

9 LEGAL ASPECTS

This chapter describes some of the general legal aspects of concern to Supply, Service- and Works Contracts.

9.1 CONTRACTUAL DOCUMENTS

The different types of contracts are comprised of a series of documents including special conditions, General Terms and Conditions, Code of Conduct for Contractors, terms of reference, technical specifications and other relevant documents, which shall be listed in the clause "Order of Precedence of Contract Documents" in the contract. When doing so, documents shall generally be listed in the order from specific to more general. In case of later dispute about interpretation of contradicting provisions, the most specific obligation takes precedence over the general one.

Only the draft contract and different respective templates can be amended and filled in. Note that the text of the GTC and COC shall never be amended. However, that does not mean that there cannot be derogation(s) to some of their provisions. The GTC contains a list of rights and obligations which shall always apply in contracts, unless it is specifically indicated otherwise in the contract.

9.2 VALIDITY OF QUOTES, PROPOSALS OR TENDERS

When replying to a Tender Dossier, RFQ or RFP, the invited company binds itself for the duration of the validity period, which runs from the date of submission of its offer and for a specified number of days. Within the validity period, the Contracting Authority shall be able to convene the procurement committee, select, negotiate and interview the supplier or candidate and issue a purchase order or contract to the Contractor. During the validity period, the company is legally obliged to enter into contract with the Contracting Authority under the conditions of its quote, proposal or tender. If it is foreseen that a given Procurement Procedure is going to be particularly burdensome and there is a risk that an invited company, despite this legal obligation, withdraws its offer or refuses to enter into the contract, the option of a Tender Guarantee shall be retained when preparing the Tender Dossier. Please see section 9.3.

If it is foreseen that the evaluation process or the negotiations are taking more time than expected and the contract cannot be awarded within the validity period, the invited suppliers or candidates shall be requested to confirm in writing an extension of the validity of their quote, proposal or tender until a new specified date.

9.3 PREPAYMENT, TENDER AND PERFORMANCE GUARANTEES

Each set of documents includes the possibility of requesting a financial guarantee such as prepayment guarantee, tender guarantee and performance guarantee. These guarantees consist of a written declaration from a bank or an insurance company or another financial institution according to the national context. The institution guarantees that if the supplier or candidate fails to comply with its obligations to the Contracting Authority, the bank or insurance company will satisfy the Contracting Authority's claim for a certain financial amount.

The guarantees depend on the national context and can take the form of a bank guarantee, banker's draft, certified cheque or irrevocable letter of credit. Common for all guarantees shall be that they create an at-

first-demand obligation for the bank or guarantor. This means that the guarantor must pay as soon as requested in writing, without the Contracting Authority having to engage in a legal process. Therefore, when receiving a guarantee in a form other than the standard performance guarantee, a lawyer or the bank's trade finance department shall be consulted to ensure proper legal coverage.

Practices and costs in the project country shall guide the decision if such guarantees shall be required or may reasonably be obtained from contractors. If it is common that suppliers or candidates withdraw or change their offer in the validity period due to changes in the market price or availability, a Tender guarantee is a strong tool to prevent this.

These guarantees are payable 'on first demand' and comparable to cash money. It is therefore recommended that account references of the Contracting Authority are clearly specified in the guarantee to ensure that payment under the guarantee can only be made to that account. The guarantee shall be kept in a secure place and with a reference in the procurement file.

Advantages and Disadvantages of Using Guarantees

ADVANTAGES

When applying guarantees the Contracting Authority reduces the risk of suppliers or candidates withdrawing their offers in the validity period (tender guarantee). Moreover, they are committed to deliver the correct resources at the agreed time (performance guarantee). A tender guarantee will motivate suppliers or candidates to comply with the validity period, and it will reduce the participation of unreliable suppliers or candidates.

DISADVANTAGES

When applying a tender guarantee, some suppliers or candidates may decide not to submit an offer as they will not take the risk due to an unstable market.

Prepayment Guarantee

The prepayment guarantee assures compensation to the Contracting Authority for the prepayment lost if the Contractor is in breach of contract before completion. It is recommended that such a guarantee is requested when the contract provides for a substantial prepayment and circumstances might create uncertainties as to the future performance of the contractor. The guaranteed amount shall be for the full value of the prepayment.

In the prepayment guarantee it is stated that it will expire upon issue of an Acceptance Certificate (supplies) or, Completion Certificate (services) or Certificate of Final Completion (works). However, where the contract can be executed in successive deliveries or parts, it is possible to limit such duration. The guarantee shall then expire when the contractor has completed the part of the contract corresponding to the full value of the prepayment guarantee. A template for a prepayment guarantee is found in GEN 10-1.

Tender Guarantee

The tender guarantee assures compensation to the Contracting Authority for the time and money lost if the successful tenderer withdraws his/her offer or fails to enter into the contract. It is recommended that such a guarantee is requested for Open Tenders, or when the amount of the contract along with market conditions makes it relevant (e.g. high volatility of prices). The compensation is generally between one and two per cent of the total contract amount. The tender guarantee shall be released upon the end of the validity period, or the receipt by the Contracting Authority from the successful tenderer of the signed contract and the performance guarantee, if required, whichever date is the earliest. Therefore, if an extension of the validity period is requested, the tender guarantee shall also be extended. A template for a tender guarantee is found in GEN 10-2.

Performance Guarantee

The performance guarantee covers broadly all obligations of the contractor under the proper performance of the contract and is generally of an amount of ten per cent of the contract value. It is recommended that

such a guarantee is requested for all contracts above EUR 50,000. Depending on the context of the contract, a performance guarantee can also be requested for contracts of a lower value when risk of non-performance appears high. A template for a performance guarantee is found in GEN 10-3.

If no default by the contractor has occurred, the performance guarantee shall be terminated:

- upon expiration of the warranty period (Supply), and the guarantor will therefore likely ask for a clear determination of such a date. Please see relevant article of the GTC and the Purchase Order.
- upon completion of the contract (Service and Works). A Certificate of Final Completion may be required for works.

Guarantees shall be payable to the Contracting Authority “on first demand” in order to secure that funds are available without the Contracting Authority having to engage in a lengthy and costly legal process. The text in the guarantee shall be carefully checked to ensure that it has not been altered from the original text. If doubt exists on the credibility of the bank issuing the guarantee, the Contracting Authority’s own bank shall be requested to confirm the guarantee. By doing this the Contracting Authority’s bank vouches for the guarantee.

9.4 APPLICABLE LAW

The question of applicable law in international contracts raises some of the most complex legal issues which this Manual and the contracts cannot attempt to address in an exhaustive way. The standard contractual documents proposed in this Manual strive at removing the unpredictability in the supply/service/works relationship by providing a contractual framework setting out as far as possible the rights and obligations of the parties.

However, owing to the diversity of applicable laws and fundamental conceptual differences existing between the different systems of laws prevailing in the different countries of operation, it cannot be ensured that all provisions of the GTC can be found legally binding in any country, and that no mandatory rules of the country of execution of the contract will override the standard provisions. Since most legal systems recognise freedom of contract, it is nevertheless expected that, in case of dispute, a contractor will first refer to the provisions of the contract (GTC and other contractual documents), and that if he refers the case to a court, this court will recognise the validity of the contractual provisions.

The GTC for the three types of contracts provide that the law applicable to the contract (substantive law) is the law of the country of establishment of the Contracting Authority. However, it might be adequate to derogate to this clause and choose another applicable law depending on the circumstances of a given contract or project.

Generally, it might be relevant to apply law of the project country in the following cases: supplies bought and delivered in the project country; services performed by a contractor in the project country, and when Works Contracts are implemented by a contractor in a specific project country. When a given law in a project country is underdeveloped or subject to uncertainties, or the contract is concluded with a contractor established in another country, it can be better to designate a foreign law¹.

In case of a high value complex Works Contract, it is recommended that legal advice is sought before choosing the applicable law (see section 8.3).

¹ British law is frequently designated as the applicable law for Construction Contracts in South Asian countries. Whereas such countries generally have insufficient construction laws, British law is fairly well developed in the area of construction disputes. Using British law as the governing law is common in South Asia and comfortable to most people.

9.5 SETTLEMENT OF DISPUTES

This issue is closely connected to the question of applicable law, since it is of importance to avoid giving competence to the courts of a given country, when the law applicable to the contract is the law of another country, even though national courts generally recognise their ability to apply foreign laws. The GTC therefore provide that the courts of the country of establishment of the Contracting Authority are competent and that procedural law of that country is applicable to such litigation. For Works Contract, please see section 8.3. Consistency between the applicable law and settlement of disputes provisions shall be ensured if derogating to the GTC is considered.

The judicial system of some countries where projects are implemented may be unfit for such litigation due to backlogs, lack of capacity or corruption. In such cases, and if the contract in question is closely connected to that country e.g. contractor and execution in the project country, it shall be investigated whether there could be a more effective 'Alternative Dispute Resolution' mechanism, established by a Chamber of Commerce in the project country. For contracts with foreign companies, consider choosing the courts of their respective country. For contracts of high value, providing for a settlement through international arbitration shall also be considered e.g. for Works Contracts, see section 8.3.

When choosing courts of a country different from the country of establishment of the contractor, it shall be considered that even if a judgment in that first country can be obtained, enforcing it against the contractor in his/her country of establishment or where he has some assets shall be attempted. But the ability to enforce a judgment from one country to another country, depends on whether there is a treaty between the two countries which provides for enforcement of such judgments or on the willingness of the project country courts to enforce foreign judgments. Often such judgments are not warmly received.

Settlements of Disputes

Despite the high complexity of these legal issues, it shall be noted that an amicable settlement of disputes is always preferred, and it is highly improbable that the Contracting Authority will undertake a costly international litigation in case of a breach of a contract. If problems and disputes arise with a contractor, assistance from your own organisation's Procurement and Logistics Unit can be requested.

9.6 AUDITS

All donor funded projects are subject to immediate audit by donors. It is therefore important to keep the procurement files up to date at any given time. Please see chapter 5 for detailed information on documentation requirements.

The standard GTC of the three types of contracts provide for the Contracting Authority's right to check and audit all documents related to the contract and give the same right to the funding agency. Audits can also be added as a condition in the Purchase Order or Contract as a special clause.