

**February 2016**

## **Employers be cautious of notification requirements**

Employer's claims are governed by sub-clause 2.5 in the Red, Yellow and Silver Books of FIDIC Contracts (and sub-clause 20.2 in the Gold Book). If an employer considers itself to be entitled to any payment from the contractor in connection with the contract, the employer is required to follow the procedure set out in this sub-clause, which includes the requirement to give notice to the contractor. But is an employer precluded from claiming payment at any later stage from a contractor if a notice in terms of sub-clause 2.5 is not given under the FIDIC contract?

In answering the question, regard must be had to the relevant provisions of sub-clause 2.5 which provides as:

"If the Employer considers himself to be entitled to any payment under any Clause under these Conditions, or otherwise in connection with the Contract..... the Employer or the Engineer shall give notice and particulars to the Contractor.

A notice shall be given as soon as practicable after the Employer became aware of the event or circumstance giving rise to the claim.....

The particulars shall specify the clause or other basis of the claim, and shall include substantiation of the amount..... to which the Employer considers himself to be entitled in connection with the Contract. The Engineer shall then proceed in accordance with sub-clause 3.5 [Determinations] to agree or determine (i) the amount (if any) which the Employer is entitled to be paid by the Contractor.....

This amount may be included as a deduction in the Contract Price and Payment Certificates. The Employer shall only be entitled to set off against or make any deduction from an amount certified in a Payment Certificate, or to otherwise claim against the Contractor, in accordance with this sub-clause."

The sub-clause makes it clear that an employer is entitled to claim a deduction or set-off from any amount owing to a contractor as set out in a Payment Certificate if the employer has complied with the requirements set out in sub-clause 2.5. But what if the contract is terminated

and no further Payment Certificates are issued? Is an employer entitled to claim payment from a contractor by way of a counterclaim in subsequent proceedings?

This is one of the issues which were recently decided upon by the Privy Council in the matter of *NH International (Caribbean) Limited v National Insurance Property Development Company Limited (Trinidad and Tobago)*. In summary, the relevant facts of the case were as follows:

- On 6 March 2003, the contractor and employer entered into a contract based on the FIDIC Redbook for the construction of a hospital in Tobago.
- The project started during March 2003 and the original completion date of the project was March 2005.
- The contractor suspended the works on 23 September 2005 and terminated the contract on 3 November 2006.
- Various disputes arose between the parties and those were referred to arbitration. The contractor claimed damages arising out of the determination of the contract and the employer submitted various counterclaims in the arbitration proceedings.
- The contractor only became aware of the counterclaims during the arbitration proceedings given that the employer had failed to deliver a notice in terms of sub-clause 2.5 at any stage following the conclusion of the contract.

The contractor contended that the employer was precluded from raising any counterclaims in the arbitration proceedings given that the employer had failed to give notice of an employer claim under sub-clause 2.5. The arbitrator rejected the contractor's contention in this regard and held that "clear words are required to exclude common law rights of set-off and/or abatement of legitimate cross-claims". Given that the words of sub-clause 2.5 were not clear enough, a notice was not required by the employer to raise counterclaims during the arbitration proceedings.

The contractor appealed against this decision (among other findings) of the arbitrator. The High Court and the Court of Appeal agreed with the decision made by the arbitrator in this regard.

However, the Privy Council overruled this decision. It found that the wording of sub-clause 2.5 is clear. If an employer wishes to raise claims, whether or not they are intended to be relied on as set-offs or counterclaims, those should not be allowed unless they have been the subject of a notice referred to in sub-clause 2.5. Moreover, this notice must have been given "as soon as practicable". If the employer could rely on claims which were notified well after that, no purpose would be served by the first two paragraphs of sub-clause 2.5. The Privy Council stated that "If an Employer's claim is allowed to be made late, there would not appear to be any method by which it could be determined, as the Engineer's function is linked to the particulars, which in turn must be contained in a notice, which in turn has to be served 'as soon as practicable'".

The Privy Council found that although the final sentence of sub-clause 2.5 limits the right of the employer to claim by way of set-off or to make any deduction from an amount certified in a Payment Certificate, the words "or to otherwise claim against the Contractor" extends this limitation beyond the claim against any Payment Certificate. In other words, to have a valid claim

for payment against a contractor, the employer must comply with provisions of sub-clause 2.5 by giving a notice to the contractor if it wishes to make a claim, such notice must be given as soon as practicable and the notice is to contain the particulars referred to this sub-clause.

The Privy Council also found that the provisions of sub-clause 2.5 apply to any claims which the employer wishes to raise. The clause makes it clear that if the employer wishes to raise a claim, it must do so promptly and in a particularised form (given the engineer's role to agree or determine the employer's entitlement by way of a sub-clause 3.5 determination). Moreover, the Privy Council found that if the employer has failed to give notice of a claim as required "the back door of set-off or cross-claims is as firmly shut to it as the front door of an originating claim". The employer's counterclaims, raised by way of set-off, were disallowed.

However, the Privy Council did concede that sub-clause 2.5 does not preclude the employer from raising a plea in abatement for example that no payment is justified to the contractor given that the work was so poorly carried out or that it was defectively carried out so that it is worth significantly less than the contractor is claiming.

An employer is therefore well advised to give notice of any claim, which it considers it may be entitled to, in writing to the contractor and as soon as practicable after it has become aware of the event or circumstance given rise to the claim. The notice is to contain sufficient particularity of the claim and shall specify the clause or other basis, including the substantiation of the amount to which the employer considers itself to be entitled to from the contractor. If the employer fails to comply with the notification requirements as set out in sub-clause 2.5, the back door to raising the claim at a later stage is firmly shut. It follows that the employer is not entitled to set-off or counterclaim against any amount owing to the contractor, unless a notice has been given to the contractor as provided for in sub-clause 2.5.

To the best of our knowledge, the interpretation of sub-clause 2.5 has not yet been pronounced on by an arbitral tribunal or a court in the Republic of South Africa. There is, however, little doubt that if an arbitral tribunal or court is faced with an argument by a contractor that an employer's claim should be disallowed for want of compliance with the provisions of sub-clause 2.5, the arbitral tribunal or court will have careful regard to the decision by the Privy Council referred to above.

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