

MANAGING COVID-19 WITHIN CONTRACTS

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INTRODUCTION

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This guide was originally produced by Build UK in 2020 to help the construction industry deal with the effects of coronavirus (COVID-19) – and similar pandemics – within existing and future contracts. Since then, COVID-19 has continued to have a profound impact upon the industry, with projects being disrupted, delayed and postponed. Moving forward, projects that are yet to commence will have to deal with any current restrictions, in addition to changes that might occur over the life of the project.

The Government continues to put construction at the heart of its recovery plans, and it is vital that the industry is ready to respond to the challenges and opportunities that this presents. This will be possible only if parties at all tiers have the cash and confidence to invest in the assets to be delivered and the resources needed to deliver them.

There has been detailed guidance from both Government and industry on dealing with the commercial issues arising from COVID-19 over the last 18 months, and this guide provides a summary of the information available. It builds on Build UK's [Contract Terms Guidance](#) by encouraging active management of risks and pragmatic allocation of residual risks that cannot be mitigated.

The Construction Leadership Council (CLC) has issued a range of guidance which can be accessed via [CLC Taskforce: COVID-19 Contractual Guidance](#). The CLC has been clear that actions at this time will be remembered and that all firms should think hard about how their reputation could be damaged by not doing the right thing, and its guidance is designed to help parties put this collaborative philosophy into practice. Now, more than ever, it is crucial that the industry works together to restore both itself and the wider economy to full health.



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THE CONTRACTUAL POSITION

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Initially, there was considerable focus on whether or not COVID-19 constitutes a ‘force majeure’ or ‘prevention’ event or satisfies the principle of ‘frustration’. The existence of a right to claim relief for such an event will depend on the contractual background against which the claim is made. Even now, there is no definitive answer and it is likely that even a decision such as a court ruling would not apply universally.

Whilst there has been a reluctance on the part of some clients to *formally* acknowledge COVID-19 as an event of this nature, guidance published by [Government](#) and industry bodies, such as the [CLC](#) and [NEC](#), *informally* recognises the position that COVID-19 was not foreseeable before March 2020 and has not arisen due to the fault of any one party.

Such guidance, which remains valid, recommends taking a pragmatic approach to dealing with the supply chain and offering an extension of time, and in some instances loss and expense, on the basis that the supply chain will reciprocate by helping to mitigate the impact on projects. Build UK supports this approach, and this guide builds on the broad consensus that has been developed across the industry during the pandemic.

There is no commercial or contractual arrangement that will be appropriate in all circumstances; every project will have different priorities and each party involved in the project will have varying capacity to accept and manage financial risk. This needs to be recognised and openly discussed on a project-by-project basis so that all parties are aware of the risks and incentivised by project outcomes.

Where parties intend to rely solely on the formal provisions in their contract, entitlements and obligations will need to be determined by reference to that contract. Every contract is different and it is rare for unamended standard forms to be used.

If COVID-19 were ever to be accepted or determined legally to constitute a force majeure event, then the general position is that under JCT forms of contract, the Contractor is entitled to an extension of time, but not money, if a force majeure event occurs, whereas under NEC forms, the Contractor is entitled to time and money if a prevention event occurs. The parties can agree to vary these terms if practical considerations, such as those outlined in sections 4.9 and 4.10 of the updated [Contractual Best Practice Guidance](#) published by the CLC, will offer a better outcome for the project.

Change in Statutory Requirements

Under JCT forms of contract, force majeure may not be the only route to recovery. JCT provides that alterations or modification to works that are necessitated by a change in ‘Statutory Requirements’ – which arguably includes the introduction of new rules – gives rise to an entitlement to both time and money. For example, HSE enforcement of social distancing on construction sites suggested that the industry was required to comply with such rules, and this may have given rise to an entitlement to an extension of time and/or loss and expense under JCT terms.

The extent to which these provisions will apply will vary according to the terms of the contract and the specific circumstances giving rise to the delay or cost, and it is recommended that parties take a pragmatic and reasonable approach to their application.

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There are three basic scenarios that the industry is having to manage:

- 1.** Existing projects that commenced without express provision for the impacts of COVID-19.
- 2.** Contracts that have not yet commenced.
- 3.** Contracts that have commenced in the last few months and which contain bespoke COVID-19 provisions.

Where parties have already made bespoke arrangements in recently formed contracts to deal with COVID-19, those arrangements will take precedence. However, in the event that issues arise, the parties may wish to refer to these recommendations to help resolve them.

There are some principles that apply equally, whether dealing with the allocation of the cost and time impacts of what has already happened on existing projects, or the management and ownership of risks in relation to future projects.

In both cases, the focus of all parties should be on working collaboratively to resolve challenges in the most time and cost effective manner, ensuring that any costs are distributed fairly based on what each party can bear.

Build UK's [Contract Terms Guidance](#) deals with the pitfalls of asking the supply chain to take on 'unquantifiable risks' and 'uncapped liabilities', and this advice is directly applicable to COVID-19 and should guide parties in their approach to managing both the historic and future impact.

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All stakeholders need to recognise the specific impacts on time and cost that COVID-19 has had on their projects, agree that they are nobody's fault, and make a fair and commercially viable contribution to meeting them.

An adversarial approach increases the risk of disputes, abandoned projects and insolvencies. The reality is that fighting for everything may leave you with nothing, so it is essential that all parties work together to find fair and reasonable settlements for what has happened, and mechanisms for managing what is to come.

With almost two years having passed since COVID-19 first started to impact the industry, it is likely that on many existing projects the parties will have found a way to move forward. For those that have not, the CLC [Contractual Best Practice Guidance](#) contains advice for parties and the key messages are summarised as follows.

1. Protect the supply chain

- Specialist Contractors in particular are often cash negative for the majority of their contract period, making them extremely vulnerable to cash starvation and the risk of becoming insolvent. It is in the interests of Clients and Contractors to ensure that their supply chains are able to complete their projects by reducing the financial burden.
- Relieving financial pressure on businesses may also help to control the spread of the virus itself, as economic pressure can lead people to take greater risks in relation to social distancing in order to complete work and maintain programme.
- Where Clients take steps to support their supply chains, it is important that they actively monitor that payments flow quickly through the whole supply chain.

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2. Progress projects safely

- The safety of the workforce and the general public is paramount, and any arrangements to progress projects should avoid placing cost and/or time ahead of safe working practices.
- Challenges should not be considered problems for individual parties to solve; they should be viewed as project issues requiring project solutions. Regardless of the contractual arrangements in place, all parties should cooperate as a project team with a shared focus on finding the most time and cost effective solution for delivering the project objectives within the current situation.
- Clients should lead the discussions as they know what their priorities are. For example, could they accept delayed completion if it mitigates cost, or is there a cost they can live with for completing on time?
- Direct engagement with the lower tiers of the supply chain is critical and may result in imaginative approaches to mitigate cost and/or time impacts on projects. Specialist Contractors often plan and resource their work within constraints and timelines determined by others earlier in the construction process; however, they may be able to offer flexibility to preserve or accelerate progress, for example longer hours, multiple or split shifts, or weekend working.
- Similarly, Consultants may be able to increase resources to speed up approval and/or acceptance processes. For example, 28 day periods for review and approval of drawings or method statements could be shortened.
- Ultimately, the Client knows what they want and what they are willing to pay for it and the supply chain understands what can practically be achieved and how much it will cost to deliver it. This is the dialogue that will form the basis for developing project completion strategies that all parties can live with.
- Whatever actions are taken, it is essential to make a record to allow the impacts of these actions to be evaluated, whether by negotiation or in a dispute scenario – see *'Keep good records'* below.

EXISTING CONTRACTS

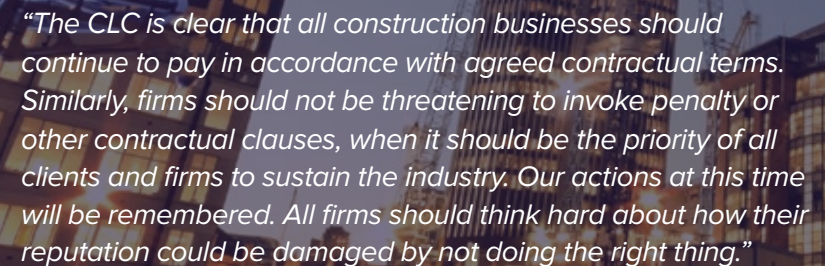
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3. Negotiate quickly and in good faith

- Act quickly to reach agreement on both historic issues and strategies for project completion to relieve all parties of uncertainty so they can focus on delivering the project.
- Be honest and take a realistic view of how to allocate responsibility for any problems that pre-dated the impact of COVID-19. It may be worth trying to separate the pre-COVID-19 phase of the project from the post COVID-19 period, for example by agreeing a *'pre-COVID-19 Final Account'* and any extensions of time to draw a line from which to move forward. If necessary, make the agreement non-binding and, in the event a final agreement cannot be reached, all parties will have the right to have the dispute ultimately determined by a third party. The CLC has published a [COVID-19 Cost Assessment Toolkit](#), which provides guidance on assessing the COVID-19 impacts on a project.
- Where contracts commenced after the pandemic started, it is likely they included recognition of the constraints that existed at the time the contract was agreed. If those constraints changed as the work proceeded, then the approach should be the same as for contracts that were ongoing when COVID-19 first struck and any changes should be recognised as a shared challenge and dealt with on a collaborative basis.
- Once historic events have been resolved, parties should agree strategies for the completion of the project. Open book arrangements may be beneficial as this will allow changes in COVID-19 restrictions to be managed – see *'Use open book processes'* below.
- To give negotiations the best chance of success make use of 'without prejudice' forums for open and honest discussion of options across all tiers. The CLC [Managing Contractual Disputes & Collaboration – Summary Guide](#) includes advice on creating a *'without prejudice – safe place'* environment for parties to explore options. More detailed advice can be found in the [Contractual Best Practice Guidance](#) together with [template](#) letters and notices for use with the most common forms of contract.

4. Settle

- It is rare that either the project or its participants benefit in the long run from allowing disputes to fester, so every effort should be made to reach a settlement agreement that allows cash to flow, projects to be completed and businesses to continue.
- However, where this is not possible, parties may need to obtain third party assistance in finding a settlement and should use the quickest method of dispute resolution available. The relative merits of dispute resolution options are outlined in the CLC [Managing Contractual Disputes & Collaboration – Summary Guide](#).



"The CLC is clear that all construction businesses should continue to pay in accordance with agreed contractual terms. Similarly, firms should not be threatening to invoke penalty or other contractual clauses, when it should be the priority of all clients and firms to sustain the industry. Our actions at this time will be remembered. All firms should think hard about how their reputation could be damaged by not doing the right thing."

CLC Statement on Payments and Contracts

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Whilst the emergence of the COVID-19 pandemic in March 2020 *may* have been considered an unforeseeable event that would give rise to contractual relief on projects that were running at that time, it would not be considered unforeseeable now.

Any contracts entered into going forward would be expected to allow for the known impacts of the outbreak at the time of pricing and to include mechanisms for dealing with further developments. This will include sub-contracts that have not yet been awarded on projects that started before COVID-19 struck. Parties should resist the temptation to try to pass the risk down the supply chain. They should operate a *risk management* rather than a risk transfer approach. Further information on this can be found in Build UK's [Contract Terms Guidance](#).

Essentially, the parties should agree whether a COVID-19 event gives rise to:

Option 1: an extension of time.

Option 2: an extension of time and payment of all the Contractor's/Sub-Contractor's loss and expense.

Option 3: an extension of time and payment of a pre-determined percentage of the Contractor's/Sub-Contractor's loss and expense.

The CLC [Future Proofing Guidance: JCT/NEC Contract Amendments](#) includes model clauses for use in common JCT and NEC contract forms to allow parties to give effect to whichever of the three options they agree. For NEC contracts, there is a joint CLC/NEC guide, [NEC and CLC Guidance for Dealing with the Effects of COVID-19 Under NEC3/4 Contracts](#), to help parties to agree what is and is not included in the contract price and programme and to deal with changes to those allowances.

To ensure any agreement is effective and simple to operate, parties should take care to consider the issues as follows.

1. Establish a baseline for the level of restriction included in the contract price and programme

- Contracting parties should clearly set out what is and is not included in the contract price and programme so that there is clarity as to which COVID-19 related events give rise to time and/or cost relief. As price and programme can be developed months ahead of contract commencement and legislation and guidance may change during that time, the parties should also include a 'base date' from which change is measured.
- A contract signed today should reasonably be expected to allow for *current* legislation and guidance on matters such as international travel, transport constraints and provision of PPE, and parties might choose to agree that these would not count as relief events.
- However, it is more difficult to make allowances for other matters, for example one or more project workers contracting COVID-19 or changes in legislation or guidance, such as local lockdowns, and these would give rise to relief should they occur.
- The CLC [COVID-19 Cost Assessment Toolkit](#) provides templates for recording inclusions and exclusions, as do collaborative standard form contracts, such as NEC Option C and JCT Constructing Excellence.

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2. Use open book processes

- In the current circumstances, where there is a high risk that developments around COVID-19 could cause fundamental changes to the time and/or cost of a project, there is a strong case for making contracts at all tiers 'open book'. This provides visibility and established target cost and disallowable cost mechanisms, such as those used in NEC and the JCT Constructing Excellence contract, can be used to transfer reasonable contracting risk and incentivise efficiency.
- Such mechanisms are important to ensure that open book is not confused with 'cost plus' or 'cost reimbursable' where the entire time and cost risk of a project rests with the Client.
- Open book processes are therefore particularly helpful when it comes to measuring time and/or cost impacts of a COVID-19 event. For example, if a change in guidance reduces the number of operatives that can be on site at one time, it is very difficult to measure the effect if there is no transparency as to how many operatives were assumed in the original price.
- This avoids any arguments about what was included or should have been included and leaves the parties free to focus on how best to work around the new constraint.

Using this Guidance

This publication is issued by Build UK Group Limited in order to give general guidance only on what it considers to be best practice; if you require guidance on a specific issue, you should seek your own independent professional advice.

3. Do not ignore the possibility that things could get better

- It is natural to focus on the risks of further outbreaks or increases in restrictions; however, construction projects can run for months or years and it is possible that restrictions might be relaxed or removed before a project is completed.
- Open book arrangements will allow Clients to benefit from such improvements to the same extent that they are taking the risk on delays or additional costs.
- Sub-contracts that are entered into later in the construction period might be subject to different restrictions to those that were in place when the main contract was entered into. Contracts should contain sufficient flexibility to ensure that best value can be delivered throughout the construction period.

4. Keep good records

- Whether the parties have agreed to work collaboratively or one party has given notice of a contractual claim, good records are essential.
- If a Client is to be asked to reimburse costs, they will expect to be able to audit what those costs are and that they were actually and necessarily incurred. If a party seeks to demonstrate a contractual entitlement, they will need records of the event giving rise to the entitlement and of the time and/or cost incurred. Further information on what records to keep and how to maintain them can be found in the CLC [Record Keeping Guidance](#).