WHITE & CASE

Managing construction risks in Asia-Pacific

There are many ways to resolve a construction dispute when it arises—but what are the best methods for mitigating risks, avoiding or resolving such disputes for projects based in Australia, India, Indonesia, Malaysia, the Philippines, Singapore and Vietnam?

Contents

Managing construction risks in Asia-Pacific

The construction sector in Asia-Pacific is set for considerable growth, although that comes with challenges. In any large-scale construction project, myriad risks exist to cause disruptions and delays, but there are best practices for mitigating these risks and resolving disputes.

The International construction industry, sensitive though it is to global economic cycles, has proven itself remarkably resilient in the face of the pandemic. In much of the developing world, including countries in the Asia-Pacific region, it also holds the key to economic recovery due to its potential for job creation. Coupled with a drive toward sustainability and digital transformation, the sector is set for considerable growth in the next few years. Some market observers suggest that the construction industry in Asia-Pacific might reach US$312.67 billion by 2024.

Governments across Asia-Pacific are looking to infrastructure to help stimulate growth as the region begins to return to some form of normalcy post-COVID-19. Encouraged by this government focus, investors are turning to view Asia-Pacific as a land of opportunity. But with rapid growth comes challenges. Construction projects around the world rely heavily on long supply chains: equipment, material and labor. A disruption to any link in that chain can result in delay and increased costs, and the way parties approach risk allocation and mitigation can have significant financial implications.

As construction projects around the world were interrupted or suspended against the backdrop of the pandemic, project owners, developers and contractors have started to look at their contractual terms more closely. Force majeure is not the only option for obtaining relief, often other—and more appropriate—avenues exist that merit exploring at an early stage. Savvy market participants will proceed with great caution and will take steps to mitigate risk, avoid disputes and ensure the best possible outcome through settlement or arbitration should disputes arise.

Australia

By Lee Carroll

TOTAL POPULATION

25.69 million[1]
2020

GDP

US$1.33 trillion[2]
2020

KEY INDUSTRIES

66% of GDP
BUSINESS SERVICES

25% of GDP[3]
INDUSTRY INCLUDING CONSTRUCTION

DEMAND FOR CONSTRUCTION

US$260 billion[4]
2021

WORKING LANGUAGE

English

Australia is a highly advanced mixed economy, with investors particularly drawn to its economic stability and resilience. As of 2021, Australia has the world's 12th-largest GDP.[5] The construction industry is a key driving force in Australia's recovery from the COVID-19 pandemic, with various major projects underway, or close to completion, across Australia. Australia is a common law jurisdiction, which finds its roots in English law. Australia is also a federation with six states and two major territories, overseen by a federal government. Both the common law and legislation at the federal and state level will be relevant to investors in the construction space.

Are there any restrictions on foreign investment?

Australia's current foreign investment review framework took effect on January 1, 2021. This framework is set out by the Foreign Acquisitions and Takeovers Act 1975 (Cth) and the Foreign Acquisitions Fees Impositions Act 2015 (Cth), and the regulations associated with those pieces of legislation.

Under this foreign investment review framework, a "foreign person" planning to make investments in Australia, which meet certain criteria, must notify the Australian Treasurer. The Treasurer may then grant or deny approval for the investment. In deciding whether to approve the proposed investment, the Treasurer is advised by the Foreign Investment Review Board (FIRB). FIRB, and the Treasurer, make these decisions on a case-by-case basis.

"Foreign person" is defined broadly to include individuals not ordinarily resident in Australia.[6] It also includes any companies in which an individual not ordinarily resident in Australia holds at least a 20 percent interest, or a

company in which two foreign persons hold an aggregate interest of at least 40 percent.

Depending on the nature of the proposed investment, a lower interest percentage threshold may apply. Some relevant examples are:[7]

- **Interests in land**: As a general rule, any acquisition of an interest in commercial land, residential land, mining tenements or national security land will require FIRB approval
- **National security business interests**: Generally, a threshold of at least 10 percent applies where a foreign person proposes to acquire a direct interest in a national security business. This includes investments relating to telecommunications, electricity, ports or water networks[8]

Where Australia has a bilateral investment treaty or free trade agreement in place with another country, foreign investors from that country may benefit from certain substantive investment protections.

Is your contract enforceable under Australian law?

Australian law follows the classic English law test for contract formation (offer/acceptance, consideration, etc). All contracts, including construction contracts, must meet these requirements to be enforceable.

Standard-form contracts are often, though not always, used for construction projects in Australia. Australian Standards is the primary non-government standards development body in Australia. Its forms are the most common type of standard form used, though other forms such as FIDIC and GC21 are also used, particularly for large projects.

A key principle of Australian contract law is the freedom to contract, whereby parties may strike whatever bargain they choose. However, the common law and statute provide for certain limitations to the freedom to contract. Rules around penalties or liquidated damage clauses, and limitations and exclusions of liability clauses, may be particularly relevant to construction contracts:

Any company in which an individual not ordinarily resident in Australia holds at least a 20% interest is included in the broad definition of a "foreign person"

a. Penalty or liquidated damages clauses

Construction contracts often include liquidated damages clauses. These clauses define the damages that a contractor must pay to the principal if they fail to complete the works within the timeline specified in the contract. Liquidated damages clauses are often included in construction contracts because they provide certainty to both parties.

To be valid, the liquidated damages must be a genuine pre-estimate of the principal's likely losses.[9] If not, a court might construe the liquidated damages to be a penalty, which will not be enforceable.[10]

When construing a liquidated damages clause, a court will look at the substance of the clause over form: Even if the contract explicitly states that the amount in the clause is not a penalty, a court might still identify it as a penalty.[11]

b. Exclusion and limitation of liability clauses

Construction contracts also commonly include exclusion or limitation of liability clauses. These clauses reduce (either partly or wholly) parties' legal responsibility for certain breaches of their contract. For example, parties often exclude consequential losses.

In general, the freedom to contract allows parties to limit their liabilities as they see fit. Australian courts will generally enforce exclusion or limitation of liability clauses using a strict interpretation of the relevant clause.[12]

However, there are certain limits to contracting parties' ability to limit their liability. At common law, parties are not permitted to agree to a blanket exclusion of liability for any breach of a party's obligations.[13] Courts will also refuse to enforce clauses that exempt a party from the consequences of fraudulent conduct.[14]

In addition, parties cannot limit or exclude their liability for breach of certain provisions of the Australian Consumer Law. For any transaction that is "in trade or commerce" (which includes construction contracts), these provisions will include at a minimum: misleading or deceptive conduct; unfair practices; and unconscionable conduct.

c. Conditional payment clauses

Conditional payment clauses (also known as "pay when paid" clauses) are generally not enforceable in Australia. Each state and territory has enacted security of payment legislation invalidating conditional payment clauses.[15] Contractors' rights under this legislation are discussed in the following section.

How does a contractor secure adequate cash flow in Australia?

Each Australian state and territory has enacted a statutory regime (known as security of payment regimes) regulating the submission and payment of regular progress claims for construction projects. The regimes are broadly similar, but there are differences.

The security of payment regimes

establish a right for contractors to progress payments, and bespoke adjudication processes when these progress payments are disputed. The security of payment regimes also provide contractors with a right to suspend work where a progress payment is due but unpaid, or where security for payment has not been provided.

When does a right to terminate arise from a breach of contract under Australian law?

Most construction contracts include termination clauses, permitting a party to terminate a contract in certain situations. These situations might include the breach of particular obligations.

However, there are a number of limits to termination clauses:

- **Notice requirements**: Termination clauses tend to have specific notice requirements before termination. Australian courts do not always enforce notice requirements strictly. But in large construction projects, where the consequences of termination are serious, courts are more likely to require strict compliance with notice requirements
- **Good faith**: Australian courts may read in an implied requirement of good faith such that a party seeking to exercise a contractual right to terminate a contract must do so reasonably.[16] A court will not do so where the clause provides for an unqualified right to terminate[17]
- **Unconscionable termination**: Where a party terminates in circumstances that make the termination unconscionable, the counterparty may be able to seek relief against termination[18]

Termination for breach may also be possible even where a contract does not expressly include a right to terminate.

For example, a party may terminate a contract where the counterparty renounces the performance of its obligations. This is known as repudiation. Repudiation can occur where a party is unable, or unwilling, to perform its obligations. Sometimes a party expressly renounces its obligations, but a party's conduct alone might also amount to repudiation.[19]

A party may also in some circumstances terminate for breach of certain obligations:

- **Breach of condition**: A party may terminate for breach of a "condition." A condition is a term that is fundamental to the parties' agreement, without which they would not have entered into the contract. The contract might specify that an obligation is a condition, or a court might determine that it is a condition by looking at the parties' intentions[20]
- **Serious breach of an intermediate term**: A party can also terminate in some circumstances for a serious breach of an intermediate term (that is, an obligation other than a condition). To permit termination, the breach must deprive the terminating party of "substantially the whole benefit which it was intended that [it] should obtain from the contract."[21]

> **The main forms of dispute resolution for construction disputes in Australia are adjudication, mediation, arbitration and litigation**

January 1, 2021

Australia's current foreign investment review framework took effect on January 1, 2021

When might the parties' obligations be amended, or performance be excused due to unforeseen circumstances?

Parties can agree to a contractual mechanism to deal with unforeseen circumstances affecting the performance of their obligations. In some circumstances, the common law will also permit parties to amend or avoid the performance of their obligations, even when the contract does not expressly permit them to do so.

Force majeure clauses, for instance, might relieve a party from liability arising from its inability to fulfill its contractual obligation in certain circumstances beyond its control. Australian courts will interpret these clauses narrowly by reference to the express words used, rather than undertaking any broader determination of the parties' intention.[22] Some examples of force majeure events commonly provided for in construction contracts include wars, pandemics, riots, floods, hurricanes and earthquakes.

Where a force majeure clause does not cover unforeseen circumstances, or where a contract does not include a force majeure clause, parties may also be able to rely on the common law doctrine of frustration to excuse the performance of their contractual obligations.[23]

To rely on frustration, a party must show that a "frustrating event," which was not caused by either party, has significantly changed the nature of the party's contractual obligations, making it unjust to enforce those obligations. Whether an event constitutes a

frustrating event will depend on the facts of the case. The event must bring about a "radical" change: The fact that the event has made performance more expensive or onerous is not enough. Only exceptional circumstances will constitute a frustrating event.

How can disputes under construction contracts be resolved?

In many construction contracts, the parties agree to specific mechanisms for the resolution of disputes. This might be in the form of one dispute resolution mechanism, or multiple mechanisms (for example, one specifically for security of payment disputes, and another for general contractual disputes).

The main forms of dispute resolution for construction disputes in Australia are adjudication, mediation, arbitration and litigation:

- **Adjudication**: As discussed above, each Australian state and territory has implemented a statutory security of payments scheme. These schemes permit parties to bring their disputes before specialized disputes boards. Adjudication is a useful way for parties to rapidly secure cash flow. However, disputes boards can only hear disputes relating to interim progress payments—they cannot adjudicate on broader contractual disputes
- **Mediation**: Mediation is frequently provided for in construction contracts in Australia. In some instances, a court may also exercise its case management functions to direct parties to make genuine attempts at negotiations or mediation before proceeding to court. Mediation entails a meeting between the disputing parties, facilitated by an impartial mediator, whose role is to facilitate negotiations. Mediations are confidential and voluntary
- **Arbitration**: Construction contracts also frequently contain arbitration clauses, whereby the parties agree to the resolution of their dispute before an arbitral tribunal. Parties often choose arbitration because it is private and generally confidential, and can be quicker than going to court. From a practical perspective, international arbitration is the only real choice available to parties resolving international disputes. The International Arbitration Act 1974 (Cth) governs international commercial arbitrations in Australia. Part II sets out Australia's implementation of the New York Convention. Part III provides that the Model Law has the force of law in Australia. Domestic arbitration is regulated at the state and territory level. Model Commercial Arbitration Acts have been adopted in each state and territory that are consistent with the Model Law. The Australian Centre for International Commercial Arbitration has adopted modern arbitration rules consistent with international best practice
- **Litigation**: Despite Australia not having specialist construction courts, the Australian courts have significant experience in resolving construction disputes. Certain jurisdictions, such as New South Wales and Victoria, also have specialist lists that deal with construction disputes

Endnotes

1 World Bank, https://data.worldbank.org/indicator/SP.POP.TOTL?locations=AU.
2 World Bank, https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=AU.
3 World Bank, http://wdi.worldbank.org/table/4.2, numbers established in 2019.
4 CAustralian Industry and Skills Committee, 'Construction' (2021) available at: https://nationalindustryinsights.aisc.net.au/industries/construction.
5 International Monetary Fund, 'IMF Datamapper: GDP, Current Prices' (2021) available at: https://www.imf.org/external/datamapper/NGDPD@WEO/OEMDC/ADVEC/WEOWORLD/APQ.
6 Foreign Acquisitions and Takeovers Act 1975 (Cth), section 4 ('foreign person').
7 For further detail, see Foreign Investment Review Board, 'Guidance Notes' (2021) available at: https://firb.gov.au/guidance-notes.
8 For further detail, see Foreign Investment Review Board, 'Guidance Note 8: National Security' (9 July 2021) available at: https://firb.gov.au/sites/firb.gov.au/files/guidance-notes/GN08_NationalSecurity.pdf.
9 O'Dea v Allstates Leasing System (WA) Pty Ltd (1983) 45 ALR 632, 636–7 (Gibbs CJ), citing *Dunlop Pneumatic Tyre Co Ltd v New Garage and Motor Co Ltd* [1915] AC 79, 86 (Lord Dunedin).
10 See *Paciocco v ANZ Banking Group Limited* [20216] HCA 28 (27 July 2016).
11 *Bridge v Campbell Discount Co Ltd* [1962] AC 600, 624 (Lord Radcliffe).
12 See, for example, *Insight Vacations Pty Ltd v Young* (2011) 243 CLR 149. See also *Chubb Insurance Company of Australia Limited v Robinson* [2016] FCAFC 17, 83, 98, 101.
13 *MacRobertson Miller Airline Services v Commissioner of State Taxation (WA)* (1975) 133 CLR 125.
14 *Petera Pty Ltd v EAJ Pty Ltd* (1985) 7 FCR 375, 377-8
15 See, for example, *Building and Construction Industry Security of Payment Act 2002* (Vic) section 13.
16 See, for example, *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234.
17 See, for example, *DR Design (NSW) Pty Ltd v Grand City International Development Pty Ltd* [2017] NSWSC 1778, [21]-[27].
18 See Australian Consumer Law, section 20; *ispONE Pty Ltd v Telstra Corporation Ltd* [2013] FCA 823, [18]-[20]. In New South Wales, a court might also find that a termination clause is unjust and declare the contract void or vary the contract pursuant to the Contracts Review Act 1980 (NSW).
19 *Universal Cargo Carriers Corp v Citati* [1957] 2 QB 401, 446, 449 (Devlin J); *Sunbird Plaza Pty Ltd v Maloney* (1988) 166 CLR 245, 263–4 (Mason J).
20 *Tramway Advertising Pty Ltd v Luna Park* (NSW) Ltd (1938) 38 SR NSW 632, 641 (Jordan CH).
21 *Hong Kong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd* [1962] 2 QB 26, 69-70 (Diplock LJ).
22 *Coastal (Bermuda) Petroleum Ltd v. VTT Vulcan Petroleum SA (The Marine Star (No 2)* [1996] 2 Lloyd's Rep 383, 385 (Saville LJ).
23 *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 69, 729 (Lord Radcliffe).

India

By Aditya Singh

TOTAL POPULATION

1.38 billion[1]
2020

GDP

2.62 trillion[2]
2020

KEY INDUSTRIES

53.9% of GDP
BUSINESS SERVICES

29.1% of GDP,
of which **manufacturing** is
16.7%
INDUSTRY

17.1% of GDP[3]
AGRICULTURE

DEMAND FOR CONSTRUCTION

~US$454.8 billion[4]
2015 – 2020

WORKING LANGUAGES

Hindi (Devanagari script) and English

The construction industry in India consists primarily of two segments: real estate and urban development.[5] The real estate segment covers areas such as residential premises, office premises, hotels and leisure parks.[6] The urban development segment consists of infrastructure for water supply, sanitation, urban transport and healthcare.[7]

By 2025, the construction market in India is expected to emerge as the third-largest globally, with output expected to grow on average by 7.1 percent each year.[8]

India is a common law country, with its laws based historically on English law.

Are there any restrictions on foreign investment?

In recent years, the construction industry in India has emerged as an attractive destination for foreign investment. For the construction sector, to support this heightened interest, the government of India has enacted an attractive foreign direct investment policy (FDI Policy) that provides a clear, predictable and secure framework. For context, all inward foreign investments into India must meet the eligibility criteria stated in the FDI Policy. Under the FDI Policy, foreign investments fall under two routes, namely, (1) automatic route (where prior government approval is not needed) and (2) approval route (where prior government approval is needed). The construction sector falls under the "automatic route."[9]

Thus, there are no restrictions on foreign investment in the construction sector.

However, in light of the COVID-19 pandemic, India has imposed certain foreign investment restrictions aimed at preventing "opportunistic takeovers or acquisitions of Indian companies" by investors situated in countries that share a land border with India.[10] These restrictions extend to sectors otherwise covered under the "automatic route" such as the construction sector. Since these restrictions are responsive to the evolving situation created by the COVID-19 pandemic, they are subject to change from time to time.

Is your contract enforceable under Indian law?

The Indian Contract Act, 1872 (Contract Act) codifies Indian contract law, which is rooted in English common law, with elements of civil law, equitable law and customary and religious laws.

The Contract Act defines a "contract" as "an agreement enforceable by law."[11] Under the Contract Act, for a contract to be enforceable by law, it must meet these requirements: offer and acceptance; free consent; capacity to contract; lawful consideration; lawful object; and the contract must not have been expressly declared as void.[12]

Consequently, under Indian law, all contracts including construction contracts must meet these criteria to be enforceable. There is no separate regime governing construction contracts in India.[13]

There is no "Indian" standard-form construction contract.[14] Instead, in the construction sector, contracting parties often prefer to use conditions such as the FIDIC form contracts for their project requirements. That said, for government contracts, often the ministry or department prescribes the underlying construction contract.

Contract Act, 1872

The Indian Contract Act codifies Indian contract law, and is rooted in English common law

Both bespoke construction contracts and forms such as FIDIC, NEC, etc., are enforceable under Indian law if they meet the requirements of the Contract Act.

a. Penalty or liquidated damages clauses

Under the Contract Act, there are two main remedies for breach of contract: damages and specific performance.

The non-breaching party can bring a claim for damages under either Section 73 (damages for breach) or Section 74 (liquidated damages) of the Contract Act.

Generally, Indian courts will enforce a liquidated damages clause if it is a genuine pre-estimate of losses resulting from a breach of contract. However, if an Indian court deems that the liquidated damages clause is actually a "penalty" clause, then it will not enforce it.

Indian courts acknowledge that different classes of contracts may exist, for which it is impossible to assess compensation for breach.[15] In such cases, Indian courts defer to any liquidated damages provision contained in the contract.

Nevertheless, where a non-breaching party is in a position to prove its actual loss, it should do so. Simply invoking the liquidated damages clause in the underlying contract will not entitle the non-breaching party to liquidated damages unless it actually proves its loss.[16]

In case of liquidated damages, Indian courts will only award reasonable compensation "not exceeding the amount so stated." This gives the courts discretion to consider what amount of damages is reasonable and whether to award the full amount stated as liquidated damages in the contract.

b. Exclusion and limitation of liability clauses

Exclusion or limitation of liability clauses are valid under Indian law. Parties to a construction contract are free, for example, to exclude liability for indirect and consequential losses.[17] A limitation of liability clause could also cap the liability of the contractor, usually agreed as a percentage of the contract price.

Most construction contracts, however, carve out from exclusion or limitation of liability clauses fraud, willful misconduct, recklessness or gross negligence. Establishing any of these exceptions generally requires the non-breaching party to discharge a high burden of proof.

Indian courts construe limitation or exclusion of liability clauses strictly and they are unlikely to go beyond the terms of the contract.[18] Usually, Indian courts will enforce a limitation of liability clause, unless doing so defeats the purpose of the contract or is against the public interest or public policy.[19] Where an exclusion of liability clause is inconsistent with the main purpose of the contract, Indian courts will not apply the clause to the extent of any inconsistency.[20]

c. Conditional payment clauses

The Contract Act recognizes the validity of pay-when-paid clauses. Such clauses provide that the payment to subcontractors may be subject to payment by the owner to the main contractor if so agreed by the parties under the subcontract. The subcontractor will have to bear the risk of the owner's non-payment.[21] That said, pay-when-paid clauses are not a common industry practice.[22]

How does a contractor secure adequate cash flow in India?
From a legal standpoint, a contractor can secure adequate cash flow in several ways under the Contract Act:

- First, a contractor may suspend performance of its obligations under a construction contract on grounds provided for in the contract. Grounds for suspension may include non-payment for work performed, non-fulfillment of conditions upon which the performance is contingent, force majeure, etc.[23]
- Second, the contractor may place liens on the property, as Indian law recognizes the contractual right to lien of a party to a contract[24]

Apart from these general contractual mechanisms, there are no statutes protecting unpaid contractors per se in case of interruption or cancellation of major projects.[25]

When does a right to terminate arise from a breach of contract under Indian law?
Under Indian law, the Contract Act entitles a party to terminate a contract under these circumstances:

- Section 39 of the Contract Act entitles a party to terminate a contract if the other party refuses to perform its promise in its entirety. However, if the party entitled to terminate the contract allows the breach and acquiesces to the contract continuing despite the breach, then this ground for termination no longer remains available
- Section 53 of the Contract Act entitles a party to terminate a contract for breach if, in case of reciprocal promises, one party prevents the other party from performing its part of the contract. In such a case, the party prevented from performing its obligations has the option of terminating the contract
- Section 55 of the Contract Act entitles a party to terminate a contract if "time is of the essence" and the other party fails to perform its obligations within the stipulated time. In such a case, the non-breaching party has the option of terminating the contract

Disputes under construction contracts can either be resolved through the dispute resolution mechanism agreed in the contract or through avenues available at law if no contractual mechanism exists

7.1%

The output of the construction market in India is expected to grow by 7.1% each year by 2025

The termination of a contract obliges parties to restore any benefits that they have received under the contract. The parties may additionally claim damages and compensation that are foreseeable and arising from the breach of contract, as provided under Sections 73, 74 and 75 of the Contract Act.

When a breach of contract arises, a party may exercise its right to terminate under the contractual provisions or under the Contract Act.

The parties may prescribe certain circumstances that allow either party to terminate the contract. Examples include completion of work beyond a certain time limit, force majeure, liquidation or bankruptcy, abandonment of work, and failure to carry out remedial work, and failure to secure relevant local licenses or permissions.

When might the parties' obligations be amended, or performance excused due to unforeseen circumstances?
The Contract Act permits the amendment of contractual obligations, or excuses performance in two scenarios: occurrence of a force majeure event; or occurrence of an event that renders performance impossible (also called frustration of contract).

Force majeure applies only if agreed. If the contract contains a force majeure clause, then amendment of obligations or exemption from performance will depend on the language and scope of the force majeure clause.

Force majeure typically occurs when:

- An event beyond the control of the contracting parties occurs
- It prevents the affected party from meeting contractual obligations and
- The event is unforeseeable and its impact cannot be mitigated

Generally, a force majeure clause will include specifically events such as floods, sabotage, earthquake, strikes, riots, epidemics, etc. They sometimes exclude circumstances from their coverage, such as fluctuations in foreign exchange rates, increases in costs of machinery, equipment, materials, spare parts, etc.[26]

In the case of construction projects, contracts usually contain detailed risk allocation provisions outlining who bears the risk of unforeseen circumstances such

as force majeure or impossibility of performance.

Section 56 of the Contract Act deals with "impossibility of performance" or frustration. Frustration occurs when it becomes physically or commercially impossible to perform the contract; performance becomes unlawful; or contractual performance becomes radically different from what the parties had contemplated when entering into the contract.

To invoke Section 56 of the Contract Act, the frustration event:

- Must occur after the contract has been signed
- Could not have been foreseen by the parties
- Cannot be in the control of any party and
- Cannot have occurred due to any fault of the parties themselves

Fulfilling all these conditions will exempt a party from performance. Section 56 does not apply when performance merely becomes inconvenient, economically infeasible, burdensome or onerous.[27] Further, if the party undertaking performance knew, or, with reasonable diligence could have known that performance was or would be impossible or unlawful and if the other party did not know this (or could not reasonably have known this), then the party that has undertaken such performance must compensate the other party for any loss sustained due to such non-performance.

How can disputes under construction contracts be resolved?

Disputes under construction contracts can either be resolved through the dispute resolution mechanism agreed in the contract or through avenues available at law if no contractual mechanism exists.

India does not have any specialized courts or tribunals that deal with construction disputes. Nonetheless, the Commercial Courts Act 2015 empowers commercial courts in India to adjudicate disputes arising out of construction contracts.

Below is a brief overview of each available mechanism:

- **Dispute boards:** In construction disputes, it is quite common for parties to refer their disagreement for adjudication to a dispute board first. However, the decision of the dispute board is generally not binding on the parties. Consequently, subject to any contractual requirements, often, dispute board decisions are referred to arbitration
- **Conciliation:** The Arbitration and Conciliation Act 1996 (as amended in 2015 and 2019) provides a framework for settling disputes through conciliation. Conciliation is a non-binding procedure in which a neutral conciliator assists the parties in reaching an amicable settlement of their dispute in an independent and impartial manner.[28] The conciliator may make proposals for settlement or formulate the terms of a possible settlement. Section 30 also empowers a sole arbitrator or arbitral tribunal to encourage parties to conciliate and clarifies that doing so is compatible with the parties' arbitration agreement. If a settlement is reached, it can be recorded in the form of an arbitral award and is enforceable in court
- **Mediation:** Mediation in India is divided into two categories: judicial mediation[29] and private mediation. The mediator facilitates the settlement process, while the parties are free to decide according to their convenience and terms. In August 2019, India signed the Singapore Mediation Convention, which aims to facilitate the enforcement of a mediated settlement agreement in foreign jurisdictions[30]
- **Litigation:** The hierarchy of courts in India is broadly divided into: local or district courts; regional High Courts; and the Supreme Court of India. Foreign investors may be reluctant to agree to this choice, due to the possibility of having to engage with an unfamiliar judicial process. They also often have concerns about the independence, impartiality and efficiency of the Indian courts
- **Arbitration:** The Arbitration and Conciliation Act 1996 (as amended in 2015 and 2019) contains the framework for arbitration in India. The act is modeled on the 1985 UNCITRAL Model Law and the UNCITRAL Arbitration Rules 1976. Arbitration is a popular choice of dispute resolution for construction contracts, particularly international contracts. The Arbitration Act covers both domestic arbitration

US$454.8 billion

Demand for construction in India in 2015 – 2020

"India's ongoing efforts to modernize its arbitration landscape have led to the establishment of new arbitration institutions

(involving all Indian parties) and international commercial arbitration (involving at least one foreign party). If the "legal seat" of the arbitration is in India, then Indian courts will have supervisory jurisdiction over matters such as the appointment of arbitrators, interim relief and set-aside proceedings. Even though India's arbitration landscape has evolved as arbitration-friendly, foreign investors may still prefer to choose institutional arbitration under the auspices of the LCIA, SIAC, ICC or the like and their specialized arbitration rules, which offer consistency, transparency and predictability.

That said, India's ongoing efforts to modernize its arbitration framework have led to a number of arbitration institutions being established in India. These include:

- The Delhi International Arbitration Center, New Delhi
- The Indian Council of Arbitration, New Delhi (which also offers specialized Dispute Board services)
- The Mumbai Center for International Arbitration, Mumbai
- The Construction Industry Arbitration Council, New Delhi (which has collaborated with the SIAC in Singapore to set up a modern arbitration center focused on construction disputes)

Endnotes

1 World Bank, https://data.worldbank.org/indicator/SP.POP.TOTL?locations=IN.
2 World Bank, https://data.worldbank.org/indicator/NY.GDP.MKTP.CD?locations=IN.
3 Press Information Bureau, Ministry of Finance, Government of India https://pib.gov.in/newsite/PrintRelease.aspx?relid=186413.
4 https://www.investindia.gov.in/sector/construction. See also https://www.giiresearch.com/report/time270376-construction-india-key-trends-opportunities.html, which reports that India's construction industry regained growth momentum in 2018, with output expanding by 8.8% in real terms, an increase from 1.9% in 2017. This was driven by positive developments in economic conditions, improvement in investor confidence and investments in transport infrastructure, energy and housing projects. In 2018-2019, the government increased its expenditure towards infrastructure development by 20.9%, going from INR4.9 (trillion) (US$ 75.9 billion) in the Financial Year 2017-2018 to INR6.0 trillion (US$89.2 billion) in Financial Year 2018-2019. The industry is expected to rise from a value of US$505.7 billion in 2018 to US$690.9 billion in 2023.
5 See https://www.investindia.gov.in/sector/construction *(Snapshot: Building a sustainable future)*.
6 See https://www.investindia.gov.in/sector/construction *(Snapshot: Building a sustainable future)*.
7 See https://www.investindia.gov.in/sector/construction *(Snapshot: Building a sustainable future)*.
8 See https://www.investindia.gov.in/sector/construction *(Snapshot: Building a sustainable future)*.
9 Among others, 100% FDI is permitted in construction (development) projects such as: (1) development of townships; (2) residential/commercial premises; (3) roads or bridges; (4) hotels, resorts; (5) educational institutions; (6) recreational facilities; and (7) city and regional level infrastructure (see India's FDI Policy for 2020, available at https://static.investindia.gov.in/2020-04/FDI%20Policy%202019%20revised_19%20April%202020.pdf).
10 According to the restrictions, any investing entity (1) that belongs to/ is incorporated in a country sharing a land border with India; or (2) that is beneficially owned by a citizen of or a person situated in a country sharing a land border with India must obtain approval (from the Government of India) prior to making its investment. These restrictions came into effect on 22 April 2020. The following transactions will require government approval: (a) direct acquisitions; (b) indirect acquisitions; and (c) transfer of existing foreign investments that resulting in beneficial ownership by a foreign investor from a country that shares a land border with India. (see Department of Economic Affairs Notification No. S.O. 1278 (E) dated April 22, 2020, available at http://egazette.nic.in/WriteReadData/2020/219107.pdf.).
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Indonesia

By Dr Matthew Secomb and Gabriella Richmond

TOTAL POPULATION

273.52 million[1]
2020

GDP

US$1.06 billion[2]
2020

KEY INDUSTRIES

41% of GDP
BUSINESS SERVICES

39% of GDP
INDUSTRY INCLUDING CONSTRUCTION

20% of GDP[3]
MANUFACTURING

DEMAND FOR CONSTRUCTION

US$32.2 billion[4]
2018

WORKING LANGUAGE

Bahasa Indonesian

Indonesia represents approximately 40 percent of the ASEAN economy and population, and investors are particularly attracted to its strong economic growth and resilience. The construction industry has largely been considered the backbone of Indonesia's economic and social development. In 2019, the construction industry registered an annual growth rate of 5.8 percent[5], and is expected to continue to grow throughout 2021 – 2024.

Are there any restrictions on foreign investment?

Foreign investment in Indonesia was first recognized in the Foreign Investment Law of 1967, which was amended and consolidated into the new Investment Law in 2007. Regulations are being continuously amended by the government of Indonesia, with the aim of easing complexity and expediting processes for businesses and foreign investors. However, there are some restrictions on foreign investment. These restrictions are contained in the Negative Investment List, which specifies industries for which foreign investment is closed, or open only up to a certain percentage of its capitalization.[6] For example, a construction services business is open for up to 67 percent foreign investment (70 percent if the foreign investor is from an ASEAN nation).[7] Before conducting business, approval must be obtained from the Indonesian government and any other relevant agency for the business sector.

Is your contract enforceable under Indonesian law?
Generally, Indonesian law recognizes and upholds the freedom to contract,[8] subject to mandatory provisions of law.[9] Indonesian law does not require the use of a particular standard form of contract. However, Law No. 2 of 2017 on Construction Service (Construction Law) requires a construction agreement to contain certain provisions including, for example:

- A clause detailing work formulation, which contains the scope of work, including a clear description of the value of work, unit prices, lump sum and time limits
- A clause for the period of work and maintenance to be covered by the contractor
- A clause detailing the method of payment, including the employer's obligation to complete payments for the construction services, along with payment guarantees
- Event of default provisions
- A clause for termination upon a party's non-compliance with its obligations
- A force majeure clause and
- A dispute resolution clause

On April 21, 2020, the Indonesian government issued an implementing regulation under the Construction Law (GR 22/2020). The regulation provides clarity on, among other things: (i) the construction resources supply chain; (ii) direct appointment provisions (i.e., no public tender/ selection process); (iii) aspects of public interest; and (iv) construction services agreements. For example, the Construction Law gives state companies the opportunity to directly appoint service providers under "certain conditions." GR No. 22/2020 sets out those conditions.

40%

Indonesia represents approximately 40% of the ASEAN economy and population

a. Penalty or liquidated damages clauses

Although the general principle of Indonesian law is that the parties are free to determine the terms of the agreement between them,[10] it also provides that the terms of that agreement should not violate principles of fairness or a sense of justice.[11] There is therefore a degree of uncertainty around the enforceability of liquidated damages clauses.

b. Exclusion and limitations of liability clauses

The principle of the freedom to contract allows contracting parties to limit liabilities, including for indirect or consequential damages. However, the enforceability of such restrictions is subject to principles of fairness (keadilan), customary practice (kebiasaan), and laws and regulations, as provided under Article 1339 of the Indonesian Civil Code.[12] Limitations of liability for damages resulting from gross negligence or willful misconduct may be considered contrary to public policy.

c. Language and currency requirements

An important requirement under Indonesian law is for the Indonesian language to be used in a memorandum, agreement or contract involving an Indonesian party.[13] This requirement applies regardless of the contract's governing law. If the agreement involves a non-Indonesian party, the contract must also be drafted in the foreign party's national language or English.[14] Generally, the Presidential Regulation No. 63 of 2019 provides that parties may agree on the governing language of the contract in case of a difference in interpretation between the Indonesian and non-Indonesian versions. However, in the case of construction work contracts involving foreign parties, the Construction Law specifically states that contracts must be in both English and Indonesian, with Indonesian as the prevailing language in the case of dispute.[15]

Contracting parties must also be mindful that Indonesian law[16] provides that the Indonesian Rupiah (IDR) must be used in all commercial transactions effected in Indonesia. Non-compliance with this law will result in one-year imprisonment, a fine of IDR 200 million, or both, unless a contracting party can satisfy one of the following exceptions:[17]

- It is a transaction related to state revenue or expenditure
- The revenue or awarding grant will come from abroad or go abroad
- International commerce transactions
- Bank deposits in a foreign currency or
- International finance transactions

d. Conditional payment clauses

Under Indonesian contract law, freedom of contract permits parties to establish pay-when-paid clauses, which are not addressed by specific Indonesian laws or regulations. Such clauses allow contractors to make payments to their subcontractors only upon payment by the employer.

How does a contractor secure adequate cash flow in Indonesia?
Indonesian law allows parties to a construction contract to freely negotiate the payment terms.

Payment methods may include progress payments and milestone payments; parties may also agree to retain certain amounts in advance, only to be payable upon completion of the works.

Project delays often affect contractors' cash flow. The Construction Law does not generally address suspension or termination of project works. However, construction contracts often give the contractor the right to suspend its work while retaining title and rights over the goods and supplies used in the works. Indonesian law permits contractors to claim that title, the right to remove goods and materials supplied from the site that will remain with the contractor until it has been paid. Article 1459 of the Indonesian Civil Code also provides that ownership of goods will not be transferred as long as there is no handover from the seller (i.e., the contractor) to the buyer (i.e., the employer) for goods or supplies that are not fixed to the land. This means that the contractor may hold back the formal handover of goods until it has been paid.

When does a right to terminate arise from a breach of contract under Indonesian law?

The Construction Law requires contracts to contain a clause specifying the conditions for termination arising from a party's non-compliance of its obligations.

Otherwise, the Construction Law is silent on the grounds on which a contract can be terminated. Typically, parties will include provisions for an employer's right to terminate for a default or bankruptcy of the contractor. Similarly, the contractor is often entitled to do so if the employer goes bankrupt, or it fails to pay within a specific period.

> **An important requirement under Indonesian law is the use of the Indonesian language in a memorandum, agreement or contract involving an Indonesian party**

When might the parties' obligations be amended, or performance excused, due to unforeseen circumstances?

The concept of force majeure is found in Articles 1244 and 1245 of the Indonesian Civil Code. To qualify as a force majeure event:

- The event must have been unforeseeable when the parties signed the contract, and have caused the non-performance or late performance of one parties' obligations
- The event must not be attributable to the affected party, and not within its control (the affected party must perform its obligations to the extent possible) and
- The affected party must act in good faith

The burden of proof for demonstrating a force majeure event is on the non-performing party.

Under the Construction Law, construction contracts must contain a force majeure clause. Contractors must be mindful that while the concept of force majeure is recognized in the Indonesian Civil Code, it is relatively unspecific, and a party seeking to relieve itself from performing its contractual obligation may find it difficult to prove the necessary elements. As a result, parties are advised to include a clear force majeure clause in their contract. Ideally the clause should strike a balance between being broad (to take into account appropriate circumstances) and specific (so it is clear when it can be relied on).

5.8%

Annual growth rate of the construction industry in Indonesia in 2019

How can disputes under construction contracts be resolved?

Under the Construction Law, construction contracts must contain a dispute resolution clause. Various methods of dispute resolution can be used:

- **Litigation**: Construction disputes are categorized as general civil disputes. No separate court specifically handles construction disputes. Disputes will be heard by the District Court, and may be appealed to the High Court
- **Arbitration**: This is the preferred alternative to litigation in Indonesia.[18] The Indonesian National Board of Arbitration (BANI) and Indonesian Construction Arbitration and Alternative Dispute Resolution Board (BADAPSKI) are arbitration organizations that are commonly referred to in Indonesia. For international projects or large construction contracts, arbitration also commonly occurs under the ICC or SIAC Rules.

  Arbitration is governed by Law No. 30 of 1999 Concerning Arbitration and Alternative Dispute Resolution (Arbitration Law). Article 60 of the Arbitration Law provides that an arbitration award shall be final and binding upon parties to the dispute. The Arbitration Law also provides that the existence of a valid arbitration agreement precludes

the parties from submitting the dispute to the Indonesian District Court.[19] As a party to the New York Convention, Indonesia also recognizes and enforces arbitration awards made in other contracting states. Article 66 of the Arbitration Law sets out the requirements for the enforcement of foreign awards in Indonesia, including:

- The award must be rendered by an arbitrator or arbitral tribunal in a country which, together with Indonesia, is a party to a bilateral or multilateral treaty on the recognition and enforcement of international arbitration awards (e.g., the New York Convention)
- The award may only be enforced in Indonesia if the award falls within the scope of commercial law, and is consistent with the public order
- An award may be enforced in Indonesia only after obtaining an order of Exequatur from the Chief Judge of the Central Jakarta District Court and
- If one of the disputing parties is the Republic of Indonesia, the award may only be enforced after obtaining an order of Exequatur from the Supreme Court of the Republic of Indonesia that will be delegated to the Central Jakarta District Court for execution

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Malaysia

By Dr. Matthew Secomb and Philip Tan

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TOTAL POPULATION

32.37 million[1]
2020

GDP

US$336.66 billion[2]
2020

KEY INDUSTRIES

54% of GDP
BUSINESS SERVICES

37% of GDP[3]
INDUSTRY INCLUDING CONSTRUCTION

DEMAND FOR CONSTRUCTION

US$28.22 billion[4]
2020

WORKING LANGUAGE

Bahasa Malaysia

Its strategic location in the heart of Southeast Asia, coupled with its significant natural resources, makes Malaysia an attractive business environment. Indeed, Malaysia is internationally recognized as an investment-friendly destination.

Malaysia is a common law country, with its laws based historically on English law.

Are there any restrictions on foreign investment?

Malaysia is generally open to foreign investment, though a number of sectors are subject to foreign ownership restrictions. Such sectors include: financial services; insurance and Islamic insurance; oil & gas; communications and media; and professional services. A separate set of regulations is also imposed in certain industries (e.g., distribution and wholesale trade) to require a minimum ownership by ethnic Malays or bumiputera.

Ownership restrictions impose a 70 percent limit for foreign ownership, for example, for insurance companies.

Is your contract enforceable under Malaysian law?

Contracts are broadly enforceable under Malaysian law, and there are few form requirements.

It is good practice for parties to record their bargain in writing. While an oral contract would remain legally valid and enforceable under Malaysian law, in the case of default or disagreement, an aggrieved party under an oral contract will not have access to the statutory processes afforded under the Construction Industry Payment and Adjudication Act (CIPA Act). The CIPA Act is beneficial because it provides procedural safeguards and a mechanism for speedy dispute resolution through adjudication to facilitate regular and timely payment under construction contracts.

Parties may choose to use standard-form construction contracts, such as those published by the International Federation of Consulting Engineers (FIDIC), Pertubuhan Akitek Malaysia (PAM) or the Public Works Department (PWD). The PAM standard form is the de facto standard form for domestic building contracts, while the PWD form is that for domestic infrastructure contracts. A relatively new option is the Asian International Arbitration Centre (AIAC) suite of standard forms broadly based on the PAM form. The FIDIC form is the preferred choice of international contractors. Such standard-form contracts may aid the parties in ensuring effective and efficient contract administration.[5]

The three key categories of clauses below should be closely considered in construction contracts governed by Malaysian law.

a. Penalty or liquidated damages clause

Until recently, the general view under Malaysian law was that Section 75 of the Contracts Act would render liquidated damages clauses to be penal and therefore invalid. This was based on the idea that an injured party may not recover a fixed sum in a damages clause unless it can prove the actual damages suffered (except where it is difficult to establish the suffered damage or loss).

However, in a recent case,[6] the Federal Court held that an injured party will not have to prove actual damage or loss in every case, although such evidence may be useful as a starting point. Instead, "reasonable compensation" as stipulated under Section 75 of the Contracts Act is to be determined through concepts such as "legitimate interest" and "proportionality." Reasonable compensation must also not exceed the amount stated in the contract.

b. Exclusion and limitation of liability clauses

Construction contracts often include exclusion or limitation of liability clauses. Generally, Malaysian courts uphold these clauses, especially in contracts entered between sophisticated parties dealing at arm's length. However, clauses that attempt to carve out from the Court's supervision consumers' right to enforce a contract and exclude all liability would be "patently unfair"[7] and ultimately "void to that extent."[8] Specifically, clauses that seek to limit the time that a party has to bring a claim may be rendered void by Section 29 of the Contracts Act 1950, as interpreted by the apex court in Malaysia.[9]

The courts construe exclusion clauses strictly. Courts will not enforce a clause that is so broad as to defeat the purpose or main object of the contract (e.g., excluding liability for a fundamental breach of contract).

c. Conditional payment clauses

Under Section 35 of the CIPA Act, "clauses which obligate conditional payment" are unenforceable under Malaysian law. This limitation is notable, as contracts in the construction industry often use such provisions. For instance, contractors commonly sublet work to subcontractors on a pay-if-paid basis.

Section 35(2) of the CIPA Act defines "conditional payment provisions" to be those that make: (i) the obligation of one party to make payment conditional upon that party receiving payment from a third party; or (ii) the obligation of one party to make payment conditional upon the availability of funds or financing facilities of that party.[10] In interpreting Section 35(2) of the CIPA Act, the courts have held that Section 35 is to be given an expansive interpretation and conditional payment is not limited to the two instances provided in Section 35(2) of the CIPA Act.[11] Section 35 effectively takes away the right of the paying party to conditional payment upon satisfaction of certain conditions (such as completion of the construction project, or receipt of payment by a third party). Instead, Sections 36(3) and 36(4) provide default payment provisions, which provide that the frequency of progress payment shall be "(a) monthly, for construction work and construction consultancy services; and (b) upon the delivery of supply, for the supply of construction materials, equipment or workers in connection with a construction contract,'[12] and that the "due date for payment under subsection (3) is 30 calendar days from the receipt of the invoice.'[13]

The CIPA Act applies to construction contracts signed after April 15, 2014.[14] In 2019, the Federal Court affirmed the

Under Malaysian law, a contractor cannot suspend its works even when the employer fails to pay, unless the contract contains that right

70%

Foreign ownership of companies in certain industry sectors could be limited to 70%

Court of Appeal's decision that the CIPA Act, including Section 35, did not apply to a contract entered prior to the CIPA Act's implementation. Thus, conditional payment clauses agreed prior to April 15, 2014 may be valid and enforceable. It has also been held that a conditional payment clause is only void for purposes of adjudication, stating that if Parliament had wanted the prohibition to be of general application, it would have amended the Contract Act, and not restricted the prohibition against conditional payment clauses to statutory adjudication under the CIPA Act. [15]

How does a contractor secure adequate cash flow in Malaysia?

Various contractual and statutory mechanisms allow a contractor to secure adequate cash flow in Malaysia. The CIPA Act in particular was enacted to deal with payment disputes (critical to contractors' cash flow), through an interim dispute resolution process.

The CIPA Act aims to address the issue of non-payment for work performed within the construction industry. It applies to all construction work, including consultancy agreements, although excluding buildings of fewer than four stories that are occupied by natural persons.[16]

Under Malaysian law, a contractor cannot suspend its works even when the employer fails to pay, unless the contract contains that right.[17] Generally, if a contractor suspends work owing to non-payment, this would constitute a repudiatory breach entitling the employer, in turn, to terminate the contract. Many contracts also expressly disallow suspension for late or non-payment.

Section 29 of the CIPA Act seeks to militate against the harsh effects of a strict application of the common law.

US$36 billion

Demand for construction in Malaysia in 2019

It provides that a party "may suspend performance or reduce the rate of progress of performance of any construction work or… consultancy services" if a contractor has obtained a favorable decision in adjudication, and the owner fails to pay the adjudication amount. The contractor would also be entitled to a fair and reasonable extension of time for the period of the suspension.

This section therefore suggests that if a party wishes to suspend, or reduce the rate of work, they must first pursue an adjudication process under the CIPA Act. This tiered process is thus consistent with the stated objectives of the CIPA Act to streamline the performance of the construction industry, and secure a more efficient and effective process.

When does a right to terminate arise from a breach of contract under Malaysian law?

The position in Malaysia mirrors the approach reflected in most common law jurisdictions.

Generally, the right to terminate a contract arises when there has been a fundamental breach.[18] Section 40 of the Contracts Act provides that when a party to a contract has refused to its obligations, the other party may terminate unless the reneging party has signified, by words or conduct (including silence), that it wishes to keep the contract going.

Section 54 of the Contracts Act also provides separate grounds for termination. When a contract contains reciprocal promises, and one party to the contract prevents the other from performing those promises, the contract becomes voidable at the option of the aggrieved party. Similarly, Section 56 provides that if time is of the essence and a party promises to perform a certain act by a specified time and fails to do so, the aggrieved party may elect to void the contract.

When might the parties' obligations be amended, or performance excused, due to unforeseen circumstances?

While Malaysian law does not have a generally recognized concept of force majeure, it allows parties to agree on the legal consequences of force majeure events or circumstances. Parties may freely agree which circumstances will qualify as to frustrate performance of the contract.

Separately, Section 57 of the Contracts Act provides that a contract is rendered void if some event "which the promisor could not prevent" makes performance of the contract impossible or unlawful.[19] Case law suggests that "impossibility" includes circumstances in which performance of the contract is radically different from what was originally agreed between the parties.[20]

When an agreement is rendered void, any person who has received any advantage must restore the status quo, or compensate the person from whom benefit was (wrongly) received.[21] A contractor must also be aware that if it fails to conduct reasonable due diligence —which might have made it aware that the promised act was either unlawful or impossible—it must make compensation to the promisee (i.e., the employer) for any loss that the promisee sustained following non-performance.[22]

How can disputes under construction contracts be resolved?

The CIPA Act aims to provide an efficient and expedient dispute resolution processes. Under Section 37(1), a party may commence adjudication, arbitration or litigation concurrently. It is uncertain, however, whether this position would still apply if the contract contained specific clauses that

barred concurrent actions. Arguably it would apply, as the courts have held that the parties cannot contract out of the CIPA Act[23] and that the provisions of the CIPA Act would trump contractual provisions.[24] Due to the complexities involved with resolving a dispute once it arises, parties would do well to provide advance consent to clearly drafted dispute resolution mechanisms.

- **Litigation:** One option is for the dispute to be resolved through litigation before specialized courts in the Kuala Lumpur High Court and Shah Alam High Court (in the state of Selangor). These courts have jurisdiction over: building, engineering and other construction disputes; claims by or against engineers, architects, surveyors, accountants and other specialist consultants; claims by or against local authorities in connection with their statutory duties in relation to land development and building construction; and arbitration-related proceedings, including challenges against arbitral awards[25]
- **Statutory adjudication:** Under the CIPA Act, statutory adjudication is temporarily binding in nature. Section 37(3) allows for a party to refer its dispute to both arbitral and adjudication processes. However, parties who desire a final and binding process that is both fast and effective ought to consider arbitration
- **Arbitration:** This is the preferred forum of dispute resolution. It is defined by efficient procedures, confidentiality (often desirable in large-scale construction projects) and certified qualified adjudicators. The Asian International Arbitration Centre (AIAC) is Malaysia's hub for alternate dispute resolution. It provides for a "Fast Track"[26] arbitration process that allows for "summary" or "documents-only" hearings. Substantive oral hearings must be completed within 160 days from commencement,[27] and a documents-only proceeding must be completed within 90 days.[28] The arbitrator's fee and administrative charges are fixed in accordance with a pre-established scale. Malaysian parties are not limited to choosing the AIAC as the applicable arbitral institute. For example, parties to a Malaysian contract frequently choose the rules of the Singapore International Arbitration Centre (SIAC) or the Hong Kong International Arbitration Centre (HKIAC).

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Philippines

By David Robertson, Karim Mariey and Khadija El-Leithy

The authors would like to thank Gulapa Law, Philippines, for its contributions to this chapter.

TOTAL POPULATION

109.58 million[1]

2020

GDP

US$361.49 billion[2]

2020

KEY INDUSTRIES

2020

61.42% of GDP

SERVICES

28.4% of GDP

INDUSTRY

10.18% of GDP

AGRICULTURE

DEMAND FOR CONSTRUCTION

US$5.4 billion[3]

2020

WORKING LANGUAGES

Filipino/English

The Philippines is becoming an increasingly attractive place for investment as a result of its sustained economic growth, active labor market and favorable business conditions. According to a recent World Bank report, the Philippine economy carried its strong growth momentum from the second half of 2019 into early 2020. While growth in the Philippines decelerated in 2020 due to the impact of COVID-19, economic growth is expected to rebound in 2021 – 2022.[4] Such economic growth, particularly as it relates to investments, is largely due to the government's ambitious "Build, Build, Build" infrastructure program. This program focuses on high-impact projects that are intended to increase the economy's productivity, create jobs, generate higher incomes and strengthen the investment climate to foster sustained growth. More specifically, the "Build, Build, Build" initiative is aimed at raising infrastructure investments to 7.4 percent of the country's gross domestic product (GDP) by 2022, as compared to the 5.1 percent figure in 2016.[5]

Are there any restrictions on foreign investment?

Foreign investment in the Philippines is regulated by the Foreign Investments Act of 1991 (Republic Act No. 7042, as amended). While it is the policy of the Philippines to attract, promote and welcome foreign investments, the Foreign Investments Act, and other special laws, place restrictions on foreign ownership in certain sectors. These restrictions are summarized in the 11th Foreign Investment Negative List (11th FINL) issued by the president through Executive Order No. 65 series of 2018.[6] The restrictions most relevant to

investment in the construction industry include:

- A 40 percent limit on foreign ownership in respect of contracts for the construction and repair of locally funded public works (subject to certain exceptions under the Build-Operate-Transfer Law (Republic Act No. 7718, as amended)) and
- A 40 percent limit on foreign ownership in the exploration, development and utilization of natural resources, except under a financial or technical assistance agreement entered into with the president for large-scale exploration, development, and utilization of minerals, petroleum and other mineral oils[7]

The 11th FINL does not provide an exclusive list of restrictions or exceptions to such restrictions. For example, the president may agree to waive or modify the application of nationality restrictions or preferences in the procurement of contractors for projects financed through official development assistance under Republic Act No. 8182, as amended.

The Philippine Congress is due to vote on legislation amending a number of laws, including the Foreign Investments Act.[8] It is understood that these amendments would serve to loosen the restrictions on foreign ownership and foreign investment.

Is your contract enforceable under Philippine law?

The Civil Code of the Philippines (Republic Act No. 386, as amended) will apply to a construction contract that is both governed by the law of the Philippines and relates to a project to be constructed in the Philippines. Otherwise, the applicability of the Civil Code to a construction contract will depend on a number of factors including the governing law of the construction contract, place of performance of the contract and the nationalities of the contracting parties. For example, a contract for execution of a project in the Philippines that is not governed by Philippine law but where one of the parties is Filipino is likely to be sufficiently connected to Philippine law such that the Civil Code will apply to it.

The Civil Code defines a contract as "a meeting of minds between two persons whereby one binds himself, with respect to the other, to give something or to render some service."[9] For a valid contract to exist, three requirements must be satisfied: consent, object and cause.[10] A construction contract that is freely entered into and signed (signifying consent) for the construction of a specific scope of works (the "object" of the contract) in return for payment of a contract price (the "cause") is likely to satisfy these three requirements.

Generally, Philippine law recognizes and upholds the freedom to contract insofar as it allows contracting parties to freely agree on the terms and conditions of their contracts, provided such terms and conditions are not contrary to law, morals, good customs, public order or public policy.[11]

The Civil Code does not impose any specific requirements for the enforceability of construction contracts. There is no requirement under the Civil Code that contracts must be recorded in writing. This means oral contracts are enforceable, although this is subject to the application of the Statute of Frauds, which requires certain contracts, including those relating to goods, chattels or things in action at a price not less than 500 pesos, to be reduced to writing.[12] By way of example, in the construction context, the Statute of Frauds would apply to an EPC contract (due to the procurement aspect of that contract) and, therefore, an EPC contract should be made in writing to ensure that it is enforceable.

7·4%

The Philippines' Build, Build, Build initiative is aimed at raising infrastructure investments to 7.4% of the country's GDP by 2022

Except where a provision of the Civil Code is drafted in mandatory or prohibitive terms, the applicable sections of the Civil Code are not compulsory—meaning parties are generally at liberty to contract out of them as they see fit. Subject to the mandatory or prohibitive terms of the Civil Code, where a construction contract contains provisions that are inconsistent with provisions of the Civil Code, the courts will generally look at the parties' intentions and treat the contract as the law between the parties, i.e., apply the doctrine of pacta sunt servanda, such that the terms of the contract will prevail over the Civil Code.

Examples of non-compulsory provisions of the Civil Code that parties to a construction contract may consider expressly contracting out of include:

- Article 2200, which permits recovery of lost profit, in addition to actual damages and
- Articles 1714, 1561 and 1566, which provide that where a contractor has carried out works using its own materials, the contractor is deemed to have given a warranty against hidden defects, unless: (a) the construction contract provides otherwise; and (b) the contractor was not aware of the relevant defects

a. Penalty or liquidated damages clauses

Under the Civil Code, liquidated damages provisions, defined as "damages agreed upon by the parties to a contract to be paid in case of breach thereof,"[13] are generally enforceable. However, if the amount of liquidated damages provided for in the

contract is found to be iniquitous or unconscionable[14] the court (or an arbitral tribunal applying Philippine law) has the authority to equitably reduce such amount while still enforcing the liquidated damages provision.[15] In reducing the amount of liquidated damages, the courts of the Philippines will consider, among other things, the actual loss suffered, or likely to be suffered, by the employer as a result of the relevant breach. The courts, however, cannot increase the amount of liquidated damages, although they may, in addition to liquidated damages, award exemplary damages.

b. Exclusion and limitation of liability clauses

Under the law of the Philippines, provisions seeking to exclude liability for future fraud are void.[16] Similarly, and in the context of construction contracts, provisions seeking to exclude or limit a contractor's liability for defective work are void if the contractor acted fraudulently. Provisions seeking to exclude or limit liability for gross negligence and willful misconduct may also be considered contrary to public policy and, therefore, unenforceable. Aside from these limitations, the law of the Philippines generally does not restrict the losses or types of liability that can be excluded or limited by parties to a construction contract.

c. Conditional payment clauses

Philippine law recognizes certain conditional payment obligations, such as pay-when-paid clauses,[17] provided such clauses are not contrary to law, morals, good customs, public order or public policy.[18] Under the Civil Code, conditional obligations that depend upon the will of a third person will take effect, assuming conformity of such obligations with mandatory provisions of Philippine law. Insofar as pay-when-paid clauses typically make payment by a contractor to its subcontractor contingent on the contractor's receipt of payment from the employer, such clauses would therefore fall within this category of conditional obligations.

Similarly, a pay-if-paid clause, which provides that a contractor is not required to pay subcontractors unless and until it receives payment from the employer, is also enforceable under Philippine law.[19] A pay-if-paid clause, in simple terms, is a condition precedent to payment that shifts the burden of potential non-payment to the subcontractor. In effect, the subcontractor assumes the risk of the owner's non-payment.

How does a contractor secure adequate cash flow in the Philippines?

Pursuant to Presidential Decree No. 1746, the Construction Industry Authority of the Philippines (CIAP) has a duty to promote, accelerate and regulate the growth and development of the construction industry. The CIAP has recommended prevailing industry best practice with respect to payment terms for parties to a construction contract, which have the effect of helping contractors in the Philippines secure adequate cash flow.

Under CIAP Document 102 (Uniform General Conditions of Contract for Private Construction, as amended) for private construction projects, payment mechanisms such as monthly payments are frequently used to manage a contractor's cash flow.[20] CIAP Document 102 recommends that an owner make an advance payment to the contractor for mobilization and purchase of materials, and that such payment is to be recouped pro rata in subsequent milestone payments.[21] It should be noted, however, that CIAP Document 102 will only apply to a private construction contract to the extent necessary to deal with conflicts in, or supplement omissions from, that contract.

40%

Limit on foreign ownership in respect of contracts for the construction and repair of locally-funded public works

Contracts with the government of the Philippines for the construction of buildings and other infrastructure works are generally governed by the Government Procurement Reform Act (GPRA). Pursuant to the GPRA, and its Implementing Rules and Regulations, the Government Procurement Policy Board has issued standard bidding documents for the procurement of government contracts involving the disbursement of public funds for the construction of infrastructure works. These bidding documents envisage payment of an advance payment to the contractor of an amount not exceeding 15 percent of the contract price, with the advance payment being proportionately repaid by the contractor through deductions from its progress payments.

When does a right to terminate arise from a breach of contract under Philippine law?

Philippine law states that in the event of a breach of contract, the injured party may choose between "specific performance" (i.e., the fulfillment of the obligation), and the rescission of the obligation, if the breach is so substantial and fundamental as to defeat the object of the parties in making the agreement.[22]

If expressly provided for in the construction contract, parties may also terminate the contract for specified reasons, such as bankruptcy or insolvency.[23] Typically, a contractor is given the right to

suspend work or terminate the contract upon written notice to the employer if the employer fails to pay the contractor an approved request for payment.

When might the parties' obligations be amended, or performance excused due to unforeseen circumstances?

The Civil Code excuses contractual performance, or allows for the amendment, of parties' obligations if one of these things occurs: (i) a force majeure event;[24] (ii) legal or physical impossibility;[25] or (iii) a difficulty beyond the contemplation of the parties.[26]

The principle of force majeure under the Civil Code provides that "no person shall be responsible for those events which could not be foreseen, or which, though foreseen, were inevitable."[27] In the context of construction contracts, this may include natural occurrences such as floods, typhoons, or an "act of man", such as wars, riots or terrorism. However, parties are free to contractually expand, or limit, the scope of events that may constitute force majeure.

Separately, the Civil Code provides that an obligor will be released from an obligation when the obligation becomes legally or physically impossible without the fault of the obligor.[28] An event of legal impossibility refers to instances where the obligation is prohibited or prevented by law (e.g., the non-renewal of a work permit or contractor license, preventing a contractor from continuing its work). On the other hand, physical impossibility refers to an act that can no longer be fulfilled by reason of its nature. For instance, a contractor would not be in breach for failing to complete works on a building destroyed by fire through no fault of their own.

Philippine law does not provide clear guidance on the differences between force majeure and legal or physical impossibility. The two principles differ in that force majeure focuses on the nature of the event that caused the breach (i.e., whether the event was foreseeable or inevitable) and legal or physical impossibility focuses on the obligation undertaken by the parties (i.e., whether the obligation becomes impossible to perform).

The Civil Code also permits an obligor to be released from its obligation, in whole or in part, where the service has become manifestly difficult beyond the contemplation of the parties.[29] This includes scenarios where there have been exceptional changes in circumstances, taking into account the risks assumed by the parties when the contract was signed.

How can disputes under construction contracts be resolved?

Disputes under construction contracts can be resolved through litigation or alternative dispute resolution methods recognized under the Republic Act No. 9285 (The Alternative Dispute Resolution Act of 2004) such as arbitration, mediation and the use of dispute boards.

- **Litigation**: Disputes arising from construction contracts that do not contain arbitration clauses are resolved through litigation before the first and second-level courts in the Philippines
- **Arbitration**: By virtue of Executive Order No. 1008 (Creating an Arbitration Machinery in the Construction Industry Authority of the Philippines), the Construction Industry Arbitration Commission (CIAC) was created in 1985. The CIAC's primary functions are to (i) formulate and implement an arbitration program for the construction industry; (ii) articulate policies and stipulate rules and procedures for construction arbitrations; and (iii) supervise the arbitration program and exercise the authority necessary with regards to the appointment, replacement or challenging of arbitrators.[30]

An interesting feature of Philippine law, as it relates to the resolution of construction disputes, is that where: (i) parties to a contract have voluntarily agreed to submit any disputes to arbitration; and (ii) the relevant dispute arises from, or in connection with, a contract entered into by parties involved in construction in the Philippines, that arbitration must be conducted under the auspices, and will fall within the exclusive jurisdiction of, the CIAC. Importantly, where these two requirements are met, the CIAC's mandatory jurisdiction will apply even where the CIAC is not specified in the arbitration agreement, and even where the arbitration agreement makes provision for another arbitral institution.

In this respect, therefore, the CIAC has exclusive jurisdiction over disputes arising from, or in connection with, construction contracts in the Philippines, whether the dispute arises before or after the completion of the contract or as a result of a breach thereof. This means that even where the relevant contract is not by its nature a construction contract, but the dispute in relation to that contract arises from a construction contract, the arbitration will nevertheless fall within the CIAC's jurisdiction.

By way of example, if a finance contract document is incorporated by reference into a construction contract (for example, in the context of project finance projects), the Philippine courts are likely to rule that any disputes arising under the finance contract document will be arbitrable before the CIAC. This is because the dispute arises *from* a construction contract. Parties to construction contracts should, therefore, exercise caution when incorporating documents by reference into their construction contract.

There is, however, scope for parties to challenge the jurisdiction of the CIAC on the following grounds:[31]

- The dispute is not a construction dispute
- The respondent was represented by one without capacity to enter into a binding arbitration agreement
- The arbitration agreement is invalid for some other reason, or does not cover the particular dispute sought to be arbitrated or
- Other issues of interpretation or nonfulfillment of pre-conditions to arbitration that are raised in the arbitration agreement

□ **Mediation**: Under the CIAC Mediation Rules, mediation is defined as a voluntary process in which a mediator selected by the parties in dispute[32] facilitates communication and negotiation as well as assists the disputing parties in reaching a voluntary agreement regarding a dispute. A party may initiate the mediation process by delivering a written Request for Mediation to the other party in accordance with the CIAC Mediation Rules. If mediation fails to resolve the dispute after a non-extendable period of 48 days, the parties should refer their dispute to the CIAC for settlement.[33]

It is worth noting that while the Philippines has signed the Singapore Mediation Convention, an international agreement recognizing mediated settlements, the Convention has not yet come into force.

Endnotes

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31 CIAC Rules of Procedure, as of 22 June 2019, Section 2.4.1.
32 CIAC Mediation Rules, as of 19 November 2005, Section 6.
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Singapore

By Dr. Matthew Secomb and Philip Tan

TOTAL POPULATION

5.69 million[1]
2020

GDP

US$339.99 billion[2]
2020

KEY INDUSTRIES
2020

70%
SERVICES INDUSTRIES

25.5%
GOODS-PRODUCING INDUSTRIES INCLUDING MANUFACTURING AND CONSTRUCTION

4.3%[3]
OWNERSHIP OF DWELLINGS

DEMAND FOR CONSTRUCTION

US$27 - 34 billion[4]
2020 – 2021

WORKING LANGUAGE

Predominantly English

Singapore is a vibrant country in Southeast Asia. With its excellent location, it is a hub for resolving many construction disputes across the Asia-Pacific region. This has allowed Singapore to develop a significant and coherent body of case law on construction disputes. Singapore has also been active in passing legislation (e.g., the Building and Construction Industry Security Payment Act) and promoting dispute resolution mechanisms (e.g., the Singapore Infrastructure Dispute-Management Protocol) which are specifically tailored toward the construction industry.

Singapore is a common law country, with its laws primarily based on English law.

Are there any restrictions on foreign investment?
In comparison to other countries in the region, Singapore has limited restrictions on foreign investment. There are some sectors where foreign investment controls are imposed, for instance in real estate, media broadcasting and national security. Generally, the approach is one of consultation between regulators and foreign investors. Singapore has an investor-friendly tax regime.

Is your contract enforceable under Singapore law?
Generally, Singapore law recognizes and upholds freedom of contract. It is the exception, rather than the norm, that a clause might be deemed unenforceable. Nevertheless, in a few situations, key clauses of a construction contract may be unenforceable under Singapore law.

Two types of clauses are of particular interest:

a. Penalty or liquidated damages clauses

Liquidated damages are ascertained damages that the parties agreed to be payable should the contract be breached.

A liquidated damages clause is enforceable in Singapore, as long as it represents a genuine pre-estimate of loss. Otherwise, it will be treated as a penalty and not be enforced.

Whether a clause is a liquidated damages clause or a penalty is a matter of construction. It is determined in light of the facts and circumstances when the contract was signed. As set out recently by the highest court in Singapore (the Court of Appeal), the key test is whether the stipulated sum is "extravagant and unconscionable" in amount in comparison with the greatest loss that could conceivably be proved to have followed from the breach.[5] The position in Singapore differs from that in the United Kingdom where the question is whether the clause imposes a detriment that is out of proportion to any "legitimate interest of the innocent party."[6] The Singapore Court of Appeal had noted the considerable uncertainty over what constitutes a "legitimate interest," and declined to adopt the UK approach.

b. Exclusion and limitation of liability clauses

Exclusion or exemption of liability clauses seek to completely exclude a contracting party's liability. Limitation of liability clauses seek to limit contractual liability.

Whether an exclusion or limitation of liability clause will have its intended effect depends on three main elements: incorporation; construction; and regulation.

For the clause to be effective, it has to be incorporated into the contract. This could be done by signing the contract,[7] bringing the clause to the other party's attention before or at the time the contract is made,[8] or on the basis of the parties' prior course of dealing.[9]

The clause has to clearly set out the situations under which a party's liability would be excluded. Any ambiguity will be resolved against the party seeking to rely upon the clause.[10] For example, to exclude liability for negligence, it would be preferable to expressly refer to the word "negligence" in the clause.[11]

Singapore adopts a less strict approach for limitation of liability clauses as compared to exclusion clauses. This is because Singapore law recognizes that these clauses are part of the overall risk and remuneration allocation between the parties, and that it is possible for the other party to insure.[12]

An exemption of liability clause might also be subject to certain statutory restrictions. The Unfair Contract Terms Act (UCTA) imposes two key restrictions on commercial contracts.[13] First, any exclusion or limitation of liability for negligence must satisfy the requirement of "reasonableness," as defined in the statute.[14] Second, where a party deals on the other's written standard terms of business, any exclusion or limitation of liability (whether for negligence or otherwise) must also satisfy the reasonableness test.[15]

Depending on the location of the parties/transaction, these restrictions might not apply (e.g., they generally do not apply to international sale of goods contracts, or where the governing law of the contract would have been the law of some country other than Singapore, but for the parties' choice of Singapore law).[16]

April 1, 2015

The SOP Act broadly applies to contracts for construction work entered on or after April 1, 2015

How does a contractor secure adequate cash flow in Singapore?

The Building and Construction Industry Security Payment Act (SOP Act) broadly applies to contracts for construction work or related goods or services, to the extent it deals with construction work carried out in Singapore.[17] It applies to contracts entered on or after April 1, 2005. It aims to improve cash flow in the construction industry by giving parties the right to seek progress payments for work done, and providing fast and low-cost adjudication for payment disputes.

The SOP Act provides, among other things, a right to progress payments. This means that under certain circumstances, a contractor can claim payments for the carrying out of construction work, or the supply of related goods or services, under a construction contract. The claims process is relatively straightforward. A contractor first serves a "payment claim" on a respondent, who must then

Under Singapore law, a breach of contract does not automatically allow a party to terminate the contract

serve a "payment response." Where payment is disputed (or the respondent otherwise fails to pay), the contractor may apply to an authorized nominating body, which appoints an adjudicator. The respondent may reply to the application, after which the adjudicator will make a determination. The process typically takes a matter of weeks.

The adjudication decision is binding on the parties unless or until any dispute between them is resolved by agreement or determined by a court or arbitral tribunal.

Under the SOP Act, a contractor may suspend works upon failure of the respondent to pay an adjudicated amount (upon giving notice).[18] The contractor may also exercise a lien on goods supplied by the contractor to the respondent.[19]

Separately, the SOP Act makes pay-when-paid clauses unenforceable. Under a pay-when-paid clause, a party (e.g., a sub-contractor) is paid only when the other contracting party (e.g., the main contractor) has received payment from some third party (e.g., the employer). Parties should consider how this affects the risk allocation among themselves.

When does a right to terminate arise from a breach of contract under Singapore law?

The starting point is that a breach of contract does not automatically allow a party to terminate the contract.

An innocent party may terminate the contract where the contract clearly and unambiguously provides for events under which it could terminate the contract, and those events have occurred.

If the contract does not provide such a right, the innocent party may terminate the contract in broadly three situations:

> **An innocent party may terminate the contract when the contract clearly and unambiguously provides for events under which it could terminate the contract**

a. **Repudiation:** Repudiation occurs when a party refuses to perform the contract (i.e., it renounces the contract). Examples of repudiation by the employer in construction disputes include: the employer's failure to give possession of the site to the contractor; when the contractor is wrongfully ejected from the site; or when the architect or contract administrator refuses to certify payment at the appropriate time or constantly under-certifies the amount due because of undue influence from the employer.[20]

b. **Breach of a condition:** A condition is defined as a term that the parties have agreed to be so important that its breach would entitle the innocent party to treat the contract as discharged. The focus here is on the nature of the term breached, and not the consequences of the breach.[21]

c. **Fundamental breach:** Even if the clause that was breached is not a condition, the innocent party may terminate the contract if the breach was "fundamental."[22] A fundamental breach "deprives the innocent party of substantially the whole benefit that it was intended to obtain from the contract".[23] For example, a fundamental breach may occur when defects to a building are so serious that the entire building has to be rebuilt.[24]

When might the parties' obligations be amended, or performance excused due to unforeseen circumstances?

Under Singapore law, the parties are free to agree to contractual provisions dealing with unforeseen circumstances. For example, the parties can agree to a hardship or force majeure clause. A force majeure clause is an agreement on how outstanding obligations should be resolved when affected by *unforeseeable* events.[25] It contractually allocates the risks between the contracting parties with regard to those events, which would be specified in the clause.[26]

Even if the parties have not provided for it, a contract can be discharged by frustration. This is when, without the default of either party, a contractual obligation has become incapable of being performed because performance in the circumstances would be radically different from what was undertaken in the contract.[27] Frustration can happen in situations when the subject matter of the contract has been destroyed, the contractual promisor has died or become physically incapacitated, and when the source of supply of the contract has failed.[28] The doctrine of frustration is only applied in exceptional circumstances.[29]

When a contract is frustrated under common law, it is automatically discharged.[30] Parties can exclude the doctrine of frustration by doing so clearly and unambiguously in the contract.[31]

A Singapore court may allow a party to recover payments made or expenses incurred before the

frustrating event occurred, depending on the circumstances of the case and whether it is just to allow such recovery.[32]

Because of their nature and function, both frustration and force majeure could be relevant when there is a radical external event that occurs during the course of the contract's performance, which was not due to the fault of any of the contracting parties.[33] Whether either applies would depend heavily on the circumstances of the case and, for force majeure, the precise wording of the force majeure clause.

How can disputes under construction contracts be resolved?

The two most common methods of dispute resolution in Singapore are litigation and arbitration:

- **Litigation:** The Singapore courts have deep expertise with construction disputes. In particular, the Singapore International Commercial Court (SICC) draws together a panel of international judges, comprising both civil and common law jurists, many of whom have significant experience in resolving construction disputes

- **Arbitration:** Equally, the Singapore arbitration scene is robust and active. Courts in Singapore are generally seen as pro-arbitration. The Singapore International Arbitration Centre (SIAC) is a well-regarded arbitral institution. The ICC also administers cases from a Singapore office. The two key pieces of legislation governing arbitrations in Singapore are the International Arbitration Act (which applies to international arbitrations) and the Arbitration Act (which applies to domestic arbitrations)

Singapore has also been at the forefront of developing alternative dispute resolution procedures, including mediation and dispute board determination:

- **Mediation:** The Singapore International Mediation Centre (SIMC) offers mediation services, with a diverse panel of international mediators. The SIMC and SIAC, together, also offer an innovative hybrid mechanism combining mediation and arbitration. This is known as the Arb-Med-Arb process. Under such a mechanism, the claimant files a notice of arbitration and the respondent files a response. The tribunal is constituted but it stays the proceedings. The parties then enter into mediation. If the mediation is successful, the tribunal enters a consent award. However, if the mediation is not successful, the parties are referred back to arbitration

- **Dispute Board:** The Singapore Infrastructure Dispute-Management Protocol (SIDP) aims to help parties involved in large infrastructure projects manage disputes and minimize the risks of time and cost overruns. Under the SIDP, parties from the start of the project will appoint a Dispute Board that follows the project from start to finish. The board proactively helps manage issues as they arise to mitigate a full-blown dispute.

SGD 500 million

The SIDP is designed and recommended for construction of infrastructure projects of more than SGD 500 million in value

The Dispute Board will meet the parties to establish a schedule of Dispute Board meetings and site visits.[34] At any stage of the project, the parties themselves or the Dispute Board may raise a difference between the parties that must be resolved. In such circumstances, the Dispute Board may discuss with senior representatives of the parties and provide assistance to enable the parties to proceed or continue with their negotiations.[35] Parties may also apply to the Dispute Board for an opinion[36] or determination.[37]

The SIDP is designed and recommended for construction or infrastructure projects worth more than SGD 500 million. This may be due to the potentially high expenses of engaging a Dispute Board from the start of the project.

> **Singapore has been at the forefront of developing alternative dispute resolution procedures, including mediation and dispute board determination**

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7 *Consmat Singapore (Pte) Ltd v Bank of America National Trust & Savings Association* [1992] 2 SLR(R) 195, at para. 29.
8 *Thornton v Shoe Lane Parking Ltd* [1971] 2 QB 153 (referred to in *Tjjoa Elis v United Overseas Bank* [2003] 1 SLR (R) 747, para. 75).
9 *Zicom Pte Ltd v Antara Koh Pte Ltd* [1997] SGHC 215, at paras. 5-7.
10 This is known as the contra *proferentem* rule.
11 *Rapiscan Asia Pte Ltd v Global Container Freight Pte Ltd* [2002] 1 SLR(R) 701, at paras. 44-45. The starting point is that parties to a contract do not normally agree to accept the consequences of each other's negligence, unless the contract does not allow any other reasonable construction.
12 *Rapiscan Asia Pte Ltd v Global Container Freight Pte Ltd* [2002] 1 SLR(R) 701, at para. 61.
13 There are other restrictions in the Unfair Contracts Terms Act (UCTA), but we only note those which typically arise in the context of commercial, business-to-business contracts.
14 Unfair Contracts Terms Act (Cap 396, 1994 Rev Ed), section 2(2). The test for reasonableness is set out in section 11.
15 Unfair Contracts Terms Act (Cap 396, 1994 Rev Ed), section 3.
16 Unfair Contracts Terms Act (Cap 396, 1994 Rev Ed), sections 26 and 27.]
17 This is regardless of whether the parties chose Singapore law as the governing law. Building and Construction Industry Security of Payment Act (SOP Act), section 4.
18 SOP Act, sections 23 and 26.
19 SOP Act, sections 23 and 25.
20 See Halsbury's Laws of Singapore, Building and Construction (2010 issue), para. 30.203.
21 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte Ltd* [2007] 4 SLR 413, at para. 97.
22 *Sports Connection Pte Ltd v Deuter Sports GmbH* [2009] SGCA 22, at para. 74.
23 *Sports Connection Pte Ltd v Deuter Sports GmbH* [2009] SGCA 22, at paras. 75-76.
24 See e.g., the Malaysian decision of *Hwa Chea Lin v Malim Jaya (Melaka) Sdn Bhd* [1996] 4 MLJ 544 (court finding a fundamental breach where 'the said building when delivered to the plaintiffs was in a terrible shape that required massive remedial works and eventually had to be rebuilt'), which may be regarded in Singapore as persuasive.
25 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 56.
26 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 53.
27 *Alliance Concrete Singapore Pte Ltd v Sato Kogyo (S) Pte Ltd* [2014] SGCA 35, at paras. 34-36; *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 59 (citing *Davis Contractors Ltd v Fareham Urban District Council* [1956] AC 696).
28 *Alliance Concrete Singapore Pte Ltd v Sato Kogyo (S) Pte Ltd* [2014] SGCA 35, at para. 55; Andrew Phang Boon Leng, *The Law of Contract in Singapore* (2012), para. 19.027; *Taylor v Caldwell* (1863), 122 ER 309.
29 *Alliance Concrete Singapore Pte Ltd v Sato Kogyo (S) Pte Ltd* [2014] SGCA 35, at para. 38.
30 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 61.
31 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 63.
32 Frustrated Contracts Act (Cap 115, Rev Ed 2014), section 2..
33 *RDC Concrete Pte Ltd v Sato Kogyo (S) Pte* [2007] SGCA 39, at para. 57.
34 Singapore Infrastructure Dispute-Management Protocol, Clause 4.1.
35 Singapore Infrastructure Dispute-Management Protocol, Clause 5.
36 Singapore Infrastructure Dispute-Management Protocol, Clause 8. An Opinion is not binding on the parties (if any party objects to the opinion). If there is no objection, the Opinion must be complied with unless it is successfully challenged in litigation or arbitration.
37 Singapore Infrastructure Dispute-Management Protocol, Clause 9. A Determination is binding on both parties, unless it is successfully challenged in litigation or arbitration.

Vietnam

By Dr. Matthew Secomb, David Robertson and Catherine Yoon

The author would like to thank TNP Law, Vietnam, for its contributions to this chapter.

TOTAL POPULATION

97.34 million[1]
2020

GDP

US$271.16 billion[2]
2020

KEY INDUSTRIES
2019

41.6% of GDP
SERVICES

34% of GDP
INDUSTRY INCLUDING CONSTRUCTION

16% of GDP
MANUFACTURING

14% of GDP[3]
AGRICULTURE

DEMAND FOR CONSTRUCTION

US$57.5 billion[4]
2018

WORKING LANGUAGE

Vietnamese

Vietnam is the third-largest country in Southeast Asia. Due to favorable government policy and an abundance of natural resources, it is increasingly attractive to both domestic and foreign investors. Vietnam is strategically located in the heart of the Asia-Pacific region and is committed to global trade integration and trade liberalization. This is evidenced by its participation in APEC (which it hosted in 2017), the ASEAN Free Trade Area, the WTO and a growing network of free trade agreements, including the ASEAN-Australia-New Zealand Free Trade Agreement, and its trade agreement with the European Union.

Vietnam is a civil law country, modeled on the French and Soviet systems until the late 1980s.[5] From 2015, the Vietnamese Courts recognized court precedents as a source of law, which is likely to give greater certainty and stability to the legal regime in Vietnam.[6]

Are there any restrictions on foreign investment?

Vietnamese law explicitly provides that investors shall be treated equally in all economic sectors, as between domestic investment and foreign investment, and that industry "shall encourage and create favorable conditions for investment activities."[7] Different forms of foreign investment are subject to different licensing processes. Foreign investors or enterprises that wish to establish a new enterprise to implement an investment project must register the project to receive an investment registration certificate.[8]

Similarly, every enterprise must receive an enterprise registration certificate before beginning operations, which is issued by the provincial-level State Business Registration Authority. An "enterprise" is defined broadly as an "organization having its own name, having assets and a transaction office, and registered for establishment in accordance with law for trading purposes."[9]

Is your contract enforceable under Vietnamese law?

Freedom to contract constitutes one of the fundamental principles of Vietnamese contract law. Parties are generally free to agree on the specific contents and clauses of their contracts. In fact, a contract does not have to be in writing, except where required by a specific law.[10]

Two key types of clauses that are often the subject of significant negotiations are of particular interest:

a. Penalty or liquidated damages clauses

Penalty clauses fix, in advance and independently of the real loss suffered, the amount of damages due by one party if it breaches a contractual obligation.

Penalty clauses are valid under Article 300 of the Commercial Law, and Article 146 of the 2014 Construction Law. They are triggered if: (1) there is a breach of contract, and (2) the penalty for breach is stated in the contract. Parties can agree on the level of penalty for breach, unless otherwise prescribed by law. In particular, the level of penalty may be subject to a limitation of 8 percent of the contract value under the Commercial Law, or 12 percent of the contract value under the 2014 Construction Law.[11]

Liquidated damages clauses are similar in that they allow the parties to agree in advance on a fixed sum to be paid should the contract be breached. However, they are meant to be a reasonable and proportionate estimation of the damages payable in case of breach. If liquidated damages are disproportionate, they may be unenforceable.

Although liquidated damages are often included in construction contracts as a remedy for delay, they are not expressly authorized under Vietnamese law. Pursuant to Article 304 of the Commercial Law, the party claiming damages bears the burden of proving the loss and its amount. Therefore, the efficacy of liquidated damages clauses under Vietnamese law is questionable.[12]

b. Exclusion and limitation of liability clauses

Exclusion of liability clauses seek to completely exclude a contracting party's liability. In contrast, limitation of liability clauses seek to limit contractual liability. Such clauses will generally be enforceable under Vietnamese law, except in specific circumstances. Parties should take certain steps ensure that these clauses are enforceable, as outlined below.

The Commercial Law recognizes exemption of liability clauses agreed upon by the parties, without setting out particular conditions for their validity.[13] Parties to a contract should therefore ensure that they clearly agree upon the relevant contractual modalities.

Generally, a judge or arbitrator will not vary exemptions of liability agreed upon by the parties to a contract except in specific circumstances. In particular, (1) in arbitration, arbitrators must respect the parties' agreement as long as the agreement neither breaches any prohibitions nor contravenes "social ethics,"[14] and (2) in civil proceedings, the court's function is limited to deciding the dispute as set out in the relevant claim or petition. As a result, if the relevant exemption of liability clause does not contravene any "social ethic" or breach any prohibition, then an arbitrator or judge will generally not have discretion to vary that exemption of liability clause.

2015

Vietnamese Courts recognized court precedents as a source of law as of 2015

However, in certain circumstances a court might vary an exclusion clause. For example, a court may exercise its discretion to terminate or revise a contractual clause if requested by a party based on hardship. A party may also seek termination where the circumstances of the contract change substantially.[15] Circumstances will be deemed to have changed substantially when:

- The change is due to reasons beyond the control of either party or the change was unforeseen at the time of contracting
- The change is so significant that the parties would not have entered into the contract (either at all, or on the same terms)
- The continuation of performance of the contract without changing its terms would cause serious loss and damage to one party and
- The party claiming termination has taken all necessary measures but is unable to prevent or mitigate such loss and damage[16]

How does a contractor secure adequate cash flow in Vietnam?

Vietnamese government regulations on construction provide for various contractual mechanisms that have

the effect of helping a contractor secure adequate cash flow.

Under both Decree 37/2015[17] and Circular 30/2016,[18] parties can agree on advances that correspond to an amount of money offered in advance by the employer to the contractor for necessary preparations before implementation of the tasks under the contract. Details of the advances, including the level, date and terms of recovery, are determined by the parties. The sums paid under advances are deducted from the contract price at the date of payment. Although such agreement is not mandatory, both Decree 37/2015 and Circular 30/2016 include detailed guidelines to assist parties.

When does a right to terminate arise from a breach of contract under Vietnamese law?

In certain circumstances, Vietnamese law provides for the ability of a party to terminate a contract for breach. It also provides for the cancellation of contracts in certain circumstances.

Termination and cancellation are governed by the Civil Code.[19] The Civil Code sets out the circumstances where a contractual relationship may be deemed to be terminated or cancelled. This includes where termination may occur by agreement, including where a contract provides for termination upon the occurrence of certain events.[20] Even if the contract contains no termination or cancellation provisions, the Civil Code provisions on termination will automatically apply.

Under Vietnamese law, the starting point for termination is that a breach does not automatically allow a party to terminate a contract. If the parties have not agreed on the circumstances in which the contract may be terminated, then under Article 428 of the 2015 Civil Code, unilateral termination can only occur if the other party "violates its obligations seriously." If one party unilaterally purports to terminate a contract without basis, then it will be in breach.

However, if a contract clearly and unambiguously provides for events under which one party can terminate the contract, and such events have occurred, the contract can be terminated. For this reason, it is recommended that termination clauses be carefully drafted so as to expressly outline the circumstances in which a party may terminate.

Moreover, a substantial or serious breach of a contract may also give rise to a right to unilaterally terminate that contract (either if the parties agree so, or if otherwise prescribed by law).[21] A serious breach is defined as a failure by a party to correctly fulfill its obligations, so that the other party is unable to achieve the purpose of entering into the contract.[22]

Termination of a contract results in that contract becoming null and void from the time the other party receives a notice of termination. The terminating party should receive compensation for the damage caused by the improper performance of the other party.[23] In construction contracts, the contractor is entitled to terminate the contract if the principal does not perform its payment obligations in the time limit agreed by the parties.[24]

US$57·5 billion

Demand for construction in Vietnam in 2018

> **Under Vietnamese law, the starting point for termination is that a breach does not automatically allow a party to terminate a contract**

The Civil Code also provides for the cancellation of contracts in certain circumstances. If a contract is cancelled (for an inability to perform, for example) then it ceases to be valid from the time of its conclusion. This means that parties are not required to perform the obligations already agreed upon, except the agreements on penalty for breach, compensation for damage and dispute settlement. Late performance of a contractual obligation may also constitute a ground for cancellation of the contract.[25]

When might the parties' obligations be amended, or performance excused due to unforeseen circumstances?

Under Vietnamese law, parties are free to agree to contractual provisions dealing with unforeseen circumstances. For example, parties can agree to a hardship or force majeure clause.

If a contract does not provide otherwise, the parties may also claim force majeure under Vietnamese law. Under Article 161.1 of the old Vietnamese Civil Code and Article 156 of the new Civil Code, an event of force majeure is defined as circumstances that occur objectively and unpredictably and cannot be overcome despite all necessary measures having been taken (for example, a pandemic such as COVID-19 and consequences of the outbreak, war, strike or riot, or a natural disaster such as an earthquake or flood).

If a force majeure event occurs, the parties may be relieved from their liability for losses or damages, or performing their obligations.[26]

Under the Commercial Law, for the force majeure event to qualify for an exemption of liability, the defaulting party must immediately notify the other party in writing of the force majeure event and its possible consequences. It must also notify the other party when the force majeure event ends.[27]

In practice, construction contracts generally define a list of force majeure events. These clauses are valid under the principle of freedom of contract recognized under Vietnamese law. In the case of force majeure, employers or contractors are relieved from their liability for losses or delays in work.[28]

The new Civil Code introduced the concept of change of circumstances, which allows for renegotiation of the contract and, if that renegotiation fails, for termination of the contract by the court. However, the court may only amend the contract if the contract's termination would cause greater damage than the cost to perform the modified contract.[29]

Termination will only be justified if:

- The change in circumstances is due to objective reasons that occurred after the contract was signed
- The change in circumstances could not have been foreseen by the parties when the contract was signed
- The circumstances have changed in such a way that, if the parties had foreseen such a change in advance, they would not have concluded the contract or would have negotiated different terms and
- The party whose interests are adversely affected has undertaken all possible measures to prevent or minimize the effect of the change in circumstances

> **Most foreign investment contracts contain a dispute resolution clause specifying a preferred seat of arbitration in a country that is party to the New York Convention**

How can disputes under construction contracts be resolved?

There are a number of dispute resolution mechanisms available to foreign investors in Vietnam. These include litigation, arbitration and mediation.

- **Litigation:** Foreign investors may be reluctant to agree to litigation, due to the possibility of having to engage with an unfamiliar judicial process. They may also have concerns about the independence, impartiality and efficiency of the court system
- **Arbitration:** In 2003, arbitration was officially recognized by Vietnam as an alternative method of dispute resolution.[30] In recent years, arbitration has become an increasingly popular dispute resolution method in Vietnam. To date, there are 23 arbitration institutions in Vietnam registered with the Ministry of Justice, with the Vietnam International Arbitration Center (VIAC) at the Vietnam Chamber of Commerce and Industry being the most active international institution. The VIAC's panel of arbitrators include a number of high-profile foreign arbitrators, and it released an updated edition of its Rules of Arbitration in 2017.[31]

  The Law on Commercial Arbitration, which came into effect from January 1, 2011, addressed the shortcomings of the previous law, making the choice of arbitration more attractive as a dispute resolution forum for foreign investors. Notably, the Law on Commercial Arbitration adopted various changes, including: the option to appoint foreign arbitrators and the ability to apply for interim measures to protect the legitimate interests of the parties
- **International arbitration:** Foreign investors may, in most cases, choose that a dispute be resolved by international arbitration. International arbitration is expressly permitted under the Investment Law for disputes involving at least one foreign investor or foreign-owned company.[32] Similarly, in general terms, the law provides that commercial disputes can be resolved by arbitration. [33]

  Most foreign investment contracts contain a dispute resolution clause specifying a preferred seat of arbitration in a country that is a member of the New York Convention on the Recognition and Enforcement of Arbitral Awards. Vietnam

January 1, 2011

The Law on Commercial Arbitration came into effect on January 1, 2011

has ratified this Convention. This demonstrates Vietnam's commitment to maintaining arbitral integrity, and to enforcing foreign awards

- **Mediation and Dispute Adjudication Boards:** VIAC established the Vietnam Mediation Centre (VMC) in 2017 to regulate commercial mediation in Vietnam. Many multi-tiered dispute resolution clauses require that the parties conduct mediation before a matter can be referred to arbitration. The Civil Code also contains a provision recognizing mediated settlement agreements.

  Dispute Adjudication Boards (DAB) are often used when a construction dispute arises. The use of a DAB is stipulated in the FIDIC forms, and the Vietnamese government encourages parties involved in construction projects to use the FIDIC international standard conditions of contracts. Use of a DAB would come before mediation or arbitration, and is a chance to achieve settlement before referring the dispute to mediation or arbitration.

Endnotes

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3 World Bank, 'World Development Indicators: Structure of Output', available at: <http://wdi.worldbank.org/table/4.2>.
4 The construction industry's output value is expected increase from USD 57.5 billion in 2018 to USD 84 billion in 2023. Growth during 2014–2018 was driven by positive developments in regional economic conditions and government investment in energy and transport infrastructure. According to the government's estimates, Vietnam requires an investment of USD 48 billion until 2023 to develop its transport infrastructure. See Global Data, 'Construction in Vietnam — Key Trends and Opportunities to 2023' (30 January 2019) available at: <https://www.giiresearch.com/report/time242093-construction-vietnam-key-trends-opportunities-2016.html>.
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7 Vietnam Investment Law (Law No.59/2005/QH11), Article 4(2).
8 Vietnam Investment Law (Law No. 67/2014/QH13).
9 Law on Enterprises (Law No. 68/2014/QH13), Article 4(8).
10 For instance, Article 16 of the Law on Commercial Arbitration (Law No. 54/2010/QH12) provides that '[a]n arbitration agreement must be in writing'.
11 See Circular No. 30/2016/TT-BXD on Guidelines for Engineering, Procurement and Construction Contracts.
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13 Commercial Law (Law No. 36/2005/QH11), Article 294.
14 Law on Commercial Arbitration (Law No. 54/2010/QH12), Article 4.1
15 2015 Civil Code (Law No. 91/2015/QH13), Article 420(3)
16 2015 Civil Code (Law No. 91/2015/QH13), Article 420(1).
17 Decree No. 37/2015/ND-CP on Detailed Regulations on Construction Contract.
18 Circular No. 30/2016/TT-BXD on Guidelines for Engineering, Procurement and Construction Contracts.
19 2015 Civil Code (Law No. 91/2015/QH13), Article 4.1.
20 2015 Civil Code (Law No. 91/2015/QH13), Article 422.
21 2015 Civil Code (Law No. 91/2015/QH13), Article 428; Commercial Law (Law No. 36/2005/QH11), Article 310.
22 2015 Civil Code (Law No. 91/2015/QH13), Article 423(2).
23 2015 Civil Code (Law No. 91/2015/QH13), Article 428.4.
24 2014 Construction Law (Law No. 50/2014/QH13), Article 145.3(c).
25 2015 Civil Code (Law No. 91/2015/QH13), Article 424.
26 2015 Civil Code (Law No. 91/2015/QH13), Article 351.2.
27 Commercial Law (Law No. 36/2005/QH11), Articles 294, 295.
28 Nguyen Trung Nam, 'Vietnam' (2017) 17 Projects and Construction Review 321, pages 325–326.
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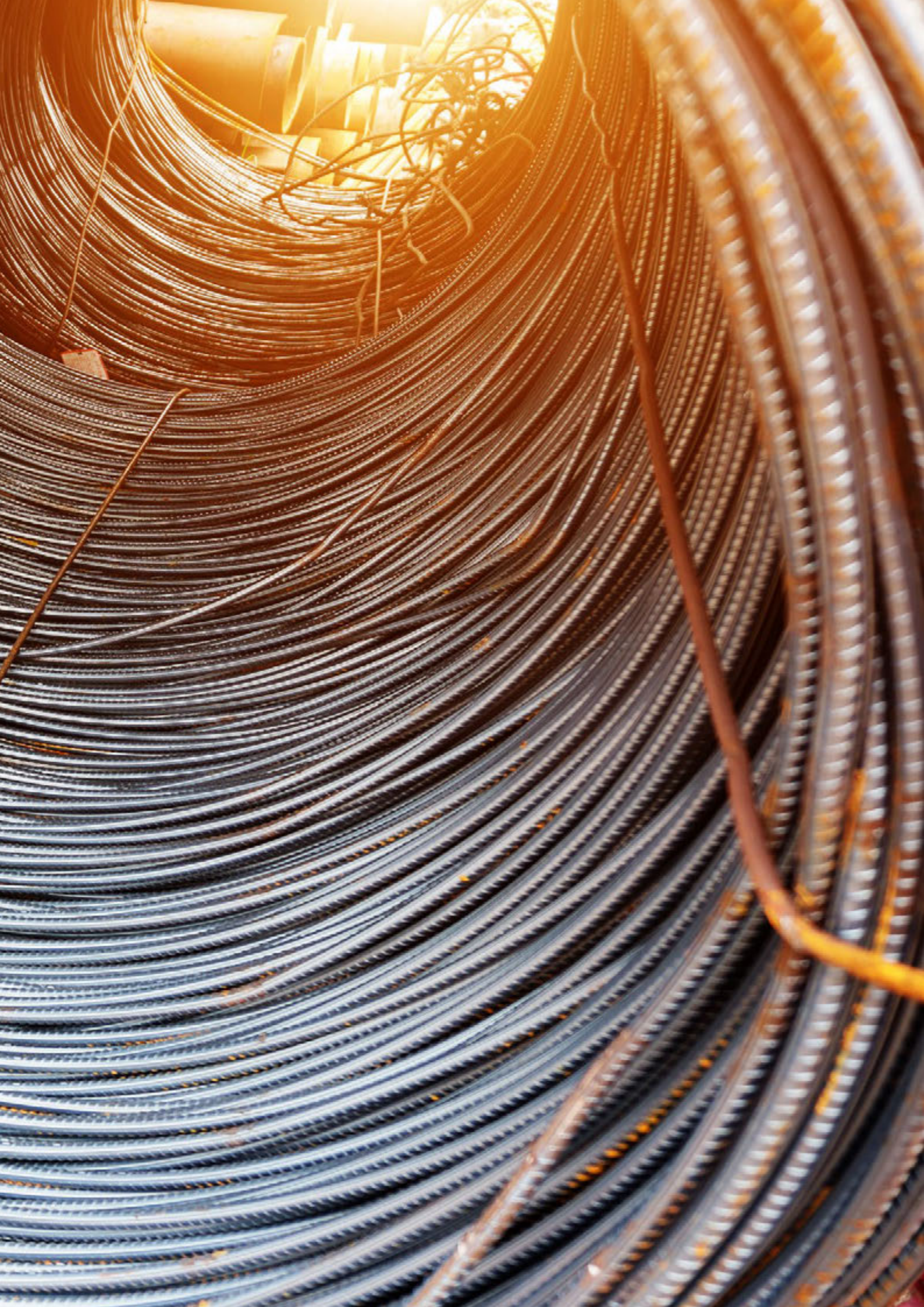

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