

Liquidated Damages vs Delay Damages: What is the difference?

Where a contractor fails to complete works by the date for completion the typical expectation is that such a breach would allow the principal to claim damages calculated as the actual loss resulting from the delay to completion.

Alternatively, the contract may allow for the contractor to claim damages for delay caused by the principal, or in some cases a wide range of events that are not of their causing (such as wet weather).

The principle of damages for delay (which is what liquidated damages are) has a few elements that need to be understood:

- First, the [construction project](#) must have a contract.
- Second, that contract must have a date for when the works are to finish, commonly the date for Practical Completion.
- Third, the contract needs to include a mechanism to claim liquidated damages or delay damages.

What are liquidated damages?

Liquidated damages (LDs) are those which set a rate under the contract that applies in the event a particular breach of the contract occurs. The idea behind this is that it removes the need to prove an entitlement to damages at general law. Most commonly, liquidated damages are for the owner, principal, and head contractor.

What are delay damages?

Delay damages (as they are commonly known) are still a form of liquidated damages but are usually the defined term used by contractors in claiming damages. They are most commonly used when seeking damages arising from the principal's delay.

While LDs are able to be applied to any breach in respect of which a genuine pre-estimate of the losses suffered may be made, the most common breach to which LDs apply is the failure of a contractor to reach completion in the stated time.

Why are damages clauses so important?

LDs clauses are of critical importance for principals (or for down the line contracts between head contractors and subcontractors) as they provide:

- A clear and defined consequence for the contractor if it fails to carry out work efficiently, and thereby achieve practical completion on time; and
- A right for principals to claim compensation at an agreed rate for their genuinely estimated loss incurred as a result of certain delays.

LDs clauses, believe it or not, are also beneficial for contractors, as they allow the parties to apply a pre-determined rate of damages and avoid costly and time-consuming dispute resolution processes arguing about what the actual damages are.

LDs clauses also provide contractors with a means to limit their liability in the event delays occur, by including a cap on the amount claimable.

Delay damages clauses are also critical. The contractor must consider what is a reasonable genuine pre-estimate of loss if the works are delayed.

Contractors should be methodical and considered in calculating the amount to be included in a delay damages amount.

How to calculate a liquidated damages amount

When calculating an amount to be paid in the event of a breach, developers, principals and head contractors should consider:

- The interest cost on the funded amount of the project (per day);
- The lost opportunity cost (either renting or sale (per day));
- Any employee expenses,

And many other project-specific risks.

How to calculate a delay damages amount

When calculating an amount to be paid in the event of a breach, subcontractors and head contractors should consider:

- The potential daily cost of employees and plant on site;
- Daily business operation costs

And many other project-specific risks.

How to ensure liquidated damages clauses are enforceable

The most common way a LDs clause may be contested is where it is argued to be a penalty and not a genuine estimate of the losses that will be incurred as a result of delays.

A clause will be considered a penalty where the rate specified in the contract is wholly out of proportion to the interests of the non-defaulting party.^[1] Therefore, a lot hinges on the proposed activities that will result from the project and the degree to which the non-defaulting party will forego its planned income.

In *Grocon Constructions (Qld) Pty Ltd v Juniper Developer No. 2 Pty Ltd & Anor* [2015]^[1], the Queensland Supreme Court held that in determining whether a rate of LDs stipulated in a contract constitutes a genuine pre-estimate of the non-defaulting party's loss, consideration must be given to the parties' negotiations in respect of LDs.

In *Juniper*, the parties had paid particular attention to the LDs clause and Juniper had even issued a detailed breakdown of the calculations of its potential losses, identifying what it considered would be its loss if practical completion was not achieved on time.

The Supreme Court also found it highly relevant that the parties were commercially savvy and had equal bargaining power at the time of negotiating the contract. The amount of evidence the defaulting party was provided with regarding the estimates and calculations of potential

losses was pivotal in the Supreme Court finding the LDs clause to be a genuine pre-estimate of loss.

This means the losses that will be suffered by the non-defaulting party, as a result of it being unable to use the works or the site from the date it could expect to as per the time frame for completion, must be accurately reflected by the rate specified in the contract. For example, if the principal intends to use the works or the site for manufacturing or other business purposes, the rate of LDs should take into account the lost profit and costs associated with the principal having to delay the commencement of its business operations.

How are other damages excluded?

The courts have taken and upheld the approach that general damages are typically only to be excluded where it is expressly stated in the construction contract.

Claiming losses for delay beyond liquidated damages

So what happens if LDs are not listed as the sole remedy for delays?

An interesting situation arises where LDs are not specifically listed as the sole remedy for delays in a construction contract.

In many instances, contractors have sought to rely on the fact that LDs were stated in their contract at a rate of “\$NIL” or “N/A” as the basis for arguing that general damages were also excluded from the contract.

However, as the courts have held in cases such as *J-Corp v Mladenis* [2009] WASCA, if the parties have agreed to a positive amount for LDs, this will reflect the intention of the parties to exclude the right to recover general damages. The Western Australian Court of Appeal held that as no clear and unequivocal words were present in the contract excluding the owners’ right to claim general damages for delay, but merely wording that provided for “\$NIL” liquidated damages, the owners remained entitled to claim unliquidated damages.

In *Adapt Constructions Pty Ltd v Whittaker* [2015], the ACT Supreme Court found that a construction contract based on a standard form which left blank the amount for LDs to be paid for delays did not prevent the principal from recovering unliquidated damages at common law. The ACTSC suggested that in determining the parties’ intention to allow a principal to claim unliquidated damages, the following aspects of the contract must be considered:

- Whether the parties intended for the principal to have that entitlement, having regard to the language of the contract;
- if the contract provides that the principal may elect to claim liquidated damages, this may indicate that the parties intended that the principal would be entitled to claim both liquidated and unliquidated damages;
- if the contract provides for liquidated damages to be payable automatically, this may indicate that liquidated damages are intended to be the only remedy; and
- an intention to exclude a right to unliquidated damages at common law must be expressed clearly in the contract.

As is evident from the various courts’ comments on the issue, the prudent course of action is to include clear and unequivocal words that reflect the parties’ intentions. Do not assume the

party on the other side of the contract has the same expectations as you, as the costs resulting from delays can add up at an alarming rate.

If you have any questions regarding your liability to pay or entitlement to receive liquidated damages, please do not hesitate to contact [Morrissey Law + Advisory](#).

This article was prepared by Hamish Geddes.

[1] *Paciocco v Australia and New Zealand Banking Group Ltd* (2016) 333 ALR 569.

[2] *Grocon Constructions (Qld) Pty Ltd v Juniper Developer No. 2 Pty Ltd & Anor* [2015] QSC 102.

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