

FIDIC CONTRACTS: INTERNATIONAL COMPETITION ON THE NORTH MACEDONIAN INFRASTRUCTURE PROJECTS

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Abstract

Nowadays, FIDIC forms of contract are intended to be suitable for infrastructure projects carried out around the world by all types of employers, often in a civil law environment with the extensive support of large investors such as the World Bank or the European Union. The construction market in North Macedonia experiences the development of larger infrastructure projects with bigger budgets than ever before. Increasing foreign direct investment and reforming the public procurement procedure have increased competition and transparency, encouraging new participants to enter the market.

This paper provides an overview of the current situation in the construction market in North Macedonia, addressing the following research questions: What are the biggest opportunities and challenges of operating in the construction market, and how to ensure healthy and fair competition in infrastructure project procurement? Furthermore, the paper aims to analyze how the FIDIC contract conditions can influence the implementation of infrastructure projects in North Macedonia.

Public infrastructure projects financed by international institutions and executed according to FIDIC conditions of contracts provide a considerable value-added input to developing economies. Achieving best procurement practice depends widely on the leadership and competence of the procurement stakeholders, procurement officers should understand all the procurement objectives and principles since it all encompasses the concepts of efficiency and effective procurement, transparency, competitiveness, and fairness.

Keywords: FIDIC, infrastructure projects, public procurement, construction market, North Macedonia.

1 Introduction

To achieve sustainable economic development in developing countries, significant investments are needed in environment protection and infrastructure, many of which come from international financial institutions. The construction industry in North Macedonia promises development for the future, large infrastructure projects are expected with bigger budgets than ever before. Increased foreign direct investment is pushing for public procurement reform to ensure a transparent and sustainable public procurement procedure, increasing competitiveness, and encouraging new entrants from around the world to enter the industry. Many contractual methods have been developed on how to choose the best approach to fit public needs. In developing countries, where budgets are limited, public institutions face many financial constraints, shortages of materials, and a lack of skilled personnel to run projects, particularly for infrastructure development. Large projects in the public sector are usually funded through loans and grants from international agencies such as the World Bank, the European Union, and the United Nations [1]. This situation requires the host country to manage the funds for project implementation efficiently.

Borrowers must operate projects according to their requirements. However, donors/lenders are getting more involved in project execution to ensure that money is used effectively. A project can be considered successful if the product is delivered at the right time, at the appropriate price and quality, and provides the client with a high level of satisfaction [2]. Many problems arise during a project due to unclear roles and responsibilities within construction teams. Lines of communication are often not well defined, and the teams are sometimes not aware of the social and economic background of the contractual arrangement. All tendering procedures and contractual arrangements are normally aimed at selecting the most suitable contractor for a project and securing from him a suitable offer and using this as a basis for an agreement for execution of the project.

To have a collaborative working environment, all participants in the construction process may sign an alliance contract [3]. Nowadays, FIDIC forms of contract are intended to be suitable for construction projects carried out around the world by all types of employers, often in a civil law environment with the extensive support of large investors such as the World Bank or the European Union. FIDIC is the French acronym for the International Federation of Consulting Engineers, headquartered in Geneva, Switzerland. FIDIC is a truly international organization with 101 members and associates from across the world from both common law and civil law jurisdictions [4]. In North Macedonia, the FIDIC conditions of the contract have been applied only to projects financed by international institutions.

The purpose of this research paper is to present an overview of the current situation in the construction market in North Macedonia, with a focus on infrastructure and environmental projects, analyzing how the FIDIC contract conditions can influence the implementation of projects financed by the European Union through IPA (Instrument for Pre-Accession Assistance) components. Furthermore, the research presented in this paper has addressed the following research questions:

- What are the biggest opportunities and challenges of operating in the North Macedonia construction market, specifically on the infrastructure projects financed by the European Union, for international and domestic companies
- How to ensure a healthy and fair competition in projects public procurement

The first research question maps the different opportunities and challenges in the North Macedonian construction market. The answers are related to why so many international contractors choose to compete in the construction market and what kind of challenges the different actors are facing today. However, the second research question shows that we are not only interested in how the situation today is affecting the competition. We also seek to investigate how the authorities in the future can facilitate a market that attracts new contractors, but at the same time develop the already established contractors.

2 Theoretical framework

Large international contractors face several challenges when they try to enter new markets. Their entry is always related to risk. Contractors can enter different markets with different strategies, and two contractors establishing a joint venture company is a well-known strategy [5]. Establishing a joint venture together with a local company, to get local expertise in the project organization is very often the situation in North Macedonia. Having local knowledge in a market can be crucial for success in many ways [6]. Underestimating the consequences of both language and cultural differences can be fatal for contractors when operating in a new market [7]. The importance of the cultural factors is also supported in Öz, as he refers to the Turkish contractors having successfully entered the construction market in other countries. He relates their success to the Turkish contractors' ability to adapt and high cultural proximity to several construction markets in European countries [8]. Even though many countries are following the same international laws and regulations, international contractors still must know and interpret the national laws, local policy guidelines, and taxation rules given by the authorities. Failing to adapt a business plan to this can cause projects with bad profits [9].

Construction work in many developing countries suffers from administrative and allocative inefficiencies. Because of a lack of a sound framework of institutional and legal arrangements, especially those affecting public sector procurement, the construction industry is not shaped to respond quickly and efficiently to the client's needs [10]. Some of the pitfalls in trying to manage projects effectively and maximize project performance are problems associated with misunderstanding contract documents, especially general and special conditions that have a tremendous impact on project performance [11].

Important factors for contractors when considering an entry-strategy for new markets are [12]:

- Laws and regulation
- Political and economic stability
- Corruption
- Currency

The political and economic stability of the country can be a big challenge in terms of guarantees for the contractors to get paid for their work. The political stability may also affect the promises made for future projects, which can be a factor that international contractors have considered when determining whether to establish an organization in the respective country or not. These factors are also directly related to the risk of corruption in the country, as a country with a tradition of corruption can make it difficult for any contractor to play by the legal rules and win projects.

A well-functioning market is crucial for getting the most out of the invested funds. The use of the FIDIC contracts is widespread throughout the world due to such contracts being mandated by the European Union and World Bank and the acceptance of FIDIC as the accepted standard in jurisdictions without their standards, such as in developing countries [13]. The Rainbow Suite of FIDIC contracts is intended for use for major works, and these books provide a practical guide to the key elements that practitioners prepare and administering these contracts, in terms of risk allocation [14].

FIDIC rainbow suite covers:

- The obligations and responsibilities of the Employer, the Employer's Representative, the Engineer and the Contractor
- Quality and Defects Liability
- Design Responsibility, and Liability
- Variations, Measurement, and Payment Procedures
- Progress, Delays, Extensions of Time, and Completion
- Suspension and Termination
- Insurances
- Employer's and Contractor's Claims
- The Dispute Avoidance/Adjudication Board and the Resolution of Disputes
- Tendering

3 Methodology

The research started with a literature study of the tender protocols and procedures for projects financed from European Union through the IPA (Instrument for Pre-Accession Assistance) components in North Macedonia, in area of road infrastructure and environment protection, analyzing the conducted project also the cancelled one. Were analyzed ten projects, that were chosen specifically because of their area and complexity, in the period from 2016 to 2021, in order to see, firstly, tender procedures and results, and secondly, the development in contract model and background of the awarded contractors. Not all of the information from these protocols and documents are easily available to the public. This means that we can't share detailed information about the tender documents, but just the results of the research.

The study also included what kind of challenges and opportunities contractors are facing when entering in North Macedonia construction markets, as well as how FIDIC condition of contract affects time, quality and costs in different projects. The initial literature study was followed by twenty semi-structured interviews with key persons involved on these projects, from both sides of the industry, established local and international contractors in North Macedonia and public clients, in terms of getting a clear picture of the market as a whole and not only from one perspective. We interviewed, project managers, project directors and client administrators. After request, the participating respondents are anonymous. The interviews were carried out mainly on site, the same questions were asked on all management levels, so that the answers would be more comparable.

4 Findings

4.1 Present situation in construction market, opportunities and challenges

The Government of North Macedonia as has stated in the Work Program for 2020-2024, that they will announce several infrastructure projects in cooperation with EU in the near future, who will be implemented with FIDIC condition of contract [15].

From the document study and the interviews, it is possible to conclude that there are many opportunities and at the same time many challenges of being on the North Macedonia construction market. The challenges that the domestic contractors are facing is primarily not the same as the international are facing.

Table 1: List of challenges

Challenges of being on the North Macedonian construction market	As a international contractor	As an domestic/local contractor	As a client/public institutions
	Lack of local knowledge	Lack of technical and financial references	High amount of disputes with the contractors
	National legislation	Low trust between the client and the contractor makes cooperation difficult	Low trust between the client and the contractor makes cooperation difficult
	Language barriers	Increased competition	Political influences
	Cultural differences		Lack of quality administration

The opportunities in the North Macedonian construction market are primarily related to the contractors. But as a result of the increased competition the clients have the opportunity of getting lower prices for the projects and getting qualified contractors for the project.

Table 2: List of opportunities

Opportunities on the North Macedonian construction market	As a contractor, international and domestic/local	As a client/public institutions
	Complex and large projects	Getting many qualifies contractors in the tender phase
	Low political risk	Getting the right price for the project
	Payment guarantees	

4.2 Projects Financed by European Union, International Players, and FIDIC Condition of Contract

The results were identified by analyzing the data from the Central Financing and Contracting Department of North Macedonia, as a coordinator for the financial management of projects financed under the IPA Component I, II, and III. These findings show which projects are managed successfully, the name of the winning company, and the canceled projects. From the results of the document study, it is possible to get an overview of the current situation in the construction market in North Macedonia regarding the projects financed under the IPA components.

Table 3: List of a project financed by the European Union [16].

The name of the project	The name of the contractor	Financial institution European Union	Form of contract	Year
Rehabilitation of state road A1, section Kumanovo – Miladinovci as a part of corridor X	Strabag AG Austria	IPA I - component III	FIDIC	2016
Rehabilitation of state road A2, Kumanovo – Stracin, section 1	Hydrostoj Bulgaria Eskavatori MK	IPA II - component IV	FIDIC	2020
Construction of WWTP in Radovish – Kichevo – Strumica	WTE Germany Vardar Gradba MK	IPA I - component III	FIDIC	2016
Rehabilitation and extension of sewerage network in Berovo and Kumanovo	Chemkostav Slovakia Zhikoll DOOEL MK	IPA I - component III	FIDIC	2016
Rehabilitation and extension of sewerage network in Prilep	Ludwig Pfeifer Germany	IPA I - component III	FIDIC	2016
Improvement of waste water collection infrastructure in the city of Skopje	Guintoli France Bauer MK	IPA II - component III	FIDIC	2017
Construction of road section Gradsko – Interchange Drenovo	Tirrena Scavi Italy	IPA II - component IV	FIDIC	2018
Rehabilitation and extension of sewerage network in the municipality of Kichevo	Canceled	IPA II - component III	FIDIC	Funds approved from 2017
Construction of WWTP and rehabilitation and extension of sewerage network in Bitola	Canceled	IPA II - component III	FIDIC	Funds approved from 2017
Construction of WWTP and rehabilitation and extension of sewerage network in Tetovo	Cancelled	IPA II - component III	FIDIC	Funds approved from 2018

Regarding the presented projects it can be concluded that the tender conditions and contract conditions were based on FIDIC rules, and these projects were either awarded to international contractors or they are canceled and failed to be successfully managed, even though the funds were approved. The reason for the failure is the low capacity of the state administration to manage these capital projects according to FIDIC rules and political influences and lobbying. From interviews, we also understood that local contractors cannot meet the required technical and financial conditions and they are forced to seek support from international contractors while presenting themselves as a subcontractor.

5 Discussion

The North Macedonian construction market is having a major change due to the large income of new international contractors. A competitive construction market is something that the international financial institutions especially the European Union have been striving for the past years, to make sure that they do have a sufficient number of competent contractors to submit tenders for a large number of future projects. The international contractors have chosen specifically to enter the North Macedonian construction market because of the political and economic situation, as important factors in their decision to come. It has been often said that in certain Central and Eastern European countries, employers have managed to impose in public works contracts, largely financed by the European Union, very onerous provisions for the contractor which radically change the allocation of risks established by the general conditions of

contract [17]. Such a trend calls for a rapid change in European Union secondary legislation to ensure that financed contracts reflect FIDIC's principles of balanced risk sharing.

Researchers and practitioners in the construction and legal sectors alike have questioned the possibility of creating a "common law of construction contracts" across countries and regions owing to the vast and often insurmountable differences between national jurisdictions [18]. International financing institutions like European Union, in North Macedonia, require FIDIC conditions of the contract to be used in the tendering procedures in all project phases.

The competition in the North Macedonia construction market today is high, too high according to some contractors. The international financial institutions think that the competition is good in some segments, and they still support more competition on the biggest contracts, especially on the projects that are financed by European Union. The most alarming situation seems to be that in large infrastructure projects domestic/local companies do not meet the required condition in technical and financial terms. It is an unpleasant situation, where domestic companies seek support from international companies in different tenders, only in the application phase, to meet certain conditions. The realization of the project they try to do themselves and unfortunately, we have project failure either during the evaluation or implementation phase. Projects do not end based on initial projections, it takes more time, and more money and the quality is poorer. In our interviews, there have been indications that the international contractors have had problems with the national law and regulation of North Macedonia, but many of them said that these factors were simple to manage. Some domestic contractors, which we interviewed, have had several problems regarding the implementation of FIDIC conditions of contract and procurement procedures.

Conclusions

Contract management is a significant issue in construction organizations, particularly for a complex project which deals with numerous parties. Contract conditions must be written in terms of contract language, fairness of clauses, and clear definition of roles and responsibilities of parties. Common problems occur in the construction industries in many developing countries because of unclear contract conditions. Contracts are often prepared with an emphasis on the owner's rights and the contractor's obligations. This leads to disputes, contract termination, project delays, and cost overruns. Although the North Macedonian authorities have tried to harmonize the FIDIC conditions of contract with existing national legislation, they have not succeeded in finding a uniform approach that can be transposed and used for infrastructure projects in the form of specific conditions or in otherwise adjusting the existing legislation to comply with the FIDIC forms of contract. From the document study and the interviews, it is possible to answer the research questions and conclude that there are many opportunities and at the same time many challenges of being on the North Macedonian construction market. The biggest challenge that the local contractors are facing is the lack of technical and financial references to enter increased competition with international contractors. For the client, in this case, public institutions, the identified challenges are mainly the lack of quality administration to run these projects in all phases and the political influences. The opportunities are primarily related to the contractors, with the implementation of FIDIC conditions of contracts they have payment guarantees. Also, the client, because of the increased competition, have the opportunity of getting the right prices and qualified contractors. Today's competition in North Macedonia is hard, there are many international bidders, the prize pressure is high, and the margins are low. This of course benefits the public clients that get more for every euro invested. Competition on equal terms is of course very important to the contractors, but also for the clients. The clients' opportunity to create unequal terms in projects financed by the international institution is small because the tender process is strictly regulated through European Union regulations, and they support the application of FIDIC conditions of contracts and procurement procedures. The tender competitions themselves happen on equal terms, but there is still the question of the laws and a regulation, regarding technical and financial references, stuff, and so on are unfair, and creates a competitive advantage for the international established contractors, who also can rent cheap laborers from other developing countries

where they operate. The government must develop its strategy to maintain a well-functioning market, and that all involved parties are treated equally, and compete on equal terms but also find a way to support domestic companies.

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