

Construction Law Update

Employer Entitled to Full Liquidated Damages Despite Having Taken Possession of Majority of Works

In the recent case of *Eco World – Ballymore Embassy Gardens Company Ltd v Dobler UK Ltd* [2021] EWHC 2207 (TCC), the TCC considered the construction and enforceability of a liquidated damages clause where the employer had taken partial possession of the works.

Background

On 11 July 2016, Eco World – Ballymore Embassy Gardens Company Ltd (“**EWB**”) engaged Dobler UK Ltd (“**Dobler**”) to carry out the design, supply and installation of the façade and glazing works (the “**Works**”) for part of a development of apartments known as Embassy Gardens in London (the “**Contract**”).

The Contract contained a liquidated damages (“**LDs**”) clause that entitled EWB to recover £25,000 per week for delay to completion of the entire Works beyond the contractual completion date, subject to a four-week grace period and a cap of 7% of the total Contract sum.

The Contract did not provide for sectional completion of the Works, however, there was provision for EWB to take early possession of “*any part of parts of the Works*” from Dobler at “*any time*” prior to practical completion of the whole Works. In such circumstances, the Contract provided that “*practical completion of [that part] shall be deemed to have occurred*” on the date possession was taken.

A deed of variation altered the contractual completion date to 30 April 2018, however, the Works were not completed by that date. EWB took possession of two of the three blocks forming the Works around 15 June 2018. Practical completion of the Works was certified on 20 December 2018.

A dispute arose over the true value of the final account which largely turned on the validity and application of the LDs clause in the Contract.

The Proceedings

In October 2020, EWB issued Part 8 proceedings seeking the Court’s determination of the following questions: (i) was the LDs clause in the Contract void and/or unenforceable?; and (ii) if so, was EWB entitled to claim uncapped general damages for delay?

Was the LDs clause void/unenforceable?

EWB claimed that the LDs clause was unenforceable because it did not contain a mechanism for reducing the level of LDs to reflect EWB taking early possession of parts of the Works and therefore EWB was entitled to claim uncapped general damages.

Dobler argued that the LDs clause was valid and that the Contract contained an “*effective mechanism*” for reducing LDs to reflect EWB’s partial possession. Alternatively, Dobler argued that if the LDs clause was void, general damages were nevertheless limited to the same cap as LDs would have been.

In deciding whether the LDs clause was void and/or unenforceable, the court had to consider whether the clause was (i) sufficiently clear and certain; and (ii) a penalty.

Was the LDs clause sufficiently clear and certain?

Having considered the usual rules of contractual interpretation, the court concluded that the effect of the LDs clause was “*reasonably clear and certain*,” which distinguished it from similar cases referred to the court by EWB. Dobler was obliged to complete *all* of the Works, to achieve ‘practical completion’. If Dobler failed to complete *any* of the Works by the contractual completion date, EWB would be entitled to LDs at the full rate set out in the Contract.

Whilst the effect of EWB taking possession of part of the Works meant that that part was agreed to be practically complete for limited purposes, the LDs

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clause did not provide that the rate of LDs was to be reduced accordingly.

Was the LDs clause a penalty and therefore void?

Given the court's findings as to the true construction of the LDs clause, it turned to consider whether the same was a penalty. EWB's key argument in support of this position was that the LDs clause used the same LDs rate irrespective of whether the late completion concerned *all or part* of the Works, despite the fact that different levels of loss would be incurred.

The court considered the "penalty test" set out in *Cavendish Square Holding BV v Makdessi* [2015] UKSC 67 which asks whether a LDs clause is "extravagant, exorbitant or unconscionable". In determining this "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". In addition, "where the test is to be applied to a clause fixing the level of damages to be paid on breach, an extravagant disproportion between the stipulated sum and the highest level of damages that could possibly arise from the breach would amount to a penalty and thus be unenforceable".

Applying the "penalty test" to the LDs clause, the court held that "the liquidated damages provision in this case [was] not unconscionable or extravagant" meaning it was not a penalty. The four key factors in determining this were that: (i) the LDs clause was negotiated by the parties with professional legal advice; (ii) EWB had a legitimate interest in ensuring Dobler completed the whole Works by the completion date; (iii) the quantification of damages without the clause would be difficult; and (iv) neither party suggested the level of LDs was unreasonable or disproportionate. The LDs clause was therefore valid and enforceable.

Would EWB have been entitled to claim uncapped general damages for delay?

Whilst not strictly necessary given its findings in relation to the LDs clause, the court nevertheless considered whether EWB would have been entitled to

claim uncapped general damages had the LDs clause been deemed unenforceable.

It is common ground that where a LDs clause is found to be unenforceable an innocent party will instead be entitled to general damages; the question for the court was whether anything in the LDs clause would have acted as a cap to those damages.

Having considered relevant case law, the court concluded that "even where a LDs clause is found to be wholly unenforceable as a penalty, it may on a true construction be found to operate as a limitation of liability provision." Applying established principles of contractual interpretation to the LDs clause the court found that the LDs clause served two distinct purposes: (i) to provide for and quantify automatic liability for delay damages of £25,000 per week; and (ii) to limit Dobler's overall liability for late completion to 7% of the total Contract sum. In the event the LDs clause was found to be unenforceable, therefore, the court would still have given effect to the overall cap set out in the same meaning EWB's entitlement to general damages would have been capped at 7% of the total Contract sum.

Analysis

This case considers several key issues relating to the construction and enforceability of LDs clauses. Of particular note is the court's decision that a LDs clause which fails to reduce the rate of LDs in line with possession of the site is not necessarily unenforceable, a clear move away from the past focus on whether LDs in a contract represent a genuine pre-estimate of loss.

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