

# Clause 17

## Summary

Although Clause 17 is titled ‘Risk and Responsibility’ it also sets out other provisions relating to indemnities, limitation of liability and, unusually, the specific topic of intellectual and industrial property rights. The clause provides that the Contractor assumes responsibility and bears the risk for the care of the works during execution and for remedying any defects during the Defects Notification Period. Risk transfers to the Employer on issue of the Taking-Over Certificate to the extent of works defined as being completed.

Generally, in construction contracts ‘risk’ is understood to mean an event or circumstance which causes delay, loss or damage to the Works. A risk can be said to be Employer caused, Contractor caused or neutral. The purpose of risk allocation is to determine which party bears the risk for such events. The Contractor may be required to remediate the damage at his own cost or the Employer may be required to pay for the damaged works. It has been stated that the “FIDIC standard forms are generally recognised as being well balanced because both parties bear parts of the risks arising from the project.”<sup>1</sup>

The structure of Clause 17 has been criticised as indemnities are dealt with before risk.<sup>2</sup> It has been suggested that Clause 17 ought to start with Sub-Clause 17.3 for the provision regarding risk and that Sub-Clause 17.1 for indemnities should follow after Sub-Clause 17.2. In respect of indemnities, the insurance provisions at Clause 18 closely relate to Clause 17 and should be considered together to ascertain the scope of indemnities for losses which are not covered by insurance (or otherwise non-recoverable). Further specific indemnity provisions are provided elsewhere in the contract which must be considered together with Clause 17. These are found at:

- Sub-Clause 1.13 [*Compliance with Laws*]
- Sub-Clause 4.2 [*Performance Security*]
- Sub-Clause 4.14 [*Avoidance of Interference*]
- Sub-Clause 4.16 [*Transport of Goods*]
- Sub-Clause 5.2 [*Objection to Nomination*]

**Risk allocation must be considered against the governing law of the contract. In civil law countries risk may be allocated by the applicable Civil Code, however, in common law**

---

<sup>1</sup> Dr. Götz-Sebastian Hök; *Risk allocation in the FIDIC Conditions of Contract (1999) for Construction (Red Book) and the FIDIC Conditions of Contract (1999) for EPC / Turnkey Projects (Silver Book) from the perspective of a German lawyer*

<sup>2</sup> Nael Bunni – Third edition – see at pages 530-531

countries the risk is allocated by the terms of the contract (express or implied), subject to

any statutory prohibitions.<sup>3</sup> Where the contract fails to set out who bears the risk of loss then the substantive law of the contract must be considered. Civil law courts are more likely than common law courts to interfere with the risk allocation, which may then disrupt or displace the agreed balance of risks.<sup>4</sup> The English courts tend to uphold the contractual agreed terms for allocation of rights and obligations.<sup>5</sup>

**A term will be implied if certain criteria are met in a common law system. In *BP Refinery (Westernport) Pty Ltd v Shire of Hastings*<sup>6</sup> the court stated that for a term to be implied "(1) it must be reasonable and equitable; (2) it must be necessary to give business efficacy to the contract, so that no term will be implied if the contract is effective without it; (3) it must be so obvious that 'it goes without saying' (4) it must be capable of clear expression; (5) it must not contradict any express term of the contract". This statement has been approved recently by the English Supreme Court and Privy Council.<sup>7</sup>**

## Origin of Clause

The Red Book 4<sup>th</sup> edn dealt with the topics of risk, responsibility, liability and indemnity for damage, loss and injury at Clauses 20, 21, 22, 24 and 65. The Red Book 4<sup>th</sup> edn followed the illogical sequence of ICE Form 5<sup>th</sup> Edition. Clauses 20, 22 and 24 allocate responsibility to the Contractor. Clause 21.3 deals with the Contractor's responsibility for losses not recovered by insurance. These clauses are interwoven with various Sub-Clauses providing terms for insurance requirements with the general insurance requirement at Clause 25.

The Red Book 4<sup>th</sup> edn provisions were re-organized within FIDIC 1999 so that terms for risk, responsibility and indemnity are predominantly found at Clause 17 which then leads to the separate insurance obligations for the indemnities in Clause 18. By segregating insurance topics under FIDIC 1999, it is simpler to use and understand.

The Employer's indemnity provisions at Sub-Clause 17.1 originated from Clause 20.1, 22.2 and 22.3 of the Red Book 4<sup>th</sup> edn. The Employer risks at Sub-Clause 17.3 were found at Clause 20.3 of the Red Book 4<sup>th</sup> edn.

---

<sup>3</sup> See, for example, the Unfair Contract Terms Act 1997 which prohibits certain exclusion clauses that seek to pass risk

<sup>4</sup> Axel-Volkmar Jaeger et al – see at Chapter 19, page 335

<sup>5</sup> *Trollope & Colls Ltd v North West Metropolitan Regional Hospital Board* [1973] 1 WLR 601, 609

<sup>6</sup> (1977) 180 CLR 266, 282-283

<sup>7</sup> See *Marks and Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd and another* [2015] UKSC 72 [15] and *A-G of Belize v Belize Telecom Ltd* [2009] UKPC 10 and *BDW Trading Ltd (t/a Barratt North London) v JM Rowe (Investments) Ltd* [2011] EWCA Civ 548

### **Cross-References**

Reference to Clause 17 is found in the following Sub-Clauses:

- Sub-Clause 18.2 [*Insurance for Works and Contractor's Equipment*]
- Sub-Clause 18.3 [*Insurance against Injury to Persons and Damage to Property*]

Reference to Risk which is construed as either a Contractor or Employer risk is found in the following Sub-Clauses:

- Sub-Clause 4.13 [*Rights of Way and Facilities*]
- Sub-Clause 4.19 [*Electricity, Water and Gas*]
- Sub-Clause 4.20 [*Employer's Equipment and Free-Issue Material*]
- Sub-Clause 8.6 [*Rate of Progress*]
- Sub-Clause 9.2 [*Delayed Tests*]
- Sub-Clause 11.2 [*Cost of Remedying Defects*]
- Sub-Clause 11.6 [*Further Tests*]
- Sub-Clause 15.2 [*Termination by the Employer*]
- Sub-Clause 18.2(d) [*Insurance for Works and Contractor's Equipment*]
- Sub-Clause 19.6 [*Optional Termination, Payment and Release*]

Reference to Responsibility which is construed as either a Contractor or Employer responsibility is found in the following Sub-Clauses

- Sub-Clause 3.1 [*Engineer's Duties and Authority*]
- Sub-Clause 4.6 [*Co-operation*]
- Sub-Clause 6.7 [*Health and Safety*]
- Sub-Clause 7.3 [*Inspection*]
- Sub-Clause 8.8 [*Suspension of Work*]
- Sub-Clause 10.2(b) [*Taking Over of Parts of the Works*]
- Sub-Clause 11.4(a) [*Failure to Remedy of Defects*]

Reference to “indemnify”, “indemnification” or “indemnified” which is expressed as either a Contractor or Employer obligation is found in the following Sub-Clauses:

- Sub-Clause 1.13(a) and (b) [*Compliance with Laws*]
- Sub-Clause 4.2 [*Performance Security*]
- Sub-Clause 4.14 [*Avoidance of Interference*]
- Sub-Clause 4.16 (c) [*Transport of Goods*]
- Sub-Clause 5.2 [*Objection to Nomination*]
- Sub-Clause 14.14 [*Cessation of Employer's Liability*]
- Sub-Clause 18.4 [*Insurance for Contractor's Personnel*]

Reference to “liable”, “liability” or “liabilities” is found in the following Sub-Clauses

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.

- Sub-Clause 1.14 [*Joint and Several Liability*]
- Sub-Clause 4.5 [*Assignment of Benefit of Subcontract*]
- Sub-Clause 4.20 [*Employer's Equipment and Free-Issue Material*]
- Sub-Clause 5.2(c) [*Objection to Nomination*]
- Sub-Clause 10.2(b) [*Taking Over of Parts of the Works*]
- Sub-Clause 11.6 [*Further Tests*]
- Sub-Clause 11.10 [*Unfulfilled Obligations*]
- Sub-Clause 14.14 [*Cessation of Employer's Liability*]
- Sub-Clause 18.1 [*General Requirements for Insurances*]
- Sub-Clause 18.2 [*Insurance for Works and Contractor's Equipment*]
- Sub-Clause 18.3 [*Insurance against Injury to Persons and Damage to Property*]
- Sub-Clause 18.4 [*Insurance for Contractor's Personnel*]
- Sub-Clause 19.6(b) and (c) [*Optional Termination, Payment and Release*]
- Sub-Clause 20.1 [*Contractor's Claims*]

### **Sub-Clause 17.1 Indemnities**

Under Sub-Clause 17.1 the responsibility of the risk for certain types of claims (summarised below) is allocated by way of indemnities so that each party indemnifies the other for the consequence of such claim.

- a) Personal injury
- b) Damage to personal or real property (other than the Works)
- c) Other specific matters for which the Employer indemnifies the Contractor

The Contractor is required to give a wide indemnity against “*all claims, damages, losses and expenses*” in respect of these types of damage. The indemnity would include legal fees. The indemnity is not subject to any exclusion of liability for loss of profit, loss of contract or other indirect losses under Sub-Clause 17.6.

The Contractor is obliged to indemnify not only the Employer but also the ‘*Employer's Personnel and respective agents*’. This covers any personnel who have been ‘notified’ to the Contractor by the Employer or Engineer and assistants delegated with authority by the Engineer pursuant to Sub-Clause 3.2 (see Sub-Clause 1.1.2.6). Visitors on site or any specialist advisors must be notified to the Contractor to ensure that the indemnity covers such persons.

Similarly, the Employer has the equivalent obligation to indemnify the Contractor and the ‘*Contractor's Personnel and their respective agents*’ in respect of *claims, damages, losses and expenses* for death and personal injury and specific matters which may be excluded from insurance cover. This captures any personnel ‘assisting’ with the works; however, the difference here is that there is no requirement to notify the Employer of such persons. The Employer indemnity will

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.

therefore capture those falling within the category.

This Sub-Clause has been developed from Clause 22 of Red Book 4<sup>th</sup> edn. Sub-Clause 17.1 introduces a new term ‘hold harmless’ to the indemnity obligation. Specifically, each party is required to give an “*indemnity and hold harmless*” the other party. Courts in different jurisdictions are likely to have different conclusions over the meaning and usage of ‘hold harmless’. It may introduce uncertainty. In the Scottish case of *Farstad Supply AS v Enviroco Ltd*<sup>8</sup>, the Supreme Court considered the meaning of these terms<sup>9</sup>. It was held:

*“the word ‘indemnity’ is capable of having a wide meaning but, even assuming that by itself it might (depending upon the context) have a narrow meaning, it does not stand alone in the clause. The owner must “defend ... and hold harmless” the charterer, not only against liabilities and causes of action, but also against “all claims, demands” and proceedings...*

*the obligation to hold harmless goes further than the obligation to reimburse because they are words of exception. In some contexts the words “indemnify” and “hold harmless” have the same meaning... The word “indemnify” can sometimes mean indemnify a third party. As ever, all will depend upon the context. Here the context is plain.*

*The expression “defend, indemnify and hold harmless” is wide enough to include the exclusion of liability for loss incurred by the owner or charterer...[and] is wide enough both to provide a defence for one party to claims made by the other party and to provide an indemnity in respect of the claims of third parties.*

The Ontario Superior Court of Justice in *Stewart Title Guarantee Company v. Zeppieri*<sup>10</sup> considered the same terms and held:

*“This language imposes two obligations on Stewart Title with respect to a member of the LSUC—to “indemnify” that member, and to “save harmless” that member from claims arising under a title insurance policy. The contractual obligation to save harmless, in my view, is broader than that of indemnification... the obligation to “save harmless” means that a LSUC member should never have to put his hand in his pocket in respect of a claim covered by the terms of the 2005 Indemnity Agreement.”<sup>11</sup>*

---

<sup>8</sup> [2010] UKSC 18

<sup>9</sup> The agreement provided that “*the owner shall defend, indemnify and hold harmless the charterer... from and against any and all claims, demands, liabilities, proceedings and causes of action resulting from loss or damage in relation to the vessel (including total loss) or property of the owner...irrespective of the cause of loss or damage including where such loss or damage is caused by, or contributed to, by the negligence of the charterer...*”

<sup>10</sup> [2009] O.J. No. 322

<sup>11</sup> See <http://www.adamsdrafting.com/2009/05/10/revisiting-indemnify-and-hold-harmless/> for case *Stewart Title*

This indicates that the indemnity obligation is to fully and completely indemnify a party. The interpretation of the indemnity provision is affected by the governing law of the contract.

### **The Extent of the Indemnity Provisions**

The indemnity provisions relate to:

a) *Personal Injury*

Both Contractor and Employer are responsible for claims relating to personal injury (bodily injury, sickness, disease or death). The indemnity obligation applies to personal injury caused to any persons which may include each Party's personnel. The insurance procured in accordance with Sub-Clause 18.3 will provide cover for this type of loss where personal injury is caused to persons other than the Contractor's Personnel and under Sub-Clause 18.4 where personal injury is caused to the Contractor's Personnel.

For losses not recoverable under a particular policy, the Contractor bears the risk by way of its indemnifying obligation for personal injury claims which may arise "*out of or in the course of or by reason of the Contractor's design (if any), execution and completion of the Works and the remedying of any defects*". The Contractor's indemnifying obligation is therefore limited to the Works as it is not drafted in the widest possible terms (such as 'howsoever caused').

- **The terms "*any person whatsoever*"**

The Contractor's indemnity obligation for personal injury relies on wide language and in particular extends to injury caused to '*any person whatsoever*'. The effect is that in addition to personal injury to the Employer's personnel and agents, personal injury to the Contractor's Personnel or agents, visitors and the public is also captured.

- **"*unless attributable to*"**

The Contractor's obligation to indemnify for personal injury losses is excluded where such losses are caused by the negligence, wilful act or breach of contract of the Employer (its personnel or agents). The use of the words by any 'negligence, wilful act or breach' illustrate that there must be a factual connection relating to the conduct (act or omission) of the Employer (its personnel or agent's) which causes the injury sustained so that the injuries are attributable to the Employer's fault.

The provision is silent on whether the personal injury must be attributable in whole to the Employer's negligence, wilful act or breach of contract or whether attribution in part would

---

*Guarantee Company v. Zeppieri* [2009] O.J. No. 322 (S.C.J.) Ontario Superior Court of Justice

suffice for the exclusion clause to apply. In *Central Asbestos Co. Ltd v Dodd*<sup>12</sup> Lord Pearson examined the meaning of "attributable to" in the context of 'attributable to that negligence, nuisance or breach of duty.' In contrast, under Sub-Clause 17.1 the words used are 'attributable to any negligence, nuisance or breach of duty'. Lord Pearson held that the words 'attributable to':

*“ refers to causation but it has to cover cases of dual or multiple causation and perhaps another element of responsibility in the case of contributory negligence... In such cases there would have to be an apportionment of the responsibility, and in the case of contributory negligence the apportionment would take into account degrees of blameworthiness as well as causative potency. If this involves another element additional to causation, it is aptly covered by the phrase 'attributable to' ... ”*

It is submitted that the position in England for use of the words “*if any*” has the meaning that the Contractor will be liable to provide the full indemnity less any apportionment for personal injury which is attributable to the fault of the Employer (its personnel or agents). The Contractor is not exempt from providing an indemnity where the Employer is less than 100% at fault for the resulting injury. The Contractor is obliged to provide an indemnity for resulting injury for the proportion not attributable to fault of the Employer (its personnel or agents).

Specifically, Sub-Clause 17.1 provides that the Contractor is responsible ‘*unless*’ the personal injury is due to Employer fault. The meaning and effect of the word ‘unless’ varies across different jurisdictions. In some jurisdictions the use of the word ‘unless’ will result in a total exclusion of Contractor indemnity where there is some negligence resting on the Employer irrespective of whether some (or most) fault is due to the Contractor. *Elis Baker et al* suggest<sup>13</sup> that where the governing law follows the total exclusion interpretation and where parties intend merely a narrow carve out from the Contractor’s indemnity obligation so that the Contractor remains liable to provide an indemnity where some fault does rest on the Contractor (i.e. by way of contributory negligence) then Sub-Clause 17.1 should be amended to add ‘*except to the extent that*’ in replacement of ‘unless’. This would then allow for the indemnity to be assessed according to proportionate liability of each party for the damage, loss or injury.

#### **- The Employer’s Indemnity Obligation**

The Employer’s indemnity obligation is narrow, specifically limiting the indemnity obligation to injury caused by the Employer (or its personnel or agents). However, it doubtful whether the Employer’s liability to third parties can be restricted by the contract where the issue is likely to be governed by local laws. Provided that the claim is not the fault of the Employer, the Contractor’s responsibility extends to all personal injury claims which arise and even to those claims arising without any act or negligence (see FIDIC Guide 1999). The result is that

---

<sup>12</sup> [1972] 3 W.L.R. 333

<sup>13</sup> *Elis Baker et al* see at page 361, paragraph 7.67.

the Contractor will be liable to indemnify the Employer for a third-party personal injury claim against the Employer which may exist in law even if there is no negligence, wilful act or breach of contract by the Employer (or its personnel and agents) or the Contractor. For example, injury sustained to an employee as a result of a defective product used in the construction (Product Liability claims).

**b) Damage to Property**

Similar to the indemnity obligation for personal injury claims, the Contractor is required to indemnify the Employer (and Employer's personnel and agents) for claims for loss or damage to real or personal property other than the Works. The corresponding insurance obligation is provided under Sub-Clause 18.3 [*Insurance Against Injury to Works and Property Damage*].

Similar to the personal injury indemnity obligation, the Contractor's indemnity obligation for property damage is also limited to such loss and damage arising during the course of the Works.<sup>14</sup> The difference here is that the caveat exists to limit the Contractor's indemnity obligation to Contractor faults. The Contractor will not be liable for such damage and loss unless 'to the extent' that it is attributable to any negligence, wilful act or breach of contract by the Contractor (its personnel and agents). This is a newly introduced restriction by way of Sub-Clause 17.1(b)(ii). Under Sub-Clause 22.1 of the Red Book 4<sup>th</sup> edn the Contractor's indemnity was based on his legal liability as a whole and was not limited. *Nael Bunni*<sup>15</sup> identifies that neither the Contractor nor the Employer benefits from this change and that insurers are the only beneficiary to provide cover for non-negligence to cover this gap. For a consistent Contractor's indemnity obligation for both property damage and personal injury then Sub-Clause 17.1(b)(i) should include the terms "*unless and to the extent that any such damage or loss is attributable to the negligence, wilful act or breach of contract by the Employer [its personnel and agents]*". This is adopted in FIDIC MDB Harmonised Edition 2010.<sup>16</sup>

The Contractor's indemnity obligation under Sub-Clause 17.1(b)(ii) is far reaching as it extends to loss or damage attributable to Contractor Personnel, their respective agents or "*anyone directly or indirectly employed by any of them*". These terms are not used elsewhere in FIDIC 1999. In contrast, the Employer's indemnity obligation is limited to the damage caused by its personnel and agents only. An indirect employee not captured within the definition of Contractor's Personnel is likely to include appointed professional advisors, material suppliers and manufacturers.

---

<sup>14</sup> Sub-Clause 17.1(b)(i) specifically provides "*out of or in the course of or by reason of the Contractor's design (if any), execution and completion of the Works and the remedying of any defects*"

<sup>15</sup> *Nael Bunni* – third Edition – see at page 532.

<sup>16</sup> See at Sub-Clause 17.1(b)

c) **The Employer's Indemnity - Specific Matters**

The Employer's obligation to indemnify extends only to the Contractor, its personnel and agents. The obligation relates only to:

(i) **Personal Injury**. The Employer's indemnity obligation for personal injury is explained above. It is important as it includes injury attributable by the Employer's Personnel, or any of their respective agents. Injury caused by the Engineer's design is therefore covered. It has undergone substantial re-drafting from its origin at Sub-Clause 22.2(d) the Red Book 4<sup>th</sup> edn, where there was an express provision to provide an indemnity to be apportioned between the Employer and Contractor according to the proportion of any contributory negligence.<sup>17</sup>

(ii) **Property**

The Employer gives an indemnity to the Contractor for third party property damage and thirdparty injury for certain claims which are allocated as Employer responsibility or risk. The wording of this indemnity is not as clear as it should be and can be interpreted in a number of ways.

*“the matters for which liability may be excluded from insurance cover, as described in sub-paragraphs (d)(i), (ii) and (iii) of Sub-Clause 18.3.”*

The intention of this wording appears to be that only where certain risks have been excluded from the insurance cover will the Employer's indemnity obligation arise. The use of the word 'may' recognises that insurance may be available for some of these risks on commercially reasonable terms. However, the use of the word “may” rather than “have” leads to some confusion. One could argue that if any insurance cover relevant to the events described in sub-paragraphs (d)(i), (ii) and (iii) of Sub-Clause 18.3 proved to be ineffective the indemnity obligation would then kick in. However, this is clearly not the intention.

Sub-Clause 18.3(d)(i), (ii) and (iii) list the matters which may be excluded from insurance cover. These are:

*“Liability to the extent that it arises from:*

- (i) *the Employer's right to have the Permanent Works executed on, over, under, in or through any land, and to occupy this land for the Permanent Works,*
- (ii) *damage which is an unavoidable result of the Contractor's obligations to execute the Works and remedy any defects.*

---

<sup>17</sup> See Sub-Clause 22.2(d) of the Red Book 4<sup>th</sup> edn...”*injury or damage was contributed to by the Contractor, his servants or agents, such part of the said injury or damage as may be just and equitable having regard to the extent of the responsibility of the Employer, his servants or agents or other contractors for the injury or damage”*

(iii) *a cause listed in Sub-Clause 17.3 [Employer Risks], except to the extent that cover is available at commercially reasonable terms.”*

Sub-Clause 18.3(d)(i) is similar to Sub-Clause 22.2(a) and (b) of the Red Book 4<sup>th</sup> edn. Sub-Clause 18.3(d)(ii) is similar to Sub-Clause 22.2(c) of the Red Book 4<sup>th</sup> edn. EC Corbett, FIDIC 4<sup>th</sup> A Practical Legal Guide, gives examples of the claims which could arise such as reduced property value caused by the construction activity or injunctions brought over boundary disputes which bring works to a halt.

A question arises as to whether the excluded matters must be read alongside the opening words of Sub-Clause 18.3, which refer to “any loss, damage, death or bodily injury which may occur to any physical property (except things insured under Sub-Clause 18.2 [*Insurance for Works and Contractor’s Equipment*]) or to any person (except persons insured under Sub-Clause 18.4 [*Insurance for Contractor’s Personnel*]), which may arise out of the Contractor’s performance of the Contract”? The words restrict the scope of the indemnity to third party losses. On balance we take the view that a restrictive interpretation ought to be placed on the Employer’s indemnity provisions.

“damage which is an unavoidable result of the Contractor’s obligations to execute the Works and remedy any defects.”

The FIDIC 1999 Guide states that this does not extend to any other damage which is a result of the particular arrangements and methods which the Contractor elected to adopt in order to perform his obligations. Here the Contractor would remain responsible for the risk and the Contractor should adopt appropriate arrangements and methods to minimise claims from third parties due to its performance of contractual obligations.

“a cause listed in Sub-Clause 17.3 [Employer Risks], except to the extent that cover is available at commercially reasonable terms.”

The Employer’s indemnity obligation is therefore for all third party<sup>18</sup> loss, damage, death or bodily injury arising from a cause listed in Sub-Clause 17.3, except to the extent that insurance cover is available at commercially reasonable terms. Sub-Clause 17.1 read together with Sub-Clause 17.3 and 18.3(d)(iii) shows that the Employer is generally allocated responsibility for Sub-Clause 17.3 matters where it is not insurable.

The FIDIC 1999 Guide does not define what constitutes ‘commercially reasonable’ although it mentions that it may be a matter of opinion given that the scope of cover required may have been clarified by early agreement of terms. The meaning of

---

<sup>18</sup> Those events which are not covered by Sub-Clause 18.2 or Sub-Clause 18.4.

commercially reasonable terms is likely to lead to conflict as it is an imprecise concept although the phrase “commercially reasonable” has recently been considered by the English courts.<sup>19</sup> In the Particular Conditions parties should define which risks are to be covered by indemnity. If insurance is available for a particular risk under Sub-Clause 17.3 on commercially reasonable terms which has not been effected then the Employer will not be liable to provide an indemnity if the Contractor is the insuring Party. Here the Contractor would then be in breach of its obligation to insure and would be liable for all or part of the resulting loss.

The FIDIC Guide recognizes that although the Sub-Clause 17.1 indemnities may apply widely they do not necessarily cover every type of claim and so there may be claims for which neither Party is entitled to an indemnity under this Sub-Clause.

### **Sub-Clause 17.2 Contractor’s Care of the Works**

This provision sets out the Contractor’s responsibility for the care of the Works. The clause originated from Sub-Clause 20.1 and 20.2 of the Red Book 4<sup>th</sup> edn. The Contractor assumes full responsibility for the “*care of*” the Works and Goods. The insurance requirement for these risks is set out at Sub-Clause 18.2. ‘Goods’ include items such as Contractor’s Equipment, Materials and Plant. Employer’s Equipment<sup>20</sup> does not fall within the definition of Works and Goods and so the Contractor does not assume responsibility for the Employer Equipment which is identified in the Specification. Also, the Contractor does not assume responsibility for Plant taken over by the Employer. The Contractor remains responsible for the acts or defaults of any Subcontractor or its agents and employees pursuant to Sub-Clause 4.4 [*Subcontractors*].

The Contractor’s responsibility runs from the Commencement Date (and the execution of the Works commence as soon as is reasonably practicable thereafter) and ends on issue or deemed issue of the Taking-Over Certificate for the Works, Section or part of the Works under Sub-Clause 10.1 and Sub-Clause 10.2 (as the Works are then completed).

The expression adopted by FIDIC for ‘*care of the Works*’ may lead to some misunderstanding across different jurisdictions. *Axel-Volkmar Jager et al*<sup>21</sup> refer to civil law jurisdictions where ‘care of the works’ is understood to mean the risk of accidental damage to the Works.<sup>22</sup> German Civil Code provides that the contractor bears the risk until the work is ‘accepted.’ In Civil Law countries it is considered that the risk for the care of the Works shifts to the Employer when the Engineer issues the Performance Certificate (and not on issue of the Taking-Over Certificate as provided in

---

<sup>19</sup> *Lehman Brothers Special Financing Inc v National Power Corporation & Anor* [2018] EWHC 487 and *Barclays Bank Plc v Unicredit Bank Ag & Anor* [2014] EWCA Civ 302

<sup>20</sup> See Sub-Clause 1.1.6.3 [*Employer’s Equipment*], 1.1.5.2 [*Goods*] and 1.1.5.1 [*Contractor’s Equipment*].

<sup>21</sup> Axel-Volkmar Jaeger, Gotz-Sebastian Hok “FIDIC – A Guide for Practitioners” at page 341

<sup>22</sup> A similar definition was also given in the English case of *Skanska Construction Ltd v Egger [Barony] Ltd* [2002] EWCA Civ 310 at [18]

the contract). French law is similar and where this applies, parties should understand that issue of the Taking-Over Certificate does not mean ‘acceptance of the works’. This is only achieved on issue of the Performance Certificate. Under Romanian law (Law 10/1995 and GD 273/1994) the Taking-Over Certificate is considered to have the effect of provisional acceptance.<sup>23</sup>

Sub-Clause 17.2 expressly provides that responsibility passes to the Employer when the “*Taking-Over Certificate is issued (or is deemed to be issued under Sub-Clause 10.1 [Taking Over of the Works and Sections])*”. Under Sub-Clause 10.1 the Engineer in issuing the Taking-Over Certificate will state the date that the Works or Section was completed. The Taking-Over Certificate may therefore record that the Works or Section was completed on an earlier date than the issue date of the Certificate. Given that under Sub-Clause 17.2 liability does not pass to the Employer until the issue date (or deemed issue date), the Contractor may, in certain circumstances, remain responsible for the Works for the gap between the actual taking over date and the date of issue of the relevant Taking-Over Certificate or deemed issue.

For insurance purposes it is the issue of the Taking-Over Certificate and not the date stated in the certificate which is relevant. The FIDIC 1999 Guide suggests that insurance to provide cover for the Employer risks for the Works should become effective by the date of issue of the Taking-Over Certificate.

It is important to clearly define what constitutes a Section (or part of the Works). The FIDIC 1999 Guide suggests that precise geographical definitions are set out in the tender documents for each Section or part of the Works as opposed to merely defining a Section by way of construction milestones.

### **Contractor Responsibility for Outstanding Works**

Following the issue of the Taking-Over Certificate (for Works, Section or part of the Works) the burden of care for the works remains on the Contractor for any outstanding minor works and defects to be carried out under Clause 11 [*Defects Liability*]. The Sub-Clause provides that “*the Contractor shall take responsibility for the care of any work which is outstanding on that date stated in the Taking-Over Certificate, until this outstanding work has been completed*”. Such outstanding works are then executed and completed by the Contractor during the Defects Notification Period (which commences on issue of the relevant Taking-Over Certificate). The Contractor remains responsible and therefore liable for loss and damage until the outstanding work is completed. This is when responsibility of the outstanding works then passes to the Employer.

---

<sup>23</sup> Axel-Volkmar Jaeger, Gotz-Sebastian Hok “FIDIC – A Guide for Practitioners” at page 329

### **Risk Allocation for Loss and Damage to the Works**

Before a Taking-Over Certificate is issued, or deemed Taking-Over occurs, the Contractor is responsible for the care of Works, Goods and Contractor's Documents. The Contractor will, however, not be liable for loss or damage caused by any event or circumstance which is expressly allocated to the Employer under Sub-Clause 17.3 [*Employer's Risks*] so far as they cause loss or damage to the Works (Sub-Clause 17.4 [*Consequences of Employer's Risks*]). The Contractor must, however, rectify the loss or damage if required by the Engineer.

If the loss or damage is caused by an event, other than one covered by Sub-Clause 17.3, then the Contractor is liable to rectify that loss and damage at his risk and cost.<sup>24</sup> It should be noted that the preceding provisions of Sub-Clause 17.2 do not refer to Contractor Documents. Specifically Sub-Clause 17.2 is silent on the Contractor's responsibility for the care of the Contractor's Documents. This obligation is found under Sub-Clause 1.8 [*Care and Supply of Documents*], which provides that the care of Contractor Documents does not pass to the Employer until they are taken over.

#### **Dominant Cause**

There is nothing within Sub-Clause 17.2 which deals with the situation where damage is caused by multiple events – one being a Contractor's risk and one being an Employer Risk. The Employer's liability is not expressed to be limited 'to the extent that' loss or damage is caused by an Employer risk, which would then allow for split liability between the parties. In practice a split liability will rarely occur unless it is an Employer risk falling within Sub-Clause 17.3 (f), (g) or (h).

#### **Loss and Damage after Taking-Over Certificate**

On the issue of a Taking-Over Certificate the responsibility for the care of the Works passes to the Employer (except for outstanding works and defects). However, Sub-Clause 17.2 confers liability on the Contractor after the issue of the Taking-Over Certificate for "any" loss and damage:

1. Caused by any actions performed by the Contractor after issue of the Taking-Over Certificate (and therefore actions carried out during the defects notification period).
2. Occurring after issue of the Taking-Over Certificate and which arose from a previous event for which the Contractor was liable (such as latent defects or poor workmanship).

This liability is consistent with the insurance obligation for Contractor risks at Sub-Clause 18.2 [*Insurance for Works and Contractor's Equipment*].

There is no express provision that the Contractor must rectify the loss or damage to the Works. The Employer, who has care of the Works at this stage, may execute such works itself or arrange for the works to be carried out by another contractor and recover such cost from the Contractor.

---

<sup>24</sup> Sub-Clause 17.2 specifically provides "*If any loss or damage happens... during the period when the Contractor is responsible for their care, from any cause not listed in Sub-Clause 17.3 [Employer Risks], the Contractor shall rectify the loss and damage at the Contractor's risk and cost...*"

### **Sub-Clause 17.3      Employer's Risks**

Sub-Clause 17.3 must be considered in conjunction with Sub-Clause 17.2. These two Sub-Clauses deal with risk allocation between the parties and liability for loss and damage. However, these are not the only clauses dealing with risk and regard must be had to Sub-Clauses 17.1, 8.4 and also the clauses specifically dealing with risk as identified above in the section “cross-reference”.

The Contractor is not responsible for the risks identified in Sub-Clause 17.3, so far as they result in loss and damage to the Works, Goods or Contractor's Document. Generally Sub-Clause 17.3 is an amalgamation of risks which the Contractor has no control over or, more usually, are beyond the control of both the Contractor and the Employer. They are risks which directly affect the execution of the work.

#### Overlap with Clause 19 [*Force Majeure*]

The four categories of force majeure events at Sub-Clause 19.1(d)(i) to (iv) are identical to the Employer Risks listed at Sub-Clause 17.3(a) to (d). There is therefore a complete overlap between these four provisions and these clauses should be read together. The FIDIC Guide mentions that Sub-Clause 17.3 (a) to (d) Employer Risks may constitute a force majeure event depending on the severity and adverse consequence of the risk event.

Sub-Clause 17.3 is relevant when an event has caused loss or damage to the Works, Goods or Contractor's Documents whereas Clause 19 is relevant where an exceptional event prevents performance of obligations and causes a delay. This distinction is important. The Contractor will have no right to claim additional time or Cost arising from a Sub-Clause 17.3 event except where it causes loss and damage to the Works, Goods or Contractor's Document. For example, if war occurs and the Contractor is prevented from carrying out the Works (but there is no damage to the Works), Sub-Clause 17.3 will not assist the Contractor. In order to recover time and cost the Contractor will have to rely on Clause 19.

Sub-Clause 17.3 risks may cause the Contractor delay or result in additional costs for the Contractor. Under Sub-Clause 17.4 the Employer bears the risk for rectifying loss and damage which occurred to the Works, Goods or Contractor Documents as a result of the Sub-Clause 17.3 risks. Pursuant to Sub-Clause 17.4 the Contractor may claim (following the Sub-Clause 20.1 procedure) for additional Cost to 'rectify' the loss or damage for Sub-Clause 17.3 risks. Similarly, under Sub-Clause 19.4 the Contractor can claim (under Sub-Clause 20.1) the 'additional Cost' for cost incurred as a result of *force majeure* events. The difference is that for a force majeure event all damages may be recovered from the Employer whereas under Sub-Clause 17.3 the Employer's liability to remunerate the Contractor is limited to repair of the Works to the extent that the Employer instructs repair.

The loss or damage which results such as personal injury or property damage is insurable.<sup>25</sup> The FIDIC Guide recognizes that the risks at Sub-Clause 17.3 are generally uninsurable on general insurance cover<sup>26</sup>. These risks are summarized below:

- a) War and act of foreign enemies
- b) Terrorism or civil war
- c) Riot and disorder (by persons other than the Contractor or Contractor's Personnel).
- d) Explosives and radioactivity
- e) Pressure waves caused by aircraft and other aerial devices

Sub-Clauses 17.3(c), (d) and (e) add the restriction of “*within the Country*”. This restriction is absent under the corresponding Clause 19 [*Force Majeure*] provision<sup>27</sup>. Terrorism or riots occurring in countries where the Works are not carried out could affect the progress of Works by the Contractor. It is possible that destruction or seizure of equipment or materials manufactured in other countries may occur during a civil war. It therefore seems that where such events arise outside the country then it will not fall within a risk at Sub-Clause 17.3(b). It may then be captured under the provision for *force majeure* at Clause 19 where the Contractor is prevented from performing its obligation as a result. However, where the Contractor is not prevented from performing its obligations (i.e. the Contractor obtains the equipment and materials from another country) but incurs cost as a result of the equipment or materials seized then the liability for the risk will rest with the Contractor – see for example the decision in *ICC Case No 20930/TO Partial Award*<sup>28</sup>, where the Tribunal held that disturbances caused by the Arab Spring did not necessarily constitute a force majeure event where the materials which had to be supplied were readily available from other countries.

As a result of changes to the global society some additions to FIDIC 1999 have been made since its predecessor at Clause 20.4 of Red Book 4<sup>th</sup> edn. Sub-Clause 17.3(b) now includes the event of terrorism. Under Sub-Clause 17.3(c) the restriction of “...and arising from the conduct of the Works” has been removed. The effect is that the Employer does not bear the risk for any riots, commotions or disorder which is attributable to the Contractor (or its personnel) and therefore the Contractor bears the risk for such events.<sup>29</sup>

---

<sup>25</sup> Nael Bunni – third edition – see at Page 531. These risks are identified as being insurable.

<sup>26</sup> See Ellis Baker et al ‘FIDIC Contracts Law and Practice’ at page 345 and footnote 13 which refers to the FIDIC Contract Guide (1<sup>st</sup> Edition, 2000).

<sup>27</sup> However, in order for a party to recover Cost the event must have occurred in the Country – Sub-Clause 19.4(b).

<sup>28</sup> Unreported

<sup>29</sup> see Clause 19 and the case of *Rumdel Cape v South Africa Roads Agency Soc Ltd* (234/2015) [2016] ZASCA 23 where this issue was considered in relation to a force majeure claim

The event of munitions of war and explosive materials is added to Sub-Clause 17.3(d) whilst the description for matters constituting contamination by radio-activity has been removed, widening this category, (see Clause 20.4(c) of Red Book 4<sup>th</sup> edn). Terms are also added at Sub-Clause 17.3(d) to exempt or restrict the Employer's liability for risks arising due to Contractor fault. The words used for the exemption are "...except as may be attributable to the Contractor's use of such [munitions, explosives, etc.]". This drafting is similar to that found at Sub-Clauses 17.1(a) and 17.1(b)(ii) where the provision is silent on whether the loss or damage to the Works (Goods or Contractor Documents) must be attributable in whole or in part to the Contractor's fault for the use of those materials.

The term 'may be' means 'might be' or 'could be' attributable to the Contractor. It is submitted that under English law the phrase "except as may be attributable" will exempt the Employer's liability for the proportion of the loss and damage which is attributable to the fault of the Contractor. The meaning and effect of this phrase is likely to differ across different jurisdictions. The terms "may be" could result in a total exclusion of Employer liability even in circumstances where the Contractor is less than 50% responsible for the loss and damage as a result of the Sub-Clause 17.3(d) risk. The position under the governing law of the contract must be considered especially where the parties do not intend a full exclusion interpretation for the Employer liability for this risk. Where parties intend to adopt the apportionment approach according to each party's proportion of liability, the terms should be amended to "except to the extent attributable" to avoid ambiguity and to recognize and apply split liability.

Sub-Clause 17.3(d) does not expressly exempt the Employer from liability where the loss and damage results from the Contractor's Personnel or its agents for the use of such materials. English courts are unlikely to construe this provision to include Contractor Personnel as some of the other provisions under Sub-Clause 17.3 expressly refer to "Personnel". Given that the 'Contractor' is defined as the person named as contractor in the letter of tender (see Sub-Clause 1.1.2.3) the Employer will then be liable for the Sub-Clause 17.3(d) risk where the loss and damage arises from personnel whom the Contractor utilizes on site such as staff, labour, other employees and other personnel assisting the Contractor and for each Subcontractor. It is unlikely that this is what FIDIC intended. Sub-Clause 17.3(d) should be amended to add 'Contractor Personnel' to the exception. Care is required for drafting in respect of Subcontractors which the Employer retains responsibility for. For such Subcontractors (where the Contractor has little or no responsibility) the Employer should retain liability for the risk.

The Employer Risks at Sub-Clause 17.3(f), (g) and (h), which are considered below, are not captured as a *force majeure* event under Clause 19 as they involve an element of party default.

**f) Use or occupation by the Employer of any part of the Permanent Works.**

This is relevant for loss and damage where the Contractor has retained responsibility for the care of the Works under Sub-Clause 17.2 either (i) prior to Taking-Over or (ii) for the

outstanding works and defects at post Taking-Over. This Employer risk will apply irrespective of whether the Employer's use or occupation of the permanent works is minor or temporary. This is a contentious point as disputes are likely to concern what constitutes use or occupation especially where the Employer has more than one contractor on Site. In contrast, under Sub-Clause 10.2 [*Taking Over of Part of the Works*] the Employer is permitted to use part of the Works as a temporary measure unless and until it is Taken-Over. Where the Employer uses a part of the Works for purposes other than a temporary measure then that part of the Works is deemed to have been Taken-Over (and therefore the Contractor responsibility and liability ceases).

- g) ***Design of any part of the Works by the Employer's Personnel or by others for whom the Employer is responsible.*** This Sub-Clause makes the Employer responsible for damage to the Works or the Goods caused by the design of the Works, which has been undertaken by the Employer's Personnel or others for whom he is responsible. The design must have caused the loss or damage to the Works or Goods. In most cases under a Red Book form of contract the Employer will have responsibility for the design of the works except to the extent specified in the Contract (see Sub-Clause 4.1). Problems may arise where it is unclear how the damage to the Works or Goods has been caused. Where there are concurrent causes then, similar to the Red Book 4<sup>th</sup> edn, each party is liable to the extent that their error in design (or workmanship) is causative of the loss.
- h) ***Any operation of the forces of nature which is Unforeseeable or against which an experienced contractor could not reasonably have been expected to have taken adequate preventative precautions.*** This Sub-Clause makes the Employer responsible for damage to the Works or Goods in two situations. First, where the damage is caused by the operation of the forces of nature which is Unforeseeable. Second, where the damage is caused by the operation of the forces of nature which an experienced contractor could not prevented by using adequate preventative precautions.

#### Unforeseeable Events

Sub-Clause 1.1.6.8 defines "Unforeseeable" to mean "not reasonably foreseeable by an experienced contractor by the date for submission of the Tender". The FIDIC Guide gives some guidance on whether a natural event of forces of nature is Unforeseeable. It is suggested that this could be determined by consideration of historic statistical records for the frequency of the occurrence of various events against the period of time to be taken to complete the works:

*“if the Time for Completion is three years, an experienced contractor might be expected to foresee an event which occurs (on average) once in every six years, but an event which*

*occurs only once in every ten years might be regarded as Unforeseeable.”*

EC Corbett refers to civil law and highlights that for exceptional and unforeseen events which render the Contractor’s obligation onerous resulting in excessive loss then under French law (*Théorie de l’imprévision*) such loss may be reduced by way of compensation by the Employer. This doctrine has wider application in Egypt as the Contractor is completely relieved of responsibility.

Where the Employer risk under Sub-Clause 17.1(h) (operation of forces of nature) falls within the risk at Sub-Clause 19.1(v) for natural catastrophes then it may still be treated as an Employer risk regardless of where it occurs in the world. The risk under Sub-Clause 17.1(h) is not limited to occurrence in the Country where the Site is located.

Foreseeable Events which an experienced contractor could not have taken adequate preventative precautions against

The Employer will also bear the risk for loss or damage to the Works or Goods in cases where the forces of nature were foreseeable but where it would not have been reasonable to expect an experienced contractor to take adequate preventative precautions. There will be many borderline cases. This risk is insurable under Sub-Clause 18.3(d).

The terms adopted of ‘experienced’, ‘could not reasonably’ and ‘adequate preventative precautions’ introduce ambiguity into the Contract. ‘...adequate preventative precautions’ is a new term. It has been included to place an express duty on the Contractor to mitigate any resulting loss.

#### **Sub-Clause 17.4      Consequences of Employer’s Risks**

Sub-Clause 17.4 sets out a procedure which the Contractor must follow when loss or damage is caused by one of the Employer risks listed at Sub-Clause 17.3.

##### Procedure - First Notice

Sub-Clause 17.4 provides for a two stage notice procedure which the Contractor must follow. For the first notice, the Contractor is required first to give ‘prompt’ notice to the Engineer in compliance with requirements under Sub-Clause 1.3[*Communications*] that loss and damage has been caused by a Sub-Clause 17.3 risk. Specifically the notice should (1) identify and define the Employer’s risk and (2) define the resulting loss or damage to the Works, Goods and/or Contractor’s Documents.<sup>30</sup>

---

<sup>30</sup> See FIDIC Guide 1999

The giving of ‘prompt’ notice is not defined although its natural meaning is that notice should be given without delay. Jackson J. in *Multiplex Construction v Honeywell Control Systems [2007]*<sup>31</sup> explains the reasons for giving prompt notice:

*“...serve a valuable purpose, such notice enables matters to be investigated while they are still current. Furthermore, such notice sometimes gives the employer the opportunity to withdraw instructions when the financial consequences become apparent”.*

The aim of giving prompt notice of an event under Sub-Clause 17.4 is to allow the finding of a prompt solution and to allow the Engineer to investigate the facts of any potential claim and the resulting financial outcome whilst the event is still recent, current and existing. Indirectly, prompt notice acts as a medium to notify the Engineer (and Employer) of any consequential foreseeable amendments to the Contract Sum.

English courts will construe the contract as a whole and are likely to treat the giving of notice ‘promptly’ as directory and not mandatory. The notice requirement under Sub-Clause 17.3 is not a condition precedent as there is no sanction attached to this provision if the Contractor fails to give ‘prompt’ notice – see *Aspen v Pectel [2008]*.<sup>32</sup> In *Aspen v Pectel* (which concerned notice requirements in an insurance policy) the Court held that giving ‘immediate notice’ meant “*with all reasonable speed considering the circumstances of the case.*” Similarly in *SHV Gas Supply and Trading SAS v Naftomar Shipping & Trading Co Ltd Inc*<sup>33</sup> the court decided that notice had to be given within a reasonable time after the occurrence to give notice has arisen. Here, time begins to run from when loss or damage occurs to the Works (Goods or Contractor Documents) as a result of a Sub-Clause 17.3 risk. It is an objective evaluation of the facts known to the Contractor to determine when the duty to provide such notice commences.

#### Engineer’s Instruction to Rectify

Having issued the notice, the Engineer may require the Contractor to rectify the loss or damage to the Works or Goods. It is noted that there is no express obligation placed on the Engineer to give an instruction to the Contractor either “*promptly*” or at all. If the Engineer does not issue an instruction then the Contractor ought to request an instruction under Sub-Clause 1.9. It should also be noted that the FIDIC Guide states that the Contractor may have an obligation to repair the Works under the applicable law or other contract provisions.

If the Engineer does give an instruction to the Contractor to rectify the loss or damage to the Works then the Contractor is required to comply with that instruction. In the event that the Contractor incurs delay or Cost it must then give notice of its claim under Sub-Clause 20.1.

---

<sup>31</sup> EWHC 447 (TCC), see paragraph 103

<sup>32</sup> [2008]EWHC 2804 (Comm)

<sup>33</sup>[2005] EWHC 2528 (Comm), see paragraph 37

#### Further Notice pursuant to Sub-Clause 20.1

Where the Contractor is instructed by the Engineer to rectify loss or damage to the Works or Goods caused by a Sub-Clause 17.3 risk and the Contractor suffers delay or incurs loss as a result of the rectification work then the Contractor is entitled to the type of remedy specified at Sub-Clause 17.4(a) and (b).

The reliefs expressed at Sub-Clause 17.4(a) and (b) are consistent with the reliefs which the Engineer has power to grant under Sub-Clause 20.1 in conjunction with Sub-Clause 3.5 namely an extension of time and payment of such Cost, respectively. The Sub-Clause 20.1 notice must be given “*as soon as practicable, and not later than 28 days...*” after the Contractor became aware (or should have become aware) of the event or circumstance. Sub-Clause 17.4 shows that the relevant ‘event or circumstance’ is the delay and/or additional cost suffered as a result of the instructed rectification work to the loss and damage caused by a Sub-Clause 17.3 risk event. When read in conjunction with Sub-Clause 20.1 the Contractor does not give notice unless the Contractor considers himself to be ‘*entitled*’ to claim for an extension of time or additional cost. The ‘entitlement’ to claim is not subject to the opinion of another (such as the Employer or Engineer).

Unlike the first notice, this 28 day requirement for giving the second notice is a condition precedent. There is a sanction attached which discharges the Employer from ‘*all liability in connection with the claim*’ and bars the contractor from its claim where the notice period is not complied with. This limitation provision is therefore expressed to extinguish the claim by failure to serve the notice within the prescribed time. The law governing the contract should be considered on this issue – see narrative of Clause 20. The notice should state that it is given under Sub-Clause 17.4 and Sub-Clause 20.1. The FIDIC Guide recommends that the further notice refers back to the earlier notice.

#### Claim for additional Cost

Although the Sub-Clause 17.3 Employer risks overlap (to some extent) with Clause 19 [*Force Majeure*] they have a specific purpose. Sub-Clause 19.4 deals with the Contractor’s prevention from performing and so an extension of time or additional cost may be granted whereas Sub-Clause 17.4 deals with loss or damage to the Works as a result of an Employer risk event under Sub-Clause 17.3 with the result that additional profit may be granted in specific circumstances.

The Employer’s liability is limited to compensate the Contractor for the payment of ‘Cost’ incurred from ‘rectifying’ the loss or damage (the rectification cost) which is attributable to any of the Sub-Clause 17.3 Employer risks. The Employer is not therefore wholly liable for ‘all’ the consequences of these risk events. The burden rests on the Contractor to prove that the loss or damage falls within the extent of the Employer’s liability.

Sub-Clause 1.1.4.3 defines Cost as follows:

*“means all expenditure reasonably incurred (or to be incurred) by the Contractor, whether on or off the Site, including overhead and similar charges, but does not include*

*profit.”*

Reasonable financing costs will be captured within the definition of Cost. The Contractor may need to borrow funds as a result of carrying out the rectification work. The Cost recoverable will only include costs attributable to the relevant event or circumstance and not those costs which are not attributable.

For the Employer risks at Sub-Clause 17.3(f) or (g) which relate to Employer default (Employer use of the Works and employer design issues) the Contractor is entitled to claim Cost plus additional ‘reasonable’ profit. FIDIC Guide 1999 explains that the reason for this is that the Employer is regarded as being directly responsible and at fault for these two risks. The Contractor is therefore entitled to recover reasonable profit where the Employer is in breach of contract. Where the Employer is not at fault, the risk is shared and the Contractor gives up any entitlement to profit. The parties may wish to specify the amount of profit recoverable. If so an amendment may be included at Sub-Clause 1.2 [*Interpretation*] to provide that “Cost plus reasonable profit means profit to be at [5%] of this Cost”. Under the MDB version the term ‘reasonable’ is deleted so that the Contractor is entitled to profit.

#### Claim for Extension of Time

The Contractor is entitled to claim for an extension of time for delay to complete whether completion has been delayed or will be delayed as a result of compliance with the instruction to carry out rectification works. The entitlement for relief relates only to rectification of the loss and damage. It does not relate to any other ‘incidental’ delay or loss incurred as a result of the Employer risk. However, the Contractor may still have an entitlement to claim an extension of time or payment for Cost for these ‘incidental’ claims under Sub-Clause 8.4 [*Extension of Time for Completion*] or Sub-Clause 19.4 [*Consequences of Force Majeure*].

### **Sub-Clause 17.5 Intellectual and Industrial Property Rights**

This Sub-Clause deals with Employer and Contractor respective responsibilities for “claims” arising out of “infringement” of intellectual property rights relating to the Works and the indemnity obligations for each Party against certain claims. Sub-Clause 17.5 is an expansion of Clause 28.1 of the Red Book 4<sup>th</sup> edn. The title of this Sub-Clause “Intellectual and Industrial Property Rights” has changed from its predecessor of “Patent Rights”.

Claims made by third parties is defined to mean either a claim alleging infringement of such intellectual or industrial property rights or which concern the proceedings pursuing such a claim. Under Sub-Clause 17.5 the term ‘other Party’ is usually (not always) used to describe the party who is entitled to an indemnity under this Sub-Clause.

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.

### Indemnities

Earlier editions of FIDIC provided for a Contractor indemnity obligation only. Clause 28.1 of the Red Book 4<sup>th</sup> edn introduced protection in favour of the Contractor to narrow the Contractor's indemnity obligation to the Employer for infringement of patent rights. Specifically, Clause 28.1 provided an express exclusion of claims (from the Contractor's indemnity obligation) where the infringement results from the Contractor's compliance with design or specification provided by the Engineer.<sup>34</sup> Sub-Clause 17.5 of FIDIC Red Book 1999 developed this further by introduction of an Employer indemnity obligation. There are separate indemnities for the Employer and the Contractor for claims made against a Party by a third party alleging infringement of their rights.

Unlike the indemnities provided under Sub-Clause 17.1, the indemnities under Sub-Clause 17.5 do not expressly provide for legal fees and expenses of the innocent party. The scope of the indemnity obligation under Sub-Clause 17.5 is also narrower than its predecessor. Under Clause 28.1 of the Red Book 4<sup>th</sup> edn the indemnity was for "...costs, charges and expenses whatsoever...", whereas under Sub-Clause 17.5 each Party's obligation is to indemnify and hold harmless the other Party "*against and from any claim*".<sup>35</sup>

The FIDIC Guide recommends each Party consider specialist legal advice for third party claims alleging infringement. There is a defined list of specific matters constituting an infringement or an alleged infringement as set out below. The items identified in bold text are also specifically referred to in the Red Book 4<sup>th</sup> edn. The other items are new additions in FIDIC 1999:

- **Patent**
  - Registered design
  - Copyright
  - **Trade mark**
  - **Trade name**
  - Trade secret
  - Other intellectual property right or other industrial property right '*relating to the Works*'.
- This sweep up provision also appeared under Clause 28.1 of the Red Book 4<sup>th</sup> edn, although it was expressed to limit the Contractor indemnity for items "*used for or in connection with or for the incorporation in the Works...*"

Sub-Clause 17.5 deals with many types of infringement; however, the FIDIC Guide recognizes that this Sub-Clause does not cover all types of infringement and for those claims neither party will be entitled to an indemnity under Sub-Clause 17.5.

### Employer's Indemnity Obligation

The Employer's indemnity obligation is for any claim alleging an infringement which was an unavoidable result of the Contractor executing the Works in compliance with the contract or as a

---

<sup>34</sup> Nael Bunni 'The FIDIC Forms of Contract' - see at page 144

<sup>35</sup> see commentary at Sub-Clause 17.1 which addresses use of the term 'hold harmless'

result of the Employer's improper use of the Works. The Employer's improper use is either:

- (1) for a purpose not provided in the Contract or *reasonably inferred* from the contract or
- (2) *in conjunction with any thing not supplied* by the Contractor (unless such use was disclosed to the Contractor in the Contract or prior to the Base Date).

#### Contractor Indemnity Obligation

The Contractor has a limited indemnity obligation to the Employer. The Contractor is required to indemnify the Employer for claims 'arising out of or in relation to':

1. *the manufacture, use, sale or import of any 'Goods'*. 'Goods' means the Contractor Equipment, Materials, Plant and Temporary Works used for execution and completion of the Works to include the remedy of defects (see Sub-Clause 1.1.5.2).
2. *"any design for which the Contractor is responsible"*. These terms confer a narrower indemnity obligation on the Contractor than in comparison to its predecessor. Under the Red Book 4<sup>th</sup> edn the risk remained with the Contractor unless if shown that the infringement resulted from the Contractor's compliance with the design provided by the Employer/Engineer. At Sub-Clause 17.5 the default position for responsibility and liability rests with the Employer unless it is proven that the infringement results from a design for which the Contractor is responsible.

#### Management of Claims

The Parties must co-operate where claims arise which are being contested by the indemnifying Party. The indemnifying party may conduct negotiations to settle the claim or deal with litigation or arbitration which may arise and against which it is liable to indemnify the other Party.

The other Party, including its Personnel, must assist in contesting the claim. The indemnifying Party is liable for the costs incurred by the other Party in assisting it to contest the claim. The other Party (and its Personnel) will be in breach of contract if they make any admission which might be 'prejudicial' to the indemnifying Party without the consent of the indemnifying Party. The exception to this is where the other Party requests the indemnifying Party to take over conduct of any negotiations, litigation or arbitration but the indemnifying Party fails to do so.

#### **Notice Provision and Waiver**

A Party receiving the claim must give notice to the other Party within 28 days of that claim. A Party failing to give notice of the claim is deemed to have waived 'any' right to an indemnity under Sub-Clause 17.5. The purpose of the sanction is to provide a strong incentive for the indemnifying Party to inform the other Party in good time so as to enhance the opportunity for the other Party to defend and assist in contesting the claim.

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.

There is no time limit on the indemnity obligations. For example, the obligation is not limited for infringements in existence at the date of agreement (such a restriction has been criticized previously as being unusual and unjustified) or to correspond to a time limit for contractors' liability for defects.

## **Sub-Clause 17.6      Limitation of Liability**

### Introduction and origin of the Sub-Clause

FIDIC has introduced a new Sub-Clause into all three 1999 Books which limits the parties' liability to each other in certain circumstances. The FIDIC Guide explains that the rationale for the Sub-Clause is to maintain a reasonable balance between differing objectives of the parties each of whom will wish to limit his liability whilst maintaining his right to full compensation in the event of default on the part of the other. As with most other forms of contract nowadays one of the purposes of the introduction of this Sub-Clause appears to be to assist the parties to appraise their risks at the contract negotiation stage. On a practical level it is presumably intended to enable the parties to identify and insure (so far as they can) their potential liabilities under the contract.

Previous incarnations of the Sub-Clause appear in the old Yellow Book (for E&M works) at Clause 4.2.1 and 4.2.2 and Clause 17.6 of the old Orange Book (for design-build and turnkey contracts), but it does not appear at all in the Red Book 4<sup>th</sup> edn.

### Explanation of and Function of the Sub-Clause

The Sub-Clause is in three parts; the first substantive part states that neither Party shall be liable to the other for certain types of loss, i.e.; loss of use of any Works, loss of profit, loss of any contract or for any indirect or consequential loss or damage which may be suffered by the other Party in connection with the Contract (other than under Sub-Clauses 16.4 and 17.1, i.e.; in the event of payment on termination and where indemnities are provided). These clauses will generally be upheld.<sup>36</sup> It should be noted that loss of Works, loss of profit and loss of contract may include both direct and consequential losses.

The second part goes on to limit the *Contractor's* liability to the Employer under or in connection with the Contract (save in four situations, namely where Sub-Clauses 4.19, 4.20, 17.1 and 17.5 apply) to the sum inserted in the Particular Conditions or, if that sum is not stated, to the Accepted Contract Amount. Note that the Accepted Contract Amount is defined in Sub-Clause 1.1.4.1 as the amount accepted in the Letter of Acceptance for the execution and completion of the Works and the remedying of any defects. There is no similar restriction on the Employer's liability to the Contractor.

---

<sup>36</sup> *Persimmon Homes Ltd v Over Arup & Partners* [2017] EWCA Civ 373

The way in which this part of the Sub-Clause operates will therefore be different for each party. One can see that where, for example, an Employer's notice of termination takes effect under Sub-Clause 15.2, following one of the Contractor defaults set out there, Sub-Clause 15.4 would allow the Employer to recover any losses and damages incurred by him and any extra costs of completing the Works, but Sub-Clause 17.6 is triggered to limit the Contractor's liability in this scenario. On the other hand, in the event that the Employer defaults and termination is effected by the Contractor under Sub-Clause 16.2, payment by the Employer to the Contractor will not be limited and the Contractor will, under the provisions of Sub-Clause 16.4, be entitled to loss of profit or other loss and damage sustained by him as a consequence of the termination. The provisions of the FIDIC 1999 Red Book do allow the Contractor to recover profit in addition to cost in the event of an Employer default but the text of the relevant clause should be carefully checked and profit is not in any event recoverable for events which are regarded as "neutral" i.e.; the fault of neither party.

The third and last part of the Sub-Clause speaks for itself. In the event of fraud, deliberate default or reckless misconduct by the party in default the Sub-Clause will not apply to limit its liability.

### **Direct and Indirect and Consequential Loss and Damage**

In the seminal case of *Hadley v Baxendale*<sup>37</sup> the English House of Lords stated:

*“Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such a breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e. according to the usual course of things, from such breach of contract itself, [The first limb] or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it. [The second limb]”*

Direct losses are therefore those losses which flow naturally from the breach of contract.

Indirect losses are those which may reasonably be supposed to have been in the contemplation of the parties, at the time they made the contract, as a probable result of the breach. The distinction is easy to demonstrate. In *Victoria Laundry (Windsor) Ltd v Newman Industries Ltd*<sup>38</sup> it was

---

<sup>37</sup> [1843-60] All ER Rep 461; (1854) 9 Exch 341, 354

<sup>38</sup> [1949] 2 KB 528

held that the direct losses arising from a five month delay to provide an industrial washing machine would include lost profits from contracts which the claimant would normally carry out as part of its business whereas the loss of a special contract for the army was an indirect loss, the losses of which would only be recoverable if the defendant was aware of the existence of that contract at the time it entered into the contract with the claimant.

It has been stated that the phrase ‘consequential loss’ is not very illuminating, as all damage is in a sense consequential: *per Atkinson J., Saint Line Ltd v Richardsons Westgarth & Co*<sup>39</sup>. Atkinson J. proceeded to state that an exemption clause referring to ‘consequential loss’ does not exclude direct losses; i.e. losses that flow naturally from the breach.<sup>40</sup> In the case of *British Sugar plc v Projects Ltd*<sup>41</sup> it was argued that loss of profits were consequential losses. The argument was advanced that to a reasonable businessman ‘consequential losses’ would include loss of profits. However, the Court of Appeal held that it was bound by authority and that loss of profits would usually be a direct loss and therefore not covered by the phrase ‘consequential loss.’ The Court of Appeal confirmed this in *Hotel Services Ltd v Hilton International (Hotels) Ltd*<sup>42</sup> and stated that loss of profits were a natural consequence of the faulty equipment “and therefore untouched by the exemption clause which (since all recoverable loss is literally consequential) plainly uses ‘consequential’ as a synonym for ‘indirect’.” Therefore, the traditional approach of the English courts has been to treat the words ‘consequential loss’ as being synonymous with ‘indirect loss’.

The traditional approach was questioned in *Caledonia North Sea v British Telecommunication*<sup>43</sup> and *Transocean Drilling v Providence Resources*.<sup>44</sup> Both Lord Hoffman and Moore-Bick LJ considered whether the traditional line of cases, which had considered the words ‘consequential loss’ to be synonymous with ‘indirect loss,’ would be decided in the same way now. In the recent case of *The Star Polaris*<sup>45</sup> the High Court had to consider an arbitrator’s award which concluded that the words ‘consequential or special losses’ had a wider meaning than simply being limited to indirect losses (i.e. the second limb of *Hadley v Baxendale*). The High Court considered two recent Supreme Court cases on contractual interpretation - *Chartbrook v Persimmon Homes*<sup>46</sup> and *Arnold v Britton*<sup>47</sup>. The High Court found that the exemption clause

---

<sup>39</sup> [1940] 2 KB 99

<sup>40</sup> See also *Croudace Construction Ltd v Cawoods Concrete Products Ltd* (1978) 87 BLR 20

<sup>41</sup> (1997) 87 BLR 42

<sup>42</sup> [1998] EWCA Civ 1822 [8]

<sup>43</sup> [2002] BLR 139 (HL)

<sup>44</sup> [2016] BLR 360 (CA)

<sup>45</sup> [2016] EWHC 2941

<sup>46</sup> [2009] 1 AC 1101

<sup>47</sup> [2015] AC 1619

had to be construed having regard to the parties' intentions and against the relevant factual matrix. The court concluded that despite the line of authorities supporting the traditional approach "the well-recognised meaning was not the intended meaning of the parties and that the line of authorities is therefore nothing to the point." The court therefore held:

*"...as in the judgment of the Arbitrators, 'consequential or special losses, damages or expenses' does not mean such losses, damages or expenses as fall within the second limb of Hadley v Baxendale but does have a wider meaning of financial losses caused by guaranteed defects, above and beyond the cost of replacement and repair of physical damage."*

The recent Supreme Court case of *Wood v Capita Insurance Services*<sup>48</sup> also supports the view that when construing a contract the court may find on the facts that the parties' objective intentions were to give the words 'consequential loss' a broader meaning than just simply 'indirect loss'. The court, when construing a contract, has to look at the contract as a whole. The court must analyse both the language of the contract (a textual analysis) and the factual background and implications of the rival constructions (a contextual analysis). As Lord Hodge stated:

*"The extent to which [textualism or contextualism] will assist the court in its task will vary according to the circumstances of the particular agreement or agreements. Some agreements may be successfully interpreted principally by textual analysis, for example because of their sophistication and complexity and because they have been negotiated and prepared with the assistance of skilled professionals. The correct interpretation of other contracts may be achieved by a greater emphasis on the factual matrix, for example because of their informality, brevity or the absence of skilled professional assistance. But negotiators of complex formal contracts may often not achieve a logical and coherent text because of, for example, the conflicting aims of the parties, failures of communication, differing drafting practices, or deadlines which require the parties to compromise in order to reach agreement. There may often therefore be provisions in a detailed professionally drawn contract which lack clarity and the lawyer or judge in interpreting such provisions may be particularly helped by considering the factual matrix and the purpose of similar provisions in contracts of the same type. ..."*

### Other Jurisdictions

In Australia there has been a significant departure from the approach taken by the English courts to the interpretation of the words 'consequential loss'. In *Environmental Systems Pty Ltd v Peerless Holdings Pty Ltd*<sup>49</sup> the court stated that consequential loss would include any loss which did not "naturally and ordinarily" flow from the breach of contract and therefore would include

---

<sup>48</sup> [2017] UKSC 24

<sup>49</sup> [2008] VSCA 26

loss of profits. This approach has been adopted and extended by other courts in Australia: see *Alstom Ltd v Yokogawa Australia Pty Ltd (No 7)*<sup>50</sup>. In the *Alstom* case it was held that an exemption clause prohibiting claims for consequential losses would include all types of loss except for claims for liquidated damages and damages associated with performance guarantee payments, which were expressly provided for in separate clauses of the contract.

The issue of what is covered by the phrase ‘consequential loss’ was recently considered again in *Regional Power Corporation v Pacific Hydro Group Two Pty Ltd*<sup>51</sup>. In this case the court held that the *Hadley v Baxendale* and the *Peerless* approach were both wrong. The court stated that the words in the exclusion clause had to be given their “natural and ordinary meaning, read in light of the contract as a whole.” In this case the court found that the losses which had been suffered were direct losses and not consequential losses and therefore were not covered by the exclusion clause.

The approach taken by some American courts also differs from the English approach. In *Jay Jala v DDG Construction*<sup>52</sup> the court followed a similar approach to that taken in the *Peerless* case. In this case the court stated:

*“Direct damages are the costs of getting what the contracting party was supposed to give – the costs of replacing [the Defendants] performance. Other costs that may not have been incurred [but for the breach of contract], but that are not part of what [the Claimant] was supposed to get from [the Defendant], are consequential or a secondary consequence.”*

Loss of profit or loss of income would therefore be classed as a consequential loss applying the principles in the *Jay Jala* case. In other countries it has been suggested that indirect losses are economic losses (i.e. non-physical) that are a consequence of a defect.<sup>53</sup>

### **Effectiveness of Exclusion Clauses under English Law**

Under English law an exclusion or limitation of liability clause will not apply in every circumstance. An exclusion clause that seeks to exclude all liability might be considered as ineffective.<sup>54</sup> In the case of *A. Turtle Offshore SA Assuranceforeningen Gard-Gjensidig v Superior Trading Inc*<sup>55</sup> the court considered the situation of an abandonment of the Works. The court stated that despite the wide wording of the exclusion clause there were some breaches of

---

<sup>50</sup> [2012] SASC 49

<sup>51</sup> [2013] WASC 356

<sup>52</sup> [2016] (US District Court of Pennsylvania)

<sup>53</sup> See [www.ibanet.org/Forum](http://www.ibanet.org/Forum) - Thread: FIDIC 17.6 Limitation of Liability

<sup>54</sup> However, see *Motortrak v. FCA Australia Pty Ltd* [2018] EWHC 990 (Comm) below where the court held that it would uphold the exclusion clause that severely limited a party’s remedies.

<sup>55</sup> [2008] EWHC 3034 (Admlty)

duty against which the exclusion clause cannot have been intended to provide protection.<sup>56</sup> The court referred to the opinion of Lord Wilberforce in *Suisse Atlantique*<sup>57</sup> where his lordship stated that there was a principle that a "total breach of the contract" disentitled a party to rely on exceptions clauses. In *A. Turtle Offshore* the court found that not all contracts must be construed literally. Teare J stated [110]:

*"[An exception clause] must, ex hypothesi, reflect the contemplation of the parties that a breach of contract, or what apart from the clause would be a breach of contract, may be committed, otherwise the clause would not be there; but the question remains open in any case whether there is a limit to the type of breach which they have in mind. One may safely say that the parties cannot, in a contract, have contemplated that the clause should have so wide an ambit as in effect to deprive one party's stipulations of all contractual force; to do so would be to reduce the contract to a mere declaration of intent. To this extent it may be correct to say that there is a rule of law against the application of an exceptions clause to a particular type of breach. But short of this it must be a question of contractual intention whether a particular breach is covered or not and the courts are entitled to insist, as they do, that the more radical the breach the clearer must the language be if it is to be covered."*

Teare J. then stated that despite this, a strained construction should not be placed on exclusion clauses where the words were clearly written.

In *Swiss Bank v Brink's Mat*<sup>58</sup> Bingham J. held at paragraph 93 that the words "under no liability whatsoever howsoever arising" were susceptible of one meaning only. However, he went on to find that despite this wide wording the words were not intended to apply where there was a wilful default.

In the recent case of *In Motortrak v. FCA Australia Pty Ltd*<sup>59</sup> the High Court considered an exclusion clause that was similar to that in Sub-Clause 17.6. The Contract was wrongfully rescinded by Employer. The Employer thereafter failed to pay the Supplier and the Supplier claimed that this failure was itself a repudiatory breach of contract. The Supplier therefore terminated the Contract and claimed, amongst other things, loss of profit against the Employer. The Employer argued that it had no liability for such losses because of the exclusion clause. The Supplier argued that the exclusion clause only applied where loss of profits arose in connection with the performance of the Contract and not where the Employer simply refused to perform the Contract. The Supplier argued that the Employer's interpretation of the exclusion clause would result in a breach of the Employer's obligations having no contractual remedy. Moulder J.

---

<sup>56</sup> *Ibid* at [99]; see also *The Cap Palos* [1921] P. 458. at p. 471-2

<sup>57</sup> [1967] 1 AC 361 at p. 432

<sup>58</sup> [1986] 2 Lloyd's Rep.79

<sup>59</sup> [2018] EWHC 990 (Comm)

rejected the Supplier's argument and therefore rejected the Supplier's claim for loss of profits. His lordship stated:

129. *"...although Motortrak on the defendant's construction, would be left without a claim for loss of profits, the clause does not preclude a claim for wasted costs arising out of the repudiation of the contract. It is a feature of Motortrak business that the revenue to be earned from this particular contract was largely, if not wholly, profits but there is no evidence that this was part of the factual matrix against which this agreement was concluded. Accordingly (adopting the approach of Carr J in Fujitsu) it cannot be said that FCAA's construction would deprive the contract of all contractual force.*

130. *The court has to balance the indications given by the literal interpretation of the words used and the provisions of the contract against the factual background and the implications of the rival constructions. In my view in this case there is nothing in the factual background or the contract as a whole to override the language used in subclause 9.5. The commercial consequences, whilst adverse to Motortrak are not in my view such as to have the effect that the court can find that the objective meaning of the language of subclause 9.5 is other than as it appears on its face. It is a clear exclusion in the context of a clause which taken as a whole appears to have been drafted with some precision from the perspective of Motortrak and in relation to subclause 9.5, to the mutual benefit of both parties. As stated in Wood the court has to be alive to the possibility that one side may have agreed to something which in hindsight did not serve his interest."*

## **Loss of Profit**

Under Sub-Clause 17.6 both direct and indirect loss of profit claims are excluded from liability. However, the Sub-Clause then provides exceptions to the exclusion clause; these are that the loss occurs under Sub-Clauses 16.4 or 17.1. Therefore, following a termination by the Contractor, the Contractor is entitled to claim loss of profit. The Contract does not provide the Employer with a similar exception in the event that it terminates the Contract under Sub-Clause 15.

## **Fraud, Deliberate Default and Reckless Misconduct**

### Fraud

There is no definition of "fraud" within the FIDIC contract. Fraud may encompass many different types of action, both criminal and civil. Under the criminal law in England, for example, fraud is committed under the Fraud Act 2006 where there is a fraudulent representation; a failure to disclose information when there is a legal duty to do so; or fraud by

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.

abuse of position. In each case a party's conduct must be dishonest and his/her intention must be to make a gain; or cause a loss or the risk of a loss to another.

There is no single cause of action for civil, or commercial, fraud. What may loosely be defined as 'fraud' is a set of heads of claim at common law and in equity. Each of these claims will have their own distinct elements which need to be pleaded and proved. Fentem and Walker provide some examples of 'fraud', which include: "claims in fraudulent misrepresentation or deceit, the economic torts of conspiracy and inducing breach of contract, bribery, certain breaches of fiduciary duty and claims founded on secondary liability for breach of trust in dishonest assistance and knowing receipt, as well as claims for wrongful or fraudulent trading and for transactions defrauding creditors made in the context of the Insolvency Act 1986."<sup>60</sup>

'Fraud' will be defined by the substantive law of the contract. Under some laws, where fraud is proven, a party may be entitled to punitive damages. The laws of the USA, India and the Philippines allow awards of punitive damages. Under English law a claim for punitive or exemplary damages is limited to a few cases and will not be successful for a breach of contract.<sup>61</sup> The laws of France, Germany, Japan, Korea, Taiwan and Switzerland do not permit claims for punitive damages. There is then the question of whether a DAB or an arbitrator is entitled to award punitive damages – see, for example, *Garrity v. Lyle Stuart, Inc* (353 N.E. 2nd 793 (N.Y. 1976)).<sup>62</sup> This again raises jurisdictional issues.

### **Deliberate Default**

The phrase 'deliberate default' has now been considered by the English courts on a number of occasions. In *Astra Zeneca UK Ltd v Albermarle International Corp and Another*,<sup>63</sup> the court had to consider whether or not the stoppage of a shipment was a deliberate breach of contract. Flaux J. found that the person involved had a mistaken view of the terms of the supply agreement and was therefore not entitled to act in the way that he did. He was in breach of contract. However, the judge went on to find that it was not a deliberate breach of contract because the individual was acting on the advice of US attorneys and had wrongly believed that he was entitled to do as he was doing.

In *De Beers UK Limited v Atos Origin IT Services*<sup>64</sup> the court held that deliberate default means "a default that is deliberate, in the sense that the person committing the relevant act knew that it

---

<sup>60</sup> [http://www.guildhallchambers.co.uk/files/Civil\\_Fraud\\_Back\\_to\\_basics\\_RossFentem&LucyWalker\\_November\\_2012.pdf](http://www.guildhallchambers.co.uk/files/Civil_Fraud_Back_to_basics_RossFentem&LucyWalker_November_2012.pdf)

<sup>61</sup> *Final Award in Case 6216* (2002) ICC International Court of Arbitration Bulletin Vol. 1. No. 2 at 58

<sup>62</sup> See further Werner J., *Punitive and Exemplary Damages in International Arbitration* (2006) Dossier of the ICC Institute of World Business Law: Evaluation of Damages in International Arbitration at page 101

<sup>63</sup> [2001] EWHC 1574 (Comm)

<sup>64</sup> [2010] EWHC (TCC) at [206]

was a default (i.e. in this case a breach of contract).” This has been recently confirmed by the High Court in *Mutual Energy Ltd vs Starr Underwriting Agents Ltd & Anor*<sup>65</sup> where Coulson J, as he then was, reviewed the authorities on the meaning of the phrase deliberate default. Coulson J held that:

*“There is plenty of authority to the effect that the use of the word 'deliberate', in the context of a 'breach' or 'default', means an intentional act; in other words, a breach or default which the relevant party knew at the time that it committed the relevant act was a breach or default. ...*

*[Counsel] expressly accepted that the "deliberate...breach" referred to in the proviso would require, not only a breach of contract or warranty on the part of MEL, but a breach which MEL knew, at the time of the relevant act or omission, was a breach of the term or warranty. Only then would the Insurers be entitled to avoid for deliberate breach. ...I find (for the same reasons) that a 'deliberate misrepresentation' must also involve the knowledge that what is being said or not said is a misrepresentation (and therefore a breach of duty).”*

## Reckless Misconduct

There is a difference between “wilful misconduct” and “reckless misconduct”. Willfulness means that a party intended to cause harm. Recklessness means the person knew or should have known that his action was likely to cause harm. Under English law “wilful misconduct” will include “reckless misconduct”<sup>66</sup>. However, it does not follow that the words “reckless misconduct” are broad enough to cover intent.

In *PK Airfinance SARL & Anor v Alpstream AG & Ors*<sup>67</sup> the court examined the phrase wilful misconduct. The court stated that this would include recklessness and would occur where a party was “*indifferent to whether their actions were right or wrong and as to whether loss would result.*” This has been often described as closing one’s eyes to an obvious risk (*R v Parker*<sup>68</sup>) or not caring what the results of one’s carelessness would be (*Forder v Great Western Railway Co*)<sup>69</sup>. In *De Beers UK Limited v Atos Origin IT Services*<sup>70</sup> the court expressed its opinion of recklessness in similar terms and stated that a party would be reckless where it acted “not caring whether or not he commits a breach of duty.”<sup>71</sup>

<sup>65</sup> [2016] EWHC 590 (TCC) at [28-29]

<sup>66</sup> *National Semiconductors (UK) Ltd v UPS Ltd* [1996] 2 Lloyd’s Law Rep. 212

<sup>67</sup> [2015] EWCA Civ 1318

<sup>68</sup> (1976) 63 CAS 211

<sup>69</sup> [1905] 2 KB 532

<sup>70</sup> [2010] EWHC (TCC) at [206]

<sup>71</sup> See also *National Semiconductors (UK) Ltd v UPS Ltd* [1996] 2 Lloyd’s Law Rep. 212 at 214 and the Court of

In *Standard Chartered Bank v Pakistan National Shipping Corp & Ors*<sup>72</sup> the court considered that where a party raised either intentional or reckless misconduct, as well as negligence, this might give rise to the defence of contributory negligence at common law.

Written by Liz Slattery and Nathalie Matharu-Khan  
Clause 17.6 written by Andrew Tweeddale  
Edited by Andrew Tweeddale

---

Appeal in *Lacey's Footwear (Wholesale) Ltd. v Bowler International Freight Ltd* [1997] 2 Lloyd's Law Rep. 369 at 374 per Beldam LJ

<sup>72</sup> [2000] EWCA Civ 230

The content of this commentary is not legal advice. You should always consult a suitably qualified lawyer regarding a particular legal issue or problem that you have. Please contact us if you require legal assistance.