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THE IMPLIED WARRANTY OF HABITABILITY—CHANGING PRIVITY REQUIREMENTS

Robert G. Drummond

I. INTRODUCTION

The implied warranty of habitability in new construction is developing into an important concept to protect home buyers. The ordinary home buyer is not in a position, by skill or training, to discover defects lurking in the plumbing, the electrical wiring, or the structure itself. These defects are usually in areas that are not open for inspection.1 Home buyers, often making the largest single purchase of their lifetime, rely on the superior knowledge and experience of the builder to construct a home in a workmanlike manner that is suitable for habitation. As this reliance has grown, courts have shifted away from their historical rule of caveat emptor in the purchase of real property, and moved in the direction of finding that a builder vendor2 implies warrants the workmanlike construction and habitability of the dwelling he constructs.

The implied warranty of habitability is a theory that has only recently emerged in Montana. The purpose of this comment is to examine the genesis and development of the implied warranty of habitability in Montana and the breakdown of privity requirements between the builder vendor and the subsequent purchasers of homes. This comment also reviews and compares the standing of the implied warranty of habitability in Montana with its standing in other jurisdictions.

II. THE IMPLIED WARRANTY OF HABITABILITY IN MONTANA

The Montana Supreme Court first addressed the issue of whether a builder vendor impliedly warrants the habitability and

2. A builder vendor for purposes of this comment is an individual who is in the business of building houses designed for residential dwelling purposes upon land owned by him, and who then sells the houses, either after they are completed or during the course of construction, together with the tracts of land upon which they are situated, to members of the house-buying public. To be distinguished are cases in which a landowner hires a general contractor to erect a house on the landowners' lot, in which case liability is determined by ordinary rules of liability of an owner of land and an independent contractor and the express and implied warranties arising out of it as between the owner and the builder. Annot. 25 A.L.R.3d 383, 387 (1969).
workmanship of a new dwelling in Chandler v. Madsen. In Chandler, the court held that the builder vendor of a new home impliedly warrants that the residence is constructed in a workmanlike manner and is suitable for habitation.

The Chandlers purchased a house built by the defendant. The house began settling a short time after the plaintiffs occupied the dwelling. The house was located on moisture sensitive soil which became compressible when wet. The presence of water in the soil caused settling of the footings, foundation and other parts of the house which in turn caused extensive damage to the structure. The Chandlers experienced problems with cracking walls and floors and inoperative doors and windows. The settling caused the interior of the house to become generally unsightly.

The Montana Supreme Court followed the reasoning of the earlier Oregon case of Yepsen v. Burgess and found that the buyer is not in equal bargaining position with the seller and is thereby forced to rely on the seller’s skill and knowledge regarding the habitability of the house. The Montana court reasoned that while the doctrine of caveat emptor developed at a time when the buyer and seller were not on an equal footing, the modern world is different and the buyer is not in a position to avoid or mitigate the risks associated with the construction of a new home.


5. Chandler, 197 Mont. at 237, 642 P.2d at 1030.
7. Chandler, 197 Mont. at 239, 642 P.2d at 1031.

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seller of real estate enjoyed equal bargaining positions,\(^8\) that equality of position no longer existed and that the builder was in a better position to examine and discover defects.\(^9\) The builder, therefore, should bear the loss because he is in a better position to avoid problems linked to defects in the construction of the dwelling.

### III. Extending the Implied Warranty of Habitability

In *Degnan v. Executive Homes*\(^{10}\) the Montana court determined whether privity\(^{11}\) of contract must exist between the builder vendor and purchaser before the implied warranty of habitability becomes effective. This was a case of first impression in Montana. The *Degnan* court examined the theories underlying the implied warranty and extended it to parties who lacked privity of contract. In that case the plaintiff was the purchaser of a new home and the defendant Mora Brothers, Inc. was the builder. The plaintiff Degnan purchased the home from Executive Homes who in turn contracted with Mora Brothers, Inc. to build the home. The Degnans moved into the home shortly after it was completed by Mora Brothers, Inc. After the Degnans moved into the home, it sustained structural damage when the entire hillside upon which it was built began shifting, slowly moving downward. The foundation broke and forced the Degnans to vacate the premises. The Degnans filed suit against the sellers, selling agent, engineering firm, and builders.\(^{12}\)

The trial court denied the Degnans' motion for summary judgment because it found an unresolved issue of material fact—whether or not Mora Brothers, Inc. was a builder vendor. The court did grant a second motion for summary judgment on the issue of implied warranty of habitability.\(^{13}\) Mora Brothers, Inc., appealed, contending that the district court erred in finding that there was a breach of an implied warranty of habitability and in granting summary judgment because the parties lacked privity of contract.

The Montana Supreme Court found that an implied warranty of habitability did exist. The court relied on its earlier decision in

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8. *Id.* at 238, 642 P.2d at 1031.
9. *Id.* at 239, 642 P.2d at 1031.
11. Privity for purposes of this comment shall be defined as the connection or relationship that exists between two contracting parties.
13. *Id.* at ___, 696 P.2d at 434.
Chandler as the basis for its holding. It reaffirmed that the builder can better determine the effect, if any, of constructing a house on unstable ground. The case was analogous to Chandler in that the defects arose from constructing the house on unstable ground.

The second important issue addressed by the Montana Supreme Court was whether privity of contract is necessary for the builder vendor to be liable under the theory of implied warranty of habitability. The court found privity of contract unnecessary and held that builder vendors may be liable to subsequent purchasers under the theory of implied warranty of habitability. In doing so the court has correctly reasoned that the implied warranty of habitability does not depend upon a contract for its existence but, rather, is an idea born in tort.

In Degnan, the Appellant Mora Brothers relied upon contract theory and argued that the implied warranty of habitability extends only to parties in privity of contract. Mora Brothers relied upon an earlier Montana Supreme Court decision and stated that a party to a contract must be in privity with the party from whom he is seeking recovery. Referring to State v. District Court as it cited Hyink v. Low Line Irrigation Co., they contended the parties must occupy a contract status towards each other, and that to recover, privity of contract must exist.

The supreme court completely rejected the contract theory and found the privity argument inapplicable to the theories under which the plaintiff was attempting recovery. Mora Brothers ignored the possibility that the court would consider the warranty under tort theories. Their argument was logical, however, because the Chandler decision had suggested that the implied warranty was a contractual theory rather than a theory arising out of tort concepts.

The Degnans relied primarily upon a case handed down from the Court of Appeals of Washington in arguing in favor of extending the implied warranty to subsequent purchase of homes.

16. Id.
18. 62 Mont. 401, 205 P. 236 (1922).
19. The court stated "We agree with the Oregon Supreme Court which stated in Yepson that 'the essence of the transaction between a builder vendor and a buyer is an implicit agreement that the seller will transfer a house which is suitable for habitation.'" Chandler, 197 Mont. at 239, 642 P.2d at 1031 (citing Yepson, 269 Or. 635, 525 P.2d 1022).
The case of *Gay v. Cornwall* was similar to *Degnan*; the plaintiffs had been the first occupants of a new house, but had not purchased the dwelling from the builder. That court imposed liability on the defendant builder without regard to privity. The Degnans used *Gay* to demonstrate that Mora Brothers were builder vendors and could be held liable in the absence of privity of contract. The Montana court, however, went beyond the reasoning of *Gay*, and determined that breach of seller's implied warranty is a tort and torts do not require privity of contract.

The Montana court has joined other jurisdictions which have held that the warranty arises out of tort concepts rather than contract concepts. It recognized that while warranty exhibits characteristics of both tort and contract principles, the implied warranty is a legal duty, the breach of which is a tort. The court reasoned that torts do not require privity of contract and clarified what had proven to be a confusing concept. Its action has followed other courts that have extended the implied warranty of habitability to subsequent purchasers. Some courts, however, have limited their extension of the implied warranty and still others have refused to extend it beyond the first purchaser.

IV. Theories Underlying Extending the Implied Warranty to Subsequent Purchasers

The same logic used to extend the implied warranty of habitability to first purchasers can be used to extend the implied warranty to subsequent purchasers. The Indiana Supreme Court, in *Barnes v. MacBrown & Co.*, reasoned that lack of privity would not preclude a plaintiff's recovery on the theory of the implied warranty of habitability. That court reasoned that privity need not exist in a warranty action based on a defect in personal property. It further reasoned that the same logic which had been applied to change the common law in personal property warranty actions

21. 798, 494 P.2d at 1374.
22. The court cited PROSSER, LAW OF TORTS § 95 at 634-35 (4th ed. 1982) saying:

The seller warranty is a curious hybrid, born of the illicit intercourse of tort and contract, unique in the law. In its inception the habitability was based on tort. Thereafter the warranty gradually came to be regarded as a term of the contract of sale, express or implied, for which the normal remedy is a contract action. But the obligation is imposed upon the seller, not because he has assumed it voluntarily, but because the law attaches such consequences to his conduct irrespective of any agreement; and in many cases, at least, the language of pure fiction.

23. Degnan, Mont. at ___, 696 P.2d at 435.
could be extended to real property. The Indiana court was one of the first to recognize the requirement of privity as outmoded in real property actions. 25

Similarly, the Illinois Supreme Court found the privity requirement outmoded. It reasoned in Redarowicz v. Ohlendorf that the subsequent purchaser relies on the expertise of the builder as much as the initial purchaser. 26 Like the initial purchaser, the subsequent purchaser has little opportunity to inspect the construction methods used in building the home. The subsequent purchaser usually lacks knowledge of construction practices, and must, to a substantial degree, rely upon the expertise of the person who built the home. If construction of a new house is defective, the responsible builder vendor who created the latent defect should bear the repair cost. 27

In holding that the implied warranty extended beyond the initial purchaser of the home, the Illinois Supreme Court recognized that we are an increasingly mobile people. A builder vendor should know the house he builds might be resold within a relatively short period of time and should not expect that the warranty will be limited by the number of days that the original owner chooses to hold onto the property. The Redarowicz court, however, carefully confined its decision to latent defects which manifest themselves within a reasonable time after the purchase of the house. 28

Similarly, in its decision of Moxley v. Laramie Builders, Inc. 29 the Wyoming Supreme Court stated that the protection afforded the initial purchaser of a home should be extended to subsequent purchasers. The Wyoming Court referred to its earlier decision of Tavares v. Horstman 30 where it had stated that those who buy homes are entitled to rely upon the skill of the builder and that the house should be constructed so as to be reasonably fit for its intended use. "We can find no reason not to apply the basic concepts leading to establishment of the rules of Tavares to builders generally, and to a purchaser subsequent to the first owner." 31

The Wyoming court determined that those who hold them-

25. Id.
27. Id. at 412, 441 N.W.2d at 331. The Illinois court reasoned the public policies underlying the implied warranty of habitability should not be frustrated because of short intervening ownership of the first purchaser; in these circumstances the implied warranty of habitability survives a change of ownership.
28. Id.
30. Tavares, 542 P.2d at 1275.
31. Moxley, 600 P.2d at 735.
selves out as builders must be just as accountable for the workmanship that goes into a home that a buyer or his successor expect to occupy in the years that follow as are builder developers. It recognized the realities that homes change hands frequently and that a subsequent buyer should also be protected if he takes possession of the home a short time after the home was built. Because the home can easily reach the subsequent buyer without substantial change from its original condition, the Wyoming court extended the principals of tort to the implied warranty of habitability. It reasoned that upon manifestation of a defect, an implied warranty or a right of recovery on any other ground should not be cut off by an intervening sale.\textsuperscript{32} \textit{Moxley v. Laramie Builders}\textsuperscript{33} and \textit{Degnan v. Executive Homes}\textsuperscript{34} demonstrate the logical step of eliminating privity requirements in actions based on the implied warranty of habitability. In each case the courts treated the warranty as a tort concept rather than a contract concept.

The Indiana Supreme Court in \textit{Wagner Construction Co., Inc. v. Noonan},\textsuperscript{35} followed the reasoning of \textit{Moxley v. Laramie Builders, Inc.}\textsuperscript{36} saying:

\begin{quote}
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The purpose of the warranty is to protect innocent purchasers and to hold builders accountable for their work. With that reasoning in mind, any reasoning which would arbitrarily interpose a first buyer as an obstruction to someone equally as deserving of recovery is incomprehensible.

No reason has been presented to us whereby the original owner should have the benefits of an implied warranty or a recovery on a negligence theory, and the next owner should not simply because there has been a transfer. Such intervening sales, standing by themselves, should not, by any standard of reasonableness, effect an end to an implied warranty or, in that matter, a right of recovery on any other ground, upon manifestation of a defect. The builder always has available the defense that the defects are not attributable to him.\textsuperscript{37}
\end{quote}
\end{quote}

The \textit{Wagner} court went on to hold that five years was not an excessive period of time for the latent defect to manifest itself.\textsuperscript{38}

The Colorado Supreme Court considered the extension of the

\begin{itemize}
\item \textsuperscript{32} \textit{Id.}
\item \textsuperscript{33} \textit{Moxley}, 600 P.2d 733.
\item \textsuperscript{34} \textit{Degnan}, ___ Mont. ___, 696 P.2d 431.
\item \textsuperscript{36} \textit{Moxley}, 600 P.2d 733.
\item \textsuperscript{37} \textit{Wagner Constr. Co.}, 403 N.E.2d at 1144 (citing \textit{Moxley}, 600 P.2d 733).
\item \textsuperscript{38} \textit{Wagner Constr. Co.}, 403 N.E.2d at 1148.
\end{itemize}
warranty to parties not in privity in *Eldon v. Simmons.* The *Eldon* court extended the implied warranty of habitability to subsequent purchasers. The court reasoned that a manufactured product placed in the chain of distribution may literally pass through dozens of hands before it reaches the ultimate consumer. When the ultimate consumer finds the product to be defective, it makes little sense to limit him to redress against his immediate vendors. If such were the case, the consumers immediate vendor, if he were to have the full benefit of his bargain, would have to sue his immediate vendor, who would in turn have to sue his vendor, and so on up the chain, until the party ultimately responsible for placing a defective product in the market is reached. "It defies common sense to require such an endless chain of litigation in order to hold the party at fault responsible." The Colorado court compared the purchase of a home with the purchase of any personal property. It reasoned that warranties that extend to personal property should also apply to homes.

A different approach was used by the Texas Supreme Court in *Gupta v. Ritter Homes.* That court stated that as between the builder and owner, it does not matter whether there has been an intervening owner. The effect of the latent defect is just as great on a subsequent buyer and the builder is no more able to justify his improper work as to a subsequent owner than to the original buyer. The *Gupta* court went on to reason that the implied warranty of habitability and good workmanship, implicit in the contract between the builder vendor and original purchaser, is automatically assigned to the subsequent purchaser.

In citing its approval of extending the implied warranty of habitability to subsequent purchasers, the Arkansas Supreme Court expressly held that the warranty extends to subsequent purchasers for a reasonable length of time. The Arkansas court, however, limited the extension of implied warranty to a reasonable length of time where there is no substantial change or alteration in the condition of the building from the original sale.

In extending the implied warranty of habitability to subsequent purchasers, the New Jersey Superior Court in *Hermes v.*

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40. *Id.*
41. *Gupta,* 646 S.W.2d 168.
42. See *Thornton Homes Inc. v. Grevner,* 619 S.W.2d 8 (Tex. 1981). *Gupta* expressly overruled an earlier Texas Court of Appeals decision holding that the implied warranty of habitability did not apply in cases where the house was "used." *Gupta,* 646 S.W.2d at 169.
44. *Id.* at 187, 612 S.W.2d at 322.
Staiano reasoned that the builder vendor was in a better position to prevent the occurrence of major problems. The builder knows that the systems will remain hidden to initial as well as subsequent purchasers. Anyone else who purchases the home will rely upon the skill and experience of the builder vendor to construct the home in a workmanlike manner. The Hermes court recognized that often defects will not be revealed for several years after the house is first occupied. The effect of a defect in the systems is felt by the subsequent purchasers who should be protected by the implied warranty of habitability.

V. IMPLIED WARRANTY ARISING OUT OF CONTRACT

Some courts have held that the implied warranty of habitability and fitness arises from the contractual relation between the builder and the first purchaser and therefore does not extend to subsequent purchasers. For example, the Alabama Supreme Court has continually refused to extend the implied warranty of habitability beyond the original parties to the contract. In its ruling in Cooper & Co., Inc. v. Bryant, the court ruled there is no implied warranty of habitability in the resale of used homes. Citing its earlier decision of Ray v. Montgomery, the court determined that the doctrine of caveat emptor still applied to the sale of used homes. The Alabama court is joined by several courts which have recently held that privity of contract is essential to recover under the implied warranty.

These views are distinguished from the view of the Montana Supreme Court as expressed in Degnan. Those courts rely on contract principles as the basis of their decisions and carve out exceptions based upon the unique circumstances of those cases. Prior to Degnan, the Montana Supreme Court indicated that contract principles applied in implied warranty actions. A majority of courts, however, limit recovery under the warranty to the first purchaser-occupant of the house. This limitation is rooted in the view adopted by the Montana Supreme Court in Chandler, that the

46. Id.
47. 400 So. 2d 1016, 1018 (Ala. 1983).
48. 399 So. 2d 230 (Ala. 1983).
50. Degnan, Mont. at 239, 696 P.2d at 431.
51. Id.
52. Chandler, 197 Mont. at 239, 642 P.2d at 1034.
warranty of habitability arises from a contract and is subject to traditional contract principles. Privity is one such principle which most courts are not willing to stretch beyond the first purchaser. 53

V. CONCLUSION

In Chandler, 54 the court only acknowledged the existence of the implied warranty and the fact that the theory of caveat emptor had become outmoded. The Chandler opinion implies that contract principles would apply to the warranty. Degnan represents a turnabout from that stance. The Montana court in Degnan recognized and addressed the confusion regarding whether the implied warranty is a tort or contract concept, and in so doing has correctly extended the implied warranty of habitability to parties not in privity of contract. This is significant where a subsequent purchaser, rather than the original vendee, seeks recovery premised upon the implied warranty. 56 The Montana Supreme Court has cut through the confusion and correctly applied tort concepts to the warranty. The application of tort concepts should allow subsequent purchasers to recover in actions for breach of the warranty. In doing so the Montana court has also opened the door for new disputes in the future. The court left open the issues of what length of time would be appropriate for application of the implied warranty to subsequent purchasers. While several jurisdictions have simply held that the standard of reasonableness will apply in limiting the time in which latent defects must manifest themselves, the Montana court in Degnan did not have to deal with the issue of how long after construction of the home the builder vendor remains liable for latent defects. "The issue of who may recover under the warranty will depend on the duration of the warranty which in part depends on the nature of the defects." 57 A logical conclusion would allow recovery by subsequent purchasers for latent defects that manifest themselves within a reasonable time after construction. While the case of Degnan is not the typical case which would demonstrate that the implied warranty would be ex-

55. Id.
57. Id.
59. Toole and Habein, supra note 54, at 166.
60. Degnan, ___ Mont. ___, 696 P.2d 431.
tended beyond the parties to the contract, the court made it clear that the implied warranty will be treated as a tort concept rather than contract concept, thereby allowing extension to persons not in privity of contract.