

Client Update

Shaping the future of insurance law

Operational and consequential impacts of COVID-19 on the construction industry

2 APRIL 2020

AT A GLANCE

- Between government-imposed social distancing measures and global supply chain disruptions, the construction sector is suffering the impacts of the coronavirus.
- The industry is experiencing significant direct operational impacts, ranging from WHS issues and contractual exposures to the erosion of asset values.
- Professionals working in the industry are also suffering flow-on effects, including (in some instances) mounting pressure on discharging their obligations when they cannot physically attend sites.
- Insurers need to recognise the risk of parties potentially trying to pass coronavirus-related losses down the contractual chain.

To say that the coronavirus (COVID-19) has had far-reaching effects across all industries is an understatement – and the construction sector has not been spared. This article examines the operational and consequential impacts of coronavirus on the construction industry so far, and predicts claims we might see in the future, particularly in the construction professionals space.

DIRECT OPERATIONAL IMPACTS

Workplace Health and Safety

Like most industries, the construction industry is finding itself having to navigate issues of safety in the workplace and on the worksite due to the spread of coronavirus. As social distancing

measures take greater effect, the workplace has become much less able to mobilise. This is making it increasingly difficult for builders and supervisors to manage their sites, particularly because of the close confines in which construction personnel tend to work.

As recently as this week, the Victorian Building Authority (VBA) issued an updated circular¹ reinforcing its best practice regarding worksite management and protecting workers, and those who enter the worksite, from the effects of coronavirus. A similar circular has been issued by the Housing Industry Association, which is

1

https://www.vba.vic.gov.au/data/assets/pdf_file/0018/110628/COVID19-Best-Practice-Managing-Construction-Sites.pdf

supported by the Insurance Council of Australia (in the context of insurance work which involves the repair and rebuilding of properties)².

If federal and state governments continue to increase the restrictions on the movement of people, this will likely continue to have a detrimental effect on the construction industry. It will also heighten the responsibilities of construction companies and consultants to properly protect their workforce.

Contractual Implications

There have already been reports of parties to construction contracts enforcing rights of force majeure by reason of the unexpected and disruptive effect of coronavirus.

In simple terms, a force majeure clause entitles a party to a contract to terminate a contract, or avoid liability for non-performance, where events beyond their control mean the contract cannot be performed. Sometimes events giving rise to a force majeure are defined by the contract, but often they are not. The question then becomes whether the spread of coronavirus, and the associated government restrictions, constitute a force majeure event.

The terms of construction will require careful review to assess whether parties are entitled to rely on any force majeure clause if they are unable to perform their contractual obligations by reason of coronavirus. If such a clause is incorrectly relied on, then contractors risk being found in breach of contract for non-performance, or perhaps for having repudiated the contract. This would potentially make them liable for full contractual damages by reason of repudiatory breach.

Other contractual issues are delay and liquidated damages. Predictably, many construction projects are likely to fall into delay by reason of the impact of coronavirus. Obvious causes of this, for example, are the unavailability of materials from affected countries or of trades or consultants. This may or may not entitle contractors to extension of time (EOT) claims under their contracts, depending how the EOT clauses are structured. Assuming EOT clauses entitle a contractor to make an EOT claim, it is imperative that the requirements of the contract are adhered to, for example regarding the

giving of notice within the stipulated time with the requisite information. Contractors that are not entitled to an EOT are susceptible to damages or liquidated damages claims if they fall into delay.

Commercial Implications

While the effect on the property market of coronavirus remains to be seen, the overwhelming view of commentators seems to be that property prices are likely to fall. This raises the very real risk of declining equity in developments, and in turn the potential for continued financing to be compromised. If margins are slim, and equity declines, there is a very real risk of developments grinding to a halt. In turn, more losses will be suffered and more claims will be pursued downstream.

CONSEQUENTIAL EFFECTS

Many construction professionals are reporting that government work is continuing. In fact, some state and federal governments have moved to fast-track medical and hospital projects, including temporary accommodation for coronavirus patients. Clearly, this will be an ongoing source of work for the construction industry that increases the demand for professional services. Conversely, non-government funded projects have, by all reports, started to slow.

Beyond the client-base exposures, construction professionals are also finding it difficult to discharge their obligations under contracts in circumstances where physical attendance to site is required. For example, under statute, surveyors and certifiers are required to conduct mandatory inspections of building works to a required standard. That raises the question: if they are unable to attend site, because of a government requirement or because they can't practically mobilise their workforce, how can they meet the mandatory statutory requirement to inspect? Similar difficulties arise, albeit not in a statutory context, with building inspectors and certifying engineers.

In theory, there is also a risk of conflict between the professional discharging their statutory obligations and their obligation as employers to protect employee health and safety – not to mention the requirements imposed by governments around social distancing and

² <https://hia.com.au/Publications/InformationSheets/how-should-i-manage-my-construction-sites-during-coronavirus>;

mobilisation. For example, a failure to properly discharge an inspection obligation due to social distancing requirements could potentially amount to a breach of professional duty.

Claims may also be brought by owners and developers against contractors and construction professionals if owners and developers suffer loss because of the impact of coronavirus. While this does not necessarily mean that contractors and construction professionals are to blame for those losses, the current environment might incentivise owners and developers to make claims that might normally be considered marginal at best.

THE ISSUES FOR INSURERS

First and foremost the COVID pandemic is likely to see some contractors seeking to cut costs. Experience tells us that this is one of the most common causes of claims. This is likely to make the financially secure contractors who are not under margin pressures more attractive to underwriters.

NEED TO KNOW MORE?

For more information please contact us.

AUTHORS



Nick Lux

Partner, Melbourne

T: +61 3 9604 7902

E: Nick.Lux@wottonkearney.com.au



Andrew Moore

Partner, Sydney

T: +61 2 8273 9943

E: Andrew.Moore@wottonkearney.com.au

There is also likely to be an incentive to try and pass losses which will eventuate down the contractual chain in the hope that some form of recovery will help ease the burden of the negative financial impacts of coronavirus. While there is bound to be a lag between the losses being suffered and the claims being pursued, it seems likely this will be an issue insurers will have to face.

This likelihood underscores the need for increased vigilance around record-keeping and contemporaneous correspondence. Those practices will help make claims, no matter how unmeritorious, defensible.

Insurers should also encourage insured construction professionals to review their standard terms and conditions to better understand their potential exposure to upstream claims should their businesses be affected by coronavirus. This will include their ability to adequately perform their services in a timely way, or at all.

ADDITIONAL STATE CONTACTS



Andrew Brennan

Partner, Melbourne

T: +61 3 9604 7933

E: Andrew.Brennan@wottonkearney.com.au



Raisa Conchin

Partner, Brisbane

T: +61 7 3236 8702

E: Raisa.Conchin@wottonkearney.com.au



Tim Searle

Partner, Perth

T: +61 8 9222 6925

E: Tim.Searle@wottonkearney.com.au

© Wotton + Kearney 2020

This publication is intended to provide commentary and general information. It should not be relied upon as legal advice. For mal legal advice should be sought in particular transactions or on matters of interest arising from this publication. Persons listed may not be admitted in all states and territories. Wotton + Kearney Pty Ltd ABN 94 632 932 131, is an incorporated legal practice. Registered office at 85 Castlereagh St, Sydney, NSW 2000