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Construction Law Update

Enforceability of Liquidated Damages

In the recent case of *GPP Big Field LLP & Anor* ("**GPP**") *v Solar EPC Solutions SL* ("**Solar**") [2018] the Commercial Court considered a number of issues relating to the enforceability of liquidated damages, an issue which commonly arises in construction disputes.

Background

GPP entered into five engineering and procurement contracts with Prosalia UK Ltd for the construction of solar power generation plants in the UK. Prosalia became insolvent and GPP claimed against Solar, Prosalia's Spanish parent company and guarantor under four of the contracts, for liquidated damages for Prosalia's failure to commission each of the plants by the date specified in the relevant contract.

Was the liquidated damages clause a penalty?

Solar argued that the rate of liquidated damages could not have been based on any genuine pre-estimate of loss (and was thus a penalty) because each of the contracts stated the same rate of liquidated damages, despite the fact that the loss which GPP was likely to suffer as a result of delay depended on the output of each plant and the prevailing electricity price, which differed in each of the contracts. In addition, each clause referred to the amount as a "penalty".

The Court rejected this argument. GPP and Prosalia were experienced and sophisticated commercial parties of equal bargaining power and the sum specified was neither exorbitant or unconscionable in comparison with GPP's legitimate interest in ensuring completion of the projects on time. As for terminology, the contracts also used the term "Delay Damages" but, in any event, the use of the term "penalty" was not conclusive, as the Court looks to the substance of the term and not the label the parties attached to it.

Did liquidated damages continue after termination?

GPP terminated one of the contracts before commissioning of the plant had been achieved. In that case, Solar argued that its liability for liquidated damages ended when GPP terminated the contract. However, relying on the decision in *Hall v Van Den Heiden (No 2)*, the Court held that liquidated damages continued to accrue until the actual date of commissioning and did not cease on termination.

Could GPP claim common law damages as well as liquidated damages?

As part of the Renewable Obligations scheme in the UK, accredited energy generators receive Renewable Obligations Certificates ("ROCs") which can be sold to other electricity suppliers for a premium. Delays to commissioning led to some of the projects being eligible for ROCs of a lower value than expected. Therefore, and in addition to the liquidated damages it had claimed, GPP claimed unliquidated damages to compensate it for these shortfalls. Solar argued that GPP's entitlement to claim damages was limited to the liquidated damages only.

The Court held that failure to achieve ROCs of the required value was a consequence of the failure to achieve commissioning on time and was not a separate breach. Ordinarily, this would have meant that the losses were compensated by the liquidated damages.

However, the Court also found that the contracts treated the losses stemming from failure to achieve the required value of ROCs as falling outside the ambit of the liquidated damages provision. Central to the Court's finding on this point was the fact that the contracts provided an express right of termination for failing to achieve the stated value of ROCs. On termination, the parties were obliged to attempt to agree a revised price and the contracts stated the intended value of ROCs *"for guidance in the negotiations*". This indicated that the parties intended that, in addition to liquidated damages, GPP would be entitled to separate compensation in respect of a shortfall in the value of ROCs. Further, the contracts expressly stated that in the event no agreement was reached, GPP had the right to claim damages.

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Accordingly, GPP was entitled to damages in respect of the shortfall in value of the ROCs in addition to its entitlement to liquidated damages.

Could Solar rely on force majeure?

Solar argued that the delays to one project had been caused by force majeure, which relieved Prosalia from its obligation to achieve commissioning by the contractual date. It argued that protests carried out by local residents amounted to "disturbance, commotion or civil disorder" and prevented progress with the works. The contract required that should a party consider a force majeure event to occur, it must notify the other party of the same without unjustified delays. A separate provision imposed general requirements for giving and receiving notices and communications. The Court held that an effective notice of a force majeure event had to comply with these requirements and that Prosalia had failed to provide a compliant notice. The Court also found that the delay was caused by Prosalia's assessment that, given the strength of the local opposition, it was unlikely to get the necessary planning permissions for its originally intended substation location and cable route. Under the terms of the contract it was Prosalia's responsibility to obtain these. The risk that they could not be obtained was therefore the Prosalia's and it was this that caused the delay, not the protests themselves. Accordingly, it was held that the facts complained of did not amount to a force majeure event and notice had not been given as required in any event.

Analysis

The decision that the liquidated damages clause was not a penalty is unsurprising. The courts will almost always uphold a liquidated damages provision in a negotiated contract entered into between two commercial entities of equal bargaining power.

However, other elements of the decision are more controversial. Despite the decision in *Hall v Van Der Heiden (No 2)*, the orthodox view remained that liquidated damages provisions do not survive termination because the contractor no longer has control of the time for completion. Whilst the contracts in this case related to energy and power generation, this decision will surely change the balance of that argument and the issue may need to be resolved by the Court of Appeal in the future. In the meantime, parties should ensure that the terms of their contract are clear as to what the procedure is, and what their rights are, as a consequence of termination.

Further, the decision raises questions as to when delay related losses can fall outside the ambit of a liquidated damages provision. The conclusion reached in this case seems to have been based on the fact that the contract included a separate compensation mechanism for failing to achieve ROCs of the required level, but the case could serve as precedent for a wider principle. Accordingly, parties should make clear exactly what losses are covered by their liquidated damages provisions.

Finally, the decision that the contractual notice requirements applied to a notification of a force majeure is a useful reminder of the need to understand notice requirements and the serious consequences of failing to adhere to them. In this instance, should the Court have accepted that there was a force majeure event, the failure to notify GPP would have deprived Prosalia/Solar of its right to an extension of time.

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