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Forewords

It is a privilege for me to be invited to write this foreword for *The Belt and Road Initiative: Legal Risks and Opportunities Facing Chinese Engineering Contractors Operating Overseas* (the Book).

The Permanent Forum of China Construction Law (PFCCL) conducted a study (the Study) on the risk analysis and management that Chinese engineering contractors which operate overseas are facing. As an outcome of the Study, PFCCL successfully presents Chinese readers this Book, which comprehensively covers the topics of political, social and market environment of host countries, legal environment in host countries, risks of project stakeholders, project risks and internal risks of contractors, which will serve as a very useful guidance for Chinese engineering contractors when operates construction and engineering projects overseas. Its importance to Chinese contractors operating overseas becomes even more significant in the context of the Belt and Road Initiative (BRI) because BRI is such a dynamic project that involves the global flow of hundreds of billions of dollars, many of which are and will be used in engineering and construction projects delivered by these leading Chinese contractors.

Furthermore, looking from another perspective, the Book could also perfectly serve for two additional purposes: (1) the perspectives on risk analysis and management from Chinese engineering contractors presented by the Report may help their counterparts to better understand the worries and concerns of the Chinese engineering contractors and the Chinese business culture and philosophy behind them; (2) more broadly speaking, some of the risks that Chinese engineering contractors are facing in their overseas operation are in fact the same as those faced by the contractors from other countries and thus may serve as a general guidance to the same, both of which will eventually help the improvement of business practice in the captioned sector in real life practice. I understand that PFCCL will work with multiple international organizations towards an updated report in the future from a more global perspective to benefit the general international arbitration practice in the captioned field, to which I am looking forward.

Being the world's leading arbitral institution, with more than 20% of its caseload in engineering and construction sector, ICC International Court of Arbitration (ICC

CHAPTER 2

Legal Environment in Host Countries

2.01 WORK VISA

To protect local employment, host countries usually restrict foreign managers, professionals and workers who are not normally resident there ("foreign personnel") from entering and/or working thereby requiring work visas or work permits ("work visas") in respect of type of work, education, number, duration, etc. The time taken to obtain work visas is uncertain as this is determined by the laws of the host country and employment policies of state and local governments. If the work visas needed cannot be obtained in good time, the contractor cannot dispatch foreign personnel to the project at the time(s) required by the project schedule, and the project progress will be delayed.

[A] Quota and Duration of Visa

To apply for a work visa, a contractor usually needs to comply with any quota imposed by the host country. The size of the quota and the type of work allowed to be carried out with the relevant work visa has to sufficiently satisfy the needs of the project. Usually the type of work for which the visa is sought must be urgently needed locally, and the foreign personnel applying for the visa must have relatively high professional or technical skills. The work cycle to obtain a visa is relatively long, and Chinese contractors need to plan in advance in order to comply with the project schedule.

For example, in a general contracting project for construction of a hotel in a Central Asian country, in order to obtain work visas for Chinese workers in accordance with local laws, the Chinese contractor had to comply with the following requirements: (a) the contractor first had to apply for sufficient amounts of work quota to the Ministry of the Interior. All workers introduced from abroad have to be urgently needed in that Central Asian country and must be highly skilled or to satisfy other special requirements; (b) the workers introduced from abroad needs to have appropriate educational

backgrounds and skills. Documents evidencing educational backgrounds and skills had to be obtained and double authenticated. Double authentication is a procedure to be completed before obtaining visas: Notarizations have to be obtained and submitted to the Ministry of Foreign Affairs of the People's Republic of China and the embassy of that Central Asian country in China for verification and authentication of the content of the notarizations. This generally takes 15 working days; (c) All documents must be translated into Kazakh or Russian. If visas are needed for a large number of personnel, the translation will take about one month. In summary, the difficulties in obtaining work visas in the Central Asian country are: (1) the work quota is very limited and insufficient to satisfy the need for workers on construction sites; (2) in order to protect employment of nationals of that Central Asian country, its authorities will examine strictly the professional qualifications of foreign technical personnel. In particular, the professional qualifications of foreign personnel do not match the openings for personnel on the project, or if that Central Asian country has technical personnel qualified in the same type of work, work visas will not be granted for the foreign personnel, and that Central Asian country strictly controls entry of personnel with professional qualifications of less than three years; (3) the cycle for obtaining work visas is generally four to six months. As a result, if Chinese personnel cannot arrive on site in good time, the construction progress on site will be affected.

For another example, in an African country, in order to protect local employment, governments impose increasingly stricter restrictions on import of labor services by Chinese contractors into the African country, and especially for personnel with low technical capabilities, who will face tough regulations on entry. Entry and visa administration issues have loomed large to become serious problems faced by Chinese contractors in Africa. As found by the "In-Depth Investigation on Project Contracting in Seven African Countries by Chinese Enterprises" published by China Council for the Promotion of International Trade, some African countries have strengthened control over the entry of and visa administration for foreign personnel, which has constituted a very important obstacle for many foreign engineering companies. In other African countries, visas for Chinese workers are also difficult to obtain, which is regarded by some investigated enterprises as a bottleneck in development. In another African country, the expense for work visas increased to USD 2,000 per visa in 2015 and thus increased the enterprise costs. In summary, apart from some African countries where situations are better, regulations on visas in African countries are increasingly strict and this is unlikely to improve.²⁷

In Europe, countries generally restrict the entry of Chinese workers by requiring work visas and specifying the maximum number of and requirements for foreign staff in contracts for the purpose of protecting local employment, labor conditions and interests of special professions. This results in failure to obtain entry of large numbers of Chinese workers or delay in obtaining work permits for them. Most Chinese

27. Excerpt from "In-Depth Investigation on Project Contracting in Seven African Countries by Chinese Enterprises" published by China Council for the Promotion of International Trade. Refer to http://www.ccpit.org/Contents/Channel_3430/2015/0921/489451/content_489451.htm on March 2, 2018.

contractors lack experience in managing subcontractors and teams in developed countries, and the Chinese way of managing workers does not operate well in European countries, which has adverse impact on the normal operation of projects.²⁸

(B) Adverse Impact of International Politics on Obtaining Visa

To obtain work visas, applicants may need to avoid the adverse impact of international political relationships or political situations.

For example, a Chinese contractor in investment and construction in Southeast Asia faced difficulties in obtaining work visas for its engineering, procurement and construction (EPC) project because of tense international politics. The funds had been sent, and machinery had been imported, but technical and management personnel could not arrive at the site on time due to problems in obtaining work visas. In another project implemented by that contractor, technical personnel on key posts had to return to China upon expiration of their work visas, and such professionals were in short supply in the local market, so the project had to be suspended until key technical personnel obtained work visas again.

For another example, affected by changes in the political situation between China and a southeast Asian country from 2013 to 2014, the Immigration Bureau of that country strengthened administration on visas and searched for and detained illegal workers on construction sites of Chinese contractors. As a counteraction to changes in the policies of the Immigration Bureau, a Chinese contractor applied for Special Working Permit (SWP), Alien Employment Permit (AEP), Special Resident Retiree's Visa (SRRV) and various other work permits to obtain corresponding types of visa for qualified personnel, established a good contact mechanism and relationship with the Chinese embassy in the host country and the embassy of that country in China and thus established an emergency countermeasure mechanism²⁹ to minimize the adverse impact of this crisis.

We suggest, first, that Chinese contractors overseas should strengthen the training of human resources, and recruit or train local skilled workers, to satisfy actual demands for workers of the project and/or of Chinese contractors. Second, Chinese contractors should take care to communicate and coordinate with the relevant government authorities of the host country, take different actions on different categories of issues and flexibly handle those issues when applying for work visas and link approval and implementation of the project with approval of work visas of the number and type

28. Excerpt from "Which Problems Will Chinese Enterprises Encounter in Contracting Projects in Middle and East Europe", written by Zhang Xiwei, Zhang Lihua and published in Journal of International Economic Cooperation, Issue No. 6, 2017.

29. Predict and Control Commercial Risks in International Engineering Projects, written by SHEN Weidong, assistant general manager of Shandong Electric Power Engineering Consulting Institute Corp., Ltd.; WANG Hua, manager of commerce department of Shandong Electric Power Engineering Consulting Institute Corp., Ltd., quote from China Investigation & Design, Issue No. 12, 2016, page 18.

required through coordination and interaction with the relevant government authorities. Third, Chinese contractors should also formulate in advance a contingency plan to avoid risks of difficulty in obtaining work visas as indicated in the example above.

[C] Avoid Illegal Labor

Chinese contractors should not take part in any fraudulent or corrupt conduct applying for work visas and should avoid employing illegal labor in host countries.

For example, a foreign enterprise investing in a Southern Asian country and undertaking international engineering projects had failed to obtain work permits for foreign employees and allowed them to work locally with only travel visas. The government of that country has now amended the law in the new Immigration Law for foreign employees and employers of foreign employees such that for each illegal foreign worker employed by the employer, the employer will be fined THB 4,00,000 to THB 8,00,000 and the illegal foreign worker employed will face up to five years' imprisonment or fines of THB 2,000 to THB 1,00,000.

[D] Other Certificates or Certifications

When granting work visas to foreigners, governments of some Middle East countries require the applicants to provide special certificates or certifications. For example, since February 4, 2018, the UAE government has required applicants for work visas in the UAE to provide an authenticated "Certificate of Good Conduct." This "Certificate of Good Conduct" is also referred to as Certificate of No Criminal Conviction, which is issued by the state of nationality of the applicant for work visa or the state in which the applicant has resided for the past five years. Upon issuance, the certificate will not become effective until it is authenticated by a UAE embassy abroad or the Authentication Center of Ministry of Foreign Affairs and International Cooperation.³⁰

[E] Prevention and Allocation of Risks Related to Work Visas

Since the abovementioned risks relating to work visas often cause delays in the construction period, Chinese contractors should conduct due diligence on the legal environment of the host country in advance and solicit help from professional institutions when necessary. So as to avoid misjudgment, this due diligence should be a factor in work visa processing time when calculating the project construction period. In some cases, due to political risks and other reasons, contractors encounter obstacles in obtaining work visas for their workers by themselves and must ask for the assistance of the employer. For those cases, the relevant obligations of the employer must be made clear in the contract.

30. Quote from www.dibaichina.com, website address as <http://www.dibaichina.com/forum.php?mod=viewthread&tid=359323&highlight>, visited on February 14, 2018.

In a relevant case provided by the International Court of Arbitration (ICC) for this project, Chinese contractors contracted projects in a country that had not yet established diplomatic relations with China. The contractors, therefore, could only apply for work visas through third-country governments, which caused a great deal of inconvenience. Judging from the correspondence between the employer and the contractor, the contractor had always believed and expected that the employer would provide assistance with respect to the work visa situation. However, the contractor did not insist on memorializing this an obligation of the employer in the contract. On the contrary, the EPC contract between the parties clearly provided that the contractor was required to get work visa by itself.

During the course of performance of the contract, work visas and other issues caused delays in the construction period, and the employer filed an arbitration request to terminate the contract and made claims based against the Chinese contractor's liability for breach of contract. The Chinese contractor contended that the employer did not fulfill its obligation to assist with the work visa and that the difficulties in getting the visas were beyond its control which could not be attributed to the contractor.

According to the explicit provisions of the EPC contract, the arbitral tribunal held that there was no obligation on the employer to assist in the visa application and that the absence of diplomatic relations between China and the host country preexisted the contract. This fact, therefore, could not be used as a defense by the contractor, and the tribunal found that the contractor breached the contract.

§2.03 CUSTOMS CLEARANCE

Delay in customs clearance of goods for overseas construction projects may cause demurrage, warehousing fees, and progress of the project on site may be delayed. In particular, delay of key equipment and facilities or materials will seriously prolong the construction period. To avoid delay in customs clearance, the following factors should be noted.

[A] Focus on Logistics and Customs Clearance in EPC Project Procurement

Logistics and customs clearance are two processes with the highest risks of delaying progress in procurement for overseas EPC projects since they are inherently uncertain and uncontrollable. We emphasize that the logistics and customs clearance cycle for most equipment and materials may well be longer than anticipated. The risks of delay in logistics are mainly caused by shipping schedules for transportation by sea, which are predictable but often uncontrollable. The risks of delay in customs clearance are caused mainly by two factors: first, complicated work procedures and inefficiency of customs authorities in the country where the project is located and into which goods are imported and second, the great variety of documents required for customs clearance. These two factors can be controlled through careful coordination and preparation in advance to mitigate the impact of work procedures and inefficiency and

to improve control of progress. In overseas projects, contractors must take initiative to set aside enough scheduled and float time for procurement and consider risks of customs clearance in procurement, carefully formulate countermeasures, prepare for customs clearance and produce equipment and materials at the same time.³¹ Particular care should be taken in obtaining and presenting documentation.

[B] Understand in Advance the Product Admittance Criteria of the Project Country

At the time of customs clearance for imported project equipment and materials, some countries and regions request contractors to provide technical certificates and certificates certifying compliance with the technical standards specified in the contract.

For example, as regards the Russian Federation: (a) as a precondition for importation, all products need to have certification of satisfaction of Russian technical specifications, and such certification must be carried out by Russian institutions. In most cases, the certificates required by the Russian government for imported products are a Technical Passport and Permit to Use issued by Rostekhnadzor. For contractors, it is a heavy burden to obtain such certificates. If they are not arranged in advance, the project progress may be seriously delayed; (b) in addition, EPC contractors will be requested to engage local design institutes in Russia (Russian Design Institute, RDI) to implement certification for SRO (Self-regulating organization) permits,³² and in carrying out certification, RDI will review and verify all design works for EPC projects. The impacts must be taken into consideration when assessing construction period and contract price. Also, it is critical to choose RDI capable in this field and experienced in cooperating with foreign contractors to avoid risks.³³

Another example is Europe, where for many industrial projects the engineering equipment used in the project needs to have CE certification.³⁴ If the contractor does not understand the product admittance criteria, the equipment cannot pass customs clearance and the contractor will also be denied access to the European market. For example, in an EPC project for a thermal power station in Turkey contracted by a Chinese contractor, since the engineering equipment transported to Turkey had not

31. Considerations on Implementation of Overseas EPC Projects written by Liu Ying, Project Management Review, Issue November to December, 2015.

32. SRO is a self-regulating organization for construction projects. In accordance with Town Planning Code of Russia, the main obligations of contractors with respect to approval and permission for construction projects are joining "SRO" which satisfy project requirements and obtain corresponding qualification certificates.

33. Key Legal Risks in International Engineering Projects in Russia, written by Gregory Jones, a practicing lawyer in England and Wales and senior associate of Pinsent Masons LLP, London office; HU Yuanhang, senior associate of Pinsent Masons LLP, a practice lawyer in England and Wales and hold a Chinese lawyer's license. This article was published in Sailing Abroad Share SA Issue No. 33.

34. CE mark is a safety certification mark regarded as the passport for manufacturers to open and enter European market. CE stands for unity of Europe (CONFORMITE EUROPEENNE). Products with "CE" marks can be sold in Member States of EU and do not need to comply with requirements in each Member State, which realizes free circulation of commodities among Member States of EU.

obtained CE certification and could not pass customs clearance, the project progress was delayed and the cooperation between that contractor and the employer broke down. Not only all equipment was returned and the contractor subject to the employer's claim for monetary damages but also the contractor was blacklisted by EU countries, which made it more difficult for the contractor to expand into the European market.

[C] Check Whether Any Special Certificate Is Required

Some countries require special certificates for customs clearance of project materials of foreign contractors.

For example, due to restrictions in Russian laws, foreign contractors may encounter difficulties in customs clearance in Russia. The customs clearance of certain goods needs approval certificates, and in practice, these certificates can only be obtained by Russian legal entities. To avoid possible delay and expense in customs clearance, it is suggested that contractors provide in the contract that the employer shall be responsible for completing the customs clearance of all goods imported into Russia, paying all customs duty/fees and obtaining all certificates required for customs clearance.

For another example, in Southeast Asia, the customs law of some countries provides that all imported M&E equipment, tools and materials shall have a factory test report, certificate of approval, necessary quality certification and other documents. A Chinese contracting enterprise won the bid for an electrical engineering project in a country in Southeast Asia. When implementing the project, in addition to permanent equipment procured under subcontracts, the contracting enterprise produced many items of construction equipment, special tools and materials, but these products did not have factory test reports, certificates of approval or quality certification by designated institution. When the permanent equipment and construction equipment tools and materials arrived at the port of that country, the customs clearance could not be completed and the goods could not be released. Prior to the aforesaid reports being obtained and certification formalities being completed, all the equipment tools materials were held at the port, for which the contracting enterprise paid high demurrage fees and fines. Further, the construction period was seriously affected.³⁵

[D] Try to Avoid Customs Clearance in Any Red Light Period

To export project materials to host countries, contractors should avoid customs clearance in any "red light period." For example, Indonesian customs are well known for strict control on customs clearance. However, generally speaking, December in each year to March in the next year is a particular "red light period" for customs

35. Excerpt from "Risks in Overseas Operation by Chinese Engineering Contractors—Analysis Based on Risk Cases", written by China Association of International Engineering Consultants. Please refer to <http://caiec.mofcom.gov.cn/article/jingmaotongji/201705/20170502567422.shtml> as of March 2, 2018.

CHAPTER 3

Risks of Project Stakeholders

International projects usually involve multiple stakeholders, including employers, contractors, suppliers and subcontractors. Often, the project stakeholders have differing priorities and agendas, and such tensions may affect the outcome of the project. Throughout the duration of a project, the risks associated with stakeholders' differing priorities and agendas may lead to project cost increase, project delays and even losses. Chinese firms operating in the construction space are often responsible for the failure of projects. They need to improve their management skills and get familiar with the norms, practices and operating methods in local markets in order to effectively manage the risks associated with project stakeholders' differing priorities and agendas. Knowing the game rules well is vital to success.

3.1 CREDIT AND MANAGEMENT LEVEL OF EMPLOYERS

Chinese contractors win overseas projects usually through competitive bidding. The leading role played by employers in public bidding naturally puts contractors in an unfavorable position during the project execution. In addition, Chinese contractors are often involved in EPC projects which use the 1999 edition of the FIDIC Silver Book as a template. As a typical "pro-employer" form of contract, the Silver Book places most of the risks on contractors. Since an employer typically owns the project and awards the engineering contract, its credit and management level determines whether the project will be a success or not.

From previous experience, Chinese contractors typically have to deal with the following types of risks because different stakeholders often have different priorities and agendas.

[A] Transferring Risks to Contractors in Contract Conditions

Employers in international construction projects are often in a strong negotiating position. When drafting a contract, it is natural for a contracting party to introduce terms which protect its interests and reduce its risks, at the expense of its counterparty's rights and interests. The strong negotiating position that employers enjoy means that very often they are able to delete standard contract terms that are beneficial to contractors, and to unreasonably transfer the risks that are to be undertaken by employers, given their acquaintance with the political, economic and natural conditions in the host country.⁶² When contractual rights and obligations are skewed in this way, disputes often arise that may culminate in project failures.

In most international construction projects undertaken by Chinese enterprises, the employers are usually the government of the host country, state-owned enterprises or private enterprises. With years of engineering practice, many employers have accumulated rich experience in contract design. For example, the unique natural resources and geographical conditions of countries in South Asia attract numerous international contractors. Consequently, contractors from a few developed countries have entered the engineering market in South Asian countries as early as the 1950s. The public procurement department of the said countries, based on years of experience in claims and counterclaims in international projects, has made targeted adjustments and revisions of standard contract documents to eliminate what are perceived as contractual defects which give contractors better chances of success when making claims. In addition, a series of factors increase the risks borne by the international contractors when performing a contract. For example, the employer adds terms in the project contract such as terms which oblige the contractor to execute the instructions of the engineer, including changes to the work program, immediately after receiving such instructions, notwithstanding that the engineer and contractor may not have reached a consensus on the new price of the project. Such contractual provisions encourage the employer to be tardy in approving price changes in case of variations. After completion of the project, the price approved by the employer is vastly lower than the actual cost incurred, causing losses to the contractor.⁶³

An employer who is able and intent on skewing contract provisions against a contractor is surely a serious risk to the contractor. The "contract trap" designed by the employer aims at elaborately "setting up" the contract in such a manner that the contractor assumes maximum risk while the employer assumes minimal risk. The common contract traps take the form of one-sided text description, vague language and deletion of necessary procedural protections. In order to reduce or avoid risks and losses, a contractor must pay attention to contract appraisal and risk identification before signing a contract.⁶⁴

62. Zhao Pixi, "Key to Contract Review—Risk Identification", *International Project Contracting & Labour Service*, 2018 (3).

63. Liu Zeqin, "Common Contractual Risks in Nepal International Projects", *International Project Contracting & Labour Service*, 2017 (3).

64. Zhao Pixi, "Key to Contract Review—Risk Identification", *International Project Contracting & Labour Service*, 2018 (3).

Employer's Payment

The primary purpose of project contracting is profit. Any risks or problems affecting an employer's fulfillment of its payment obligations will negatively influence the project.⁶⁵ According to Article 2.4 [Employer's Financial Arrangements] in the 1999 edition of the *International Project Contracting Handbook*, the employer, after receiving the contractor's request, shall provide sufficient evidence proving his financial arrangement and such arrangement shall be continuously maintained so that the employer will be able to pay to the contractor according to the contract provisions. This article emphasizes the employer's obligation of guaranteeing payment to the contractor. In practice, however, the employers of government projects are reluctant to provide such evidence of financial arrangement to the contractor. The employer usually deletes this article, and the contractor's interests cannot be protected.

Most Chinese contractors' businesses are located in developing countries or regions. The economy of the host country may be such that the employer cannot provide sufficient funds due to difficulty in financing. This leads to high probability of default by the employer in relation to its payment obligation. Alternatively, there may be institutional or legal constraints on the employer's ability to meet its payment obligations as and when they fall due. A case on point is a government project in an Asian country ("country A") funded by a bank loan agreement signed between China and country A. The financial support offered by the local government was limited to the loan amount, which did not include the employer's proprietary fund. As it transpired, a series of changes occurred during construction and the accumulated cost increased by about 10% of the original contract price. While the bid price was USD 150 million, it is estimated that the final contract price will be in the order of USD 180 million (including the approved changes, the subsequent possible changes and the contractor's claims). Although the employer probably has access to other sources of financing, the increase of a project budget is regulated by the Public Procurement Law and relevant regulations, which stipulate elaborate and time-consuming procedures for increasing a project budget, including a requirement that the cost increase should be incorporated into the national construction budget and approved by the legislature. The contractor may suspend construction according to the contract, but the problem still remained.⁶⁶ In this project, the employer was willing to pay but lacked the ability to pay within a reasonable time due to objective factors, which puts the contractor in a dilemma. In practice, the employer's ability to pay is a key factor which needs to be considered by the contractor while preparing the proposal.

Besides, contractors must also pay close attention to the payment terms in the contract to avoid the risk of employers' nonpayment due to loopholes in the contract. Another case in point involves an African project with loans offered by the World Bank. The contract made no specific provision for the timing of the advance payment, putting

65. Liu Junying, Li Zhiyong, "Risk Management of International Project", China Architecture & Building Press, 2013.

66. Yang Yunkai, "Case Analysis: Prepayment and Change Risks in International Projects", *Journal of International Economic Cooperation*, 2015 (2).

the contractor at risk of delayed payment. According to the contract, the completion date was August 25, 2004. The contractor provided advance payment guarantee on August 9, 2004, and the employer paid the installments of advance payment on August 17, September 3, September 4 and November 5 of the same year. The contractor believed that according to the contract, it ought to have received all advance payment as start-up fund immediately after signing the contract. The contractor then initiated a claim against the employer for interests due to delayed payment. The resident engineer disapproved the claim for the following reasons: (1) there was no provision in the contract which specified a time for making the advance payment at any reasonable time was acceptable, and there was no payment default in the contract which stipulates that interest will be paid for delay in making the advance payment; (2) the provisions on interests for delay in making the advance payment in the contract only applies to the interim payment and cannot apply to the advance payment since interim payment and advance payment are two different things. The two parties failed to settle the dispute and submitted it to the dispute settlement committee. The committee presumed that the advance payment guarantee provided by the contractor on August 9 satisfied the preconditions for the employer to make advance payment on August 10 according to the provisions on preconditions for advance payment in paragraph 60.7 of the project contract. According to paragraph 60.8 of the contract, the contractor shall receive the interim payment within 42 days after submitting the interim payment request and the employer shall be obliged to pay interests to the contractor in case of delayed payment. As for the counterclaim made by the engineer that advance payment was different from interim payment, the committee considered that advance payment is a kind of interim payment due to its inherent characteristics, although this is not clearly prescribed in the contract. According to the final verdict, the employer shall make advance payment within 42 days from August 10 and shall pay interests for delay. This case reflects the importance of specifying terms and time of payment in the contract. Where the employer defaults its advance payment obligation, express contractual terms increase the contractor's chances of success when it commences a claim to protect its interests.

[C] Employer's Credit Risk

Employers in international projects often enjoy a favorable position arising from the instruments provided by contractors to secure advance payments.

A case in point shows how an employer can abuse the leverage afforded it by the advance payment security instruments. In 2010, a Chinese contractor undertook a homeless shelter project promoted by a company in "country A." The contractor applied to the bank for advance payment guarantee and performance guarantee in favor of the employer. By the end of 2013, the Ministry of Labor in country A had changed its policy in relation to illegal immigrants from a policy of sheltering them to a policy of repatriating them. Consequently the project was terminated. At the time of termination, the contractor had received about USD 7.2 million advance payment from the employer. The contractor initiated a claim against the employer for USD 13.1

However, the employer recognized only about USD 2.8 million as payable to the contractor. Since the advance payment guarantee provided by the contractor was about to expire, the employer requested the contractor to immediately return the advance payment of USD 4.4 million advance payment, failing which the employer would cancel the advance payment guarantee. The employer also requested the contractor to sign a written agreement to waive its claim as a precondition for returning the advance payment guarantee and performance guarantee. However, the contractor thought that the project was slowed by the employer's delay in making the advance payment, the amount of USD 2.8 million recognized as payable by the employer to the contractor was not the amount of the amount due to the contractor and about USD 2.1 million worth of work completed by the contractor had not been recognized as payable by the employer to the contractor. In the above situation, the contractor suggested that the advance payment guarantee be extended so that the two parties could negotiate a settlement of the dispute. The employer turned down the suggestion. Given that the advance payment guarantees held by the employer were on-demand, it was easy for the employer to make a demand on the guarantees. The contractor could try to obtain a restraining order from the court, but the process would be long and probably complicated. Further, if the contractor had to sue on the guarantees, the contractor would suffer economic loss and a decline in its credit rating. The two parties subsequently reached an agreement by which the contractor returned the sum of the advance payment claimed by the employer and signed a memorandum of understanding on claims with the employer. In this case, the employer threatened the contractor with its potential demands on the guarantees which put pressure on the contractor and constrained the contractor to accept unreasonable conditions.⁶⁷

Currently, most guarantees involved in international projects are on-demand guarantees. If the employer fails to act in good faith and demands the guarantees to be returned, huge risks and losses will occur to the contractor. In practice, the employer's credit status may impose risks on the contractor, so the contractor should review the employer's credit during the bid process.

(ii) Employer's Excessive Interference

Contractors are responsible for EPC in international EPC projects. Compared with DB (Design-Build) projects, EPC projects, generally speaking, give more independent choices to the contractor in engineering and construction. According to our survey, employers' day-to-day management and control of the project have been increasingly severe in the past five years. In order to seek advantages, employers excessively interfere with the project construction, leading to many variation instructions and even delay and cost increase, which the employer is often reluctant to assume responsibility for. Under such circumstances, it would be difficult for the contractor to claim for compensation. Some employers delay approving the claim documents submitted by

⁶⁷ Zhang Qian, "Discussion on Risk Prevention in Guarantee Management Based on an International Project Case", *Practice in Foreign Economic Relations and Trade*, 2017 (5).

