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CONSTRUCTION PAPERS



Mandatory Terms and Elements of Construction Contracts under Hungary's Act LXIX of 2023 on Public Works Projects

As noted in a previous article, Hungary's Act LXIX of 2023 on Public Works Projects (hereinafter: "Act") took effect on 8 November 2023. In addition to dispute resolution procedures, the Act also includes provisions on certain mandatory terms and elements of construction contracts. This article discusses additional requirements that the Act sets beyond what is included in Government Decree No. 191/2009 on Construction Activities (hereinafter: "Decree").

Model contracts

[1] An important rule is that construction contracts concerning public works projects must be concluded using one of the model contracts published on a government website. As of this writing, however, the model contracts have yet to be published. Consequently, it is not clear what impact these contracts will have on the freedom of contract and the parties' ability to determine the terms of their contract as they desire. So it remains a question whether the model contracts will serve as guidelines for the general framework of contracting, or construction contracts in public works projects may now only be concluded with specific, statutorily fixed clauses.

Mandatory elements

[2] The Act lists certain elements that construction contracts must include in addition to what is stated in the Decree. The following table shows these elements, with bold font signifying provisions with which the government aims



to prevent financial disputes at a legislative level. The inclusion of such clauses in a contract can facilitate dispute resolution.

Elements of construction contracts under the Act, beyond the requirements of the Decree	
determination of project milestones	rules pertaining to the certification of performance and technical handover
rules and methods of determining and modifying technical specifications, and in particular, how extra work and additional work can be ordered	rules pertaining to faulty performance, warranties and guarantees
construction hourly rate charged on the basis of the winning bid	contractual sanctions and penalties
the process of approving equivalent solutions proposed during construction	provisions on liability insurance
the conditions of modifying contractor's fees and handling claims for extra expenses, including the management of materials price increases and cases where the contractor is not entitled to extra fees	provisions on force majeure and unforeseeable events
the maximum rate of advance payments, the conditions for claiming an advance payment, and the rules of paying it	provisions on intellectual property, project communications, confidentiality and the use designs
rules on the allocation of tasks, liabilities and risks between parties	rules concerning reliance on subcontractors, and a rule stating that the contractor is required to inform the developer without delay about all subcontractors hired and their fees, in a manner that allows comparison with the contractor's fees
general rules pertaining to the performance of the construction project	claim management and dispute resolution procedures
detailed rules of cooperation with other entities participating in the project	cases where the contract terminates

Escalation clause

[3] The construction industry is very sensitive to changes in general economic circumstances. The effects of this include wild fluctuations in the prices of construction materials, while fees can also increase drastically. In spite of all this, contractor's fees are more frequently charged in flat rate arrangements. In such an arrangement, the developer is exposed to the risk of price drops, while the contractor to that of price hikes, and this system works well enough in normal market circumstances. However, market trends can be atypical at



times. We believe that it is advisable to include an escalation clause in any construction contract as a preventive measure, where the parties regulate excessive price increases due to hyperinflation. Subject to the parties' agreement, these clauses can be designed to manage the contractor's unexpected costs in ex-post negotiations or in an automatic manner with a predetermined methodology. Such a clause is included for example in the FIDIC Yellow Book.

- [4] The government has also clearly identified widespread disputes about price increases as a problem. Section 47 of the Act states that in the case of a public works project, the relevant construction contract must include a formula, based on objective market indicators, for the predictable management of risks associated with unforeseeable increases in the prices of construction materials and construction fees. However, price increases may only be recharged in the period between the date of the construction contract and the date when the relevant construction materials are ordered in line with the construction schedule attached to the construction contract, on the basis of the confirmed purchase date of the materials.

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