



Construction contracting in the Middle East:

regional departures from international practices

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As the familiar language of international construction contracts unites parties across the globe, it pays to ensure that local departures from global practices are not overlooked and that contractual agreements adapt international forms to national laws. This article takes a close look at some of the pitfalls observed in the booming United Arab Emirates construction industry, especially in relation to levying of liquidated damages, as an indication of regional tendencies in the Gulf Cooperation Council (GCC) states in general.

It is a common occurrence in the United Arab Emirates (UAE): contractors are lulled into a false sense of security, thinking that they have budgeted for all delay-related liquidated damages that may be imposed upon them, the contract specifies the daily amount and, in any event, there is a cap on it of usually no more than ten per cent of the contract value. The contractor would, of course, try to avoid any delays – or at least avoid responsibility for them – but as long as they have factored that ten per cent into their figures, the worst case scenario, they feel, has been forecasted and budgeted for.

Generally speaking, this perception would probably be right in the UAE: contracts do almost always include a liquidated damages clause, and the parties agree that a predetermined daily amount would be subtracted from the contractor's monthly invoices if, in the opinion of the employer, the contractor has been late (subject always to a maximum total cap of a percentage of the contract – usually ten per cent, or five per cent or less in very large contract values).

There are, however, some variations to this arrangement in the UAE, relating mainly to the desire some employers have to appropriate

that daily amount whether they have actually been affected by the delay or not. It is common to see attempts seeking to set out the parties' true intentions by using words along the lines of '...without the employer having to prove actual loss' or '...regardless of whether the employer has incurred any loss'.

In short, parties sign off the deal and in the mind of the contractor the good news would hopefully be that it will never have to pay more than ten per cent of the contract value no matter how late the project is. In the mind of the employer, the good news seems to be that, if there is any delay, it can arguably allege it is the fault of the contractor and then enjoy an automatic discount on the original contract price.

Having said all that, UAE law, like most civil law-based codified legal systems, includes provisions that could surprise the unwary contractor or employer given the right set of circumstances.

For a start, in UAE law, the concept is generally upheld that damages actually incurred by an employer cannot be lower in quantum than the liquidated damages deducted. Allowing the employer to deduct a predetermined amount in the event of delay, regardless of whether such delay has actually affected it proportionately, would arguably be tantamount to undue enrichment. As such, it would be subject to scrutiny by the contractor's lawyers who would be asked to put the employer to strict proof of not only who the culprit for the delay was but also of whether that delay actually made a financial and measurable difference to the employer.

In practice, the employer has the initial privilege of simply activating the liquidated damages clause and reducing the amount it considers payable under the contractor's invoices by the agreed daily amount. This places the contractor in a defensive position as it would have to go through the whole process of filing its claim with the engineer and – if the amount justifies it – referring the issue to arbitration.

In that scenario, the employer may find that, although it has stated that deduction would take place regardless of any loss incurred, it could be asked to prove more

than whether the delay was attributable to the contractor: it may have to discharge the burden of proving that this delay has caused it quantifiable actual loss and, if not expressly excluded, consequential loss. In most cases this would be a difficult hurdle to overcome for the employer, as any evidence adduced (pointing to loss of income, for example) would in all likelihood be circumstantial. This could mean that the financial pressure initially applied to the contractor by the employer's application of liquidated damages, might in the end prove to be a pyrrhic victory: any amounts withheld and not applied to provable loss may have to be returned to the contractor.

There are arguments expressed in the UAE and elsewhere in the Middle East that the onus of proof is not actually on the employer (that it has incurred loss) but on the contractor (that the employer has not).

Whatever the case may be, the message to be borne in mind for the employer is that a liquidated damages clause is not an irrevocable right for deductions to be made. It would ultimately need to prove that it has actually incurred a loss along the lines the parties had initially contemplated would actually be incurred. Alternatively, it may have to counter evidence adduced by the contractor that no such loss has actually been incurred. The provision of liquidated damages is not considered in the UAE as an unassailable predetermination of actual losses to be incurred and it is always open to the parties to revisit the issue and adduce evidence that would prove presence or absence of an alleged loss.

However, all is not rosy for the contractor either. The maximum exposure that it had initially factored in could, under UAE law, be exceeded if the delay is substantial and if it resulted in losses being incurred by the employer that are not only quantifiable but are also well in excess of what were originally envisaged as likely.

Prudent and locally seasoned international contractors often question in advance the validity of their anticipated contractual arrangements. Particularly those that are more worldly-wise and have experienced different treatment of a liquidated damages clause across the globe, often ask whether they can indeed rest assured that when the contract says ten per cent maximum for delay damages, this is always going to be the case.

The fact is that UAE law does allow courts to exercise their discretion on the facts of the

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claim put before them: if they deem it right, they can break the limit of delay damages. In doing so, they may apply a higher limit that may be closer to any significant damages proved to have been sustained by the employer. The greater the disparity between the employer's damages and the contractual cap agreed, the more probable it would be that courts may, if requested to do so by the employer, apply the discretion afforded to them by law.

An overview of the legal position in potentially breaking limits of liability for delay can be illustrated by the diagram opposite.

Whilst this judicial discretion (available also to arbitrators) is rarely applied in practice, the legal provision opening the door for breaking limits of liability is available in the UAE. Like any other mandatory law provisions, it will apply to all construction contracts: no matter how 'standard', they are all subject to the overriding laws of a given jurisdiction.

At least with regard to liquidated damages, which can mean different things in various countries, it may be wise for both the employer and the contractor to be clear on their intentions. They could set out in the contract a list of the specific and foreseeable instances that may lead to a tangible loss for the employer and which the liquidated damages clause is in each case meant to address.

On the backdrop of an unprecedented construction boom witnessed in the UAE, it is fair to say that the landscape of construction law and practice is in the process of being shaped by parties moulding their intentions into better thought out contracts. It is encouraging to see contractors, as well as architects, throughout the Middle East become increasingly aware of the significant risks in treating international contracts as a universal and infallible text transcending cultures, laws and practices.

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