Adjusting the Curriculum – Strategies for Mitigating Construction Delays in Student Housing

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Universities and their students are demanding updated or new student housing. While this demand has been great for owners, developers and investors in student housing developments, delays can cause a failing grade for a project. Frost Brown Todd (FBT) is offering the following crash course on how to address construction delays in student housing so that readers of this blog post can get an A+.

Orientation

Student housing developments (SHDs) produce unique opportunities and challenges compared to other common commercial real-estate assets. One of the challenges owners, developers and investors have recently faced is a significant increase in construction delays impacting the critical path of the SHD project. While construction delays are not unique to SHDs, the impact of delays on SHDs is particularly detrimental. While a one-week delay may seem insignificant on its face, such delay could result in the SHD failing to be completed prior to the beginning of the school year, potentially adding a full year to the SHD's lease-up schedule.

Student housing market participants have experienced considerable headwinds the past few years following the global COVID-19 pandemic, including ongoing supply chain disruptions, rising inflation, and interest rate hikes, resulting in steadily rising construction costs for materials and labor. As such, it is critical participants remain cognizant of how to mitigate risks they *are* able to control.

Course Syllabus

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FBT has assisted its owner, developer, and investor clients in negotiating numerous workarounds to reduce harmful impacts stemming from delays to the critical path. Unlike delays caused by contractor labor shortages, which arguably could be addressed at least in part by paying higher wages, if the delay is created by non-labor-related effects (e.g., supply-chain disruptions, COVID restrictions, interest rate increases, or extreme weather), then increased wages will do little to address the impacts caused by the delay. These non-labor issues not only create delays to the critical path but can also cause price uncertainty and increased costs beyond pricing. Thus, SHD market participants must be forward-thinking, proactive, and creative in order to address non-labor delays and the pricing and cost issues associated with such delays.

Required Reading

The customary allocation of responsibility for construction delays is set forth in the suite of American Institute of Architects (AIA) documents that form the backbone of the agreements pertaining to the SHD project; however, they are often insufficient in addressing the totality of issues presented by non-labor-related delays. Moreover, if the parties have a separate development agreement (for example), or they are securing financing, as is typical, it is critically important to ensure the development, construction, and loan documents are internally consistent.

In addition, the form AIA documents do not adequately account for recent trends and the increase in delay events in general. The potential outcome by utilizing the AIA documents without project-specific changes may include (a) a sub-optimal party being left with the burden of addressing the delay and (b) inconsistent project documents as to responsibility for the delay which may result in costly and time-consuming litigation.

Extra Credit

One strategy to avoid outcomes (a) and (b) above that sophisticated counsel such as FBT often employ is to ensure that construction delay events, specific project details, and risks are

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thoughtfully considered and carefully measured throughout the negotiation of all relevant project documents. This thoughtful consideration and measuring will likely require substantial revisions by counsel to the AIA forms and may include:

- Riders to the standard AIA documents
- Consideration beyond "compensable" and "non-compensable" delay events
- Additional sub-sections to narrow the scope and properly assess and assign responsibility for delay events and their effects
- Ensuring that force majeure event language tracks the underlying construction and financing documents to ensure continuity across all applicable documents

Beyond the construction loan agreement and the general construction contract, it may be necessary for counsel to draft separate project documents, including the joint venture agreement and development agreement, in conjunction with each other—with consistent and relevant defined terms to ensure that all project documents result in the same party being responsible for bearing the costs and effects of any construction delays. This practice will result in the following:

- A consistent party being held responsible for the impacts of the event
- The party that is best positioned to bear the impacts having the obligation to do so
- Increased clarity among the project documents
- The parties assessing and pricing risks more effectively
- A decreased potential for litigation

FBT's Office Hours

In addition to the practices outlined above, FBT has negotiated provisions to promote cohesiveness among the various documents and parties and to anticipate and address common issues. For example, we have successfully negotiated provisions in

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construction loan documents whereby the lender (x) expressly permits the developer to purchase construction materials well in advance of their incorporation into the project and store them offsite, (y) is required to fund draws for these advanced purchase materials, and (z) waives the retention requirement related to such advance purchase materials. This enables the developer to reduce the likelihood and effects of construction delay events.

Another example of situation-specific provisions that FBT has utilized is an "anticipated conditions" clause that prevents a contractor from arguing that a known or reasonably foreseeable non-labor delay and its impacts are not compensable. FBT has seen this provision result in clearer and more concise project documents and the mitigation of potential disputes over the burden of the delay event effects.

Final Exam

With some initial forethought, careful planning and assistance of counsel, construction delays do not have to result in a failing grade for student housing owners, developers and investors.

FBT routinely counsels multifamily investors, developers, sponsors, lenders, and other key stakeholders on their developments, assets, and rentals across the country. We stay at the forefront of all industry trends, developments, and legislative and executive efforts affecting the industry, and we are ready to assist and guide our clients throughout the life of their projects. For more information, please contact the authors of this article or any attorney with Frost Brown Todd's Multifamily Housing industry team.

Multifamily Matters Blog

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