

Liquidated & Ascertained Damages 2021 Update



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Recent case law developments have demonstrated that courts continue to back LAD provisions in contracts – confirming the need for contracting parties to take these provisions seriously.

Liquidated and ascertained damages ('LAD' or just 'LD', or even "Delay Damages") are a pre-determined amount agreed between the parties to a contract and are used to deal with culpable delay and specified contract breaches. LAD provisions provide certainty as to the consequences of the specified breaches, they limit liability, and are time and cost efficient. Well-drafted LAD clauses mean the parties avoid costly debates about how much the defaulter should pay for a breach. Two important decisions concerning LAD clauses have been handed down in 2021, *Triple Point Technology* and *EWB v Dobler*, dealing with the issue of calculating costs for delay and the contractual interpretation of LAD clauses, respectively.

Accrual of LAD – Return to the 'Orthodox' Approach

In July 2021 the Supreme Court handed down its judgment for *Triple Point Technology Inc v PTT Public Company Ltd*. In short, *Triple Point* confirms that LAD stop at termination. After termination damages must be proven.

The Supreme Court recognised that whilst the application of a LAD clause will be dependent on the specific drafting of that clause, certain approaches to LAD clauses that have developed at common law are "inconsistent with commercial reality" and fail to provide legal certainty on the issue of liquidated damages.

The Supreme Court highlighted that LAD clauses are intended to be used a tool of predictability and certainty for providing remedies in particular circumstances. Up to this point the accrual of LAD ended upon termination of a contract. The Supreme Court moved to restore this "orthodox" method of construction for LAD clauses: LAD clauses WILL apply up to the date of termination, unless otherwise EXPRESSLY agreed by the parties in writing.

It is now a point of law that the accrual of LAD comes to an end upon termination of a contract: after this, the aggrieved party must seek damages for breach of contract under the common law or tort law. The *Triple Point* decision removes the need to draft express provisions for the termination of a contract prior to completion of the Works in LAD clauses and provides certainty to contracting parties regarding the enforceability of LAD clauses, specifically where completion of the Works has been delayed.



Penalty clauses v. LAD

The Court in *Law v Redditch Local Board* provided a definition for a penalty clause: “If the intention of the LD’s clause is to secure performance of the contract by the imposition of a fine or penalty, then the sum specified is a penalty.” A Court will not uphold a penalty clause against a defaulting party – “The court should not be astute to descry a ‘penalty clause’” (*Robophone Facilities Ltd v Blank*). Rather, when assessing whether a clause constitutes a penalty or not, courts will, more often than not, uphold LAD.

The decisions in *Cavendish Square v El Makdessi* and *ParkingEye Ltd v Beavis* are the relevant authorities for distinguishing between penalty clauses and LAD:

“32. The true test is whether the impugned provision is a secondary obligation which imposes a detriment on the contract-breaker out of all proportion to any legitimate interest of the innocent party in the enforcement of the primary obligation. The innocent party can have no proper interest in simply punishing the defaulter. His interest is in performance or in some appropriate alternative to performance.”

So, the relevant clause must impose an obligation on the defaulting party which reflects the legitimate interests of the innocent party, rather than the clause purporting to simply penalise and punish the defaulting party. The Court recognised that the innocent party’s interest will rarely extend beyond compensation for the breach in the case of a straightforward damages clause, but compensation is not the only form of legitimate interest.

EWB v Dobler

The recent decision in *EWB v Dobler* explored the validity of a LAD clause and whether it amounted to an unenforceable and void penalty clause. The key takeaway from this decision is that the threshold to find an unenforceable penalty clause, instead of LAD, is very high.

A dispute arose over whether liquidated and ascertained damages could be accrued for late completion of the whole of the Works where two thirds of the Works were deemed to have met practical completion as EWB took partial possession of the site.

EWB issued Part 8 proceedings, seeking determination of:

- i. *Are the liquidated damages provisions in clause 2.32.1 void and/or unenforceable?*
- ii. *If so, is EWB entitled to claim general damages for delay and, if so, are any recoverable damages limited by reference to the void and/ or unenforceable provisions of clause 2.32.1?”*

Clause 2.32 provided for liquidated damages to be paid by Dobler if the Works were not completed by “the relevant Date for Completion” and no provision was included for separate completion dates for each block. The full rate of liquidated damages continued to be applicable to the reduced scope of the outstanding works. The Court then moved on to consider whether the liquidated damages provision was penal and unenforceable in the context of the Contract as whole. Applying the test set out in *Cavendish Square*, it was found that the clause was not unconscionable or extravagant to amount to a penalty for the following reasons:

- i. The clause was negotiated by the parties who were both advised by external lawyers, the Court noted Lord Legatt's position in *Triple Point* that a court should be cautious about interfering with the freedom of parties to allocate risk in their business dealings - they agreed to such a provision to limit exposure to an unknown and open-ended liability whilst simultaneously creating certainty as to the recoverable amount of compensation.
- ii. Late completion of any part of the Works would risk EWB becoming both liable for liquidated damages to the local authority and losing purchasers for the apartments. EWB had a legitimate interest in enforcing the primary obligation of Dobler to complete the whole Works by the New Completion Date.
- iii. The agreed amount of liquidated damages payable for late completion of the whole Works allowed the parties to avoid the difficult task of calculating and proving loss for different combinations of partially completed Blocks.
- iv. Neither party submitted evidence to the Court, or even suggested in their submissions, that the level of damages set out in the Contract were unreasonable or disproportionate to the probable losses suffered in the event of late completion for any or all of the Works.

In these circumstances, the contractual provisions were not found to be penalty clauses, or extravagant, exorbitant or unconscionable. The provisions created a legitimate secondary obligation which imposed detriment on Dobler proportionate to the legitimate interest of EWB in the enforcement of the primary obligation to complete the Works in accordance with the terms of the Contract.

EWB v Dobler reinforces the necessity of clearly reflecting the intentions of both parties when drafting a contract. When drafting liquidated damages clauses parties should take care to consider the impact of partial completion before the contracted Completion Date and whether their contract should purport to reduce the contractor's liability for liquidated damages in this situation. Contracting parties should also be careful to consider how the quantity of liquidated damages are to be calculated - how an employer assesses damages for loss will aid a court in deciding if these damages or 'unconscionable or extravagant'.



Quigg Golden Comment

Triple Point has provided much needed certainty to contracting parties regarding when LAD accrual begins and ends. *EWB v Dobler* has provided a tale of caution about carefully drafted LAD clauses that consider partial completion. Moreover, this decision further highlights the reluctance of Courts to go behind the allocation of risk negotiated by the contracting parties, especially when the parties enjoy similar bargaining power and have the benefit of expert legal advice throughout the negotiations of the commercial terms of the contract. The function of the court is not to relieve a party from a bad bargain, it will not imply a term unless it is necessary to make the contract work.

Quigg Golden can provide further advice and guidance on any of the issues above, do not hesitate to contact us.