An alternative to fixed price supply contracts is the use of escalation clauses in the construction subcontract that the subcontractor signs with the general contractor which in turn might be included in the general’s contract with the owner. Such escalation clauses will shift the full risk or part of the risk of price increases to the general contractor or the owner. Although there are many variations of escalation clauses, three basic types of escalation clauses are: day one-dollar one escalation clauses, significant dollar increase escalation clauses, and delay escalation clauses.

Day one-dollar one escalation clauses reimburse the contractor or subcontractor for the costs of any price increases in materials or equipment that occurs after the signing of the contract or acceptance of the bid. The owner or general contractor pays the difference in the cost of the materials or equipment between the date of the contract or bid and the time of installation. Under a day one-dollar one escalation clause, each dollar increase in materials or equipment is reimbursed from the first day of the contract or bid. A typical day one-dollar one escalation clause is as follows:

*The prices of materials and equipment contained in this bid or contract are those in effect as of (date) ; Subcontractor shall be reimbursed for all increases in the cost of material and equipment as of the date of installation plus ___% overhead and _____% profit.*

Significant dollar increase escalation clauses are calculated to reimburse the subcontractor only for the large price increases which occur in materials or equipment between the bid or contract date and the date of installation. This type of clause places the burden of small price increases upon the subcontractor but shifts the risk of significant price increases to the general contractor or owner. A typical significant price increase escalation clause which also provides for an extension of contract time due to unavailability of materials is as follows:

*In the event of significant delay or price increase of material, equipment or energy occurring during the performance of the contract through no fault of the subcontractor, the contract sum, time of completion or contract requirements shall be equitably adjusted by change order in accordance with the procedures of the contract documents. A change in price of an item of material, equipment or energy will be considered significant when the price of an item increases ____% between the date of this contract and the date of installation.*

The subcontractor may want to specify that any price increases above 5% or above 10% an item of materials would be reimbursable. The percentage price increase should be a reasonable calculation of what the owner and general contractor will accept and of the maximum increase the subcontractor is willing to assume.

Delay escalation clauses are calculated to hold a fixed price contract for a limited period of time, but allow the subcontractor to
receive escalation benefits if the job is delayed beyond a given number of days or a specified date. This type of escalation clause seeks to reimburse the subcontractor for those price increases and expenses that arise during the period of delay. A typical delay escalation clause is as follows:

it is contemplated that the performance of the subcontractor’s work will be completed by (date). In the event that subcontractor’s work is not completed by that date, through no fault of the subcontractor, then the subcontractor shall be reimbursed for all increases in the costs of labor, material and equipment by reason of said delay including reimbursement for extended on-site supervision and overhead plus _____% general overhead and _____% profit.

The parties should agree upon the estimated completion date and the percentage of overhead and profit should represent a reasonable calculation of the subcontractor’s overhead and desired profit.

When subcontractors experience difficulty in successfully obtaining open-ended escalation clauses into contracts, they might consider combining an escalation clause with a guaranteed maximum price. This would in effect be submitting two prices by combining a price based upon current market prices of materials and equipment to be increased by some form of escalation with a maximum upset price. There are other methods of combining approaches. Some subcontractors submit one price based upon escalation and another lump sum price and give the general contractor and owner the choice of either. Whatever the approach the individual subcontractor chooses to solve the problem of the price-supply squeeze on materials in the construction industry, the subcontractor should make an individual judgment of what is best for his company or what is best in a particular contract situation.