Contractors’ exposure to delay damages under Qatari law

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Introduction

Of pressing concern to all contractors is the extent and duration of their liability in respect of the works they agree to perform. Parties to a construction contract will routinely agree to allow for the payment of liquidated damages (‘LDs’) by the Contractor in the event that he breaches certain of his contractual obligations thereunder. The Contractor derives some comfort from being able to estimate his potential exposure to the Employer in such circumstances (and to price the risk accordingly); for his part, the Employer benefits from having a mechanism to quickly recover pre-agreed amounts to compensate for losses flowing from such breach, without having to prove his actual damage in the context of costly and time-consuming formal legal proceedings. While liquidated damages are generally enforceable as a matter of Qatari law, this article will examine the scope for their imposition to be refuted in certain circumstances.

Furthermore, where the Employer is a state entity whose contracting activities come within the scope of Law No. 26 of 2005 (‘the Tender Law’) – as is almost invariably the case in relation to the most high-profile and valuable infrastructure projects currently being let in Qatar – we will also see that pre-agreement as to compensation in the form of an LDs clause might not be sufficient to limit a contractor’s exposure to the Employer in respect of delay.

The Mechanism in Practice

While liquidated damages clauses can be used to regulate various contractual breaches – such as the failure of a power station, constructed under a Design and Build, to meet specified target outputs for a particular period; or where agreed noise tolerances are exceeded in transport infrastructure contracts – they are most commonly used in the context of delayed completion of the whole works or, in a multi-phase project, to compensate for a contractor’s failure to achieve sectional completion milestones. Indeed, in the 1999 version of the FIDIC Red Book, the term “liquidated damages” was replaced with the more specific “delay damages”.

Delay damages are commonly calculated on the basis of a specific amount for each day that the Employer is deprived of the use of the works for their intended purpose – usually the period between the contractual completion date(s), (adjusted to take account of any Extension of Time granted), and actual handover. In practice this amount might equate to the daily cost of financing the contract price, together with an element of loss of profit. All of the FIDIC Books allow for an upper limit to be placed on the Contractor’s liability to compensate for delay – in practice, usually in the range of 5-15% of the value of the contract.

While many common law jurisdictions require that liquidated damages represent a genuine and reasonable pre-estimate of the Employer’s probable loss in the event of delay – or risk being construed as penalties and rendered unenforceable on that basis – Qatari law simply empowers the court (or tribunal) of competent jurisdiction to reduce the compensation payable to a level more reflective of the Employer’s actual loss in such circumstances.

The Qatari Law Context

1. General Principles under the Civil Code (Law No. 22 of 2004)

The general principle enunciated at Article 171 of the Civil Code is that of pacta sunt servanda, often referred to as 'freedom of contract'. As such, contracting parties can agree to structure their relationship on any terms which do not contravene the law, and will be bound accordingly. More specifically, pre-agreement as to the amount of compensation due for specified instances of breach – the purpose of a liquidated damages clause – is expressly permitted by Article 265 of the Civil Code: "if the subject matter of the obligation is not a sum of money, the contracting parties may agree in advance to the value of the compensation, whether in the contract or in a later agreement."

2. Challenging the Imposition of Liquidated Damages

(i) The Employer's Actual Loss is Non-Existent, or is Greatly Outweighed by the LDs

Liquidated Damages clauses, by their very nature, obviate the need for a creditor to prove his damage; instead, a debtor who breaches his obligations will be liable, upon default, to pay the prescribed amount of compensation. However, unlike many other jurisdictions, Qatari law provides for a contractor to wholly resist the imposition of delay damages where he can establish that the Employer suffered no damage whatsoever as a result of the delay; the law also grants the local courts (and by extension, a tribunal applying Qatari law) discretion to reduce the amount payable if it finds the agreed rate to be vastly disproportionate to the Employer's actual loss in the circumstances. The operative provision of the Civil Code in this context, Article 266, provides as follows:

"The agreed upon compensation shall not be due if the debtor proves that the creditor did not suffer any damage. The court may reduce the compensation from the one agreed upon if the debtor proves that the assessment was exaggerated to a high degree, or that the obligation has been partially performed. Any agreement to the contrary shall be null and void."

As a mandatory provision of Qatari law, Article 266 will prevail over any provision of the contract which purports to render LDs payable irrespective of the actual loss to the Employer.

It is noteworthy that where the amount of the LDs is insufficient to discharge the full loss occasioned to the Employer as a result of the Contractor's delay, there is no scope under Qatari law – absent the presence of 'deceit or gross mistake' – for a court or tribunal to intervene in order to increase the amount of damages payable by the Contractor in respect of such breach.

The foregoing interpretation of the provisions of Article 266 is consistent with reported case law emanating from the Qatari courts, including the decision of the Court of Cassation in Case No. 70 of 2006, and the more recent Court of Appeal Judgment in Joint Case Nos. 1612 of 2012 and 90 of 2013.

(ii) The Delay is Attributable to Extraneous Causes

A contractor who finds himself faced with payment of LDs, but without grounds to rely on Article 266, may look to more generally to other provisions of the Civil Code to support an argument that the delay was totally or partially caused by another party, and the Contractor's liability for any resultant losses to the Employer should be eliminated or proportionately reduced as a result.

Article 256 of the said law stipulates that "if a debtor does not perform the obligation specifically, or is delayed in its performance, he is obliged to compensate for the damage caused to the creditor, unless it is proved that the non-performance or the delay was for an extraneous cause for which the debtor is not responsible" (emphasis added).

Such 'extraneous cause' can take one or more of only three forms, as follows:

a) Force majeure, or an 'exceptional incident'

Circumstances of force majeure render the due performance of a contractual obligation impossible and result in its termination. ‘Exceptional incidents’ are those which fulfil the five criteria set out at Article 171(2) of the Civil Code – that is, are public; exceptional in nature; could not have been anticipated or reasonably foreseen; render the contractual obligation(s) onerous (though not necessarily impossible) to perform; and cause, or threaten to cause, great loss to the party burdened by performance.

b) Breach by the Employer – Concurrent Liability

Examples here would include the Employer’s failure to grant site access in good time, or to take over works which were completed in accordance with the requirements of the contract.

c) Mistake of a third party (such as a sub-contractor, or a party with no involvement in the contractual chain).

It is noteworthy that, unlike the prohibition on attempts to contract out of Article 266 (discussed above), parties can expressly agree assign to either one of them the risk of delay attributable to an ‘extraneous cause’.

3. Increased Exposure under the Tenders Law

The provisions of Law No. 26 of 2005 are stated to apply to the contracting activities of all Ministries, governmental bodies, public institutions and authorities in Qatar, with the exception of Qatar Petroleum and, in specified circumstances, the Armed Forces and the Police. In the event of delay, Article 56 of the said law permits a Government Employer to impose upon the Contractor, without advance warning, a penalty which does not exceed 10% of the contract value, in exchange for the granting of an extension of time to complete the works. This entitlement is expressly stated to be without prejudice to the Employer’s right to recover from the Contractor any compensation otherwise payable in relation to such delay.

The aforementioned Article 56 does provide for the Contractor to be exempted, by virtue of a Decision issued by the Minister of Finance, from payment of some or all of the specified fine, if it is established that he is not responsible for causing the delay and same did not cause the Employer to suffer any damage. However, this exemption is discretionary and, as such, even where a contractor working on a government-funded project is ultimately successful in refuting the imposition of LDs by relying on one of the grounds referred to above, he might first find himself subjected to an irrecoverable penalty equivalent to 10% of the total contract price.

Conclusion

While contractors might be comforted by the scope Qatari law offers to resist the imposition of liquidated damages in certain circumstances, those tendering for State-funded projects should be mindful of Employer’s legal entitlement to impose an additional penalty of up to 10% of the contract price in the event of delay, and should price accordingly.