Insights from a legal perspective on proving costs and schedule impacts arising from COVID-19

Claims/impacts due to COVID-19 will likely need to be proved/litigated two to three years from now. Through the myopic element of 20/20 hindsight, you will need to show that costs were reasonably incurred and that reasonable efforts were made to mitigate and minimize those costs. It’s time to develop a strategy showing that these claims have merit and should be compensable.

Consider the audience that will respond or evaluate your case.

- Some claims will be asserted against project owners while others will be against subcontractors.
- Claims may come up against various government agencies, and relief may be afforded from government programs.
- Various insurers may come into play: Builder’s Risk, General Liability, Business Interruption or Subcontractor Default Insurance (SDI).
- Outside evaluators like auditors, lawyers, judges, juries, arbitrators and mediators will be reviewing your documentation.

Jobs are not going to resume with complete efficiency and productivity; the impact of these events will be felt over a long period of time.

- Segregate and document the impacts on your project and track them in as many discrete buckets as possible. Avoid just one cost code for COVID and use it to aggregate everything related to the crisis.
- Assemble a short narrative describing each category to explain the cost, why the cost was incurred, and how it was incurred.

- Have your mitigation strategies in place and document them well. Every party has an inherent obligation to reasonably mitigate damages, control costs and minimize exposure.

Different costs are going to face different entitlement challenges from different audiences. For example, one insurance policy may provide coverage for disinfection costs for a COVID-confirmed case on a job, but it may not cover the costs related to delays or acceleration.

- Recoverability will depend on unique policy and contract terms as well as the unique factual circumstances that drove the basis for the costs.
- Tracking costs in discrete categories permits correlation of those costs with their potential entitlements once the costs and avenues of recovery are determined.

Schedule and efficiency costs are specialized claims.

- Record the cause of the delay and provide a short narrative about why it happened. For instance, document deliberate slowing down of a given trade because a predecessor trade could not perform.
- Measure productivity on a project prior to COVID impact and compare that with the diminished productivity on projects that still have the ability to progress once jobs ramp up again.

Finally, revisit your strategy periodically to make sure it remains effective and current in this fluid and dynamic situation.
SDI Market Update and How to Incorporate Delays and Impacts to the Project Schedule

The project schedule is the key document to support claims and should be the main focus of your project manager’s attention. Making the appropriate adjustments will allow you to use it as an effective tool to build your impact or delay narrative.

Market Update
- There’s been no uptick in notice activity or losses. There will be challenges as the situation evolves. The extent of this impact will depend on how owners and contractors manage expectations when ramping back up to the “new normal.”

The health and status of your project schedule pre-COVID will be an important factor when addressing productivity and other downstream effects.

Make sure your as-built dates are rock-solid, both before and after the impact. Inaccurate data will create credibility problems and challenge support for any claim.

Do’s and Don’ts
- Avoid just one cost code for COVID and use it to aggregate everything related to the crisis.
- Avoid the impulse to adjust your schedule to show your project owners that you can minimize the delays from this crisis. This will result in an overcompressed, extremely altered and unreliable schedule.
- Avoid setting commitments prematurely, as the impacts are more far-reaching than we are probably anticipating today. Take a really deep look and analyze every task; no two tasks will be impacted the same way.
- Engage your subcontractors and understand the logistical constraints in this new environment and the impact they will have on productivity levels.
- Delays within the supply chain will be difficult to predict as you will experience production and delivery delays for every trade differently.
- New logistical limitations were not factored into your original schedule. You will need to add task-specific variances for all the work that was impacted or expected to be impacted.
- Do not generalize. Don’t just add a common delay fragment for each floor/phase. This needs to be done for every task and trade, each of which will be impacted differently.
- Go back to the basics; they still apply. Monitor your planned versus your actual, and use your project schedule as an effective tool to build your impact or delay narrative.

Surety Industry Update and Perspective

The surety and construction industry are in this event together, and our objective is to find a responsible way to deal with it. The surety industry is writing bonds and will continue to do so long after this crisis is over.

There’s been no significant claims activity in the surety market directly related to COVID. This is due to:

- Unprecedented cooperation within the industry to lobby state and local governments to keep construction—both public and private—classified as essential and ongoing.
- The construction industry has received over $35 billion from the CARES Act, and it was structured more as capital than debt.

Markets will undoubtedly harden, but underwriting will adjust and adapt to this event.

- Closer attention will be paid to bond and contract terms to ensure fair allocation of risk to those who can best control it.
- Less reliance on financial analysis and more personal contact with principals to learn about what is going on and which jobs are impacted.
- Perhaps less flexibility on the release of personal indemnity.
- Personal, more frequent visits by web videoconference may well become the norm for underwriters, brokers and their principals as time goes forward.
- Underwriters appreciate proactive reporting and strategy review requests from principals.

Claims are expected to emerge from two different areas:

- Suspended jobs will cause financial distress in terms of cash flow interruption, delayed payments, cost of warehousing, etc.
- Ongoing projects are more likely to result in direct claims, where a principal will be unable to perform due to supply line interruption, job site inefficiencies or the unavailability of labor.
Evaluating and Managing Liquidity Through Scenario Planning

There will be opportunities for well-capitalized general contractors who planned in advance and that knew what they had available because they went through scenario planning.

- **Manage and monitor the liquidity of your subcontractors:**
  - Financial statements are a lagging indicator, so monitor in real time and rely on personal contact.
  - Identify subcontractors who were already stretched before this event and monitor metrics like vendor supplier payments, union benefit payments and their statuses on other jobs.
  - Support your subcontractors to free up cash yet continue to monitor performance.
    - Find out which subs tapped into CARE resources and educate them on what might be available nationally or through local association support.
    - Have a conversation with your owners about payment terms.
    - Determine if retainage can be released early on jobs that were moving forward.
    - The real liquidity crunch is likely going to happen during the ramp-up as the impact of delayed payments begins to be felt.

- **Support your own company’s liquidity in order to survive and take advantage of opportunities that are going to happen:**
  - Revenues through 2020 are expected to decline between 10-30%, representing a use of cash. However, there will be opportunities for GCs who are well positioned and well capitalized.
  - Determine the amount of liquidity needed to survive for the next 30, 60 and 90 days.

- **Monitor working capital and fixed cost needs** to determine how to improve your position.
- **Create a liquidity reserve and consider a line of credit to ensure cash availability.**
- **Revisit strategic principles and consider where you want to be in the future.**
  - Do not forgo investments in your business, but definitely prioritize them.
  - Consider picking up talent that was not available before the pandemic.
  - Ability to move into new markets.
    - Pick up backlog and market share for firms that did not survive or are in a diminished state.
    - Opportunities for mergers and acquisitions are emerging.
    - Potentially may need to take over some subcontractors and step into a self-performing capability.

- **Consider your own personal liquidity.**
  - Most GC ownership transfers occur internally through family/key employees, and they often take time and profits within a business to fund.
  - Industry demographics are unchanged with an aging ownership base.
  - Personal indemnities are likely to increase with the need to potentially put cash back into the businesses to keep underwriters happy with the financial ratios.
  - Revisit your exit strategy/buy-sell agreements and do scenario planning on how you planned to get your liquidity out of the businesses.
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