

Construction costs for COVID-19 claims: what's the difference between Level 4 and Levels 3 & 2?



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Having survived Level 4, it is a brave new world as we move to accelerate infrastructure projects under Levels 3 and beyond. The welcome Government guidance on the approach to contractual claims under Level 4 has resulted in, anecdotally, contractors being quite pragmatic in the claims they are submitting under their NZS 3910:2013 contracts. However, the position is less straightforward under Levels 3 and 2.

The uniqueness of the COVID-19 suspension under Level 4 resulted in two different paths under unamended General Conditions of NZS 3910:2013 to deemed variations either due to a suspension of the Contract Works being necessary (GC 6.7.1) or as a result of a change in law (5.11.10). An extension of time due to the net effect of those variations resulted in an EOT (GC 10.3.1(a)) and thereafter time-related costs (GC 10.3.7). Valuation of the variation then proceeds through the well-trodden process in GC

9.3 whereby the parties are to first attempt to reach agreement and in the absence of agreement the contractor's claim is to be assessed:

- On the basis of applicable rates in the Schedule of Prices (SOP) (if any);
- Where there was not a directly applicable item in the SOP, then to derive a rate; and
- Where a rate could not be derived, then to value as Net Cost.

In practice, the contractual mechanism has proved challenging to apply in these circumstances. Particularly when it comes to assessing time-related costs a number of contractors are finding that the overall value of the variation, after applying the contractual percentages for overheads and profit, gives rise to a substantial under-recovery for both onsite and offsite resources, from the actual costs incurred during the Level 4 lockdown. Similarly, in some cases, the working day rate has been found to be inappropriate, either because it did not anticipate a full shutdown of the industry, or because of the relative stage of completion of the works. Parties have instead been looking to GC 9.3.12 to determine equitable compensation.

We are seeing pragmatic parties having open discussions more akin to an overall Net Cost claim generally with many principals accepting that this approach fairly compensates their contractors, for the Level 4 shutdown.

The same approach is neither required nor appropriate for claims dealing with the period after the Level 4 lockdown was lifted. There is a substantial difference between the unique suspension of all construction work in New Zealand (barring essential

services) under Level 4 and the environment we are now in during Level 3 and beyond. Under Level 3, projects are underway, the Contract Works are being performed and aside from disruption to productivity rates, life is gradually returning to normal. This is not to understate the challenges faced by all parties under Levels 3 and 2, but it is to highlight that we are back to the 'new normal' albeit at perhaps a less productive rate.

The starting point at Level 3 and beyond is that the contractual rates are to be paid for work performed under the contract in the normal way. Ordinary monthly claims can be made as before. There is no reason for the parties to be moving to a Net Cost approach to valuing these claims as if all of the works are a Variation or for there to be any substantial change in the presentation of the contractor's claims, unless there are certain additional costs or an EOT claimed due to the Level 3 restrictions, or a loss of productivity element to those claims.

For those additional costs and any EOT claimed, the correct approach by the parties is still to consider the Variation claim under GC 5.11.10 as there has been a change in law in the issuing of the Health Act (COVID-19 Alert Level 3) Order 2020 on 24 April 2020, COVID-19 Public Health Response Act 2020 and COVID-19 Public Health Response (Alert Level 2) Order 2020, dated 13 May 2020. The valuation of that deemed variation will be on any additional costs and resources needed to manage the increased health and safety requirements, any additional costs in sourcing materials both locally and from overseas due to the border restrictions and the impact the restrictions are having on manufacturing and distribution of materials, any any disruption/reduction in productivity. The time impact will be dealt with under GC 10.3.1(a) for the net effect of that Variation. The disruption will likely be assessed by looking at the pre-shutdown programme and productivity records compared to the programme and productivity records for Levels 3, 2 and 1. Claims for time-related costs will need to be considered as the project will take longer to complete and therefore P&G expenses will be incurred for a longer period than planned, including for onsite and offsite supervision and management.

It will be critical to the assessment of these claims for the parties to maintain accurate records of productivity. Contractors should be keeping daily

records of the activity of workers, machinery and plant. Information should also be sought from manufacturers and suppliers so that accurate records can be kept on lead times for materials and plant both from within in New Zealand and overseas.

While the environment changed substantially once we moved to Level 3, life is still not back to normal as we know it. The mechanisms under the contract became far more workable and easier to apply in Level 3, however, this should not be to the exclusion of a collaborative and pragmatic approach to a claim resolution. As we all know, the ultimate goal for a sustainable industry is for all parties to work together to achieve a successful outcome on the project and for both principal and contractor to come out the other end in a relatively healthy position. What should not occur is an insistence by either party that all future claims are to be assessed according to Net Cost simply because that approach may have been taken to address claims under Level 4.

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