Applicability of the 1975 law on subcontracting to construction contracts governed by French law for international projects

A question that is often asked (and with good reason) when negotiating EPC contracts governed by French law for projects located outside of France is the extent to which certain French laws will apply to the contract and confer rights or impose obligations on the parties (or in some cases, third parties). A law that is of particular concern to employers and contractors is the 1975 law on subcontracting ("*Loi n°75-1334 du 31 décembre 1975 relative à la sous-traitance*"), which allows subcontractors to directly claim against the employer in the event of a payment default by the main contractor.

Why use French law for an EPC contract on a project outside of France?

The logic of using French law to govern an EPC contract for a project located outside of France is the same as using French law to govern the loan documentation for the same project: the interpretation of certain types of clauses are tried and tested under French law, giving comfort to the parties that such clauses will work as drafted and intended. English law may be a suitable alternative, and may be favoured by employers or contractors that are more familiar with it or for projects located in common law jurisdictions (French law being favoured in civil law jurisdictions).

Choosing French law or English law to govern an EPC contract does not mean that the contractor should disregard local rules when performing the works. On the contrary, a well drafted EPC contract will specify that the contractor must comply with all applicable laws, meaning the local laws applicable in the jurisdiction in which the works are located. This is captured by the Clause 1.13 (*Compliance with Laws*) in the FIDIC SilverBook standard.

What does the 1975 law on subcontracting say?

The 1975 law on subcontracting was passed with an objective of establishing a statutory regime for the protection of subcontractors in France, in response to a wave of contractor insolvencies in France at the time (on which see the draft notes to the *projet de loi*, 1974, Doc. Ass., note n° 1449).

It applies to "subcontracts" and "subcontractors" in the strict sense of the term, meaning subcontractors engaged to perform works forming part of the construction of a plant, including civil works, equipment supply and installation and engineering and design. The law does not apply to other types of contracts, for example agency contracts or contracts of sale where the main contractor purchases standard materials from a supplier off-the-shelf. A manufacturer or supplier may be treated as a subcontractor for the purposes of the law if it manufactures equipment designed specifically for the plant, even if it does not work on site.

The 1975 law firstly requires the main contractor to **obtain the approval of the employer** in respect of (i) the **identity** of the subcontractors it hires and (ii) the **terms of payment** under the relevant subcontracts. This disclosure and approval rule applies in respect of any subcontractor of any level in the subcontracting chain, meaning that an employer will ultimately be required to provide its approval for any subcontractor working on a project. To grant its approval, the employer may request the disclosure of the entire subcontract.

If the main contractor fails to obtain the employer's approval, the main contractor will still be liable under the relevant subcontract but will not be entitled to enforce such subcontract against the subcontractor. The subcontractor may suspend performance of the subcontract until approval is obtained from the employer.

If the employer becomes aware of the existence of subcontractors engaged on a project in respect of which it has not given its approval, the law requires the employer to notify the contractor on notice and request disclosure of the relevant subcontract, failing which the employer may find itself liable to the subcontractor for any loss resulting from the failure to obtain approval.

The 1975 law secondly gives the subcontractor the right to **directly claim** against the employer in the event of a failure by the main contractor to pay amounts due under the subcontractor, within a period of one month after the subcontractor's notice to the main contractor with a copy to the employer. The law specifies that the parties may not renounce this direct claim right by way of contract.

The law clarifies that the subcontractor's direct claim may only cover the part of the works that the employer benefits from under its main contract, to the exclusion of any works conducted outside of the scope of the project or exclusively for the main contractor.

Does the 1975 law apply to projects outside of France?

Whilst being clearly beneficial to subcontractors in France and providing protection against insolvency risk of the main contractor, the application of the 1975 law to international projects raises several issues, creating additional liabilities on the employer and the main contractor, giving the employer insight into the prices of subcontractors and the profit margins of the main contractor and adding additional layers of administration to the construction process. Parties to an EPC contract governed by French law may naturally be inclined to exclude the application of the law to projects located outside of France.

Given the latest decisions of the *Cour de Cassation* on the matter as well as certain published decisions of international arbitral tribunals, it is possible today to argue with relative certainty that **the 1975 law is only applicable to, and mandatory for, construction projects located in France**. It would also be difficult to argue that the intention of the French legislator was to protect all subcontractors, regardless of the location of the project and the nationality of the subcontractor.

In a string of decisions starting in 2007, the *Cour de Cassation* repeatedly confirmed that the 1975 law constituted a "*loi de police*" or a mandatory rule of public order, but for construction projects located in France (see Cass. ch. mixte, 30 novembre 2007, n°06-14.006, *Soc. Agentis et autre*; Cass. civ. 3ème, 30 janvier 2008, n°06-14.641, *Soc. Diw instandhaltung GMBH* and Cass. civ. 3ème, 8 avril 2008, n°07-10.763, Soc. *Basell production France*). These cases involved construction projects in France with foreign contractors and with governing laws other than French law.

In ICC Case No. 7528 in 1993, the tribunal accepted to apply French law to a subcontract for works in Pakistan, but rejected the subcontractor's request to void the subcontract for non-compliance with the 1975 law. The French main contractor in this case and a French

subcontractor had agreed that the subcontractor would remain undisclosed to the Pakistani employer. Whilst the subcontract did not expressly exclude the application of the 1975 law, the tribunal concluded that it was sufficient that the parties "consciously set aside" the requirements of the 1975 law. The tribunal concluded that such an exclusion was valid because the 1975 law "*has mandatory character (d'ordre public) in domestic transactions, as evidenced by article 15*" (of the law).

In ICC Case No. 9970 of 2000, the parties agreed and the tribunal accepted that in respect of a subcontract for works outside France between two French parties governed by French law, the 1975 law did not constitute an international *loi de police*. The tribunal gave effect to certain provisions of the law, but only to the extent that the parties did not expressly or impliedly exclude the application of certain rules of French law.

What is best practice for French law-governed EPC contracts?

Although several arguments point to the 1975 law applying only to projects in France, the most prudent approach today in international projects outside of France remains for parties to **expressly exclude** the application of the law in main EPC contracts and subcontracts governed by French law.

An employer could further seek to insulate itself from direct payment claims by subcontractors by requesting an indemnity from the contractor in the event of such claims and the right to deduct such amounts from amounts owed to the contractor.

Employers should be mindful of requesting main contractors to disclose the full payment terms of their underlying subcontracts, as this is a characteristic aspect of the 1975 law and could be interpreted as intending for the law to apply if it is not expressly excluded by the parties.