

COVID-19: its impact on the construction industry

Euan Lloyd - Partner - Construction and Infrastructure
e.lloyd@tamimi.com - Abu Dhabi

Several months have now elapsed since the COVID-19 pandemic took hold across the GCC and the extent of its ongoing consequences are becoming apparent.

This article provides an overview of some of the key legal consequences of the pandemic and how it may shape the future of the construction industry.

Position to date

In our experience, parties have, thus far, largely collaborated in good faith in an effort to address the impact of the pandemic and to find mutually acceptable solutions (which do not necessarily fall within the strict confines of the underlying contract).

In part, this has meant that the deluge of claims and disputes that were anticipated has yet to materialise. However, it would be perhaps naïve to believe that positions will not subsequently harden and that significant disputes arising out of the pandemic will not crystallise. Indeed, the current position may well be the 'lull before the storm', particularly as some agreements that were reached between parties have been short term in nature and were only ever going to be 'quick fixes'. This collaboration was, in certain circumstances, predicated on the assumption that the impact of the pandemic would be short-term and that the consequences could be addressed relatively informally. While this approach has been suitable in some instances, other situations have proved (or are proving to be) more contentious. This is particularly the case in respect of larger projects and especially those that have completion dates sometime in the future and involve international and complicated supply chains. Such projects are more likely to become adversarial with parties scrutinising their legal entitlements and this may well pave the way for subsequent litigation. We therefore briefly set out below some of the key contractual and legal issues that are likely to be pivotal in such issues

Common contractual issues

As with any other legal issue, the impact of COVID-19 has to be carefully assessed on a case by case basis, especially by reference to the underlying contract and the relevant governing law. Although some parties have looked at the impact of COVID-19 from a force majeure perspective, this has not always been the correct characterisation of the situation and can be a 'red-herring'. This is because force majeure clauses usually operate on the basis that performance has become impossible (or performance has otherwise been prevented). In our experience, impossibility (or prevention) is a very high threshold to satisfy and is therefore typically contested, sometimes fiercely.

Indeed, we recently encountered the extreme proposition that illegality does not constitute impossibility as the obligor was still physically able to perform the obligation in question (although such performance may result in a sanction being imposed). We do not consider this position to be credible but it nevertheless illustrates the difficulties that can be encountered by a party seeking to rely on force majeure. In any

event, COVID-19 (and its consequences) have tended to make performance more difficult (or expensive), but not impossible as, for example, work-around solutions (which complement the pervasive obligation to mitigate) can often be deployed. For example, design work could usually be performed remotely when offices were locked-down while construction activities at site were typically permitted to proceed (although subject to restrictions) throughout lock-downs.

Another issue is that the force majeure clause may be limited to the country in which the project is physically located. The prevalence of 'back to back' drafting in subcontracts may mean that subcontractors and members of the supply chain may be unavailable to avail themselves of relief in respect of force majeure if their obligations are performed offshore while issues regarding foreseeability are likely to create significant hurdles in respect of contracts executed after the onset of the pandemic. Accordingly, parties may be well advised to look to other avenues for relief while, even if force majeure is a viable option, other approaches may provide more generous compensation regimes.

Using the FIDIC 1999 Red Book as an example, a contractor is usually entitled to an extension of time if the consequences of the pandemic caused unforeseeable shortages in labour and/or materials, or caused unforeseeable delays in the authority approval process (provided that the contractor diligently followed all applicable processes).

Further relief (in the form of both an extension of time and costs) may also be available on account of changes in laws as well as the introduction of new laws implemented to address the impact and to contain the pandemic (such as in respect of social distancing in workers' accommodation and transport to and from site). It may also be possible for the contract price to be adjusted to reflect any rise or fall in labour or materials (although this provision is frequently deleted from executed forms of contract).

As a generic point which applies to all claims, care must be taken to ensure that the relevant claims procedures are strictly adhered to, particularly as time-bars may apply if claims are made outside of the relevant notice periods.

Common issues at law

If the contract does not address the consequences of COVID-19 (or, alternatively, if the contractual position is unhelpful for a particular party), relief may be available under the relevant applicable law. Using Qatar as an example, Article 187 of the Qatari Civil Code states that a contract is "*automatically annulled*" if performance "*becomes impossible for some external reason in which the debtor played no part*" (although the contract will remain in place in respect of any aspect of the contract that remains capable of being performed).

As noted above, impossibility may be inapplicable and, in this situation, Article 171(2) of the Qatari Civil Code may become relevant.

This is a mandatory provision of law that potentially provides relief to the obligor "*if general exceptional events occur that it was not possible to anticipate, and the consequence of their occurrence is that execution of the contractual obligation, even if it does not become impossible, yet becomes burdensome to the debtor, such that it threatens him with massive loss*". In this situation, the judge (or arbitrator) has the discretion to adjust the obligations of the parties so that the serious consequences of the "*exceptional*" and unanticipated event can be rebalanced to prevent the obligor from suffering "*massive loss*", which is generally considered in the context of the relative values under the underlying contract. The party seeking to have the contractual obligation realigned has the evidential burden of demonstrating that the mutually agreed contractual provision should be readjusted.

Traditionally, this is an onerous burden to discharge, particularly as this is contrary to the overarching

principle of freedom of contract while construction contracts are frequently concluded by two experienced commercial entities. However, we consider that decisions makers may be more inclined to consider applications made under Article 171(2) of the Qatari Civil Code in the context of the COVID-19 pandemic. The Civil Codes of other jurisdictions across the GCC (including the UAE and Kuwait) contain similar provisions to the foregoing.

General consequences of COVID-19

Obtaining relief and enforcing rights under existing construction contracts obviously only constitutes one aspect of the impact the pandemic. A further and more profound impact is that economies across the globe have inevitably contracted and that has resulted in fewer projects being procured (as well as other projects being mothballed). This has inevitably meant that competition has significantly increased in respect of the projects that are being let, although we do expect to see an uptick in infrastructure and industrial projects. This, in turn, has often resulted in both contractual terms being made more 'employer friendly' and for contract prices being reduced (meaning that the more onerous risk profile is not priced). Such reductions and more onerous terms are then almost invariably imposed on the supply chain. It is becoming increasingly apparent that the COVID-19 pandemic will not be resolved in the near future and, accordingly, it follows that the construction market will remain competitive for the foreseeable future.

Given downward pressure on contract prices, it will be incumbent on participants in the industry to increase and improve internal efficiencies. One way of achieving this is to look towards embracing new technologies. However, this will inevitably result in significant upfront expenditure and it is unclear how many contractors will have the appetite to incur such costs when liquidity and cashflow can be problematic. A further consequence of a contracting construction market is that liquidity issues invariably increase, while certain projects may become unviable in the current circumstances and are therefore indefinitely 'mothballed'. This often paves the way for a more contentious environment in respect of which parties seek to recover and claw back outstanding amounts, some of which may have been outstanding for a significant period of time.

Although (as with the consequences of COVID-19) we are aware of parties reaching amicable settlements in this regard, this is not always possible and parties therefore need to carefully consider how best to enforce their rights. This can be problematic if the underlying contract prescribes that disputes are to be determined by arbitration but the amount at stake (although significant) may not justify the costs that will necessarily be incurred by arbitration. In our experience, this is a common problem. While there are ways to potentially resolve issues of this nature (in respect of which we frequently advise), there is no substitute for the underlying contract to provide a clear mechanism for the expeditious, proportionate and cost effective resolution of disputes.

As a general consequence of the pandemic, we expect that parties will, going forward, carefully consider and negotiate the dispute resolution mechanism (i.e. by introducing different mechanisms dependent on the amount of the value of the claim) to ensure that there is certainty as well as the cost effective enforcement of rights in respect of key issues, including certification and payment.

In closing, COVID-19 has undoubtedly impacted on the construction market and its consequences will be felt for some time to come.

However, confidence is slowly starting to return to the sector and, in this regard, we expect parties to pay significant attention to and to seek to negotiate key risk provisions under their contracts.

For further information please contact [Euan Lloyd \(e.lloyd@tamimi.com\)](mailto:e.lloyd@tamimi.com).