



Switzerland: The contractor's right to remedy defects

Matthias Scherer
LALIVE, Geneva

The owner's remedies in the case of alleged defects are a key issue in any construction contract. For instance, the conditions of contract (Red Book) issued by the International Federation of Consulting Engineers (FIDIC) provide that the contractor shall remedy defects. If the contractor fails to remedy the defects despite proper notice by the owner, the owner may carry out the work or engage others to do so (clause 11).

Swiss law, which is often selected as the governing law in international construction projects, notably in FIDIC contracts, provides for a similar statutory regime. Three decisions rendered by the Swiss Federal Supreme Court in 2006 clarify the scope of the owner's and the contractor's respective rights, in particular the contractor's right to perform remedial work.

Pursuant to Article 368 of the Swiss Code of Obligations and the relevant case law of the court, the owner is entitled to three distinct remedies in the event of defects in the contractor's works:

- if the defects are of such a serious nature that the owner cannot reasonably be expected to accept the works, the owner can refuse to do so and, where the contractor is at fault, the owner may claim damages;
- if the defects are minor, the owner is entitled to a proportionate reduction of the price or can request the contractor to remedy the works at its own cost, provided that such costs are not disproportionate – the owner may claim damages if the defects are the fault of the contractor; and
- if the contractor is incapable of remedying or unwilling to remedy the defects, the owner is entitled to ask a third party to perform the remedial works and to claim full compensation from the contractor. In certain circumstances, the owner is entitled

to ask the contractor to pay in advance the amounts that the owner will have to pay to the third-party contractor.

In a decision of 29 May 2006 (4C.91/2006), the Swiss Federal Supreme Court elaborated on the conditions that must be met before the owner can request a third party to remedy defects allegedly caused by the contractor. A municipality had awarded certain carpentry works to a contractor. During the performance of the works, the municipality complained about defects and refused to make the contractual progress payments. The contractor terminated the contract for lack of payment in accordance with the applicable contract conditions (Article 190 of *Société Suisse des Ingénieurs et Architectes Norm 118*).

The termination letter was qualified, in substance, as follows:

'We are ready to complete the works any time, and, as the case may be, improvements and remedial work taking into account mutually agreed prices. Please advise when we can meet to discuss the completion of the works, the improvements and prices.'

The owner merely replied stating that it accepted the termination but it did not allow the contractor to remedy the defects; nor did the owner agree to pay the contractor for the works already performed. The contractor brought an action against the owner seeking payment for the works. Eventually, the owner accepted that certain amounts were due to the contractor. It submitted, however, that the costs of remedial works that had to be performed by a new contractor should be offset against the amount due to the contractor.

The lower court denied the owner's right of set-off, finding it at fault in denying the contractor the opportunity to remedy the defects. It also found that the owner should have allowed the contractor to visit the construction site and to comment on the defects alleged in the owner's expert report. The contractor should have then been requested to remedy all defects that had been properly notified. The owner was not entitled to have such remedial works performed by a third party, unless it was obvious that the contractor was neither able, nor willing to perform them. Here, there was no evidence that the contractor was incapable of performing the remedial works. Moreover, it was perfectly admissible for the contractor to insist on a site visit to examine the alleged defects prior to offering to perform the remedial works.

The owner appealed the decision to the Swiss Supreme Court but to no avail. The Supreme Court fully upheld the lower court's decision. It also rejected the owner's additional arguments that the contractor's offer to remedy the defects came too late, since the owner had never notified the contractor of any time limit in the first place and that the contractor's offer to remedy was subject to undue conditions. Under Swiss law, the owner may ignore its obligation to give the contractor notice before awarding remedial works to a new contractor only if the contractor has clearly expressed its intention not to perform such works. In this instance, since there was no such clear expression in the contractor's termination letter, the owner should have invited the contractor to remedy the defects before requesting a new contractor to do so.

Accordingly, the Supreme Court held that the owner had wrongfully asked a third party to perform the remedial works and could not charge the contractor for the costs of such works.

However, in a decision handed down less than a month later (4C.79/2006, 22 June 2006) and involving similar (although not identical) facts, the Supreme Court decided in favour of the owner. The contractor argued that the owner had rejected its offer to remedy certain defects and had thus forfeited its right to have the contractor perform remedial works. The

Supreme Court (upholding the lower court's decision) held that since the contractor's offer had not been an unconditional and specific offer to remedy defects, but had been framed as a global solution, the owner, by rejecting the offer, had not forfeited its right later to insist on the contractor remedying the defects.

In conclusion, contractors confronted with an owner's defect notice are well advised to draft their reply carefully to ensure that the owner cannot order a third party to perform the works at the contractor's cost. Similarly, owners should draft proper defect notices and should grant the contractor an appropriate deadline and allow the contractor to inspect the allegedly defective works before retaining a new contractor to carry out the remedial works.

The statutory regime is not mandatory. The parties may agree that the only remedy available to the owner is to request the contractor to perform remedial work. If the contract includes language to this effect, the owner is not entitled to reduce the payment due to the contractor if the repair work is duly performed, as was shown in a Supreme Court decision of 25 July 2006 involving a Swiss owner and an Italian contractor (4C.77/2006).

Matthias Scherer is a partner at LALIVE in Geneva, Switzerland. This article originally appeared in the International Law Office Construction newsletter of 18 December 2006. Reproduced by permission.

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