


International Construction Contracts Under Swiss Law: An Introduction

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 International construction contracts; Switzerland

Introduction

Swiss law frequently applies to international construction contracts. It is concise and easily accessible, and is often chosen as “neutral” law to govern the main contract in a construction project and, more frequently, ancillary contracts—in particular, sub-contracts. In the absence of a choice of law, the Swiss conflict of law rules point to the law of the party that is providing the characteristic service—in other words, the construction contractor. In construction contracts, the provisions of Swiss law are normally completed by reference to standard contractual conditions: in international projects, these would, in particular, be the standard conditions issued by the Geneva-based International Federation of Consulting Engineers (*Federation internationale des ingenieurs conseils* (FIDIC)).

Legal framework and definition of construction contracts

The Code of Obligations is the principal source of Swiss contract law. The code is published in three languages (French, German and Italian), and both the law and its application by the courts take account of developments in neighbouring civil law countries. It is drafted in clear language as a key priority of the Swiss legislators was that it be comprehensible to the layman; this also facilitates understanding by foreign users. As a result, the Swiss law of contracts—despite some differences from other legal systems, especially in the common law world—is relatively easy to understand by users familiar with other systems and using other languages. There are many cases, especially in international arbitration, where the Swiss law of contracts is applied in English in proceedings with common law participation. Decisions in such proceedings

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are frequently published, creating a body of international case law on the Swiss law of contracts.

The Code of Obligations first sets out the rules applying to obligations and contracts in general; this section is followed by chapters on specific contractual relations. Chapter 11 (Arts 363–379 of the Code) concerns contracts for works. Article 363 of the Code defines this type of contract as “a contract whereby the contractor obliges himself to produce a work and the employer to pay compensation”. The chapter also contains some provisions which are specific to immovable works; such contracts for immovable works are referred to as construction contracts.

A contract for works must be distinguished from a contract for services, where the contractor must provide efforts of a defined standard but does not owe a specific result or work product.¹

While contracting practices and specific rules may vary, the provisions of the code apply without distinction to contracts for civil engineering work, mechanical and electrical work, process plant work, and so on, as well as to different forms of delivery (e.g. turn-key, multiple contracts, delivery and erection). The provisions of Arts 363 and following of the Code of Obligations also have universal application to the relationship between the employer and the contractor, and to that between the contractor and his sub-contractors.

However, a distinction must be made with respect to contracts with suppliers and other relationships governed by the law of sale, regulated in a separate chapter of the Code (Arts 184 and following). In international sales, for contracts which are subject to Swiss law, the United Nations Convention on Contracts for the International Sale of Goods applies. Care must be taken concerning the convention’s scope of application: its Art.3(1) provides that contracts for the supply of goods to be manufactured are regarded as sales, and hence subject to the convention, unless the buyer supplies a substantial part of the materials required for the manufacturing process, Contracts for the manufacture of machinery or equipment—and in some circumstances possibly also certain construction contracts—are therefore subject to the convention, unless materials for the manufacturing process are supplied by the buyer. Convention case law would suggest that a design provided by the buyer meets the condition for this exclusion; but a recent report of the convention’s advisory council criticised this approach and indicated that the convention does cover contracts if the buyer supplies only drawings or the design.²

Most building contracts, however, would seem to fall under the ambit of Art.3(2) of the Convention, which provides that the Convention does not apply if the preponderant part of the obligation of the party that furnishes the goods involves the supply of labour or other services. In practice, the distinction is not always easy to make, since international construction contracts are not limited to the performance of work on site, but include a multitude of other

¹ A leading work providing an introduction to these issues is by Pierre Tercier, now president of the ICC Court of International Arbitration, *Les contrats spéciaux*, 3rd edn (Zurich, 2003), No.3840, p.560.

² CISG Advisory Council Opinion No 4—Contracts for the Sale of Goods to Be Manufactured or Produced and Mixed Contracts, October 24, 2004 (posted at www.cisg.law.pace.edu/cisg/CISG-AC-op4.html). For a discussion see Christoph Brunner, *UN-Kaufrecht* (Berne, 2004), pp.28 and following.

obligations; manufactured goods often comprise a large part of the contractor's obligations. The question of whether it is the supply of labour and services which predominates or that of manufactured goods depends on the individual circumstances of the case. Such uncertainties may be avoided by clarifying the matter in the contract; since the Convention is not particularly suited to construction work, the neatest solution would appear to be the exclusion of its application to construction contracts.

Contracts concluded with engineers or architects may have different objects. If they are limited to the preparation of the design, the object is a product to be delivered and they are treated as contracts for works. However, if the object is to assist the employer in awarding the construction contract, and in directing and supervising its implementation, the contract is normally treated as a contract for services and thus may be terminated at any time. In many cases the contract involves a combination of both and is thus treated as a "mixed" contract, to which elements of both chapters of the Code of Obligations apply as appropriate.

In the Swiss legal tradition, engineers and architects are representatives of the employer and their powers are granted to them by the employer. Like most other civil law systems, Swiss law does not recognise the specific function of "certification", nor the role of the engineer or architect as a neutral administrator of the contract.³

Conclusion and interpretation of construction contract

Construction contracts, like most other contracts in Swiss law, are not subject to particular formal requirements (Art.11 of the Code of Obligations).⁴ In order for the contract to be valid, it is sufficient that the parties define the works to be supplied by the contractor and the compensation to be paid by the employer.⁵ In practice, construction contracts are invariably executed in writing. Parties frequently use model contracts and general conditions. In Swiss domestic contracts, the construction conditions prepared by the Swiss Society of Engineers and Architects (*Société suisse des ingénieurs et des architectes*) are widely used.⁶ In international construction projects, the most frequently used conditions of contract are the various sets of conditions issued by FIDIC, which are often modified as appropriate.⁷

General conditions or model contracts apply only when specifically agreed by the parties. In some respects, they might be considered to reflect industry practice. To that extent, the parties may be deemed to have accepted them tacitly.⁸ Under the International Chamber of Commerce (ICC) Rules of

³ Peter Gauch, *Le contrat d'entreprise* (Zurich, 1999), Nos 47–64, pp.15–21; Michael E. Schneider and Matthias Scherer, "Swiss Country Report", in R. Knutson, *FIDIC contracts* (Kluwer, 2005), pp.315 and 322; Tercier, loc. cit. No.3896, p.569.

⁴ Tercier, loc. cit. No.3978, p.582.

⁵ Tercier, loc. cit. Nos 3835–3839, p.559.

⁶ SIA Standard 118, for details see Gauch, loc. cit. No.265, p.85.

⁷ Other international conditions that can be found in particular in contracts for mechanical and electrical works are those of the United Nations Economic Commission for Europe (188 series) and of ORGALIME.

⁸ In Swiss Supreme Court Decision (SCD) 4C.261/2005 of December 9, 2005 the Swiss Supreme Court admitted that two companies active in the construction business were deemed to have tacitly accepted the SIA standards even though their contract did not provide for them specifically.

Arbitration, for instance, arbitral tribunals must take into account relevant trade practices (Art.17.2).

With regards to interpretation, the basic rule requires the arbitral tribunal or court to give effect to the parties' "true" and "common" intent. Both words are equally important, as it is not the subjective intent of a party which is decisive, but rather what the parties have agreed upon—their shared or common intent.

As in other civil law countries, the court or arbitrator must go beyond the literal meaning of the words used in a contract to determine what the specific parties in the specific circumstances intended by using those words. In doing so, the judge or arbitrator will normally start with the wording of the contract, but need not end there. In Swiss law, there is no prohibition against parol evidence. A Swiss judge will expect that in a dispute over the proper interpretation of a contract clause, the parties will rely on evidence outside the four corners of the contract (e.g. drafts of the disputed provisions, testimony of individuals involved in the negotiation and elaboration of the contract, evidence of the conduct of the parties during implementation of the contract and once the dispute arose). Parties to construction contracts are therefore well advised to retain relevant documentation for evidentiary purposes and to review post-execution correspondence carefully, as it may be taken as evidence of the parties' understanding of their contractual commitments.

There is no "clarity rule": even if a contractual clause appears clear at first glance, it may be subject to interpretation.⁹ However, the court will not depart from the literal meaning of the text adopted by the parties where there is no serious reason to believe that it does not coincide with their intent.¹⁰

In the event that the true and common intent of the parties cannot be established, or if it appears that there was no common intent, the court or arbitrator will determine how a statement or the conduct of a party could reasonably have been understood in good faith by the other party.

Arguably, it makes a difference whether Swiss law is used in a domestic context or in an international contract by parties unrelated to Switzerland.¹¹ Such situations arise primarily where the parties have chosen Swiss law as a "neutral" law without being familiar with its particularities. In such cases the law should not be applied strictly if this would lead to a result which none of the parties anticipated or, worse, which is contrary to the parties' common expectations. In other words, a party might argue that the real and shared intent of the parties differed from the solution under Swiss law if it were applied strictly as it might have to be applied by a Swiss court.

Contractor's obligations

The contractor must perform the works as specified in the contract and deliver them at the agreed time and free of defects. In addition, he has a number of ancillary obligations.

⁹ Supreme Court Decision 129 III 118 of October 14, 2004, c2.5.

¹⁰ Supreme Court Decision 4C.23/2005 of June 24, 2005.

¹¹ Gauch, No.1133 who advocates, as a supplementary interpretation method, that the arbitrator may consider the understanding of foreign parties which reflects their respective legal tradition. See also Supreme Court Decision of February 4, 2005, 4P.236/2004, English translation in ASA Bull 3/2005, 508,517.

Performance of the works

The contractor owes a concrete result: the works as defined in the contract. Where the design for the works is provided by the employer, as frequently occurs in building contracts, this definition of the works is normally contained in contract specifications and other documents which describe in detail the output that the contractor must deliver. In turn-key contracts, where the contractor also provides the design, the functions and parameters of the works must be defined, while the specification need not be as detailed as in contracts that include the employer's design.

While the work product which the contractor must deliver is defined in the contract, it is left to the contractor to decide what methods to use to achieve this result, as long as these are safe and suitable for the purpose. This notwithstanding, however, certain qualities of the works are normally defined by the method of construction or manufacture.¹²

Article 364(2) of the Code of Obligations provides that the contractor:

“is obliged to carry out the work personally or to have it carried out under his personal direction, except in cases where, due to the nature of the work, the personal qualities of the contractor are not important.”

This provision establishes the principle of personal performance of the works by the contractor; sub-contracting is the exception. Sub-contracting is permitted where the contractor has not been selected for his personal qualifications (which is rare in international construction contracts),¹³ or where the contractor directs and controls the sub-contractors as if they were his own employees. In most international construction contracts, performance by sub-contractors is subject to the express consent of the employer and lists of approved sub-contractors are included in many such contracts. In some cases the employer will nominate certain sub-contractors which he requires the contractor to use for the performance of certain works or for certain supplies.¹⁴

Except where sub-contractor guarantee and warranty obligations are assigned to the employer, as required under some main contracts, the employer normally has no direct contractual relationship with the sub-contractors. Contractors are responsible for their work as part of their own performance (Art.101 of the Code of Obligations). As in many other countries, however, Swiss law grants sub-contractors a statutory right, comparable to a mechanics' lien, allowing the unpaid sub-contractor to require the registration of a lien in his favour on the works for unpaid compensation under the sub-contract (Arts 837 and 839 of the Code of Obligations).¹⁵ Such liens on the works are considered a defect for which the contractor is liable.¹⁶ In view of this risk, employers can require proof from the contractor that payments to the sub-contractors are actually made or, under certain circumstances, may make direct payment to them.

¹² Tercier, loc cit. No.4000, p.585.

¹³ Tercier, loc cit. No.4007, p.586; Francois Chaix, in *Commentaire Romand, Code des Obligations I, Art 1-529* (Basel, 2003), Nos 18 and 20, Art.364, p.1880.

¹⁴ Chaix, loc cit. fn.13, Nos 24–25, Art.364, p.1881.

¹⁵ Tercier, loc cit. No 4008, p.586 and No.4384, p.634.

¹⁶ Supreme Court Decision, 104 II 348 of December 14, 1974, *Trajan v Beton Bau*.

Duty to inform

The contractor is presumed to be a specialist and thus expert in matters concerning the construction project. Therefore, he has a continuing obligation to advise the employer of all circumstances that are important in the performance of the contract (Arts 364 and 365 of the Code of Obligations). If the contractor fails to do so, he may be liable for damage that could otherwise have been avoided.

If the contractor believes, or could reasonably be expected to know, that a nominated sub-contractor is not in a position to perform the works required, the contractor must inform the employer clearly of this fact. Failing a clear reservation, the contractor might become liable to the employer.¹⁷

Delivery of the works

Once the contractor has completed the works, he must deliver them to the employer.¹⁸ In construction contracts, delivery takes place by notice of completion addressed to the employer or its representative.¹⁹ Delivery in the sense of Art.372(1) is the transfer from the contractor to the employer of all parts of the works completed in conformity with the contract. The presentation of final accounts may amount to delivery.²⁰

Completion under Swiss law corresponds to some extent to the term “substantial completion” as it is frequently used in international construction conditions: it does not require that the works be free from defects. The contractor’s liability for defects in principle arises only upon completion and delivery.

Delivery of the works by the contractor has other important effects, particularly with regards to responsibility for the works and the passing of risk, and as a starting point for the period of limitation. In addition, many contracts provide that some partial payment is due at the time the employer takes over the works.

Employer’s obligations

The employer’s principal obligation is payment of the contract price. The employer may also have a number of additional duties, the nature of which is subject to discussion.

Price and payment

The parties are free to agree on the price and the manner of determining it.

The parties can agree on a fixed price, either for the works as a whole (lump sum, Art.373 of the Code of Obligations) or on a per-unit basis.²¹ Occasionally, contracts also contain day work rates. Cost reimbursement contracts are rare.

¹⁷ Supreme Court Decision, 116 II 305 of June 6, 1990.

¹⁸ Supreme Court Decision, 115 II 456 of November 23, 1989.

¹⁹ Supreme Court Decision, 115 II 459.

²⁰ Supreme Court Decision, August 18, 2005, 4C.34/2005.

²¹ Tercier, loc. cit. Nos 4272 and 4277, pp.620 and 621.

