THE TARIFF QUAGMIRE:
How To Protect Your Subcontract Business From Tariffs; Lessening the Direct and Indirect Risks

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SAUL EWING LLP

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Agenda

I. The Uncertain Tariff Crisis

II. Pre-contract Steps to Lessen Risks from Tariffs

III. Contract Provisions to Avoid Damages from Tariffs

IV. Dealing with the Fallout from Tariffs

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An Introduction to Tariffs and Pre-Contract Risk Avoidance

I. A Brief History and Description

II. Tariffs Currently in Place

III. Assessing the Threat and Providing Notice

IV. Pre-contract Steps to Minimize Risks From Tariffs

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Tariffs | Definition and History

Taxes imposed on products or services imported from another country.

- Typically charged as a percentage of the value of the imported goods, and the importer is responsible for paying the tariff to the government.
- Under Article I, Section 8 of the United States Constitution, Congress has the power to "lay and collect Taxes, Duties, Imposts and Excises, …"
- This clause grants Congress the authority to impose tariffs on goods and services imported into the United States for the purpose of regulating commerce, for instance to protect domestic manufacturers, or for the purpose of raising money, like a tax.

Tariffs | History

- In the early years of the Republic, tariffs were used primarily to raise revenue, then income taxes were enacted in 1913.
- Tariff Act of 1789, intended primarily to raise revenue for the government.
- Today, Tariffs are a means of protecting domestic industries from foreign competition.
- Smoot-Hawley Tariff Act of 1930 imposed significant tariffs during the Great Depression on over 20,000 types of imported goods.
  - Intent was to protect American businesses and farmers.
  - Most historians credit it with worsening the global economy, prompting retaliatory tariffs from many other countries, and worsening and prolonging the Great Depression.

Tariffs | History

- Trade Act of 1974, Congress gave the President the power to unilaterally negotiate trade agreements, which included the ability to impose tariffs.
  - Granted Presidents authority to negotiate trade agreements.
  - Purpose was to encourage open and fair world economic system to stimulate fair and free competition between the United States and the rest of the world.

Tariffs | Use in Modern Times

- In 2003, President George W. Bush imposed tariffs of 8% - 30% on certain steel products, but those were lifted the same year, after an adverse ruling from the World Trade Organization.

- In 2018, President Donald Trump imposed a 25% tariff on steel and a 10% tariff on aluminum imports. The following year, the tariffs were lifted for Mexico and Canada when the North American Free Trade Agreement (NAFTA) was replaced by a new trade agreement, the United States-Mexico-Canada Agreement (USMCA). The steel and aluminum tariffs were lifted in 2021 for the European Union by the Biden administration.

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Tariffs | “A Beautiful Word”

- In 2025, the second Trump administration has made sweeping use of its tariff authority.
  - Tariffs were imposed and suspended several times earlier this year, making it difficult to know which tariffs are in effect, as of what date, for which goods, produced in which country.
- This raises problems with allocating responsibilities for tariffs in a contract, and if a dispute occurs, unclear which party has responsibility in a subsequent dispute.
  - What happens to goods in transit?
  - What tariffs will be imposed on goods manufactured, assembled or partially made in more than one country?

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Tariffs Currently in Place

Some tariffs are still in place from the first Trump term. In addition:

- January
  - Announced plan to impose 25% tariffs on Canadian and Mexican imports.
- February
  - Implemented 25% tariffs on steel and aluminum imports from Canada and Mexico and 10% tariffs on imports from China, then suspended for Canada and Mexico.
  - Lumber
- "Liberation Day" - April 2, 2025
  - 100%+ China Tariffs

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Identify Supply Chain Vulnerabilities

- Critical Materials for upcoming projects, how are they sourced?
- Are they sourced from countries impacted by trade restrictions or tariffs?
- How likely is a material price increase and delay?
- How reliable are current suppliers? Relationship?
- Possibility of locking in price?
- Are there domestic alternatives or alternatives from lower tariff countries?
- Are there alternative materials with lower tariffs?
- Modify supply chain, such as assembling off-site, i.e., pre-fab.

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Tariffs | Pre-Contract Steps to Minimize Risks

- Once you identify risk, what can you do?
  - Notify customer early so they can raise issue with owner and owner can raise with lender.
  - Many owners are willing to assume some risk, but only if they can address with others and plan for it.
  - Obviously, include risk in your price.
  - Discuss with customer the subcontract provisions that Matt will recommend.

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Tariffs | Pre-Contract Steps to Minimize Risks

- How best to quantify risk fairly?
  - What is a new tariff and when does impact begin?
  - Need to quantify existing tariffs to support subsequent change
- Ordering materials in advance
- Storing materials off-site, cost and additional freight expense
- Confirmation of commitment to absorb additional costs -- e.g., Letter of Intent (LOI), or Limited Notice to Proceed (LNTP)
- Will customer pay for buying materials in advance?

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Tariffs | Incidental Issues

- If tariffs are "suspended" are they new or existing at time of contract?
- Difficult to identify supply chains
  - Where did materials originate if made in several countries?
  - What tariff applies if finished goods are composed of several materials with differing tariff rates.
  - If we don't know, which tariffs will apply?
- If the material supplier or subcontractor are designated by owner or GC, does that affect responsibility?
- What if government determines after tariffs are paid and allocated that materials are of a different type or were primarily originated in a country with higher tariff than expected?
- When is indemnification from source or customer possible?
  - Tariff increase after sale but before onshore
  - Tariff obligation determined by subsequent audit

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Tariffs vs. Price Gouging

- If Price is increased by domestic supplier, or foreign supplier with lower tariff, based on higher priced component materials?
- If Price is increased by domestic supplier, or foreign supplier, due to shortage of domestically sourced materials, caused indirectly by tariffs?
- If Price is increased by domestic supplier, or foreign supplier, because shortage of materials requires overtime or otherwise causes price increase or production inefficiencies.
  - For example, domestic steel manufacturer raises prices because it utilizes inefficient night shifts, pays more for scarce domestic raw materials, or needs to purchase foreign-made component materials?

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Increased Risk of Nonpayment

- Project failures, price turbulence, and economic uncertainty indirectly due to domestically tariffs
- Obtaining confirmation of financial ability from customer
- Contract provisions - in addition to directly contracting for tariff impacts:
- Lower retainage, advance payments, payments into escrow
- Avoid pay-if-paid provisions
- Mechanics lien rights .. keep watch
- State by state peculiarities, e.g., leasehold interest and notices

Other Government Actions

- Expelling immigrant labor
- Repealing issued permits
- Stock and bond market volatility on financing and project viability
- On April 16th, US Dept of Interior ordered work to stop on a large off shore wind project, the Empire Wind project, saying it had concerns that there had been corners cut to approve the project, though it did not describe any specific issues. Does this represent a change of law? Is it a force majeure event? Depends on what the contract says about such things.

Addressing the Problem

- Which party will pay the tariffs?
- Which party will pay for the indirect consequences, such as mobilization, demobilization, double freight charges, storage costs, and unused materials if projects are suspended or cancelled?
- How is risk of delay and disruption allocated between the parties?
- Can the Supply Agreement or Subcontract prevent or at least reduce risk?
- If the Contract doesn’t provide a cure, what remedies are available to the subcontractor?

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Future Contracts

Managing Risk

How should contractors manage tariff risk, materials availability, and price escalation in future contracts?

NEGOTIATION

Managing Risk

What should parties focus on in negotiations?

Balance

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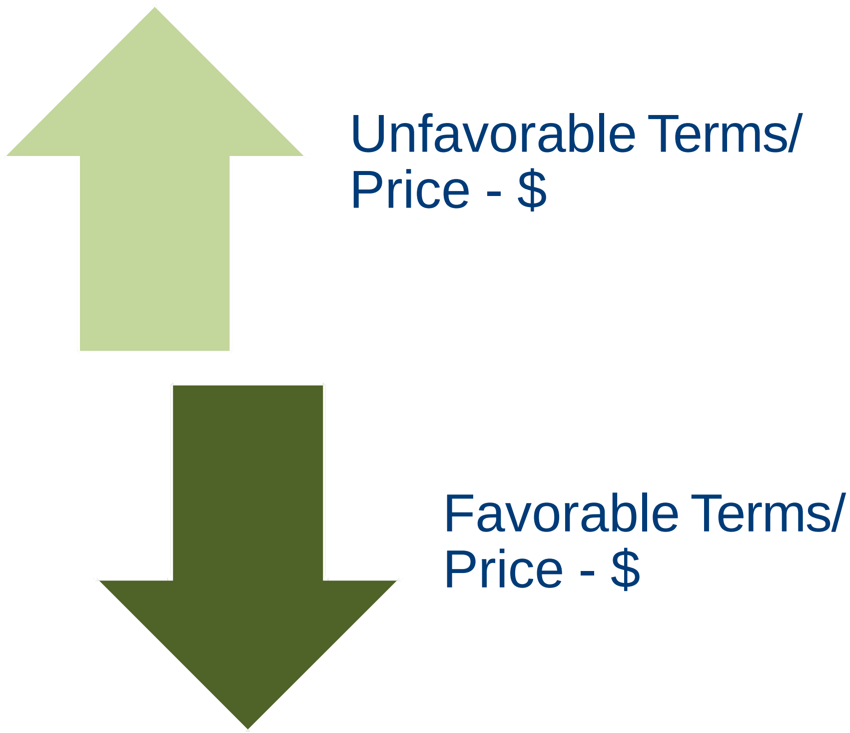
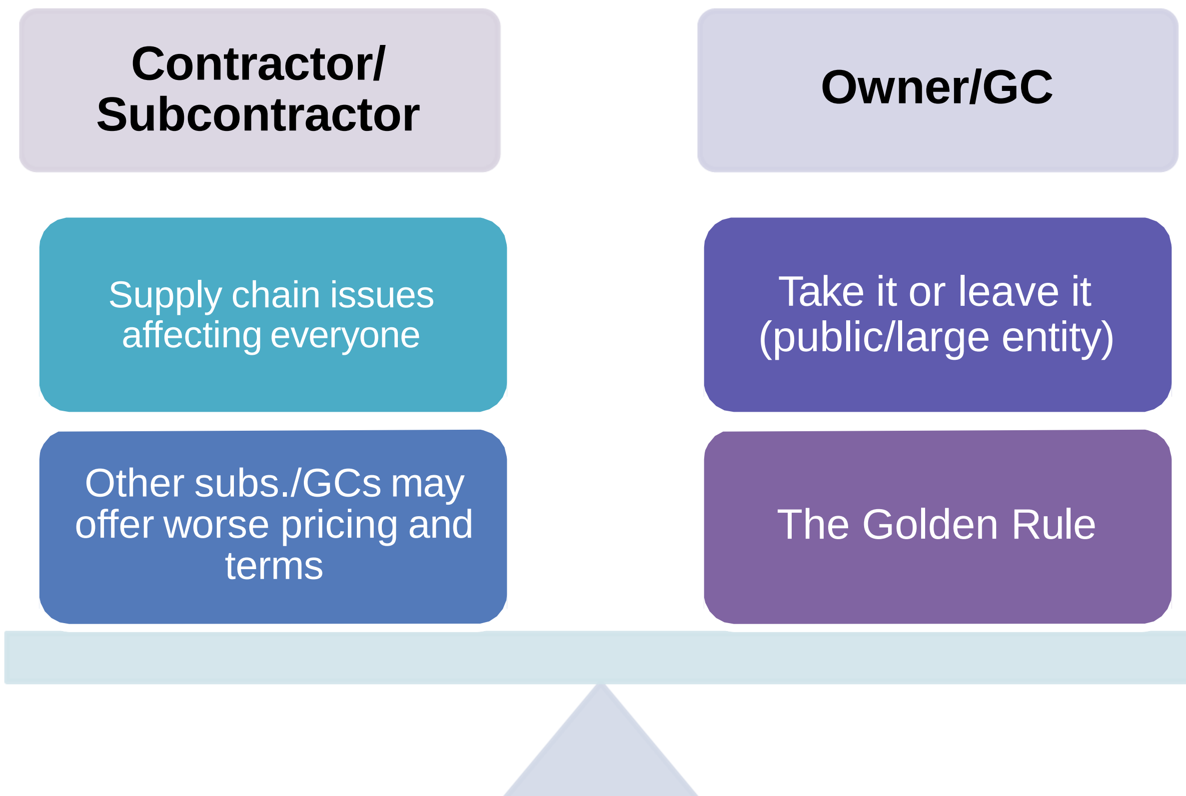
Managing Risk

The Balanced Contract



Managing Risk

The key to any negotiation . . .



Leverage

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Managing Risk

With any negotiation, details matter

Problem	Contract Term	How Achieved	Purpose
Delays from untimely or unavailable materials	Materials Availability/ Excusable Delay Clause	Provision expressly includes materials availability as excusable delay	Protects subcontractor against delays costs and provides compensation for unavoidable delay
Increased cost from price escalation	Materials Pricing/Price Escalation Clause	Contract price is increased where materials pricing at delivery exceeds at-bid price based on agreed-upon threshold or index	Shifts price increase risk from subcontractor to GC if the price exceeds normal business expectations

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Materials Availability Clause

Materials Availability Terms

- Excusable Delay/Force Majeure
- Substitutions
- Line Item for supply chain delays

Materials Availability Terms

Excusable & Compensable Delays, Essential Terms

- Definition of delay/force majeure expressly includes
  - Unexpected long delivery
  - Unavailability of materials
  - Owner/GC delays on submittals or materials selection
- Exception to “No Damages For Delay”
- Need to coordinate with other contract provisions

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Materials Availability Terms

Excusable & Compensable Delays, Essential Terms

- **Sample Contract Language:**
  - If the Subcontractor is delayed at any time in the commencement or progress of the Work by (1) an act or neglect of the Contractor, Owner, or Architect or of an employee of either, including any failure to return submittals or RFIs or perform any contractual obligation timely; (2) by changes ordered in the Work; (3) by labor disputes, fire, **unusual delay in any delivery, including delivery of materials necessary for Subcontractor's work, unreasonable increase in materials costs,** unavoidable casualties, adverse weather conditions documented in accordance with Section 15.1.6.2, or other causes beyond the Subcontractor's control; . . . then the **Contract Sum shall be increased** and the Contract Time shall be extended for such reasonable time as the Architect may determine.

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Materials Availability Terms

Substitutions and Design Changes

- Require Owner to use “best efforts” to mitigate supply chain issues
- Remedial action includes:
  - Accept substitute materials
  - Consider alternative designs
- **Sample Contract Language:**
  - In instances when the Parties determine that there will be delivery delays or [commercially unreasonable ***or*** in excess of __%] increases in costs for necessary project materials, the Contractor/Subcontractor may propose substitutions of materials available for more timely delivery or more reasonable cost, and the Owner agrees to use its best efforts to accept such substitute materials.

Materials Availability Terms

Lead Times

- Need to know lead times before executing
- Provide materials lead times in the agreement's provisions regarding the project schedule
- Include exculpatory language
- **Sample Contract Language:**
  - In preparing the construction schedule, Contractor shall consider and account for all lead times for all materials for Subcontractor's scope of work as timely provided or submitted by Subcontractor to the Contractor, and should the Subcontractor determine the construction schedule does not afford Subcontractor sufficient time to complete its work, then upon the Contractor's failure to adjust the schedule after three days' notice from Subcontractor, the Contract Time shall be extended to the extent Subcontractor's project work was delayed.

Materials Availability Terms

Schedule of Values

- Negotiate allowance for supply-chain related delays
- Include excusable delay language
- Grant subcontractor entitlement to an extension of time and cost
- **Sample Contract Language:**
  - If the Subcontractor is delayed at any time in the commencement or progress of the Work by . . . then the **Contract Sum shall be increased** to the extent of Subcontractor's additional costs from such delay up to the delay allowance amount of $10,000 and the Contract Time shall be extended to the extent Subcontractor's project work was delayed.

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Materials Price Escalation Clause

Multiple Forms

- Triggering mechanism
- Consequences/Results
- Sample terms:
  - Threshold trigger
  - Index trigger
  - Shared cost

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Escalation Clauses

Percentage Trigger – Change Order

- Set percentage price increase triggers remedy
- Remedy depends on COR approval
- **Sample language:**
  - 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 trade contractor, **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 20% percent** between the date of this Contract and the date of installation.

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Escalation Clauses

Increase Trigger – Full Coverage

- Any price increase triggers change
- Guaranteed coverage
- **Sample language:**
  - The contract price for this project has been calculated based upon current material prices. However, the market for materials, **including, but not limited to**, copper and lighting, is considered volatile and a sudden price increase could occur. Contractor agrees to use its best efforts to obtain the lowest possible prices from qualified material suppliers, but should there be an increase in the price of those materials that are purchased after the execution of the contract for use in this project, the owner agrees to pay the contract price increase to contractor. Any claim by contractor for the payment of a contract price increase, as provided above, shall require written notice to the owner from contractor stating the increased cost plus a 10% markup, the material(s) in questions and the source of the supply.

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Escalation Clauses

Index Trigger – Shared Coverage

- Price change triggered by increase based on price index
- Cost-shifting formula allocates costs to Contractor and Subcontractor
- **Sample language:**
  - As the Contract Sum includes a price for electrical metal tubing (EMT) based upon the EMT index price of ($__.00 per ton) (the "EMT Index price"), both Owner and Contractor recognize that the price of EMT may fluctuate between the time of execution of this agreement and the actual installation of the EMT on the project. The EMT Index at the time of installation will be based upon the EMT Index existing at the time the material is installed. The EMT Index shall be in accordance with the **[industry-accepted price index].**

Escalation Clauses

Up or Down Trigger – Change Order

- Increase **OR** decrease triggers change
- Change order according to terms
- **Sample language:**
  - **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%** between the date of this Contract and the date of installation.

Other Strategies

Additional methods to address tariff costs

- Separate tariff allowance
- Dedicated tariff contingency
- Separate tariff line item in Schedule of Values
- Short time periods for accepting proposals
- Early purchase of tariff-threatened products

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Tariff Related Claims

Tariff Claims | Next Steps

So . . .

. . . you have studied the tariff problem . . .

. . . you understand the key contract terms to protect against supply chain delays and price escalations . . .

. . . now – what to do when material delivery delays or price increases occur?

Tariff Claims | Scenarios

Contract Terms	Risk
No price escalation provisions No supply chain clause	Poor
Price escalation provisions No supply chain clause	Good
Price escalation provisions Supply chain clause	Best

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Tariff Claims | No Escalation Clause

Presents Very Difficult Situation

- Most existing contracts do not contain
  - Price escalation clause
  - Supply chain delay language
- Traditionally, contract places on GC or subcontractor the risk of
  - Price escalation
  - Delivery delays
- Such risks considered "price of doing business"

So, what should a contractor do?!?!

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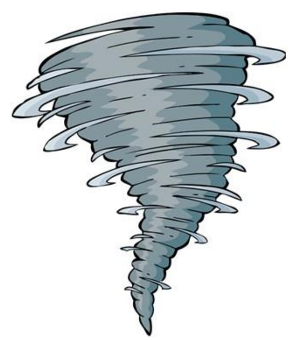
Tariff Claims | No Escalation Clause

The "Hail Mary Pass"

Tariff Claims | No Escalation Clause

Check the Force Majeure Clause

- Force Majeure = “superior force”
  - A force majeure event is an unexpected event outside of the control of both of the parties to the contract
- Clause provides that force majeure event triggers result
  - “If force majeure event occurs, then X happens”
- Force majeure clauses are not standardized; parties may customize to whatever they want



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Tariff Claims | No Escalation Clause

Check the Force Majeure Clause

- What occurrences constitute “triggering” events”?
  - Natural events (e.g., “severe floods” or “earthquakes”)
  - “Acts of God”
- What does state law say about enumerated events?
  - Most courts construe the list narrowly
  - Not on the list = not covered
  - Remember when lots of people forgot “pandemic” in the FM clauses
- Many construction contracts do not use the term “force majeure”
  - Instead, look for a “delay” or “time extension” section.

Tariff Claims | No Escalation Clause

Check the Force Majeure Clause

§ 8.3 Delays and Extensions of Time

§ 8.3.1 If the Contractor is delayed at any time in the commencement or progress of the Work by (1) an act or neglect of the Owner or Architect, of an employee of either, or of a Separate Contractor; (2) by changes ordered in the Work; (3) by labor disputes, fire, unusual delay in deliveries, unavoidable casualties, adverse weather conditions documented in accordance with Section 15.1.6.2, or other causes beyond the Contractor's control; (4) by delay authorized by the Owner pending mediation and binding dispute resolution; or (5) by other causes that the Contractor asserts, and the Architect determines, justify delay, then the Contract Time shall be extended for such reasonable time as the Architect may determine.

. . . unusual delays in deliveries . . .

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Tariff Claims | No Escalation Clause

Check the Change in Law Clause

- Operates like Force Majeure clause
- Provides that change in law triggers result
  - “If change in law occurs, then *X* happens”
- Impact determined by state law
  - What constitutes a change in law
  - Whether application of law constitutes a change in law

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Tariff Claims | No Escalation Clause

Check the Change in Law Clause

"If due to any change in applicable law, regulation, or interpretation thereof by any court of law or other governing body having jurisdiction subsequent to the date of this Agreement, performance of any provision of this Agreement or any transaction contemplated hereby shall become impracticable or impossible, the parties hereto shall use their best efforts to find and employ an alternative means to achieve the same or substantially the same result as that contemplated by such provision."

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Tariff Claims | No Escalation Clause

No Force Majeure or Change in Law Language

- With no contractual support, contractors will need to seek mutually acceptable business proposition
- Five-part plan
    1) Provide written notice to owner or GC about how tariffs are impacting materials' costs and delivery times
    2) Offer to collaborate to find solution
    3) Propose revised price tracking
    4) Request shared responsibility for increased costs
    5) Seek to meet and discuss details of such an arrangement

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Tariff Claims | No Escalation Clause

Step 1: Written Notice to Owner/GC

Escalation letter to Owner when Contract has no escalation clause

As you know, over the past few months, the construction industry has been and will continue
to face unprecedented escalation in material pricing and materials supply chain delays due to

As you know, over the past few months, the construction industry has been and will continue to face unprecedented escalation in material pricing and materials supply chain delays due to recently implemented tariffs on construction materials. Such an unexpected change in economic policies demand all parties to a construction contract work together to confront staggering price increases. For example, a recent report from ENR forecast that blanket tariffs on imports from Mexico and Canada would cause widespread cost increases to construction materials, in particular for cement, lumber, copper, steel, and aluminum. We could continue to list other materials price increases from recent proposed or implemented tariffs, but we believe we should devote our energies to finding a solution and not more facts and figures.

overcome such pricing and delivery issues. Such solutions could begin with value engineering, substitutions, or early purchasing warehousing, but, should those not suffice, include change orders to share costs from increased prices and delayed deliveries.

Such change orders will never include overhead or profit mark-ups on the increases from either us or our subcontractors or suppliers. In addition, because contractors can agree to consider some risk of costs from price escalations and delivery delays, we are willing to bear the first ___% of any such cost increase. 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 would like to schedule as soon as possible a first meeting to address these issues and proposed solutions and ask for days. Although no owner wants to see a higher project price due to the change orders proposed, in the alternative they face a real possibility of a default or a delayed project due to whims in the materials market. The entire team of the owner, design professionals, contractor, and subcontractors must work together to eliminate these detrimental business outcomes.

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Tariff Claims | No Escalation Clause

Step 2: Offer to Collaborate

<u>Escalation letter to Owner when Contract has no escalation clause</u>

As you know, over the past few months, the construction industry has been and will continue to face unprecedented escalation in material pricing and materials supply chain delays due to

So, we are reaching out to determine how we can work together to overcome these escalation and delay issues so as to bring in our present project on time. Doing so will 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 the industry did in confronting price escalations and supply chain delays following the COVID pandemic, we need to find a middle ground with such issues and share the burden of their potential impacts.

means we will share our estimated costs for those materials with price escalations and delivery delays that are impacting on our ability to work the most. We will then track those costs through either (a) price and delivery time changes from the provider or (b) recognized timely and credible, third-party price indices such as RS Means, Steel Market Update, and the like. Keeping everyone fully informed about market changes would facilitate collaborating to overcome such pricing and delivery issues. Such solutions could begin with value engineering, substitutions, or early purchasing warehousing, but, should those not suffice, include change orders to share costs from increased prices and delayed deliveries.

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Tariff Claims | No Escalation Clause

Step 3: Propose Revised Price Tracking

Escalation letter to Owner when Contract has no escalation clause

As you know, over the past few months, the construction industry has been and will continue

In that vein, we would like to suggest an open book approach to materials purchases. That means we will share our estimated costs for those materials with price escalations and delivery delays that are impacting on our ability to work the most. We will then track those costs through either (a) price and delivery time changes from the provider or (b) recognized timely and credible, third-party price indices such as RS Means, Steel Market Update, and the like. Keeping everyone fully informed about market changes would facilitate collaborating to overcome such pricing and delivery issues. Such solutions could begin with value engineering, substitutions, or early purchasing warehousing, but, should those not suffice, include change orders to share costs from increased prices and delayed deliveries.

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Tariff Claims | No Escalation Clause

Step 4: Request for Shared Cost

Escalation letter to Owner when Contract has no escalation clause

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Tariff Claims | No Escalation Clause

Step 5: Meeting

Escalation letter to Owner when Contract has no escalation clause

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Tariff Claims | Escalation Clause

Preserving Claim

- Give timely notice
  - In accordance with contract
  - Content and method
- Propose alternatives or substitutions
  - Fulfills mitigation obligations
- Watch out for waivers!
  - Do not sign lien waivers unless you have exceptions for any pending claims
  - Consult counsel if payment withheld
- Keep proper documentation
  - Make sure to track costs
  - Then keep accurate records of such tracking

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Tariff Claims | Escalation Clause

Preparing Claim

- Collect documentation
  - Price indices, supplier invoices
  - Job cost reports, daily reports
- Prepare change order request or claim letter

Tariff Claims | Escalation Clause

Presenting Claim

- Submit your claim as the contract requires
- Follow the claim procedure

Claim Meeting

Initial Decision Maker

Project Neutral

Mediation

Arbitration/ Litigation

Conclusion

Make sure you protect yourself against tariff risks in your contracts!

"By failing to prepare, you are preparing to fail."

- Benjamin Franklin

Questions?

Thank You For Attending

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