

# **M**ain Contractual Issues

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**Sezione  
Componentistica  
di Impianto**



**Associazione Nazionale di  
Impiantistica Industriale**

**Autore:** Nicolaj Diulghe  
**Titolo:** L'uomo razionale, 1928

# Indice

-> Note esplicative e ringraziamenti	<i>Pag. 2</i>	7) Exclusivity of Remedies	<i>Pag. 21</i>
-> Note introduttive	<i>Pag. 3</i>	8) Applicable Law and Dispute Resolution	<i>Pag. 22 / 25</i>
-> Introduction	<i>Pag. 4</i>	9) Order Suspensions	<i>Pag. 26 / 27</i>
1) Contract stipulation and document discrepancies	<i>Pag. 5 / 7</i>	10) Temporary Storage and relevant Costs/Liabilities	<i>Pag. 28 / 30</i>
2) Warranties Liabilities, Corrective Actions and Indemnities	<i>Pag. 8 / 11</i>	11) Force Majeure	<i>Pag. 31 / 33</i>
3) Direct and Indirect Damages, Consequential Damages/Losses	<i>Pag. 12 / 13</i>	12) Payments, Credit Issues, Assignments	<i>Pag. 34 / 38</i>
4) Compliance with Laws and Regulations	<i>Pag. 14 / 15</i>	13) Intellectual Property and related issues	<i>Pag. 39</i>
5) Delivery, Risk and Title Transfer, LDs for late delivery	<i>Pag. 16 / 18</i>	14) Order Changes	<i>Pag. 40</i>
6) Termination for Default and/ or Convenience	<i>Pag. 19 / 20</i>	15) Insurance	<i>Pag. 41</i>

Il presente testo divulgativo è stato elaborato in ambito ANIMP – Sezione Componentistica di Impianto

In qualità di Membri del Comitato Direttivo della Sezione Componentistica di ANIMP, hanno aderito all’iniziativa promossa dal Delegato di Sezione Ing. Marco Pepori e sostenuta dall’Ing. Maurizio Gatti:

●	Alstom Power Italia	●	Ing. Riccardo Pozzi
●	Emerson Process Management	●	Ing. Francesco Bianchi
●	Flowserve Worthington	●	Ing. Marco Pepori
●	Foster Wheeler Italiana	●	Ing. Nicoletta Manzini
●	Maire Tecnimont	●	Ing. Vincenza Panighini/Ing. Mauro Zucchetti
●	Saipem	●	Ing. Renato Di Loreto
●	Technip Italy	●	Ing. Giovanni Del Serrone
●	Tenaris Dalmine	●	Avv. Guido Maglionico

Hanno collaborato alla stesura di questo testo:

●	Alstom Power Italia	●	Avv. Marco Migliavacca
●	Flowserve Worthington	●	Ing. Federico Fella
●	Foster Wheeler Italiana	●	Avv. Patrizia Tanzola
●	Maire Tecnimont	●	Avv. Laura Furlanetto
●	Saipem	●	D.ssa Isiré De Risi
●	Technip Italy	●	Dr. Achille De Nino
●	Tenaris Dalmine	●	Avv. Guido Maglionico

Coordinatore dei lavori:

●	Tenaris Dalmine	●	Avv. Guido Maglionico
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*Il Delegato della Sezione Componentistica d’Impianto Ing. Pepori, ringrazia il Gruppo di Lavoro a nome di ANIMP.*

*\*Aderente **Federprogetti** (Federazione dell’Impiantistica Italiana)*

# ANIMP

## MAIN CONTRACTUAL ISSUES

### NOTE INTRODUTTIVE

Il presente documento nasce dall'iniziativa, approvata nella seduta del Comitato Direttivo della Sezione Componentistica di ANIMP del 6 Settembre 2007, di fornire ai Soci uno strumento di libera consultazione che possa essere utile alle figure che operano nelle fasi di analisi dei rischi, valutazione dei contenuti ed approccio alla negoziazione dei contratti che vedono coinvolte le proprie Società.

Esso è nato dal lavoro di un Gruppo formato da Legali e Contrattisti di Società appartenenti ad ANIMP, i quali ne hanno elaborato e discusso i contenuti sulla base delle comuni competenze legali e delle soggettive esperienze acquisite in materia.

Scopo di "Main Contractual Issues" è quello di essere enunciazione di una serie di principi la cui conoscenza e consultazione può favorire una maggiore consapevolezza del significato e delle conseguenze di una determinata previsione contrattuale, in un'ottica puramente informativa e divulgativa, obiettivo di ANIMP e del presente lavoro, fermo restando il necessario supporto delle Funzioni Legali e Contrattuali.

"Main Contractual Issues" non intende e non deve essere, pertanto, recepito come documento in alcun modo vincolante per i Soci ANIMP o per altri soggetti, ma come documento che ciascuna Società potrà utilizzare nella propria piena autonomia e nel rispetto delle proprie regole interne, per trovarne, ove lo ritenesse opportuno, un supporto informativo per la interpretazione e valutazione delle più comuni clausole contrattuali.

# ANIMP

## MAIN CONTRACTUAL ISSUES

### INTRODUCTION

This document was thought of and planned during ANIMP - Componentistica's Managing Committee of September 6th 2007. Through it, ANIMP's aim is to provide its own Members with an-easy-to-consult instrument, useful for those who work in the Company's Risk Analysis and Contracts' Management Departments, during their evaluation of and approach to contract's negotiations.

It was worked out by a Group of Lawyers and Contracts' Management Executives belonging to Companies which are ANIMP's Members and who discussed and finalized it based upon their own legal knowledge and personal field experiences.

The scope of "Main Contractual Issues" (as the document is named) is to list and mention a number of principles, which, upon knowledge and review, may enable a better awareness of the meaning and consequences of certain contractual provisions, in a purely informative and training perspective, which is ANIMP's and this present work's target, given the needed support of the Company's Legal and Contracts' Management Departments.

For the above reasons, this "Main Contractual Issues" document is not aimed at and must not be intended in any way binding for ANIMP's Members or anyone else, but as a document which each Company may potentially use, subject to its own complete autonomy and internal procedures, as an informative support for the interpretation and evaluation of the most repetitive contractual clauses.

# 1) Contract stipulation and document discrepancies

(To be cont'd)

## a) Definitions

- When the contract is deemed executed and binding to the parties.
- List of documents composing the contract.
- The priority of documents.

## b) Analysis

- Importance of the moment of contract execution pursuant to Applicable Law – Common Law and Civil Law in order to establish when rights, duties and risks shall be effective for the parties.
- Value of contractual premises (“whereas”).  
Some legislations give value to contractual recitals as the “reasons for contracting”.
- Value of contractual negotiations.  
The main steps of negotiations should be recorded by the parties in order to have evidence of the willingness of the parties in the event of contractual interpretation.
- Carrying out of contract’s obligations before of contract’s signature – execution by means of *facta concludentia*.
- Particular interpretative issues:
  - (i) value of priority of documents and irremediable documents discrepancy;
  - (ii) unconscionable clauses pursuant to Italian law.

# 1) Contract stipulation and document discrepancies

(Cont'd)

## c) Impact

- Consequences on contract execution deriving from the choice of applicable law.
- The correct reference to the premises as integral part of the contract.
- Contract elements let on "Hold" or "to be agreed" - impact on the essential requirements of contract.
- Managing of prospective contractual amendments so as not to invalidate the contract.

## d) Comments/Lines of interpretation

(To be cont'd)

Contract's stipulation/execution is differently looked at and provided for by different law systems, even if the essential requirements of the various contracts are normally undoubted and undisputed.

Then, it is paramount to establish **when** the contract is validly stipulated, i.e. the Parties are bound by and must fulfil the obligations agreed upon.

Even though the written format is not normally required by law for most of the contractual agreements, their complexity, the different consequences under different law systems and the vital need to correctly assess the Parties respective obligations, require said agreements to reflect in a formal document.

The above must not be left to the controversial interpretations of the Parties' behaviours.

In order to protect both Parties' interest, one Party's proposal must be formally accepted through a written

**acknowledgement** of the receiving Party, either to confirm acceptance or to submit a counter proposal to the other Party.



# 1) Contract stipulation and document discrepancies

(Cont'd)

## d) Comments/Lines of interpretation

(Cont'd)

This would also:

- (i) highlight potential pending terms and clarify whether essential terms are not yet agreed upon;
- (ii) clarify the Parties' undoubted agreement on all topics or potential differences to be looked at as counter proposals;
- (iii) clarify the impact and validity, or otherwise, of the basic assumptions and earlier negotiation steps;
- (iv) define the liabilities linked to this contractual stage;
- (v) clarify the order of precedence in the event of document discrepancies, stressing each Party's own liability for its documents.

### **Conclusions**

A Purchase Order must be normally matched by a proper, accurate and complete Supplier's written **Purchase Order Acknowledgement** form, in order to protect both Parties' interest.

## 2) Warranties, Liabilities, Corrective Actions and Indemnities

*(To be cont'd)*

### a) Definitions

- Warranty definition.  
An obligation to pay damages in the event of violation of some contractual obligations.
- Liability definition.  
The responsibility and the duty in respect of contractual commitments. Example: the vendor is “liable to deliver the goods”.
- Corrective action definition.  
The duty to make actions in order to eliminate material defects.
- Indemnity definition.  
The duty to make indemnification, i.e. compensation remedy or “to save the promise harmless” in the event/s defined by the contract.

### b) Analysis

*(To be cont'd)*

- Vendor's Warranties:
  - (i) correct execution of contractual obligations;
  - (ii) supply of goods pursuant to Purchaser specifications;
  - (iii) time of delivery.
- Purchaser Warranties:
  - (i) payment of price;
  - (ii) collaboration.

## 2) Warranties, Liabilities, Corrective Actions and Indemnities

(Cont'd)

### b) Analysis

(Cont'd)

- Liabilities:

- (i) care of the Works until Taking Over; Vendor's liability after Taking Over;
- (ii) liability towards Purchaser's and Employer's other Properties;
- (iii) liability towards Vendor's Property and Personnel;
- (iv) liabilities towards Third Parties.

- Corrective actions:

- (i) make good of works or remaking of supply;
- (ii) liquidated Damages for Delay or for Underperformance.

- Indemnities:

- (i) indemnity against Damages;
- (ii) Liens and Claims;
- (iii) Vendor's Maximum Liability.

## 2) Warranties, Liabilities, Corrective Actions and Indemnities

(Cont'd)

### c) Impact

- Consequences on Warranties, Liabilities, Corrective Actions and Indemnities deriving from the choice of applicable law.
- The practice of self-regulatory contract, i.e. the accurate and detailed contractual provisions on Warranties, Liabilities, Corrective Actions and Indemnities.
- Maximum Liability and Insurance coverage.
- Performance Bond, Advance Payment Bond.

### d) Comments/Lines of interpretation

(To be cont'd)

Depending on different Contracts, like Sales of Goods or Services, **warranties** given may differ.  
Different laws may also impact on agreed terms differently.

Therefore, in a well balanced Contract the following issues should be addressed:

- clarify the quality commitments accurately, **excluding** any vague wording like “**fit for intended purpose**” or equivalent, if accepting to comply with goods specifications set by the Purchaser and/or by international Norms or Standards and/or agreed service specifications;
- fix the **warranty expiry terms**, **avoiding** any inaccurate (ex.: so called **ever green warranties**) and/or linked-to-third-contract terms;
- provide for the potential **corrective actions** and relevant time terms accurately and, in the event of multiple choices, agree upon whose final decision;

## 2) Warranties, Liabilities, Corrective Actions and Indemnities

(Cont'd)

### d) Comments/Lines of interpretation

(Cont'd)

- (iv) define the **liabilities linked to warranties** given;
- (v) clarify the **delivery terms** agreed upon (also see LDs for late delivery in section 5);
- (vi) clarify the other Party's obligations and liabilities for non-or-late fulfilment and/or for actions not allowing the other Party's regular fulfilment (i.e. cooperation clauses);
- (vii) set **risk and title transfer** provisions accurately for sales of goods or "handover" terms for sales of services (also see risk and title transfer section);
- (viii) assess whether the Contract's provisions are consistent with the nature of either a **Sales of Goods** or a **Sales of Services** Contract;
- (ix) **Overall Limitation of Liability** (aka Limitation of Liability in the aggregate):  
under both Civil and Common Law, liabilities are not limited and possible limitations are left to the Parties contractual freedom.  
Therefore, should the Contract miss any relevant specific provisions, Supplier's Liabilities would be unlimited. It is common business/industry practice to address this issue/gap by negotiating specific clauses aimed at setting forth limitations of specific contractual liabilities and/or establishing an overall limitation of Supplier's Liabilities. In this event the agreed price (aka Contract's value) is normally assumed as reference to determine such overall limitation.  
Even though standard clauses are suggested under Contract's model forms, it is difficult to identify standard contents for such clauses, which are normally left to the Parties freedom and are strongly depending on drivers like the individual Companies/Parties contractual policies, their commercial and/or strategic targets, their negotiating strength.

### 3) Direct and Indirect Damages, Consequential Damages/Losses

(To be cont'd)

#### a) Definitions

- Definitions under Italian Law
- Definitions under Common Law

#### b) Analysis

- **Italian Law**

The damages that can be compensated in case of breach of contract are those actually suffered as well as loss of profits insofar as they:

- (i) are **direct and immediate consequence** of the breach (1223 cc): **definition** of "direct and immediate";
- (ii) **could have been foreseen** when the obligation arose (unless in case of wilful misconduct) (1225 cc): **meaning and interpretation.**

**Definition** of **indirect** damage (loss of profit as direct damage).

**Liability can be limited** by excluding compensation for specific kind of damages, even if directly and immediately arising out of the breach, such as: loss of profits, loss of production, loss of use...

**Liability for gross negligence, wilful misconduct and breach of public security rules cannot be excluded.**

- **Common law**

- (i) **Definition** of direct damage;
- (ii) **Definition** of indirect or consequential damage;
- (iii) Examples;
- (iv) Differences in comparison with Italian law.

### 3) Direct and Indirect Damages, Consequential Damages/Losses

(Cont'd)

#### c) Impact

- **Italian Law**

Consequences of the exclusion/non exclusion of liability in case of loss of profit, production...

- **Common Law**

Consequences of the exclusion/non exclusion of liability for consequential and indirect losses and damages.

- **Note**

Under both Law systems, i.e. Civil Law and Common Law, unlimited or non-relating-to-the contract-value damages can be claimed by one Party and badly impact on the other Party's financial status, up to receivership or bankruptcy.

#### d) Comments/Lines of interpretation

Given the concept of liability limits as per above, in a well balanced Contract the following issues should be addressed:

- (i) exclude or at least limit **Indirect and Consequential Damages/Losses.**

The choice of the Applicable Law and Jurisdiction (see section 8) may have a strong impact, due to the relevant definitions of the different Law systems (under Common Law Punitive Damages or equivalent must be excluded);

- (ii) accept **Direct Damages** liability only (also see section 2 on Limitation of Liability);

- (iii) expressly list both excluded and accepted damages to overcome the different Law system definitions (also see section 2 on Limitation of Liability);

- (iv) consider that, as reported above, **Civil and Common Law systems do not provide for liability limits;**

- (v) know that one Party's "**wilful misconduct**" would make contract's provisions on liability limits agreed void.  
Under Common Law specific attention should be given to provisions regarding **Negligence**;

- (vi) know that **Product Laws** cannot be excluded or relevant damages limited by contract.

## 4) Compliance with Laws and Regulations

(To be cont'd)

### a) Definitions

Definition of laws and of regulations

### b) Analysis

#### ● Particular cases:

- (i) EU norms
- (ii) Health and Safety rules;
- (iii) Specific technical norms applicable to the supply.

### c) Impact

#### ● Possible consequences in case of breach of law:

- (i) immediate termination for default;
- (ii) no limitation of liability;
- (iii) others.



## 4) Compliance with Laws and Regulations

(Cont'd)

### d) Comments/Lines of interpretation

Good contractual practices:

- **Sales of goods**

Suppliers to comply with the laws of Country of manufacture.

With other laws, only upon Purchaser's information at time of Purchase Order booking (later information subject to P.O. change provisions – see relevant section);

- **Sales of services**

Vendor to be aware of laws applicable in the Country of work site.

Proper evaluation should be carried out at time of acceptance.



## 5) *Delivery, Risk and Title Transfer, LDs for late delivery*

(To be cont'd)

### a) Definitions

- Definition of delivery
  - (i) *"Time is of the essence";*
  - (ii) Proof of delivery.
- Definitions of title/risk transfer (in accordance to applicable law/ Incoterms).
- Definition of Liens/legal charge on the supply.
- Definition of LDs and/or Penalties (in accordance to applicable law)

### b) Analysis

(To be cont'd)

- Different options on delivery:
  - (i) Partial delivery;
  - (ii) Late delivery;
  - (iii) Extension of time;
  - (iv) Prior delivery.

## 5) Delivery, Risk and Title Transfer, LDs for late delivery

(Cont'd)

### b) Analysis

(Cont'd)

- Different options to transfer title and risk  
(In accordance to applicable law and contractual provisions).  
Liability for Liens/legal charges.
- Burden of proof.
- CAP of liabilities on LDs.
- Right to ask for "*further damages*".

### c) Impact

- Consequences of delay and right of termination.
- Consequences of transfer of title based on:
  - (i) delivery;
  - (ii) progress of supply and /or payments;
  - (iii) last payment.
- *Waiver of rights and Exclusivity of remedies;*
- Termination Rights.

## 5) Delivery, Risk and Title Transfer, LDs for late delivery

(Cont'd)

### d) Comments/Lines of interpretation

Delivery provisions usually refer to:

#### ● **Delivery time**

**"Time is of the essence"** (or any equivalent) wording allows Buyer's immediate termination for default if supplier does not deliver in "perfect" accordance with the agreed delivery terms.

Where **LDs for late delivery** are not agreed to be or qualified as **only remedy** for such occurrence, Buyer may claim further damages (subject to evidence to be provided by the claimant) beyond the LDs agreed limit, as arising from such delay.

If rate steps and maximum limit are agreed upon, LDs are automatically due if delivery goes beyond the agreed date, without the need of any damage's evidence from Buyer.

The maximum limit may vary depending on the actual type of supply and the reasonably expected damage.

If agreed upon as per the above, LDs even though automatic, fix the limit of this damages category.

Should any such LDs provision be missing, damages for late delivery should be proved and would be payable with reference to the actual damage suffered.

Termination for default of the contract's late portion should only be allowed when maximum LDs limit is achieved unless, considering the specific Contract's delivery time, the accrued delay materializes in Supplier's obligation non-fulfilment (i.e. real default, subject to the relevant Contract's provisions – also see sections 2, 3, 6 and 7 for reference and details).

#### ● **Delivery terms**

**Incoterms** should always be agreed upon, as costs and risk transfer are accurately provided for.

Amendments to Incoterms can be agreed by the Parties, but these amendments usually increase the risk and cost levels.

#### ● **Title transfer**

Can be agreed by contract upon delivery, payment etc.

The relevant decision potentially impacts on operation liabilities.

Under different laws, even though belonging to same law systems, title transfer impacts on buyer's right to dispose of the goods. Title transfer in sales of services contract environment refers to both the goods used and the final work: relevant provisions are usually different.

## 6) Termination for Default and/or Convenience

(To be cont'd)

### a) Definitions

- Definition of termination for default (contractual provision and "at law" rights).
- Definition of Corrective actions, notification obligations and period to remedy.
- Termination for Convenience definitions.

### b) Analysis

- Definition of period to remedy the default and/or start the corrective actions.
- Corrective Actions.
- Definition of costs compensation in case of Termination for Convenience (Direct costs, Cancellation Fee, exclusion of indirect/consequential losses...).

### c) Impact

- Compensation in case of termination for default and right to ask for damages incurred as result of the default.
- The practice of self-regulatory contract, i.e. the detailed contractual provisions based on explicit list of termination rights of the parties and Corrective Actions.
- Maximum Liability.
- Bank Guarantees.
- Burden of proof.

## 6) *Termination for Default and/or Convenience*

(Cont'd)

### d) Comments/Lines of interpretation

#### ● **Termination for default**

The Contract must provide an accurate definition and include relevant steps and time terms, in order to allow the correct use of the rights.

This is usually linked to the correct and detailed definition of obligations taken, warranties given, liabilities accepted, corrective actions agreed and relevant time terms.

It is normally coded in Civil Law systems, more widely left to the Parties contractual freedom under Common Law.

One Party must be in full control of all steps pertaining to the obligations accepted, to avoid the risk of running in circle, by giving the other Party the right to control the basic terms of its own obligations ("catch 22" situations).

Same principles apply to the potential Bank Guarantees and Bank payment instruments.

(Also see sections 2, 3 and 7 for reference and details).

#### ● **Termination for Convenience**

It is the right to unilaterally terminate the contract one Party may accept to give the other.

Under Civil Law systems as well as under Common Law, proved incurred costs are anyhow due to the Party subject to the other's unilateral decision.

It is good commercial and industry practice to provide in the contract for costs and other expenses to be reimbursed to supplier in the event of termination for convenience.

Such cancellation curves, drivers, and/or parameters may be negotiated by the Parties, providing fixed amounts to be paid to supplier, based on production steps and/or milestones achieved at time of cancellation.

## 7) *Exclusivity of Remedies*

### a) Definitions

- Definition of remedies  
Legal or judicial means by which a right is enforced or the violation of a right is prevented, redressed, or compensated.

### b) Analysis

- Remedies under the Contract and remedies "at Law"  
Beyond the remedies expressly set forth in the contract, the parties have available those remedies granted by the automatic operation of applicable Law (remedies at Law). The parties may agree to exclude the application to the contract of some or all of such "additional" remedies through an express waiver.

### c) Impact

- Exclusivity of remedies
  - (i) Allows a clear definition and consciousness of the remedies available to the parties in case of breach of Contract and of the associated potential liabilities.
  - (ii) Constitutes a substantial limitation of the liabilities arising out of the performance of the Contract, in particular where the applicable law provides for cumulative remedies (ex.: action to obtain the make good of the supply and action to recover damages)

### d) Comments/Lines of interpretation

It is common and good risk management practice to know the potential implications and costs of contract's obligations non fulfilment, either partial or otherwise, also with reference to warranties given and/or indemnities accepted (see earlier sections 2, 3, 5 and 6 for reference and details).

If no such a clause was included in the Contract, in addition to the contractual remedies, Buyer would be entitled to claim vs. Supplier in accordance with any other available remedy, including those remedies available by law.

Therefore other potential sources of liabilities require explicit exclusions.

Furthermore an "exclusive remedies" provision under the contract allows to cover risks originating from a limited knowledge of the applicable law.

## 8) *Applicable Law and Dispute Resolution*

(To be cont'd)

### a) Definitions

- Definition of Applicable Law

Applicable Law (or governing law) may be defined as the body of rules and principles governing the interpretation of the contract and the rights and the obligations of the parties under the contract.

- Definition of dispute resolution

The process to be employed by the parties to solve possible disputes as agreed under the relevant contract provisions or, where the contract is silent, as determined pursuant to the applicable provisions of law.

### b) Analysis

(To be cont'd)

- The choice of Applicable Law

- (i) ***Freedom of Choice.***

In principle the parties have freedom of choice over the applicable law of the contract. Even though criticised by some scholars, the parties can also select that a specific law shall apply to a part of the contract only and a different law to the other part (the "dépeçage").

- (ii) ***Limits to the Parties' freedom.***

Where all the main elements of the contract are connected with one country only, the parties are free to select a different applicable law but the "mandatory rules" of such country shall in any case apply to the contract.

- (iii) ***Absence of choice by the Parties.***

Where all the Parties are from different Countries and the contract is silent on the applicable law, then the rules of the "Private International Law" shall apply to determine the applicable law of the contract.

- State Courts or Arbitration

The Parties may elect to solve possible commercial disputes arising out of the contract either before the Courts or by Arbitration.



## 8) Applicable Law and Dispute Resolution

(Cont'd)

### b) Analysis

(Cont'd)

#### ● Institutional Arbitration and "ad hoc" Arbitration

- (i) Institutional Arbitration is an arbitration administered by one of the several national and international Arbitration Institutes which can be selected by the parties, according to pre-established rules and procedures applied by the above Institutes.
- (ii) "Ad hoc" Arbitration is a process where the parties define the rules and procedures to be applied without using arbitration Institutes.

### c) Impact

(To be cont'd)

#### ● The Private International Law

The Convention on the law applicable to contractual obligations of 1980 (the Rome Convention) is the main source of rules of EU applicable where the parties are silent on the applicable law and the choice between the laws of different countries is required.

#### ● Sales contract

Vienna United Nations Convention on Contracts for The International Sale Of Goods, 1980.

It is applicable to contracts for the sale of goods between parties whose place of business are in different States which are parties to the convention (Contracting States) or when the rules of Private International Law lead to the application of the law of Contracting State. In principle is not concerned with the validity of the contract and with the effects that the contract may have in the property of the goods sold.

#### ● The United Nations Convention on recognition and enforcement of foreign arbitral awards, 1958 (the New York Convention).

Prior to accept international arbitration as dispute resolution mechanism, it is mandatory to ascertain whether the Country of the counterpart (as well as the country where the arbitration will take place) is party to the New York Convention which grants the enforcement in such Country of the foreign arbitral award issued by the arbitrators. Actually about 120 countries are parties to the Convention.

## 8) Applicable Law and Dispute Resolution

(Cont'd)

### c) Impact

(Cont'd)

- The "non arbitrable issues"

In principle all the dispute of "commercial" nature can be settled by arbitration. According to Italian Law disputes involving rights which cannot be subject of a transaction ("*diritti non transigibili*"), cannot be referred to arbitration.

- Key elements of an Arbitration Agreement in "ad hoc" and Institutional arbitration

Where the parties agree to arbitration they must be sure of the validity of the arbitration agreement (which normally is embodied under the arbitration clause of the contract but could also be executed as separate agreement) and that all the key issues of the arbitration agreement are properly addressed (number of arbitrators, choice of arbitrators, location, language of the arbitration, substantive law to be applied in the arbitration, choice of rules). Model clauses are recommended by each Arbitration Institute to facilitate the parties in the execution of a proper arbitration agreement. "Ad hoc" arbitration, not being based on pre-established rules and procedures, requires a more extensive and accurate drafting of the arbitration agreement.

The main Institutional Arbitration: ICC and LCIA

### d) Comments/Lines of interpretation

(To be cont'd)

- Applicable Law

The most important issue to be provided for by the Parties is the contract's applicable law, because of the consequences arising out of this decision.

Due to the strong development of international trade after WWII, many instruments have been worked out to facilitate the commercial relationships among Parties in different Countries, as subject to different law rules.

The system includes Conventions (UNCISG), Principles (UNIDROIT), Payment Instruments etc., all widely known as Lex Mercatoria.

These instruments have been widely signed for adhesion and incorporated in the signing Countries law systems, becoming part of them.

Submission to these general rules or trade laws, does not mean that all major issues are covered and it is up to the Parties to add potential missing provisions or indicate which law to integrate.

## 8) Applicable Law and Dispute Resolution

(Cont'd)

### d) Comments/Lines of interpretation

(Cont'd)

The Parties' freedom on this issue is not jeopardized by the above, but neither Party should ever accept not to include such a provision in the Contract.

World's main Law Systems are Civil Law and Common Law, but specific Countries' laws may put at risk known and agreed upon Contract's principles.

**The UNCISG (United Nations Convention on contracts for the International Sale of Goods) is a reasonable and fair compromise to agree upon for Parties registered in different Countries.**

Also it will automatically apply, should the applicable law provisions not show in the Contract, providing both Parties' Countries signed it.

#### ● **Jurisdiction - Dispute resolution – Court Trials – Arbitration**

Once the applicable law is agreed upon, jurisdiction must be as well, as not necessarily linked to the choice of the applicable law and to avoid potential "Courts shopping".

**Arbitration** is faster than Court Trials and not necessarily more expensive.

ICC, AAA and other associations provide procedural rules regarding the Arbiters' council formation, but are not Contract's "applicable law".

Arbitration decisions binding power can be agreed upon by the Parties in the contract.

International agreements are also source of said binding power.

#### **Alternative Dispute Resolution**

**(ADR)** may provide a different way to progress on and solve disputes.

## 9) Order Suspensions

*(To be cont'd)*

### a) Definitions

A temporary stop, a temporary delay, interruption of a Contract requested by the Purchaser.

### b) Analysis

The written notice of suspension shall specify the date of suspension and the duration of same.

Should the Vendor believe that such suspension justifies modification of the Contract price and delivery date the Vendor shall apply for a Change Order procedure.

Should the duration of suspension exceed the forecasted period, or aggregation of periods, the Parties shall agree on further actions to be taken in terms of suspension or termination.

### c) Impact

#### ● Sales of goods

- (i) Impact on production planning;
- (ii) Impact on goods already in production;
- (iii) Impact on stocking spaces, premises and costs;
- (iv) Impact on Finance (working capital, invoicing etc.).

#### ● Sales of Services

- (i) Impact on Finance (man power, milestone payments, insurance etc.);
- (ii) Impact on sourcing of components;
- (iii) Others.

## 9) Order Suspensions

(Cont'd)

### d) Comments/Lines of interpretation

It is usually acceptable to provide for potential **Order Suspensions**, but important terms must be agreed upon at time of Contract's signature, i.e.:

- (i) maximum suspension time allowed;
- (ii) delivery changes (with reference to Incoterms) and postponement terms, if suspension is lifted within maximum time allowed;
- (iii) consequences if suspension is not yet lifted after maximum suspension time allowed (Termination for Convenience: see relevant section).

The above because any industrial process is subject to planning, which is inevitably disrupted by suspensions.



# 10) Temporary Storage and relevant Costs/Liabilities

(To be cont'd)

## a) Definitions

Safekeeping of goods, for an identified negotiated time, in a warehouse or other depository.

## b) Analysis

This is normally requested by Purchaser in the case of slippage of Plant construction schedule.

All risk of the stored goods, including storage costs and necessary insurance cost which cover the risk of loss in Vendor's warehouse, will be at Vendor's care and costs.

In addition, unless the:

- Title is transferred
- Goods are invoiced
- Payment is collected

Vendor will also bear financial costs up to the end of the storage period. For Vendor Companies quoted in the USA stock exchange, therefore subject to US GAAP (US General Accepted Accounting Principles) Sarbane Oxeley Act (SOX), will also not be entitled to Recognise the Revenue and sales will not be reported in the Company balance sheet.

## c) Impact

- Sales of goods
  - (i) Impact on stocking spaces, premises and costs;
  - (ii) Impact on Finance (working capital, invoicing etc.);
  - (iii) Goods protection and relating liability.

# 10) Temporary Storage and relevant Costs/Liabilities

(Cont'd)

## d) Comments/Lines of interpretation

(To be cont'd)

Whatever the reason for the request, **Temporary Storage** bears specific contractual obligations, if agreed upon by the Parties. It is therefore reasonable and fair to provide in advance for the relevant consequences and costs, otherwise impacting on the supplying Party.

For different reasons, last but not least the International Revenue Recognition rules, such provisions impact on the following issues:

- (i) contractual terms on delivery (Incoterms, LDs for late delivery etc.);
- (ii) title transfer;
- (iii) risk transfer and relevant liabilities, which include goods' conditions and property protection;
- (iv) costs to be agreed on a conventional basis in advance - rather than later and based on actual - since Supplier provides an additional service with implications on cash flow, working capital, balance sheet and stock exchange quotations;
- (v) time terms and consequences at expiry date;
- (vi) invoicing and impact on company's balance sheet;
- (vii) counting of payment terms;
- (viii) payment;
- (ix) accurate indication of withdrawal time;
- (x) others.

# 10) Temporary Storage and relevant Costs/Liabilities

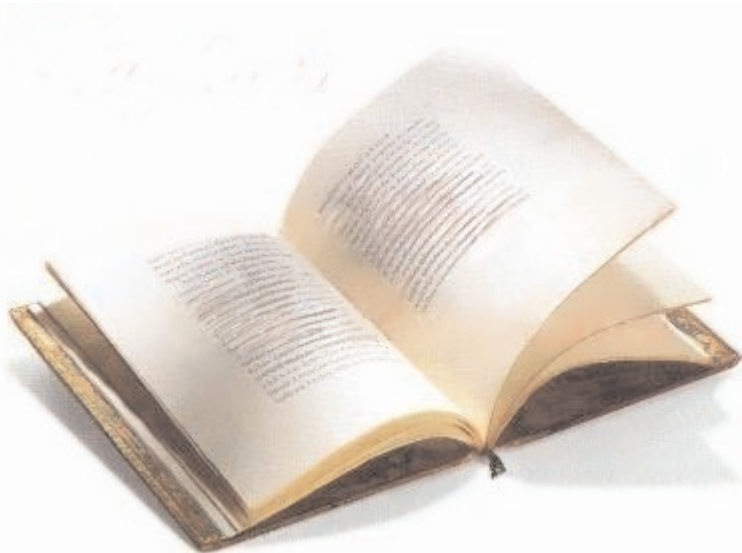
(Cont'd)

## d) Comments/Lines of interpretation

(Cont'd)

### **Conclusions**

If Temporary Storage is required by one Party, a good balanced contract must accurately cover the above issues in advance for the benefit of both Parties, by clarifying rights and obligations.





# 11) Force Majeure

(To be cont'd)

## a) Definitions

### ● General definition

Force Majeure is a common clause in contracts which essentially frees both parties from liability or obligation when an extraordinary event or circumstance beyond the control of the parties, prevents one or both parties from fulfilling (even partially) their obligations under the contract.

## b) Analysis

(To be cont'd)

### ● Usual samples of Force Majeure events

- (i) Operation of the forces of nature (act of God) such as earthquake, hurricane, lightning, tidal wave, tsunami, typhoon, or volcanic activity;
- (ii) epidemics;
- (iii) war, hostilities (whether war be declared or not), invasion, act of foreign enemies;
- (iv) rebellion, terrorism, revolution, insurrection, military or usurped power, or civil war;
- (v) riot, commotion or disorder, unless restricted solely to employees of the contractor or of its subcontractors;
- (vi) ionizing radiation or contamination by radio-activity except as may be attributable to the contractor's use of such radiation or radio-activity;
- (vii) contamination by or other hazardous effects of any toxic substance except as may be attributable to the contractor's use of such substance;
- (viii) discovery of archaeological relics or historical artifacts;
- (ix) industrial disputes.

# 11) Force Majeure

(Cont'd)

## b) Analysis

(Cont'd)

- Consequence of a force majeure event

Most contracts require the work to be performed within a certain time and unless expressly agreed, the contractor normally has the risk of delay. Therefore we must describe clearly those cases where we expect to be allowed time relief. Force Majeure is maybe the most important.

It is generally accepted that, while there should be an entitlement to extension of time for Force Majeure, there is normally no entitlement to extra cost. This is acceptable up to a point, but cannot last forever: the contractor should always have the right to terminate the contract for prolonged Force Majeure suspension after a certain time (ex.: 6 months aggregate), and/or to require the client to pay its costs above an agreed period, in order to limit the costs to an acceptable amount.

However, Force Majeure is not intended to excuse negligence or other bad fulfillment of a party, as where non-performance is caused by the usual and natural consequences of external forces, or where the intervening circumstances are specifically contemplated. In particular Force Majeure cannot excuse the client's obligation to pay sums already due, on time. The contractor remains entitled to full payment and to suspension/termination for non-payment according to the contract.

- Uninsurable force majeure events

There are certain Force Majeure risks, which insurers typically will not cover (war, nuclear radiation, radioactive contamination, sonic boom).

## c) Impact

(To be cont'd)

- Sample force majeure clause and relevant consequences

The contractor shall not be liable for loss or damage resulting from any delay or failure to make delivery or complete the work within the time specified due to Force Majeure events like acts of God, war, acts of the public enemy, riot, civil commotion, sabotage, federal, provincial or municipal laws or regulations, strikes or other labour disputes, fire, flood, accidents, epidemics, quarantine or embargoes, damage to or destruction in whole or in part to the equipment or manufacturing plant, lack of or inability to obtain raw materials, labour, fuel or supplies for reason constituting force majeure, or similar events which prevent or hinder the manufacture, delivery or completion of the work.

# 11) Force Majeure

(Cont'd)

## c) Impact

(Cont'd)

Any such causes of delay, shall extend the time of the contractor's performance by the length of delays occasioned thereby, including delays which reasonably incident to the resumption of the work. Each party may terminate the contract if Force Majeure events last, or their effects cause a delay exceeding an agreed period of time in the aggregate.

## d) Comments/Lines of interpretation

- **Force Majeure**, as internationally accepted, covers events beyond the Parties' control, excusing the non or partial fulfilment of one Party's obligations.  
It mainly refers to the Party performing a production or construction activity, even though reciprocity is often agreed upon.  
The application of Force Majeure to the Party whose obligation is only to pay a price for either goods or services provided by the other Party, does not really make any logical/juridical sense.  
In fact such situation is usually covered by provisions referring to the financial status of the Parties, initial or later incurred: these provisions may affect one Party's Contract(s) acceptance/signature or the negotiation on termination's rights.  
Any Force Majeure concept's mitigating provision must be carefully evaluated for avoidance, as potentially making void the concept, with a different scale of consequences under the various law systems.  
Such mitigating provisions may reasonably attain to the effects of the event instead.

## 12) Payments, Credit Issues, Assignments

(To be cont'd)

### a) Definitions

- General definition

**Payment** is the transfer of wealth from one party to another and is usually made in exchange for the provision of goods, services, or both, or to fulfil a legal obligation.

- General definition

**Assignment** is the transfer of rights and/or obligations by one party—the assignor—to another party—the assignee.

### b) Analysis

(To be cont'd)

- Usual payment structure and procedures

Mainly in contracts for the Sales of Services, an offer assuming cash-neutral terms of payment is usually based on the following:

- (i) agreed advance payment, against a bank guarantee for the same amount;
- (ii) regular progress payments during the works, based on the payment schedule set out in the tender and subject to the achievement of agreed milestones;
- (iii) monthly progress payments for civil works and mechanical and electrical installation according to certified progress of work at site.

- Advance payment

A good test of the client's ability to pay is his willingness to make an advance payment upon the effectiveness of the contract. Contractor immediately incurs costs (mobilization; engineering; bonds; insurance; sub-contracts; etc.) and need to be sure that the client has obtained all necessary internal and external finance, approvals and permits, etc.

If he is not willing to make an advance payment, there is normally a (bad) reason.

The contractor is usually ready to provide an advance payment guarantee to the value of the advance payment, reducing pro rata to the value of goods delivered / work done.

## 12) Payments, Credit Issues, Assignments

(Cont'd)

### b) Analysis

(Cont'd)

- Documentation allowing payment

It is essential to specify, in the contract, clear invoicing, payment and documentation procedures (ex.: allow a time period from invoice to payment). It's also essential to ensure compliance with the agreed procedures: the best possible irrevocable letter of credit will not pay if the contractor does not submit accurate documentation, on time. The documents to be presented to the bank must be clearly identified in the contract so as to avoid any delay due to possible disputes as to inaccuracy and/or incompleteness.

- Securities

A contractual golden rule is to check carefully, prior to the signature of the contract, the financial status of the Client. Based on the results of such check, proper security of payment (e.g. letters of credit) could be required (see Comments column).

- Payment following change order

A project, a contract, is rarely static, it is a living thing. Particularly in the case of contracts for non-standard or engineered products and systems. Change orders are unavoidable. As for the main contract work scope, it is essential that change orders specify clearly agreed terms of payment and the agreed payment mechanism / security of payment (where required). If the main contract scope is the subject of export credit financing, or other documentary security, all change orders must have access to the same (or equivalent) secure source of funds. These requirements, as well as variation procedures, notice periods and documentation must be stated in the contract.

- Retention

Traditionally in the construction contracts, retention has been used by clients as a security device by holding back, or retaining, a certain percentage of progress payments made to contractors in lieu of the release by the supplier of bank guarantees. The same device has been employed by contractors on progress payments made to subcontractors. The holdback is intended to provide clients with funds to be used to finance completion or correction of a defaulting contractor's work. The money held back is actually money earned by the contractor for services and materials provided for the project, which, in most cases, have been approved and certified. Retention is usually held until completion of construction of the project and is then released along with the final payment to the contractor. In the private sector, 5/10 percent retention is not unusual.

## 12) Payments, Credit Issues, Assignments

(Cont'd)

### b) Analysis

(Cont'd)

- Assignments of contract rights (ex.: credit sale) and/or obligations.

Assignment of rights under a contract is the complete transfer of the rights to receive the benefits accruing to one of the parties to that contract.

- Liability of the Assignor

Where the assignee is not known to the Supplier, the Assignor should remain jointly and severally liable with the assignee (see Comments column).

- Requirements for a contract right assignment

Assignment right must be subject to the contractual parties prior written consent (see Comments column).

Sometimes contracts contain an explicit non-assignment clause, which prohibits the assignment of specific rights, or of the entire contract, to another party.

Two other possible contractual ways to prevent the assignment are:

(i) recession clauses or

(ii) clauses creating a condition subsequent.

The first would give the other party to the contract the power to terminate the contract if an assignment is made.

The second would terminate the contract automatically in such circumstances.

### c) Impact

(To be cont'd)

- Sample **payment** clause and relevant consequences

(See payment structure in Analysis column). All payments shall be deemed to be effected by the client if fully credited to contractor's bank account. The payments have to be made in accordance with the payment schedules laid down in Article ... of the contract. Mainly in contracts for the Sales of Services and except for advance payments agreed, the payment schedules are based on progress payments related to the progress of the work in connection with controlling events.

## 12) Payments, Credit Issues, Assignments

(Cont'd)

### c) Impact

(Cont'd)

- Sample **assignment** clause and relevant consequences

Neither party shall be entitled to assign or transfer the contract or any part thereof or any of its rights or obligations thereunder without the prior written consent of the other party.

Any purported assignment by either party without said prior written consent by the other party shall be void and of no effect.

In case of such assignment the assigning party shall remain jointly and severally responsible with the assignee for the execution of the contract or any part thereof.

### d) Comments/Lines of interpretation

(To be cont'd)

- **Securing the Credit**

It is the final target behind the variety of payment terms that the Parties can agree upon.

Main issues:

- (i) credit insurance (and Buyer exposure under all Contracts);
- (ii) advance payment (if partial, may just be sufficient to buy raw materials, but not to enter the order into production in case of sales of goods, or to go ahead with construction in case of sales of services);
- (iii) L/C I/C and relevant documents include Contract's provision which may prevail on main Contract's provisions;
- (iv) right of set-off under all Contracts (not to be accepted);
- (v) parent Company (or else's) Letter of Guarantee and/or Letter of Comfort: the latter really does not work like a payment guarantee;
- (vi) others.

## 12) Payments, Credit Issues, Assignments

(Cont'd)

### d) Comments/Lines of interpretation

(Cont'd)

#### ● **Assignment**

Given the above indications on Credit, the rights of assignment become a fundamental Contract's issue, in order not to make void all the Credit provisions aimed at securing payments.

This right **must be subject to the contractual Parties prior written consent.**

In fact it is a Contract's change (see relevant section).

Exceptions can be made only if:

- (i) the Party assigning the Contract's rights and obligations remains jointly obligated with the new assigned Party;  
and/or
- (ii) the assigned Party is known at Contracts acceptance/signature, in order to enable the other Party's Credit controls and insurances: it may implicate additional costs.



## 13) Intellectual Property and related issues

### a) Definitions

Intellectual Property rights protected by Patents

### b) Analysis

Patent offices under various jurisdictions can issue patents for widely used products and processes

### c) Impact

Indemnities for Patent's rights infringement

### d) Comments/Lines of interpretation

A correct evaluation of the obligations and relevant risks must be carried out by the Parties to avoid useless hurdles during Contract's negotiation.

Often the subject provisions are included in GPC documents covering any kind of sourcing, including goods and commodities, but also specialties as well as services.

**Sometimes the risk of infringing Intellectual Properties rights is real, often it is not or very remote.**

Normally, in the sales of goods, the Supplier manufactures goods according to international Norms or customer's specifications, the latter not subject to Patents.

In different situations a clear Contract should identify the patented subjects.

Supplier may also confirm, to the best of its knowledge, whether any procedure for infringement has been started vs. the company.

**Supplier's indemnity obligations should be based on clear and undisputable evidences of Patent's infringements (up to Court's decisions).**

Supplier's obligations potentially linked to simple "**Assertions**" of Patent's infringements should be clearly defined in the Contract.

A careful evaluation of the actual Contract's obligations and/or supply may avoid lengthy, but useless discussions between the Parties.

## 14) Order Changes

### a) Definitions

Changes to the Contract's agreed Terms

### b) Analysis

When Contract's agreed terms can be considered validly changed and Parties subject to said changes

### c) Impact

- Correct evaluation of the obligation accepted as a Contract's Party.
- Certainty of Contract's terms and relevant obligations.
- Correct Contract's execution.

### d) Comments/Lines of interpretation

**Any change affecting a Contract validly stipulated** (see relevant section) **must be agreed in writing** in order to avoid any confusion on each Party's obligations.

The above mainly applies to the Sales of Goods, while during construction, i.e. Sales of Services, the contractual procedures sometime give the right of direction on changes to the Buyer, for the Seller only to claim the different costs and delivery implications, if any.

This Sales of Services procedure, even though reasonable, provided time terms are agreed upon, cannot be simply reverted on contracts for the Sales of Goods.

For this kind of contracts, proper changes going through a written agreement will be needed.

In the event of changes implying cancellations of ordered quantities, Termination for Convenience provisions (see section 6) may apply.

The above because production planning and allocations are very different from construction planning and activities relating to work force.

## 15) Insurance

### a) Definitions

Definition of the appropriate, required and available insurance

### b) Analysis

Requests of specific insurances for specific scopes of business/work, amounts and events

### c) Impact

- Impact on specific order profitability
- Applicability depending on Contract's scope of work
- Financial status of the Parties and liability limits agreed

### d) Comments/Lines of interpretation

Sales of Services and Sales of Goods stress here their differences again.

It is normal for Plant Owners to ask Suppliers of Services for insurances to cover the potentially terrific impact that delays or damages igniting indemnity rights might have.

Same request (specifically with reference to insurance limits) cannot simply be reverted back on Suppliers of Goods, as Contract's value and potentially caused direct damages are far lower (usually there are no activities performed or producer's personnel working on site and therefore the risk is limited to defects in the supply causing direct damages to the plant). Buyers' intention to reduce its own financial exposure through these requests to Suppliers does not justify such requests.

**Suppliers of Goods in fact normally reject such requests and only offer copy of the certificate of their own Insurance.**

Their policy cannot cover 100% of the producer's activities and risks.



**Sezione  
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*Associazione Nazionale di Impiantistica Industriale*

*Via E. Tazzoli, 6 - 20154 Milano*

*Tel. 0267100740 - Fax 0267071785*

*[www.animp.it](http://www.animp.it)*