

Finer points of delay issues, termination

STUART JORDAN* discusses issues related to termination and delay damages, stressing the need to address them in contract drafting.

WE don't often report on case decisions from the courts but one recently decided dispute concerning solar developments has considered several important issues which we come across often in the Gulf.

These issues include an examination of the relationship between liquidated damages and contract termination and the nature of a performance guarantee. The decision also examined whether liquidated damages are a penalty, whether general damages can be claimed in addition to liquidated damages for the consequences of delay, and a *force majeure* defence. It is rare to see so many issues in one dispute and in this article, we'll tackle just the first two.

Each of these issues also provides us with some points we might consider when drafting contracts. The court case in question related to the following:

GPP Big Field LLP entered into a series of five EPC contracts with Prosolia UK Limited for construction of five separate solar plants. All these contracts provided for delay liquidated damages and four of these plants were late in achieving commissioning, so GPP was claiming for the liquidated damages at the agreed rates.

EFFECT OF TERMINATION

All of the above looks fairly straightforward, but there was one complicating factor: GPP had also terminated the EPCs and on one of them, the works still remained incomplete at the time of termination. The works under that contract were completed, with commissioning achieved, some 61 days later by another contractor. The question was whether termination had put a stop to the accrual of the liquidated damages or whether they continued up until the works were actually completed.

At a guess, most observers would assume that liquidated damages would stop at termination. After that point, we might reason that the contractor has no way of influencing the outcome and his fate should not logically depend on how quickly someone else can organise to complete the works.

In fact, the English High Court decided that the liquidated damages continued to accrue until actual completion. The judge's reasoning was based partly on the fact that termination was not expressly stated to end liquidated damages, and partly on the idea that termination somehow rewards the contractor for his own default, by letting him off the hook.

My respectful view is that this looks odd. Looking at it the other way: if delay damages continue to accrue, then a commensurate obligation (and opportunity) to complete the works should also persist – and if it did, then terminating a contractor's employment and locking him out of the site must be the ultimate act of prevention! That would mean an extension of time for the remainder of the build.

In fact, there are still conflicting court decisions on this point and we don't need to decide which is correct. But perhaps we could address the point in contract drafting and clarify that, in the event of termination, liquidated damages shall continue or shall stop – and if they stop, whether general damages may be claimed instead. In that situation, of course, we would also need to consider amending any exclusion

of indirect and consequential losses.

PERFORMANCE GUARANTEE

The other complicating factor here was that Prosolia had become insolvent by the time the legal action surfaced, so GPP brought the litigation against Prosolia's parent company, Solar EPC Solutions SL (SEL) under parent company performance guarantees embedded in four of the EPCs.

In that guarantee, SEL guaranteed Prosolia's due performance. It additionally and "as a separate and independent obligation and liability" promised to indemnify GPP against all loss, damage, costs etc in the event of Prosolia's breach.

SEL raised some interesting defences:

- That there were "unusual features" in the dealings between GPP and Prosolia (as creditor and debtor) which were not disclosed to SEL as surety and which changed the creditor-debtor relationship from that which would naturally be expected; and

- That the guarantee was discharged because of material changes in the underlying EPC which prejudiced SEL as surety. This arose from variations in works scope.

These defences were both rejected because the court held that they only apply to simple guarantees and not to indemnities. Although there was some ambiguity, they decided that there was an indemnity here, separate from a simple guarantee to make right any contractor breach. The decision was based on examination of the substance of the provision and not the description of it as a guarantee.

This is a reminder to us about drafting performance guarantees, indemnities and bonds. So often the title and language of these provisions are confused, mixing these different concepts together. We are reminded also that scope variations are everyday events. Of course, variations do not change the contract itself but parties should clarify that variations will not discharge a guarantee. ■

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Jordan ... the issue of liquidated damages should be addressed in contract drafting.