

THE IMPACT OF THE NEW CIVIL TRANSACTIONS LAW ON CONSTRUCTION CONTRACTS IN THE UNITED ARAB EMIRATES

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UAE Litigation and Dispute Resolution Alert

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On 1 June 2026, Federal Decree Law No. 25 of 2025 Issuing the Civil Transactions Law (New Civil Code), will come into effect, replacing Federal Law No. 5 of 1985 (Old Civil Code). Under the Old Civil Code, muqawala contracts—which include construction contracts—were governed by the specific provisions of Articles 872 to 896. Under the New Civil Code, muqawala contracts are subject to the specific provisions of Articles 812 to 839. The Old Civil Code will continue to apply to contracts concluded prior to 1 June 2026, whereas contracts concluded after that date will be subject to the New Civil Code.

Below are some key points to note arising out of the New Civil Code:

EMPLOYER'S RIGHT TO TERMINATE FOR CONVENIENCE

The Old Civil Code does not expressly entitle an employer to terminate a contractor for convenience. However, the United Arab Emirates (UAE) Courts of Cassation have acknowledged that an employer has the right to terminate for convenience provided that the employer compensates the contractor, not only for its expenses and the value of the work completed, but also for the profit the contractor would have made had it completed the work (for example, Dubai Court of Cassation in Case No. 223 of 2023 (Commercial)). The New Civil Code codifies this right. Article 836 states that the employer can withdraw from a contract at any time prior to the completion of the work, but it must compensate the contractor for its expenses and the work completed, as well as all profits the contractor would have earned had it completed the work. However, the court has the power to reduce the compensation for lost profit to reflect that the contractor may have saved money by being released from the contract or profited from undertaking alternative work.

THE COURT'S POWER TO ADJUST LIQUIDATED DAMAGES

Article 390 of the Old Civil Code expressly recognises that contracting parties may fix in advance the compensation payable (liquidated damages), but it provides the court with the power, upon application of either party, to adjust the pre-agreed compensation to reflect actual loss. The onshore Dubai courts have confirmed that this power can be exercised to reduce or increase the pre-agreed compensation (for example, Dubai Court of Cassation Case No. 194/2024 (Real Estate)). Article 340 of the New Civil Code confirms that parties are permitted to agree in advance on the value of the compensation payable and expressly addresses the circumstances in which the pre-agreed compensation can be adjusted by a court. Articles 340(2) and 340(3) of the New Civil Code provide that the court may reduce the pre-agreed level of compensation if the debtor proves

that it has been exaggerated, if it exceeds the loss actually suffered when taking into account the partial performance of the work, or if the creditor contributed to, or exacerbated, the harm by its own fault. In addition, a court may decline to award damages if the creditor's fault significantly exceeds the debtor's fault. Article 340(4) states that a creditor may claim an amount exceeding the pre-agreed compensation; however, the creditor must prove that the debtor committed fraud or gross negligence. This new requirement to establish fraud or gross negligence is consistent with other jurisdictions (such as Egypt) and means that there is a higher threshold for upwards revision.

ENFORCEABILITY OF LIQUIDATED DAMAGES POST-TERMINATION

The UAE Courts of Cassation have repeatedly held that liquidated damages cannot be claimed following termination of a contract, as the termination of a contract entails invalidity of the liquidated damages clause (for example, Dubai Court of Cassation Case No. 590 of 2025 (Real Estate)). Upon termination, the employer is required to prove the actual losses that it has suffered. This principle has not been codified in the New Civil Code and it remains subject to the approach taken by the onshore UAE courts.

ADJUSTMENTS TO LUMP SUM CONTRACTS

Article 829 of the New Civil Code addresses a contractor's entitlement to an increase in payment in a lump sum contract. Article 829(2) confirms that if there is a change or increase in the scope of the work, the contractor is only entitled to an increase in payment by agreement of the parties (as per Article 887(2) of the Old Civil Code) and introduces an entitlement to additional payment where the change is due to the fault of the employer. This provision will apply unless otherwise agreed by the parties. Article 829(3) of the New Civil Code further provides that, where exceptional general circumstances arise which could not have been foreseen at the time of contracting and undermine the foundation upon which the contract was based, the court is empowered to restore the balance between the parties. This may include extending the completion period, increasing or decreasing remuneration, or terminating the contract. This entitlement may be of assistance to contractors in the event of another global pandemic or extreme cost inflation.

NOTICE PROVISIONS

The Old Civil Code does not expressly address notice obligations. Article 816(3) of the New Civil Code adopts a stricter approach, requiring the contractor to notify the employer immediately if events or circumstances arise that may impede the proper execution of the work. It also provides that if the contractor fails to give due notice, it bears the consequences arising from such event or circumstances. A failure to give the required notice may therefore result in a contractor being liable for damages, or precluded from an entitlement to additional time to complete the work or additional payment. Article 816(3) of the New Civil Code does not specify what constitutes proper notice, and this will be subject to interpretation by the onshore UAE courts.

ANALYSIS

The muqawala provisions of the New Civil Code appear to be a positive development as they introduce clearer rights and remedies for parties to construction contracts. However, they remain, in large part, nonmandatory and

therefore only apply if the parties' contract is silent on the relevant matter. It is therefore critical that contracting parties exercise care when negotiating contracts and allocating risk between the parties. It is also worth noting that, although the New Civil Code does not, strictly speaking, apply to contracts executed prior to 1 June 2026, it may nonetheless influence the decisions of the onshore courts going forward.

ABOUT THE FIRM

Our Litigation and Dispute Resolution practice has a long history of acting as counsel on high-stakes international arbitration and litigation mandates. Our lawyers in Dubai have extensive experience advising on litigation and arbitration with respect to complex, high-value commercial disputes and construction contracts in the UAE and wider Middle East region.

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