



**Town of Aurora
General Committee Report**

No. FS19-037

Subject: Procurement Exemptions to Library Square Project

Prepared by: Anna Ruberto, Procurement Manager

Department: Finance

Date: November 5, 2019

Recommendation

- 1. That Report No. FS19-037 be received;**
- 2. That an exemption to the Procurement By-law be approved to permit Colliers Project Leaders, the project Architect and Planning/Landscape Architect, including RAW Architects and the Planning Partnership, to participate on the Evaluation Committees for the Library Square Project; and**
- 3. That an exemption be approved to waive the requirement for liquidated damages for the Library Square Project.**

Executive Summary

The Community Services department has requested that Colliers Project Leaders (“Colliers”), The Planning Partnership (TPP) and RAW Architects participate on the Evaluation Committees for the Library Square Project and that the requirement for a liquidated damages clause be waived on this project. Both these requests require approval from Council.

- Colliers TPP and RAW Architects possess extensive industry knowledge and experience
- Colliers TPP and RAW recommend not using a liquidated damages clause

Background

The Town’s Procurement By-law 6076-18, defines as consisting of Town staff only. Within the Procurement By-law 6076-18, Section 3. Definitions 3.1 (aa) “Evaluation Committee” is a component of the Request for Proposal process, where a committee of

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three or more staff, is established to conduct proposal evaluations, interviews, and demonstrations, during proposal evaluations for goods, services, or construction. Consequently, in order to permit an external party to be part of an evaluation committee, the requirement to only have Town staff as part of the committee has to be waived by Council.

The review of the Procurement By-law 2020 will include the review of the definition for "Evaluation Committee".

With respect to liquidated damages, Council passed a motion on February 24, 2015 that mandated that liquidated damages clauses be included in all construction project contracts, unless approval is obtained from Council not to include one and that staff report to Council on the effectiveness of a liquidated damages clause. Later that year, staff brought forward Closed Session Report No. LLS15-047, Effectiveness of Liquidated Damages Clauses, which Council deferred to the August 25, 2015 open session meeting. At this meeting, Council received the report for information. No further direction was provided with respect to liquidated damages. As such, and in accordance with the February 24, 2015 resolution, staff have been inserting such clauses on every construction contract.

Analysis

Colliers Project Leaders, The Planning Partnership and RAW Architects possess extensive industry knowledge and experience

The Library Square Project will be the Town's largest procurement and project undertaken by the Town. The Town has engaged Colliers to assist in the process and provide their expertise in managing the project. As part of their service team, Colliers brings a team of industry experts that have taken part in leading and managing projects with a similar scope to Library Square. As the design consultant team, TPP and RAW will be working closely with the General Contractor and need to have input into the selection.

Following a review of the Town's procurement process, it has been recommended that Colliers Project Leaders, TPP and RAW Architects be permitted to be part of the evaluation committees to evaluate any contractors to be hired by the Town to conduct work on the Library Square Project. The Town's Community Services department is in support of this approach in order to ensure that the evaluation team involved on this project is equipped with an appropriate level of relevant knowledge and experience.

As per the Town's process, any members of the evaluation committee will be required to avoid any conflicts of interest and will be required to sign a statement attesting to their impartiality in the evaluation prior to their involvement.

Colliers Project Leaders, TPP and RAW recommend not using a liquidated damages clauses

As part of developing the terms of reference that will be applicable to the Library Square project the matter of liquidated damages was discussed. Colliers and TPP/RAW has suggested that a liquidated damages clause not be employed as part of the Library Square project. Colliers recommends the utilization of contract documents through the Canadian Construction Documents Committee (CCDC). The CCDC contract documents are commonly used and accepted throughout the construction industry. The CCDC contains clauses pertaining to all aspects of the construction process. It has been developed and vetted by professionals in the construction industry.

As per recommendation from Colliers, the contract document that would be part of the Library Square project would consist of CCDC terms and Supplementary Conditions. With respect to recovery of damages caused by delay, the contract documents would contain a clause that provides an ability for the Town to recover reasonable costs from the contractor, incurred as a result of delays, provided such damages can be demonstrated and are shown to have been caused by the contractor. Colliers has expressed the following with respect to liquidated damages clauses:

- A liquidated damages clause creates an adversarial relationship with the general contractor from the initiation of the project. Colliers has found this not to be a productive approach on such projects, as from the start of the project the contractor is preparing back-up documentation to justify contractually why this schedule milestone could not be met.
- If liquidated damages are to be assessed for delays, contractors also expect to be rewarded, by way of financial incentives, if milestones can be achieved ahead of schedule. If such bonuses are not introduced, it eliminates the motivation for the contractor to do anything more than is expressly required by the contract documents.
- It would be difficult to accurately ascertain the actual value of liquidated damages to apply to this contract, especially with respect to the Square and Library work. Such estimates involve an amount of speculation and assumptions which begin to qualify the estimates as a penalty rather than an actual cost. The estimates must not be overstated in order to be valid. However if not directly addressed in

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the contract, the Supplementary Condition clause permits the Town an ability to recover the actual costs incurred by the Town, due to the contractor's delay in achieving the schedule

Advisory Committee Review

None

Legal Considerations

Council has mandated by resolution in 2015 that all Town construction projects include a liquidated damages clause, which requirement can only be waived by Council. A detailed report from Legal Services with respect to liquidated damages clause was previously presented to Council in an open session on August 25, 2015 and is attached to this report.

If the clause is not included as part of the Library Square contract documents, it cannot be added later in the project. A liquidated damages clause is used to define the scope of damage that the Town is estimated to suffer as a result of delays on a project. In case of delays that are caused by a contractor and not approved by the Town, the Town could demand payment of the predetermined amount for every day of delay. The Town would generally be limited in recovery to the estimated amount set out in the contract.

If a liquidated damages clause is not part of the contract, the Town may still recover for delay. The contract document that would be part of the Library Square project would contain a standard clause that would allow for recovery of damages suffered by the Town as a result of a delay. The difference in not having a liquidated damages clause is that the amount of losses would not be a predetermined daily amount, but rather it would be based on a reasonable amount of losses or damages that is demonstrated by the Town, and shown to have been caused by the contractor. Consequently, without having a predetermined estimate, when making a claim to recover delay damages, the Town would have to show the actual losses suffered attributable to the contractor.

Financial Implications

None

Communications Considerations

None

Link to Strategic Plan

The development of Library Square supports the following strategic Plan goals and key objectives:

Supporting an exceptional quality of life for all in its accomplishment in satisfying requirements in the following key objectives within these goal statements:

- **Invest in sustainable infrastructure**
- **Celebrating and promoting our culture**
- **Encourage an active and healthy lifestyle**
- **Strengthening the fabric of our community**

Alternative(s) to the Recommendation

1. To not approve the request for an exemption to allow Colliers Project Leaders, RAW Architects and The Planning Partnership to participate on Evaluation Committee for the Library Square Project.
2. To not approve the request to waive the requirement for Liquidated Damages to be included in the tender documents.

Conclusions

Town staff is recommending that Colliers Project Leaders, The Planning Partnership and RAW Architects be permitted to be part of the evaluation committees that will be involved in evaluating submissions from contractors for the work on the Library Square Project. The members of the Colliers Project Leaders team working on this project possess extensive industry experience including large construction projects and their participation would be valuable in the evaluation process. Further, based on recommendation from Colliers, TPP and RAW, staff are also asking that Council waive the requirement for a liquidated damages clause on this project.

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Attachments

Attachment #1: Extract from Council Meeting of Tuesday, February 24, 2015

Attachment #2: Report No. LLS15-047, Effectiveness of Liquidated Damages Clauses dated July 14, 2015

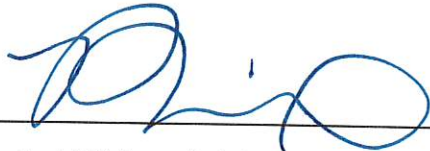
Previous Reports

N/A

Pre-submission Review

Agenda Management Team review on October 16, 2019

Departmental Approval



**Rachel Wainwright-van Kessel, CPA,
CMA
Director, Finance
-Treasurer**

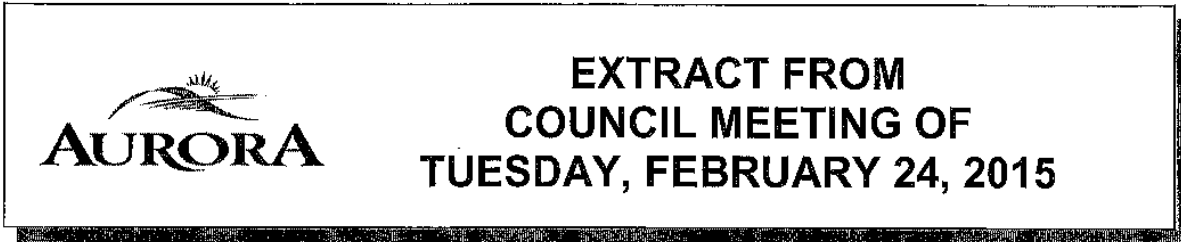
Approved for Agenda



Doug Nadorozny

Chief Administrative Officer

Attachment #1



10. NOTICES OF MOTION/MOTION FOR WHICH NOTICE HAS BEEN GIVEN

(ii) Motions for Which Notice Has Been Given

**(b) Councillor Mrakas
Re: Liquidated Damages**

**Main motion as amended
Moved by Councillor Mrakas
Seconded by Councillor Pirri**

WHEREAS most forms of building contracts include a clause referred to as "liquidated damages" that specifies the amount of damages that a contractor may be responsible for should the contractor fail to meet project timelines, including the completion date; and

WHEREAS "liquidated damages" are a tool that can be used to ensure that projects meet timelines and the completion date; and

WHEREAS the ability to meet time of delivery or performance of contractual obligations is an important factor in the award of any contract, and the Town may reasonably expect to suffer financial damages if performance targets and/or project timelines are not met; and

WHEREAS the Town currently includes "liquidated damages" clauses in its tender/RFP documents that form part of the construction contract between the contractor and the Town; and

EXTRACT/CORRESPONDENCE ROUTING INFORMATION							
External Correspondence was sent by Council Secretariat:		YES		NO	X		
External Correspondence to be sent by:							
ACTION DEPT.: (To Director and Assistant)	CAO	Building & By-law	Corporate & Financial	Infrastructure & Environmental	Legal & Legislative X	Parks & Recreation	Planning & Development
ACTION STAFF: (If other than above)							
INFO. DEPT.: (To Director and Assistant)	CAO	Building & By-law	Corporate & Financial	Infrastructure & Environmental	Legal & Legislative	Parks & Recreation	Planning & Development
INFO STAFF: (If other than above)	Pending List						

WHEREAS the absence of a "liquidated damages" clause in a construction contract does not prevent the Town from recovering any financial losses against a contractor due to breach of contract terms such as a failure to meet a completion date, but its inclusion does serve as an important tool and warning to contractors that project timelines and completion dates must be met.

NOW THEREFORE BE IT HEREBY RESOLVED THAT if staff determines that a "liquidated damages" clause should not be included in a construction project contract, then staff must obtain the approval of Council prior to the removal of such clause; *and*

BE IT FURTHER RESOLVED THAT staff report back to Council on the effectiveness of a liquidated damages clause as well as other tools available to ensure contractors meet project timelines and completion dates.

CARRIED AS AMENDED

Attachment #2



**TOWN OF AURORA
CLOSED SESSION REPORT**

No. LLS15-047

SUBJECT: *Effectiveness of Liquidated Damages Clauses*
FROM: *Warren Mar, Director of Legal & Legislative Services/Town Solicitor*
DATE: *July 14, 2015*

RECOMMENDATIONS

THAT Report No. LLS15-047 be received for information.

PURPOSE OF THE REPORT

The purpose of this report is to inform Council about the effectiveness of liquidated damages clauses, as well as other tools, in ensuring contractors meet project timelines and completion dates. In addition, the report discusses strategies to improve the potential of liquidated damages clauses being enforceable and effective.

BACKGROUND

At the Council meeting of February 24, 2015, Council directed staff to:

"BE IT FURTHER RESOLVED THAT staff report back to Council on the effectiveness of a liquidated damages clause as well as other tools available to ensure contractors meet project timelines and completion dates."

This report satisfies this request of Council and reviews the effectiveness of liquidated damages clauses in ensuring contractors meet project timelines.

COMMENTS

Summary

A liquidated damages clause is a stipulation in a contract providing for the payment of a specific amount of money by the breaching party in the event they fail to perform or comply with the terms of the contract.¹ Generally, a contract is negotiated by parties

¹ Richard Manly, "The Benefits of Clauses that Liquidate, Stipulate, Pre Estimate or Agree Damages" (2012) 28 BCL Rev 246 at 246.

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who agree to a specific amount and terms of such a clause prior to executing the contract and in turn, decide how a breach of contract will be dealt with. For example, if a party to a contract fails to complete the project by the specified deadline, the non-breaching party may collect the amount stipulated in the liquidated damages clause. Usually, the clause stipulates a fixed amount, to be calculated on a daily or weekly rate.

It is important to note that only those liquidated damages clauses that are a “genuine pre-estimate” of damages are enforceable.² A clause that provides for an excessive amount of damages beyond the actual loss will likely be deemed a penalty and therefore unenforceable by a court, if the clause is challenged judicially. If the liquidated damages clause is unenforceable due to being too excessive, the Town will be limited to a claim for damages flowing from any loss actually suffered as a result of the contractor’s breach of contract.

The benefits of utilizing such a clause include: (a) greater contractual certainty that work will be completed on time; (b) reduced costs associated with calculating and challenging a claim for damages; and (c) the likelihood that reasonable timelines have been negotiated. In addition, utilizing a properly calculated liquidated damages clause eliminates the need to mitigate or prove the loss of the innocent party. Lastly, a liquidated damages clause may act as an incentive for a contractor to complete work on time, since not doing so will result in them paying damages to the non-breaching party.

However, unless resources are used to calculate an accurate pre-estimate of the losses, these benefits may not be realized as the clause may not be enforceable. A liquidated damages clause that provides for an amount significantly greater than the actual loss suffered is likely to be challenged by a contractor and consequently not enforced by the courts. Also, an arbitrary amount, if challenged, may be difficult to support if there is no actual justification for it and it appears to be excessive. To avoid having a liquidated damages clause struck down as being a penalty, too excessive, or unconscionable, the Town needs to have tools to accurately calculate pre-estimates of damages.

Treatment of Liquidated Damages Clauses by the Courts

Whether or not a liquidated damages clause is enforced by the courts is determined by the wording and effect of the clause. The House of Lords first set out the test for determining the enforceability of a liquidated damages clause in the United Kingdom decision of *Dunlop Pneumatic Tire*. If the clause is a “genuine pre-estimate” of the loss, it will likely be enforced. However, if the clause is punitive or provides for an amount that is extravagant and unconscionable, it will likely not be enforced.³ A penalty may be defined as “a requirement for a fixed sum to be paid upon a default or breach of a

² *Dunlop Pneumatic Tire Co v New Garage and Motor Co*, [1915] AC 79 at 86 [*Dunlop*].

³ *Ibid.*

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specified clause(s) where the amount does not bear an apparent relationship to the actual loss suffered.”⁴ If the amount is far beyond the actual loss suffered, the clause will likely be unenforceable as a penalty. Thus, under the strict *Dunlop* test, a provision that amounts to a penalty will not be enforced.

Many years later, the Supreme Court of Canada, in *Elsley Estate v JG Collins Insurance*,⁵ introduced a less stringent approach, suggesting that even if a liquidated damages clause was not a genuine pre-estimate of the loss, it may still be enforced as long as there is no oppression and the clause does not provide for an amount that is unconscionable.⁶ An analysis of jurisprudence reveals that courts now use a combination of the approaches set out in *Dunlop* and *Elsley*.

The use of the words “penalty” or “liquidated damages” is not in and of itself conclusive of what the Court will determine the clause to be. If the clause does not mention the word “penalty,” the Court may still consider whether or not the clause is a genuine pre-estimate of damages, and may still conclude that the clause is actually a penalty, despite the absence of such words.⁷ On the other hand, if the clause does include the word “penalty,” this alone does not make the clause unenforceable.⁸

The onus of establishing that a liquidated damages clause is a penalty rests with the party against whom the damages are claimed.⁹ A court will provide relief by striking down a liquidated damages clause that is a penalty and oppresses the party against whom a claim for damages is made. Where there is no oppression, the clause will likely not be struck down.

However, a penalty clause that is excessive, unconscionable or oppressive risks being struck down by the courts. In *MTK Auto West Ltd v Allen*, the British Columbia Supreme Court struck down a penalty clause as being unconscionable because the damages provided for in the clause amounted to three times the actual damages suffered and thus the clause was oppressive.¹⁰ The Court went on to say that “a court should not strike down a penalty clause as being unconscionable lightly because it is a significant intrusion on freedom of contract.”¹¹ *MTK* confirms the *Elsley* approach to not automatically strike down a penalty clause, unless it is unconscionable or oppressive.

In *Don West Construction Limited Corporation of the Village of Port Stanley*, the Court

⁴ Kevin McGuinness & Stephen Bauld, *Municipal Procurement*, 2d ed (Markham, ON: LexisNexis Canada, 2009) at 1008.

⁵ *Elsley Estate v JG Collins Insurance Agencies Ltd*, [1978] 2 SCR 916 at 937, 83 DLR (3d) 1 [*Elsley*].

⁶ Paul-Erik Veel, “Penalty Clauses in Canadian Contract Law” (2008) 66:2 UT Fac L Rev 229 at 233-240.

⁷ SM Waddams, *The Law of Contracts*, 5th ed (Aurora, ON: Canada Law Book, 2005) at 325.

⁸ John Swan, *Canadian Contract Law*, 1st ed (Markham, ON: LexisNexis Canada, 2006) at 715.

⁹ *Elsley* at 937.

¹⁰ *MTK Auto West Ltd v Allen*, 2003 BCSC 1613 at para 22 (available on CanLII) [*MTK Auto*].

¹¹ *Ibid*.

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upheld a clause providing for a penalty of \$100 per day in the event the contractor failed to complete an extension to an arena.¹² Thus, a liquidated damages clause that provides for a daily rate of damages may be enforced by the courts.

In *Exel Environmental v Ottawa-Carleton (Regional Municipality)*, the Ontario Superior Court of Justice found a liquidated damages clause providing that a waste disposal company pay the municipality \$1,500 for every route collected late, to be excessive and unconscionable.¹³ The Court went on to say that the clause amounted to a penalty and had “nothing to do with the actual damages suffered by the Region nor the pre-estimate of damages initially made by the Region.”¹⁴ Thus, contracting parties must carefully pre-estimate damages or risk having their clause be deemed unenforceable.

Recommendations for an Enforceable Liquidated Damages Clause

If the Town chooses to include a liquidated damages clause in its construction contracts, it should ensure that the following requirements are satisfied, in order to avoid judicial scrutiny:

1. The clause must be a “genuine pre-estimate of loss” in order to be enforceable, otherwise the court will not enforce it. Consequently, parties should engage in a “genuine pre-estimate” of anticipated damages and record any negotiations that occur as evidence that the amount provided for in the clause is agreed upon by both parties. In a tender scenario, generally there is very little, if any, room for actual negotiation and such clauses have to be established unilaterally by the Town. This puts even more onus on the Town to ensure that such estimates are genuine and defensible.
2. It is recommended to have a formula for calculating the amount of damages to be paid, i.e., daily rate, or different rate for given breaches.
3. Ensure that the clause provides for an amount that is not punitive or unconscionable. If the clause provides for an amount far greater than the actual loss resulting from the breach of contract, courts will likely not enforce it using either the *Dunlop* or *Elsley* approach.
4. If the project for which the parties are contracting involves sectional completion, apportion the clause into individual amounts for each section of the project.¹⁵

¹² *Don West Construction Limited Corp of the Village of Port Stanley* (1983), 2 CLR 243 at para 27, 21 ACWS (2d) 442 (Ontario County Court – Elgin County).

¹³ 2889218 *Canada (Exel Environmental) v Ottawa-Carleton (Regional Municipality)*, [2001] OJ No 3360 (ONSC) at para 85-86.

¹⁴ *Ibid* at para 85.

¹⁵ Turner and Townsend, “Liquidated Damages Contract Risk Management” (March 2009)

<www.turnerandtowntsend.com/Liquidated_Damages_oeN9s.pdf>

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5. The clause must provide that the liquidated damages run from a specific date. Otherwise, courts may not enforce the clause, since without a specific date, damages cannot be calculated.
6. Ensure the clause does not provide for a lump sum amount – this will be presumed to be a penalty by the courts.¹⁶
7. The clause should include a provision for extending the completion date in order to ensure the clause will be enforced. Otherwise, in the eyes of the courts, it would be unfair to charge liquidated damages against a breaching party without a mechanism for extension of a deadline, particularly for delay caused by events beyond the control of the party.

Benefits of Liquidated Damages Clauses

If a liquidated damages clause is valid and enforceable, it may provide the following benefits:

- Greater contractual certainty
- No duty to mitigate loss
- Reduced risk of under compensation
- Allocation of commercial risk
- No need to prove loss
- Freedom of contract generally upheld, unless penalty
- General public interest
- Assurance that contract will be performed

Greater Contractual Certainty

By pre-determining the compensatory obligations of the breaching-party, a liquidated damages clause avoids the difficulty, uncertainty, and expense of proving loss and calculating damages in court.¹⁷ Thus, liquidated damages clauses provide contracting parties with contractual certainty and promote economic efficiency by avoiding the expenses associated with disputing damages calculations in court.

Contractual certainty and risk allocation is “a central motivating factor in every commercial transaction.”¹⁸ A liquidated damages clause may encourage parties to enter into a contractual relation in circumstances where they would otherwise not have if no such clause was in place. For example, if the contract is risky and the calculation of damages is too difficult, a liquidated damages clause may provide the certainty and risk allocation that the parties need before agreeing to enter into the contract.

¹⁶ *Lord Elphinstone v Monkland Iron and Coal Co* (1886), 11 AC 332. See Swan, *supra* note 6 at 717.

¹⁷ Manly, *supra* note 1 at 250-252.

¹⁸ *Ibid* at 254.

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No Duty to Mitigate Loss

Traditionally, a non-breaching party has a duty to mitigate the losses it will suffer by taking reasonable steps. However, where a contract contains a liquidated damages clause, there is no such duty to mitigate losses.¹⁹ Breach of contract alone would be sufficient to trigger the breaching party's obligation to pay the liquidated damages.

Reduced Risk of Under Compensation

A liquidated damages clause helps a non-breaching party avoid the risk of under-compensation that may otherwise arise by the legal restrictions on damages one would have to prove if no such clause was included. These restrictions on damages include: remoteness, certainty of proof, mitigation, and intangible losses.²⁰ In situations where damages for breach of contract result in consequential, indirect or idiosyncratic losses, damages are usually difficult to calculate, or deemed to be too remote and not reasonably foreseeable. In this event, a liquidated damages clause may cover such consequential and indirect damages that otherwise would not normally be recoverable under the general rules for damages from breach of contract.²¹

Allocation of Commercial Risk

A liquidated damages clause allows a contractor to allocate and assess the risk of a potential delay or late completion of a project. At the tendering stage, a contractor is able to know in advance their liability in the event of a delay or late completion.²² A contractor can take this risk into account when calculating their tender price; however, this may increase the tender price if the genuine pre-estimate of damages is high, or where a project is complex and the difficulty of certain components is unknown.

No Need to Prove Loss

Another benefit of including a liquidated damages clause is that there is no requirement on the non-breaching party to prove actual loss, an otherwise lengthy and costly process. Additionally, a non-breaching party is entitled to claim the liquidated damages as soon as the project timeline in the contract passes, without having to have suffered actual loss at that moment in time.²³ However, the amount may not be excessive or unconscionable.

Freedom of Contract Generally Upheld, Unless Penalty

The Supreme Court of Canada in *Elsley* urges courts to "be careful not to set too stringent a standard and bear in mind that what the parties have agreed to should normally be upheld."²⁴ The Court went on to say that the power of courts to strike down

¹⁹ Manly, *supra* note 1 at 253.

²⁰ Waddams, *supra* note 7 at 327.

²¹ Manly, *supra* note 1 at 255.

²² *Ibid* at 256.

²³ Manly, *supra* note 1 at 257.

²⁴ *Elsley*, *supra* note 5.

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a penalty clause is “a blatant interference with freedom of contract and is designed for the sole purpose of providing relief against oppression for the party having to pay the stipulated sum.”²⁵ Thus, parties to a contract can rest assured that their agreed upon terms, including a liquidated damages clause, will almost always be upheld and enforced by the courts. However, where the stipulated sum is a penalty, only the damages that can be proven are recoverable, but the amount recoverable may not exceed the sum stipulated.²⁶

General Public Interest

Some scholars suggest that liquidated damages clauses are even beneficial for public interest reasons. For example, Manly purports that “[l]iquidated damages clauses are beneficial and in the public’s interest because they promote the common good, reduce the incidence of litigation and promote commercial certainty.”²⁷

Assurance that Contract will be Performed

A liquidated damages clause gives additional assurance to all parties to the contract that the contract will be performed, since not meeting certain timeframes or deadlines will force the breaching party to pay the agreed upon amount.

On the other hand, the potential breaching party or the contractor also benefits from agreeing to include a liquidated damages clause in their contract. A contractor who is in the early years of their business, without a commercial history or a previous contractual relationship with the Town, may be able to convince an otherwise hesitant Town to enter into a contract by agreeing to include a liquidated damages clause.²⁸

In addition, a party to a contract may offer to include an extra-compensatory liquidated damages clause that is of a significantly larger amount than would otherwise be agreed to, as a signal of their intention to complete the work on time and as a demonstration of their reputation.²⁹ However, caution should be exercised with an extra-compensatory clause, because if challenged, it may be deemed unenforceable for being too excessive.

Drawbacks of Liquidated Damages Clauses

If a liquidated damages clause does not meet the tests in *Dunlop* and *Elsley*, and is consequently not enforced, the parties risk the following:

- Risk of under compensation
- Cost of determining the amount of damages and settling enforceability disputes

²⁵ *Elsley*, *supra* note 5 at 937.

²⁶ *Ibid* at 938.

²⁷ Manly, *supra* note 1 at 260.

²⁸ *Ibid* at 262.

²⁹ Veel, *supra* note 6 at 251.

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Risk of Under Compensation

In the event that the actual loss suffered as a result of a breach of contract is greater than the amount provided for in a liquidated damages clause, the non-breaching party may be held to the terms of the contract and limited to only recover the agreed upon amount from the breaching party. This is because contract law does not prevent people from entering into bad bargains.³⁰

By including a liquidated damages clause in a contract, a non-breaching party assumes the risk of any excess loss over the amount stipulated in the clause.³¹ This is another reason to ensure that such clauses are in fact genuine estimates and that arbitrary or standard amounts are not utilized. The risk of under compensation may be mitigated by obtaining insurance (if available) to cover for any loss beyond the agreed amount set out in the liquidated damages clause (i.e., insurance coverage for business interruption in the event of a delay).

Costs of Determining the Amount of Damages

This report has previously stated that liquidated damages clauses reduce legal fees for both parties to a contract, by avoiding the expense associated with calculating damages and assessing breach of contract claims in court. However, significant pre-contract work must be undertaken by the hiring party (i.e., the Town) to determine a genuine pre-estimate of damages that it may suffer as a result of a delay. This work may include additional costs from an architect and the use of internal staff resources across the organization to provide justifiable calculations for the liquidated damages amount. Thus, the cost of determining the amount of a liquidated damages clause, in some circumstances, may be more expensive than calculating actual damages suffered after the loss has occurred and is easily quantifiable.

Other Tools to Ensure Contractors Meet Project Timelines

While the timely completion of a project is never guaranteed, various tools other than the inclusion of a liquidated damages clause may be utilized to help ensure that contractors meet project timelines.

Forfeiture of Deposit

If a contract stipulates that a deposit is "non-refundable," it may be forfeited by the non-breaching party. However, the mere labelling of a payment as a deposit does not preclude the judicial scrutiny of the amount as being a penalty, excessive or unconscionable, in which case it may be challenged and found unenforceable.³² Thus, by providing for the forfeiture of a deposit in a contract, a party to a contract may be

³⁰ Veel, *supra* note 10 at 253.

³¹ Manly, *supra* note 1 at 261.

³² See *Tang v Zhang*, 2013 BCCA 52 at para 27, 223 ACWS (3d) 894.

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encouraged to complete the work on time for fear of losing the deposit.

Holdback of Payment

Similar to the forfeiture of a deposit, the holdback of payment may be exercised by the non-breaching party. This may provide an incentive to the contractor to complete the project on time. It is useful to have a provision in the contract stipulating that payment will be withheld in the event of a delay.

Project Management

Parties to a construction contract are encouraged to implement a detailed project management plan, in which both parties are actively engaged. By setting realistic goals and timelines, allocating for potential delay in setting dates and being actively engaged in project oversight, the Town may reduce the risk of delay.

Bonuses for Performance Targets

To encourage the timely completion of construction projects, bonuses may be offered as an incentive to meet project timelines. In addition, several bonuses may be made available, to be awarded to the contractor for every early successful completion of a project stage. While likely to be a successful strategy, there are financial implications of awarding such bonuses that should be considered when discussing this alternative tool.

LINK TO STRATEGIC PLAN

None.

FINANCIAL IMPLICATIONS

In order to ensure that a liquidated damages clause is upheld for being a genuine pre-estimate of damages, additional resources may have to be utilized to accurately pre-estimate damages before a contract is executed. Although an additional expense, the benefits of investing in an accurate pre-estimate of damages during initial contract formation may outweigh the drawbacks and expenses associated with proving loss, mitigating damages, and disputing damages in court, where a liquidated damages clause is not utilized.

ALTERNATIVE(S) TO THE RECOMMENDATIONS

1. Further options as Council may direct.

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CONCLUSIONS

This report has considered the effectiveness of liquidated damages clauses in ensuring that contractors meet project timelines. An analysis of jurisprudence suggests that if a carefully drafted and calculated clause is included in a contract, it will likely be enforced by the courts and provide various benefits to the parties, including: reduced costs, commercial certainty, allocation of commercial risk, and increased assurance that the project will be completed on time.

However, if the clause is seen as a penalty by the courts, provides for the payment of an amount in excess of the actual loss suffered, and/or is oppressive or unconscionable, the clause will likely be deemed unenforceable by the courts. Thus, if the Town is to benefit from including a liquidated damages clause in its construction contracts, it should carefully draft such clauses to ensure that they reflect a genuine pre-estimate of damages that are not excessive, oppressive, or unconscionable. In addition, the Town may utilize other tools to ensure that contractors meet project timelines, including the forfeiture of deposits, holdback of payment, increased project management, or performance target bonuses.

ATTACHMENTS

None.

PREVIOUS REPORTS

LLS15-044 – “Aurora Family Leisure Complex Renovations”, dated June 23, 2015

PRE-SUBMISSION REVIEW

None.

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Warren Mar

Director of Legal & Legislative Services/Town Solicitor