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Group Publisher
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Published by
Global Legal Group Ltd.
59 Tanner Street
London SE1 3PL, UK
Tel: +44 20 7367 0720
Fax: +44 20 7407 5255
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Serbia

Uroš Marković

Ivan Petrović

JPM Janković, Popović & Mitić

1 Making Construction Projects

1.1 What are the standard types of construction contract in your jurisdiction? Do you have contracts which place both design and construction obligations upon contractors? If so, please describe the types of contract. Please also describe any forms of design-only contract common in your jurisdiction. Do you have any arrangement known as management contracting, with one main managing contractor and with the construction work done by a series of package contractors? (*NB* For ease of reference throughout the chapter, we refer to "construction contracts" as an abbreviation for construction and engineering contracts.)

The Serbian Law on Contracts and Torts defines construction contracts as the agreement between the investor and the contractor whereby the contractor undertakes to develop the building according to a specified design, within a specified deadline and on a specified location, and the investor undertakes to pay the price to the contractor.

The types of construction contracts are not explicitly prescribed by the law.

The types of construction contracts, based on "price defining" criteria may be:

a) Fixed-price contracts (in which the contractor guarantees for the calculation of the volume and type of works).

b) Non-fixed price contracts (whereby the contractor provides only the price of the work and material).

The types of construction contracts based on "volume of works and price" criteria may be:

a) Turn-key contracts (whereby the contractor provides the overall sum for completion of works).

b) Unit price contracts (whereby the contractor provides the price of work/material per each part of works without specification of quantities).

In recent practice, parties agree on FIDIC contracts, mainly Red Book and Silver Book.

Serbian legislation does not define design-only contracts. In practice, investors and designers define their rights and obligations through the agreements whereby the designers undertake to create a main design and obtain a construction permit for the development of the building in accordance with request of the investor. Prior to obtaining a construction permit, the designer has to execute an independent official control of the main design, and remains liable for deficiencies in design.

Regardless of the definition of the construction contract, which implies that the investor has to provide the design to the contractor, the contractors occasionally undertake both to create a main design and to execute construction works. Design and Build contracts impose a high level of responsibility to the contractors, which includes liability for omissions in designs and construction works.

The obligation of the creation of designs during construction, such as execution design, as-build design, workshop drawings and similar, is, commonly, undertaken by the contractors.

According to the Serbian Law on Spatial Planning and Construction, the investor has to engage the main contractor for the execution of construction works. Unless provided otherwise in the agreement, the main managing (general) contractor is authorised to engage subcontractors for execution of part of the works to a third party. In such cases, the main contractor is considered as responsible to the investor as well as officially responsible for acting in accordance with official obligations arising from construction prescribed by the Law on Spatial Planning and Construction (such as health and safety at work, responsibility for executing of the construction in accordance with design, obligations on keeping accurate construction site records, etc.). Due to the numerous official responsibilities of the main managing (or general) contractor, which cannot be transferred to subcontractors, contractors avoid entering into main managing agreements.

In practice, some employers engage project management companies, but general contractor agreements are still concluded between the employer and the contractor directly, while the project management company only has a supportive and/or supervising role during the construction.

1.2 Are there either any legally essential qualities needed to create a legally binding contract (e.g. in common law jurisdictions, offer, acceptance, consideration and intention to create legal relations), or any specific requirements which need to be included in a construction contract (e.g. provision for adjudication or any need for the contract to be evidenced in writing)?

The Serbian Law on Contracts and Torts considers that the agreement is concluded when the consent on essential elements of the agreement is reached (i.e. intention to create legal relations) in the form requested by the law.

Essential elements of the construction agreements are the works (building and location), the design, the deadline, and the price. The Law on Contracts and Torts prescribes the written form as the obligatory form of construction agreement.

The construction agreement is considered as concluded after the investor and the contractor agree on the construction works according to the design, deadline, and price in written form.

1.3 In your jurisdiction please identify whether there is a concept of what is known as a "letter of intent", in which an employer can give either a legally binding or non-legally binding indication of willingness either to enter into a contract later or to commit itself to meet certain costs to be incurred by the contractor whether or not a full contract is ever concluded.

According to Serbian Law on Contracts and Torts, the employer may provide a potential contractor with an "offer" which should include essential elements of the construction contract (design, construction works, deadlines, and price). If the potential contractor provides the employer with the statement that the offer is accepted, the contract is considered as concluded under the terms stipulated in the offer. Both the offer and the statement of acceptance must be in written form.

The concept of non-legally binding offers with commitment of an employer to meet certain costs to be incurred by the contractor, whether or not a full contract is ever concluded, does not exist in the Serbian jurisdiction. However, the Serbian Law on Contracts and Torts recognises the right of compensation of the damages to the party which enters negotiations with another party that does not intend to conclude the agreement, or if that party withdraws from negotiations without reasonable grounds.

In more complex procedures, when the employer organises bidding in order to choose the best offer, the employer provides potential contractors with the design and other data on the further contract and invites them to make offers for the price. In such cases, invitations to bid usually include the provision that the employer is not obliged to conclude the contract and that potential contractors are not authorised to request any compensation for the costs incurred during preparation of the offer for participation in the bidding procedure.

1.4 Are there any statutory or standard types of insurance which it would be commonplace or compulsory to have in place when carrying out construction work? For example, is there employer's liability insurance for contractors in respect of death and personal injury, or is there a requirement for the contractor to have contractors all risk insurance?

a) Professional liability insurance

According to the Serbian Law on Spatial Planning and Construction, the designers and contractors may be legal entities registered with the relevant registry. The legal entity which creates the main design or executes the construction works must have an employee who holds a licence as the responsible designer or responsible contractor, respectively.

Licences held by the responsible designers and responsible contractors are assigned by the Serbian Chamber of Engineers, which obtains professional liability insurance for its members.

b) Death and personal injury insurance

Death and personal injury insurance is the statutory insurance prescribed by the Serbian Law on Health and Safety at Work. Each company has to insure its employees against injuries, occupational illness, and illnesses arising from work.

According to the law, each company is responsible for its employees. In construction contracts, the employer cannot be held liable for the death and injuries suffered by a contractor's employees.

c) All risk insurance

It is usual practice in Serbia for the employers to request that the contractors provide an all risk insurance policy. In some cases, the employers request that the contractors allow them to pay insurance premiums for contractors all risk insurance directly to the insurance company, and deduct the amounts paid for premiums from the price.

1.5 Are there any statutory requirements in relation to construction contracts in terms of: (a) general requirements; (b) labour (i.e. the legal status of those working on site as employees or as self-employed sub-contractors); (c) tax (payment of income tax of employees); or (d) health and safety?

Statutory requirements which must be included in the construction contract are essential elements of construction agreements and written forms of the agreement.

Statutory requirements related to construction, which are not related to the contractual relationship between the employer and the contractor, are prescribed by other laws. It is common that the employer agrees with the contractor on the fulfilment of the contractor's obligations arising from construction laws, labour law, tax laws, and health and safety laws. In such cases it is agreed that the employer has the right to penalise the contractor or, in some cases, terminate the contract, in the case of non-compliance of the contractor with respective obligations.

With regard to a): labour laws are applied to both the contractor and the employer whereby each party keeps the responsibility for its employees. Employers commonly request that the construction contract includes the obligation of the contractor to act in accordance with labour laws.

Regarding b): payment of taxes and other labour charges for employees is the responsibility of the contractor, i.e. each party is responsible for its employees. Employees of the contractor are not authorised to claim payments from the employer.

With regard to c): the Law on Health and Safety at Work is applied to both the contractor and the employee, whereby each party keeps the responsibility for its employees. In the case of there being two or more contractors at the same construction site, or when the contractor engages sub-contractors which are present simultaneously with the contractor, an independent coordinator for health and safety at work must be provided either by the employer or by the contractor.

1.6 Is the employer legally permitted to retain part of the purchase price for the works as a retention to be released either in whole or in part when: (a) the works are substantially complete; and/or (b) any agreed defects liability is complete?

Serbian legislation does not forbid arrangement whereby the employer is entitled to retain part of the price as collateral for completion of works and/or removal of defects during warranty period.

It is common practice that retention is agreed between the parties. In most cases, the contractor is authorised to change the defects liability retainer with another type of collateral (e.g. a bank guarantee).

1.7 Is it permissible/common for there to be performance bonds (provided by banks and others) to guarantee performance, and/or company guarantees provided to guarantee the performance of subsidiary companies? Are there any restrictions on the nature of such bonds and guarantees?

Performance bonds are common in Serbian construction contract practice. The contractors usually provide a performance bank

guarantee to the employer for the amount of 10% of the price. The wording of the bank guarantee is, usually, one of the appendices to the construction contract.

In rare cases, other types of collaterals, such as promissory notes or mother company guarantees, are agreed as collateral for performance.

Promissory notes do not provide certainty of collection, since they cannot be collected in cases where the debtor does not have the funds in its bank accounts.

Company (or corporate) guarantees do not exist in the Serbian legal system, but are sometimes used as collateral. However, corporate guarantees neither expedite nor facilitate the collection of the due amount.

1.8 Is it possible and/or usual for contractors to have retention of title rights in relation to goods and supplies used in the works? Is it permissible for contractors to claim that until they have been paid they retain title and the right to remove goods and materials supplied from the site?

In general, retention rights are recognised by Serbian legislation as the pledge over the property of the debtor which is in possession of the creditor, provided that such property came into possession of the creditor on a valid legal basis and that the debt is due.

The creditor, having the property in retention, is authorised to sell such property and collect the due debt from the price.

The contractor is allowed to retain the goods and materials belonging to the employer as the pledger, in cases where a there is a due claim of the contractor against employer.

However, according to existing court practice in Serbian courts, in cases of construction contracts, the contractor is not granted retention rights over the building due to the specific legal nature of the pledge over immovable property, i.e. mortgage (registration of the mortgage in the public real estate register). In this respect, after the goods and materials are used by the contractor and incorporated into the building, the contractor no longer has retention (to keep the building and sell it) rights over such goods and materials. In Serbian legal theory, some hold the opinion that the contractor has the right to retain the building (i.e. refuse to hand over the possession over the building), but does not have the right to sell the building and collect the due debt from the sale price.

2 Supervising Construction Contracts

2.1 Is it common for construction contracts to be suspended on behalf of the employer by a third party? Does any such third party (e.g. an engineer or architect) have a duty to act impartially between contractor and employer? Is that duty absolute or is it only one which exists in certain situations? If so, please identify when the architect/engineer must act impartially.

In cases where a third party, such as an engineer, is appointed by the employer for the purpose of supervising the execution of construction works, such party is authorised to act on behalf of the employer when relating to the actual execution of the works (quantity, quality, types), and meeting the agreed deadlines.

In practice, the role of the engineer is in solely supervising the execution of the works and informing the employer on matters of progress and other events on the construction site. The engineer is, usually, not authorised to suspend the construction contract, except in cases of emergency.

Since the engineer is engaged by the employer, on the basis of a separate agreement, it is considered that the engineer cannot act impartially, e.g. in favour of employer. Therefore, regardless of an obligation of the engineer to act impartially, any of the decisions of the engineer can be challenged before the court/arbitration, and the court/arbitration may render a different decision. However, decisions by the engineer can be used for the temporary resolution of the dispute between the employer and contractor, until the rendering of a court/arbitration decision. Also, the decisions made by the engineer may be used as proof before the court/arbitration.

2.2 Are employers entitled to provide in the contract that they will pay the contractor when they, the employer, have themselves been paid; i.e. can the employer include in the contract what is known as a "pay when paid" clause?

"Pay when paid" clauses can be interpreted as: i) a condition precedent for payment whereby the contractor assumes risk of payment from the employer; or ii) a timing mechanism for payment.

According to the Law on Contracts and Torts, a condition precedent may affect only the validity of the contract (after the fulfilment of a condition precedent the contract becomes legally binding), but cannot affect the existence of the obligations of only one contracting party. In this respect, agreeing on "pay when paid" clauses as a condition precedent for the constitution of payment obligations of the employer is not possible.

If a "pay when paid" clause is agreed as the time of starting the deadline for payment (timing mechanism), the contractor would still be authorised to request from the court a reasonable deadline for payment regardless of the existence of this provision.

Provisional "pay when paid" clauses could seriously affect one of the main principles of the Law on Contracts and Torts: equivalency of remunerations, in cases where this clause is considered as a condition precedent, and also if the clause is considered as a timing mechanism.

Other provisions of the Law on Contracts and Torts provide the possibility of pledging and the assignment of claims. Such arrangements may create a legal situation similar to that of "pay when paid" clauses. The employer may pledge its claim against a third party and/or assign such claim to the contractor instead of payment of the price.

2.3 Are the parties permitted to agree in advance a fixed sum (known as liquidated damages) which will be paid by the contractor to the employer in the event of particular breaches, e.g. liquidated damages for late completion? If such arrangements are permitted, are there any restrictions on what can be agreed? E.g. does the sum to be paid have to be a genuine pre-estimate of loss, or can the contractor be bound to pay a sum which is wholly unrelated to the amount of financial loss suffered?

According to the Law on Contracts and Torts, the party in default is obliged to compensate the damages to the other party arising from the default.

In construction agreements, it is common that the parties agree that the contractor shall pay a contractual penalty to the employer in the event of (i) non-fulfilment of its obligations, and (ii) delay in fulfilment of its obligations.

In the event of a non-fulfilment of contractual obligations by the contractor, the employer is entitled to request either the fulfilment of obligations (finalisation of construction), or a contractual penalty. In the event of a delay by the contractor, the employer is

entitled to request both fulfilment of contractual obligations and a contractual penalty.

The employer is authorised to request the full amount of penalties in any case, regardless of the damages it has suffered due to default/delay of the contractor.

In cases where the damages an employer suffers due to non-fulfilment or a delay by the contractor exceeds the agreed amount of any contractual penalties, the employer is entitled to request the difference.

The contractor is authorised to request a reduction of the penalties in cases where the penalty is disproportional to the amount and significance of the subject of obligation. In construction practice, it is considered that 5% of the contracted sum is a reasonable amount for a contractual penalty for delays, and/or 0.05% per day of delay.

3 Common Issues on Construction Contracts

3.1 Is the employer entitled to vary the works to be done under the contract? Is there any limit on that right?

According to the Law on Contracts and Torts, the employer is authorised to request variation. In such situation, the contractor is authorised to request an extension of deadlines and an adjustment of the agreed price.

3.2 Can work be omitted from the contract? If it is omitted, can the employer do it himself or get a third party to do it?

An agreement on type and volume of works that shall be executed is in the sole discretion of the contracting parties. Prior to entering into a contractual relationship, the employer may decide to have part of the works done by himself or by a third party.

The parties may also agree that the employer may decide whether it shall appoint the contractor for a specified scope of works, and/or obligations of the contractor to appoint a nominated subcontractor.

In practice, the majority of construction contracts are turn-key fixed price contracts, whereby the contractor is obliged to execute/is responsible for the execution of overall construction works.

3.3 Are there terms which will/can be implied into a construction contract?

The terms which are implied in construction contracts are the description of the work, the price, the design, and the deadline. Subject terms are essential/significant elements of the construction agreement, and must be included in each construction agreement.

3.4 If the contractor is delayed by two events, one the fault of the contractor and one the fault or risk of his employer, is the contractor entitled to: (a) an extension of time; or (b) the costs occasioned by that concurrent delay?

According to the Law on Contracts and Torts, in the case of a delay, a diligent party may primarily request the fulfilment of the obligations of the other party within a reasonable deadline, unless it is agreed that the fulfilment of obligations within given deadlines is a crucial element of the contract.

If the deadline is agreed as crucial, and the contractor is experiencing a delay, the contract is considered terminated.

In any case, the diligent party is authorised to claim the damages arising from a default.

In cases where that delay is caused by an event which is the fault and risk of the contractor, the employer would be entitled to request fulfilment or otherwise terminate the contract. In cases where that the delay is caused by an event which is the fault and risk of the employer, the contractor is authorised to request an extension.

In cases where two events occur, one the fault of the contractor, and one the fault or risk of his employer, rights and obligations would depend on the time of the event's occurence. If the event that was the fault and risk of the employer occurred first, the contractor is authorised to request an extension and *vice versa*.

3.5 If the contractor has allowed in his programme a period of time (known as the float) to allow for his own delays but the employer uses up that period by, for example, a variation, is the contractor subsequently entitled to an extension of time if he is then delayed after this float is used up?

In any variation requested by the employer, the contractor is authorised to an extension of the deadlines. In some cases, the employers request the contractors to include the time for variation in their programme, and in such cases the contractors are not entitled to an extension.

3.6 Is there a limit in time beyond which the parties to a construction contract may no longer bring claims against each other? How long is that period and from what date does time start to run?

According to the Law on Contracts and Torts, the claim is invalid after a period of ten years, starting from the day on which the creditor was able to claim fulfilment (the typical period of time before a claim becomes unenforceable).

The claims from a commercial contract are considered invalid after three years, starting from the day on which the creditor was able to claim fulfilment.

General terms of invalidation are applied to construction contracts.

The start of the invalidation period begins at the due date, and therefore the existence of invalidation cannot affect warranty periods or guarantee the stability of the building.

The warranty periods for the works are, commonly, included in the construction agreement.

3.7 Who normally bears the risk of unforeseen ground conditions?

Unforeseen ground conditions risk may occur in two phases: (i) before and during execution of construction works; and (ii) after the execution of construction works.

(i) If unforeseen ground conditions occur before and during the execution of construction works they would affect the volume of the works, time delay, and the price. Unforeseen ground conditions are considered unforeseen works, and the costs of these works may be borne by the contractor, in cases where a turn-key construction contract is concluded, or by the employer in cases where a unit-price construction contract is concluded. Where unit-price contracts are involved, the employer is authorised to terminate the contract if the costs of the unforeseen works significantly increase the overall cost of construction.

(ii) According to the Law on Contracts and Torts, the contractor is responsible for any ground defects on which the building is developed for ten years after the handover of the works,

unless a specialist gives the professional opinion that the ground is suitable for construction, and there were no indications that such an opinion is incorrect during the execution of construction works.

3.8 Who usually bears the risk of a change in law affecting the completion of the works?

The employer bears the risk of a change in law affecting the completion of the works. Depending on the type of the changes, the parties may terminate the agreement, or amend the contract in a manner which is in compliance with changes of the law.

3.9 Who usually owns the intellectual property in relation to the design and operation of the property?

According to the Law on Intellectual Property, the intellectual property rights may be divided into the material and personal rights of the author. Material property rights may be transferred to the employer, while personal rights (e.g. signing of the design) cannot be transferred to a third party.

In practice, after the design is created and handed over to the employer, the employer may use it, but has to keep the name of the author on the design.

The author of the architectural designs cannot oppose any alterations of his work if the need to make alterations was borne of circumstances involving safety risk or for technical reasons.

The author's moral rights shall be observed if alterations in a building are not made in accordance with the modification of the work made by the author.

3.10 Is the contractor ever entitled to suspend works?

The Serbian Law on Contracts and Torts does not provide any regulation on suspension of works by the contractor. In practice, the contractor`s right to suspend the works is excluded by construction contracts.

In cases where the construction contract does not regulate the suspension of the works by the contractor, and there is a dispute between the parties about the contractor's right to suspend the works, the court would consider previously applicable Special Provisions on Construction.

According to the Special Provisions on Construction, the contractor is authorised to suspend the works in following cases:

(i) If the actions of the employer prevent or impede the execution of works (this also relates to delays in payments to the contractor).

(ii) If the defects in technical documentation endanger the safety of the building, life and health, traffic, or neighbouring buildings.

3.11 On what grounds can a contract be terminated? Are there any grounds which automatically or usually entitle the innocent party to terminate the contract? Do those termination rights need to be set out expressly?

Each contract can be terminated in case the other party does not fulfil its due obligation, unless agreed otherwise between the parties.

In practice, the parties usually:

(i) Agree on the events which are considered as reasons for termination, though not directly connected with the fulfilment of contractual obligations such as: bankruptcy of one of the parties; bribery; protection clauses; etc.

(ii) Agree on the mechanism of termination, especially in cases of automatic termination and previous notice period termination.

(iii) Specify the obligations which are not considered as essential, i.e. which do not create a reason for termination, such as: an obligation of the contractor to keep the site in clean condition; and an obligation to place a construction fence, etc.

(iv) Exclude specific events as reasons for the application of "changed circumstances" conditions (such as monetary fluctuations, changes in regulations or standards, etc.).

3.12 Is the concept of *force majeure* or frustration known in your jurisdiction? What remedy does this give the injured party? Is it usual/possible to argue successfully that a contract which has become uneconomic is grounds for a claim for *force majeure*?

The Law on Contracts and Torts recognises "impossibility of fulfilment" as an event which prevents one of the parties from fulfilling its obligations. If the impossibility of fulfilment of obligations is not caused by one of the parties (as in *force majeure* or frustration), the obligation of the other party ends and the parties may only be obliged to *restitutio in integrum*.

In practice, the employers usually keep the right to terminate the contract at any moment, with an obligation to compensate the contractor for the works already executed, and certain fee for early termination.

3.13 Are parties which are not parties to the contract entitled to claim the benefit of any contract right which is made for their benefit? E.g. is the second or subsequent owner of a building able to claim against the original contracts in relation to defects in the building?

The contractor is liable for the stability of the building and this liability (and respective warranty) extends to subsequent owners of the building.

In practice, other warranties are transferred to the subsequent owners of the buildings via transfer agreement.

3.14 Can one party (P1) to a construction contract which owes money to the other (P2) set off against the sums due to P2 the sums P2 owes to P1? Are there any limits on the rights of set-off?

Serbian law recognises rights to set-off, provided that all claims, which are subject to setting off, are due. Set-off is usually executed by a simple set-off statement given to the other party in the contract.

Right to set-off can be excluded in the construction contract. Exclusion of set-off rights is usually requested by financial institutions in cases of project financing.

Serbian tax laws forbid set-off for the entities under administrative proceedings for tax collection.

3.15 Do parties to construction contracts owe a duty of care to each other either in contract or under any other legal doctrine?

Due care is a general principle in the Serbian Law on Contracts and Torts, and is applied to construction contracts as well.

3.16 Where the terms of a construction contract are ambiguous are there rules which will settle how that ambiguity is interpreted?

The general rules of the Law on Contract and Torts prescribe that ambiguous rules shall be interpreted with the goal of finding the shared will of the contracting parties, and should be understood in a manner which complies with the general principles of the Law on Contracts and Torts (equality of the parties, prohibition of the misuse of rights, prohibition of the misuse of a monopoly position, equivalency of remunerations, due care in fulfilment of obligations, etc.).

3.17 Are there any terms in a construction contract which are unenforceable?

Some provisions of FIDIC agreements are unenforceable i.e. obligation of the contractor to remove specific worker from the construction site, provide sufficient food supply for workers and similar.

3.18 Where the construction contract involves an element of design and/or the contract is one for design only, are the designer's obligations absolute or are there limits on the extent of his liability? In particular, does the designer have to give an absolute guarantee in respect of his work?

Serbian laws do not regulate the guarantees of the designers to the investor for the work. In general, the parties may agree on the extent and limits to the guarantees that the designer gives to the investor. In cases where the contractor is obliged to provide designs during construction, it also guarantees that such designs shall meet legal requirements for obtaining of the operational permit.

4 Dispute Resolution

4.1 How are disputes generally resolved?

Disputes are generally resolved in court legal proceeding, extrajudicial proceeding (settle the dispute amicably) or in proceeding before arbitration.

4.2 Do you have adjudication processes in your jurisdiction? If so, please describe the general procedures.

Adjudication processes are regulated by Civil Procedure Law. Adjudication processes could be carried out before the court with general or special jurisdiction. The parties have the right to appeal against the first instance court's decision. Decisions rendered by second instance courts are final decisions.

4.3 Do your construction contracts commonly have arbitration clauses? If so, please explain how arbitration works in your jurisdiction.

Construction contracts usually have an arbitration clause. In most cases, the parties agree on the number and election of arbiters, jurisdiction of arbitration court, and rules of procedure. When parties agree on Serbian arbitration, provisions of Serbian law on arbitration are obligatory.

4.4 Where the contract provides for international arbitration do your jurisdiction's courts recognise and enforce international arbitration awards? Please advise of any obstacles to enforcement.

International arbitration decisions are equated with domestic arbitration or judicial decisions. Prior to enforcement, any international arbitration decision has to be recognised before a competent court in Serbia.

4.5 Where the contract provides for court proceedings in a foreign country, will the judgment of that foreign court be upheld and enforced in your jurisdiction?

The judgment of a foreign court has to be recognised by the competent court of the Republic of Serbia.

4.6 Where a contract provides for court proceedings in your jurisdiction, please outline the process adopted, any rights of appeal and a general assessment of how long proceedings are likely to take to reduce: (a) a decision by the court of first jurisdiction; and (b) a decision by the final court of appeal.

Depending on the type of the dispute, a first instance procedure before Serbian court may last from a few months to one year. The parties can appeal for (1) substantial violation of civil procedure rules, (2) erroneous or incomplete establishment of the facts, and/or (3) erroneous application of the substantive law. Appeal procedures may last up to six months.

Uroš Marković

JPM Janković, Popović & Mitić
6 Vladimira Popovića Street
Belgrade
Serbia

Tel: +381 11 207 6850
Fax: +381 11 207 6899
Email: uros.markovic@jpm.rs
URL: www.jpm.rs

Uroš is a Partner in the Real Estate Department of JPM. Uroš and his team have advised: Bauhaus AG, Germany in the course of acquisition of the site and construction of Bauhaus retail centre in Belgrade; Immorent AG, Austria in negotiations in relation to the acquisition of a site for the development of a retail park in Sabac; the state-owned company Srbijagas Novi Sad on the restructuring of the real estate of Srbijagas in the process of establishment of JVC Banatski Dvor and in the construction for underground gas storage in Banatski Dvor; FMTG-Falkensteiner Michaeler Tourism Group in procedures and related legal services for the development of hotel and office facilities in Belgrade; Kaufland in the acquisition of a location for development retail centres; the German Embassy in relation to the long-term lease of the new embassy building and reconstruction of the current embassy building; and the U.S. Government in relation to the real estate issues pertaining to its embassy building.

Ivan Petrović

JPM Janković, Popović & Mitić
6 Vladimira Popovića Street
Belgrade
Serbia

Tel: +381 11 207 6850
Fax: +381 11 207 6899
Email: ivan.petrovic@jpm.rs
URL: www.jpm.rs

Ivan is a Senior Lawyer in the Real Estate Department of JPM. Ivan specialises in mortgage law and construction agreements. Ivan has advised: FMTG-Falkensteiner Michaeler Tourism Group in preparing the construction contract for the development of hotel and office facilities in Belgrade; Kika Leiner in the acquisition of a location and the development of a retail centre in Belgrade; Delta Real Estate in the sale of the location for a new distribution centre in Stara Pazova; Swarovski Austria in the bidding procedure and conclusion of the construction contract for the development of a new production plant; state-owned company Srbijagas Novi Sad on the restructuring of the real estate of Srbijagas in the process of establishment of JVC Banatski Dvor and construction for underground gas storage in Banatski Dvor; the German Embassy in relation to the reconstruction of the current embassy building; and the U.S. Government in relation to the real estate issues pertaining to its embassy building.

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GLG
Global Legal Group

59 Tanner Street, London SE1 3PL, United Kingdom
Tel: +44 20 7367 0720 / Fax: +44 20 7407 5255
Email: sales@glgroup.co.uk

www.iclg.co.uk