Two wrongs don't make a right – or do they?

In Part 1 of Nigels’ article he concluded with the question as to whether two failures, one by the owner in hindering the contractor’s performance, and one by the contractor in failing to give notice of said delaying event, give the owner an entitlement to recover liquidated damages in circumstances where it has clearly delayed the works? Part 2 provides the answer.

To the lay person the proposition that two wrongs make a right may sound inequitable. However, it has been the subject of much debate over recent years with conflicting court decisions.

It has long been established in many common law jurisdictions that a party cannot insist upon the performance of a condition where that party is the cause of said non-performance.

This doctrine, commonly referred to as the Prevention Principle, has long been applied to construction contracts. It can be traced back to the old English case of Holme v Guppy (1838). In this case the contractor failed to complete its works at a brewery within the stipulated time, but avoided liquidated damages for late completion as part of the cause was delay by the employer in giving possession and delay by the employers own workmen.

A more recent influential case is that of Peak Construction v McKinney Foundations (1970) where the employer delayed the contractor and it was held that the employer could not require completion by the original contract completion date nor could it rely on the liquidated damages clause given its own complicity in the cause of the delay.

It should be noted that in both these cases the contract did not provide any expressed provision for the granting of an extension of time due to the employer caused delays. Nevertheless, support to this position was also provided in 1999 in the Australian case, Gaymark Investments Pty Ltd v Walter Construction Group Ltd. It was an appeal from the decision of an arbitrator that the Prevention Principle prevented the employer from deducting liquidated damages, even though the contractor had failed to satisfy the notice requirements for an extension of time. It was held that the Prevention Principle presented an impediment to the employers claim for liquidated damages based on delays of its own making and the arbitrators finding was upheld.

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As time has gone by, construction contracts have become more defined and onerous. Notice clauses are often now drafted as a “condition precedent” to an entitlement to an extension of time. The problem is that if the contractor does not give notice when it is condition precedent, the employer may have a right to the benefit of the liquidated damages even though he is the cause of the delay, contrary to the Prevention Principle.

Such a view was expressed in another Australian case, that of Peninsula Balmain Pty Ltd v Abigroup (2002), and restated in the Scottish case of City Inn Ltd v Shepherd Construction Ltd (2003). In this case the contract was JCT 1980 in which an additional clause 13.8.1 was inserted requiring the contractor to give notice within 10 days of the architects instruction if he considered it led to delay to completion. He was required not to carry out the instruction in that case unless he had given the notice. More importantly, clause 13.8.5 stated that the contractor was not entitled to extension of time if he failed to comply with any one of the provisions in clause 13.8.1. The presiding judge held that:

“The fact that the Contractor is laid under an obligation to comply with clause 13.8.1, rather than merely given an option to do so, does not in my opinion deprive compliance with clause 13.8.1 of the character of a condition precedent to entitlement to an Extension of Time. Non-compliance with a condition precedent may in many situations result in a party to a contract losing a benefit, which he would otherwise have gained, or incurring a liability, which he would otherwise have avoided. The benefit lost or the liability incurred may not be in any way commensurate with any loss inflicted on the other party by the failure to comply with the condition. The law does not, on that account, regard the loss or liability as a penalty for the failure to comply with the condition. In my opinion, it would be wrong to regard the ‘liquidated damages’ to which the Defendants remained liable because they failed to comply with clause 13.8.1 and thus lost their entitlement to an Extension of Time, as being a penalty for that failure.”

Perhaps the strongest statement to cast doubt on the Gaymark decision and the Prevention Principle came in the case of Mutiplex Construction v Honeywell Control Systems (2007). In this case Justice Jackson stated:

“Whatsoever may be the law of the Northern Territory of Australia, I have considerable doubt that Gaymark represents the law of England. Contractual terms requiring a Contractor to give prompt notice of delay serve a valuable purpose; such notice enables matters to be investigated while they are still current. Furthermore, such notice sometimes gives the Employer the opportunity to withdraw instructions when the financial consequences become apparent. If Gaymark is good law, then a Contractor could disregard with impunity any provision making proper notice a condition precedent. At his option the Contractor could set time at large.”

To date, the weight of opinion both from the courts and industry professionals in the UK appear to support this position. However, it should be noted that many international jurisdictions often contain broad equitably based powers and discretions which can provide relief to the contractor. Such discretions are consistent with the Prevention Principle concept recognising that there are circumstances where it has become unfair and morally unacceptable to allow the owner to benefit from its own preventative acts.

“A more equitable position could be for the parties to agree that liquidated damages should only be assessed if the prime reason for delay is due to the act or omissions of the contractor”

Such appears to also be the case in the United States. As a general rule courts will enforce the express terms of the contract, as written. However, in federal cases, the courts do not always strictly enforce the notice provisions, “where fairness demands.” Federal courts have refused to strictly enforce such provisions where it can be shown that the owner had actual or constructive notice of the facts giving rise to the delay or where the notice would have been of no use. However, it should be emphasised that some states follow this rule and others strictly enforce the notice requirements so the position can depend upon jurisdictional considerations.

In Vanderline Electric v City of Rochester (1976), a contractor sued the owner for delay damages suffered as a result of the owner’s unreasonable interference. The owner argued that the contractor was not entitled to damages because it failed to comply with a contract notice provision which required that the owner be provided with written notice five days after the claim arose. In addition,
the provision required that the notice included the amount of damages sustained. In analysing the provision, the court held that the owner could not use the provision as a defence to the contractor's delay claim. The court stated that a claim for delay damages by the contractor would not have arisen but for the owner-caused delays and interference with the project. Therefore, because the contractor was not responsible for the delays, failure to abide by the notice provision would not bar the contractor's claim for extension of time and delay damages.

Some industry commentators have gone so far as to postulate that where such notice clauses appear in a contract, contractors should avoid serving notices if delays are caused by the owner, as the provision of notice will have the effect of keeping the liquidated damages clause in play and reliance on the Prevention Principal negated. However, most professionals from all jurisdictions advise that until the law is settled in this area contractors would be wise to adhere to the notice provisions of the contract in order to avoid liability for liquidated damages.

In the longer term it is suggested that perhaps the parties to a contract should consider a more equitable view of liquidated damages for delay. A more equitable position could be for the parties to agree that liquidated damages should only be assessed if the prime reason for delay is due to the act or omissions of the contractor. A suggested clause may be along the lines:

“Regardless of any notice provision contained herein, and notwithstanding anything to the contrary elsewhere in the contract or at law, the Owner and Contractor agree that no liquidated damages for delay shall become due and payable by the Contractor to the Owner unless the Owner could have completed the facility and started receiving beneficial use of said facility but for the Contractor caused delay.”