

Evaluating Exposure to Cost Overruns and Claims During Tumultuous Times

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Abstract

In this white paper, Sonny Jester, Managing Director at Cumming, discusses some of the key factors that owners should consider when their project is impacted by unforeseen events, including how to effectively mitigate disruptions and successfully reopen a project after work stoppage.



Construction projects can be impacted by any number of unforeseen events, including economic or financial issues, differing site conditions, natural disasters, and — as we’re experiencing now — pandemics. Any one of these events can be unanticipated and might introduce complications that might threaten the health and progress of your project. In the cases of natural disasters, pandemics, and other potentially disruptive events, impacts to the supply chain may also occur, resulting in longer lead times, more competition for materials, and higher prices. These factors, in turn, affect project schedules and budgets and can lead to a rise in the number of disputes.

To effectively mitigate these disruptions, a number of key questions must be answered: What is the impact to the project? Which of the parties on the project is affected and how? Who bears responsibility or risk? Is there a collateral resource (such as bonds, insurance, etc.) that might be available to offset the costs occasioned by the events? Are there alternatives to shutdown or suspension?

Other factors that should be carefully considered include:

Force Majeure

One of the foundational questions to ask in our current situation is whether the pandemic is a force majeure, thus justifying an Extension of Time (EOT). This question can most likely be answered by reference to the contract; however, confusion on this point may exist even in a well-drafted contract. For example, pandemics may be expressly included as a defined force majeure event, but even if they are not, a government shutdown as a result of the pandemic might be.

The inquiry does not end there. One must assess the impact of applicable local laws, which may enforce specific definitions of key terms or set different requirements or limitations on how work may continue. It must also be determined whether or not the contract provides time and money allowances for schedule impacts, and what impacts the answers to these questions might have on the compensability of the delay.

Additionally, be aware that some contracts, and the legal interpretations in some jurisdictions, also often require that continued work be impossible and that the impact not be foreseeable. These provisions, if present, may require the contractor to continue with such work as may be possible. Also, if the epidemic did not result in an immediate shutdown, but one followed later, is that later impact foreseeable?

Deceleration/Pacing

Deceleration (or pacing) may be employed to allow the project to continue progressing, albeit not at the rate originally intended. Nonetheless, if it is an option made available by the contract or subsequent agreement of the parties, it may provide a cost-efficient alternative when compared to outright suspension. It may also help avoid some of the difficulties of completely pausing and then restarting projects, which is a complex and often fraught process. When deciding whether to decelerate or suspend a project, it is essential that the costs of the shutdown and restart be accurately projected so that an “apples to apples” comparison between suspension and deceleration can be made.

Suspension and Shutdown

If the project cannot proceed — whether because of governmental and regulatory restrictions, supply chain limitations, or labor inefficiencies or availability — the way in which a suspension or shutdown proceeds may determine the viability of restarting the project after the crisis has been mitigated. Accurate evaluations of the work-in-place and the cost-to-complete should accompany an evaluation of the schedule impacts. A comparison of the costs expended against the schedule of values and the total amount of approved pay applications should also be made, and a proper securing of the work in place and project as a whole should be undertaken. Stored materials should be included in the protection of the works.

Contractor Acceleration vs. Owner Acceleration

If project acceleration is an option to recover any time impact, it is important to understand the answers to a couple of basic questions, along with their not-so-basic implications. Who is demanding acceleration of the project — the contractor or owner? Who is willing or obligated to pay for it? Is the request overt or implied? Being clear on these points is crucial, as acceleration often means bringing on additional team members, which in turn raises costs. Without clarity, confusion can ensue, leading to disputes.

Opening Up and the Potential Ripple Effect

Some construction projects have been significantly impacted by COVID-19 shutdowns, whereas others have not. At the time of writing this paper, many industries that were restricted or closed down, including construction in many places, are reopening or on the verge of doing so. While it is not possible to cover every possible impact that reopening will have on every kind of project, we have attempted to cover some of the main ones below.

Re-mobilization

Most construction contracts contain an allowance for contractor mobilization and, by extension, subcontractor efforts. Also, while it is possible that materials and equipment may already be stored on site, it may also be the case that some of these things were removed from the site for reasons related to storage capacity or security. These items will have to be returned to the site, carrying with them additional transport costs.

Transportation and the labor market

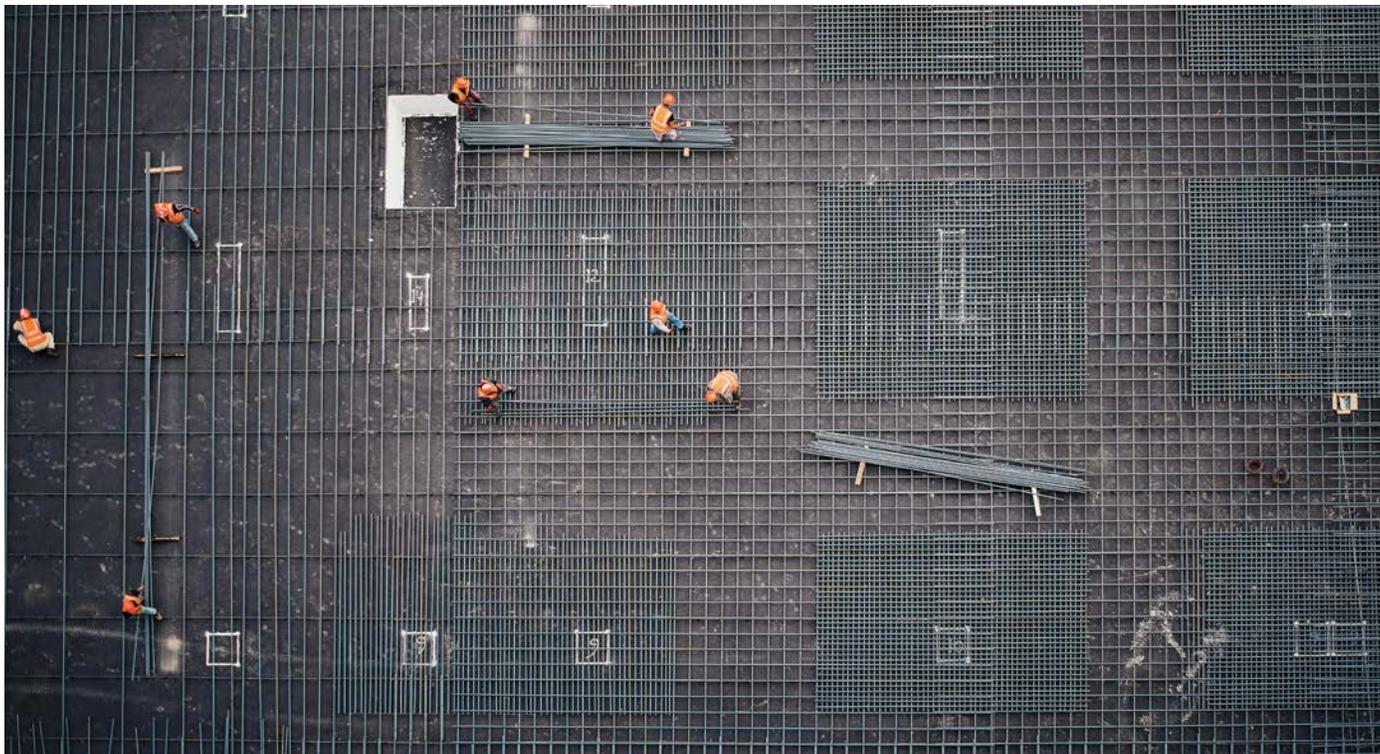
There is little doubt that most people would prefer to return to work and earn a living, but there are other factors that may impact this decision. For instance, some people may have understandable reservations about returning to work without being tested, or about using public transportation if that was how they



commuted to and from work. Perhaps someone in their family has been directly impacted and requires care. For large-scale projects, especially those that utilize buses to transport workers, new arrangements (such as staggered schedules) may be worth looking into. As with all novel arrangements, there will likely be cost and schedule impacts that must be understood in advance to ensure informed decision-making. Additionally, the availability of skilled labor may be an issue if the project was suspended. That manpower may have been in demand on projects that were not shut down, and so no longer available for the restarted project. Specialty trades and those requiring skilled labor should be considered carefully in this regard.

Maintaining distancing

In some instances, practicing social distancing will be easy; in other cases, it may prove exceedingly difficult. For example, road construction crews may encounter



few issues in maintaining space between one another, whereas large sites may have multiple areas of high congestion, including turnstile entry systems or boiler rooms where several workers are sharing a tight space. Again, staggered start times and/or offsite fabrication alternatives may have to be considered. Under social distancing requirements, projects that require the frequent use of lifts or elevators may see a negative impact to productivity, as queuing to use these vertical transportation systems becomes the norm.

“Distancing requirements may cause other productivity impacts, which should be realistically considered in developing a restart baseline schedule and potential recovery plans.”

Material availability and supply

The availability of steel and other essential materials from offshore sources may very well impact progress. Consider plastic, which state and federal governments have been purchasing in large amounts to assist in the production of ventilators and personal protective equipment. Not only has the increased purchasing of plastic impacted prices and availability, but manufacturing companies have changed their equipment

and processes to help produce the needed items. This shift in production and manufacturing priorities could result in longer lead times for materials, whether locally supplied or shipped from abroad. Additionally, the shift to transporting critical medical, food, or other essential products will potentially leave less shipping available for construction materials.

Project funding

Owners of projects that have been delayed will have to consider whether additional funding is necessary. If so, and insofar as it is economically viable to pursue that funding, the owner will first need to approach its bank or investors. It is possible that lenders may be reluctant to fund loan increases because of continuing uncertainty, or they may enforce stricter reviews of requests to draw against construction loans. This reticence may lead to approval delays for pay applications, with a resulting ripple effect traveling down the contracting chain.

This situation creates several issues for the owner, as they are forced to consider whether it is better for the contractor to proceed on the current basis while it pursues funding, suspend the contractor and the project, or stop everything and mothball the project. The issue with delaying any of these decisions is that each day of delay increases the cost to the owner and potentially makes restarting and/or completing the project problematic.

Plan ahead

No one is sure how things will go over the next few weeks or months, but each project should have a best plan in place, just as they would with a baseline schedule. Since no one knows exactly what to plan for, it would be beneficial to have a number of alternatives so that the best one can be utilized when the reopening occurs.

During this period, it is recommended that the involved parties hold frank, good-faith discussions of current costs, incurred costs (both actual and potential), and

what can be achieved in the available timescale and budget. The team may also consider working together in a value engineering exercise. Value engineering is not only about saving money; it can also help the team determine which items can be procured in advance during a project shutdown and which can be eliminated or deferred. By engaging all parties to the contract and thinking carefully through all of the impacts and their implications, and working together to anticipate and solve problems before they happen, most issues related to COVID-19 shutdowns can be successfully mitigated or avoided.



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Sonny has more than 25 years of experience as an attorney with expertise in construction law. He also has extensive experience in the construction sector directly, having worked with owners, contractors, subcontractors, design professionals, vendors, and sureties in a variety of capacities for nearly 15 years. He has participated in hundreds of mediations, arbitrations, and trials, both as an advocate and a consultant, and has presented in many venues on a variety of construction issues, including contract document analysis, process assessment, issue management with an emphasis on risk mitigation, mid-project intervention and turnaround, dispute resolution, and claims support.