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Further Court Guidance on the Enforceability of Liquidated Damages

Shortly after the long-awaited Supreme Court judgment on the operation of liquidated damages in the event of termination, the English courts have delivered another important judgment on the operation of liquidated damages, this time in the event of early take-over or possession of the works by the employer.

Provisions regarding early take-over or possession are common in construction contracts, offering flexibility to employers by allowing early use of part of the works that are complete. However, the interplay between take-over provisions and liquidated damages (“LD”) provisions is often forgotten when drafting construction contracts, resulting in disputes over what happens to the agreed rate of LDs when part of the works is taken over early and is therefore deemed completed. Do the LDs become a penalty, which is void and unenforceable? If they do become a penalty, does the limit on the maximum level of LDs payable also fall away, exposing the contractor to a much higher, or potentially even unlimited, liability for delay?

The English law position on these issues was considered in detail by the Technology and Construction Court in *Eco World – Ballymore Embassy Gardens Company Limited (“EWB”) v Dobler UK Limited (“Dobler”)* [2021] EWHC 2207 (TCC). In its decision, the Technology and Construction Court held that there was no general principle of English law that LD provisions automatically become unenforceable where part of the works is taken over by the employer and there is no corresponding reduction in the level of LDs payable. The enforceability of the LD provisions depends on the proper construction of the terms of each contract; and in the case of the contract between EWB and Dobler, the LD provisions were not a penalty and were enforceable even after early take-over.

While the court emphasised that its decision was based on the particular wording of the contract between EWB and Dobler, it nevertheless serves as a broader reminder that English courts will not easily hold LD provisions void and unenforceable. It also highlights the English courts’ desire to give effect to the parties’ bargain and not interfere in their freedom to agree commercial terms.



Background

The underlying dispute concerned delay to the design, supply and installation of the façade and glazing works at an apartment building in London.

Under the contract (which was based on the JCT 2011 Construction Management Trade Contract form) and a subsequent deed of variation, Dobler was required to achieve practical completion of the whole of the works by 30 April 2018. If it failed to do so, it would be liable for LDs of £nil per week for the first 4 weeks of delay and then £25,000 for each further week of delay, up to a maximum of 7% of the final contract price. The contract also permitted EWB to take over part of the works prior to practical completion.

The works were delayed and on 15 June 2018 EWB took over those blocks of apartments that were complete, in order to mitigate its losses. Practical completion of the whole works was finally achieved on 20 December 2018.

Following completion of the works, the parties went through three adjudications regarding the sums payable to or from Dobler, including Dobler's liability for LDs. During the adjudications, it became apparent that EWB may be able to recover significantly higher damages for delay if the LD provisions in the contract (including the cap on such LDs) were unenforceable. EWB therefore started proceedings in the Technology and Construction Court, arguing that:

1. the LD provisions are void and/or unenforceable, because the contract did not provide for a reduction in LDs following EWB's partial take-over of the works and the LDs therefore became a penalty; and
2. EWB is entitled to general damages for delay instead and such damages are not limited to a maximum of 7% of the final contract price, as the cap only applied to the contractual LDs.

The Court's Decision

Are LDs void and unenforceable where the employer takes over part of the works?

The court stated that there was no "*inflexible rule of law*" in English law that LD provisions will never be enforceable where part of the works is taken over by the employer with no corresponding reduction in the LDs payable. Whether the LD provisions will be valid after partial possession or take-over by the employer depends on the precise wording of the contract.

The court held that the LD provisions in the contract between EWB and Dobler were clear, certain and operable even after EWB's partial take-over, and were not extravagant, exorbitant or unconscionable so as to make them void or unenforceable, for the following reasons:

1. The LD provisions were negotiated by the parties with the benefit of advice from external lawyers.
2. EWB had a legitimate interest in enforcing Dobler's obligation to complete the whole works on time, as the delay would likely impact fit-out and finishing works by other contractors, expose EWB to liability for LDs to the local authority acquiring some of the apartments and result in loss of purchasers for other apartments.
3. Quantification of damages suffered by EWB would have been difficult, a difficulty that has been avoided by the parties by setting the rate of LDs in the contract.
4. The level of LDs agreed in the contract was not unreasonable or disproportionate to the likely losses suffered by EWB due to the late completion of blocks that were not taken over early.

In her judgment, O'Farrell J also stated that while the contract terms gave EWB the discretion to levy LDs at a lower rate than £25,000 per week, there was no need to imply a term that EWB should exercise such discretion "*in a rational or reasonable manner*". EWB had an express absolute contractual right to receive LDs at the rate of £25,000 per week and was entitled to exercise that right as it saw fit.

Does the cap on LDs apply to general damages for delay?

The court acknowledged that it did not need to consider whether general damages would be capped at 7% of the final contract price, since it held that LDs (rather than general damages) were due. However, O'Farrell J decided to offer some views on this frequently contested issue anyway.



Again, the court emphasised that, in accordance with general principles of interpretation under English law, each clause setting the maximum level of LDs payable would have to be interpreted in its own right. Whether such cap would also apply to general damages for delay would depend on the proper construction of each particular contract.

In this instance, the court held that the cap would apply to general damages if the LD provisions were void or unenforceable due to being a penalty. This is because on an objective understanding of the parties' commercial agreement, the LD provisions in the contract between EWB and Dobler served two purposes: to quantify the automatic liability for damages in the event of delay and to limit Dobler's overall liability for delay. If the first part of the LD provisions were void or unenforceable, the second part containing an express limitation on liability at 7% of the contract price would remain valid and continue to apply.

Discussion and Key Takeaways

There is no doubt that the judgment in *Eco World – Ballymore Embassy Gardens Company Limited v Dobler UK Limited* is important, as it tackles two issues on which there is limited authority from the English courts despite the fact that they arise in disputes quite frequently. While the court emphasised that its decision was based on the particular wording of the contract between EWB and Dobler, it is likely to have a wider impact and influence on employers and contractors alike.

It serves as a useful reminder of the courts' attitude towards LD provisions, confirming that it is difficult to argue under English law that LDs are a penalty and therefore void and unenforceable. It also highlights the courts' desire to give effect to the parties' bargain and not interfere with their freedom to agree commercial terms and to allocate risk in their business dealings, particularly when the terms were negotiated and agreed with the help of external lawyers.

Further, and together with the Supreme Court's earlier judgment in *Triple Point*, the decision recognises the importance of certainty when addressing the risk and consequences of project delay. By enforcing LD provisions, the courts provide an employer certainty on the amount it will recover (without having to spend time and money on proving its losses) and the contractor certainty on its exposure to damages in the event of project delay.

In addition, the judgment serves as an important reminder that parties should, at all times, draft their contract in a way that clearly matches their intentions. In the context of project delay, it makes sense to pay particular attention to the level of LDs, any limits on their recovery, whether sectional completion may be required or preferred, whether early possession or take-over may be required, and the impact of such take-over on the contractor's obligations and the enforceability of LD provisions.

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