

## Liquidated Damages: Are They the Owner's Sole Source of Recovery for Delay Damages?

Construction contracts often contain liquidated damage ("LD") provisions. Basically, these LD provisions specify in advance the amount of damages recoverable for delays in completing the contract.<sup>1</sup> The LDs are usually stated in the form of a dollar amount of damages per day of delay. The purpose of LDs is to provide an agreed quantification for damages that are uncertain or difficult to calculate.<sup>2</sup> Some examples of LD provisions include:

- Failure to complete the work by the Completion Date specified in Section 2 will result in the assessment of liquidated damages of \$2,000 per calendar day until the work is complete.
- Should the Contractor fail to complete the work within the required number of working days as determined under the provisions of Section 6 or within such time as may have been allowed by extension, the Engineer shall deduct from any moneys due or coming due to the Contractor the amount indicated in the Schedule of Liquidated Damages for each calendar day that the work shall remain uncompleted. This sum shall be treated, not as a penalty, but as fixed, agreed and liquidated damages.

The courts will uphold LD provisions if the damages are difficult to ascertain and the agreed amount is fair and reasonable so that it does not constitute a penalty.<sup>3</sup> As a corollary rule, the courts have frequently stated that LDs preclude recovery of actual damages.<sup>4</sup> They view a LD provision as both a sword and a shield. A LD provision allows the injured party to recover damages without proving actual damages. At the same time, a LD provision shields the breaching party from damages in excess of the agreed LDs even if the actual damages are provable and greater than the LDs. The injured party cannot recover both actual and liquidated damages for the same breach.

As with most general rules, however, the rule that LDs preclude actual damages is not as simple as it sounds. In some circumstances, a party can recover both LDs and actual damages under the same contract. The courts have held that a contract can provide that LDs are recoverable for certain types of damages caused by delay while actual damages are recoverable for other types of delay damages.<sup>5</sup>

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<sup>1</sup> *Gilbane Building Co. v. The Nemours Foundation*, 666 F. Supp 649, 652 (D. Del 1985).

<sup>2</sup> *Id.* at 652.

<sup>3</sup> *J.R. Stevenson Corp. v. County of Westchester*, 493 N.Y. S.2d 819 (2d Dept. 1985).

<sup>4</sup> 666 F. Supp at 652; *Harper v. L&M Granite Co., Inc.*, 197 Ga. App. 157, 397 S.E.2d 739 (1990); *International Fidelity Ins. Co. v. Chautauqua*, 245 A.D.2d 1056, 667 N.Y.S.2d 172 (4<sup>th</sup> Dept. 1997).

<sup>5</sup> 666 F. Supp at 652; *Twin River Construction Co., Inc. v. Public Water District No. 6*, 653 S.W.2d 682 (1983).

The key issue in such cases is the scope of the LD provision. In deciding this issue, the courts apply standard principles of contract construction. They focus primarily on the language of the LD provision but they also view the contract as a whole and consider other provisions that might have a bearing on the issue. For example, the LD provision might state specifically that the LDs are intended to quantify the lost income to the owner if construction of an office building is delayed. In that case, the court probably would allow recovery of actual damages other than lost income sustained as a result of the delay. Even more clearly, if the LD provision states that it covers lost income but expressly excludes damages for the owner's extended inspection and supervision costs, those costs would be recoverable as actual damages in addition to the LDs.

However, in many cases, the contract is not that clear. A LD provision typically refers to damages caused by delay. It often does not specify the types of damages included in the LDs. One interpretation of such a provision is that every type of damage flowing from the delay is included thus barring recovery of any additional actual damages for delay. However, the injured party will sometimes argue that another provision in the contract evidences an intent to exclude certain types of actual damages from the LD provision.<sup>6</sup> In one such case, the court held that LD provisions do not preclude recovery of actual damages unless the contract expressly states that damages other than those enumerated are not recoverable.<sup>7</sup> Although the contract in that case specified LDs for each calendar day that the work remained uncompleted after the scheduled completion date, the owner asserted that an indemnity provision in the contract authorized recovery of payments to other contractors for additional costs caused by the contractor's delay.<sup>8</sup> The court agreed and allowed the owner to recover actual damages for additional costs charged by the follow-on contractors.

Similarly, another court held that a LD provision did not bar recovery of actual damages incurred by the owner when a contractor's delay caused a follow-on contractor to incur additional costs.<sup>9</sup> Although the contract contained a standard LD clause for delay damages, the court determined that a separate provision in the contract indicated an intent to exclude certain types of damages from the LDs. The separate provision stated that the contractor was liable to the owner for additional costs incurred because of the failure of the contractor to complete its work on time. The court allowed the owner to recover LDs and the additional costs charged by other contractors because of delays by the original contractor. The court appeared to distinguish between damages incurred directly by the owner because the project was not completed on time and indirect damages incurred by follow-on contractors that were chargeable to the owner. In its view, the LDs encompassed the former but not the latter.

In contrast, other courts, while recognizing that contracts can provide for LDs and actual damages for the same delay, have been more restrictive in their contract interpretation. For example, one court held that despite a separate provision regarding the contractor's liability for damages to other contractor's work or property, the LD clause encompassed all damages caused by delay in completing the work, including the owner's additional payments to other contractors.<sup>10</sup> In another case, the court held that a broadly worded LD provision precluded the owner from recovering actual damages from a contractor in the form of additional costs paid to follow-on contractors as a

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<sup>6</sup> *El Dorado Irrigation District v. Traylor Bros. Inc.*, 2006 WL 38593 (E.D. Cal 2006).

<sup>7</sup> *Van Kirk v. Green Construction Co.*, 466 S.E. 2d 782 (W. Va., 1995).

<sup>8</sup> *Id.* (The indemnity provision stated that "The Contractor shall indemnify and save harmless the Department . . . from all suits, actions or claims of any character brought because of any injuries or damage received or sustained by any person . . . on account of the operations of the Contractor . . . or because of any act or omission, neglect or misconduct of the Contractor.") *See also* *Saturn Construction Co., Inc. v. Connecticut*, 1994 WL 590604 (Conn. Super. 1994).

<sup>9</sup> *Hillsborough County Aviation Authority v. Cone Brothers Contracting Co.*, 285 So.2d 619 (Fla. App. 2 Dist. 1973).

<sup>10</sup> *Gilbane Building Co. v. The Nemours Foundation*, 666 F. Supp 649, 653 (D. Del 1985) (The separate provision stated that "if [a] separate contractor sues . . . the Owner on account of any damage alleged to have been caused by the Contractor, . . . the Contractor . . . shall defend such proceedings . . . and . . . pay [any judgment] . . .")

result of the contractor's delay.<sup>11</sup> Even though the contract also contained a provision specifically addressing the contractor's responsibility for such damages, the court concluded that the conflict between the two provisions created an ambiguity and construed the contract against the owner because it had drafted the contract.

Of course, one way to avoid any ambiguity and protect the contractor from delay damages other than LDs is to include in the LD provision a clear statement of the parties' agreement that the owner's sole and exclusive remedy for delay is limited to the LDs. The exact wording and enforceability of such a provision may vary by jurisdiction. However, the following language is an example containing some of the key concepts.

Notwithstanding any other provision of this contract, the only damages that the Owner may recover for delay by the Contractor in completing this contract or any intermediate milestone or deadline are the liquidated damages provided in this paragraph. This paragraph provides the sole and exclusive remedy for the Owner regarding damages caused by the Contractor's delay in performing this contract and bars recovery of any separate damages for delay, including, but not limited to, any damages for any indemnity obligation, any additional or extended inspection or supervisory costs, any attorneys, architect or engineer fees, any fees for consultants, any loss of income or profits, and any additional payments to other contractors or subcontractors of any level for costs or damages caused by the Contractor's delay.

In summary, the general rule is that LDs preclude recovery of actual damages. However, it is not safe to assume that a LD provision will bar recovery of actual damages in all cases. A beneficiary of a LD provision can sometimes recover actual damages as well, if the scope of the LD provision does not encompass damages of that type. Therefore, in analyzing this issue, it is important to consider the exact language of the LD provision and the nature of the actual damages in comparison with the types of damages intended to be covered by the LDs. In addition, the contract must be viewed as a whole to determine whether there are provisions other than the LD provision that address specific types of damages and indicate an intent to exclude such damages from the LD provision. One way to assure that LD's are the sole and exclusive remedy for the contractor's delay is to include in the LD provision a clear statement to that effect.



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<sup>11</sup> *Edward Kraemer and Sons, Inc. v. Kansas City*, 1995 WL 405098 (D. Kan. 1995) (The LD provision covered damages suffered because of "interference with business, inconvenience to the public, added cost of engineering, administration, supervision, inspection, maintenance of detours, and other items which have caused an expenditure of public funds resulting from [the Contractor's] failure to complete the work within the time specified in the Contract".)