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The Penalty for Delay in the Construction Contract

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Abstract

A construction contract is a consensual agreement that becomes binding once the offer and acceptance match. The agreement covers two key aspects: the work to be completed by the contractor and the payment agreed upon by the employer. Building professionals and construction experts bear a specific responsibility regulated by civil law, known as the decennial liability, which is considered a matter of public policy. This liability is defined by several factors, including the presence of a construction contract and the task assigned to the contractor or architect being the construction of fixed structures or buildings. The contractor and architect's responsibility arises after the completion of the delivery; prior to that, the contractual relationship follows general liability rules. The contractor's commitment to completing the work by the agreed deadline is an obligation to achieve a result, not merely to make an effort. If the contractor or architect delays delivering the work without a valid excuse or prior notice, the employer may include a clause in the contract imposing a penalty for each day of delay or specify a lump-sum penalty as agreed. The purpose of this penalty is to compel the contractor to avoid delays and complete the work on time. The delay penalty serves as a warning, making the contractor liable for financial consequences (compensation) if they fail to deliver the work on time. However, contract execution might be delayed for reasons shared by both parties, such as the employer's delay in making payments or the contractor's failure to execute the work without written protest from the employer. In such cases, the contractor may be granted additional time to complete the work without incurring the delay penalty.

Keywords: Construction contract, contractor, employer, delay penalty.

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Introduction

The nature of construction contracts, especially those involving the state as a party, necessitates their completion within the agreed timelines between the employer and the contractor. To prevent the contractor from delaying the fulfillment of their obligations and ensure timely project completion, the employer imposes a financial penalty, leaving the contractor with two choices: either complete the work within the stipulated period or face financial penalties for delayed completion. These penalties, known as delay penalties in fixed-term contracts, are pre-agreed amounts imposed by the creditor when the debtor fails to complete the work on time. They are typically calculated based on a time unit (day, week, month) or a specific percentage of the contract's agreed value, serving as a means to ensure the timely execution of construction contracts. Delay penalties are thus regarded as contractual compensations imposed by the employer on the contractor who fails to meet their contractual obligations.

To recover these penalty amounts, court authorization or a judicial decision is necessary, except when the employer is a governmental entity. In such cases, the mere delay in completing the work by the specified deadline entitles the state to collect the agreed delay penalties for the sake of public interest.

First: The Importance of the Topic and the Reason for Choosing It

The topic of delay penalties in construction contracts is of significant importance due to the substantial and ongoing urban development we are experiencing at the end of the current century, coupled with the increasing global population and the bright face of urban civilization woven by humanity throughout history. The international competition to attract tourists across various fields underscores the necessity of avoiding delays in construction contracts, particularly building contracts, and respecting the agreed timelines to prevent execution delays. These contracts have a direct impact on the urban development of nations. The importance of this topic stems from the special status of these contracts as they aim to provide services and serve as a common framework through which many professionals offer their services. Another reason for selecting this topic is the legal implications of the contractor's failure to fulfill their contractual obligations and the social repercussions of such delays.

Second: Research Methodology

Given that our research is confined to the delay penalty in construction contracts, I have opted to divide this study into two main sections. The first section will address the characteristics of the delay penalty and distinguish it from similar legal constructs, elaborated in two subsections. The second section will be dedicated to the determination and imposition of the delay penalty, as well as the possibilities of exemption or reduction, also discussed in two independent subsections. The study will conclude with a summary encapsulating the key findings and recommendations pertinent to the topic, followed by a list of references.

First Section: Characteristics of the Delay Penalty and Its Distinction from Similar Legal Constructs

As previously mentioned, the delay penalty consists of lump sum amounts agreed upon in advance by the contractor and the employer in their contract. It acts as a penalty imposed by the employer on the contractor for delayed completion of the assigned tasks within the contractually stipulated timeframe. Given this definition, the delay penalty resembles other penalties commonly included in contractual agreements, such as liquidated damages and punitive damages(1). Therefore, it is necessary to outline the key characteristics of the delay penalty and distinguish it from other similar legal situations.

First Subsection: Characteristics of the Delay Penalty

The delay penalty is defined as "a means to ensure specific performance within the stipulated timeframe or to guarantee the execution of contracts within their agreed periods." Socialist civil laws describe it as "a means to protect production facilities by ensuring discipline in work and adherence to deadlines(2)." Additionally, it is characterized as "compensation imposed by the administration automatically without the need to prove damage(3)." Thus, the delay penalty consists of lump sum amounts predetermined in the contract as an administrative and financial penalty, applied whenever the contractor fails to complete the work within the specified period(4).

A Court of Cassation ruling states that it is "a penalty intended to ensure that the contractor fulfills their obligations within the agreed timelines... The contractor cannot contest the employer's right to the full or

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partial penalty on the grounds of no damage or excessive estimation disproportionate to the actual damage[5]." The delay penalty is due immediately upon the contractor's failure to meet the deadline, without the need to prove any harm to the employer. This differentiates it from compensation, which requires the occurrence and proof of damage[6]. The penalty is usually calculated based on the size, importance, and cost of the project, either as a fixed amount per day, week, or month of delay or as a percentage of the work's value. There is also a predetermined upper limit for the total penalties, depending on the project's nature. This signifies that the delay penalty has a unique legal framework distinguishing it from other legal constructs.

The Egyptian Administrative Court, in its ruling on January 11, 1957, outlined the key features of the delay penalty as follows:

1. **Pre-Agreement**: The penalty must be specified in the contract beforehand; if not predetermined, the employer cannot later enforce it[7]. However, it need not always be explicitly mentioned in the contract itself but may be included in the general conditions of government contracts, which are considered part of the contract[8].

2. **Automatic Application**: The penalty is enforced automatically without the need for the employer to prove the occurrence of damage. It cannot be increased even if the actual damage exceeds the predetermined amount, as the damage is presumed to occur, establishing an irrefutable presumption.

3. **Administrative Enforcement**: If the employer is a government entity, the penalty is imposed through an administrative decision without the need for judicial intervention. This is a characteristic unique to administrative contracts[9]. However, if the employer is a private individual, judicial intervention is necessary, and courts have the discretion to reduce the penalty if deemed excessive based on the contract's circumstances, in accordance with Article 170, Paragraph 2 of the Iraqi Civil Code[10].

4. **Immediate Liability:** The penalty is due immediately upon the completion of the specified period for contract execution without the need for prior notice or warning. This differs from interest on delay in private law, which requires notification of its accrual even if the contract includes a penalty clause for delay[11].

Second Subsection: Distinguishing the Delay Penalty from Similar Legal Constructs

A comprehensive understanding of the legal concept of the delay penalty necessitates differentiating it from other similar constructs in terms of agreement and resulting effects. Here, we will provide a comparative analysis between the delay penalty and related legal situations such as punitive damages, liquidated damages, and coercive fines, with each discussed in a separate subsection.

Subsection One: Distinguishing the Delay Penalty from Punitive Damages

As previously mentioned, the delay penalty is a measure intended to ensure the contractor's compliance with the agreed deadlines. In contrast, punitive damages, as defined in Article 91 of the Iraqi Penal Code No. 111 of 1969, are described as "a penalty requiring the convicted to pay a specified amount to the public treasury." Legal scholars and judiciary in France and Switzerland unanimously agree that once punitive damages are imposed by a court, they become a civil debt burdening the convicted and are transferable to their heirs. Thus, they can only be settled by payment to the public treasury.

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This interpretation has been critiqued, as some argue that most penal codes convert unpaid punitive damages into imprisonment, unlike civil debts which do not incur such transformation upon non-payment. Punitive damages are subject to statutes of limitations and pardons, and most Arab legal scholars regard them as purely punitive, devoid of any compensatory nature.

In summary, the delay penalty is a civil debt due upon the contractor's failure to fulfill their obligation within the contractually specified period, whereas punitive damages are purely punitive without any compensatory aspect. The delay penalty ensures adherence to contractual obligations, while punitive damages serve as both a material and moral punishment intended to rehabilitate and socially reintegrate the offender. Additionally, punitive damages may convert into imprisonment if unpaid, unlike the delay penalty, which does not transform into any form of incarceration. The delay penalty is predetermined and influenced by the employer's discretion, whereas punitive damages are strictly defined by law and determined by judicial authority.

Subsection Two: Distinguishing the Delay Penalty from Liquidated Damages

Liquidated damages, also known as agreed-upon compensation, are defined as "an agreement wherein the contracting parties pre-determine the amount of compensation the creditor is entitled to if the debtor fails to perform or delays in performing their obligation[12]." Typically, the court determines the amount of compensation, or the law specifies it if the obligation involves a monetary amount. However, the contracting parties can agree in advance on the compensation amount for damages incurred due to non-performance or delayed performance by either party[13].

Some legal scholars suggest that the purpose of including liquidated damages in contracts is to avoid judicial discretion in determining compensation and to prevent disputes over the existence, absence, or nature of damage[14]. However, we disagree with this view, asserting that the primary purpose is to ensure contract performance. Article 170, Paragraph 2 of the Iraqi Civil Code empowers courts to reduce the agreed compensation amount if the debtor proves that the estimate was excessive or that part of the obligation was fulfilled.

In summary, the delay penalty is predetermined in the contract, while liquidated damages can be agreed upon later. The delay penalty is due immediately upon the contractor's delay[15], without the need for notice, differing from liquidated damages, which require notice since they involve an agreement between two parties and must meet the conditions for entitlement to compensation.

Subsection Three: Distinguishing the Delay Penalty from Coercive Fines

Coercive fines[16], also known as financial coercion, are defined as "a court order requiring the debtor to perform the obligation specifically, with a coercive fine imposed for each unit of time or each instance of non-performance, intended to compel specific performance without being considered compensation for the delay[17]." In this sense, it is an indirect means to compel the debtor to perform their obligation specifically. The judge issues an order, at the creditor's request, obligating the debtor to either perform the obligation within the specified period or pay a specified amount for each day, week, or month of delay until the obligation is fulfilled[18].

The distinction between the delay penalty and coercive fines can be summarized as follows:

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1. **Application Criteria**: The delay penalty is applied for delays in completing the work within the specified period, whereas coercive fines are applied for the refusal to perform the obligation specifically.

2. **Predetermination**: The delay penalty is a predetermined amount agreed upon in the contract, without judicial discretion for reduction. In contrast, coercive fines are imposed by the judge in cases of refusal to perform the obligation, with judicial discretion for determination and imposition.

3. **Nature of the Right**: The delay penalty is a right for the employer, particularly if the employer is a government entity, allowing direct deduction from the contractor's due amounts without judicial intervention. Coercive fines, however, are not considered a creditor's (employer's) right or a debt on the debtor (contractor) and cannot be enforced by the creditor directly[19].

Chapter Two: Determination and Deduction of Delay Penalties and the Possibility of Exemption or Reduction

As previously mentioned, a delay penalty becomes due when the contractor fails to fulfill their obligations within the agreed timeframe specified in the contract. Given that the contract is the law between the parties, they have full authority to determine the amount of the penalty based on time units or other measures. To delve deeper into this topic, we will divide this chapter into two sections: the first will discuss the determination and deduction of delay penalties, while the second will address the possibility of exemption or reduction of these penalties.

Section One: Determination and Deduction of Delay Penalties

The employer, whether an individual or an entity, has the right to specify the amount of the delay penalty, taking into consideration the importance and nature of the work. The penalty can be set as a certain percentage of the total contract value, or as a fixed amount for each day, week, or month of delay[20]. The basis for calculating the penalty is the actual amount determined by the final measurement lists, as it represents the true value of the contract, disregarding the estimated costs that have not been realized [21]. The employer has the right to deduct the delay penalty from the amounts due or to become due to the contractor or from any other performance guarantees. Generally, the payment or deduction of penalties does not exempt the contractor from their obligations to complete the work or from any other responsibilities under the contract[22].

Section Two: Exemption from or Reduction of Delay Penalties

For a delay penalty to be imposed on the contractor, the delay in completing the contract must be due to the contractor's fault, not due to external causes. This approach is supported by legal logic and is often upheld by the judiciary[23]. External causes that may lead to delays in contract performance can include unforeseen circumstances, force majeure, unexpected material difficulties, third-party actions, or actions by the employer. It is noted that the Iraqi legislator did not provide an explicit provision in the civil code addressing delay penalties, leaving the matter to general principles and the parties' agreement. As the contract is the law between the parties, the employer, who has the right to impose the penalty, can also exempt the non-compliant contractor from the penalty amount entirely or reduce it to the agreed extent.

Conclusion

After concluding the study on "Delay Penalties in Construction Contracts," we arrived at several findings and recommendations, summarized as follows:

Findings:

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1. Construction contracts are consensual agreements that do not require a specific form to be valid, but the delay penalty clause must be clear, definite, and free from ambiguity.

2. The delay penalty becomes due as soon as there is a delay in delivering the work and fulfilling the obligation within the contractually specified period.

3. The employer has the authority to exempt or reduce the delay penalty owed by the contractor.

4. The contractor's obligation to complete the contract by the agreed deadline is an obligation to achieve a result, not merely to exert effort. The contractor is only excused by proving an external cause.

5. Both parties to the contract, the contractor, and the employer, may contribute to the delay. For instance, if the employer fails to fulfill the contractor's dues, leading to the contractor's non-performance, the contractor is not liable for delay penalties.

Recommendations:

1. Given the importance of delay penalties in construction contracts, attention must be paid to this issue due to its impact on urban development plans, as any delay in project completion adversely affects the country's economic development.

2. The Iraqi civil code does not explicitly address delay penalties, causing the judiciary to rely on Article 170 of the civil code, which pertains to liquidated damages. Therefore, it is necessary to include a legislative provision specifically for delay penalties, establishing general binding rules to keep pace with modern development and fill the current legislative gap.

3. It is crucial to adopt a fixed percentage range for delay penalties based on the delay units, setting both minimum and maximum limits, with the employer having the discretion to choose within these limits based on the importance, nature, and cost of the contract.

4. A provision should be included in the Iraqi civil code stating that delay penalties are not applicable after the work has been withdrawn from the contractor and executed at their expense, as the contractor cannot be held responsible for delays caused by others after being removed from the project.

Footnotes:

(1) Dr. Ghazi Abdul Rahman Naji, *Economic Balance in the Contract During its Execution*, Legal Research Center Publications, Ministry of Justice, Baghdad, 1986, p. 59 and beyond. Dr. Mohammed Jaber Al-Douri, *Responsibility of the Contractor and Engineer*, Master's Thesis, University of Baghdad, College of Law, 1975, p. 42. Dr. Mohammed Shukri Sarour, *Responsibility of Engineers and Contractors in Construction*, Dar Al-Fikr Al-Arabi, Cairo, 1985, p. 154.

(2) Dr. Abdul Baqi Mahmoud Sawadi, *Supply Contract*, Ph.D. Thesis submitted to the College of Law and Politics, University of Baghdad, 1983, p. 304 and beyond.

(3) Dr. Shukri Habib Jabr, *Contracting and Wealth*, Dar Al-Kateb Al-Arabi for Printing and Publishing, Cairo, p. 298.

(4) Dr. Hamid Younis, *Construction Contracts Involving the State*, Dar Al-Fikr Al-Arabi, Baghdad, 1970, p. 50. Dr. Suleiman Al-Tamawi, *General Principles of Administrative Contracts*, Dar Al-Kateb Al-Arabi for Printing and Publishing, Cairo, 1984, p. 506 and beyond.

(5) Iraqi Court of Cassation Decision No. 42, 654 / Rights / 65 on 25/10/1965, Journal of the Legal Codification Bureau, Volume 4, 1965, Issue 1 and 2, p. 313 and beyond, and Judiciary Magazine, Issue 2, June / 1966, Volume 21, p. 52.

(6) Dr. Tharwat Anis Al-Asyouti, *Philosophy of Law in Light of Economic and Social History*, Lecture No. 10, University of Baghdad, College of Law and Politics, p. 334-343. Dr. Ahmed Abdel-Aal Abu Qareen, *General Provisions of the Construction Contract*, Applied Study, First Edition, Dar Al-Fikr Al-Arabi, Cairo, 2003, p. 2.

(7) Dr. Ahmed Othman Ayad, *Manifestations of Public Authority in Administrative Contracts*, Dar Al-Nahda Al-Arabia, Cairo, 1973, p. 346 and beyond.

(8) Iraqi Court of Cassation, Decision No. 1036 / Administrative / Second / 86 / 1987 on 4/5/1987 in the case filed by the plaintiff, the Governor of Sulaimaniya, in his capacity against the defendants, the contractors, for failing to complete the contract for constructing 500 houses within the specified period (unpublished).

(9) Iraqi Court of Cassation, Decision No. 723 / H / 965 on 1/11/1965.

(10) States: "The agreed compensation shall not be due if the debtor proves that the creditor did not suffer any damage, and it may be reduced if the debtor proves that the assessment was exorbitant or that the principal obligation has been partially performed, and any agreement to the contrary is void."

(11) Refer to Article 171 of the Iraqi Civil Code.

(12) Dr. Abdul Baqi Al-Bakri, *Explanation of the Iraqi Civil Code*, Part Three, Provisions of Obligation - Performance of Obligation, Al-Zahraa Printing House, Baghdad, 1971 edition, p. 146. Dr. Saeed Saad Abdel-Salam, *Summary of Named Civil Contracts (Sale, Construction)*, Dar Al-Nahda Al-Arabia, Cairo, 1999, p. 605. Dr. Mohammed Hussein Mansour, *Architectural Responsibility During and After Construction and Mandatory Insurance*, Al-Maarif Institution, Alexandria, no year.

(13) See Article 170 of the Iraqi Civil Code.

(14) Dr. Abdul Majeed Al-Hakim, *Summary of the Explanation of the Iraqi Civil Code*, Part Two, Provisions of Obligation, Second Edition, National Printing and Publishing Company, Baghdad, 1967, p. 32.

(15) Dr. Najdat Sabri Akravi, *Implementation of Foreign Companies' Development Projects in Iraq*, Legal Study, Al-Qadisiyah Printing House, 1986, p. 213-223.

(16) See Articles 253 and 254 of the Iraqi Civil Code.

(17) Dr. Abdul Baqi Al-Bakri, *Previous Source*, p. 67 and beyond.

(18) Dr. Abdul Majeed Al-Hakim, *Previous Source*, p. 15 and beyond.

(19) Iraqi Court of Cassation, Decision No. 732 / H / 1966 on 24/9/1966.

(20) Dr. Abdul Jabbar Naji Saleh, *Problems in Implementing Government Contracts*, Legal Research Center Publications, Ministry of Justice, Baghdad, 1983, p. 119.

(21) Iraqi Court of Cassation, Decision No. 274 / H / 1968, Journal of Court of Cassation Decisions, Volume 5, p. 341.

(22) Dr. Aydin Khalid Kader, *Penalty Clauses in Iraqi and Comparative Law*, Police Printing House, Baghdad, 1984, p. 85 and beyond.

(23) Iraqi Court of Cassation, Decision No. 3764 / Administrative Second / 84 / 1985 (unpublished).

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2. Iraqi Court of Cassation, Decision No. 765 / M 1 / 87 on 6/11/1997, Journal of Judicial Decisions, Issue 4, Volume 10.

3. Iraqi Court of Cassation, Decision No. 723 / H / 65 on 1/11/1965.

4. Iraqi Court of Cassation, Decision No. 732 / H / 66 on 24/9/1966.

5. Iraqi Court of Cassation, Decision No. (274/H/1968), Journal of the Court of Cassation, Volume Five.

6. Iraqi Court of Cassation, Decision No. (1469/H/68 on 7/6/1969), Journal of the Court of Cassation, Volume Six.

7. Iraqi Court of Cassation, Decision No. (3764/Second Administrative/1985), unpublished.

Fourth // Laws.

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