



CONTRACTUAL CLAUSES AND CONSIDERATIONS FOR CALCULATING DAMAGES FOR CLAIMS RELATED TO COVID

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ABSTRACT

This session will explore “no-damage for delay,” force majeure, and “no escalation” clauses in the context of COVID-19 claims and especially the nuanced difference of direct vs. indirect costs and how one is more likely recoverable versus the other. The presentation will also explain how to calculate such claims. The first relates to the additional direct costs being incurred to perform the contracted work. These are items like additional PPE, reduced crew sizes to maintain social distancing, reduced workforce availability due to vaccine mandates, etc. How you perform the job now is more expensive because of COVID. The second relates to additional indirect costs like material cost escalation, higher labor rates, etc. These additional costs are because COVID has affected the marketplace and delayed the progression of the project. It is more expensive now to perform the job than it was before COVID.

NO DAMAGE FOR DELAY

Most public works contracts and a good deal of private ones as well contain what is referred to as a “no-damage-for-delay clause.” Under a no-damage-for-delay clause, the superior party in the contractual chain is not liable for any monetary damages resulting from delays on the project. Instead the exclusive remedy is an adjustment of the contract schedule. These clauses are not bilateral so that the inferior party although unable to collect monetary damages can be held liable should it cause delays to the project.

Some states have limited the enforceability of such clauses and even fewer have outlawed them on all projects as a matter of law. Additionally, for subcontractors on federal projects, the Miller Act may provide an avenue to circumvent a no-damage-for-delay clause.

The ConsensusDocs standard prime and subcontracts do not include a no-damage-for-delay clause.

Exceptions to No Damage for Delay:

1. Delays that resulted from the benefiting party’s bad faith, active interference, fraud or misrepresentation. This is the most common exception to no-damage-for-delay clauses that has been fashioned by Courts.

2. Delays that were not reasonably foreseeable or contemplated by the parties at the time of contract. Many clauses attempt to contract around this exception by expressly bringing in all delays, foreseeable or unforeseeable within the purview of the clause.
3. Delays that were so unreasonable that they constituted an intentional abandonment of the contract by the party seeking to enforce the clause. Abandonment can be express or implied from a party’s conduct. Delays that are unreasonable in duration can be deemed to be an abandonment of the contract. This exception becomes especially important in the context of COVID where we saw many projects come to an abrupt halt without prospects of resumption.
4. Delays resulting from a material breach of contract by the enforcing party. A material breach must be a complete failure of a condition precedent to performance or completely frustrate the performance of one of the parties, not merely delay it for a time.

The exceptions listed above have mostly been developed through case law. Some states have also enacted statutes that curtail the enforceability of no-damage-for-delay clauses.

A few states prohibit the enforceability of the clause where it serves to excuse the public authority from any liability. For example, in Louisiana, no-damage-for-delay clauses are void on public projects if it “purports to waive, release, or extinguish the rights of a contractor to recover... for delays in performing such contract, if such delay is caused, in whole or in part, by acts or omissions within the control of the contracting public entity.” (La. R.S. 38:2216(H)) Virginia and Colorado have similar language as well. (Va. Code. Ann. § 2.2-4335(A); Colo. Rev. Stat. § 24-91-103.5.) North Carolina prohibits no-damage-for-delay clauses on public contracts with the prime contractor. (N.C. Gen. Stat. § 143-134.)

Furthermore, Kentucky, Ohio, and Washington even prohibit no-damage-for-delay clauses on both public and private projects. (See Ohio Rev. Code. § 4113.62(C); Wash. Rev. Code. § 4.24.360; Ky. Rev. Stat. Ann. § 371.405(2)(c))



On federal projects, the standard contract provisions in the Federal Acquisition Regulations (“FAR”) allow the general contractor to recover for the government’s delay. (See FAR 52.242-14 (Suspension of Work); FAR 52.242-15 (Stop-Work Order).) However, absent language to the contrary in the subcontract, state law will determine whether a no-damages-for-delay clause is enforceable, and if so, what exceptions will apply for subcontractors on federal government projects. However, there are important protections, including the Miller Act, which may prevent enforcement of a no-damage-for-delay clause against a subcontractor in certain circumstances – particularly where the subcontractor asserts a claim against the general contractor’s payment bond and the no-damage-for-delay clause includes conditional payment or recovery language.

The Miller Act requires general contractors on federal government projects to procure a payment bond for those who provide labor or furnish materials on government contracts valued at over \$100,000. (40 U.S.C. § 3131 et. seq.) The Miller Act may prevent enforcement of a no-damage-for-delay clause against a subcontractor’s claim against the general contractor’s payment bond if the clause includes conditional payment or recovery language. For example, in *United States ex rel. Kitchens To Go v. John C. Grimberg Co., Inc.*, 283 F.Supp.3d 476 (E.D. Va. 2017), the surety could not assert the no-damage-for-delay provision in the contract to prevent the subcontractor’s recovery of its delay damages against the payment bond because the clause at issue conflicted with the Miller Act. The subcontract’s no-damage-for-delay clause stated that the general contractor would not be liable for any delays on the project beyond its control. Furthermore, the no-damage-for-delay clause included language, similar to a pay-if-paid clause, which conditioned the subcontractor’s recovery for any delay costs on the general contractor’s reimbursement for delay from the federal government.

The no-damage-for-delay clause violated the Miller Act because a subcontractor’s claim against the payment bond cannot be conditioned on whether the government has paid its general contractor. The court noted that to condition the subcontractor’s recovery on the general contractor’s reimbursement from the federal government would

frustrate the Miller Act’s purpose: to guarantee payment for those who perform labor or furnish materials on federal projects.

Be cautioned that Court decision are often very specific to the contract language and the surrounding facts.

FORCE MAJEURE

A force majeure clause allocates the risk of loss if performance is hindered, delayed, or prevented because of an event that the parties could not have anticipated or controlled. Not all force majeure clauses are identically crafted so the extent of the defense it provides will largely depend on its particular language.

Care should be taken by parties to a contract to tailor the clause to the particular risks and circumstances of their transaction. Failing to do so could have negative unintended consequences as Courts will enforce the clause as written.

There are four element to a force majeure clause:

It must define the breach to be excused.

It must define what constitutes the “force majeure event”.

It must tie breach to the event (causation).

It must explain what will happen if performance is excused.

The definition of the breach will define and color the rest of the clause especially as to how the resulting performance failure is handled. The “force majeure event” is the trigger that gives life to the clause.

Take care to consider what type of significant and unforeseen event might cause a party to breach and whether it should be excused. Similarly you may carve out certain specific breaches from an otherwise broadly drafted force majeure clause. For example, including a phrase that the lack of profitability is not sufficient to excuse performance is commonly seen in construction contracts where the relief offered is limited to allowing penalty free additional time to perform.



The force majeure event is often defined as “unanticipated events beyond the parties’ control,” followed by a list of examples. Sometimes the list is concluded with a broadening clause, like “and such other events as are outside the parties’ control.” Sometimes the clause is narrow and only provides for very specific events. No one method is preferable. It’s what makes sense in a particular transaction that guides the definition.

Putting things in the context of COVID the Southern District of New York decided that defining a force majeure event as “circumstances beyond our or your reasonable control,” was sufficiently open-ended to encompass COVID even though the list of events did not include the word pandemic. In *JN Contemporary Art LLC v. Phillips Auctioneers LLC*, No. 20-cv-4370 (S.D.N.Y. Dec. 16, 2020), the court noted:

If there is other language in the contract that deals with an event that might otherwise qualify as force majeure the Court is less likely to deem that event as unforeseen and thus warrant excused performance.

The next element is causation. Although an important element it is not necessary to be too specific as to what particularly caused the breach. For example, was it COVID or the resulting shutdowns and supply chain issues that lead to non-performance? The force majeure clause will set forth some causal connection between the failure of performance and the force majeure event. Language that seeks to make the clause inoperable if there were any other contributing factors to the breach may be too restrictive and render the force majeure clause moot.

The final element is what is the result of the excused performance. Avoid an all or nothing approach. Consider the true effect of the force majeure event on performance and the relief it will necessitate. It may also be expressed in degrees. For example, the clause may provide for an extension of time but after a certain period may permit either party to terminate the agreement.

Also consider the inequity that may result from excused performance. If you represent an engineer or even a manufacturer that has performed substantial pre-

construction work for which it has not been paid for a force majeure clause that deems the contract null and void would not be a desirable result. Using the same set of facts a developer who still plans on moving forward with the project, albeit at an unspecified date in the future, may want some continued performance from the design team before the contract is terminated.

With the above in mind set forth below is a force majeure clause that I have used in subcontracts where I represent the contractor:

If the Subcontractor is delayed at any time in the commencement or progress of the work by labor disputes, fire, unusual delay in deliveries, unavoidable casualties, shutdowns of the project or supply line as a result of compliance with governmental orders related to COVID-19, adverse weather conditions documented by data substantiating that weather conditions were abnormal for the period of time, could not have been reasonably anticipated, and had an adverse effect on the scheduled construction, or other causes beyond the Subcontractor’s control; then the schedule shall be extended for such reasonable time as the Contractor may determine. For the avoidance of doubt, Force Majeure shall not include (a) financial distress nor the inability of Subcontractor to make a profit or avoid a financial loss, (b) changes in the market prices or conditions, or (c) Subcontractor’s financial inability to perform its obligations hereunder.

These subcontracts typically also contain a termination for convenience clause in favor of the Contractor. If the situation is such that the force majeure clause is yielding unfavorable results the termination clause can be used as a stop gap measure.

Which brings me to the final point. As stated in the beginning, force majeure is just one of many risk allocation clauses in contracts. Do not become too focused on any one particular clause but rather look at the contract as a whole. Be mindful of how the clauses interact and avoid inconsistencies which could result in a Court interpreting the contract in an unintended manner or void clauses altogether.



MATERIAL PRICE ESCALATION CLAUSES

A material price escalation clause allows for the adjustment of the contract price based on an agreed-upon benchmark. The adjustment can be for specific items, such as fuel, lumber, copper wire, etc. or for the entire contract as a whole, but the latter wholesale adjustment is rare. The benchmark can refer to an outside source, for example, the U.S. Energy Information Administration price for diesel fuel. The adjustment need not be immediate either. In other words the clause can provide for an agreed-upon threshold before an adjustment is made.

These provisions can also work in reverse as a savings clause if material prices decrease beyond a certain threshold. Such a savings clause can be offered as an incentive to induce the inclusion of an escalation clause. As a general proposition material prices usually trend upward, however, this would make sense if a project is being bid in situations where material prices are unusually high because of a known current event but are expected to subside at some point in the future when construction occurs. Perhaps your client is bidding a project right now but believes supply-chain issues will resolve next year and prices will go down.

Here is an example of a material price escalation clause included in contracts:

§ 8.7.1 Escalation Clause. In the event of significant delay or price increase of material, equipment, or energy occurring during the performance of the contract through no fault of the Contractor, the Contract Sum, time of completion or contract requirements shall be equitably adjusted by Change Order in accordance with the procedures of the Contract Documents. A change in price of an item of material, equipment, or energy will be considered significant when the price of an item increases 20% percent between the date of this Contract and the date of installation. The amount of the increase shall be capped at five percent (5%) of the original budgeted price for the item.

If you do not have a force majeure clause that permits adjustments to price, or a material escalation clause, you might consider requesting relief by way of equitable adjustment or change order based on the commercial impracticality of the price increase. Some courts have found that unforeseen price increases can be significant enough to merit an adjustment

or reformation of a contract. But other courts have been less sympathetic to this type of market-driven argument.

DIRECT COSTS

Direct costs are construction costs that are specifically allocable to a particular construction contract or project. These are typically materials, direct labor and subcontractor costs. In negotiating a change order due to increased costs caused by COVID activities such as additional cleaning measures, or delays associated with project access due to screening measures or material costs for cleaning supplies and PPE may be included under direct costs. These items are easier to negotiate as they are easier to quantify and directly link to the project.

INDIRECT COSTS

In contrast, indirect costs are construction costs that are not specifically allocable to a particular construction contract or project. These are the costs of simply being in business.

They commonly include:

Overhead

- Job Site Costs, Home Office Costs, and General Conditions
- Project Managers, Superintendents, and other Support Staff
- Office Trailers, Equipment, and Supplies
- Insurance, Office Salaries, and other Miscellaneous Costs

Equipment

- Owned Equipment and Small Tools
- Depreciation
- Repairs and Maintenance
- Taxes and Insurance

Labor Burden

- FICA Taxes
- Workers Compensation
- Federal and State Unemployment
- Vacation and other Fringe Benefits

Some of the above items may overlap between direct and indirect. For example, a piece of equipment that is purchased for a specific project may be allocated as a direct cost if its lifespan will be entirely consumed over the course of that project.



Indirect costs, because they are a cost of doing business, are generally harder to negotiate as a COVID change order for that reason. It is a cost that would be incurred whether or not you were on a particular project.

An interesting variation on the above is presented by vaccine mandates being imposed on projects after contracts are entered into and where the contractors on the project do not mandate their workforce be vaccinated. The mandates can have the effect of limiting the pool of workers which can lead to project delays and increased costs. We have seen notices of claims in these situations characterizing the mandates as changed job conditions but are unaware of any cases determining how such claims are resolved.

CONSIDERATIONS FOR CALCULATING CLAIMS

Calculating the value of a claim is the last of three key elements of a claim. The first two elements are proof of entitlement for the claimed impact and demonstration of a cause-and-effect between an action or inaction and the claimed impact. Establishment of these two elements justifies the calculation of a claim value.

Information specific to a claim is required to calculate the value of a claim. There are a variety of sources where this information may be found. One common source are documents found on most projects. These may include emails, written correspondence, change orders, requests for information, contractor daily reports, meeting minutes, and cost reports to name a few.

Project drawings and specifications are key to establishing baseline and revised conditions on a project. A comparison of these conditions can provide further support for quantifying the value of a claim. Project photographs can provide further insights into progress and impacts on a project. Of particular interest are photographs that depict impacted work.

Most claims involve impacts to a project's construction schedule. The value of schedule impacts often represents a significant portion of construction claims. A summary of the baseline schedule is important as the starting point for demonstrating impacts. This information is typically found in the contract between the owner and contractor.

Schedules are usually updated at regular intervals. These updates are often accompanied by a schedule narrative that describes progress on the project during the update period and highlights deviations, including impacts.

Labor productivity information is key to valuing claims, particularly when a deviation from planned productivity levels is experienced. Availability of productivity information allows the application of industry accepted methods for valuing claims. Evaluating cost claims can be challenging because of the time and effort required to track information needed for evaluation. Use of the "total cost approach" (actual costs less bid estimate) is frowned upon as it assumes all cost overruns should be reimbursed without regard to causation.

The measured mile approach is the most widely recognized and accepted means for determining impacts on labor productivity. The measured mile approach compares different periods of productivity within a project. This comparison is often used to explain and quantify the impact different conditions have on labor productivity. The measured mile represents labor's ability to perform on a particular project as opposed to a theoretical calculation. Further, the measured mile can be used to determine labor inefficiencies caused by a delay, disruption, or interference on a project. If it can be determined that there is an unimpacted or least impacted period on a project in which labor was efficiently employed, then a ratio can be established between the physical work accomplished and actual workhours expended. This time and associated percentage of work accomplished, and related actual workhours results in a ratio of workhours to percent (workhours/percent) that becomes the measured mile.

The measured mile period is then compared to the impacted period, which allows for a calculation of lost time due to the impact. Further, if the owner is responsible for the delay or disruption, the contractor may be entitled to a claim for the added labor hours associated with the inefficiency. The key advantage of a measured mile approach is the reliance on data agreed to by the architect and owner's representative on a contemporaneous basis during the actual contract performance. The labor productivity levels for both the measured mile and the impact periods are taken from project records, certified payroll, and pay applications.



There are situations when information required to perform a measured mile analysis is not available. As a result, a total cost or modified total cost approach may be applied. As noted above, the total cost method involves subtracting bid costs from actual costs and claiming the difference as damages. Damages presented using the total cost method are based on three assumptions: (1) all claimed costs more than the bid amount are the result of impacts arising from the claim; (2) the bid amount was accurate; and (3) the contractor did not cause any of the cost overrun. This approach is generally not favored but can be successful if certain criteria are met.

A four-part test is usually applied to determine if using the total cost approach is appropriate:

- The nature of the work makes it impossible or highly impracticable to reasonably determine damages by any other method.
- The contractor accurately bid the work.
- The actual costs incurred are reasonable.
- The contractor is not responsible for the additional costs.

The key to both using or defending against a total cost claim is to either support or undermine the underlying assumptions. Credibility can be added to a total cost claim by correcting for bid errors, or excluding questionable actual costs, especially those caused by the contractor (modified total cost approach).

This publication is provided for your convenience to provide general information about current construction management issues. The article does not constitute legal advice. Consult legal counsel if you have specific questions.

This paper was written in conjunction with the breakout session, 'Delay and Impact Claims Related to COVID-19' at the Association of General Contractors (AGC) 2022 Surety Bonding and Construction Risk Management Conference. This version reflects minor formatting and typographic edits from the original.

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Barrett is Executive Consultant with GREYHAWK and has over 20 years of experience in project management oversight, preconstruction and construction cost estimating, project planning and scheduling, and claims and litigation support. Barrett has over 20 years of experience in project management oversight; claims and litigation support; project planning and scheduling; as well as preconstruction and construction cost estimating. He has provided services at all stages of the construction lifecycle, from feasibility studies through project close-out, and construction claim preparation and analysis. Barrett has provided construction cost assessment services during project design, developed and updated fully detailed cost estimates throughout project design, created and analyzed project schedules, facilitated change order negotiations, prepared cost-to-complete reviews, provided construction management services, developed construction claims for both owners and contractors, assisted with insurance appraisal matters, and served as an expert witness. His clients have included public and private sector entities in the following industries: aviation, commercial real estate, financial services, hospitality/entertainment, petrochemical, power/utility, state and local government agencies, education, and residential. In addition, he has been a speaker and educator on the topics of construction cost estimating and planning and scheduling. He has stressed the importance of producing and maintaining accurate and timely cost and time records for the benefit of all project stakeholders. Barrett currently serves on the NYC Bar Construction Law Committee and is a member of the ABA's Forum on Construction Law.