ADDLESHAW GODDARD

CONSTRUCTION CONTRACTS IN LIGHT OF BREXIT

INTRODUCTION

- We look in more detail at some of the areas of risk to construction projects identified in our article on Brexit and Construction Contracts[1] in the spring edition of Constructive Comments.
- Contractors are particularly vulnerable to Brexit related consequences under fixed price contracts and some are seeking amendments aimed at mitigating the impact of Brexit and transferring risk to (or sharing risk with) their employers.

RISK ALLOCATION AND AMENDMENTS TO STANDARD FORM CONTRACTS

SHORTAGE OF LABOUR

Brexit has the potential to create both a shortage of labour and an increase in labour costs. Fluctuations provisions (such as those found in (and usually deleted from) the JCT contracts) could be adapted as necessary to protect the contractor against increases is labour costs. However, at the current time it seems unlikely that employers will be willing to bear the risks arising from a shortage of labour (in terms of an increase in the contract sum and/or the grant of an extension of time), particularly as labour shortages are traditionally a contractor risk and maintenance of an appropriate workforce is within the contractor's control.

TARIFFS, LEVIES AND FEES

It is expected that there will be new or increased costs arising from the imposition of taxes, duties, tariffs, levies, fees and customs charges on goods imported to the United Kingdom (UK) from the European Union (EU), following the UK's exit from the EU. One way to deal with any increases in tariffs, levies and fees is to include fluctuations provisions. If an employer is willing to accept (or share) the risk of any such increases he should ensure that the fluctuations provisions are tailored, so that he does not find himself out of pocket for inflationary rises which are not a direct result of Brexit. It goes without saying that a risk sharing mechanism, whereby any tariffs, levies and fees which arise as a consequence of Brexit are shared between the employer and contractor, is more likely to be acceptable to employers than a full transfer of this risk.

Increases in the cost of goods and materials, such as price increases arising from a fall in the value of sterling, are another area of risk for a contractor, and one which could be included in a fluctuations provision. The adoption of provisions of this nature are uncommon in the market and employers, used to operating under fixed price contracts, are likely to be resistant to bearing (or sharing) the risk of currency fluctuations. An employer may possibly be more likely to accept this risk where the specification expressly requires the use of particular materials which are manufactured overseas. We may also see trade-offs, with contractors bearing the risk of currency fluctuations and the employer bearing the whole or part of the additional costs of tariffs, levies and fees.

SHORTAGE OF GOODS AND MATERIALS

Brexit may also be the cause of delays and shortages of goods and materials coming into the UK from the EU and this may not be limited to goods and materials produced in the EU. Goods and materials may be coming to the UK from, say, China through the EU and so be subject to the additional post Brexit border checks, etc. The Department for Business, Energy & Industrial Strategy reported that approximately 62% of construction materials and goods are imported to the UK from the EU[2]. Based on these figures it is possible there will be shortages or delays in the import of building materials (though interestingly the UK exports 63% of the construction materials that it produces to the EU - a decline from the 2007 pre-recession level of 70%[3]). Again, in the absence of express provisions in the contract, it is the contractor who will be liable for increased costs and damages if delay arises as a result. Given the circumstances it would be prudent for contractors to consider maintaining a stockpile of imported goods and materials which are frequently used in construction projects. This approach of course, requires healthy cash flow and storage space.

[1] https://www.addleshawgoddard.com/globalassets/insights/construction/brexit-and-construction-contracts.pdf
[2] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/813407/19-cs7_-_Construction_Building_Materials_-_Commentary_June_2019.pdf
[3] https://www.addleshawgoddard.com/globalassets/insights/construction/brexit-and-construction-contracts.pdf

One approach the employer may wish to consider is to allow the contractor to substitute materials (provided they are of similar quality and the employer approves the substitution) where there is likely to be delay in the importation of goods and materials or the cost has increased as a result of withdrawal. Contractors, of course, may seek to include provisions entitling them to an extension of time where the importation of goods is delayed by border checks, although this is unlikely to find favour with the majority of employers who would consider the timely ordering of goods to avoid delay to be a contractor responsibility.

With the continued uncertainty over Brexit and its consequences these issues are likely to feature increasingly in contract negotiations over the coming months. Whether they will lead to a move away from a fixed price culture remains to be seen.

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