



Massachusetts Federal Court Declines to Enforce Liquidated Damages Provision Based on Percentage of Defendant's Revenue

Plaintiff Secure Our City, Inc. ("SOC"), a designer and provider of security systems, contracted with ECI Systems, LLC ("ECI") to install such systems for several of its clients. SOC subsequently brought suit against ECI, alleging, among other things, that ECI had breached the parties' contract. In connection with its claim, SOC sought to enforce a liquidated damages provision of the contract. That provision provided that, if ECI did business with any of SOC's customers during a five-year period, ECI was to pay SOC 25% of any revenue ECI derived from those customers.

ECI moved for summary judgment on the contract claim, arguing that this liquidated damages provision constituted an unenforceable penalty. The United States District Court for the District of Massachusetts agreed. The court explained that, under Massachusetts law, a liquidated damages provision will not be enforced if it is so disproportionate to anticipated damages as to constitute a penalty. In this case, the court found that the liquidated damages provision, which was based upon ECI's revenue, did not bear a logical relationship to any profits that SOC would have lost due to the alleged breach. The court noted that revenue is typically larger than profit because profit takes into account expenses.

The court's refusal to enforce the liquidated damages provision was also based on the deposition testimony of SOC's manager, who repeatedly referred to the provision as a "penalty."

This case demonstrates the importance of making sure that liquidated damages clauses in contracts are not disproportional to potential damages.

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