

LIQUIDATED DAMAGES CLAUSES

By their very nature, liquidated damages clauses in contracts cause an adversarial relationship to exist from the outset on a construction project. Such clauses are used in contracts to assign financial responsibility to the contractor for damages that are likely to be incurred by the owner if the specified schedule is not met. The BC Construction Association recommends against their incorporation into construction contracts.

The causes for unrealistic or condensed schedules usually lie in the early stages of the project, either in obtaining the necessary government approval or budget approvals, or in the design phase, etc. The liquidated damages clause is then often used to impose a financial penalty on the last person in the construction chain to make up for time that contractor is often not even responsible for losing. Experience has shown that liquidated damages clauses have usually been used where the schedule may be difficult or impossible to achieve.

Hence a prudent bidder has to make a choice:

1. Refuse to bid the project.
2. Qualify the bid to exclude the liquidated damages clause.
3. Make allowance in the bid for the specified damages.

None of these choices best serves the Owner of the project. Should a liquidated damages clause be used, its very nature causes an adversarial relationship to exist between all parties to the construction project, which permeates to all levels, Owner, Consultant, Sub-contractor, Suppliers. These are the very people who should be working together to make the schedule work; instead, they are using valuable time and energy to justify extensions and convey blame to other parties.

If an Owner feels compelled to resort to a liquidated damages clause, BCCA recommends that the liquidated damages be matched by equivalent incentive payments to the Contractor for earlier completion. If the Owner will suffer from late completion, it will likely benefit by earlier completion than scheduled. We further recommend that the clause be drafted carefully since potential changed work and unavoidable delays will make it difficult to administer the liquidated damages, impartially or at all. Compensation should be reasonable, realistic, itemized and accountable; it should be itemized as liquidated damages in the bid documents and calculated at a per diem rate based on the evaluation of the most probable cost to the owner.

A liquidated damages clause, in order to be sustainable, must provide for an amount that is a genuine pre-estimate of the cost or damage that an owner will likely incur if a scheduled date is not met. It should not be used as a penalty. If the amount chosen for the liquidated damages is not excessive and has some relationship to the loss likely to result from the delay, the clause will generally be upheld as being a genuine pre-estimate of the damages likely to be incurred. If, on the other hand, a liquidated damages clause is excessive and objectively unreasonable it will probably be considered a penalty clause, which is unenforceable.

In order to entitle the owner to such liquidated damages, the delay must be one for which the contractor was responsible at law. In other words, the contractor must be guilty of a breach of contract in respect of which the owner is entitled to damages. Accordingly, contributing and concurrent delays by the Owner or Consultant should not lead to the application of a liquidated damages clause.

It is in the best interest of all parties in a normal construction project to complete the project in the shortest allowable time. Job overhead costs increase for every hour and/or day the completion of the project is delayed.

Liquidated damages clauses are usually counter-productive to the successful and harmonious completion of a construction project. Accordingly, it is in the best interest of all parties that unnecessary liquidated damages clauses be excluded from construction contracts.



BC Construction
Association North
3851 Eighteenth Ave
Prince George, BC
V2N 1B1
Ph: 250.563.1744
Fax: 250.563.1107



Southern Interior
Construction Assn
104-151 Commercial Dr
Kelowna, BC
V1X 7W2
Ph: 250.491.7330
Fax: 250.491.3929



BC Construction Assn
Vancouver Island
1075 Alston Street
Victoria, BC
V9A 3S6
Ph: 250.388.6471
Fax: 250.388.5183



Vancouver Regional
Construction Assn
3636 East 4th Ave
Vancouver, BC
V5M 1M3
Ph: 604.294.3766
Fax: 604.298.9472