

Construction Arbitration in the Baltic States (Lithuania, Latvia, Estonia)

Dr. Rimantas Daujotas

PhD Scholar, Queen Mary University
Senior Associate at Motieka & Audzevičius PLP
Gyneju st. 4, Vilnius, Lietuva
www.rdaujotas.com
Email: rimantasdaujotas@gmail.com

Introduction

Construction sector is a critical element in every country's economic development. It includes exploration of traditional resources such as oil, gas and coal as well as a growing emphasis on construction of renewable sources of energy and transportation. In many cases, including the Baltic States, a substantial proportion of civil engineering construction output is generated by state-funded construction projects, and by incentives rolled out by companies in energy industry.

It is worth exploring briefly why construction arbitration is becoming the method of choice for resolving disputes for the construction industry. There are essentially two reasons: neutrality and enforcement. International projects provide unique difficulties and Lithuanian, Latvian or Estonian projects are no exception. There are "foreign" regulatory and employment issues to face. Procurement of plant and materials is different. Taxes and customs may reduce margins. Then, of course, there is the prospect of serious disputes arising on the project and the worrying thought that those disputes will be governed by a foreign law and will be determined through litigation in a foreign court. There is a natural fear of any court, more so, a foreign court. That is not to say that Baltic courts are routinely biased in favour of the local party but, when a risk analysis is being undertaken, most contractors would not wish to take the risk that a foreign court will decide whether it should be paid for work undertaken in a foreign country. The presence of an international arbitration tribunal is often vital. As well as neutrality, there is enforcement. Arbitral awards in the Baltic States may be enforced by virtue of the 1958 New York Convention.

The combined impact of neutrality and enforcement of arbitral awards ensure, in the international context, that arbitration will remain the dispute resolution method of choice for the majority of international projects, including ones developed in the Baltic States.

Although it is impossible to generalize about construction arbitration trends in the Baltics because of the lack of concrete statistical data, however, along with foreign investment, interest in

arbitration in the Baltics is growing. Many jurisdictions have ratified the New York Convention and adopted modern arbitration legislation. This note provides an overview of some of the recent trends in construction arbitration related to the Baltic States.

The contractual models

In the Baltics, the government-targeted and EU financed programmes aimed at modernising transport, energy and social infrastructure have played an important part in the construction industry's evolution in recent years. In addition, a steady increase in real disposable personal incomes has supported a steady improvement in residential construction.

It must be first mentioned that the use of standard conditions for construction projects is not typical in the Baltic States. This is due to complicated regulations in the field of construction and, at the same time, lack of uniform templates which would be valid under the local law and at the same time would comply with market practices. Parties generally prepare and negotiate contracts for each specific situation, and specialized companies have their own templates. Standard forms of construction contracts are mainly used for projects involving the state. Such forms usually refer disputes to state litigation (commercial courts).

Secondly, because of the wide variety of projects and participants, Baltic construction projects involve a broad and diverse range of commercial agreements. Energy projects often involve a licence from the government and require contractual arrangements between a government (or a state-owned entity, such as a national energy company) and a private company (or a group of companies). Some of Baltic construction projects also involve the creation of joint ventures to share the risks and costs associated with large-scale endeavours, or to meet regulatory requirements.

Most large projects necessarily involve other contracts as well. For example, there may be contracts with local and foreign companies to act as consultants, for the supply of goods and services, and the construction or use of facilities and equipment. Given the variety of agreements and parties involved in these projects, and their scale and complexity, a wide range of issues can arise between some or all of the parties. The likelihood of disputes is often also increased by the existence of political, environmental and security issues. Some of the many disputes that have arisen include issues concerning non-payment of invoices and royalty fees; delays, disruptions and cancellations (including force majeure claims); shareholder and joint venture disputes; disputes about the scope and transfer of rights; and issues about price as well as price adjustment claims in long-term supply contracts.

Lithuania

Construction law

The Law on Construction establishes all essential requirements for construction works which are being built, reconstructed and repaired within the territory of the Republic of Lithuania, and *inter alia* the minimum requirements for energy performance of buildings. The Lithuanian Law on Construction was first published on March 3, 1996 and last amended on 1 January 2017. The construction process is also regulated by technical construction acts: technical construction regulations, construction rules, technical certificates and methodological recommendations.

It is quite common practice for foreign contractors to enter into joint ventures with Lithuanian legal entities. The main reason is that Lithuanian contractors are fully informed about the legal and administrative issues regarding the project. Usually, there are no standard forms in use. There are no specified limitations when owners are private persons or private companies. For public entities there is a public tender process. General conditions of such contracts are stipulated by decisions of the director of the Public Procurement Office, but these forms are not obligatory and in certain conditions can be changed by the contracting authorities. It should be noted that the use of the standard-contract forms created by the International Federation of Consulting Engineers (FIDIC) has increased in recent years.

Changes in 2017

The new wording of the Construction Law prescribes shorter deadlines for the issuing of the terms and conditions of special requirements and connection to engineering systems. Special requirements will no longer be necessary on mandatory basis. These changes provide builders with the discretion to measure if these requirements are necessary to them at all, yet building projects still have to conform to the relevant requirements of laws and legislation as well as normative construction technical documentation.

The simplified procedure of building completion will apply not only to one- and two-flat houses and appurtenances thereof, but to other special and ordinary structures from the list drawn by the Minister of Environment of the Republic of Lithuania that do not have a material environmental or social effect. This will singularly accelerate the construction completion procedure.

Both the red tape and time needed to process planning and building permits have been significantly reduced. Instead of 16 state authorities ruling on a construction project's compliance with legal and environmental requirements, since 1 January a maximum of 10 authorities are involved in the process. The time for the receipt of the building permit has been decreased by approximately 50%. Thus, the documents required to commence construction should now be issued within 20 business days for special purpose construction projects and within 10 for all other construction projects.

One of the major new things about the new Construction Law is that the builder and the contractor will be required to guarantee the indemnity of the costs to remedy any defects as may be attributable to the contractors for the amount that, over the defects liability period, may not be less than 5 per cent of the construction cost of the building.

Arbitration

In Lithuania, the main institution of trying court disputes of the members of construction process are considered to be the courts of general competence. Court dispute resolution methods of the members of construction process frequently stimulate to choose a typical form of agreements used in construction processes as well, which generally specifies that „disputes originating shall be resolved in court“ or „disputes originating shall be resolved in the order specified in the laws of the Republic of Lithuania”.

However, according to the Vilnius Court of Commercial Arbitration (VCCA) statistics, from 2010 to 2016 the most common type of arbitrated disputes arose from trading, construction and engineering, finance, insurance contracts and contracts for services.

Article 11 of the Lithuanian arbitration law provides a list of non-arbitrable disputes, and there are limitations to the arbitrability of disputes where one of the parties is a state or municipal company. The prior consent of the state or the body that established such party is required.

As for adjudication, in Lithuania adjudication is an accepted form of dispute resolution with regard to construction contracts, but are rarely used. If the parties agree to adjudication in order to resolve their dispute, these proceedings will become a mandatory first step for the parties to solve their dispute before they are allowed to submit the dispute to court or arbitration. Various steps and rules of adjudication proceedings may be agreed by the parties. The main steps include initiation, investigation and actions after the decision is issued. The investigation can itself consist of various stages such as the construction site visits by the adjudication board, a request for the parties to provide copies of all documents related to the dispute, hearings, and separate investigations of facts or circumstances or requests for the experts to provide opinions on specific facts or circumstances.

After the decision is issued, and if parties have agreed that the decision is binding, they must submit a notice of dissatisfaction with the decision before the deadline. Even if the parties have agreed that the decision issued by the adjudication board will be binding, the decision is not final and can be referred to arbitration or court for final resolution.

There are also other types of proceedings similar to adjudication, where public authorities are involved on a mandatory basis. They resolve disputes (i.e. ascertain important circumstances and facts) which are related to public 'authorities' actions (e.g. permission to build) or are deemed to be in the public interest (e.g. inspection after a constructed building has collapsed, etc.).

Latvia

Construction law

The newly adopted Construction law of Republic of Latvia came into force on the 1st of October 2014. This law brought major changes to the field of construction. Henceforth the next (second) phase of construction process, after handing in an appropriate construction intention and a building design in a minimum composition (first phase), is going to be the receipt of a construction permit. Instead of three decisions – to issue the architecture and planning assignment, to accept the building design, to issue the construction permit – the building authority is going to have to take only one decision – to issue the construction permit.

Nevertheless receipt of the construction permit is not going to be a sufficient ground to start the construction works. Firstly, society has to be informed about receipt of the construction permit by putting out a construction board on the land on which the construction works are planned.

Furthermore the construction works can only be started when the conditions included in the construction permit are accomplished, appropriate building design is constituted and a mark is made in the construction permit about the fulfilment of the aforementioned actions. The decision of the building authority on handing out the construction permit can be disputed in the term of one month from the day when the decision has come into force. This term can be renewed by the court if it ascertains that the informing of society about the construction permit has been clearly insufficient.

When the building authority has made a mark in the construction permit about fulfilment of all the included conditions, the construction permit has become incontrovertible and the construction work can be started. Building processes that were started before the 1st of October 2014 have to be finished in the order set in to General Construction Regulations.

By the entry into force of the Construction law, many other regulations came into force as well as lapsed, others were replaced with new regulations. The new law introduces the state control office of construction which is a substitute to the liquidated State construction inspectorate. Moreover, the new law specifically regulates the competence of the participants of construction process, widely regulates the fields of responsibility, as well as significantly changes the process of construction.

Arbitration

Reputation of arbitration in Latvia has been questioned due to ‘pocket arbitrations’, in which arbitration institution established by one of the parties to an agreement (or its affiliated entity) administers the resolution of disputes which arise from an agreement, negatively affecting the neutrality and fair treatment of a dispute.

The *Saeima*, the Latvian parliament, has tried to improve the situation for a number of times. On 11 September 2014, the *Saeima* adopted new Arbitration Act, which came into force on 1 January 2015. However, the new Arbitration Act is not based on the UNCITRAL Model Law. In its essence, it is just an extraction from the Latvian Civil Procedure Law: a chapter containing provisions on arbitration, which was previously encompassed by the Civil Procedure Law, was extracted into a new legislative instrument, i.e. the Arbitration Act, leaving in the Civil Procedure Law only those provisions which prescribe court's duties in relation to arbitration.

The main aim of the Arbitration Act was to establish more specified requirements for arbitrators, and a procedure for the establishment of arbitration institutions. Drafters hoped that introduced requirements would reduce the number of arbitration institutions and would improve the quality of the arbitration procedure.

Adjudication procedures are not regulated by statute in Latvia, but parties can agree within the construction contract to use an adjudicator (an independent expert). Either party is entitled to refer a dispute arising under the contract in accordance with the provisions of the contract. Such terms are usually included in big construction contracts and/or where FIDIC contract are used (in which adjudication provisions are already provided), in which it is necessary to provide an interim solution to a dispute in order to maintain cash flow through the supply chain.

Estonia

Construction law

Requirements for construction in Estonia were enacted in the Building Act and Estonia's new Building Code entered into force on July 1, 2015. The Code gathered building regulation, previously scattered across different laws, into one place. Codifying building law has been a long process: work started in 2008 and the Code was adopted in February of 2015.

The Building Code consists of a general and a special part, although there is no "special part" heading in the Code itself. The general part gives basic guidelines and requirements for buildings. This is one of the main advantages of the Code because most of these provisions were previously divided between different laws or were, in some cases, non-existent. The special part deals with special buildings and their different requirements and determines who exercises supervision over building regulation.

Permit procedures became more efficient with entry into force of the new Code. Under the new Code, the requirement is either to file a notice regarding construction work or apply for a building permit, depending on the size of the building. Furthermore, certain smaller buildings do not require notification at all, which simplifies building for private persons.

The procedure for filing a notice regarding construction work is free of state fee, which reduces the workload of administrative bodies. The time span for building permit procedures shortened

because it will now take place in the building register and the administrative body has 10 days to decide whether or not to issue a permit, which will speed up the process. Third persons (e.g. neighbours) affected by the permit can also file objections during this timeframe. This means that it is very important to notify these persons in good time because they have limited time to express their opinions.

The new Code specifies situations requiring an application for design specifications. These are architectural and structural specifications set by the local authority in respect of a particular construction project. Under the former regulation, design specifications were always mandatory if there was no detailed spatial plan. Under the new Code, design specifications are only needed when constructing or expanding a building requiring a building permit or if there is no requirement to prepare a detailed spatial plan. Thus, the new Code significantly reduces the situations in which applying for design specifications is necessary.

Arbitration

Arbitration falls under the regulations of the Civil Code of Procedure in Estonia. The main sections referring to arbitration are Sections 712 to 757. According to the Civil Code of Procedure an arbitration agreement may be concluded as a separate contract or as a separate clause in a contract. It must also be noted that according to EU regulations Article 717 in the Civil Code has been amended in order to avoid the interpretation of arbitration agreements.

Arbitration procedures in Estonia are conducted by the Court of Arbitration of the Chamber of Commerce and Industry. It may rule in disputes from private law relations, foreign trade and international business disputes, as well as construction disputes. The arbitration procedure will be confidential and the Estonian Court of Arbitration will not disclose any information without previous consent of both parties. The Arbitration Court in Estonia will accept to conduct the mediation of a dispute based on a written agreement, if both parties have agreed that the dispute will be resolved by the arbitration court and if the dispute falls under its jurisdiction.

On 1 January 2010 the Conciliation Act took effect which, for the first time in Estonia, regulated by law the activities of private conciliators (mediators; the regulation combines both methods). The Estonian Bar Association has registered attorneys working as conciliators (mediators).