

Insights

NEC CONTRACTS IN THE KINGDOM OF SAUDI ARABIA

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Summary

In this BCLP Insight, Richard Dupay and Muhammad Hassan explore how easily parties operating in the Kingdom of Saudi Arabia (KSA) could transition to NEC from FIDIC and, specifically, consider how many Y clauses an NEC contract would need in the KSA.

Background

There are various forms of construction contracts that are recognised and suitable for use in different jurisdictions subject to appropriate adaptations being made. Popular ones include the International Federation of Consulting Engineers (FIDIC) and the New Engineering Contract (NEC). FIDIC is one of the most popular contracts in the Middle East for a variety of reasons including its long standing usage and stakeholders' (including lenders') consequent familiarity and comfort with it.

However, there is no one-size-fits-all solution when choosing a contract form and each form carries its own set of advantages and disadvantages. While, undoubtedly, familiarity with a particular form may make a party more likely to use it again (hence why, despite the introduction of successive new forms, certain parties still prefer to use the FIDIC Red Book 1989), over the last decade or so there has been a noticeable trend in certain jurisdictions of parties increasingly opting to use the NEC suite of contracts.

Indeed, NEC contracts have now become the default preferred choice for public sector construction contracts in the United Kingdom and Hong Kong, while an increase in their uptake has been observed in Australia, New Zealand, Ireland, South Africa and Peru, amongst others. Interestingly, this trend has not yet impacted the United Arab Emirates (UAE) and the KSA, where there is less use of NEC.

In the context of the KSA, public sector projects are governed by the Government Tenders and Procurement Law and its implementing regulations and have their own standard contract formats accordingly, they fall outside the scope of this article. The private sector, on the other hand, tends

to favour the FIDIC Red Book, which is often amended heavily in favour of employers. Such amendments frequently undermine the contractual certainty that standard forms are intended to provide, potentially introducing new complications and diminishing the value of the standard form.

NEC Contracts

NEC contracts distinguish themselves from other forms of contract through their plain drafting and structured style. A typical NEC contract comprises the following elements:

1. Core clauses – standard clauses that are in every NEC contract;
2. Main Option Clauses – containing clauses on various payment methods;
3. X Clauses (Secondary Options) – optional clauses that may be added depending on the project needs;
4. Y Clauses (Jurisdiction specific) – optional clauses required to be added to take account of the applicable legislation; and
5. Z Clauses – custom amendments agreed by the parties.

With the above in mind, the purpose of this article is to ascertain whether applicable Saudi laws conveniently enable parties to opt for NEC contracts in the KSA without having to make many statutory additions by way of Y clauses.

Y Clauses

Construction-related laws in some countries require construction contracts to include mechanisms for various matters. In NEC, the Y clauses section is used to capture jurisdiction-specific legislation which impacts on the existing terms included within the contract.

So to use the UK as an example, Part 2 of the Housing Grants, Construction and Regeneration Act 1996 provides that mandatory payment and adjudication provisions be included in every construction contract which falls within its ambit. The statutory Scheme for Construction Contracts implies or replaces the missing terms in the event that a construction contract in the UK does not specify the aforesaid adjudication and payment mechanisms. The NEC form when used in the UK includes Y (and W) options which address these statutory provisions.

But just because an obligation is statutorily mandated does not, by itself, mean it must be addressed in NEC's Y clauses. So, to stay with the UK as an example, other legislation, such as the Construction (Design and Management) Regulations 2015 or the various building safety legislation places statutory obligations on the parties to a construction contract, but such obligations are not expressly reflected in the Y clauses.. Therefore in a similar vein, if the NEC is used in the KSA, then

not all KSA mandatory requirements would need to be included as Y clauses although, as explored below, use of certain Y clauses would be helpful.

Y clauses in the KSA

In the context of the applicable KSA legal framework, there are three areas where a Y clause may be required:

1. the payment of interest is prohibited under Saudi law; accordingly, clauses awarding interest under the NEC contract, such as Clause 51.2, should be deleted or amended through a Y clause. Saudi law recognises and permits pre-determined liquidated damages, and therefore existing interest provisions should be substituted by alternative forms of compensation;
2. inclusion of a commitment from contractors (particularly designers, supervisors, and those carrying out implementation works) to comply with the Saudi Building Code (SBC)*; and
3. execution of a comprehensive data-processing agreement with a data processor in accordance with Article 17 of the Implementing Regulations of the Personal Data Protection Law.

* Saudi Building Code” means Royal Decree No. M/43 of 2017 (as amended from time to time) and the corresponding set of terms, requirements, laws, executive regulations, and annexes regulating the safety, efficiency, and sustainability of buildings and the construction process in the Kingdom and streamlining the execution of construction projects to ensure safety and public health.

While interest-related clauses will need to be addressed via Y clause, items 2 and 3 above are not strong Y clause contenders:

(a) item 2 falls short of a typical Y clause requirement as it merely mandates inclusion of a general statement, without prescribing any accompanying procedure or mechanism; and

(b) even though item 3 could theoretically be addressed through a Y clause, in practice parties will almost always satisfy this obligation by entering into a standalone data processing agreement.

It should be noted that the KSA does not have the type of security of payment legislation that in many other countries has given rise to the need to use Y clauses.

Additional Saudi Law Points of Note

Even if no Y clause are needed, parties must undertake a review of NEC contracts in the context of Saudi law. We have therefore also summarised how Saudi-specific considerations may be addressed within an NEC contract.

Additional Points	Description	NEC Impact
Decennial (10-year) liability	Under the SBC Implementing Regulations, contractors carry a mandatory 10-year liability for hidden defects threatening the durability and safety of a structure.	This would require the liability, data retention and PI insurance periods in X clauses to be set at least 10 years.
Mandatory permitting	All works in Saudi require building permits and other approvals from the government authorities, with the contractor responsible for obtaining these.	Any change in these requirements may be categorised as a change in law. Therefore, the inclusion of Option X2 (Changes in the law) is highly advisable.
Inherent Defects Insurance (IDI)	IDI is legally required to be procured by contractors for qualifying schemes, with mandatory Saudi Central Bank standard (SAMA) policy wording, and must be procured before building permits are issued.	It should be clarified that existing PI insurance provisions are separate from and do not satisfy the mandatory IDI requirement. IDI must therefore be listed as an additional insurance in the Contract Data insurance table cross-referencing the mandatory SAMA policy-wording.
Prohibition on excluding liability for fraud and gross negligence	The KSA Civil Transactions Law (CTL) prohibits any contractual exclusion of liability for gross negligence or fraud.	Language already exists in the limitation of liability clause to allow the law of the contract to prevail over any specified limits; however, to make the position abundantly clear, an express carve-out to this effect may be incorporated by way of a Z clause.
General Organisation of Social Insurance (GOSI) (Occupational Hazards Branch)	The KSA equivalent of employers' liability insurance is mandatory through employer contributions to GOSI, with no statutory cap on liability.	No change required. Contract Data additional insurance section may provide that GOSI contributions satisfy employer liability obligations.

Additional Points	Description	NEC Impact
Saudi Labour Law – Drinking water	Saudi Labour Law mandates the supply of safe drinking water to workers.	No change required. Clause 27.4 obligates the contractor to act in accordance with the health and safety requirements set out in the Scope; accordingly, a general commitment to adhere to safe working conditions as prescribed by applicable laws may be incorporated in the Scope.
Saudization (Nitaqat)	All entities operating in Saudi Arabia must comply with mandatory local workforce quota requirements.	Compliance with the Saudization targets throughout the Term of the contract may be incorporated as a Key Performance Indicator.
Antiquities and archaeological finds	The KSA Law of Antiquities prohibits removal or concealment of discovered items, with fines of up to SAR 15,000 for non-compliance.	The NEC contract addresses site discoveries in the context of the Project Manager's instructions. The Scope may therefore provide that the Project Manager's instructions in this regard shall align with the applicable legal requirements.
Liquidated Damages (LDs)	LDs are permissible under the CTL, but courts have a mandatory power to adjust the amount upwards or downwards.	Liquidated damages may be adjusted by the court to reflect the amount of damages actually incurred. Accordingly, while no contractual change is suggested, the LD rate should be carefully determined.
Working hours restrictions	Outdoor work is banned between 12:00 and 15:00 from 15 June to 15 September each year by the Ministry of Human Resources & Social Development.	No change suggested. Completion, early completion bonus and delay damages should take into account the said outdoor work limitations.

Additional Points	Description	NEC Impact
Saudi Copyright Law – Moral rights	Moral rights are non-transferable and cannot be waived under Saudi law, which affects how IP assignments are structured.	A carve-out in the applicable existing intellectual property related provisions of the NEC contract should be added in Z-Clauses to state that moral rights cannot be transferred.

Conclusion

As has been shown above, NEC contracts can be used in the KSA without the need for many, or any materially significant, Y clauses. Most statutory obligations in the KSA are more suitably addressed through X clauses or Z clauses. This is because the majority of construction-related statutory and regulatory requirements in the KSA are already firmly established in law and do not impose any further requirement for contractual incorporation. Put differently, even where a general inclusion requirement exists, it typically arises only in a limited or absolute sense, making it better suited for treatment via X clauses or Z clauses.

As mentioned above, different forms of contracts have their own advantages and what is important is that parties choose a form of contract which will be suitable for the nature of the project but also help, to the extent possible, with the successful delivery of the project. In that regard, there is a growing international move towards collaborative contracting and using processes such as early contractor involvement. This is reflected in the FIDIC soon to be published form of collaborative contract.

NEC has been designed as a collaborative contract and a contract which promotes better project management and therefore better delivery. This is done through contractual mechanisms such as the requirements for early warning and the detailed requirements for the use of a programme, as well as requiring parties to deal with issues contemporaneously and as they happen. There are also a number of optional provisions which address climate change, information modelling, early contractor involvement and whole life cost. It is therefore worth reflecting on whether parties should become more familiar with NEC contracts and understanding the benefits they will offer for some of the large projects being undertaken in the KSA.

Related Capabilities

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