PERSPECTIVES

Tariffs and Trade Series: Strategies to Minimize Impacts of Tariffs on Your Construction Projects

Our perspectives feature the viewpoints of our subject matter experts on current topics and emerging trends.

This paper is the third installment in a series examining the multifaceted impacts of tariff and trade policies. By delving into the nuances of these policies, we aim to provide valuable insights and perspectives that will inform strategic business decision-making and foster resilience in an increasingly volatile global market. Future papers in this series will explore the specific implications for key sectors such as agriculture, energy, and construction, offering targeted analysis and recommendations to help businesses navigate and thrive amidst evolving trade landscapes.

INTRODUCTION

Tariffs have once again become the hot headline that dominates the news. This is not the first time owners and contractors have had to manage the risk associated with tariffs and the related impacts.

This article focuses on the immediate and long-term impacts of tariffs on construction projects and even a company's financial health. It also examines potential key risk mitigation measures that can be implemented to minimize those risks.

WHAT ARE TARIFFS AND HOW DO THEY IMPACT MY PROJECT?

Tariffs are just one lever countries utilize as a trade policy instrument to *"raise revenue for the federal government, to restrict imports and protect domestic producers from foreign competition, and to achieve reciprocity through agreements that reduce trade barriers".*[1] Historically, in the United States, tariffs go back as far as the Tariff Act of 1789 signed by George Washington imposing a 5% tariff on nearly all imports to the newly formed United States. Globally, tariffs have been around since ancient Greek and Roman times.

So, what does that mean for me now? For owners, contractors, and suppliers, the concern is that these new or higher tariffs may add costs, impact the project schedule, degrade margin, cause contractual disputes, disrupt the normal supply chain ecosystem, or add challenges in the bid and estimating phase. Complicating all of the above is the global uncertainty of not just whether the tariffs will indeed be implemented, but also the amount of the individual tariffs, as well as the various downstream reactions of the countries and companies subject to the tariffs. A summary of potential impacts is included below.

Project Level

For those projects that are under contract, the implications may be both short-term (direct cost increase related to the imposed tariff) and long-term (delays impacting the critical path), for which a few examples are provided below.

- Increased costs which may not be recoverable under the contract – These could include cost increases for the tariff itself, raw materials, indirect costs, transportation, expediting or compliance costs, or costs to transfer to alternative suppliers.
- Schedule delays – Contractors may focus on the immediate cost impacts of a change in price but may initially fail to realize there could be impacts to the schedule at the time of the change, or as market conditions and secondary supply chain impacts emerge later.
- Disputes leading to costly litigation – Disputes may arise around the ability to recover costs because of tariffs through the contract which may lead to litigation.

Corporate Level

- Potential impact to margins – Impacts may roll up to financials, potentially affecting working capital and ability to bid on future projects.
- Potential impact on existing supplier / vendor network – This may lead to delays and costs to procure materials through existing suppliers or sourcing new suppliers.
- Potential change in market conditions – Uncertainty in the market may result in projects being shelved to take a wait-and-see approach before proceeding (e.g., slow-down in new construction, cancelation of projects underway).

[1] Irwin, Douglas A. "Trade Policy in American Economic History". Annual Review of Economics, August 2, 2020.

SOLUTIONS TO MITIGATE IMPACTS

Real-time project management techniques can be implemented to manage cost and schedule impacts.

Project Level

- Address Pre-contract steps – Understand the request for proposal or quotation terms and the ability to negotiate cost escalation impacts.
- READ THE CONTRACT – Understand notice provisions for change requests, or exceptions to changes for escalation or tariffs, which may or may not be excluded from reimbursement.
- Assess direct and indirect cost increases from subcontractors / vendors / suppliers – Implement additional scrutiny of potential claims from third parties for potential increases of costs due to tariffs and / or inflation.
- Assess schedule impacts and management – Evaluate impacts to determine if a schedule impact is due to the supply chain, availability of materials, or lack of inventory.
- Communicate with stakeholders – Once assessments are made of the potential direct and indirect impacts, communicate with project stakeholders as necessary.
- For federal contracts, understand the relevant federal acquisition regulations that provide for price adjustments and incorporate those into the contract(s).

Corporate Level

- Review contract strategy alternatives – Investigate use of alternative contracting strategies or pricing models such as tracking volatile costs with globally recognized indices (e.g., consumer price indices for fuel or steel, or shifting risk to subcontractor / suppliers).
- Review supply-chain logistics – Assess risks and opportunities in your supply chain to safeguard against the impacts of tariffs on cost and schedule. While diversifying your supply chain may reduce risk of delay, it may mean potential quality issues or impact longstanding relationships.
- Review opportunities to offset tariffs – Examine opportunities at local, state, or country level for leveraging trade incentives, tax credits, or other programs that may be offered by the government to offset tariffs.
- Evaluate the company's risk tolerance – During this time of uncertainty, assess corporate strategy, including market channel, volume, geographical and / or type of projects.

CONCLUSION

The current uncertainty around tariffs may present immediate and long-term impacts on construction projects and challenges within the industry. Implementing the proper key measures to manage any potential risk is critical to maintaining project stability.

At J.S. Held, we provide expert guidance to help companies adapt to these challenges, ensuring compliance, financial stability, and long-term success.

ABOUT THE AUTHOR

Robert Strahle is a Senior Managing Director and the US Lead in J.S. Held's Construction Advisory practice. Robert is a professional engineer and brings more than 35 years of experience in the engineering and construction industry, both internationally and in North America. His experience includes managing complex engineering and construction projects, the resolution of construction disputes including expert testimony, preparation of construction claims, construction cost assessments, construction fraud and forensic investigations, and process controls improvement.

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