

## Phase II Concept #1: First-Party Warranty September 19, 2006

### I. Issue

House Bill 2078 directed the Task Force to review the impact of warranties on the filing of construction claims and consider recommendations regarding construction warranties. If found, the Task Force also asked about the inclusion of design defects in warranties.

### II. Current Oregon Law

Like most states, Oregon law recognizes an implied warranty of habitability. Oregon statutes also require a one-year warranty for condominium units covering defects in plumbing, electrical, mechanical, structural and all other components of newly constructed units and common elements. Additionally, Oregon law allows a contractor to record a written warranty as part of the deed when a residential or commercial structure is sold.

### III. Alternatives

The option the Task Force moved to consider was implementing a first-party warranty in Oregon. Staff found ten states that require some type of contractor warranty by statute. The attached chart, which also includes proposed legislation from the Missouri Senate, shows the range of requirements that have been included in warranty programs. Staff did not find any state laws that mandated inclusion of design defects in warranties, and American Actuarial's research indicated that design defects are normally not addressed in warranty contracts.

As the chart indicates, warranties typically address at least three issues: labor and materials, key systems, and structural damage. For labor and materials, the general trend is one year of coverage on the structure as a whole. However, Indiana requires two years, and the proposed legislation in Missouri calls for three years for new dwellings and two years for remodeling projects. First-party warranties also generally cover the "components" of a structure – e.g., the plumbing, electrical, and ventilation delivery systems. Most of the states surveyed mandated coverage for two years. States also require warranties for structural damage. The time frame varies according to each states' statute of repose, or time limit on discovery of injury or negligence. A less common requirement was coverage for consequential damages. Many of the first party warranty statutes expressly exclude consequential damages, and staff did not find examples of jurisdictions requiring coverage of consequential damages in first-party warranties.

As these examples illustrate, the common theme in these warranty laws is that specific provisions of minimum acceptable warranty coverage are clearly defined so that both contractors and homeowners understand what is covered and not covered. The Task Force also would need to determine what types of construction would be covered. If the warranty program were aligned with the definition of residential structure in the state building code, coverage would extend to detached single-family homes, duplexes, townhouses, rowhouses, and residential structures three stories or less in height. Note that this definition would exclude high-rise condominium complexes. One final point of concern is to ensure that any statutory warranty does not undermine Oregon's implied warranty protection. The Missouri legislation would have made first-party warranties in addition to any other express or implied warranties applying to the structure.

#### **IV. Enforcement**

In their report to the Task Force, American Actuarial Consulting concluded that “in order to make a builder provided warranty successful, it appears that a strict enforcement action needs to be implemented. If a mediation process has concluded and a homeowner has prevailed, there needs to be an enforcement provision compelling builders to perform the required repairs.”

The most common enforcement provision in the current program is the right to bring a breach of contract suit against the contractor if warranty obligations are not met. Six states specify this right in their warranty statutes, though it should be noted that breach of contract is typically excluded under a general liability policy.

Staff has identified four options for additional enforcement beyond breach of contract. In five states with mandated programs, a recovery fund is in place to provide relief to affected homeowners. In Maryland, non-complying contractors are subject to a \$50,000 maximum fine and up to two years imprisonment. In British Columbia, a contractor can lose his or her license for failure to comply with the mandatory program.

The fourth option builds on the current dispute resolution process through the Construction Contractors Board. This process could be expanded to cover warranty breaches, allowing the CCB access the performance bond and perhaps take other actions against contractors who fail to perform.

Finally, the law could require the mandated warranty to be recorded as a condition of closure of the sale of property under ORS 701.605.

#### **V. Steps to Implement**

A mandatory warranty program would require statutory change.

**Summary of Warranty Statutes by State**

	Labor and Materials	A/C, Plumbing, Electrical, delivery systems	Envelope defects which permit unintended water penetration	Structural	3 <sup>rd</sup> Party mandatory	Roof	Consequential Damage	Subsidence
British Columbia	1 year	2 year	5 years	10 years	yes		yes	no
Florida (a) (b)	1 year	3 years		3 years	no	3 years	no	no
Indiana (b)	2 years	2 years		10 years	no	4 years	no	yes
Louisiana	1 year	2 years		5 years	no		no	(c)
Maryland	1 year	2 years		5 years	no		yes	yes
Minnesota	1 year	2 years		10 years	no		no	(c)
Mississippi	1 year			6 years	no		no	(c)
Missouri (d) remodels	3 years 2 years	5 years		10 years 10 years	no no		no no	yes n/a
New Jersey	1 year	2 years		10 year	yes		yes	No
New York	1 year	2 years		6 years	no		n/a	n/a
Texas	1 year	2 years		10 years	no		n/a	n/a
Virginia	1 year	1 year		5 years (e)	no		n/a	yes

- (a) Statute only pertains to condominiums
- (b) Indiana may disclaim implied warranty if 3<sup>rd</sup> party warranty meeting requirement is purchased.  
In Florida 3<sup>rd</sup> party warranty is allowed as optional coverage for contractors to purchase.
- (c) Subsidence coverage required when the builder owns and sells the land on which the home is built
- (d) Missouri warranties are only proposals, no statutory warranty has been legislated at this time.
- (e) Foundation only