Key Considerations for Liquidated Damages Clauses in Transportation Projects

Almost all delays in completing a construction project cost money, but delays on transportation-related construction projects often have more severe financial and business repercussions than a typical development. Whether a public entity replacing a bridge over a highway or building a new light rail system; a private company constructing or expanding a commercial airport, vessel or intermodal shipping yard; or a port district building a new runway or pier — failing to deliver a completed project on time not only affects your budget, but could also damage your business and reputation. Solid construction contracts can mitigate damages, but attention must also be paid when drafting those contracts on how to recover costs in the event of delay.

The ability to recover actual damages places owners in the best position when faced with delays in construction. Actual damages, however, can be exorbitant and possibly difficult and costly to prove. For example, when constructing or expanding a commercial airport, airlines often begin scheduling flights and selling tickets before construction is complete. Once those tickets have been sold, a construction delay affecting the ability to serve already scheduled flights has a domino effect — the airlines would not only incur damages from rescheduling booked tickets, but could also lose future sales due to the negative publicity or by offering future discounts to affected customers. Those damages, in turn, likely
would be passed down to the airport managing construction, which are in addition to the damages incurred by the airport as a result of:

- Breaching leases, lending agreements and vendor agreements,
- Losses of future projects caused by the damage to its business reputation by its failure to deliver on time, and
- Traditional construction-delay damages of increased construction costs, construction management fees, loan carry costs, and lost revenue.

Because of the uncertainty of and difficulty in quantifying actual damages caused by construction delays, most contractors seek waivers of consequential damages (which encompass most of the damages listed in the example above). An owner, however, should not agree to waive consequential damages without incorporating a liquidated damages clause into the construction contract — failing to doing so prevents an owner from recovering significant delay-related losses. What are liquidated damages? Liquidated damages are simply a sum certain, agreed to by the parties and set forth in the contract, as the measure of a party’s damages in the event of breach (and for this discussion in the event of construction delays). Typically, in construction, liquidated damages are a specific dollar amount incurred for each day of delay. Often, the dollar amount increases as the delay increases and can range from $50 to $65,000 per day depending on the project and potential damages. Liquidated damages clauses are regularly enforced by courts when actual damages may be incapable or very difficult to ascertain, so long as the amount of damages are not a penalty and constitute a reasonable approximation of the anticipated damages resulting from delay. Courts require such parameters because liquidated damages clauses are presumed to allow parties to allocate risks, lend certainty to agreements, and more easily resolve disputes in the event of breach. In fact, liquidated damages can usually be recovered even when actual damages cannot be shown.

For construction projects in the transportation arena, there can be varying amounts of damages for different types of delays. For instance, there could be delays in obtaining substantial completion, reaching final completion, or testing or certifying equipment or operating systems that may occur between substantial completion and final completion — all of which are associated with different costs. In considering the types of
delays, thought also needs to be given to whether there are critical completion milestones that must be met during construction. Transportation projects often have more critical milestones than typical development projects. For example, are there phases during construction where it is important that the contractor deliver one portion of an intermodal platform (such as access to a rail line) before other less important areas; or is the predictability of the delivery of a fully-functional operating system at a date set during construction more important than reaching the targeted substantial completion date set at the beginning of the project? In some cases, these critical milestones can be carved out of a liquidated damages clause to allow the owner to recover actual damages, including consequential damages. For even more protection, a contractor can be required to obtain a bond or provide a line of credit in an amount sufficient to cover any assessment of liquidated or actual damages resulting from delays. On major transportation projects, all of the above strategies can be utilized.

For public entities, standard construction contracts used for public transportation projects often include liquidated damages provisions. Many of those contracts utilize a standardized formula to determine the daily rate of liquidated damages. One example is the daily liquidated damages formula utilized by many states’ standard specifications for construction. While the use of standard formulae to calculate liquidated damages is helpful, there may be some danger in a blind use for every project. Take for example a multi-year delay in completing a significant public transportation project through a metropolitan area involving a state highway. Increased construction costs due to such a delay could be hundreds of millions of dollars. That cost, however, would not take into account the difficult-to-estimate cost of:

- The public inconvenience in navigating through construction for additional two years,
- The effect on the environment due to the increased congestion, or
- Public officials who have lost their jobs or been voted out of office because of public discontent.

All of these must be contemplated and potentially included when establishing a liquidated damage rate.
Although many courts have upheld the use of a liquidated damages amount that was based on a general formula used in the field or industry, the amount of liquidated damages for each specific project must still be a reasonable approximation of the anticipated damages at the time entered into the contract. Therefore, for any project, consideration must be given to the amount of liquidated damages in comparison to the type and amount of potential damages to the owner and others affected by the construction. It is often beneficial in the event of a dispute over the assessment of liquidated damages to have a note in the file on how the number was created.

Lane Powell understands the transportation industry and its construction attorneys have substantial experience in crafting liquidated damages provisions on almost any type of transportation-related construction project.