall not be held responsible. * * * It does not follow, however, that the City is not entitled to any damages for delay. It has been held that such damages are recoverable. * * * The penalty stipulated for in the contract appears to be a reasonable liquidation by the parties of the damages suffered by the City for delay in completing the contract * * *, and we think that the City is entitled to claim damages at that rate for such delay as a direct result from Rae's abandonment of the work.

One of the more recent decisions in this area arose in South Carolina, whose supreme court reaffirmed her allegiance to the minority view in *Austin Griffith, Inc.*

v. Goldberg, 224 S.C. 372, 79 S.E.2d 447 (1953):

> The contractor contends, and the court below held, that where the owner elects to take possession of and to complete the work himself, as authorized by the contract, the clause providing for liquidated damages does not apply. There are some authorities, particularly the older cases, so holding. See 9 C.J.S. Building & Construction Contract, Sec. 136, 12 C.J.S. Building and Loan Associations, Sec. 106. This is also the view expressed in Williston on Contracts, Revised Ed., Vol. 3, Sec. 785, where it is stated that a provision of this kind "is construed as applying only to delay, not to abandoned performance." This was the position advanced by Mr. Justice Cothran in a dissenting opinion in National Loan & Exchange Bank of Greenwood v. Gustafson, supra, 157 So.C. 221, 154 S.E. 167. But a majority of the court held otherwise where the contractor abandoned the job after the day fixed in the contract for completion. * * *
>
> The contention now advanced by the contractor is not only contrary to the view taken by this court in the foregoing case, but is not supported by the weight of authority elsewhere. In Southern Pacific v. Globe Indemnity Co., 2nd Cir. 21 F.2d. 288, 291, the court said:
>
> > * * * a close examination of the cases, however, does not in our opinion establish such a rule, and we can see no justification for it, at least when the contractor abandons after the time for completion has passed. In such a case some part of the liquidated damages has accrued before the repudiation. No intelligible reason has been suggested why the owner should lose his right to them because of a subsequent repudiation.

A few other jurisdictions have joined with the minority.[16]

As might be expected, of course, there is some difficulty, under the minority view, in ascertaining the precise extent of liability. Thus, where the abandonment occurs subsequent to the date originally fixed for completion, the courts are not in accord as to whether the contractor is liable for liquidated damages only between the fixed completion date and the abandonment date, or whether liability continues until actual completion.

In *School Dist. v. DeLano,* 95 Kan. 499, 152 Pac. 668 (1915), the court held the contractor liable for stipulated damages not only for the period between the specified completion date and the abandonment date, but for a reasonable period after abandonment in which the contractee was entitled to determine how the job should be completed, and finally the contractor was also held liable for the period between the time when the completion of the work was actually begun and the completion date itself. A basically similar approach appears to have been followed in *National Loan & Exch. Bank v. Gustafson,* 157 S.C. 221, 154 S.E. 167 (1930).

However, in *Southern Pac. Co. v. Globe Indemnity Co.,* 21 F.2d 288 (2d Cir. 1927), cert. denied, 279 U.S. 860, 49 S.Ct. 418, the court held that the contractee would be required to show the time that the contractor would have taken to complete the work had he not abandoned it, and that ordinarily this time would be no longer than the shortest period in which it could be completed.

In *Joint School Dist. v. Bailey-Marsh Co.,* 181 Wis. 202, 194 N.W. 171 (1923), the court held the contractor liable for the period between the date of his abandonment and the time when the contractee assumed control of the project.

Austin-Griffith, Inc. v. Goldberg, 224 S.C. 372, 79 S.E.2d 447 (1953), follows a general rule of reasonableness, and holds that if the contractee completes within a reasonable time, the contractor is liable for the entire period between the original and actual completion date.

[16]Williston on Contract, Rev. Ed., Vol. 3, Sec. 785; National Loan & Exchange Bank of Greenwood v. Gustafson, supra, 157 S.C. 221, 154 S.E. 167 (1930); School Dist. No. 3 v. United States Fid. & Guar. Co. (Kan., 1915) 142 Pac. 668, 670-671; Comey v. United Surety Co. (N.Y., 1916) 111 N.E. 832, aff'd, 145 N.Y.Supp. 674; McCegney v. Illinois Surety Co., (S.Ct., N.Y., 1917), 167 N.Y.Supp. 843, 845; Clemente Constr. Corp. v. P. T. Contracting Co., (S.Ct., N.Y., 1939) 16 N.Y.S.2d 483; City of Reading v. United States Fid. & Guar. Co., (E.D.Penn., 1937), 19 F. Supp. 350; Southern Pac. Co. v. Globe Indemnity Co. (2d Cir., 1927) 21 F.2d 288; Bankers' Surety Co. v. Elkhorn River Drainage Dist. (C.C.A., 1914), 214 Fed. 342.

SUMMARY

The numerous factors and the several varying views affecting the enforceability of a liquidated damage clause in construction contracts make it rather difficult to predict accurately and precisely the outcome of most matters wherein the enforcement of such a clause is in dispute. Indeed, even the problem of the draftsmanship of the clause is compounded by some of the decisions. Especially is this true in instances of complete abandonment of the job by the contractor.

The best which the practitioner can hope for is to be thoroughly cognizant of all the facts of a particular dispute, to be fully conversant with the applicable decisions within his jurisdiction, and to understand the differing philosophies which have produced the conflicting judicial viewpoints.

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4.2.3 Assignment and Sub-contracting

A. Assignment

Assignment has been a concept that is widely used in all the legal systems. In Ethiopia, the basic provisions regulating the principle of assignment are the Civil Code Articles 1962-1985. Particularly regulating assignment in the construction contracts are provided under the Civil Code Articles 3201-3205, and 3293-3296. We may also find other scattered rules in various piecemeal legislative enactments. One can mention, for example, Article 44 of the Federal Government of Ethiopia Financial Administration Proclamation No.57/1996 *cum* Article 2(7) and 54 of the Council of Ministers Financial Regulations No.17/1997. These rules govern as to how the Federal Government's rights and debts can be assigned. Likewise, particular provisions governing the assignment of particular bundle of rights and debts can also be found in areas such as Article 13 of the Petroleum Operations Proclamation No. 295/1986 and Article 17 of the Mining Operations Council of Ministers Regulation No. 182/ 1994.

B. Sub-contracting

Sub-contracting is not uncommon in the construction industry. In fact, it can be said that sub-contracting is so prevalent that most, if not all, construction projects involve sub-contracting for their completion. Generally, factors such as the following militate in favor of subcontracting:[81]

- Non-wage costs of employment such as training, pension rights, redundancy payments and sick pay;
- The increasingly diverse skill base required for the growth in

[81] Murdoch, p.259.

complexity;

- The rising expectations of workers and a concomitant shift to freelancing;
- The choice every firm faces between diversifying and contracting out;
- The perceived threat posed by trade unionization of permanently employed labor;
- Off-setting the risks associated with responsibility by transferring them; and
- The need to employ specialists of proven reliability and repute;

For these reasons, the sub-contracting agreement is growing in an ever increasing pace in the construction industry.

The questions that should be posed then are:

- What does it mean to sub-contract?
- Does the main contractor have a legal basis for doing so?
- What is the legal effect of sub-contracting?

Sub-contracting has been given of recognition in the construction industry in Ethiopia under the Civil Code of Ethiopia of 1960. Art. 3201(2) provides thus:

> *A sub-contract is a contract whereby the party having contracted with the administrative authorities substitutes a third party for himself for the performance by the latter of* ***a part only*** *or of* ***an item*** *of the contract.*

According to Murdoch, however, where there is a contract between A and B, A may not simply decide to be replaced by C is one of the basic

principles a contract. If A wishes to hand over part of the total work to C, then it should be done upon a prior authorization by the contracting authorities, or party. [82] Whenever the main contractor requests for the sub-contracting, the law provides that the authorities should give its decision on the sub-contracting request within a reasonable time.[83] The contracting authorities have the discretion to approve, or refuse to approve the sub-contract.[84] The law regulates as to what happens when and if the main contractor sub-contracts without the authorization. Art. 3204 provides the sanctions thus:

> *An unauthorized … sub-contract shall not affect the administrative authorities.*
>
> *It shall constitute a contractual fault justifying the cancellation of the contract through the fault of the party having contracted with the administrative authorities.*

Similarly, the legal relationship that should be created, once the subcontracting is authorized by the contracting authorities, is provided for under Article 3206 of the Civil Code thus:

> *The approval given by the administrative authorities to the sub-contractor shall not affect the contractual bond between the administrative authorities and their contracting party*
>
> *The original party shall remain liable for the works done and supplies made by the sub-contractor as though they had been done or made by himself.*

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[82] Art.3202(1)

[83] Art.3203(1)

[84] Art. 3203(3)

The approval of the sub-contractor by the administrative authorities shall however imply the exoneration of the contractant from the penalties for delay, where such delay is attributable to the sub-contractor.

Thus, various parts of the construction work including plastering, excavating, bricklaying, joinery, paving, tiling, ironmongery, painting, stone masonry, carpentry, plumbing, etc can be alternately be the works that can be subcontracted to be carried out by those specializing on each of the activities. In some contacts, nearly all the work can be carried out under sub-contracts, the main contractor is limiting himself to managing and controlling the process.

Despite the obvious advantages and prevalence of sub-contracting, it is given that there can be no sub-contracting without the 'authorization' being given by the contracting administrative authority. What then is meant by 'authorization' or 'approval' and how is it executed?

Art.7 of Federal Standard Bidding Document for the procurement of works provides thus:[85]

The Contractor may sub-contract with the approval of the engineer, but may not assign the contract without the approval of the employer in writing. Sub-contracting shall not alter the contractor's obligations.

On the other hand, the MoWUD Standard Conditions of Contract, under Article 4 provides the following:

The contractor shall not sub-let the whole of the works. Except

[85] Issued by the PPA

where otherwise provided by the contract, the contractor shall not sub-let any part of the works without the prior written consent of the engineer, which shall not be unreasonably withheld, and such consent, if given, shall not relieve the contractor from any liability or obligation under the eontract and he shall be responsible for the acts, defaults or neglects of any sub-contractor, his agents, servants or workmen as fully as if they were the acts, defaults or neglects of the contractor, his agents, servants or workmen. Provided always that the provision of labor on a pierce-work basis shall not be deemed to be a sub-letting under this Clause.

Whilst in the former standard condition of contract, approval is not required to be written, the latter Standard Condition of Contract demands so. Both provide that the Engineer, the agent of the employer, is the person who can give the approval without the need to refer it to the Employer. Whilst the Civil Code uses the terms 'authorization' and 'approval', the MoWUD Standard Conditions of Contract refers the sub-contractors in terms of 'nominated', 'selected', and 'approved' sub-contractors. The following conditions for Nominated sub-contractors are, however, worth noting:

- that work or supply of goods, materials, and services that is/are to be carried out by the sub-contractor have been included by way of 'provisional sum' in the contract;
- the sub-contractor have been or is to be nominated or selected or approved by the employer or engineer, and
- That all the persons to whom by virtue of the provisions of the main contract, the contractor is required to sublet any work.

In so doing, however, the contractor will not be required by the employer or the engineer, or be deemed to be under any obligation to

employ any nominated sub-contractor against whom the contractor may raise reasonable objection.[86] It should be noted here that nomination does not render the employer 'in any way liable to any nominated sub-contractor[87]. This provision should, however, be read in the light of Art.3206 of the Civil Code that expressly exonerates the contractor from any liability arising out of the delay caused by the sub-contractor.

The fact that the employer nominates and, at the same time, exonerates himself from liabilities arising from the non-performance of the sub-contractors is not, however, tamper-proof of some critique. An eminent German Construction lawyer, for example, pointed out that there is an inherent conflict in the English **nomination system** between economic reality and legal principles.[88] He adds that from a legal and commercial point of view the main contractor shall have total responsibility for all his sub-contractors, but with responsibility that must go control. To the extent that the employer, through the nomination system, deprives the main contractor of the choice of firm to carry out the relationship as between himself and the nominated firm, then it is only to be expected that the main contractor will seek to protect himself from the acts or defaults of the nominated firm and to put these on to the employer.

4.2.4 Acceptance of the Works

Once the contractor has substantially performed his contractual obligations in constructing the project, the employer will be ready to

[86]The MoWUD Standard Conditions of Contract, Clause 59 (1)-(6).

[87] Ibid, clause 59 (7)

[88] Gower, p.

accept the work. Unless there is a dispute on to the completion of the work, the employer will be happier to take possession of the work already completed without any delay, as it will expectedly be put into the intended economic and/ or residential purpose. In fact, this is the time when the employer breathes a relief of sigh as his long-dreamt vision has come to fruition. He/she will be so much happy as he/she has expended hundreds of thousands or millions of Birr/dollar to see the work as it is now completed in its most lavish and beautiful manner. Whilst it is one thing to have the work completed, it is another to find it that it has been accomplished as per the strict contractual obligations and, hence, to the best satisfaction of the employer. In this regard, a lot is left to be desired.

Today it is not uncommon to witness that construction projects are poorly carried out; in fact, for the few (both contractors and consulting engineers), once Government Construction projects are awarded to them by any stroke of magic of whatsoever sort, it is the cow to be heavy-handedly milked and out of which an instant fortune can be made.

At times, it is lamentable that contractors have been only focused on maximizing on the amount of the money that they can stash into their pocket out of the project. Worse still, the contractor steals something out of it; any sub-contractor on its part steals another thing; their employees will seek for every bit of opportunity for grabbing something out of it. As a result, many might have witnessed wide cracks in newly built buildings (including cracks in the column), hair cracks are common, sanitary systems substandard, windows letting in floods when raining, the quality of building materials being so sub-standard, etc, being the order of the day.

Fortunately or unfortunately, however, our society has unreserved

respect to professionals. Eventually, lawyers, contractors, consulting engineers, medical practitioners, etc, have been as ever immune from the legal proceedings when reasonably compared to the quite-often faults or omissions that are practiced in those professions in this Country.

What legal rights are, then, the employer is entitled to and the steps he/she it should take to exercise these legal rights?

The following provisions, being self-explanatory, from the Government Construction Laws in the Civil Code, are worth reproducing here *verbatim*

*Art. 3274. — **Provisional acceptance**. — 1. Nature*

(1) A provisional acceptance is a joint ascertainment of the works made immediately after the completion of the works.

(2) A provisional acceptance shall result from the effective taking of possession, where this has been made under reservation.

Art. 3275. — 2. Effect

(1) A provisional acceptance shall not exonerate the contractor from any defect which may appear after it is made.

(2) It shall amount to a tacit acceptance of the modifications which the contractor may have made in the project.

(3) It shall mark the beginning of the period of warranty at the expiration of which the final acceptance shall he made.

Art. 3276. — 3. Risks of loss or deterioration.

(1) Destructions or damage resulting from force majeure shall be borne by the contractor so long as the works have not been provisionally accepted by the administrative authorities.

(2) The general clauses and conditions may derogate such rule.

(3) In such case, they shall fix the amount of the right to compensation of the contractor as well as the conditions regarding the form and time of his claim.

*Art. 3277. — **Period of warranty** — 1. Nature*

(1) The period of warranty is a period during which the administrative authorities have the possibility of controlling the proper performance of the works before their final acceptance.

(2) Its duration shall be fixed by the contract.

Art. 3278. — 2. Effect

(1) During the period of warranty, the contractor shall maintain the works.

(2) He shall be liable for defects and shall repair them when he receives from the administrative authorities a requisition order to this effect.

*Art. 3279. — **Final acceptance** — 1. Nature*

(1) The final acceptance is the act whereby the administrative authorities, definitively appropriate the works after having ascertained that the contractor has performed his obligations in their entirety.

(2) It shall be made jointly and a record shall be drawn up.

Art. 3280. — 2. Default of administrative authorities.

(1) In the case of default on the part of the administrative authorities the contractor may require the court to ascertain that the works are in a condition to be accepted.

(2) In such case, the final acceptance shall be deemed to have taken place on the expiration of the period of warranty, or failing

such period on the day fixed by the court.

Art. 3281. — 3. Effect

(1) The final acceptance shall release the contractor from his obligation to maintain the works.

(2) The contractor shall be entitled to the payment of the balance of the price and to the reimbursement of the amount retained as guarantee and of the security.

During 'Provisional Acceptance', therefore, the employer examines the work whether or not it conforms to the contractual agreement and if it is tainted with any defect at all. Thus, the period of examination is extended up to one year so as to enable the employer to check the work diligently and reasonably without forcing him to do it in haste or under the influence of infatuation due to the lures and snares of the new building. It, thus, behooves upon the employer to see that any visible defect under a reasonable examination is communicated to the contractor without delay within the year period. Defects can be classified as "Latent" and "Patent" defects. Whilst the employer is duty-bound to examine and communicate "Patent" defects to the contractor within a year, "Latent" defects can still be remedied by the contractor any time they appear, if reported without delay, within 10 years. This is called the 'Decennial "Liability" Period'. Article 3279 of the Civil Code provides, therefore, that at the end of the one-year period of warranty, the Governmental Department ascertains that 'the contractor has performed his obligations **in their entirety'**. Henceforth, the contractor is said to have produced the 'Given Result' agreed upon and, thus, is entitled for all payments and release of guarantees.

Thus, Articles 3282 and 3039 of the Civil Code of Ethiopia provide to

this effect for Government Construction Contracts and Private Construction Contracts respectively, as reproduced hereunder:

Art. 3282. — Warranty in respect of defects of construction

(1) Unless otherwise provided, the contractor shall be liable to the administrative authorities for the defects of construction of the works during ten years from the day on which they have entered into possession of the works.

(2) The warranty shall not he due, however, in respect of the defects which were apparent at the time of the final acceptance of the works.

(3) The warranty shall apply to such defects only as prevent the works from being used for the purpose mentioned in the contract or as render such use more onerous or less profitable.

Art. 3039, — Warranty due by contractor.

(1) The contractor shall guarantee during ten years from its delivery the proper execution and the solidity of the work done by him.

(2) He shall be liable during this period for such loss or deterioration of the work as is due to a defect in its execution or to the nature of the soil on which the work has been done.

(3) Any provision shortening the period laid down in sub-art. (1) or excluding the warranty due by the contractor shall be of no effect.

It should be noted that the contractor’s obligation is not only to carry out and complete the building, but also to do so by the agreed date. The employer is usually very concerned to take over and use the building as soon as possible and to start to derive a benefit from what

is often a very substantial investment. Finsen[89] says, "…putting the final finishing touches to a building is generally a lengthy and involved process; trivial items of work will need to be finished off, minor defects will require to be corrected and mechanical installations such air conditioning will require a process of fine-tuning and adjustment." He adds that "…the employer will usually wish to take occupation before the final 'i' is dotted and the final 't' is crossed and will be prepared to allow the final finishing off to proceed around him provided that it does not inconvenience him to much." The stage at which the works are sufficiently advanced so that it possible for the employer to take occupation and use the building while the contractor is finishing off is termed as '**practical completion**'. 'Practical completion' has been defined as:[90]

> *It is submitted that this will, in the absence of contrary indication, mean when the work reaches a stage of readiness for use or occupation by the owner, and free from any known omissions or defects that are not merely trivial.*

Thus, the practical completion has a legal significance in that:

- The contractor's liability to pay penalties for non-completion ceases,
- Responsibility for the works passes from the contractor to the employer, and,
- The employer becomes entitled to take possession of the works

4.2.5 Guarantees in Construction Contracts

[89] Finsen, p. 129.

[90] Ibid, p.130, fn.2

The first step in business is to know your business partner thoroughly. Despite that, however, for any eventualities, businessmen make it imperative to hold for some sort of security to make sure that the contractual obligations entered into are performed fully, and completely on time and on budget by the business partner. Businessmen have always wanted to remain guarded against non-performance risks. In government construction contracts, the government department (employer) is always considered solvent and, unless there is some sort of connivance,[91] trickery, or negligence in the procurement process on the part of the governmental department, it is normally considered that the contractor will sooner or later be paid or it. This is exactly why contractors cannot raise the defense of *exceptio non adimpleti contractus* in cases of government construction contracts.[92] This may minimize the possible uneasiness on the contractors' side and less temptation to demanding security from a public employer.[93] This does not, however, mean that the governmental department cannot be short of money at any particular season. In fact, many times due to clearly blatant planning failures, and due, at another time, to the existing bureaucratic red tapes in the financial systems, it is not uncommon to observe contractors severely suffering from such defaults in payment. At any rate, the contractor

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[91] The doctrine of Cause, for example, renders the Government Construction Contracts of no effect. See Art. 3170-3171 of the Civil Code.

[92] For more discussion on the doctrine, see above.

[93] Guarantees can, however, be issued in any case necessary pursuant to Art. 42 of the Federal Financial Administration Proclamation No. 57/1996. Also see how payment is made for Government contracts under Art.26 of the afore-mentioned Proclamation. Similarly, as per Art.64(4), the contractor can be to some extent guaranteed as the Head of any public body may not authorize any contract without certifying budget appropriation, failing which he/she will be criminally liable.

may have to fall back to the legal mortgage under Art.3067 of the Civil Code on Mortgages. The legal provision provides thus:

> *The contractors who built the buildings or made the improvements… and the suppliers who supplied the materials… used in the improvements or buildings … shall have priority over mortgages on such part of the proceeds of the sale of mortgaged immovable as is necessary to cover the costs of the improvements, buildings …*

In the construction industry, therefore, there are a number of security devises that are used to attain this objective. The following can be mentioned as examples: of the dieses

- Performance Bonds;
- Bid Bonds;
- Advance Payment Guarantees;
- Retention Money Bonds, and
- Maintenance or Defects Liability Bonds,

We will briefly discuss the aforementioned security devises as they are used in construction contracts.

4.2.5.1 Contract Security (Performance Bond)

Article 43 of the Federal Public Procurement Proclamation provides thus:

> *A supplier shall provide the procuring entity with a contract security to make good on any default by the supplier under the contract. The type of procurement for which contract security is*

required and the type and amount of contract security shall be determined by a directive to be issued by the Minister.

Furthermore, the Federal Council of Ministers Financial Regulations No.17/1997 defines contract security as follows:

(5) *"Contract security" means a payment bond or a performance bond given on behalf of a contractor to the Federal Government of Ethiopian to make good on any default by the contractor under the contract by:*

- *compensating the Federal Government of Ethiopia therefore, or*
- *completing the performance of the contract to the extent required by the terms and conditions of the payment bond or performance bond, or*
- *a security deposit given by the contractor to the Federal Government of Ethiopia to secure the performance of the contract to the extent required by the terms and conditions of the contract.*

Art.11.14 of the Federal Public Procurement directives provides that PE should maintain a performance bond whatever sort of procurement method it might have used except for RFQ and when the procurement relates to a lease. Art.11.14.1 further states that the successful bidder should sign the contract and produce an acceptable performance bond within 15 days of the notice of his award. The amount of the performance bond is 10% of the contract price. The performance is aimed at redressing any loss of or damage to the PE arising out of the non-performance of his/her contractual duty. It should, however, be born high in mind that if the loss of or damage to the PE is assessed to be greater than what is held under the performance bond, the PE can

claim for the remaining amount. If it is less, the PE is obliged to refund the balance to the contractor. Accordingly, therefore, in a construction contract, the contractor produces a performance bond with the stated amount. In case of delay by the contractor, for example, the employer will deduct 0.1% of the contract price for every day that the contractor is late until this deduction amounts to 10% of the contract price.[94] After that the employer has the right to terminate the contract and substitute the contractor by another to complete the work.

4.2.5.2 Bid Security

Article 36 of the Federal Public Procurement Proclamation provides thus:

> *Unless otherwise provided in this Proclamation, the procuring entity shall include in the bid documents a condition that bids must be accompanied by security in the form of a deposit or bid guarantee. The amount of such security shall be sufficient to discourage irresponsible bids and shall remain within limits stated in the procurement directives.*
>
> *Any bid security will be forfeited if a bidder withdraws his bid within the validity period thereof or, in the case of a successful bidder, if the bidder repudiates the contract or fails to furnish performance security, if so requested.*

[94] See Art.49 of the Federal General Conditions of Construction Contracts and the Special Conditions of Contract, issued by the PPA on 'Liquidated Damages'. The MoWUD Standard Conditions of Contract, however, puts the maximum limit of liquidated damages to be 20% of the contract price.

Furthermore, the Council of Ministers Financial Regulations No.17/1997 provides, under Article 2(2) the following:

> *(2) "Bid Security" means a bid bond or security deposit given by a contractor to the Federal Government of Ethiopia to guarantee entry into a contract if the contract is awarded to that contractor.*

As we can gather from the above-mentioned provisions, Bid Bond is used to guarantee the Procuring Entity from any loss of or damage from the withdrawal by a bidder of his bid. The question, then, is: "Once the bidder has offered his bid to the PE, is it possible to withdraw from the bid"? The answer seems to be very easy in the continental legal systems, including our legal system. This is because whilst in the Common Lay system, an offer can only remain irrevocable if there is a consideration given of it, in the Civil Law system, an offer remains irrevocable without any consideration being given of it once the offer has reached him. Thus, the Basic Principles of Ethiopian Contract Law provide that if a time-bound offer is made, then, the offeror is obliged until that time will have been expired unless the offeree rejected it before the time expires.[95] In other cases, where the offeror made a 'No time-bound offer', he/she will remain bound by the offer for a reasonable period of time within which the offeror believes the offeree can decide upon it; As soon as the reasonable time has expired, the offeror has to communicate the offeree that his/her acceptance is late and that he/she will not be bound by the offer any more.[96]

Art.3156 of the Civil Code also confirms the assertion for Government contracting. Thus, Art.3156 provides:

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[95] Art.1690 of the Civil Code of Ethiopia

[96] Art.1691 of the Civil Code of Ethiopia

The tenderer may not withdraw or modify his tender until the allocation has been declared.

However, he may expressly limit in his tender the period for which he binds himself.

When, then, is the bidder or tenderer released from the bid? Art.3167 provides the an answer. Art.3167 provides thus:

The designation of a provisional successful tenderer by the Office shall not conclude the contract.

It shall have as its effect the designation of the only tenderer with whom the contract may be concluded.

*It shall **release the other tenderers** from the obligations arising out of their tender.* Emphasis added.

In other words, the PE has the right to retain until the point that it reached a decision to award the contract to a certain bidder. Once the award decision is given, the PE has the right to retain only the bid bond of the provisionally successful bidder; it is assumed that the offers by the other tenderers are rejected and, therefore, the other bidders are not any more bound by their offers.[97]

[97]Under the present Government Procurement System, bid bond is not used for RFQ (*Pro Forma*), Micro Procurement,and Direct Procurement (Single Sourcing that is currently wrongly taken in many Government Departments to mean any purchase whose value amounts below Birr 5000 as provided under art.8.1.A of the Federal Public Procurement Directives that entered into force as of Hamle 1,1997 E.C, issued by MoFED.

Can the bidder, then, withdraw from the competitive bidding once he/she is in it? Yes, he/she can withdraw from the competitive bidding on the condition that he/she is willing and can afford to forfeit the amount of money indicated in the bid bond.

The amount of the bid bond should be meted out in the manner that both discourage irresponsible bidders and cover the expenses that have been incurred in the tender processes. Art. 11.13 of the Federal Public Procurement Directives has indicated the amount of the bid bond and the conditions for their use. Hence, bid bonds will be used when the PE uses Open Bidding, Restricted Bidding, RFP, and Two Stage bidding. The amount of the bid bond should be expressed in the bid document. Furthermore, the bid bond may be produced in cash or is a bond that is issued by a recognized and NBE-licensed bank. A bond issued by the bank can either be a certified cheque,[98] Letter of Credit (L/C), or Bank guaranties.

S. No	Estimate value of the procurement	Bid bond amount
1	40,001-500000	3000-5000
2	500001-1000000	5001-10000
3	1000001-5000000	10001-50000
4	5000000 and above	50001-100000

4.2.5.3 Advance Payment Guarantee Bond

Sykes clearly and briefly puts the importance of advance payments in the construction industry:[99] as follows.

[98] It is good to note that an ordinary cheque cannot be used as a bid bond; rather the Cashier's Payment Order (CPO) is frequently used.

[99] John Sykes, Construction Claims, (Sweet and Maxwell: London, 1999), p. 57 (herein after Sykes).

There is a great demand for working capital at the commencement of a contract in order to provide plant, materials, and manpower before work starts on site. Left to his own devises, the contractor would need to provide this funding from his own resources and the cost of doing so would inevitably be a part of the contractor's tender. This requirement could in fact introduce certain inequalities between tenderers, because, for some, funding would cost more than for others. Some, in deed, might even be excluded from participation by an inability to obtain the necessary funds. The provision of advance payments by the client, when this is done, can be seen, therefore, not only as an obvious benefit to the contractor, but also as a standardization of part of the tender competition. It can also mean that the client is able to seek tenders from contractors who would not otherwise be able to submit them.

The writer, however, warns about the risk of providing money to the contractor in advance to the client.[100] Thus, it is proper to seek to cover the risk by imposing on his contractor an obligation to provide some form of security. This security produced by the contractor in return for the advance payment advanced by the employer is to be released only on the repayment of the advance payments. Thus, the Civil Code provision (Article 3271) envisages the possibility of advance payments in Government Construction Contracts. The Article provides thus:

Art. 3271. — Sums advanced by administrative authorities

(1) The contractor may receive sums in advance from the administrative authorities in respect of the contract only after having named a guarantor or given other securities

[100] Ibid

guaranteeing the reimbursement of at least half the sums advanced.

(2) The sums advanced shall be reimbursed at the rate fixed by the contract, by deducting them from the sums subsequently due to the contractor by way of installments or in settlement.

Article 2(1) of the Federal Council of Ministers Financial Regulations No.17/1997 also provides the following definition of 'advance payment':

(*1) 'Advance' means a payment for which there is no exchange of value and that is to be accounted for by the recipient at some later date and does not include a progress payment made on account of, but before the completion of a contract.*

As we can read from the aforementioned provision, advance payment is a payment in advance, which must be progressively earned until the value of the work done is in balance with the payment received.[101] If we strictly apply the rule stated under Article 3271 above, repayment is not date-related. The fact that repayment is not date-related saves the contractor from the trouble that he may encounter due to the delay in the early stages of the work; he may find himself with an

[101] One of the authors of this Material recalls the heated debate between Ethiopian Contractors, on the one hand, and the FIRA, Large Taxpayers Office (LTO) officials, on the other, on whether VAT should be levied on Advance payments in the construction industry in a Joint Seminar on "Tax Issues in relation to the Construction Sector " organized by ACCA and FIRA on the 16th of September, 2006 in Sheraton Addis, AA. Incidentally, students may also be advised to discuss on the issue. See further the Value Added Tax Proclamation No. 285/2002 and The Value Added Tax Regulations No.79/2002.

obligation to start repayments of the advance payment before he has started to earn payment for his work. On the other hand, if it is related to the value of work completed, he could find that the repayment of advance payments causes "an unacceptable diminution of his monthly income"[102] as soon as he has earned it.

Be this as it may, the Federal Public Procurement Directives regulate, to some extent, the modality of advance payments.[103] It provides, for example, that the advance payment in the procurement of government contracts may not exceed 30% of the contract price; so that contractors and suppliers should submit an Advance Payment Bond by way of C.P.O from a recognized bank or an unconditional bank guarantee.[104] More importantly, Article 28(3) of the same directives stipulates that domestic construction companies may also be forced to produce either an unconditional, irrevocable and payable on demand guarantee, or a conditional Advance Payment Guarantee from a recognized insurer. In addition, the contractor cannot use any advance payment made to him for the purchase of any construction machinery. [105]

4.2.5.4 Retention Money Bonds

Article 26 of the Federal Public Procurement Directives states that the Government Department should withhold or retain 5% of each payment made as per the Consulting Engineers Certificate of Payment in any construction works. This is done as a security for the quality of the construction work. This amount is retained over and above to the

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[102] Sykes, p.58

[103] Articles 28(1) –(4) of the Federal Public Procurement Directives

[104] We think that 'Certified Cheques' can also be used for the purpose.

[105] For further reading, please refer to Articles 28(1)-(4) of the Federal Public Procurement Directives issued by MoFED on Hamle 1, 1997.

Performance bond already held by the department. 50% of the retention money will be released on the completion of the work upon the provisional acceptance (discussed above) and the remaining 50% will be retained yet for the one-year period of warranty following the provisional acceptance. The directives, however, permit that the Retention Money Bond may be released to the contractor upon the production of an unconditional guarantee whose validity remains for 12 months.

4.2.5.5 Maintenance or Defects Liability Bonds

As discussed above under the Retention Money Bond, what is retained for a year for securing the maintenance of the work or, if released, an unconditional guarantee whose validity lasts for about a year, is called Maintenance or Defects Liability Bond. This guarantee is aimed at having any defects, omissions, or inconsistencies in constructing the work mended, if the contractor, once reported to him, fails to do so.

4.3 Variations

Once a contract is concluded between the employer and the contractor, in an ideal situation, the contractor commits himself/herself to complete and deliver the works on the agreed completion date, and the employer commits to pay the agreed contract value to the contractor. Although, as compared to other contracts, it seems that a construction contract wraps up bulky documents, such as the drawings, the specifications, the bills of quantities, general conditions of contract, special conditions of contract, the letter of acceptance, etc, it may find itself yet imperfect. Thus, the need arises that the employer would like to change or alter

one or more aspects of the construction contract. In such a case, it is not uncommon to see that construction contracts, usually via the standard conditions of contract, insert a provision to that effect. This is called a 'Variations Clause'. It is, in fact true, that all standard form construction contracts contain a variation clause which empowers the employer, usually through the engineer to vary the form, quality or quantity of the work to be carried out, whether by way of addition, modification, or omission. It is necessary to have a variation provision in a construction contract as, without it, it would be open to the contractor to refuse to carry out a request by the employer to vary the work. The contractor, when faced with a request to carry out an addition work, or to omit part of the work, could claim that he contracted to do a particular job for a particular price and did not contract to do anything else.

The need to change a particular part, quality, quantity, or design of a construction contract by the employer is well understood for many reasons. Murdoch and Hughes[106] provide for three ways in which variation might occur:

- *Clients may change their minds about what they asked for before the work is complete*
- *Designers may not have finished all of the design and specification work before the contract was let and*
- *Changes in legislation and other external factors may force changes upon the project team*.

The Civil Construction Law in Ethiopia provides that variation is allowed whether or not a clause to that effect is incorporated in the contract. While establishing the right, it imposes certain restrictions on the right of exercising and implementing changes or variations to

[106] John Murdoch and Will Hughes, p.200

the work.

Arts.3031-3034 of the Civil Code provide thus:

Art.3031. - Alterations required by client- 1. Right of client

The client may demand that alterations be made in the work as originally planned where such alterations can technically be made and are not such as to impair the solidity of the work.

Art.3032.- 2. Effect

The client may require a reduction in the price as originally agreed where the alterations required by him reduce the expenses of the contractor.

The contractor may require an increase in the price and his remuneration as originally agreed, where the alterations required by the client increase his expenses, work or liability.

Where the parties do not agree, such reduction or increase shall be settled by arbitrators appointed by the parties or, failing such, by the court.

Art.3033.-3.Contractor refusing alterations

(1) The contractor may refuse the alterations required by the client where such alterations affect plans, schemes or other documents on which the parties had agreed

(2) The contractor may also refuse the alterations where they are of such a nature or importance that they constitute a work absolutely different to the agreed work.

The work shall be deemed to be absolutely different to the agreed work where it implies an alteration exceeding by twenty per cent the value at which the original work was or could have been estimated.

Art.3034. - Alterations required by contractor

Where it appears necessary for technical reasons to make alterations in the work as originally agreed, the contractor shall, except in urgent cases, give notice thereof to the client.

The contractor shall give such notice notwithstanding that the proposed alterations do not result in the client having to pay an increased price.

The following provisions also govern variations in a Government Construction Contract as provided under the Administrative Contracts Law regime in the Civil Code of Ethiopia of 1960. The provisions clearly establish the right of the employer to vary the work at any stage of the construction phases and try to regulate how its effect should be managed.

Art.3283. _ Unilateral modification of contract. _ 1. Right of administrative authorities

During the currency of the contract of public works, the administrative authorities may, notwithstanding any stipulation to the contrary, impose unilaterally upon the contractor changes in the original conditions of the contract as indicated in the specifications.

Such changes may affect only the provisions which concern the arrangement of the public works.

They may not affect the financial conditions of the contract.

Art.3284. _ 2. New works.

The administrative authorities may, against payment of an additional remuneration, require the contractor to perform works which were not mentioned in the contract.

They may not, however, require him to perform a work which by its object would be totally different to the work mentioned in the contract or which would have no relation to such work.

Nor may they require him to perform a work under conditions entirely different to those which have been mentioned in the contract.

Art.3285. _ Rights of contractor

Unless otherwise provided in the contract, the contractor may cancel the contract where the increase or reduction of the works as a whole required by the administrative authorities involves a variation of more than one-sixth of the cost mentioned in the contract.

In the case of reduction of the works as a whole, he shall be entitled to compensation equal to the loss suffered by him and profit of which he is deprived by reason of the variation of the contract.

The court may limit the amount of compensation for deprivation of profit where it appears that the variation is due to extraneous circumstances and not to the default of the authorities having made the contract.

Summary

It has been tried to describe the various doctrines and theories that apply to the construction industry. This attempt has, been very brief, time the concepts are not developed based on the Ethiopian jurisprudence either in legal literature or court decisions. Nevertheless, a simple and brief analysis of each has been ventured here.

Students should take good note of the concepts of the government construction contracts, as Ethiopia is currently witnessing the construction boom, are given due attention in this Chapter. In this regard, the concepts of the theory of *imprevision*, the theory of *fait du prince*, the doctrine of *exceptio non adimpleti contractus*, the theory of *immixion*, etc, are briefly discussed.

Furthermore, the concept of *Quantum Meruit* is explained in detail. The role and place of liquidated damages clauses (LDCs) in construction contracts, the importance and role of sub-contracting and assignment in the construction industry are described.

Key construction securities, such as advance payment guarantee bond, retention money bond, maintenance liability bond, defects liability bond, etc, are explained.Finally, it has been indicated that variation is the typical characteristic of construction contracts, wether it as a big or small project, notwithstanding that every effort has been exerted in the accurate planning of the project. Thus, the law and the practical uses and problems have been identified and the legal provisions in our Civil Code dealing with variations have been dealt with at length.

Review Questions

1. Liquidated damages clause and penalty clause are discussed in this chapter. What is the difference and similarity between the clauses if inserted in a construction contract?
2. The doctrine of unforeseen supervening event is rejected in private contracts, except in few cases, in Ethiopia. Why do you think it is important in government contracts? Is the difference justified?
3. What are the warranties in favor of the employer in a construction contract after the completion of the work?
4. Contact a contractor and/ or a consulting engineer. How often does variation take place either on the initiation of the contractor, the employer, or the consulting engineer? Who bears the cost whenever the variation is due to a Differing Site Condition (DSC) that was not taken good care of at the formation of the contract?
5. Explain the doctrine of *exceptio non adimpleti contractus*. What is its significance in the construction industry?

CHAPTER FIVE: TRADE USAGES AND STANDARD FORMS (CONDITIONS) OF CONSTRUCTION CONTRACTS

Introduction

In the construction industry, trade usages and standard forms of contracts are pervasively in use. Their use saves time and energy. The contracting parties can also avoid complications in drafting the contracts as it naturally consists of various bulky documents and multiple contracting parties.

These standard forms of contracts are drawn up by professional organizations, financial organizations, and governmental organizations. The FIDIC Standard forms of contract is an example of those forms that are made ready by professional institutions. The SBDW, as described below, is adopted by the World Bank for procurement of projects that the World Bank finances partly or wholly. The MoWUD standard form of contract is one, among the many, forms that is prepared by the Ministry of Works and Urban Development (MoWUD) in Ethiopia.

In this Chapter, the meaning and use of trade usages are explained. It is distinguished from the standard forms of contracts. The standard form of contracts is also explained in further detail. The three prominently applicable standard forms of contract in Ethiopia are presented hereunder; namely, the 1994 MoWUD standard conditions of contract, the FIDIC form of contract (The Red Book), and The World Bank Standard Bidding Documents (SBDW).

Unit Objectives:

At the end of this Chapter, students should:

- Have an in-depth knowledge of what trade usages are and how they are applied in commercial transactions in general and construction contracts in particular,
- Assess the advantages of trade usages and Standard Conditions of Contract in general and construction contracts in particular,
- Be well introduced to the Standard Conditions of Construction Contracts that are currently widely in use at both domestic and international level, and,
- Clearly understand the legal status of the Standard Conditions of Construction Contract and their hierarchical importance within and amongst the various construction contracts documents.

5.1 Trade Usages and Standard Conditions of Contract: Distinguished

A. Trade Usages

A 'Trade Usage' consists of a particular course of dealing or line of conduct generally adopted by persons engaged in a particular trade-dealing or conduct which has become so notorious that where persons contract in that trade, they are assumed in law to have intended to be bound by such dealing or conduct, except in so far as they have by the terms of their contract expressly or impliedly excluded it. To be a valid trade usage, capable of forming part of the bargain between the parties, a usage must satisfy four conditions:[107]

[107] I.N Duncan Wallace, *Hudson's Building and Engineering Contracts*, 10th ed., (Sweet and Maxwell: London, 1970), p.53.

Firstly, it must be notorious, that is to say, so well known in the trade that, persons who make contracts of a kind to be effected by such usage must be taken to have intended that such usage should form part of their contracts. Notoriety is a matter of evidence.

Secondly, the usage must be certain; that is to say, it must have the same degree of certainty as any other contractual term. The issue of certainty is an issue of law.

Thirdly, the usage must be reasonable. Reasonability is a question of law. A usage cannot be reasonable unless it is fair and proper honest and right-minded men would adopt. A usage, which is of general convenience to all parties engaged in the trade, will not usually be regarded as unreasonable.

Fourthly, the usage must not be contrary to law; that is to say, a usage which sanctioned conduct, which was illegal, would be void.

If a usage satisfies the above conditions, then the express terms of a contract in the trade to which the usage applies are to be regarded as expressing what is peculiar to the bargain between the parties, while the usage supplies what is usual and unexpressed. The usage is just as much a part of the bargain between the parties as the express agreement. It is, however, always possible for the parties, by the terms of their contract, to exclude the operation of a trade usage, either expressly or impliedly.

The applicability of usage or custom in any commercial transaction is evident. In the Ethiopian legal system, for example, we find a plethora of legal provisions referring the parties to the applicability of the

usage or custom in the particular business relationship. For example; Civil Code Articles 1713, 1732, 2291(2), 2292(2), 2301, 2304, 2330, 2333, 2619(1), 2622(2), 2626(1)-(2) etc are just few of the legal provisions that make references to the **usage** or **custom** that is pertinent to the particular transaction in order to fill up any potential legal gap in the transaction that the parties did not or could not reach an agreement.[108]

Some international arbitration rules also provide that the arbitrators will take into account trade usages, even if they apply a national law. It is not uncommon that trade usages are frequently fill gaps in the applicable law. Since practices in the world of international commerce may well be developing more rapidly than the law. However, arbitrators may not depart from the law chosen by the parties on the ground that they are taking into account trade usages. When parties have not chosen an applicable law, arbitrators sometimes rely exclusively on trade usages to provide legal grounds for their decision. In doing so, arbitrators will have to base their choice on those international conventions and/ or arbitration rules which provide that arbitrators may, or will, in any event, take into account trade usages.[109]

The UNCITRAL Model Law on International Commercial Arbitration (1985) states blesses the applicability of 'trade usages' in the following glaring terms:[110]

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[108] See also George Krzeczunowicz, *Formation and Effect of Contracts in Ethiopian Law*, AAU, Faculty of Law, 1980, pp.59-60, 83.

[109] International Trade Center UNCTAD/ WTO, *Arbitration and International dispute resolution: How to settle international business disputes*, p.90-91

[110] Art.28(4)

… in all cases, the arbitral tribunal shall decide in accordance with the terms of the contract and shall take into account the usages of the trade applicable to the transaction.

Similarly, the ICC Arbitration rules (1998) provides for the applicability of trade usages thus:[111]

… in all cases the Arbitral Tribunal shall take account of the provisions of the contract and the relevant trade usages.

The existence of construction trade usages have been precisely indicated by Charles Molineaux. (1997:64) He writes:[112]

If there can be said to be a lex mercatoria for international traders, we should as well recognize that there are construction law principles which, by reason of the activities of the multinational engineering firms (which draft contracts) and of the development banks (which standardize contract terms), already receive de facto recognition for international construction.

B. Standard Forms (Conditions) of Contract

Standard Forms (Conditions) of Contract are issued by certain private or public organizations so as to follow them in similar contractual relationships. They may be widely followed once they are put into use by a certain body or professional association. The widespread use of standard forms of contract merely show that a large number of

[111] Art.17(2)

[112] Charles Malineaux, *Moving Toward a Construction lex mercatoria: A Lex Constructionis*, 14 J.Int.Arb.1, March 1997, at 64

builders and building owners choose to contract in the same terms. It is noteworthy to mention the following facts on the Standard Forms of contract:

- They may not be relied upon as evidence of custom;
- They are subject to frequent revision, and
- They are open to severe criticism on grounds of policy and obscurity.

A famous writer and arbitrator on construction Law, Nael Bunni, sums up the development and use of Standard Forms of Contracts thus:

In the commercial activities of today's highly complex society, standard forms of contract have become an essential part for the day-to-day transactions of most agreements. The majority of standard forms have been developed by commercial organizations for the purpose of efficiency to build on the experience gained from the repeated use of these forms, but most of all for the optimum protection of one or both parties' interests. Standard forms of contract developed for construction activities however, have mostly been drawn up by independent professional organizations, rather than by one or other of the parties to the contract, in order to establish or to consolidate a fair and just contract. Knowledge accumulated through experience and recurrent use over a long period of time brought about revisions and modifications in construction standard forms with the aim either of achieving greater certainty in the intention of the wording or of providing a response to the needs of the parties and/ or society. The use of standard form in construction contracts where tendering is the conventional method of obtaining quotations has also ensured a common basis for the comparison and evaluation of tenders.

In Ethiopia, we can observe that a number of standard forms of construction contracts have been formulated and put in use. The prominent ones are:

- The Standard Conditions of Contract for Construction of Civil Work Projects that was authored by the Ministry of Works and Urban Development in May 1994;
- BATCoDA[113] Standard Conditions of Consulting Services for Design and Supervision of Construction Works, January 1990;
- The FIDIC (Red Book) Conditions of Contract for Works of Civil Engineering, and
- The Standard Bidding Document for the Procurement of Works, issued by the Public Procurement Agency (PPA),[114] January 2006.

Furthermore, the distinction becomes clear when one sees the applicability of the trade usages and standard condition of contracts in the dispute settlement process.

5.2 The FIDIC FORM OF CONTRACT (THE RED BOOK)

The Conditions of Contract (International) for Works of Civil Engineering Construction was prepared by the *Fèdèration Internationale des Ingènieurs Conseils* (the International Federation of Consulting Engineers, FIDIC) and the *Fèdèration Internationale du*

[113] BATCoDA is an acronym and stands for Building and Transport Construction Design Authority.

[114] The PPA is established under the MoFED by virtue of the Federal Public Procurement Proclamation No.430/1997, and it is mandated, among other things, to supervise and audit whether all Federal procurements are carried out in accordance with the Public Procurement Proclamation and the Directives.

Bàtiment et des Travaux Publics (the International Federation of Building and Public Works, now known as the International European Constructors Federation, FIEC).[115] As its cover was printed in red, it has become popularly known as the '**RED BOOK**'.[116] FIDIC is the international Federation of duly elected associations of consulting engineers representing the profession in their respective countries.[117]

Since 1913, the *Fèdèration Internationale des Ingènieurs Conseils* (FIDIC) has produced the contract forms used in the majority of all transnationally financed civil engineering projects carried out in the developing world.[118] Of the various contract forms introduced by FIDIC, the FIDIC Fourth Edition has claimed an unparalleled success throughout the world today and this success is also owed to the World Bank.[119] The International Bank for Reconstruction and Development (IBRD), known as the World Bank, the largest financing agency in the international field, produced the first edition of its standard bidding documents for the procurement of works of civil engineering construction ("SBDW").[120] The use of SBDW was made a *conditio sine qua non* for contracts financed in whole or in part by the World Bank for construction works estimated to cost more than USD 10 million and it is submitted that the SBDW is almost entirely based upon the

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115 *Ibid*, at 6.

116 *Ibid*. See also similar background discussion at Robert Knutson, FIDIC: An Analysis on International Construction Contracts (edited by Robert Knutson), (The Netherlands: Kluwer Law, IBA, 2005), p. xiii.

117 *Ibid*

118 M. Beth Lyon, The Role of the Consulting Engineer in Developing Country Construction under the FIDIC Form Contract, 26 Law & Policy Int'l Business, 1994-1995, at 273.

119 *Ibid*, at 274.

120 *Ibid*

FIDIC Red Book.[121]
Bunni (1995:467) says:

The adoption of the Red Book by the World Bank in its SBDW is a major vote of confidence and an endorsement of the FIDIC Red Book. [122]

Thus, according to Nael Bunni, " …in view of the importance of the World Bank as a financing agency for works of civil engineering construction in the developing countries, the use of the Red Book has escalated considerably."*[123]*

Space and time does not allow dealing with the FIDIC Red Book here. However, in an attempt to encourage students to read the document and analyze it and as a supplement to the Chapter on the Construction Dispute Settlement,[124] one or two brainstorming issues can be raised in relation to the provisions containing the dispute settlement mechanism. For example, since the Red Book is based on the British Model, "it allots a high degree of authority to the project consulting engineer that appears to have offended developing country governments, contractors, civil law proponents and common law lawyers".[125] We believe it is within his/ her ambit for the consulting engineer to provide services such as counseling services, pre-investment studies, design, preparation of documents and supervision,

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121 Nael Bunni, *supra* note 4,p.466. The document is officially referred to as Standard Bidding Documents for the Procurement of Works- Major Contracts (over US$ 10 Million; The World Bank, Washington D.C., January 1995.

122 *Ibid*, at 467

123 *Ibid*

124 See Guide to the Use of FIDIC Conditions of Contract for Works of Civil Engineering Construction (Fourth Edition), FIDIC (1987).

125 Lyon, *Supra* note 26, at 273.

project management, etc. As it is discussed below in the next Chapters, under the FIDIC Red Book, however, “the engineer must also resolve most of the day-to-day differences of opinion which frequently occur in multi-million or multi-billion dollar projects involving years of works by multiple sub-contractors. It is this broad spectrum of decisional powers, binding both the contractor and the employer, which makes “the FIDIC engineer uniquely strong and independent.” [126] The consulting engineer, who is the agent of the employer in the particular project, is entitled to the pre-arbitral decision-making process whose non-acceptance by the parties will lead to the initiation of arbitration. This decision-making power may even relate to disputes relating to the engineer’s own design, specifications or instructions handed down to the contractor on the employer’s behalf.

In response to the severe criticism, FIDIC came up in November 1996 with a document titled ‘Supplement to Fourth Edition 1987-Conditions of Contract for Works of Civil Engineering Construction-reprinted 1992 with further amendments’[127] with a view to providing, *inter alia*, an alternative to clause 67 of the Red Book for the ‘*settlement of disputes*’, i.e., offering an option to the quasi-arbitrator consulting engineer with a ‘Dispute Adjudication Expert or Board” that gives decisions on any dispute referred to it, which decision may further be referred to arbitration.

It should be noted here *en passant* that, its being widely used notwithstanding, the irreconcilable divergence between the FIDIC Form and the existing construction principles (especially principles of public works contracts) in the Civil Law Countries has posited it as an

[126] *Ibid*, at 276.

[127] Nael Bunni,, at 15

inevitably haunting guest rather than deserving the rolling of the red carpet.

According to Sykes, however, FIDIC principles represent a balanced and fair form of contract for a number of reasons:[128]

- It is the result of continuous development work over a number of years by experts in the field of international construction and embraces, therefore, not only purely domestic but also foreign concepts.
- It has been widely used on many types of contract in different legal jurisdictions in different parts f the world.
- Its extensive use abroad has served to identify many problems associated with differing cultural, contractual and legal attitudes.
- It is based on informed advice from practitioners in many fields associated with international construction, including lawyers, bankers and insurers as well as clients, contractors and engineers.
- Successive editions have taken account of problems, disputes and arbitration and litigation cases, which have arisen following the sue of earlier editions.
- It is regarded by the World Bank as acceptable, with few reservations, for projects funded by the World Bank.

5.3 The World Bank Standard Bidding Document (SBDW)

In connection with this, it is worthwhile to note that construction projects that are partly or wholly funded by the World Bank are treated differently.

[128] Sykes, p.73

In 1985, the World Bank produced bidding documents for the procurement of works of civil engineering construction in the form of sample documents. These sample documents were upgraded by the Bank to a standard bidding documents in January 1995, having incorporated into them the valuable international experience gained during the intervening period and having made their use mandatory in all contracts fro construction works financed in whole or in part by the World Bank and whose cost is estimated to be more than USD 10 million. In January 1995, the World Bank, the largest financing agency in the international field, produced the first edition of its standard bidding documents for the procurement of works of civil engineering construction, 'SBDW'.[129] The use of these documents was made a condition in all contracts financed in whole or in part by the World Bank for construction works estimated to cost more than USD 10 million.

The SBDW included a set of conditions of contract, which was based on the Fourth Edition of the Red Book, in the form reprinted in 1992 with amendments. For example, the World Bank's SBDW provides for the use of the three-member Dispute Review Board (DRB) for the construction contracts with the estimated value exceeding USD 50 million. For other contracts under the SBDW, the employer will be free to choose from the DRB, a one-member Dispute Review Expert (DRE), or the independent consulting engineer under clause 67 of the FIDIC Red Book.

The adoption of the Red Book by the World Bank in its SBDW is a major vote of confidence and an endorsement of the FIDIC Red Book. Furthermore, in view of the importance of the World Bank as a

[129] 'Standard Bidding Documents for the Procurement of Works-Major Contracts over USD 10 million); The World Bank, Washington D.C., January 1995

financing agency for works of civil engineering construction in the developing countries, the use of the Red Book has escalated considerably.

5.4 The 1994 MoWUD Standard Conditions of Contract

This Standard Conditions of Contract for Construction of Civil Work Projects was authored by the Ministry of Works and Urban Development (MoWUD) in May 1994. It is being widely put in use in government construction contracts both at the federal and state levels.

It is not appropriate or indeed possible to discuss its terms here.[130] However queries can be posited for brainstorming purpose. It appears to have been, with minor adjustments or even rehashes, adopted from the FIDIC Red Book (1987). This is not, however, a definitive conclusion as it needs further studies regarding its origin. Be that as it may, it is dubious whether it can be applied consistently side by side with the administrative contracts principles enshrined in the Civil Code. In fact, one is bound to face with lots of difficulties in attempting to reconcile the two: the rights and obligations of the Governmental Department under the MoWUD Standard Conditions of Construction Contracts vis-à-vis the rights and obligations of the same under the Administrative Contracts Law. It is not also clear whether private parties to a construction contracts can also apply it. Furthermore, recently, its status is even dubious as the PPA's Standard Bidding document for the Procurement of Works was issued and put in use by Federal Government Departments as of January 2006. The latter covers a number of standard contractual terms

[130] However, mention of some clauses have already been made to elucidate some concepts in this Material.

subdivided into three parts: Part 1 governing bidding procedures for the procurement of works in addition to the Federal Public Procurement Proclamation and Federal Public Procurement Directives, Part 2 dealing with the schedule of requirements, and, Part 3, dealing with the contract, consisting of the General Conditions of Contract, Special Conditions of Contract and Contract Forms. This Standard Condition, its clarity and precision notwithstanding, is not as overarching in covering the number of construction issues as the MoWUD Standard Conditions of Construction Contract is.

Summary

Trade usages have wide applicability in commercial transactions in general and construction contracts in particular. They are developed by the merchants through continuous interactions in their commercial field. Construction usages are no different.

Trade usages have been resorted to as suppletory to contractual agreements in case disputes arise in international commercial arbitrations.

However, for applicability, trade usages must be notorious, certain, reasonable, and lawful. In Ethiopia, trade usages or customs in commercial transactions have been given a heightened role both in the Civil Code and Commercial Code.

Standard forms of construction contracts have also wider applicability in the Ethiopian construction industry. It has been indicated that the 1994 MoWUD Standard form of construction contracts have been used in the administration of federal and state construction contracts. The SBDW is also used for the projects that are funded, partly or

wholly, by the World Bank in Ethiopia.

Recently, the Public Procurement Agency, a small agency under the Ministry of Finance and Economic Development, has adopted the Standard Bidding Document for the Procurement of Works. This is believed to replace the 1994 MoWUD Standard Form of Contracts for the federal public works procurement contracts.

Review Questions

1. Summarize the distinguishing features of ‘trade usages’ and ‘Standard Conditions of Contracts’ in essay of half a page.
2. Let us assume that there are some contradictions between the Standard Conditions of Contract and the Civil Code Construction Law provisions. Which one supersedes the other? Why? Is your answer cognizant of both mandatory and permissive rules?
3. Take the assignment of verifying whether the MoWUD Standard Conditions of Construction Contracts can be applied in a construction contract side by side with the PPA Standard Bidding document for the Procurement of Works? If not, what happens if there are inconsistencies between the two? As a Construction Law student, which one would you advise your client for use If your client is a governmental department? Do you change your stand if your client is construction company?

4. What is FIDIC? Apart from the Red Book, how many other FIDIC standard conditions of contract exist to-date?

Chapter Six: Construction Claims and Dispute Resolution

Introduction

A construction contract, being one that involves multiple parties, is bound to lead to disputes. When a dispute arises in a construction contractual relationship, the parties often spend a great deal of time in negotiations in an attempt to resolve the dispute, rather than resorting to courts. It is easier to say that, because of the nature of construction contracts, or better yet the construction process, conflicts and disputes are almost inevitable. This is because, in construction projects, a number of different contracting entities with different needs are expected to cooperate and coordinate their efforts. To put it in better words:

> *A building contract being essentially a contract of reciprocal promises, presents a pattern of integrated actions of both parties, so correlated and timed that delay or default of any one step by any party would put out of gear the entire machinery of construction entailing extra time and expenditure to put it back in proper gear. Sometimes the machinery may even grind to a halt and to put it back into gear again would entail tremendous time and expense. Such a situation leads to mutual recrimination and raises differences and disputes which call for a settlement process, expeditious and amicable, by an independent and impartial authority acceptable to both, well qualified to appreciate the technical points involved, preferably pre-selected by name or designation*

or to be appointed by a designated authority.[131]

The need for the dispute resolution in construction industry may be due to many reasons that can be classified as follows:

- Breach of contract;
- Non-settlement of payment as per time schedule;
- Lack of proper communication;
- Insufficient specifications, drawings, designs and plans;
- Non-provision of safety practices and job site injuries;
- Alterations in the works without proper orders and
- Improper management and non-coordination between parties.

Traditionally, construction disputes and conflicts were handled by litigation. However, the court system has proven to be neither cost effective nor timely in resolving construction issues. Quite often, a spirit of give and take prevails, and the matter is settled amicably. To solve the inevitable disputes that arise in the process of performance of obligations under construction contracts through litigation may takes years and will definitely result in the spending of huge amounts of money, not to mention the stress and the feeling of distrust that it will be putting on the contracting parties. Due this need for an effective, economic and efficient means of dispute resolution in construction contractual relationships, alternative means of dispute resolution are highly availed of. The emphasis on the need for alternative means of dispute resolution is highlighted by the fact that almost all construction contracts contain specific provisions on alternative dispute resolution. Accordingly, this unit deals with litigation as well as the different alternative means of dispute resolution.

[131] Building Contracts

Unit Objectives:

At the end of this chapter, students should be able to:

- Identify the reasons behind disputes arising out of construction contracts;
- Compare and contrast the different mechanisms of dispute resolution in construction disputes, and
- Assess the advantages and disadvantages of the different dispute resolution mechanisms as applied to construction disputes and claims

6.1 Negotiation

Direct, face-to-face negotiation between the parties, without the use of a third party, involves the exchange of offers and counteroffers and a mutual discussion of the strengths and weaknesses of each party's position. This method is usually most effective if the parties are represented by skilled and knowledgeable counsel, and if both have an incentive to reach an agreed settlement.

6.2. Conciliation/Mediation

If a dispute arises out of or relates to this contract, or the breach thereof, and if the dispute cannot be settled through negotiation, the parties agree first to try in good faith to settle the dispute by mediation rules before resorting to arbitration, litigation or some other dispute resolution procedures.

Mediation is a process whereby the parties, with the assistance of a neutral third party, negotiate a resolution to their differences.

Mediation, in many instances, has been extremely effective in resolving contract disputes, thus avoiding the time, energy and cost of arbitration or litigation. Mediation is a structured negotiation in which the mediator provides the structure. The mediator will establish ground rules and acts as a referee, facilitating communications between the parties. The Mediator assists the disputants to generate options and understanding of their respective positions and manage emotions. Although the Mediator controls the process, he or she does not impose any resolution or opinion on the merits of the case, promoting a win/win situation; leaving the disputants themselves to control the outcome. Hence the process is flexible, private and confidential with legal rights of the parties protected when there is no agreement reached.

The mediator’s role is to guide and assist the parties to fashion their own settlement, serving as a facilitator to help the parties reach the desired goal of a resolution of their conflict. Parties will settle a dispute as soon as they decide it is in their mutual best interests to do so. At the most basic level the mediator’s function is to keep the parties talking and searching for ways to resolve the dispute.

A mediation clause can pressure one party to compromise, and ultimately accept less than litigation would have awarded. Nevertheless, it may result in fewer or more benefits to one of the parties. Even when parties assert that they are going to refuse to settle, the courts recognize that, in fact, settlements and compromises are often obtained through mediation notwithstanding the parties’ predisposition. Thus, although mediation, unlike arbitration, concludes a dispute only through agreement of the parties, courts generally enforce a mandatory mediation clause.

If both parties are prepared to negotiate and compromise in good faith, mediation can be one of the least expensive and most effective dispute resolution methods. In addition to the cost benefit of mediation, there are many benefits that flow from a creative solution crafted by the parties themselves. Understandably, parties are more likely to abide by an agreement that they helped negotiate and, frequently, their business or personal relationship is left intact to allow future constructive dealings.

6.3 Adjudication

It should be underlined here that “adjudication” is meant to refer to a disparate pre-arbitral dispute settlement method in the construction industry; it is commonly used in a technical sense. In the construction industry, ‘adjudication’ can be defined as:[132]

…a process whereby an appointed neutral and impartial party is entrusted to take the initiative in ascertaining the facts and the law relating to a dispute and to reach a decision within a short period of time.

‘Adjudication’, as a first tier in dispute resolution, was introduced in the UK by the Latham Report of 1994 and incorporated in the Housing Grants, Construction and Regeneration Act of 1996.[133] This Act provided that in all construction contracts, the dispute is first submitted to adjudication as a condition precedent to the bringing of arbitration or litigation. [134] It is not clear of when and how it was introduced to the Ethiopian construction contracts; it can be safely

[132] Nael Bunni,, at 437

[133] Keren Tweeddale and Andrew Tweeddale, A Practical Approach to Arbitration Law, (London: Blackstone Press Limited, 1999), p. 85.

[134] IBID, at 84.

said, however, that it has earned itself a cherished place in the resolution of construction disputes for quite some time.

According to Article 34 of the Federal Standard Bidding Document for the Procurement of Works, the adjudicator is required to act as an impartial expert to resolve disputes between the parties as rapidly and economically as is reasonably possible. The Bidding Document further expounds the role of the adjudicator as “to include, but not limited to, requiring and examining any relevant documents and written statements, making site visits, using his own specialist knowledge and holding a hearing”. Furthermore, the adjudicator’s decision should “reflect the legal entitlements of the parties and his fair and reasonable view of how the dispute should be resolved”. The adjudicator’s decision is binding on the parties unless challenged within a specified period and then varied in an arbitration or litigation depending on the terms of the contract. If the decision is not challenged within the specified period, it then becomes final and binding.

6.4 The Consulting Engineer as a Quasi-Arbitrator

The FIDIC Standard Form of Contract highlights the importance of the consulting engineer in playing a role of a quasi-arbitrator. As we have seen in the previous sections it is the different parties who a play a pivotal role in the amicable resolution of construction disputes. Among such persons is the consulting engineer. As so eloquently put by Nael Bunni:

> *In the commercial activities of today’s highly complex society, standard forms of contract have become an essential part of the day-to-day transactions of most*

agreements. The majority of standard forms have been developed by commercial organizations for the purpose of efficiency, to build on the experience gained from the repeated use of these forms, but most of all for the optimum protection of none or both parties' interests. Standard forms of contract developed for the construction activities, however, have mostly been drawn up by independent professional organizations, rather than by one or other of the parties to the contract, in order to establish or to consolidate a fair and just contract.[135]

The consulting engineer, in addition to the normal services of counseling, pre-investment studies, preparation of documents, project management, supervision, etc that he/she provides, is also entrusted by the Red Book to "resolve most of the day-to-day differences of opinion which frequently occur the construction process. The consulting engineer, who is an agent of the employer of a particular project, is entitled to the pre-arbitral decision-making process whose non-acceptance by the parties will lead to the initiation of arbitration.

6.5 Arbitration

'Arbitration agreement' is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. An arbitration agreement may be in the form of an arbitration clause in a contract or in the form of a separate agreement. The arbitration agreement shall be in writing. An agreement is in writing if it is contained in a document signed by the

[135] Nael Bunni

parties or in an exchange of letters, telegrams or other means of telecommunication which provide a record of agreement, or in an exchange of statements of claim and defense in which the existence of an agreement is alleged by one party and not denied by another. The reference in a contract to a document containing an arbitration clause constitutes an arbitration agreement provided that the contract is in writing and the reference is such as to make that clause part of the contract.

Once the parties have agreed in writing to resolve their disputes by arbitration, it is not possible for one party to unilaterally seek the court's intervention unless it can be established that a claim cannot be met by a valid defense. Moreover, arbitration bestows upon the parties, the freedom to choose one or more arbitrators; the right to determine the powers to be conferred on the selected arbitrator(s); the freedom to choose the venue of the arbitration; the right to determine how the arbitration is to be conducted; and the ability to keep the dispute private.

The parties to an arbitration are free to choose one or more arbitrators. The chosen arbitrator should have the necessary expertise to resolve the technical disputes arising from the construction contract. Accordingly, a quantity surveyor is usually chosen for disputes relating to quantities, an engineer for engineering disputes and for disputes relating to the administration of the building contract like variations, defects and extension of time, the architect would be an ideal arbitrator. As the nature of the dispute is unknown at the time of the execution of the contract, it is practical to leave open the choice of which construction profession the arbitrator should be appointed from.

If the arbitrator is not given adequate powers, he/she cannot cure the situation by acting beyond his/her powers. If he/she does act beyond his/her powers, he/she is then said to have misconducted him/herself and the parties may seek the court's help to remove him/her as the arbitrator. On the other hand, the arbitrator will suffer the same fate of removal if he/she fails to decide on all the disputes validly brought before him/her for his/her decision. To avoid this, an arbitration clause should be wide enough to empower the arbitrator to decide on all the likely disputes that may arise from the contract and to award suitable remedies as desired by the claimants. Further, the arbitrator must be aware of the scope of his powers and conscientiously ensure that he/she does not act beyond his/her powers nor fail to exercise them when required.

The essence of arbitration is that a third party renders an opinion about how the dispute should be settled. The arbitration award can be binding or nonbinding, depending on the contract or other agreement of the parties. In binding arbitration, the parties select an arbitrator or panel of arbitrators who help design the arbitration process, conduct a hearing, evaluate the evidence and make an award. The award is then binding on the parties and may be entered and enforced as a judgment by the court. There is a very limited opportunity to appeal an arbitration award. Nonbinding arbitration is identical to binding arbitration except that the parties are not bound by the result and either party still has the option to proceed to court if either party does not accept the arbitration award.

6.6 Litigation

Litigation is the mechanism of resolving disputes by using the courts

of law. It is held only when parties in any transaction are in disagreement concerning different facts and issues. It usually involves two parties, the defendant whose interest(s) the claim is made against and the plaintiff who made the claim against the interest(s) of the defendant.

Litigation is not an ordinary task that could be conducted by any person. Even in the earlier practice of traditional litigation there was a need to acquire the essential skills of the then time litigation skill and compliance with the procedure. Moreover, during this time litigation before any courts of law further needs the knowledge and skill on both the substantive and procedural laws and a talent on the logical reasoning to get acceptance before the adjudicator. For that reason, both parties in the litigation usually represented by a lawyer who traverse the necessary skills in law school as you are. A person called advocate immediately take this position in order to give the service of advocacy representing the interest of either the plaintiff or the defendant.

Accordingly, litigation requires a lot of costs and takes a lot of time, which is why most construction disputes are sought to be resolved through other means.

Summary

The involvement of multiple parties in construction contracts makes the relationships arising out of these contracts highly prone to conflict. The different types of dispute resolution mechanisms that are applied to disputes arising out of construction contracts are the ones that are ordinarily applied in resolving any dispute. Thus, arbitration,

negotiation, mediation, conciliation, adjudication and litigation are basically used to resolve disputes arising out of construction contracts. However, in the case of construction disputes and claims, disputes are resolved through alternative dispute resolution mechanisms rather than though courts.

Review Questions

1. Why do we opt for Alternative Dispute Resolution methods in construction disputes?
2. What are the differences between arbitration and mediation; and mediation and negotiation?
3. How is adjudication different from litigation?

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