



Construction

Guidance for COVID-19



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All parties to construction projects are suddenly facing the prospect of delays and disruptions due to COVID-19. The industry was certainly impacted after Sept. 11, 2001 and the 2008 financial crisis, but the COVID-19 crisis involves broader impact to supply chains, labor supply, and emerging financial challenges. Additional demand side delays should be anticipated, such as homebuyers putting their plans on hold until times seem more certain, and then creating a surge in the market with a flood of new activity.

With respect to existing contracts, all parties should review their contracts with legal counsel for relevant clauses and to make sure they issue any required notices. To remain ahead of identified concerns, prime contractors must reach out to their subcontractors and suppliers to ascertain potential sources of delay to ensure they give the proper notices to their owners. The COVID-19 threat is quickly-evolving and hitting different parts of the world at different times, so contractors will want to require periodic updates from their subcontractors and suppliers, because what is not impacted today could easily be impacted tomorrow as different areas issue additional restrictions and potentially go into “lockdown.”

All parties should review their financing agreements and land use authorizations to make sure they remain in compliance. If owners have relied on certificates of insurance for required coverages under their contracts, they should also be requesting copies of available coverages, especially Builders Risk and CGL policies to see if some of the impacts could be covered. By the same token, contractors should be looking at owner supplied policies for their projects, such as the Builders Risk Policy. Owners and contractors should be looking to payment and performance bonds and subcontractor default insurance policies to address possible financial defaults. All parties should be talking to their bankers to make sure they have the liquidity available to get through anticipated closures.

While each situation is different, some of the key construction contract clauses to consider are:

1. Force Majeure and Delay Clauses

Force majeure is an unforeseeable circumstance that prevents someone from fulfilling a contractual obligation. Most U.S.-based contract forms such as the AIA, ConsensusDocs, and EJDC forms include force majeure concepts in the delay clause. Federal Acquisition Regulations (FAR) and the ConsensusDocs and EJDC forms expressly mention “epidemics” as an example of delay outside the control of the contractor, but even if epidemics are not specifically mentioned, the contractor should be entitled to relief because the epidemic was “beyond the control” of that contractor.

Generally speaking, these clauses provide the contractor with an extension of the contract time for delays caused by forces outside the control of the contractor, but establish no right to additional compensation. To obtain relief, the delay must be on the critical path of the contractor’s work—i.e., it must cause an actual increase the duration of the work.

Although force majeure clauses generally limit relief to an extension of the contract time, the contractor may still be entitled to additional compensation. For example, if the owner refuses to grant an extension of the contract time, thereby requiring the contractor to accelerate its work, the contractor may assert a “constructive acceleration” claim. Additionally, there may be coverage for these additional costs under the Builder’s Risk policy or other contract provisions.

2. Escalation Clauses

Escalation clauses allow a contractor to receive an increase in its contract price if the costs go up under circumstances described in the clause. Unit price provisions may contain exceptions allowing for an increase in the unit cost if changes in quantities would result in a hardship to the

This is an evolving risk that Gallagher continues to monitor through the CDC and WHO.

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contractor or the owner. If the contract is cost-reimbursable up to a guaranteed maximum price (GMP), the contractor should not agree to a GMP at this time without including an escalation clause or a qualification or exclusion that would allow it to make a claim if costs increase beyond those on which the price is based. If the GMP has already been fixed, then the contractor may have savings or contingency it can use to absorb these costs.

Change in Law Clauses

Change-in-law clause can be useful to protect help against the unforeseen over the course of a project. A sample clause may read: “Should any change in law affect the contractor’s cost or time of performance, it shall receive an adjustment in the contract, price and time for performance caused by such change in law.” Ideally, the contract definitions should provide a broad definition of “law” to include not just laws and regulations, but also acts of government officials having jurisdiction over the Project.

3. No Damages for Delay Clauses

Prime contracts and subcontracts may include a no damages for delay clause that prevents the contractor or subcontractor from claiming damages for delay. These should be evaluated on a case-by-case basis.

In many states such clauses are not enforceable, or enforcement may be subject to exceptions. One of the most important exceptions is for delays that were outside the reasonable contemplation of the parties. If the force majeure or delay clause expressly identifies “epidemics” as a delay outside the control of the contractor, it would appear that the parties contemplated delay from something like COVID-19. But the contractor may still be able to recover for delays caused by the declaration of a national emergency and resulting government action as being outside the contemplation of the parties.

Additionally, it is not uncommon for such clauses in subcontracts to allow the subcontractor to recover delay damages to the extent the contractor is able to recover them from the owner. It is vitally important that subcontractors review the prime contract in evaluation of any claim submission (so long as the subcontractor does not run afoul of the subcontract notice requirements).

4. Mutual Waiver of Consequential Damages

Most prime contracts contain mutual waivers of consequential damages that include the owner’s damages for loss of use. These should be viewed more as a shield than a sword.

5. Owner’s Duty to provide adequate assurances of financing

Most form contracts require the owner to provide documentation that it has adequate financing to complete the project and have provisions allowing the contractor to request documentation that this financing is in place. Contractors may want to exercise this right if it appears that the owner’s financing may be in jeopardy.

6. Termination and Suspension Provisions

AIA General Conditions allow a contractor to terminate a contract if the work is stopped for a period of 30 consecutive days through no act or fault of the contractor, and expressly mentions an “act of government, such as a declaration of national emergency that requires all work to be stopped.” While the current declaration did not include a requirement that all work be stopped, this is a developing circumstance that requires attention for new conditions and directives that are being issued daily.

7. Emergency and Safety Clauses

Many form contracts, like ConsensusDocs authorize the contractor to act in an emergency affecting the safety of persons or property, and to obtain compensation for the costs incurred. Likewise, safety clauses generally require the contractor to provide a safe and healthy workplace.

Weekly subcontractor meetings and working in cramped places may prevent the sort of social distancing that prevents one worker from infecting another. Contractors may want to consider various ways of addressing this—for example, setting up large tents instead of using cramped trailers for subcontractor meetings or setting up separate sanitary facilities for each crew. Additional costs for this work may qualify for a claim under the emergencies clause based on federal and state declarations. As always, the contractor will need to give prompt notice of any such claim, but because owners generally do not like surprises, it would be advisable to notify the owner of such actions and the contractor's expectation of payment before incurring these costs.

Conclusion and Best Practices

All project participants should be prepared for claims arising from COVID-19. To prepare for these claims, you should consult experienced legal counsel to review the relevant contracts and insurance policies.

As with everything on a construction project, prompt and clear communication is necessary both to preserve rights and to mitigate impacts on the project. Notices, especially on government work, must conform to all appropriate formalities, including the persons to whom the notices are addressed and the means of delivery. The notices should:

- a) Explain how COVID-19 and government actions to slow its spread qualify as force majeure and entitle the contractor to relief under the contract.
- b) Explain with appropriate specificity how the project is impacted, including references to specific materials delayed and activities affected. Contemporaneous documentation, such as photos, showing that the delayed material or work was on the critical path will make for a much more persuasive presentation.
- c) Identify the potential impact in terms of time and money and the efforts the contractor is undertaking to mitigate those impacts.

As more information becomes known, these notices should be updated. Careful attention should be paid to contractual provisions regarding the contents and timing of claim submissions after the initial notices.

Finally, it is important to realize this is a human issue that affects all of us in differing degrees. Contractors and owners should try to approach the issue with empathy and sincerity and be careful not to overreach.

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