

Saudi Arabia's Civil Code: General Principles Applicable to Construction Contracts

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The Kingdom of Saudi Arabia enacted its long-awaited Civil Transactions Law on 19 June 2023 by Royal Decree N191/1444 (the Civil Code). The Civil Code entered into force on 16 December 2023 (the Effective Date). In this article you will find some key take aways of the Civil Code provisions throughout the life of your agreement and, in particular, those relevant to the construction sector.

The Civil Code is a manifestation of Saudi Arabia's broader Vision 2030 initiative aimed at modernizing its legal framework, attracting foreign investment, and fostering economic growth. This is the first time that the Kingdom has distilled its Sharia law principles into a codal system, similar to those of other jurisdictions in the region such as the UAE and Qatar. There are many commonalities between the civil codes of these countries due to their foundation in Sharia but also some notable differences of which parties need to be aware.

Overview and key principles

The Civil Code encompasses both contract and tort, covering issues from the formation of contracts and other obligations to liability and remedies under varying forms of relationship and the termination of

those relationships. As seen with other civil codes, there are bespoke sections dealing with specific types of relationships such as agency, insurance, partnerships and construction contracts.

The terms of the Civil Code govern relationships, whether contractual or tortious (but note exceptions discussed further below), entered into from 16 December 2023 as well as existing relationships as it will be applied retrospectively. This means that the Civil Code applies to events that occurred and relationships that existed, whether contractual or otherwise, prior to the Effective Date except if (a) any "statutory provision" or "judicial principle" that relates to the event in question contradicts the provision of the Civil Code, and one of the parties relies upon it, or (b) a limitation period had already started to run prior to the Effective Date. The default position is that it is for the party relying upon a conflicting statutory provision, judicial principle or limitation period, to assert and prove that fact.

The terms of the Civil Code also govern relationships that are personal / private rather than only commercial in nature. For commercial matters in particular, the Civil Code states that it applies (1) in a manner that does not contradict the nature of the commercial transaction in question and (2) to the extent that it does not contradict what is specifically provided for in other laws governing commercial matters.

When it comes to contractual interpretation going forward, Article 1 sets out a hierarchy of application: first, provisions of the Civil Code, second, the "overall rules" (described by some as "Sharia-inspired legal maxims") as listed in Article 720 of the Civil Code, and third, the provisions of the Islamic Sharia that are "most appropriate". Article 1 goes on to add that "[t]he application of the provisions of this Law shall

be without prejudice to the special statutory provisions”, which are understood to be other specialised laws.

Rules of interpretation

The Civil Code commits the general guidelines for the interpretation of contracts under KSA law to paper. This will serve to assist courts and tribunals with disputes regarding contractual interpretation and should thereby facilitate the enforcement of those contractual terms and lead to greater certainty for all concerned. As is the case under other civil codes such as the UAE Civil Code, the literal interpretation of contracts is paramount and therefore the clear words of the contract must be applied in the first instance. However, if the wording is unclear, then the common will of the parties must be ascertained by looking at custom, the circumstances of the contract, the nature of the transaction and the usual course of dealing between the parties. This provision brings in a number of pre-existing principles of Sharia law, indicating that this area of law has been codified rather than modified.

Formation of contracts

There are no major surprises in the section of the Civil Code dealing with formation of contracts. Articles 32 and 33 detail the rules for contract creation, namely the need for an offer and acceptance of that offer between parties with legal capacity. It is possible to create a contractual relationship in writing, orally or through implied actions unless specific circumstances require an explicit declaration of intent.

Parties should be mindful that Article 37 specifies that silence does not automatically indicate acceptance, except under certain conditions. However, silence can indeed be interpreted as acceptance when there is a history of dealings between the contracting parties and the current offer is related to those dealings. Therefore, ignoring correspondence with a counterparty in the hope that silence will be interpreted as disagreement is not a safe course of action. Rather, the most prudent response will be to respond with explicit disagreement.

Article 48 addresses the capacity to contract which



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provides that individuals who are minors, mentally incapacitated, or suffering from mental deficiencies lack the capacity to enter into contracts.

Setting aside of contracts

The CTL further addresses, in Articles 57 to 69, circumstances where consent is wanting by virtue of a mistake, fraud or, and duress. A contract is considered void if: (i) the mistake is substantial, known by or easily detectable by the other party, and not merely a unilateral mistake; (ii) the actions or deliberate silence of one party deceptively induce another to enter into a contract; and / or (iii) it involves coercion by material or moral means. Duress caused by a third party can only lead to contract rescission if the other contracting party was aware of it.

Ongoing obligations

Article 95 of the Civil Code codifies the Sharia principle of good faith and states that (i): a contract must be carried out in accordance with its terms and “in a manner consistent with the requirements of good faith” and (ii) the contract is not limited to binding the contracting party to its terms, but it also includes requirements arising out of statutory provisions, custom and the nature of the contract. Parties can expect the principle of good faith to be applied by the KSA courts through all stages of the life of their relationship, from negotiation and performance of the contract through to termination.

Not only must a party exercise its rights in good faith

but it must not abuse its rights. Article 29 of the Civil Code provides that “no right may be exercised wrongfully” and lists specific instances when this would be the case. Specifically, (i) if a right is exercised only to cause harm to others; (ii) if the benefit generated from exercising the right is disproportionate to the harm it causes to third parties; or (iii) if the right is exercised for an unlawful purpose or in an unlawful manner. As such, even when carrying out a contractual right, parties must keep this principle in mind and consider the purpose of their actions and the harm likely to be suffered as consequence.

Renegotiating terms

Article 97 of the Civil Code codifies the position in relation to ‘exceptional unforeseen circumstances’, allowing the court to reduce a burdensome obligation. In the event of exceptional circumstances of a general character, which could not have been foreseen at the time of entering into the contract and as a result of which the performance of a contractual obligation becomes burdensome for the debtor such as to threaten them with exorbitant loss, they may seek to renegotiate that obligation with the counterparty. However, a request to renegotiate does not permit the requesting party to stop performing the contract. If the parties cannot renegotiate the obligation, then the court has the power to restore the obligation to a reasonable level. There is also a provision of a similar nature under the muqawala section of the Civil Code which relates specifically to contracts to make a thing or perform any work in consideration of compensation (including construction contracts).

Liability

Limitation of liability

Article 173 of the Civil Code allows parties to limit liability but not in the event of fraud or gross error. It is not possible to exclude liability arising from a tort.

Strict liability

Parties to construction contracts in the Middle East will be familiar with a form of strict liability known as ‘decennial liability’ which holds contractors and consultants liable in the event of structural failures occurring within 10 years. While the Civil Code is silent on this issue, this liability is very much alive in

the Kingdom and can be found in the Implementing Regulations of the Saudi Building Code Application Law, also known as the "Building Regulations," which enshrine decennial liability in Article 29. As such, contractors and consultants involved in the construction and design of construction works in Saudi Arabia should be aware that structural failures for construction works are fully covered under the no-fault regime of decennial liability.

Loss and Damage

Liquidated Damages

The Civil Code allows parties to agree a pre-determination of damages in their contracts, as long as the object of the obligation is not pecuniary. The Civil Code also grants the courts the ability to adjust pre-determined damages to reflect the actual loss suffered. The damages can be reduced if the court or tribunal considers this appropriate but can only be increased in cases of fraud or gross error on the part of the debtor. This approach is different to that of some other legal systems in the Middle East such as the UAE, which allow the court to increase pre-agreed damages in wider circumstances not limited to gross error or fraud. Under Article 180, the damage compensated must be foreseeable at the time of entering into the contract.

Moral damages and Loss of profits

The Civil Code now expressly allows compensation for loss of profits under Article 137 and moral damages under Article 138. These provisions are found under the Acts Causing Harm section of the Civil Code and appear to also apply to contractual agreements subject to the caveat under Article 180 described above relating to foreseeability.

Interest

The Civil Code does not deal with interest and it is assumed that the situation has not changed from that prior to the Civil Code. Therefore, contractual provisions entitling the recovery of interest in the KSA remain unenforceable, and the KSA courts will not award interest.

Termination

General provisions of the Civil Code dealing with termination of contracts can be found in Articles 105

(termination by mutual consent), Article 106 (exercise of an option to terminate), Article 107 (termination for breach of an obligation) and Article 110 (termination due to impossibility of performance).

Bespoke to construction contracts, the Civil Code outlines the termination possibilities for muqawala contracts encompassing the following scenarios (Article 475-478):

- a) Termination upon the completion of the works.
- b) Termination by either party if there is an emergency excuse related to the performance of the contract, provided that the party requesting termination compensates the other party for resultant damages.
- c) Termination if the contractor initiates work but subsequently becomes incapable of completing it due to reasons beyond their control. In this scenario, the contractor is entitled to payment for the completed work and the expenses incurred for uncompleted works, to the extent of the benefit gained by the employer.

As such, parties to construction contracts must consider the particular provisions in the muqawala section of the Civil Code as of particular application when faced with termination of their agreements.

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