



A COVID-19 LEGAL TOOLKIT FOR THE CONSTRUCTION INDUSTRY: TERMINATION AND SUSPENSION

For the past 4–5 months, COVID-19 has forced construction sites around the globe to close or comply with new and changing guidelines as governments announced lockdowns and other measures to slow the spread of the virus.

Even in jurisdictions where sites were not required to shut down, other consequences of the pandemic such as labour and material shortages have left contractors and employers with little practical choice other than to close sites and suspend work. In the short term, such closures will obviously have caused serious delays and cash flow difficulties. But where sites have remained closed for lengthy periods (or where there is a possibility of further lockdowns) another larger issue looms – termination.

This briefing considers the risk of termination in two scenarios following a prolonged suspension. First, where a site has been forced to close as a matter of law and, second, where a site was closed because of other factors (rather than a government direction for the site to shut). As with our earlier COVID-19 briefings, we consider the position by reference to three commonly used standard form contracts: FIDIC 1999, NEC4 and the JCT DB 2016.

This article considers the position where both contracting parties remain solvent. It does not therefore discuss the Corporate Insolvency and Governance Act 2020, which altered the UK's insolvency regime in a number of important respects to provide parties with greater flexibility to continue trading in the face of COVID-19. Notably, the act permanently banned the exercise of certain termination clauses in contracts for the supply of goods and services (e.g. construction contracts). This means that a company supplying goods or services cannot rely on a contractual right to terminate or suspend that is triggered by the company receiving the goods or services becoming subject to a "relevant insolvency procedure" as defined in the legislation. In practice, we anticipate that this is more likely to impact suppliers and subcontractors than main contractors.

Governments have required Work to stop and Sites to close

Across the globe there has been a mixed response from governments concerning whether construction sites should stay open during the pandemic. For example, in England, there has been guidance that construction sites can stay open provided Safe Operating Procedures (SOPs) are followed, which require social distancing to be maintained. In contrast, in neighbouring Scotland, all "non-essential" construction work was required to stop for a period. Likewise, Singapore is another jurisdiction that has closed down all construction for a specified period of time.

Where sites are required to close, the parties seemingly have little choice but to suspend the works.

Table 1 - Standard form provisions allowing termination following prolonged suspension due to neutral event.

<p>FIDIC Yellow Book 1999 Clause 19.6</p>	<p>Clause 19 provides that "if the execution of substantially all the Works" is prevented due to a Force Majeure for:</p> <ul style="list-style-type: none"> • a continuous period of 84 days; or • multiple periods which total more than 140 days, <p>then either party may terminate the contract.</p>
<p>NEC 4 Clause 91.6</p>	<p>Clause 91.6 provides that either party may terminate the contract, if the Project Manager has stopped "any substantial work or all work", absent any fault from either party, for a period of 13 weeks.</p>
<p>JCT Design & Build 2016 Clause 8.11</p>	<p>Clause 8.11 provides that if "the carrying out of the whole or substantially the whole of the uncompleted works is suspended" for the relevant period stated in the Contract Particulars due to Force Majeure, then either party may terminate the contract.</p> <p>The parties are to choose the relevant period of suspension before the right to terminate arises. If no such choice is made, the default position in the un-amended Contract Particulars is a period of 2 months.</p>

Time periods giving rise to a termination right

Each of FIDIC, NEC4 and JCT DB 2016 include provisions that allow either party to terminate the contract where the works are suspended for a period of time due to a neutral event, such as force majeure, which would arguably include forced suspensions due to COVID-19. Table 1 sets out these provisions.

In regions where construction operations have been shut down, it is likely that the time periods in Table 1 will have been met or even exceeded. This is particularly the case given the rising threat of a second wave of lockdowns due to new outbreaks of the virus. We are seeing an increasing number of regions impose second lockdowns including, at the time of writing, Melbourne and parts of California and Spain.

Can I terminate following an enforced shutdown due to COVID-19?

If these time periods have been met, a party must still check carefully that a termination right has arisen before taking any action.

FIDIC and JCT specify that the suspension must be due to force majeure. We considered whether COVID-19 was likely to qualify as a force majeure event in our first briefing¹, concluding that under the standard un-amended forms it was likely to be, provided the contract was entered into before the outbreak was reasonably foreseeable. NEC4 requires the works to have been stopped by the Project Manager, absent default by either party.

It is also important to check what qualifies as a suspension of the works. FIDIC and JCT both require suspension of substantially the whole or all of the works. NEC does not draw this distinction instead referring to "substantial work or all work" (Clause 91.6).

The local laws concerning termination should also be checked. For example, in Kuwait, in some circumstances unilateral termination of a contract may not be possible. In Kuwait, even where there exists an express right to terminate under the contract, a notice of termination may not actually be effective unless/ until

Table 2 – Standard form provisions re. termination following contractor’s suspension

<p>FIDIC Yellow Book 1999</p> <p>Clause 15</p>	<p>Clause 15.2 allows the Employer to terminate the Contract if (among other reasons):</p> <ol style="list-style-type: none"> 1. The Contractor abandons the Works or otherwise plainly demonstrates the intention not to continue performance of his obligations under the Contract. 2. Without reasonable excuse, fails to proceed with the Works in accordance with Clause 8. <p>In these circumstances, the Employer may terminate the Contract and expel the Contractor from the Site, on giving the Contractor 14 days’ notice of its intention to do so.</p>
<p>NEC4</p> <p>Clause 91.2 and Clause 91.6 (R18)</p>	<p>Clause 91.2 gives the Client a right to terminate if (among other reasons):</p> <ol style="list-style-type: none"> 1. The Contractor has substantially failed to comply with its obligations. 2. The Project Manager has notified a default that the Contractor has not corrected within four weeks of the date of notification. <p>Clause 91.6 (R18) allows the Client to terminate if works have been suspended for 13 weeks due to the Contractor’s default (see above).</p>
<p>JCT Design & Build 2016</p> <p>Clause 8.4</p>	<p>Clause 8.4.1 allows the Employer to terminate the Contractor’s employment under the Contract if (among other reasons), before practical completion of the Works, the Contractor:</p> <ol style="list-style-type: none"> 1. Without reasonable cause wholly or substantially suspends the carrying out of the Works. 2. Fails to proceed regularly and diligently with the performance of his obligations. <p>Similar to NEC4, the right to terminate is subject to the Employer having notified the Contractor of its default and the Contractor continuing with that default for 14 days from receipt of that notice.</p>

the terminating party has applied to the court for an order for rescission.

It seems reasonably clear that an enforced government shutdown of construction operations for the time-periods described in the contract could allow the parties to terminate. If a party were to exercise this right, generally the payment position is neutral, with sums paid for the completed works and no additional sums due for the balance of the work.

Comment

Termination by its very nature is an option of last resort and even if there has been a prolonged suspension due to COVID-19 it does not necessarily follow that termination is an inevitable consequence. To avoid uncertainty on existing projects, parties should seek to reach an agreement to extend the time periods before a termination right accrues. When drafting future contracts parties may want to look at the time periods before termination may take place, given the possibility of multiple COVID-19 lockdowns.

Governments have allowed work to continue but the Contractor decides to close the Site

Challenges still confront contractors in jurisdictions where the local government has not closed sites to prevent the spread of COVID-19. As noted, England is one example. Similarly, in the UAE and Kuwait, the construction sector received a number of exemptions from lockdown rules to allow operations to continue. However, in those jurisdictions, other measures have been imposed, which may limit productivity. These measures include immigration restrictions, reduced transport capacity and social distancing. The public sector shutdown in Kuwait has also limited capacity to carry out inspections, grant permits and perform related functions. Globally, there has been disruption in supply chains and difficulties in personnel travelling to site locations. Individual contractors may also have taken steps to mitigate the economic impact of COVID-19, such as furloughing staff.

This presents a challenging situation, which is likely to continue until the

pandemic is overcome. Contractors may have to consider pausing or slowing some or all of their works to address the health, economic and other practical challenges posed by COVID-19. This reduction in activity may trigger an employer’s contractual rights to terminate the relevant construction contract. Contractors should consider these contractual risks when evaluating whether to take such steps.

This section discusses some of the contractual provisions that may allow an employer to terminate if a contractor suspends some or all of its activities. The relevant contractual provisions are summarised in Table 2 above.

Generally, when is there a right to terminate following a suspension under the standard forms?

The standard forms present a range of scenarios when a termination right might arise. For brevity, we will consider the broad themes rather than analysing each scenario in detail. Any party considering, or confronting the threat of, termination should carefully consider the precise

wording of the contract, including any amendments, and any relevant provisions of the applicable law.

Broadly, the standard forms permit termination in the event of a suspension of works in two scenarios:

- 1. No intention to perform obligations:** The contractor has:
 - abandoned the works; or
 - plainly demonstrated an intention not to continue to perform its obligations or has substantially failed to comply with its obligations.
- 2. Suspension or delay without reasonable excuse:** The contractor has (a) failed to proceed with the works regularly and diligently and/ or in accordance with its other obligations in the Contract relating to time; or (b) has wholly or substantially suspended the carrying out of its works, in each case without reasonable excuse.

We suggest some factors to consider in relation to each of these broad issues below.

No intention to perform obligations

Usually, it will be clear when a contractor has abandoned the works. Demonstrating an intention not to perform obligations will be more fact sensitive. Clear evidence of the contractor's intention is likely to be required. FIDIC requires the contractor to "*plainly demonstrate*" its intention. NEC4 meanwhile requires a "*substantial failure*". This is particularly important, given the risks to an employer if it terminates the contract when it does not have a right to do so, or without following the proper procedure. In those circumstances, the employer may itself be in breach of contract. In certain jurisdictions (including England), this kind of breach may give the contractor the right to terminate the contract itself and/ or claim damages.

It should be noted that some legal systems (including English Law) do not give contractors a general right to suspend their services (other than for non-payment under the Construction

Act²). Any suspension of works or curtailment of activities must be in accordance with the contract.

Suspension or delay without reasonable excuse

In a scenario where a contractor has suspended its works onsite due to COVID-19, the debate on whether this kind of termination right has been triggered is likely to focus on two points:

1. Whether the works have been 'sufficiently suspended'. For example, JCT requires the works to be "*wholly or substantially*" suspended. Arguably, an employer may not be entitled to terminate if a contractor suspends only a small number of activities. This is likely to be particularly relevant if a contractor continues offsite activities such as design, procurement or offsite manufacture.
2. Whether the contractor's decision to suspend is reasonable.

When considering the reasonableness of any suspension, parties should carefully consider the requirements of any HSE, governmental or similar guidance. However, it may also be relevant to consider other factors, for example:

1. If a significant body of contractors working on similar projects locally are also adopting measures over and above any relevant local guidance, the parties may wish to consider these measures. Any party seeking to rely on such measures will need to demonstrate that it is reasonable to do so.
2. There is arguably scope for debate about the precise meaning and application of relevant guidance. For example, in England, contractors are required to comply with the SOPs issued by the Construction Leadership Council. Version 5 of the SOPs (published on 4 July 2020) requires contractors to maintain two metres social distancing or one metre with risk mitigation where two metres is

not viable. However, if neither of these measures are possible, the SOPs do not automatically prohibit the activity. Instead, contractors: "*should consider whether the activity should continue and, if so, risk assess it...*" It is not immediately clear how a contractor is to determine this. On one view, the focus should be on limiting the scope for transmission of COVID-19 so far as possible. However, a party may seek to argue that these considerations have to be balanced against the impact of any potential mitigations on the project. Suffice to say, a prudent contractor may have to consider other relevant guidance and information to support its approach. Contractors may also need to consider whether it is necessary to explain why any adverse impacts of its actions are justified.

Practical steps when considering a suspension of works

A contractor may adopt various steps to mitigate the risk of its suspension triggering a termination right. The precise steps that a contractor should adopt will depend on the contract terms, the severity of any COVID-19 outbreaks in relevant jurisdictions, the status of the project and any applicable local laws. That said, examples of the practical steps a contractor may wish to consider are likely to include the following:

1. If possible, contractors should avoid unilaterally ceasing work on site. They should engage with the employer to agree a suspension or other practical means of mitigating the risk of COVID-19. This may avoid any disagreement on the approach adopted.
2. The contractor should notify the employer of its intention to suspend. Where possible, the contractor should refer to a contractual provision that gives it the right to suspend, to obtain an extension of time or to adjust the programme. For example, clause 8.4(d) of FIDIC or Clause 60.1(19) of NEC4. As noted above, there may be no general legal right to suspend performance of

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the obligations. The contractor should comply with any other requirements of the contractual provision(s) it relies on, including giving notice of entitlement to an EOT and/ or additional costs.

3. The contractor should provide the employer with reasons for the suspension. It may also be prudent to explain why it has not adopted less disruptive measures. It is likely to be helpful to refer to the specific provisions of any applicable guidance. This may assist in evidencing that there is a reasonable excuse for the suspension.
4. It is likely to be prudent to suspend the works for a specified period of time, which is as short as possible. The position can then be kept under constant review with the suspension extended if required. This may assist in demonstrating the contractor's continuing intention to perform the Works as swiftly as it is safe to do so.
5. So far as possible, contractors should attempt to continue to carry out work that it is reasonably safe to perform. This may include offsite manufacturing, design and procurement. The contractor

should comply with its contractual obligations while performing these activities and keep the employer apprised in writing of its progress. Again, this may assist in demonstrating a contractor's continued intention to comply with the contract and/ or that the contractor has not in fact wholly/ substantially suspended its performance of the works (i.e. that the precise contractual test is not satisfied as a significant element of the works is progressing).

Concluding comments

It may be prudent for contractors to consider pausing or slowing work to reduce transmission of COVID-19. In doing this, contractors should weigh the risk of such actions triggering an employer's right to terminate. If a contractor decides it must suspend some of its activities, there are steps it can take to mitigate the risk of termination. Employers, meanwhile, should ensure that there is an entitlement to terminate and that any contractual procedures are followed carefully. A failure to do so may result in an ineffective termination and/ or a repudiatory breach.

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