



Dear Clients and Colleagues,

Every day, the construction attorneys at Cohen Seglias are approached by clients as to how to address the current crisis due to the significant fluctuation in pricing in construction materials, equipment, and energy. Whether the product in question is steel, copper, glass or lumber, we have seen prices rise since the re-opening of the economy with some commodities hitting a 100% price increase according to some indices. Who is responsible for the burden of the price increases? Unfortunately, like with COVID-19, owners, construction managers, contractors, and subcontractors are all arriving at different answers.

The [Construction Contracts & Risk Management Group](#) at Cohen Seglias has prepared sample notice letters for use on jobs where construction has or is about to resume under pre-existing contracts. We are also providing you with language to add to your change orders and monthly releases. Also, we have included sample language to place in your contracts and proposals to help protect you in the event of a future price escalation. These are extremely difficult clauses to negotiate.

The claims arising out of contracts with a no escalation clause are even harder to prosecute. It is therefore our suggestion that the parties to any construction contract discuss the process and proofs needed to calmly deal with this situation, which is outside of the control of all of the parties. These are unusual times, and they call for out-of-the-box thinking. Even though there may be a right by contract to refuse an escalation change order, an owner must recognize that a contractor defaulting due to a bankrupt subcontractor is highly unlikely to complete a project on time. Instead, we hope that a little sharing of the risk now will save all parties a lot of unnecessary losses and attorney's fees later.

Understand that these forms may need to be revised to fit your particular circumstances. The attorneys of Cohen Seglias stand ready to provide you with assistance, when needed. Please do not hesitate to contact us.

Stay Safe,



**JOHN A. GREENHALL**

Partner

jgreenhall@cohenseglias.com  
267.238.4704



**JONATHAN A. CASS**

Partner

jcass@cohenseglias.com  
267.238.4736



**LISA M. WAMPLER**

Partner

lwampler@cohenseglias.com  
412.227.5948

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As you are aware, in 2021, the construction industry has been and will continue to face unprecedented escalation in material pricing as the world begins the rebound from COVID-19. Whether the cause is tariffs, supply shortages, weather, the blockage of the Suez Canal or other world events isn't relevant. What is relevant is that all of the parties to a construction contract must work together to face these staggering increases. For example, S&P Global Platts is forecasting copper prices to increase over 17% above what was originally forecast for 2021. Steel prices at mills in the United States are up 60% to 100% in the last 6 months, affecting the cost of structural steel, steel joists, reinforcing steel, metal deck, stairs and rails, metal panels, metal ceilings, wall studs, door frames, canopies, steel duct, steel pipe and conduit, pumps, cabinets and furniture. Similarly, according to RS Means, from the last quarter in 2020 to the end of the first quarter in 2021, lumber costs are up 32%, brick costs are up 10%, and insulating glass costs are up 12%. We could continue to list types of material and the impact that rising fuel costs, labor shortages and the lack of raw materials are having on their price, but we believe that all of us need a solution and not more facts and figures.

The purpose of this letter is to determine how we can work together to overcome these escalation issues, bring in our present project on time and avoid defaults and/or schedule delays due to our subcontractors' or suppliers' inability to obtain the needed materials to perform their work without bankrupting us or their companies. As with COVID-19, we need to find the middle ground and share the burden of these potential impacts.

In that vein, we would like to suggest an open book approach to material purchases. Specifically, we will share with the Owner our estimated costs for the relevant materials that are having the most impact on our ability to work. We will then track those costs through agreed to timely and credible, third-party price indices such as RS Means, Steel Market Update and the like. Our intention is to keep you fully apprised of the changes in the market so that you will be fully informed. We can meet on a regular basis with the idea that if the pricing cannot be overcome through value engineering, substitutions or early purchasing/warehousing, we can agree to change orders to share the burden of the escalation.

These change orders will never include overhead or profit mark-ups on the increases from either us or our subcontractors. In addition, since we must consider some risk of the escalation on our part, we suggest that the first \_\_\_\_\_% of any increase be borne completely by us. Any increase above that will be [[the responsibility of the Owner] or [shared \_\_\_\_\_% Owner and \_\_\_\_\_% Contractor]]. To be fair, if prices decrease from what was in our original estimate, we would want the Owner to be able to benefit from that in the same way.

We are happy to schedule the first escalation meeting as soon as possible and ask for days and times in the next 7 days to schedule it. We recognize that no owner wants to see a higher invoice, but the alternative of a default or a delayed project due to the whims of the material market is a real one. The entire team of the owner, design professionals, contractor and subcontractors must work together to eliminate these unpleasant outcomes.

Thank you.

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We recognize that the contract has a “no escalation” clause, but the amount of escalation presently facing the industry is staggering. Clearly, this is a “force majeure” rendering the project impossible to perform under the present [Contract Sum/GMP]. The purpose of this letter is to determine how we can work together to overcome these escalation issues, bring in our present project on time and avoid defaults and/or schedule delays due to our subcontractors' or suppliers' inability to obtain the needed materials to perform their work without bankrupting us or their companies. As with COVID, we need to find the middle ground and share the burden of these potential impacts.

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These change orders will never include overhead or profit mark-ups on the increases from either us or our subcontractors. In addition, since we must consider some risk of the escalation on our part, we suggest that the first \_\_\_\_\_% of any increase be borne completely by us. Any increase above that will be [[the responsibility of the Owner] or [shared \_\_\_\_\_% Owner and \_\_\_\_\_% Contractor]]. To be fair, if prices decrease from what was in our original estimate, we would want the Owner to be able to benefit from that in the same way.

We are happy to schedule the first escalation meeting as soon as possible and ask for days and times in the next 7 days to schedule it. We recognize that no owner wants to see a higher invoice, but the alternative of a default or a delayed project due to the whims of the material market is a real one. The entire team of the owner, design professionals, contractor and subcontractors must work together to eliminate these unpleasant outcomes.

Thank you.

# ESCALATION LETTER TO OWNER WHEN CONTRACT HAS AN ESCALATION CLAUSE



As you are aware, in 2021, the construction industry has been and will continue to face unprecedented escalation in material pricing as the world begins the rebound from COVID-19. Whether the cause is tariffs, supply shortages, weather, the blockage of the Suez Canal or other world events isn't relevant. What is relevant is that all of the parties to a construction contract must work together to face these staggering increases. For example, S&P Global Platts is forecasting copper prices to increase over 17% above what was originally forecast for 2021. Steel prices at mills in the United States are up 60% to 100% in the last 6 months, affecting the cost of structural steel, steel joists, reinforcing steel, metal deck, stairs and rails, metal panels, metal ceilings, wall studs, door frames, canopies, steel duct, steel pipe and conduit, pumps, cabinets and furniture. Similarly, according to RS Means, from the last quarter in 2020 to the end of the first quarter in 2021, lumber costs are up 32%, brick costs are up 10%, and insulating glass costs are up 12%. We could continue to list types of material and the impact that rising fuel costs, labor shortages and the lack of raw materials are having on their price, but we believe that all of us need a solution and not more facts and figures.

The purpose of this letter is to put you on notice that the escalation has gotten so bad that we have no choice but to trigger our rights under Section \_\_\_\_ of our agreement. This section provides:

In undertaking that analysis, we have determined that the following materials have been significantly impacted by the escalation:

Material	Quantity	Price from Estimate	Unit Price	Present Market Price			Average or Industry Index	Quantity Not Yet Purchased	Escalation
				Supplier 1	Supplier 2	Supplier 3			

As such, we are requesting a meeting to discuss potential ways to overcome the impact of this pricing through value engineering, substitutions or early purchasing/warehousing. After such a meeting, we can discuss the actual cost impact of this escalation and the timing of a change order.

We are happy to schedule the escalation meeting as soon as possible and ask for days and times in the next 7 days to schedule it. We recognize that no owner wants to see a higher invoice, but the market forces have been overwhelming. The entire team of the owner, design professionals, contractor and subcontractors must work together to eliminate these unpleasant outcomes.

Thank you.

## VERSION 1 (SIMPLE):

**§ 11.5.2 Escalation Clause.** In the event of significant delay or price increase of material, equipment, or energy occurring during the performance of the contract through no fault of the Construction Manager, the Contract Sum, time of completion or contract requirements shall be equitably adjusted by Change Order in accordance with the procedures of the Contract Documents. A change in price of an item of material, equipment, or energy will be considered significant when the price of an item increases \_\_\_% percent between the date of this Contract and the date of installation.

## VERSION 2 (COMPLICATED):

### §4.7 Asphalt Pricing

**§4.7.1** As the Contract Sum includes a price for asphalt based upon the Asphalt Index price of (**\$\_\_\_\_.00 per ton**) (the “Asphalt Index price” or “IB”). Both Owner and Contractor recognize that the price of asphalt may fluctuate between the time of execution of this agreement and the actual application of the asphalt on the projected. The Asphalt Index at the time of placement, IP, will be based upon the Asphalt Index in place at the time the material is placed. The Asphalt Index shall be in accordance with the Pennsylvania Department of Transportation Asphalt-Diesel Price Index.

**§4.7.2 The Price Adjustment Criteria and Conditions.** The following criteria and conditions will be considered in determining a price adjustment for bituminous materials:

1. No Price Adjustment. When the ratio IP/IB creates a price differential of less than \$1000, no price adjustment will be made for any bituminous material placed during the relevant month.
2. Price Rebate. When the ratio IP./IB is calculated to be greater than \$1000 to the negative, the Owner will receive an automatic price rebate determined in accordance with the following formula:

$$P.R. = (IP/IB) (Q) (IB)$$

Where:

P.R. = Price Rebate

IP = Asphalt Index for the last Wednesday of the month preceding the month in which the material is placed (One Month Price Adjustment Period).

IB = Asphalt Index in the Contract Sum.

Q = Quantity of Asphalt placed.

3. Price Increase. When the ratio IP/IB is calculate to be greater than \$1000 to the positive, the Contractor will receive a price increase determined in accordance with the following formula:

$$P.I. = (IP/IB) (Q) (IB)$$

Where:

P.I. = Price Increase

Q = Quantity of Asphalt Placed

IB = Asphalt Index in Contract Sum.

**§4.7.3 Asphalt Index Increase.** Should the Asphalt Index at time of placement, IP, indicate an increase of 50% or more over the Asphalt Index in the Contract Sum, IB, the Contractor should not furnish Asphalt for the project without prior written approval of the Owner.

§4.7.4 The price adjustment will be paid, or rebated, on a monthly basis with the normal Payment Application process. Price adjustment amounting to less than \$1000 will be disregarded.

§4.7.5 The Owner reserves the right to inspect the records of the Contractor and its Subcontractors and material suppliers to ascertain actual pricing and cost information for asphalt incorporated in the Work.

## VERSION 3 (PRO-CONTRACTOR):

**Escalation Clause.** The Guaranteed Maximum Price has been calculated based on the current prices for building materials. However, the market for some of the building materials that are specified in the Contract Documents (including but not limited to steel and lumber) is volatile, and sudden price increases may occur. Contractor agrees to use its best efforts to obtain advantageous prices from subcontractors and material suppliers. In the event of price increases of materials, equipment or energy occurring during the performance of the Contract through no fault of the Contractor, Contractor will provide written notice to Owner stating the increased cost, the building materials, equipment or energy at issue, and the source of supply, supported by price quotations, invoices or bills of sale. If Owner directs Contractor to proceed with the purchase at the increased cost, the Guaranteed Maximum Price shall be equitably adjusted by Change Order and Owner agrees to pay that cost increase to Contractor. If Owner directs Contractor not to purchase the materials, equipment or energy at the increased cost, or in the event that shortages prevent or delay the supply of necessary building materials, the Contract Time and Contract Sum shall be equitably adjusted to account for the resultant impact to the Project schedule.

## VERSION 4 (PRO-OWNER BUT ALLOWS FOR ESCALATION):

**Escalation/De-escalation Clause.** In the event of a significant price increase of material occurring during the performance of the contract through no fault of the Contractor, the Contract Sum shall be equitably adjusted by Change Order in accordance with the procedures of the Contract Documents as well as those set forth herein. A change in price of an item of material will be considered significant when the price of an item increases or decreases by 20% percent between the date of this Contract and the date of installation.

In order to receive an escalation change order, Contractor shall share with the Owner, in writing, prior to the time of execution of this Agreement, its estimated costs for the relevant materials that it believes may be subject to potential escalation (the "Escalation List"). The Escalation List shall be made an exhibit to this Agreement. Prior to purchasing any of the listed materials, the Contractor must provide the Owner with three (3) timely and credible proposals from suppliers as well as a third-party price index such as RS Means, Steel Market Update or the like to confirm the credibility of the proposals. If the pricing escalation cannot be overcome through value engineering, substitutions or early purchasing/warehousing, the parties may enter into a change order in the amount of the lowest proposal or price index amount. These change orders shall not include overhead or profit mark-ups on the increases from either the Contractor or its Subcontractors. Failure to include a material in the initial Escalation List shall be considered a waiver of the right to seek escalation for such materials without the Owner's consent which may be withheld in the Owner's sole discretion.

In addition, if prices decrease from what was in the Contractor's original estimate, the Owner shall be entitled to a deduct if there is a significant decrease in the price.



## VERSION 5 (SHARING OF RISK):

**§ 6.2.3 Risk of Escalation/Unforeseen Conditions Clause.** In the event of 1) significant delay or price increase of material, equipment, or energy occurring during the performance of the contract through no fault of the Construction Manager or 2) the discovery of concealed or unknown conditions as defined in Section 3.7.4 of the General Conditions, the Contract Sum shall be equitably adjusted by Change Order in accordance with the procedures of the Contract Documents and the below sharing of Costs:

1. The Costs associated with either escalation or unforeseen conditions shall first be paid through use of the Buy-out Savings as defined in Section 6.1.7.4 of this Agreement;
2. To the extent that the Buy-out Savings are insufficient to cover the Costs associated with either escalation or unforeseen conditions, the Owner shall issue a Change Order calculated in the following manner:
  - i. The first 7.5% of the increased Costs associated with either escalation or unforeseen conditions shall be included in the Change Order price;
  - ii. The second 7.5% of the increased Costs associated with either escalation or unforeseen conditions shall be borne by the Construction Manager and shall not be included in the Change Order; and
  - iii. The remaining amount of the increased Costs associated with either escalation or unforeseen conditions shall be evenly split so that half of the Cost of the Work above the 15% in i and ii above shall be included in the Change Order Price.
3. The Construction Manager shall not be entitled to its Contractor Fee on any increased Costs associated with either escalation or unforeseen conditions.

By way of example, if, after following the Change Order procedure set forth in this Agreement, there is an increased Cost of \$150,000 associated with either escalation or unforeseen conditions and there is \$50,000 left in the Buy-out Savings, the Owner shall issue a Change Order for \$50,000 (\$150,000 less \$50,000 (the Buy-out Savings) less \$7500 (the Construction Manager's share in subsection ii) less \$42,500 (the Construction Manager's share of the overage in subsection iii)).

# LANGUAGE FOR CHANGE ORDERS

This Change Order specifically excludes all escalation of prices of material, equipment or energy experienced by [Contractor/Subcontractor] from the date of this change order until the execution of the needed material, equipment or energy associated with this particular increased scope of Work.

# LANGUAGE FOR MONTHLY RELEASES IN EXCHANGE FOR PAYMENT



By executing this Release, [Contractor/Subcontractor] is in no way releasing, and is expressly preserving, its rights to any additional costs submitted in pending and/or disputed change order requests as well as to its rights to further escalation of the prices of material, equipment or energy which [Contractor/Subcontractor] has experienced to date and will experience in the future.

NOTICE: THIS PROPOSAL IS CONTINGENT ON A LACK OF FUTURE IMPACT BY THE ON GOING ESCALATION OF THE PRICES OF MATERIAL, EQUIPMENT AND/OR ENERGY. Given that the construction industry has been and will continue to face unprecedented escalation in material pricing as the world begins the rebound from COVID-19, and the possibility that the pricing of materials, equipment and energy continues to escalate, [Contractor/Subcontractor] cannot anticipate the impact of the current increases in pricing. As such, [Contractor/Subcontractor] will use its best efforts to purchase the materials, equipment and energy in such a manner as to limit the impact of the escalation. However, [Contractor/Subcontractor] reserves its right to seek an equitable change order if [Contractor/Subcontractor] or its subcontractors and suppliers are unable to supply these products at the same or similar costs as carried in their estimates. To the extent that the project is subject to provable material escalation in pricing, we reserve our right to seek any such additional costs.

By **John A. Greenhall**, **Anthony M. Bottenfield**

At this point, avoiding the cliché is, well, unavoidable. We are now past the one-year mark of the COVID-19 pandemic and much has changed. You don't need a construction attorney to tell you so. While things have changed, we all must move forward in the "new normal," including those in construction.



As we move into the second quarter of 2021, it's an opportune time to look at where we have been and where we are going. To do so, you must review your contracts and construction relationships both retrospectively and prospectively.

At the onset of the pandemic in March 2020, construction largely came grinding to a halt. Many companies turned to their contracts to see what relief, if any, they had. Construction shutdowns meant lost time and money. One provision that was helpful is known as a force majeure clause, which provides a party relief when the unforeseen—such as a global pandemic—occurs.

Now, it's difficult to argue that the COVID-19 pandemic is unforeseen going forward. So, what can construction companies do to still protect themselves?

First, companies should review their contracts to ensure that they have accounted for the ongoing pandemic. Provisions related to delay, stoppages, and safety are obvious choices. However, companies should also analyze what their contracts say, if anything, about changes in the current situation that could occur due to future strains, variants, or other complications. Should future, widespread outbreaks occur from COVID-19, or other infectious diseases, you should make sure that you are protected. We suggest revising all force majeure clauses to specifically reference pandemics, epidemics, and related governmental orders to remove all question that the repercussions of future strains are not foreseeable.

Additionally, companies should pay special attention to provisions that address material escalation, material delays, or the inability to procure certain materials. As shelved projects take off alongside ongoing work, material availability can be scarce, so it is important to anticipate the impacts that these complications can have in finishing your work or the overall project's completion.

Furthermore, many may face a backlog of work as a result of shutdowns or delayed starts. Once-promised start and completion dates may not be possible. Be mindful of the time and monetary impacts and protect yourself in these instances too.

While we cannot help but reflect on the past year, it's also important to look forward and be prepared by using what we have learned from the difficulties that we have overcome.

As always, if you have specific questions about your contracts or projects, do not hesitate to reach out.



**JOHN A. GREENHALL**  
Partner  
jgreenhall@cohenseglias.com  
267.238.4704



**ANTHONY M. BOTTENFIELD**  
Associate  
abottenfield@cohenseglias.com  
267.238.4714