

Litigation Alert: Issues to Consider If Your Construction Project Has Been Suspended or Delayed as a Result of COVID-19

May 19, 2020 – The impact COVID-19 is having on construction is unprecedented and is outside of contractor and owner control. Nevertheless, it is causing delays and impacting projects. Many have ground to a sudden halt, are not starting as planned, or are subject to slowdowns and delays. These impacts may be due to supply chain disruptions; government stay-in-place orders; and/or disruptions with designs, manufacturing, and inspections. In addition, personnel may be sick or staying home to avoid exposure, leading to a shortage of labor. The cost to each project may be overwhelming and will likely affect multiple categories within a project.

Epidemics, pandemics and other unforeseeable Acts of God do not automatically excuse contract performance and obligations. If a contractor or subcontractor cannot meet a project schedule due to the COVID-19 pandemic, whether or not this delay is an excuse warranting a time extension will normally depend on the language of the contract.

An essential step contractors must immediately take is to review their contracts and consider how a contract's delay, time extension, or *force majeure* clauses, as well as other contract clauses such as labor/material price increase provisions may allocate this risk between the contracting parties.

In relation to these provisions, you will also want to ensure that you comply with any notice requirements set forth therein. Although every contract may be different, there are some important general concepts that may assist you in evaluating what rights you have regarding contract termination or delay costs. Because many commercial construction projects are governed by standard form contracts created by the American Institute of Architects (AIA), the specific provisions of these contracts are also discussed below.

Contract Termination

The AIA contracts between the owner and the contractor (A201) and the contractor and subcontractor (A401) include provisions that may permit the parties to terminate the contract based on a COVID-19 work stoppage. For example, A201 permits the contractor to terminate the contract if the project is suspended for at least 30 consecutive days due to, among other things, an act of government. If the contractor invokes this provision, it has the right to recover payment for all work performed, reasonable overhead and profit on work not performed, and costs incurred by the termination. On the other hand, the owner is permitted to terminate the contract for convenience and without cause, but must pay the contractor for the work performed and costs incurred as a result of the termination, including costs attributable to the termination of the contractor's subcontracts.

A401 provides that the subcontractor can terminate the contract for any of the reasons that the contractor can terminate its contract with the owner. In such an event, the subcontractor may recover payment for all work performed, proven loss for materials, equipment, tools and machinery, reasonable overhead and profit on work not yet performed, and costs incurred by the termination. Furthermore, the contractor is permitted to terminate for convenience if the owner terminates its contract with the contractor. In this event, the subcontractor is entitled to payment for all work performed, costs incurred by the termination, and reasonable overhead and profits on work not yet performed.

For all other contracts, whether a party has a right to terminate the contract is dependent upon the contract terms. However, for events such as the COVID-19 pandemic, the common law may provide relief even if the contract does not. Where an event is unforeseeable and not caused by the fault of either party, the common law may provide an excuse for a party's non-performance or a basis to terminate the contract, such as unreasonable delay. However, whether you may be afforded some relief by the common law is a fact-sensitive inquiry, that is, it depends on the particular facts surrounding your project.

Delay or Suspension

Turning again to the AIA standard form contracts, A201 permits the owner to suspend the project for convenience. If invoked, the contract sum and completion time must be adjusted for increases in the cost and time caused by the suspension, including profits. A201 further provides that the time of completion of the project under the contract shall be extended if delays to the work are caused by “unusual delay in deliveries, unavoidable casualties... other causes beyond the Contractor’s control” or “by other causes that the Contractor asserts, and the Architect determines justify delay.” In such an event, the only remedy for the contractor is an extension of time.

Similarly, A401 permits the contractor to suspend work on the project for convenience, and also requires that the contract sum and completion time be adjusted for increases in the cost and time caused by the suspension, including profits.

Unfortunately, many construction contracts, including contracts with public entities, include provisions which limit a contractor’s remedies for delay to a mere extension of time. These provisions expressly prohibit any increases in the cost to the contractor caused by the delay. Generally, these exculpatory provisions are enforceable. However, there are exceptions. Whether these provisions will preclude a contractor or subcontractor from recovering increased costs due to the delay will depend on the intent of the parties and the language of the exculpatory clause. For instance, if the exculpatory clause was not intended by the parties to apply to circumstances such as a pandemic, then it may not preclude the contractor from recovering increased costs due to the delay. Likewise, an “unreasonable delay” may also not be covered by the exculpatory clause. Again, these are fact-sensitive inquiries that are contract-specific.

Whether it is invoking a force majeure clause or relying upon common law doctrines of impossibility and frustration of purpose, written construction contracts typically require a contractor to notify the owner in writing of a delay as soon as an impact occurs, stating the reasons for the delays, impacts and additional costs. Be sure to relate the reasons and the impact of the virus, explaining how COVID-19 will impact project schedules and costs. Even if you cannot fully quantify the impacts, provide the notice and identify what you can, reserving your rights to give more details at a later time. Make sure to also notify your subcontractors and suppliers, letting them know their obligations about project compliance, staffing, and health and safety.

In addition to delays, COVID-19 will likely make performance of many contracts and subcontracts more expensive. Supply chains have been disrupted, prices for materials may increase, absenteeism will negatively affect labor, and general conditions will be extended. Whether contractors can recover increased costs will depend on whether the contract has material/labor price escalation clauses allowing the contractor to modify its price or pass price increases to the owner.

Many contracts allow the upstream party to suspend or terminate the project at any time for any reason, without a showing of downstream default. When this occurs, the issue is inevitably who will pay for lost revenue, including overhead and profit, and who bears the costs to demobilize and remobilize. A contract may require the contractor to bear the costs, while others may allow for recovery. Once again, those questions can only be answered by looking at the terms of the contract.

As you review your contracts and begin assessing the impacts of COVID-19 on your projects, be sure to consider the costs of labor, materials, supplies and equipment, as well as impacts to the project schedule. Keep in mind that contractors have a duty to mitigate their damages and this pandemic is no exception. Make sure you are documenting your mitigation efforts, which should include steps you are taking to address the impact of this pandemic on your project, including resequencing project schedules and accelerating performance, if and when necessary.

If your construction project has been affected by the COVID-19 pandemic, we are available to assist in reviewing your contract and determining your rights to ensure that you are protected from further harm.

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