

Construction under the Saudi civil code

Saudi Arabia's new Civil Transactions Law (CTL) fulfils its intended role of enhancing the conditions of doing business in the kingdom, says STUART JORDAN*, as he focuses on the construction sector.

LAST year we covered the enactment of the new Civil Transactions Law (CTL) in Saudi Arabia. It was announced in June and became effective on 16th December 2023. In that article, I had said that we would look at the new laws particularly relating to construction contracts, so here we go.

This important legislation is the first codification of transactions law in the kingdom. It is intended to provide increased certainty to contracting parties and, thereby, further incentivise businesses to establish in, and to invest in, the kingdom.

Construction contracts (Muqawala: contracts for work) are specifically covered in a section beginning at Article 461. Most of this is about implying basic terms in situations where the contract is not explicit. These include:

- The contractor is responsible for the provision of materials, plant and equipment, unless the contract provides otherwise;
- The contractor holds the risk of loss and damage to employer-provided materials;
- The contractor holds the risk of loss and damage to the works unless, at the time the loss or damage occurred, the employer should have taken them over but had failed to do so;
- The contractor must complete the works within a reasonable period, if no completion date has been agreed;
- The contractor may subcontract but remains responsible for those works.

These laws align to common construction contract terms but they are unlikely to be relevant to commercial parties working off industry standard contracts, which cover all these bases. Of more interest are the general principles on contracting.

As with the equivalent codified transactions laws in other Gulf states, we begin with a statement of the principle of freedom of contract, that is, that the law seeks

first to give effect to the parties' agreed terms, as showing in the contract. This is simple enough but the important questions have always been about the limits to that principle: by what rules do we interpret contracts? What contract terms contravene the law? In operating or forming contracts, what actions contravene the law? The general legal principles on this remain based in Shari'ah, notwithstanding they have been codified. Let's start with contract interpretation.

Article 104 requires that a contract shall be interpreted in accordance with its clear words. However, if those words are not entirely clear, then wider contextual factors (an established course of dealing between the parties, custom, the type of contract and other surrounding circumstances) are to be considered to establish the parties' intention.

Also familiar from pre-codified Saudi law and other Gulf State codes, is the overriding principle of 'good faith', which is applied in several Articles of the CTL. Article 95 requires that a contract is carried out in accordance with its terms and in a manner consistent with the principles of good faith.

When looking at good faith, we mostly examine whether a contract is in itself (that is, in its own terms) in compliance with the principle, or whether the parties are performing it in a manner consistent with good faith, including in terminating it. But the CTL also expressly applies the principle to pre-contract behaviour.

As I mentioned in the first article, a party who does not negotiate in good faith or who terminates negotiations in bad faith, may be liable in damages to the other party. Bad faith may include failure to engage

properly; for instance, failing to act seriously in the negotiations or failing to make substantial or influential statements. This is radically different from the common law approach that freedom to contract includes freedom to refuse to contract – for any reason or none; and that nothing is owed to prospective counterparties until the moment of commitment to the contract.

Good faith permeates other parts of the CTL, including Article 29 which requires that no right may be exercised wrongfully.

In describing what "wrongfully" means, the Article gives some helpful examples including where the exercise of a right will only cause harm to others or where that harm is wholly disproportionate to the benefit of exercising the right.

As always, we need to consider the position on liquidated damages. Parties are not prohibited (Article 178) from agreeing predetermined damages (for example, for delayed completion or

plant underperformance) but (Article 179) a Saudi court may revise those damages to reflect the actual loss suffered. However, there may be no increase from the predetermined damages unless the liable party committed fraud or gross error.

Termination is another hot topic in construction. We have looked before at the legality of termination for cause and for convenience – and doing so with or without the formality of a court order. CTL Articles 105-114 cover termination in various situations including for breach, by mutual agreement and for impossibility of performance. Among those grounds is (Article 106) the exercise of an option to cancel – but that might not exclude the case that the exercise of the option is wrongful, depending on the harm/benefit outcomes as above.

In Saudi Arabia, as in all jurisdictions, parties need clarity and predictability of outcomes. Whilst no codified laws or bodies of common law are perfect in providing that, the CTL fulfils its intended role as a real enhancement to the conditions of doing business in the kingdom. ■



CTL ... overriding principle of 'good faith'.

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