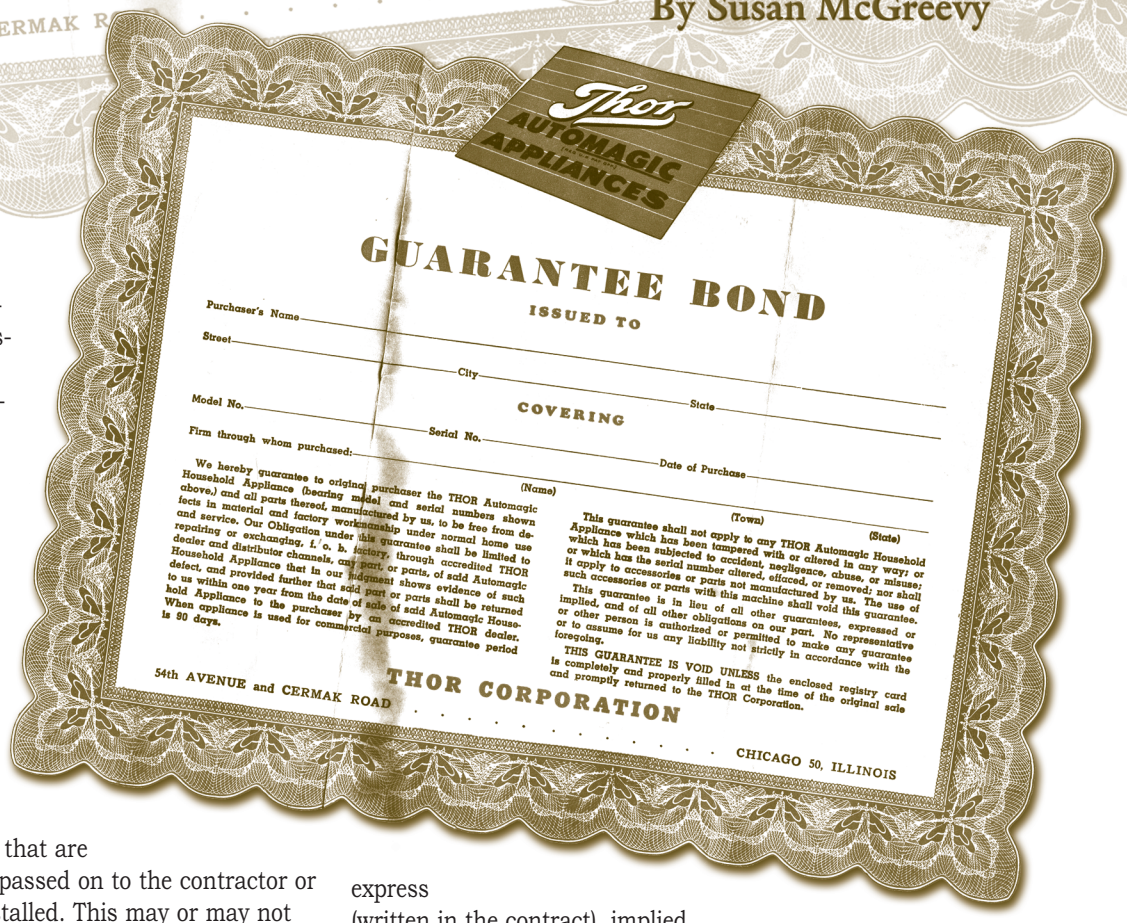
Warranties: MUCH More Than Meets The Eye

By Susan McGreevy



Experience has proven that warranties are one of the most misunderstood concepts in the construction industry. Many, including contractors, designers, owners, and yes, even lawyers, either confuse warranties with other provisions such as guarantees and/or correction remedies or fail to recognize the extent of their liability under their contract or purchase agreement. The roofing industry is no exception.

Many people dealing with the roofing industry believe that the only warranties that might be available are the ones contained in the limited warranty "certificates" that are issued by the manufacturer and/or passed on to the contractor or owner after the roofing system is installed. This may or may not be the case. The law is much more complicated than one might wish. Depending on the situation, the complete warranty "package" may be contained in several documents, including documents that were negotiated and drafted by others.

Confusion also arises when parties do not recognize the extent that warranties may be read into agreements by a court, even though the warranties are not printed in the contracts they sign. The confusion is important because it represents a failure of parties to understand the risks they face in the performance of a contract. This article is designed to provide a primer on what warranties are, where they come from, and what they mean.

What are warranties and where do they come from?

Warranties, simply, are assurances or promises given by one contracting party that a particular result will be achieved upon which another contracting party may rely. It should not be assumed that a written warranty that has been given is the only warranty that applies to one's work or product. Warranties may be express (written in the contract), implied (by the common law), or statutory (set forth in a state's statutes). Warranties can be in contracts, printed on product packaging, in plans and specifications, or arise out of conversation.

A warranty is not a piece of paper, and the fact that a paper "certificate" never gets delivered may or may not affect the existence or extent of the warranty. If two firms enter a contract in which one promises that its product will be warranted for five years, for example, the warranty is created when the contract is signed, whether a certificate of warranty is ever delivered. This all depends on the contract and dealings of the parties.

Express warranties may be written or oral

An example of a typical express warranty clause is the AIA A201 General Conditions (1997 Ed.), article 3.5.1:

> The Contractor warrants to the Owner and Architect that the materials and equipment furnished under the Contract will be of good quality and new unless otherwise required or permitted by the Contract Documents, that

the work will be free from defects not inherent in the quality required or permitted, and that the Work will conform to the requirements of the Contract Documents. . .

Although not always stated in these same words, most express warranties include representations that:

- The work will be performed in a good and workmanlike manner or will be free from defects.
- The material used will be new and of good quality.
- The work will conform to the requirements of the contract documents.

These assurances don't always appear in a section entitled "Warranties," although most standard-form construction contracts (such as AIA or AGC) do contain them in this expected paragraph. But there can also be other assurances scattered throughout the contract. This is particularly a problem where a party has added "supplemental" conditions that could contain language that expands or in some cases contradicts the language of the warranty clause. Many carefully considered risk management decisions can go right out the window if an unsuspecting party adds additional language to the contract without legal review of the entire package.

While most express warranties are memorialized in writing, they can also be created orally. In most cases, oral warranties are enforced by the courts, but the situation doesn't arise frequently because many hurdles must be cleared to enforce an oral warranty:

- If the representation was made before the contract is signed, it might be unenforceable if the contract has an "integration" clause saying that this contract reflects the final agreement of the parties.
- If the representation was made after the contract is signed, it might be unenforceable if the contract has a "changes" clause saying that all changes to the contract have to be in writing.
- The state may have a "statute of frauds" that requires some types of agreements to be in writing.

The court decisions make clear that no magical words are necessary to create an oral express warranty. Courts have held that oral assurances such as, "this roof will last at least 40 years," are enough to create an express warranty. Conversely, simply saying something is "warranted" is insufficient where the details of the assurance are not clearly established.

The biggest risk with oral warranties is that frequently a jury decides whether they were given or what their terms were. This uncertainty makes it all the more important that contracts are drafted well and reviewed in their entirety before entering into agreements.

Warranties "incorporated by reference"

Designers, when preparing specifications or plans, frequently "incorporate by reference" other documents and contract provisions, such as by referring to ASTM, ASCE, UL, NFPA, Factory Mutual, etc. Similarly, owners, when preparing contracts, will incorporate, by reference, a "boilerplate" set of general conditions such as the AIA or EJCDC general conditions. Contractors and subcontractors routinely seek to protect themselves by incorporating into their subcontracts and purchase orders the terms that have been imposed on them from above. All of these present more opportunities for additional warranties to become part of an agreement, whether the parties to the agreement intend it or not.

It is crucial to any contractor or vendor's risk assessment to obtain every one of these incorporated documents or terms and read them. If they contain warranties with which the contractor/vendor does not feel comfortable, the issue should be explored before a bid is submitted that ends up being accepted, and certainly before a contract or purchase order is signed. There is no other way to assess the risk being taken.

Implied warranties may be included without either party's action

In limited circumstances, courts have implied warranties to protect parties where there were no express warranties to do so. The theory is that in some circumstances, the parties intended a warranty to apply even though the contract doesn't expressly say so. The "warranty of habitability," which runs from residential home builders to the purchaser of the home and the implied warranty that the work will be performed in a reasonably workmanlike manner, are examples of implied warranties considered implicit in construction contracts unless they are expressly disclaimed.[1]

Most states do not impose this implied warranty of habitability on constructors of commercial projects. If the project is design-build or if the contract is based on performance specifications, however, the contractor also provides an implied warranty that its labor and materials will be of "merchantable" quality.[2] Further, courts have implied a warranty that the completed project, or at least the contractor-designed part, will be suitable for its intended purpose.[3]

Statutory warranties are imposed by legislatures

Statutory warranties are created by legislation and become part of some contracts by operation of law. The Uniform Commercial Code (or UCC), which has been enacted in some form in every state, creates statutory warranties that apply to the sale of goods. In the construction context, purchase orders to material suppliers will usually be governed by the UCC. Further, if a subcontract is characterized as being predominantly the purchase of goods more than labor, there is a chance a court will find that the subcontract primarily concerns the sale of goods such that the UCC may apply. Again, this "characterization" is being made after the fact by a judge or jury – not a place anyone wants to be. UCC statutory warranties include:

- The **warranty of fitness for a particular purpose** (that the goods will serve the buyer's intended use if the seller has reason to know of that intended use).
- The **warranty of merchantability** (that the goods will be of at least average quality, conform to the promises made on any labels, and are fit for the ordinary purpose for which the goods are used).

How long is the product or service warranted to last?

One of the most common misconceptions about construction contracts is the myth of the "standard one-year warranty." Warranties do not necessarily have any set time limitation. Unless agreed otherwise, the product or service should last as long as a "typical" product or service of the same type can be expected to last. The answer can be different for every product installed in a construction project. Masonry can be expected to last longer than caulking. Paint does not generally last as long as conduit. And if anyone gave the subject much thought, he or she would quickly realize that the average construction consumer expects its new multi-million dollar building, parking lot, or dam to last a lot longer than one year.

The warranty – for whatever length of time the contract or a court may determine – ends up exposing the builder or vendor for an even longer time period, because in most cases the time to file suit doesn't start until the party knows or has reason to know of the defect. This is called the "discovery rule" in law. Thus, if a building develops severe mold problems eight years after it is completed due to mis-connected piping, in a state where there is a five-year statute of limitations, the owner may be able to sue the contractor if it can be shown that the owner could not have known about the problem with the pipes until the evidence of the mold was apparent.

Some states have provided relief from such long potential exposure to lawsuits by enacting "statutes of repose," which operate as outside limits on how long someone can be exposed to a lawsuit. For example, a law may say that there is a five-year statute of limitations, but no matter how long it takes to "discover" the problem, suit must be filed within ten years of final completion.

Care should also be taken to examine whether the warranty is extended in the event work fails. Some contracts say that the warranty period starts all over when the repair is completed. In effect, this could extend the protection far longer than any vendor could normally be expected to service its product.

To whom is the warranty given?

Although entire legal treatises can be written on the subject, general contractors who sign contracts containing warranties are said to be in breach of contract if the product does not perform as represented. Because the warranty is in writing in the contract, any claim of "breach of warranty" is really a breach of contract.

It is possible for claims of breach of warranty to be made where there is no "privity of contract." Where the party holding the warranty did not enter a contract with the party giving the warranty – such as an owner to whom the warranty was passed on by a general contractor – it may be that third party who is claiming breach of warranty as an intended recipient of the warranty. Many contracts specify that the party giving the warranty must agree to honor claims by third party owners, to avoid this issue from being raised. Similarly, many manufacturers specify that only the original owner can make a claim ("good for as long as you own this car") to avoid such liability to unknown persons.

What will a warranty require the vendor to do?

Work not conforming to such assurances may be considered "defective." What happens next will also depend on what is in (or out of) the contract. If there is no other limitation in the agreement, typically the owner/promisee is entitled to repair or replacement of the defective work, so that the owner/promisee gets the full useful life it was promised. This can include removal and replacement of work damaged as a result of the failure and work that has to be torn out in order to get to the defective work. To the extent that damage other than the defective work itself has to be repaired, insurance may be available – but the nuances of insurance coverage are complex and far beyond the scope of this article.

Note that most warranties will typically exclude defects caused by abuse, modifications, improper or insufficient maintenance, improper operation, normal wear and tear, and normal usage.

Then what was that "one year" obligation?

The one-year period frequently included in construction contracts is generally not a warranty at all but instead an obligation to return and correct any defects caused by faulty workmanship or material within a specific period of time. Many standard form construction contracts use a one-year period for this correction of work.

Since the warranty contained elsewhere in the contract already obligates the contractor to stand behind his work, one might question the purpose of this one-year clause.[4] There has been a lot of debate about this, and not all commentators agree on how to make sense of these two different clauses. It is the belief of this author that the call-back both benefits and burdens the contractor. The benefit is that it requires the owner to contact the contractor and allow the contractor to fix his own mistakes, or the owner will be barred from making any later claims (including warranty claims). The burden is that it typically turns the contractor into a maintenance man for the owner for the one-year period.

It is not unusual for a drafter of a contract to actually decrease the warranty obligation of a contractor or vendor by modifying "standard" indefinite warranty language (such as the AIA A201, § 3.5.1) to specifically say that the contractor "shall warrant all work for a period of one year." In fact, this happens

with some frequency as a result of drafting done by people who are not fully educated as to the ramifications of some of their decisions.

Can these broad standard warranties be changed?

Absolutely. It happens all the time. In fact, it is unusual to find a construction project on which the warranties in the prime contract, subcontracts, and purchase orders are all the same. Many times these changes are made inadvertently (most owners expect that their steel beams and brick walls will last more than a year). But in just as many cases, the warranty is a carefully crafted document produced by lawyers who know exactly what they are doing: limiting liability.

Liability can be limited in several ways:

- **The extent of the warranty can be stated.** The typical roof warranty is explicitly stated in contract documents to be a certain number of years – ten or twenty – which many owners think creates a longer obligation.
- **The person or firm who can call on the warranty can be extended or limited.** Some contracts add words to assure that the warranty is assignable.
- **The remedies in the event of failure of the product can be spelled out.** Frequently, this is where the manufacturers seek to protect themselves by limiting their obligation to "repair or replacement" of the defective item itself, disclaiming all "consequential" damages such as down time, damage to other work, etc. They also may require the owner to pay the transportation fees to get the goods back to the manufacturer for inspection and repair.

As a result of these limitations, some warranties are so limited that they are practically meaningless – and certainly of far less value than the common law implied warranties or general contract warranties that might otherwise apply.

Product manufacturers are light years ahead of the rest of the construction industry when it comes to understanding the risks of "typical" warranties and doing something about it. In instances where specifications require the use of a product whose manufacturer refuses to give a broad warranty, bidders should bring this to the attention of the owner to see if the warranty for that particular item can be limited to what is available from the manufacturer.

The pitfall that most frequently thwarts an attempt to disclaim or limit a warranty is an express warranty elsewhere in the contract that is inconsistent with the disclaimer language. Courts don't like limited warranties, and if there is a way to require the party being sued to fix its defective work, they look for contract language to support that conclusion. A common example of this is found in contracts containing language that materials used on a project will be "new and of good quality" and contains, as well, a clause disclaiming the warranty of merchantability with regard to goods supplied pursuant to the agreement. A court will likely find the disclaimer ineffective because the agreement creates an express warranty that is inconsistent with the disclaimer. The lesson is that it is not enough to draft a clear disclaimer. One also has to make sure that the entire contract is consistent with the disclaimer.

Conflicts among warranties

As noted, it is also not unusual for there to be more than one warranty clause in a contract and for the clauses to be different. How this gets resolved may depend on how the contract is worded and what law applies. It has been the source of much litigation.

- **"Battle of the forms" for UCC-controlled contracts.** Materials manufacturers are among the savviest members of the construction community when it comes to warranties, and they can be expected to have explicit disclaimers or limited warranties that often are squarely at odds with the warranty clauses of contracts and purchase orders. When both the P.O. and the quote/acknowledgement from the vendor say that they "can only be accepted in strict accordance with their terms and no other terms will be agreed to," a nice basis for a lawsuit has been created.
- **When the warranty starts to run.** It is not unusual for a prime contract to provide that all warranties start to run from the date of final acceptance, while the equipment furnished by particular firms is sold with a limited warranty that says it starts to run from date of delivery. If the manufacturer's warranty has expired before the prime contract obligation expires, the general contractor must fix the manufacturer's defective work.
- **Which is most onerous?** As mentioned above, frequently a contract can be found to contain more than one warranty. A way to avoid unhappy results later would be for a contractor to provide that the broadest warranty, or the one with the longest time exposure, will control.
- **Order of precedence clause in contract.** Occasionally, contracts are written with a clause that tells the parties which clause will govern in the event of conflicting clauses. Frequently, this clause will say that specifications control over plans, special conditions control over general conditions, etc. This will not typically tell the reader which of the two contradictory warranty clauses is the operative one, however.

To help minimize being caught in this squeeze, there are some steps that can be taken:

- **If possible, try to get the owner to be as specific as possible regarding the warranty.** Where the prime contract is very explicit regarding the warranty, it allows the parties down the chain to include the terms in the subcontract or purchase order. This reduces the need to negotiate these points later on.
- **If the contracts are not specific regarding the warranty, define the scope of the warranty to be passed on to the contractor or owner.** A distributor or contractor should demand that the contract obligate it to pass on only that which it can get by way of warranty from its subcontractor or manufacturer. Alternatively, a clear disclaimer should be included if it is apparent that the distributor/contractor will be taking on more warranty liability than it can pass on to its subcontractor, supplier, or manufacturer.
- **Consider purchasing an "Installation Rider" for the insurance policy.** This would give the owner comfort that there is a source of funds to fix the equipment or material if it fails due to the distributor or contractor's installation, rather than an inherent problem with the equipment itself.

Conclusion

Warranties are a part of every construction contract. Those in the industry who take the time to understand how warranties work will gain an advantage over those who do not in managing risk on their projects. Risks can only be knowingly assumed and allocated when a party to a contract understands how warranties work. Paying attention to contract drafting as it applies to warranties can be an effective tool in managing risk and defining and limiting the remedies available under the contract. ■

1 Zenda Grain & Supply Co. v. Farmland Industries, Inc., 894 P.2d 881, 890-91 (Kan. Ct. App. 1995).
2 Aced v. Hobbs-Sesack Plumbing Co., 55 Cal.2d 573, 583-84 (1961).
3 Robertson Lumber Co. v. Stephen Farmers Coop. Elevator Co., 143 N.W.2d 622, 626 (Minn. 1966).
4 Most projects also have a "one-year warranty walk-through" conducted by the designer. All these same comments apply to the purpose and efficacy of that walk-through.

About the Author

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Susan Linden McGreevy is a member of the law firm of Husch & Eppenberger, LLC, in Kansas City, Missouri, and heads the firm's Construction Law Practice Group. Susan has a BA from the University of Michigan at Ann Arbor and a JD from George Washington University, Washington, D.C. She has been published in a variety of law, construction, and surety publications, including *Contractor, Pipeline, Construction Law,* and *CFMA Building Profits,* and is a keynote speaker at conferences and seminars across the country.

EDITOR'S NOTE:

The project profile of the Arrowhead Condominium in Big Sky, Montana, in the January 2004 issue of *Interface,* failed to note that the roof consultant on the project, Terry E. Anderson of Anderson Assoc., Consulting, Inc., is also owner of TRA Snow Brackets, the snow retention system mentioned in the article, "Sliding Ice and Snow Cause Roof and Property Damage." We regret this omission.