

Contractors' claims: How and why do claims end up costing so much?



A claim example

A flagship building which is the headquarters of a major company has serious design flaws which are affecting its structural integrity. These have been discovered after the company has moved in. It was built pursuant to a design-and-build contract entered into between the contractor and the company.

The contractor subcontracted the design and construction of the structural elements which are affected and that subcontractor had also subcontracted the design of this specific element to a design consultant.

The company clearly wanted a fully functioning building which is structurally sound and turns to the contractor to make that happen. It is of no interest to them who actually made the errors. The design-and-build contractor is the sole point of contact as far as they are concerned.

The contractor heads up the contractual chain and is the only entity the company will make a claim-and-commence litigation against. The longer the defects remain prior to being corrected the more expensive the claim, because the company has decided to vacate the building and is housing its staff in another building which it has rented. The contractor is often unable to recover from the next party down the contractual chain before paying out substantial sums for remedial works.

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At this point claim figures are already high:

- > Remedial works commence and it has been agreed that these will be carried out by the contractor and the cost borne by them before any recovery can be commenced. In order to mitigate the cost of the rent accruing on the alternative accommodation it is essential that the works start as soon as possible and therefore not await the outcome of the contractor's own claim against its subcontractor. The costs of these works may exhaust all layers of an insurance programme.
- > Although the contractor is bearing the cost of the remedial works, the company has its own claim for the recovery of the rent on the other building which it is now occupying. Legal costs will be incurred in defending the claim. The company may also seek to inflate the claim by including alleged loss-of-business opportunity caused by the disruption to its operations and it may also insist that additional works are carried out which go beyond the strict scope of remedial works.
- > Legal costs to commence a recovery action from the next contractor in the contractual chain will be high. The costs of a trial with legal and expert costs would be significant.
- > Expert costs in defending the claim against the company and ensuring the paperwork is in place for the recovery. At least three experts will be required: an engineer, a quantity surveyor, and an accountant.

Sounds familiar?

For more information about our expert risk management and claims expertise please contact our Toronto office.

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