AGENDA

01 Industry Trends

02 Negotiating Escalation Clauses

03 Practicum – Drafting Escalation Clauses

04 Conclusion
AGC 2022 National Survey Results

- Pandemic impact on projects this year
  
  **TOP ANSWER:** MATERIAL COSTS

- Postponed/Cancelled Projects in 2021 or 2022
  
  **TOP ANSWER:** HIGHER COSTS THAN EXPECTED

- Biggest concerns for 2022
  
  **TOP ANSWER:** RISING COSTS
The Trend?
RISING COSTS
Guaranteed Maximum Price Contracts

- Contractor guarantees its price against price escalations (this is the contractor’s risk).

What is the BIG DEAL?
Negotiating Escalation Clauses

Negotiating Contracts to Address Recent Challenges
Contracts – Price Escalation Clause

- Many standard industry contract templates do not contain a price escalation provision.
- Contractors must be prepared to negotiate their inclusion.
- What incentive do Owners have to allow their inclusion?
Factors to Consider

1. Define eligible materials.
2. Incorporate contractor’s proposal into the provision.
3. Define escalation clause threshold.
4. Timeliness – Define the applicable time period.
5. Documentation required to support material increase.
6. Is the Owner entitled to a price deduction?
1. Define Eligible Materials

- Is the provision applicable to ALL increased materials?
- Or is it limited to an identified list of materials?
2. Incorporate Contractor’s proposal/bid

How can we adjust the price unless we identify our starting point?
3. Define escalation clause threshold

- Does it kick in after a certain percentage of increase?
- Who bears the risk for escalation below the identified threshold?
- Technique for allocating risk.
4. Timeliness Provision

- What is the relevant timeframe?
  - Anytime after the execution of the contract?
  - Time frame specific?
  - At the time materials are purchased?
- Parties can use this timeliness provision to allocate risk.
5. Supporting Documentation

Documentation required to support material increase.

- Think about what documents must be provided as back up support.
  - Invoices?
  - Whose letterhead?
  - Evidence of multiple price quotes?
6. Is the Owner entitled to a price deduction?
Practicum – Drafting Escalation Clauses

Negotiating Contracts to Address Recent Challenges
Sample – Materials Price Escalation: The Contract Sum is based upon Contractor’s Basis of Estimate (Exhibit XXX), which in turn is based upon the respective prices of certain commodity-based construction materials as of the date of the execution of this Agreement. For purposes of this Section, the term “Eligible Material” shall mean ______________. A “Significant Price Increase” shall mean an increase in the base commodity price of an Eligible Material that (i) exceeds ______ percent (___%) of the Contractor’s price for Eligible Materials as quoted or included in Exhibit XXX and current at the time of the execution of the Agreement, and (ii) occurs __________ (timeliness provision). Any Significant Price Increase that occurs after (a) __________ (timeliness provision) and (b) directly results in Contractor incurring additional expense due to the increase in the base commodity cost of such material, above the anticipated cost for such material included within Exhibit XXX, shall cause the Contract Sum to be increased by the net amount of the Substantial Price Increase that exceeds ______ percent (___%) of the Contractor’s price for Eligible Materials as quoted or included in Exhibit XXX at the time of the execution of the Agreement. As a condition precedent to any adjustment of the Contract Sum due to a Significant Price Increase, the Contractor shall provide Owner with ______________ (supporting document requirements).

In addition, if prices decrease from what was in the Contractor’s original estimate, the Owner shall/shall not be entitled to a deduct if there is a decrease in the price.

SLIDE DOES NOT PROVIDE NOR IS IT INTENDED TO PROVIDE LEGAL ADVICE.
Sample Template – Discussion

- Group discussion about provisions

- Questions:
  - What are the owner’s priorities?
  - What are the contractor’s priorities?
  - How did these priorities impact your drafting?
Questions?

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