

# Impact of “Shelter-In-Place” Orders on Construction Loans

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Construction lenders and developers are increasingly concerned that state, local or even federal so-called “shelter-in-place” or similar orders prohibiting all non-essential business activity may halt ongoing construction projects and trigger construction loan defaults.

In response to the COVID-19 pandemic, the governors of several states, including New York, California, Illinois, Florida and New Jersey, as well as some city mayors, have issued binding, enforceable shelter-in-place orders that typically classify specific, limited business activities as “essential” and broadly prohibit all other “non-essential” business activity. At the federal level, the Department of Homeland Security, through the Cybersecurity & Infrastructure Security Agency, has issued a non-binding, advisory memorandum on identification of “essential critical infrastructure workers” during the COVID-19 pandemic (the “CISA Memo”).

Many states’ shelter-in-place orders, including those of California, Illinois, Connecticut, New Jersey and Massachusetts, expressly classify construction workers and/or the building trades as “essential” workers thereby exempting residential and/or commercial construction projects from the applicable restrictions on non-essential business activity. However, even where a state-level executive order has defined construction work as “essential”, municipal governments may enact more restrictive shelter-in-place orders. This is the case in Massachusetts, where, although construction work qualifies as “essential” under the state’s shelter-in-place order, the Mayor of Boston has placed a temporary moratorium on most Boston construction projects.

If you have any questions concerning this memorandum, please reach out to your regular firm contact or our COVID-19 task force by clicking [here](#).

For more information, please consult our [COVID-19 Resource Center](#).

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New York has taken the opposite approach. Pursuant to an executive order issued March 27, New York's Gov. Andrew Cuomo has limited "essential" construction work to very specific categories relating to emergency repairs, health care, infrastructure and affordable housing projects and deemed all other construction work "non-essential". New York City's Department of Buildings has issued guidance stating that "affordable housing" includes "affordable inclusionary housing", "mandatory inclusionary housing" and residential development in which no fewer than 30% of the dwelling units are subject to a regulatory agreement or similar restriction on rent. Pennsylvania, Washington, Michigan and Florida have enacted shelter-in-place orders that similarly classify construction and require broad closure of construction sites.

Of note, Michigan's and Florida's shelter-in-place orders incorporate by reference the "essential critical infrastructure workers" classifications of the CISA Memo. The CISA Memo classifies workers in construction of energy, public works, telecommunication and governmental infrastructure as "essential critical infrastructure workers." However, the CISA Memo classifies traditional building trades (e.g., plumbers, electricians and builders) as critical workers solely with respect to the maintenance of existing buildings. New construction is only classified as essential with respect to infrastructure and temporary structures "required to support COVID-19 response." Thus, while purely advisory, the CISA Memo classifications are informing state governments, and states like Michigan and Florida have codified the CISA Memo classifications into binding, enforceable shelter-in-place orders.

To the extent shelter-in-place orders or other governmental actions halt construction, force majeure clauses under construction agreements and loan documents may apply to suspend the performance obligations of contractors or borrowers. These force majeure provisions vary widely and are strictly construed by courts, so they must be carefully reviewed. Even if a shelter-in-place order does not prohibit construction, developers and contractors may

claim general force majeure under their contracts or loan documents due to a difficulty in obtaining employees and/or construction materials in the current environment. On the other hand, developers may leverage lower demand for construction materials and labor to push projects forward until required to stop by a shelter-in-place order.

Construction loan documents often include several covenants and/or events of default that could be impacted by shelter-in-place orders or other *force majeure* events:

- Notice: Loan documents typically prescribe a formal process for the borrower to claim *force majeure* delay, including prompt notice to the lender.
- Extension of Completion Deadlines: Completion deadlines may include a limited, capped (often at 60-120 days) extension for *force majeure*. Given the scope of the COVID-19 pandemic, an extension period for *force majeure* may expire while an applicable shelter-in-place order remains in effect.
- Near-Term or Immediate Event of Defaults:
  - *Projected Completion*: Under some loan documents, an event of default occurs if the lender projects that completion will not occur prior to the completion date (inclusive of any *force majeure* extension). In this case, the mere anticipation of material delay due to COVID-19 or a shelter-in-place order could lead to an immediate or near-term default.
  - *Work Stoppages*: Many loan documents require that the borrower continuously and diligently pursue construction and may include an automatic event of default if construction is halted for a specific period of time (which in some loan forms can be as little as 10 days). Such a stoppage is often also subject to *force majeure*, but because the *force majeure* clause typically includes a fixed, aggregate cap on all *force majeure* delays, a lengthy stoppage

due to COVID-19 or a shelter-in-place order could cause a near-term event of default.

As the COVID-19 pandemic progresses, any modification agreements between lenders and borrowers to address construction delays caused by regulatory actions related to COVID-19 should attempt to take into account the likelihood that any current shelter-in-place restrictions may be further extended.

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