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Supply Chain: Time to Saddle Up!

I. Introduction

After over a year of quarantine, businesses resume post Covid-19 operations with a supply chain affected by a year of disruption. From computer chips to lumber to labor, the building blocks for construction and development were in short supply. With the demand for housing at historic levels, the speed, constructability, and quality of today's projects will govern the pattern of claims and losses for years to come. Our panel reviews the legal, transportation, logistics, insurability and claims patterns key to understanding this future today. Join this interactive panel as we "saddle up" with tips to keep you in the race and get across the finish line.

II. A Lawyer's View of Supply Chain:

I remember the day of March 4, 2020. California Governor Newsom declared an emergency due to the Covid-19 Pandemic. Over the next few weeks, we all moved into the unknown of how to deal with a pandemic. The playbook from the Spanish Flu in 1918 was not well recorded on legal matters. Clients wanted to know what *force majeure* meant. We knew that Covid-19 was deadly, but had no idea how wide it would spread, how long it would last and how life would be different. Supermarkets were out of toilet paper, paper towels and non-perishable food items. Most courts were closed with limited emergency operations. Civil litigation stopped.

Kids were told to go home from school, learn remotely, working parents juggled their schedules and tried to maintain some sense or order. We learned of this thing called Zoom, joined onto the Microsoft Teams Team and a variety of other remote platforms.

Construction was deemed essential. So were most lawyers, though our offices once bustling were, for the most part, silent. We were making masks, helping others, learning social distancing, cheering nurses and healthcare professionals. Clients were making

claims on their business interruption coverages only to learn that this was not property damage according to most judicial decisions. Unemployment spiked to levels not seen since the Great Depression, our investment markets reverberated, and it was a good day if you brought home a loaf of bread, a roll of toilet paper and a hot meal.

Fast forward a year: we have vaccines, we managed remoteness and are looking forward to a return to whatever will become the "new normal." The loss of over 3.5 million lives and counting worldwide, together with over 500,000 here in the U.S. was a reminder of how deadly these times were-and potentially still are.

We remember those who passed in this pandemic. Their loss cannot be replaced. The impact of what has happened in society will not be fully measured for years. It was a time of remarkable sadness for who and what was lost, but also a time of renewal for what will come next as we put back together our lives, communities, nation, and world.

From the comfort of the emerging moment, and with full confidence in our arrival in Atlanta, our panel moves forward to focus on the issues that arise from supply chain.

The remote environment has increased the risk of cyber disruption. The Colonial Pipeline energy disruption was but one of many events which revealed the fragility of our assumptions. Thus, the challenge with supply chains is not only physical, but virtual. Thus, first and foremost, is exceptional care in communication on all levels as the nefarious do not offer special quarter in times of national and international challenge.

The evaluation of legal risk often tracks what clients agree to. Contracts still govern most relationships in the construction field. As a result, not only great care was needed before Covid-19, but even greater care ever since. Financial risk allocated in contract is often enforced as part of the bargain-whether it be benefit or burden. For example, in looking at *force majeure* in New York, their Court pointed out in Mc Alloy Corp. v. Metallurg, Inc (2001) 128 N.Y.S. 2d 14:

> "Increased cost alone does not excuse performance unless the rise in cost is due to some unforeseen contingency which alters the essential nature of the performance. Neither is a rise in the market itself a justification, for that is exactly the type of business risk which business contracts cover."

As a result, financial hardship, generally, is not a defense to performance. Most *force majeure* clauses focus on natural events: earthquakes, hurricanes, or other similar events. Some also focus on Acts of God. Others specifically enumerate a list of awful things, but few, to date, list pandemics. Often, event when *force majeure* does apply, it typically acts as a time period for delay in performance, rather than a source of additional compensation or full excuse from contractual duties. States vary on their

enforcement ranging from specific mention of an enumerated peril to others that focus on an unexpected, unanticipated event beyond a party's control. As these matters revolve around the application of state law, stakeholders need to examine which state, which court and even which judge to get a better read on how these matters will be evaluated.

Not surprisingly, case law development in 2020 have varied depending on the jurisdiction. With all the office space out of use due to remote workforce developments, payment of commercial rent started in our courts. While they may not reach the appellate level for some time, they illustrate the juncture of government shutdowns, risk prevention of disease and development of a mobile work force that may not need those facilities in the near or perhaps long term. For example, in Florida, the United States District Court, Southern District of Florida carefully examined the nexus between the non-payment of rent, government orders and the benefit of the contractual bargain. Last Fall, in Palm Springs Mile Associates, Ltd. v. Kirkland Stores, 2020 WL 111353, the Court weighed, very carefully, that there needed to be a strong nexus between the event and non-performance noting that commercial tenants are not free to walk from their obligations.

In the supply chain, certain states have traditionally held suppliers to comply with their service and production contracts. For example, in Texas, where base prices for alumina rose and regulations interfered with manufacture, the Court still enforced the benefit of the bargain secured by the contract. Sherwin Alumina, L.P. v. Aluchem 512 F. Supp 957, 965-968. (S.D. Texas, 2007).

In the sale and exchange of goods, the Uniform Commercial Code Section 2-615, which is adopted in most states, provides that a contingency which was an assumed non-occurrence may serve a breach of duty under a contract to furnish goods. Further, in California, common law impossibility may arise when: (a) there is an unforeseeable event; (b) which is outside the control of the parties; (c) which renders performance impossible or impracticable. Thus, even in the absence of a *force majeure* clause other doctrines such as legal impossibility may apply based on traditional common law principles. There must be a showing of extreme circumstance of which the contracting party had no part in creating combined with efforts to cure before this theory gains traction before a court.

So, as a practical matter, what are the key considerations for the claim's professional:

1. Obtain and review all contractual documents including all addenda.
2. Identify the applicable scope of work or service to be furnished.
3. Review job schedules and understand what the critical path was for the work.
4. Consider what happened to make it impracticable to perform.
5. Evaluate the reasonableness of the actions taken and all communications.
6. Was there an alternative method, material, or design to complete in another way.

Pro-actively, look for and negotiate flexibility in scheduling, allowances for time that could not be utilized, mitigate the impact of cyber events that can affect supply chains, potential waivers for claims on consequential damage and express indemnification provisions to share and allocate risk.

Recent events mean we cannot make assumptions. Backup power sources, remote platform support, develop and maintenance of good relationships with all stakeholders, early and frequent communication on job developments that may impact time and performance and real-time documentation are the best paths to ensure success. Firmness and flexibility become the watchwords with those in good relationships with multi-lateral delivery systems with an advantage to optimize importance.

III. A View from the Road

In 2018, the California Supreme Court issued a landmark decision in the field of transportation entitled: Dynamex Operations of the West v. Superior Court (2018) 4 Cal. 4th 903. In that decision, the Court adopted the ABC test regarding the classification of drivers in the trucking industry. The industry, which had moved to a more flexible, independent contractor model, was then required to re-evaluate its role. It essentially removed the assumption of the more flexible independent contractor standard enunciated in S.G. Borello & Sons, Inc. v. Department of Industrial Relations (1989) 48 Cal 3rd 341, as it established the following test:

1. The worker free from the control and direction of the hirer in relation to the performance of the work, both under the contract and in fact.
2. The worker performs work that is outside the usual course of the hirer's business.
3. The worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed by the hirer.

If the worker fails any element of the ABC test, then he or she is an employee for the purpose. This was codified in California shortly thereafter by AB 5. In January of 2021, the California Supreme Court confirmed that Dynamex applied retroactively in Vasquez v. Jan Pro Franchising (2021) 10 Cal. 5th 944. Although there are some statutory exceptions, the development of an uneven pattern throughout the country is a challenge.

Therefore, in those situations where truck delivery is necessary, there may be issues of (1) availability and scheduling; (2) higher delivered transportation costs than earlier models based on the independent contractor.

Further, road infrastructure is behind schedule in many states resulting in transportation delays, detours, weight restrictions and related factors which can have an impact on delivery to job sites. Further, as there is a shortage of skilled labor in all industries, including transportation. This affects equipment, repairs, service and performance of trucks, their drivers and related cargo.

IV. A View from Forensics:

Challenge is opportunity in disguise. The firms that evaluate post-loss damage are in the best position to leverage those skills in advance. From peer review of design, independent quality control and job walks, the capacity of forensic professional to prevent and mitigate losses in real-time has never been higher.

Regardless of the form of delivery, an independent budget analysis focused on flexibility in construction method and means is pennies on the dollar of claims risk. Many contractual arrangements, some insurance policies and other insurer requirements focus on a greater role of prevention rather than cure.

With labor, material and deliverability shortages, the focus on prevention in the Post Covid-19 timeframe have never been higher. This is especially true where key personnel may need to work remotely, use drones or other means of job site participation without physical presence.

In the post-loss context, focus will be on job file materials, level and detail of communication and examination of schedules. Availability and substitution of materials will also be a factor in assessing the extent of and potential reduction of recoverable damages. Early and precise investigation lead to better, more reliable, and quicker resolutions.

V. A View from Insurance:

In the Post Covid-19 marketplace, availability and capacity need to be considered and examined carefully. With the tightening of the market generally due to greater losses generally and severity in particular, placement will require advance planning, creativity and probably some element of shared risk.

The severity of claims in the cyber realm have been felt throughout the industry. The exposures created by recent cyber-based interruptions are of concern to underwriters

and claims professional alike. Project-specific policies tend to provide the best value where the size of the project warrants it.

Factors that will influence the underwriters will include, in addition to loss history, include the type of project, what is the percentage of document completion when the project is bid (greater than 50%/), its attendant risk to both virtual and physical risk, potential influence of weather or naturally created events. Those which bear a risk due to difficult soils related conditions, locations near major thoroughfares and power transmission also lead to further scrutiny.

For 2021, we encourage early consideration of renewal, viable market options, the leverage of towers for more sophisticated risk and evidence of state-of-the-art record-keeping and cyber security.

VI. A View from the Claims Professional:

With the growing prevalence of alternative delivery methods such as design-build, construction manager at risk and so many permutations, the time arrived for contractors to have professional liability insurance and for designers to have more general liability and product insurance. As departure from the tripod of design, bid and build evolved, the development of greater expertise followed for different stakeholders in the construction field. This has had some benefits in better recognition of variance between design and construction, consideration of constructability, and budgeting to anticipate these concerns.

Computer-generated tracking of design and construction in progress such as BIM improve the knowledge base of what was built. The ability to leverage those technologies, improved record-keeping, and alternative consideration of designs, has helped from a claim's perspective. The key issue remains mitigating severity in real-time to avoid the dangers and expense of large claims.