

Liquidated Damages

Construction Law Terms: A to Z

By Huw Wilkins

L is for Liquidated Damages

Introduction

Liquidated damages are common in the construction industry¹ and give rise to a number of different issues. This article focuses on the difference between liquidated damages and general damages, whether liquidated damages are an exclusive remedy, how one might challenge a liquidated damages provision and whether one can recover liquidated damages for a period after termination of the contract.

What's the difference between liquidated damages and general damages?

Damages for breach of contract are intended to put the innocent party in the position they would have been in had the breach not occurred. When claiming general damages, the innocent party must prove that the other party's breach of contract caused the loss claimed. The Tribunal (adjudicator / arbitrator(s) / judge) will then decide what level of damages adequately compensates the innocent party for the loss it has suffered.

In contrast, liquidated damages are a pre-determined and agreed measure of damages which a party is entitled to recover in the event of defined breaches of contract. However, the rate of liquidated damages ought not be an arbitrary figure.

Historically, the rate of liquidated damages was required to be a genuine pre-estimate of loss.² More recently, the Supreme Court reviewed the law in this regard and recast the test.³ In doing so, it recognised that a party may have a legitimate interest in enforcing a liquidated damages provision extending beyond the pecuniary compensation for the breach. The Tribunal can therefore look at more than just a comparison of the rate of liquidated damages and the loss actually incurred (for example, in certain circumstances the Tribunal could look at the impact of a delay to a project on the employer's reputation).

In the construction industry, liquidated damages are commonly used to compensate employers for a contractor's failure to complete the works by the contractual completion date, or a contractor's failure to meet specified performance requirements. Liquidated damages can, in practice, also operate as a cap on the damages the employer can recover from the contractor.

Why do parties agree liquidated damages provisions?

There are a number of reasons why parties agree to apply liquidated damages to specified breaches of contract.

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From a contractor's perspective, reasons to agree liquidated damages include:

- **Certainty:** if the contractor knows what its liability is for a specified breach, it can more easily assess and price the risk of that liability arising (and potentially pass the damages associated with that risk down the contractual chain); and
- **Limiting its liability:** liquidated damages will normally operate as a limitation on the contractor's liability for the specified breach.

From an employer's perspective, reasons to agree liquidated damages include:

- **Certainty:** if the parties have agreed a rate for liquidated damages, there is no need for an employer to prove its losses in the event of a contractor's breach (as it would have to if claiming general damages, which can be "difficult and costly" to quantify and evidence, particularly in construction cases);
- **Deterrence:** knowing its potential liability for liquidated damages will concentrate a contractor's mind on the job in hand; and
- **Mitigation:** a party claiming liquidated damages has no duty to mitigate its actual loss (*MSC Mediterranean Shipping Co SA -v- Cottonex Ansalt*⁴).

Are liquidated damages an exclusive remedy, or can you claim general damages too?

Liquidated damages provisions relate to a specific breach (commonly delay/failure to meet specified performance requirements) and will operate as an exclusive remedy in respect of that breach (see the decision of *Biffa Waste Services Ltd & Anor -v- Maschinenfabrik Ernst Hese GmbH & Ors*⁵).

A by-product of this is that in England and Wales it has been held that if parties agree liquidated damages for delay of "£nil", that will effectively limit the contractor's liability for delay to £0 by way of liquidated damages and (subject to how the contract is drafted) leave the employer with no entitlement to claim general damages in the alternative⁶ (although, this point has been decided differently in Australia⁷).

The Australian case of *Silent Vector Pty Ltd t/a Sizer Buildings -v- Squarcini*⁸ also considered the different scenario in which the parties inserted "N/A" next to "limit of liquidated damages". In that case, the arbitrator found that the use of "N/A" indicated that the clause did not apply. Consequently, whilst the employer could not claim liquidated damages, it could claim general damages.

How do you challenge a liquidated damages clause?

Typical provisions relating to delay provide that if a contractor fails to meet a contractual completion date, then the employer will be entitled to liquidated damages at a fixed rate for each day or week of delay until the contractor completes the work. In practice, when a contractor does not meet a completion date, if the contract provides for liquidated damages, the employer will deduct the liquidated damages from the next payment due to the contractor.

The rate of liquidated damages will be negotiated between the employer and contractor. The employer will want the rate to take account of all possible consequences of the contractor's breach, whilst the contractor will want to reduce the rate in order to minimise its financial risk – part of that negotiation may include the contractor accepting a higher rate of liquidated damages in return for a lower cap on liability. If a rate can be agreed, it will then be included in the contract. The Supreme Court has emphasised that there should be a "strong initial presumption" in favour of upholding the bargain of the parties "in a negotiated contract between properly advised parties of comparable bargaining power".⁹

However, there are certain grounds on which a contractor can challenge the employer's claim for liquidated damages, including:

- The liquidated damages clause is a 'penalty';¹⁰
- The liquidated damages clause is uncertain;¹¹
- The employer didn't comply with a condition precedent;
- The contract machinery has broken down;¹²
- The employer is trying to recover liquidated damages for a breach that is outside the scope of the liquidated damages clause.

Does a liquidated damages provision continue to apply on termination of a contract?

In recent years, the often-discussed issue of whether liquidated damages provisions continue to apply on termination of a contract has been heard by the English Courts, with the Supreme Court having the final say (and overturning the Court of Appeal's decision) in the case of *Triple Point Technology, Inc -v- PTT Public Company Ltd*.¹³

The Supreme Court held that a liquidated damages clause will apply to any period of delay in completing the work up to, but not beyond, the date of termination of the contract, at which point the contractor will become liable to pay general damages for breach of contract.

In April 2024, JCT launched its new suite of contracts, starting with the Design & Build ("D&B") family of contracts. The 2024 D&B form of contract includes a new clause (2.29.5) which reflects the Supreme Court's decision in the *Triple Point* case. This new clause therefore allows for liquidated damages to accrue between the completion date and the date of termination. It also confirms that liquidated damages do not apply for the period following termination, but that is "without prejudice to and not in substitution of any other rights and remedies of the Employer", meaning that the employer's common law right to prove general damages remains.

Conclusion

Liquidated damages are commonly used in the construction industry and standard form contracts typically provide for them. However, when considering whether to include liquidated damages, care should be taken to ensure that the provisions are clear (i.e. what the liquidated damages relate to) and workable, and parties must then follow the contractual mechanism.

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Footnotes

¹ They are provided for in standard form contracts, such as Optional Clause X7 in NEC4.

² *Dunlop Pneumatic Tyre Co Ltd -v- Selfridge & Co Ltd* [1915] A.C. 847.

³ *Cavendish Square Holding BV -v- Talal El Makdessi* [2015] UKSC 67.

⁴ [2015] EWHC 283 (Comm).

⁵ [2008] EWHC 6 (TCC).

⁶ *Temloc Ltd -v- Errill Properties Ltd* [1987] 39 B.L.R. 30.

⁷ *Baese Pty Ltd -v- RA Bracken Building Pty Ltd* (1990) 6 BCL 137.

⁸ [2008] WASC 246.

⁹ *Cavendish Square Holding BV -v- Talal El Makdessi* [2015] UKSC 67.

¹⁰ *Robophone Facilities -v- Blank* [1966] 1 WLR 1428 CA at 1447; *Dunlop Pneumatic Tyre Co Ltd -v- Selfridge & Co Ltd* [1915] A.C. 847; *Cavendish Square Holding BV -v- Talal El Makdessi* [2015] UKSC 67; *Dunlop Pneumatic Tyre Co Ltd -v- New Garage & Motor Co Ltd* [1915] A.C. 79; *Eco World - Ballymore Embassy Gardens Company Limited -v- Dobler UK Limited* [2021] EWHC 2207 (TCC).

¹¹ *Taylor Woodrow Holdings Ltd & Anor -v- Barents & Elliott Limited* [2004] EWHC 3319 (TCC); *Buckingham Group Contracting Ltd -v- Peel L&P Investments and Property Ltd* [2022] EWHC 1842 (TCC).

¹² *Rapid Housing -v- Ealing Family Housing* [1984] 29 BLR 5.

¹³ [2021] UKSC 29. For more details on that case, you can read Karen Gidwani's article on the judgment here: "[Triple Point: more than simply 'liquidated damages'](#)".