

When the Price No Longer Stacks Up: How NZ Contractors Can Deal with Fuel and Freight Disruption

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Geopolitical instability in the Middle East is driving fuel prices higher and freight costs through the roof. For the New Zealand construction industry, we sit at the end of long supply chains, where diesel is embedded in almost everything we do.

If you are holding a fixed-price contract and watching your margins compress, there are a couple of paths to look at that may mitigate the negative impact increases on fuel will have on your business. First: check whether your contracts provide a recovery pathway? Second: if the contract does not help you, what commercial leverage do you have, and how do you use it to negotiate potential assistance?

Check your contract

Most contracts put the risk of cost increases on the contractor. That means ordinary fuel price escalation and rising shipping rates in most cases, sit squarely with the contractor. This is, however, not always the case, and some contracts may allow full or partial recovery. The first step is to see what who bears the risk of cost increases under your contract, and to what extent.

The following are a list of provisions that you should look out for in contracts that may provide relief:

1. **Cost fluctuation provision.** A fluctuations clause allows the contract price to be adjusted, up or down, in certain situations (usually when the cost of key inputs move beyond a defined threshold, typically calculated through an agreed indexation method). If your contract has a fluctuation clause, you likely have a direct cost recovery pathway. The extent of the relief will depend on the wording of the clause. However, if the contract puts the risk on the contractor, as it often is in competitive fixed-price tenders, ordinary price escalation is

unlikely to be recoverable.

2. **Force majeure provisions.** Many contracts include a force majeure clause that excuses performance or entitles a party to relief when an extraordinary external event prevents them from fulfilling their obligations. The drafting varies considerably. Some clauses list specific qualifying events (e.g. war, sanctions, port closures or government action) which may have a pathway to time relief and, in some contracts, cost relief. Read the clause carefully however as most force majeure clauses provide only time relief, not money.
3. **Unforeseeable circumstances or risk event provisions.** Some contracts, particularly standard form contracts, include provisions giving the contractor time and/or cost relief for events that an experienced contractor could not reasonably have anticipated at tender. The current geopolitical disruption to global energy and shipping markets has a reasonable argument for meeting that threshold. As with force majeure provisions, the relief available depends on the specific wording of the contract, and it is more often than not that only time relief is provided.
4. **Change-in-law clauses.** If government action (e.g. new import tariffs or import restrictions or regulatory intervention) directly drives a cost increase after your tender date, a change-in-law clause may treat this as a variation entitling you to additional cost. The current impacts are primarily market-driven rather than regulatory however, but this is one to watch as governments respond to the broader situation.

If you find there is a provision in your contract that entitles you to claim a variation and/or time relief under the contract, be sure to read the notice requirements and notify in accordance with your contract (in terms of timing, calculation and form of notice).

No contractual entitlement? Look to negotiate

Unfortunately, there will be many contractors that have currently signed up to contracts that do not provide relief for cost increases.

New Zealand's construction sector has been here before. During COVID-19, many principals and contractors found that the formal contract mechanisms were not always sufficient to address the commercial reality of a once-in-a-generation disruption. Commercial negotiations, agreed price adjustments, and documented side agreements were common. This is likely to be common with the current situation.

If the current disruption is creating genuine financial stress, understanding your leverage and having early transparent conversations is the best way forward.

Contractors shouldn't just give up if they don't have a contractual entitlement. If you don't ask, you don't get, and the best way to start a conversation about such is by understanding your leverage. Contractors should be aware that they have the following leverage:

- 1. There is a cost in replacing you.** The cost and programme impact of terminating a contractor and engaging a replacement is enormous. Even where a principal has a legal right to terminate, exercising it is rarely in their commercial interest. A new contractor will price the remaining works at current rates, will need time to mobilise, and will not carry the knowledge and relationships built up on the project to date. Replacement contractors will also often put on a premium for taking over a half-completed project.
- 2. Insolvency creates a bigger problem for the principal than an adjustment does.** A contractor under financial stress stops performing before formal insolvency. Subcontractors go **unpaid** and walk off. Materials are not ordered. The programme slips. Principals who have been through a contractor insolvency understand that preventing it is almost always cheaper than managing the aftermath. If the cost pressure you are facing is genuinely threatening your financial position, that is not just your problem. Frame it accordingly.
- 3. Time pressure is often the principals biggest exposure.** Delay caused by dispute or renegotiation is frequently more expensive for a principal than the cost adjustment

being sought. The longer a dispute drags on, the more they have to lose. Know your project's time sensitivities and factor them into how you approach the conversation.

In understanding this leverage, contractors should feel more confident entering into a negotiation with the principal.

Approaching a negotiation

Early and transparent conversations are likely to result in a more successful negotiation. In approaching a principal, you should:

- 1. Quantify your position.** Come with a specific and documented number, with supporting evidence. The gap between your tendered cost assumptions and current actuals or firm quotes. Fuel price comparisons, freight rate data, supplier price adjustment letters, and published indices are your evidence base. The more objective your number, the harder it is to dismiss as contractor self-interest.
- 2. Lead with this being a shared problem.** You don't want to lead with this being a contractual or legal problem, but more a problem for the project as a whole, otherwise the parties can become positional before the negotiations even start. A conversation that opens with "we have a problem that is going to affect this project and we want to work through it with you" is more likely to get you into a room with decision-makers.
- 3. Come with a solution.** Bring a specific proposal: a revised rate for defined items, an agreed index to apply going forward, a lump sum adjustment for documented cost impacts to date. Use open book information, if you are being genuine.
- 4. Be transparent.** Experienced principals often respond better to early transparency about financial stress than to a contractor who goes quiet and then collapses. If the cost pressure is genuinely threatening your viability on this project, say so (with support) and frame this as something you want to solve together. This converts the conversation from a claim into a crisis-prevention exercise, which principals are usually more willing to engage with.

Where the negotiations fall will depend on many factors, such as contractual wording, reasonableness of the principal and the real risk associated with the cost increases. To give yourself the best chance of recovery, you should put your best foot forward by following the above steps.

Protecting yourself in future contracts

Every disruption is a lesson in contract risk allocation. When you are next pricing a fixed-price job, these are the protections worth insisting on:

1. Fluctuations clauses with agreed base indices for fuel, freight, and key materials and an automatic trigger at a defined threshold.
2. Short tender price validity periods. Price movements while a principal is deciding whether to accept your tender should not sit with you.
3. Clear force majeure drafting that explicitly includes geopolitical disruption, shipping network failure, and energy market shocks.
4. Advance payment mechanisms for long-lead imported items, allowing early procurement before further price movement.

If you would like further or more specific advice on construction related issues, get in touch with Rebecca Richter, our construction law expert, at rebecca@fsl.nz, or Ford Sumner's division of Tradie Law at helpdesk@tradielaw.co.nz.