

# PAYMENT PROCEDURES UNDER FIDIC CONSTRUCTION CONTRACT

KHALED HESHAM HYARI

*Dept of Civil Engineering, Faculty of Engineering, The Hashemite University, Zarqa, Jordan*

Payment provisions are of crucial importance to contractors. Owner's payments are the life blood of the contractor's work. Contractors and owners must understand the provisions governing all types of payments for a construction project. This paper presented an analysis of payment provisions under the FIDIC Conditions of Contract for Construction (2017 Redbook). FIDIC conditions of contract for Construction are widely used worldwide, especially in the middle eastern countries. The analysis includes: 1) Advance payment; 2) Interim payments; and 3) Final payment. The analysis reveals that FIDIC conditions of contract recognizes the importance of timely fulfilling of payment obligations of the owner and includes precise procedures and serious consequences for delayed payments. The contractor can take serious actions in response to delay in certifying payments or delay in receiving the certified payments, including suspending the work and/or terminating the contract after giving written notice to the owner regarding the intended action. Such notices should follow the stipulated time limit for each action depending on the type of delay. The analysis presented in this paper should prove to be useful to owners and contractors alike and can contribute to reducing disputes between the contracting parties.

*Keywords:* Progress payment, Advance payment, Final payment, Dispute, Payment certificate, Retention.

## 1 INTRODUCTION

Construction contract documents establish the rights and responsibilities of the contracting parties. FIDIC standard general conditions of contracting are an essential part of the construction contracts worldwide, including Middle Eastern countries (Shnookal and Charrett 2010). Shnookal and Charrett (2010) indicated that the most widely used construction contract worldwide is FIDIC construction contract. Construction practitioners need to understand the terms and provisions of the contract documents in order to manage their relationship with other parties in the construction project. This needed understanding is a challenging task to construction practitioners who in most cases lack the legal expertise. Each party should be aware of their rights and responsibilities as well as the rights and responsibilities of other contracting parties. Poor understanding of contract provisions and their practical interpretations and limitations can be a costly error as it may lead to a violation of contract that entitles the other contracting party to compensation. Payment provisions are of vital importance to contractors. These provisions play a major role in the performance of construction projects in addition to the profitability of the project because the financing cost of the project is significantly affected by these payment provisions as well as financial risks for both parties. Payment provisions affect the

submitted bid prices and the contractor's decision whether to bid or not to bid on a construction project.

Several scholars indicated that claims associated with payment issues represents a significant portion of construction claims (Ramachandra and Rotimi 2015, El-adaway *et al.* 2017). Many scholars investigated the impact of delayed payments on the performance of construction companies (El-adaway *et al.* 2017, Peters *et al.* 2019, Al Alawi 2021). Al Alawi (2021) indicated that delay in payments is one of the top factors that affect construction productivity and affects the financial stability of the contractor. Contractors are not supposed to finance the project. Delayed payments contribute to the unwarranted shift of the financing responsibilities of the owner to the contractor (El-adaway *et al.* 2017, Peters *et al.* 2019). Hyari (2017) considered that delayed payments are one of the top motivators for unbalanced bidding and indicated that some contractors increase the price of early performed construction activities and reduce the price of construction activities performed at the end of the project in order to get unduly higher payments from the owner at the beginning of the project (i.e., front end loading). This paper presents an analysis of payment procedures according to FIDIC general conditions of contracting for construction. The performed analysis includes advance payment; progress payments; and final payment. The analysis should be valuable to owners and contractors in understanding the contractual procedures for payment and is expected to help construction practitioners in managing their construction contracts wisely.

## 2 ADVANCE PAYMENT

Contractors in projects based on measurement contracts are usually responsible for paying for all work performed until the first progress payment is received from the owner. Also, starting a construction project entails considerable costs for mobilization. Once the construction started, the contractor needs to perform work until the performed work qualifies for measurement and submitting a request for progress payment. After that, the process of certifying the payment until actually receiving the payment usually takes several weeks. This process is lengthy and necessitates allocating considerable financial resources from the contractor's own money. Providing an advance payment is intended to be an interest free loan to the contractor to minimize financing costs of the project. Hyari (2017) indicated that the absence of such payment in contracts provides an incentive for price manipulations which carry additional risks to owners and contractors. Contractor's entitlement for an advance payment should be spelled out in the contract documents (usually appendix to tender). Similar to other types of payments, FIDIC provides a procedure for providing the advance payment to the contractor and the subsequent recovery of the payment by the owner. This procedure is outlined in the following steps as illustrated in Figure 1:

- 1) The Engineer checks that the amount of advance payment is stated in the appendix to tender. If no such amount is listed, the contractor is not entitled to receive an advance payment (C14.2).
- 2) The contractor submits statement and supporting documents to the Engineer (C14.3).
- 3) The Engineer checks that all preconditions are met by the Contractor.
- 4) The Engineer issues interim payment certificate for the advance payment or first installment. The certificate shall be issued within 28 days after receiving the Statement if all prerequisites are met. If the Engineer fails to certify, the contractor is entitled to suspend the work or even terminate the contract by the contractor (C14.3).
- 5) The Employer needs to make the advance payment (or first instalment) to the contractor within 42 days after issuing the Letter of Acceptance or within 21 days after receiving the

Performance Security (C4.2) and the advance payment guarantee (C14.2), whichever is later (C14.7). If the Owner fails to pay, the contractor is entitled to suspend the work or even terminate the contract by the contractor.

It is noteworthy that FIDIC procedure for advance payment recognizes the objective of providing advance payment and therefore involves a relatively speedy process for providing the payment to the contractor in comparison with other payments (interim and final payments).

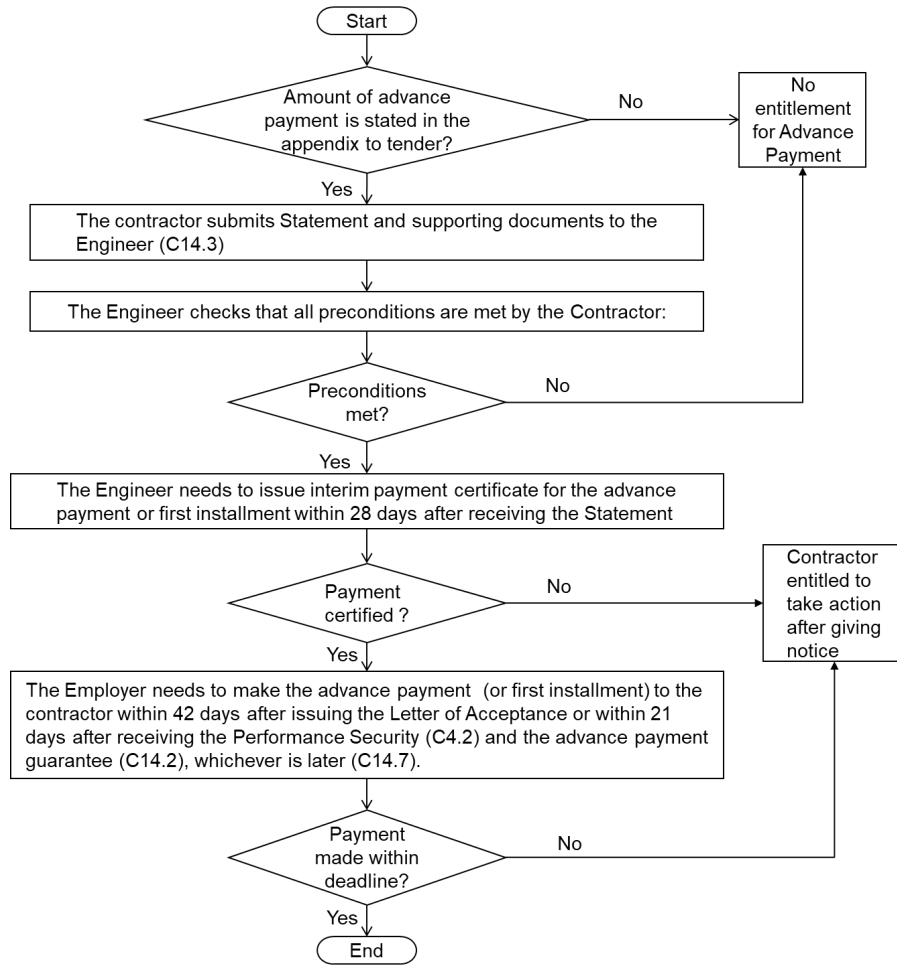


Figure 1. Advance payment procedure.

### 3 PROGRESS PAYMENTS

Progress payments are the life blood of the contractor's operations. Typically, measurement of actual work performed is the first step followed by applying for payment certificate. Actual payment follows the measurement and issuing the payment certificate. For example, owners are required to pay the contractor within 56 days from the contractor's submittal of application for payment certificate. Some contracts provide for a minimum amount of payment certificate so if the amount earned in a period is less than the specified minimum, the owner is not obligated to

pay and payment will be deferred to the next payment. As illustrated in Figure 2, the procedure for progress payment is outlined in the following steps:

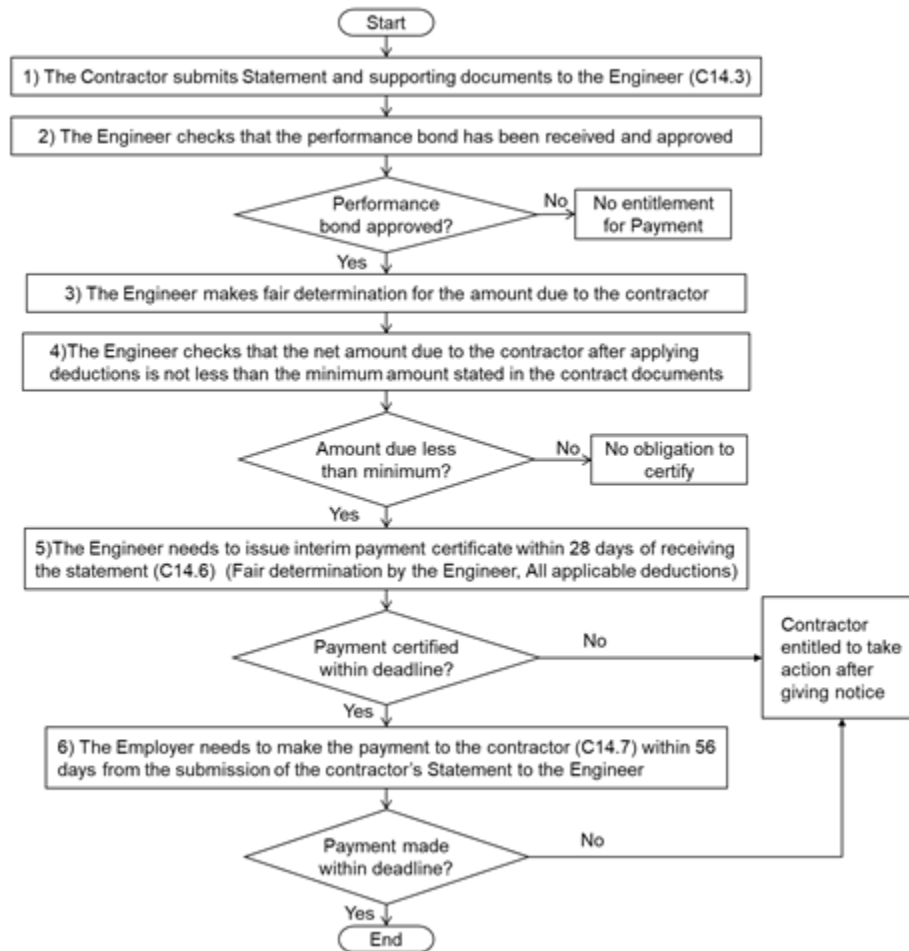


Figure 2. Progress payment procedure.

- 1) The Contractor submits statement and supporting documents to the Engineer (C14.3). Statements can be submitted monthly or according to the agreed upon payment schedule in the bidding documents.
- 2) The Engineer checks that prerequisites for certifying an interim payment are met by the contractor: a) the Owner has received and approved the performance bond (C14.6); and b) the Contractor has appointed the Contractor's representative and this appointment is approved by the Engineer (C4.3).
- 3) The Engineer makes fair determination of the amount due to the contractor (C14.6). This includes evaluation of completed work and involves applying all applicable deductions such as retention, repayment of advance payment, determined amount for Employer's claims. Also, the Engineer is entitled to evaluate all unperformed obligations by the Contractor and apply appropriate deductions. This includes the cost of replacing or

- fixing defective work/items. The Engineer is allowed in any payment certificate to make modifications to previous payment certificates.
- 4) The Engineer checks that the net amount due to the contractor after applying deductions is not less than the minimum amount stated in the contract documents if the contract specifies a minimum amount (C14.6). The contractor is not entitled for interim payment certificate if the amount due is less than the minimum amount specified in the contract documents, and the Engineer should notify the contractor. (This condition is not applicable after issuing the Taking-Over-Certificate).
  - 5) The Engineer is required to issue the Interim payment certificate (C14.6) within 28 days from receiving the statement and the supporting documents if the preconditions are met. FIDIC provisions stressed the necessity of certifying the payment as a precondition for making payment (No payment without certification). Furthermore, FIDIC provisions include serious consequences for delaying a deserved certificate or failing to certify. The contractor is entitled to send a notice for suspending the work after the deadline, and is entitled to send a notice of terminating the contract after 4 weeks from the expiry of the deadline.
  - 6) The Employer is required to make the payment to the contractor (C14.7) within 56 days from the contractor's submittal of statement and supporting documents. The employer's failure to comply with the payment deadline entitles the contractor to make serious acts. The contractor is entitled to send a notice for suspending the work after the deadline, and is entitled to send a notice of terminating the contract after 6 weeks from the expiry of the deadline. The Contractor is entitled also for financial charges (Interest on late payments). This entitlement for financial charges does not require prior notice from the contractor or certification and can be combined with other measures that might be taken by the contractor.

#### 4 FINAL PAYMENT

Processing final payment represents a significant milestone in the project closeout. Reaching an agreement with the contractor on the amount of final payment indicates that there are no disputable issues. FIDIC conditions include precise procedure for processing final payment that takes into account the possibility of having disagreement regarding the amount of final payment. The procedure for final payment involves the following steps:

- 1) The contractor receives the Performance Certificate.
- 2) The contractor is required to submit draft final statement to the Engineer (C14.11) within 56 days of receiving the Performance Certificate. If disagreement and dispute exist, the Engineer issues interim payment certificate for the agreed part in the draft statement. After resolving the dispute through dispute resolution mechanisms, the contractor submits final statement.
- 3) If the Contractor does not apply for final payment, the Engineer is required to ask the Contractor to submit the draft statement within 28 days. If the Contractor submits the statement, and an agreement reached, the Contractor will be required to submit the Final Statement. However, if the Contractor did not comply with the request, the Engineer will make fair determination and issue the Final Payment Certificate.
- 4) After agreeing on the Draft Statement, the contractor submits Final Statement (C14.11) and written Discharge (C14.12)
- 5) The Engineer is required to issue the Final payment certificate (C14.13) within 28 days from receiving the Final statement and the written Discharge. If the Engineer fails to

- certify within the deadline, the Contractor will be entitled for financial charges on the late certification.
- 6) The Employer is required to make the payment (certified amount) to the contractor (C14.7) within 56 days after the Employer receives the Final Payment Certificate from the Engineer. Employer's failure to comply with the deadline will entitle the Contractor for financial charges or interest on late payments (Cl.14.8).

## 5 CONCLUSIONS

This paper presented an analysis of payments' procedures according to FIDIC conditions of contracting for construction work. The analysis indicated that FIDIC conditions realizes the importance of timely fulfilling of payment obligations and their impact on the performance of construction projects. As such, precise time limits are established for certifying payments and actually making the payments to the contractor. The contractor is entitled for financing charges on delayed payment without the need to provide notice to the Engineer. This entitlement does not prejudice the right for more serious measures that includes suspending the work or even terminating the contract by the contractor. Suspending the work entitles the contractor to claim extra costs incurred plus reasonable profit and/or extension of time for completion. FIDIC conditions also entitle the contractor to take serious actions in response to delayed certification of payments by the engineer. These actions include suspending the work and/or terminating the contract upon giving certain time notices to the owner. Such provisions highlight the balanced perspective in drafting FIDIC conditions and the importance of balancing the interests of owners and contractors.

## References

- Al Alawi, M., *Delay in Payment Effects on Productivity of Small and Medium Construction Companies in Oman: Exploration and Ranking*, Asian Journal of Civil Engineering, 22, 1347–1359. <https://doi.org/10.1007/s42107-021-00387-8>, 2021.
- El-adaway, I., Fawzy, S., Burrell, H., and Akroush, N., *Studying Payment Provisions under National and International Standard Forms of Contracts*, Journal of Legal Affairs and Dispute Resolution in Engineering and Construction, 9(2), [https://doi.org/10.1061/\(ASCE\)LA.1943-4170.0000200](https://doi.org/10.1061/(ASCE)LA.1943-4170.0000200), 2017.
- Hyari, K., *Owner's Countermeasures to Skewed Bidding in Construction Projects: Review of Current Practices and Proposal for New Countermeasures*, Journal of Management in Engineering, 33(3), doi:10.1061/(ASCE)ME.1943-5479.0000502, 2017.
- Peters, E., Subar, K., and Martin, H., *Late Payment and Nonpayment within the Construction Industry: Causes, Effects, and Solutions*, Journal of Legal Affairs and Dispute Resolution in Engineering and Construction, 11(3), [https://doi.org/10.1061/\(ASCE\)LA.1943-4170.0000314](https://doi.org/10.1061/(ASCE)LA.1943-4170.0000314), 2019.
- Ramachandra, T., and Rotimi, J., *Mitigating Payment Problems in the Construction Industry Through Analysis of Construction Payment Disputes*, Journal of Legal Affairs and Dispute Resolution in Engineering and Construction, 7(1), [https://doi.org/10.1061/\(ASCE\)LA.1943-4170.0000156](https://doi.org/10.1061/(ASCE)LA.1943-4170.0000156), 2015.
- Shnookal, T., and Charrett, D., *Standard Form Contracting: The Role for FIDIC Contracts Domestically and Internationally*, Proceedings of the Society of Construction Law Australia, Perth, June 19, 2010.