

# Tariff Turbulence: Strengthening Construction Contracts to Weather the Storm

Alert

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In light of the Trump administration's imposition of 25% tariffs on imports from Canada and Mexico, construction industry stakeholders are facing renewed cost pressures and potential project delays. This alert discusses how targeted contractual provisions—specifically material price escalation clauses and delay provisions—can help manage these risks. Additional strategies to further protect parties in construction contracts are also outlined below.

## BACKGROUND

The recent tariffs will undoubtedly increase the cost of key construction materials imported from Canada and Mexico, including steel, aluminum and lumber. That may, inevitably, create issues for existing contracts that do not adequately address such delays and material cost increases. It may also require new, or pending, contracts to address the possibility of sudden price hikes and schedule disruptions related to the same. As a result, it is prudent for contracting parties to give due consideration to their existing contract terms (which may already adequately address the items noted below) and/or consider incorporating specific provisions into new contracts that allocate risks and safeguard the interests of all parties involved.

Benefits of doing so include enhancing contract fairness by providing pre-agreed mechanisms to manage price volatility; affording predictability for the final contract price; reducing the risks of costly disputes; and ensuring that delays resulting from external economic factors, like tariff increases, do not disproportionately penalize one party.

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## KEY CONTRACTUAL PROVISIONS

### Material Price Escalation Clauses

Given the volatility in material costs due to the new tariffs, integrating material price escalation clauses in contracts is essential. These clauses allow for adjustments to the contract price based on significant increases in material costs beyond pre-defined thresholds. The content of the clause can be as simple or as complex as desired, depending on the size and duration of the project.

- **Application:** Link price adjustments directly to tariff-induced cost fluctuations, ensuring that neither party bears an undue portion of the financial risk. Clearly identify how the cost of price increases will be allocated and include a cost adjustment index or average price in a given geographic area.

### No-Damage-for-Delay, or Excusable Delay, Provisions

Incorporating “no-damage-for-delay” clauses, where authorized by law, can protect parties from financial liabilities arising from project delays due to tariff-related disruptions. These provisions typically limit compensation to time extensions rather than monetary damages, thereby reducing potential disputes over delay-related costs. However, such provisions can also shift the risk of delay-related costs to one of the contracting parties. Another way to deal with tariff-related cost increases is to identify what constitutes “excusable delay” and/or “compensable delay.” An “excusable delay” is a delay caused by factors beyond a party’s control, meaning they are not at fault for the delay and are usually entitled to a time extension, while a “compensable delay” is a delay where a party is not only excused for the delay, but it is also entitled to financial compensation for the added costs incurred due to the delay.

- **Application:** Clearly define the scope of limitations for delays and/or define what is, and is not, excusable and/or compensable delay.

## ADDITIONAL PROVISIONS TO CONSIDER

### Tariff Adjustment Clauses

A tariff adjustment clause is a specific provision in a construction contract that allows the price of a project to change if the cost of materials increases due to tariffs. This clause helps protect the parties from unexpected price increases.

- **Application:** Draft provisions that specifically address cost escalations directly attributable to tariff increases. These clauses can help protect suppliers from the full impact of tariffs, while also providing buyers with a clear process for handling cost increases. Establish a formula or index linked to the

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applicable tariff rates and/or define thresholds that trigger renegotiation of pricing or cost-sharing arrangements.

## Force Majeure Provisions

A force majeure provision in a contract allows a party to avoid liability if it cannot fulfill its obligations due to circumstances beyond their control or unforeseen events. Consider expanding and/or defining with specificity the scope of force majeure clauses to encompass unforeseen events, like significant tariff impositions, to avoid disputes. This allows parties to seek relief from contractual obligations when external factors, such as sudden regulatory changes, impede project execution.

- **Application:** To the extent existing provisions are insufficiently broad or do not specifically address tariffs, include government-imposed tariff actions or related regulatory changes. Clarify that tariff-related delays may qualify as excusable, protecting parties from liability for schedule overruns. Provide a clear process for invoking this provision to minimize dispute potential.

## Change Order and Cost-Sharing Mechanisms

Change orders allow written modifications to the contract and can be used separately or in conjunction with cost-sharing mechanisms to address material price escalations. Enhance change order procedures and incorporate cost-sharing mechanisms to address unforeseen cost impacts resulting from tariff impositions.

- **Application:** Detail how changes in material costs or supply chain delays will be documented and approved. Consider cost-sharing provisions where both parties agree to share the burden of unexpected price increases.

## Advance Procurement, Storage Strategies and Prefabrication Agreements

Proactively procure materials and arrange for their storage, or enter into prefabrication agreements, to mitigate the impact of price escalations and shortages. Include contract terms that address storage logistics and associated costs to ensure clarity and preparedness for market fluctuations and job-site preparations.

- **Application:** Enter into advance agreements to order materials to lock-in pricing and avoid delays. Ensure you address storage rights, duties, and obligations for materials, and give due consideration to insurance coverage for the same. Finally, consider using a prefabrication agreement to facilitate the pre-purchase and off-site fabrication of materials.

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## Contingency Clauses

A contingency clause in a construction contract is a provision that sets aside a specific amount of money within the project budget to cover unforeseen costs or situations that may arise during construction, essentially acting as a safety net for unexpected expenses, like material price fluctuations, and allowing the project to continue without major disruptions if such events occur; it is a risk management tool for both the owner and contractor.

**Application:** Incorporate a contingency clause in your contracts. Be sure to address the types of contingency (owner or contractor), define its intended use, identify the approval process, and provide a mechanism for managing it.

## CONCLUSION

The evolving trade landscape underscores the importance of drafting construction contracts that are both flexible and protective in the face of economic uncertainties. By integrating material price escalation clauses, delay provisions and additional risk mitigation strategies like those outlined above, parties can better navigate the challenges posed by the current tariff regimes and the looming trade wars on the horizon.

## CONTACT

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