Guaranties and Warranties, A QS's Nightmare or Their Dilemma

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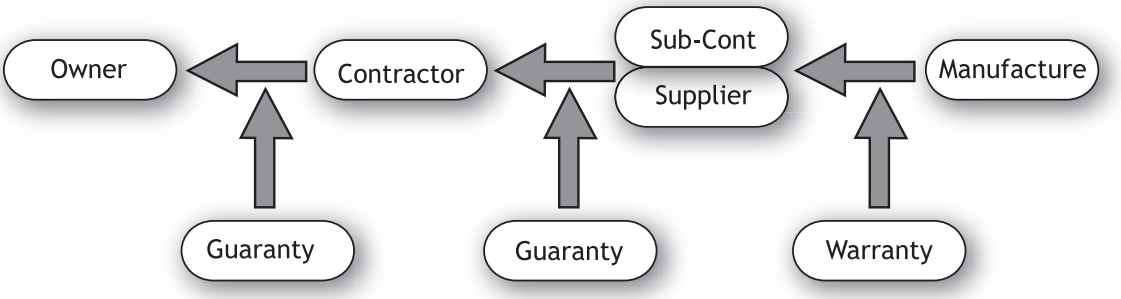
I have frequently been asked by Quantity Surveyors and Engineers alike, very senior people as well as students, to explain the difference between Guaranties and Warranties. This becomes even more confusing to some when lecturers speak about collateral warranties in respect of construction contracts.

Guaranties and Warranties have immense significance in the interpretation and administration of contracts. Both have the same meaning but in different contexts. In respect of a construction contract this can best be demonstrated by a diagram as follows:

The above diagram suggests that the contractor provides a Guaranty to the owner and the sub-contractors and suppliers give guaranties to the contractor respectively while warranties are obtained from manufacturers of plant, materials and goods they supply for incorporation in the works. The ultimate producer of the construction facility is the contractor and he guarantees to the owner that he has constructed the facility to the details and dimensions shown on the drawings and using the materials and workmanship as required by the contract specifications and also that his sub-contractors have done the same. He will also guarantee that the materials that he has procured from his suppliers have been guaranteed by his suppliers as being of the respective kinds as specified in the contract specifications.

A Warranty on the other hand (as far as our discussion is concerned) is a written guaranty given by the manufacturer to the contractor or sub-contractor whoever the purchaser is (through the vendor, the manufacturer's vendor). This in fact is an agreement assuming responsibility for the proper functioning of the product and that the product is fit for purpose. It is a promise or assurance given in writing that attests to the quality of a product or service or a pledge that something will be performed in a specified manner.

So what is the difference? Most of my students and also practicing quantity surveyors often ask me this question,



mainly at the time a project is completed and being taken over.

Defining a Guaranty seems simple but if a Warranty is also a guaranty why should it be identified differently? Looking at the diagram I have given above, it would appear that the contractor, by virtue of the contract, guarantees to the owner that he will do whatever he has contracted to do using the specified materials and best workmanship to produce the final end product to the satisfaction of the owner. Similarly, the sub-contractors, by virtue of their contract with the contractor have guaranteed to the contractor that they will likewise deliver their part of the works in the same manner. Insofar as the supplier is concerned, he can guarantee only that the materials, plant and goods supplied by him are of the brand and type ordered by the contractor and at the time he supplied them the manufacturer has warranted (guaranteed in writing) that the materials, plant and goods are of the specification that is written down.

Guaranties provide additional rights which could be a useful back-up in case of a complaint. Therefore, one must make sure that a manufacturer's guarantee given in the form of a warranty is written in clear and unambiguous terms and bears the vendor's stamp of authenticity. It is good practice to read the small print contained in a warranty in order to ensure that the product that is being bought is manufactured as specified and meets to owner's requirements. It is also essential to ensure that the vendor supplies the buyer with the manufacturer's registration card duly filled for the buyer to return this card to the manufacturer. This will serve as proof of purchase on the date the materials, plant or goods were purchased. This warranty is effective only when the buyer returns the registration card to the manufacturer to the address stated in the card.

For some plant or equipment like air conditioners, chillers, generators, heat exchangers and the like the manufacturers provide warranties extending beyond the normal defects liability period. Besides, even in the case of the normal one year warranty this might extend beyond the defects liability period depending on the date of purchase, or vice versa. This is a serious dilemma for the quantity surveyor who is administering the contract. To whom does he turn to when a breakdown happens?

In the same vein is the legal requirement in most countries for decennial liability guarantees from contractors. In most Middle Eastern countries the contractor and the designer are jointly and severally liable for stated defects including subsidence for ten years from the date of completion. A ten year guarantee of this nature is worthless if the contractor and the designer both go out of business during this period. In the United Kingdom and all European, American and North American countries, this is underwritten by insurance companies, thereby transferring the risk to insurance. In the UK there is the National House Building Council (NHBC) insurance for its members.

While the owner is protected from the contractor's guarantee by the provisions of the contract for the duration of the defects liability period and any manufacturer's warranty granted to the contractor during that period, what happens after the contractor is relieved from his obligations on the issue of the final certificate by the owner? As established in the case of Donoghue v Stevenson [1932] All ER Rep 1, the neighbor principle adduced by Lord Atkins will apply and the owner will have no remedy as he has no contract with the supplier. How, therefore can the quantity surveyor advise the owner to overcome this difficulty?

According to English law, liability arises where the defect becomes evident to the consumer within two years of delivery of the goods, unless the defect was or should have been apparent to the consumer at the time of the sale. Any defect apparent within six months of delivery is presumed to have existed at the time of delivery unless proof to the contrary is furnished or this is incompatible with the nature of the goods or the defect. The Sale and Supply of Goods to Consumers Regulation 2002 (UK) requires that when a guaranty is given free of charge with a product, it must be made available in writing and the terms of the guaranty should be set out in plain language which can easily be understood.

But whatever the law says considering the decision in Donoghue v Stevenson cited above, it will not be worth the paper it is written on for the owner, because he did not buy the goods - as such he has no contract with the manufacturer and his claim will be too remote, thus not meeting the requirements of the neighbor principle.

The difficulty in a construction contract arises when the facility is taken over and the operations and maintenance

of the facility are thereafter transferred to the owner's staff. How can the owner protect himself from a litigious situation arising out of this?

Prior to 1980 owners were able to obtain damages against negligent contractors and consultants through the courts without the need to demonstrate that they had any contractual rights. In fact they have no contractual rights in respect of a third party warranty. This all changed with the 1988 decision in the case of D&F Estates v Church Commissioners in 1988 where it was held that owners and occupiers of buildings needed a contractual remedy in order to pursue claims for certain types of losses. Thus the era of collateral warranties was born.

A collateral warranty is a contract which gives a third party (the owner) collateral to rights in an existing contract entered into by two separate parties (the contractor and the manufacturer or contractor and the sub-contractor or even the contractor and any consultant). Collateral warranties bring about a concentration of interests between those giving such collateral warranties and those receiving them. It is however not as simple as it sounds. The collateral warranty must be executed as a deed to be effective, the reason being that no consideration has passed between the owner and the manufacturer and a contract executed any other way will not be valid. There are several standard forms available. One such form is the one published by the British Property Federation and is designed to limit the warrantor's obligations.

Collateral warranties must be considered at the very outset of a construction project. It is essential to include in the construction contract and consultants' appointments the necessary provisions to protect the owner from any adverse effect on the marketability and value of the project.

The owner may require warranties from sub-contractors and consultants, particularly from those with design responsibility. Warranties from the contractor and design consultants are of prime importance. Sometimes it might be required to obtain such warranties from other consultants and sub-contractors alike depending on the extent of their involvement in the project execution.

Whatever the form of warranty selected the words therein must be very carefully formulated to include the correct warranties and the period. Sometimes the warranty is underwritten by insurance in which case the terms of the insurance must be meticulously inspected for exclusions or other adverse conditions set by the insurers.

The collateral warranty ensures a clear right for the owner to take action against the third parties who provide these warranties which he would otherwise be denied.

It would by now be clear that there is no difference between a guaranty and a warranty except that a warranty is a written guaranty.

Chichester Joinery Ltd v John Mowlem & Co plc (1987)

A quotation submitted by a sub-contractor was accompanied by their standard terms and conditions. The main contractor sent a purchase order containing their own standard terms which stated that 'any delivery made will constitute an acceptance of this order'. Sub-contractors delivered the work, but not until after they sent the main contractor a printed acknowledgement of order, which stated that the order was accepted 'subject to the conditions overleaf'.

Held that by accepting the joinery the main contractor had accepted the sub-contractor's conditions.