



# Construction Contracts Escalation Cause

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Contractors and Subcontractors do not possess a crystal ball! Generally, contracts regarding construction involve the memorialization of what will be performed at some future event and how much it will cost. Contractors and Subcontractors must then manage their labor, material, and overhead costs throughout the project in order to be profitable. In a perfect world, if the costs remain constant throughout the project the contractor will receive the anticipated profit. Unfortunately, especially in the current market environment, this seldom occurs, except for small projects that can be performed in a relatively short time span. So how are Contractors and Subcontractors able to cover the fluctuation of construction costs?

One way is to add an escalation clause to the construction contract. Essentially, the escalation clause provides of a base cost evaluation at the time of contract, but allows for the increase of costs, labor or fuel associated with the project during the course of performance through completion. The escalation clause generally covers the fluctuating, generally increasing, costs of the labor, materials, and fuel through the project conclusion. The content of the clause can be as simple or as complex as required, depending on the size and duration of the project, and include a cost adjustment index or average price in a given geographic area.

An example of a simple adjustment clause might be:

**MATERIAL COST ESCALATION:** If, during the performance of this contract, the cost of materials significantly increases, through no fault of contractor, the price of this contract shall be equitably adjusted by an

amount reasonably necessary to cover any such significant increase in the costs of materials. As used herein, a significant cost increase shall mean any increase in cost of materials exceeding \_\_\_% experienced by contractor from the date of the contract signing. Such increase in material costs shall be documented through quotes, invoices, or receipts. Where the delivery of materials delayed, through no fault of the contractor, as a result of the shortage or unavailability of the materials, contractor shall not be liable for any additional costs or damages associated with such delay(s).

A more complex adjustment clause might reference the cost per unit based upon an identified cost index, or a percentage increase based on the average price at the time of contract in the geographic area where the project is to be performed. The adjustment clause can reference an attachment to the contract where every material and fuel cost is identified and percentage of each to be the subject of an adjustment. The longer the time for the completion of the project and/or the complexity of the project will dictate the content of the adjustment clause.

Understand, the adjustment clause shifts the burden of increasing costs from the Contractor to the client or from the Subcontractor to the general contractor as the circumstances dictate. Just as with any other contract provision, the adjustment clause is negotiable or may be rejected outright. As this clause has legal effect, just as every other clause in a construction contract, it is essential that an attorney draft the clause specific to the project or at the very least review the contract before it is submitted for approval to insure the rights of the Contractor or Subcontractor are protected as much as possible. Managing costs, especially for larger projects, is essential in order to maximize profitability. The escalation clause is one method of achieving the desired result.

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