Implied Warranties in Hot Water

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An Ontario court finds that implied warranties associated with leased products apply not only at the outset of the term of the lease, but for its entirety.

The Ontario Divisional Court in December 2011 released its decision in two appeals involving property damage caused by the failure of leased hot water tanks[1]. In each case, the hot water tank located in the homeowner's basement developed a leak that resulted in damage to the home and its contents.

The appeals raised a number of issues relating to implied warranties in lease agreements: the application of the *Consumer Protection Act*; the time period during which the implied warranties were operative; the time period during which the product was defective; the differences between sale and lease agreements; and the duty to warn.

The decision is one of considerable importance, and not just because literally hundreds — if not thousands — of similar claims awaited the outcome. Essentially, the court ruling confirms that implied warranties associated with leased products apply not only at the outset of the term of the lease, but for its entirety.

A lessor, in other words, has an obligation to supply a safe and properly functioning product in each and every lease payment period, and will be liable for loss or damage resulting from a breach of that obligation, regardless of how far into the lease term that might occur.

BACKGROUND

The hot water tank in the *Collett* claim was 19 years old at the time of loss. In the *Szilvasy* claim, it was 10 years old. The tanks had each been leased for a considerable period of time. The plaintiffs in each case — Geoffrey and Sandra Collett in *Collett*, and Shirley Szilvasy in *Szilvasy* — had assumed their leases from previous homeowners. Evidence at trial indicated it was virtually impossible to detect internal corrosion that ultimately led to the failure and loss of the tanks. Also, there was no practical way of maintaining the product to prevent the type of failure that occurred.

It was common ground among the parties that no written agreement set out the terms and conditions of the lease. However, the presence of a written contract would not have made any difference given the provisions of the *Consumer Protection Act*. That statute extends the application of the statutory implied warranties of fitness for

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intended purpose and merchantable quality that are mandated by Section 15 of the *Sale of Goods Act* to goods that are leased or otherwise supplied under a consumer agreement.

The *Consumer Protection Act* also renders void any contract term that purports to negate or vary any implied condition or warranty under the *Sale of Goods Act*. Section 9(1) of the *Consumer Protection Act* adds a warranty that the services supplied under a consumer agreement are of a "reasonably acceptable quality." It should be noted, however, that the protection provided by the *Consumer Protection Act* extends only to "consumer transactions," which the act defines to mean "any act or instance of conducting business or other dealings with a consumer, including a consumer agreement," and is limited to instances in which the consumer or the person engaging in the transaction with the consumer is located in Ontario when the transaction takes place.

The lessor, Reliance Home Comfort, initially took the position that the *Consumer Protection Act* did not apply to these cases, because the act came into force well after the start dates of the two leases. At the court hearing, however, Reliance conceded that the act did apply because the failures and the losses occurred while the act was in force.

THE COURT'S FINDING

In the Small Claims Court decision from which the appeals were taken, the court held the implied warranty of fitness continued with each monthly lease payment as a new starting point. Reliance disagreed, arguing that the implied warranties applied at the start of the lease term and continued only for a reasonable period thereafter; they were no longer in place 10 and 19 years respectively after the installation of the tanks, as was the case in these claims.

The divisional court made the critical finding that "reasonableness" lay at the heart of the issues before the trial judge. The judge had to decide, in a consumer context, what it meant to provide goods of a "reasonably acceptable quality" in the circumstances before him.

The court said Reliance promised to provide the homeowners with a working hot water tank at all times. If the tank failed, Reliance undertook to replace it. If it required service, Reliance provided it. There was no meaningful way to differentiate between Reliance's contractual obligations on the basis of the age of the tank. Given Reliance's acknowledged contractual obligation to provide a working hot water tank at all times, it would be illogical to conclude that there was not a continuing warranty as to the proper functioning of the tank.

This decision is important in all claims involving loss or damage from the failure of leased products in which warranties are implied either by the *Consumer Protection Act* or under the common law. The decision stands for the proposition that unless the contract provides otherwise (and is capable of so providing[2]), those implied warranties will be effective throughout the term of the lease, regardless of how much time has passed since the start of the lease, and not just during some relatively short period of time after the start date. In other words, a lessor has an obligation to supply a safe and properly functioning product in each and every lease payment period. The lessor will be liable for loss or damage resulting from a breach of that obligation, regardless of how far into the lease term that might occur.

Although no product can last forever, lessees are entitled to assume — and to rely on the lessor's implied assurance — that a product will be reasonably fit and safe for use during the period of time that the lessor leaves the product with the lessee and charges lease payments. Lessees are entitled to rely on the lessor to tell them when the time has come to replace a leased product, such as a hot water tank. In this instance, Reliance had knowledge and experience regarding the nature of and deficiencies associated with the tanks it leased to its customers. Therefore, the court concluded, Reliance should have decided when to take leased tanks out of operation and replace them with new tanks. Apart from the implied warranties, Reliance was not entitled in the circumstances to transfer the risk of loss to its customers, the court found.

McCague Borlack LLP lawyers Hillel David and Mark Mason represented the plaintiffs (respondents) in these subrogation claims in the Divisional Court.

1 Collett v. Reliance Home Comfort; Szilvasy v. Reliance Home Comfort, 2011 ONSC 6928 (Div. Ct.). These appeals were heard together in the Ontario Divisional Court.

2 There are certain limitations to the application of the Consumer Protection Act and therefore to the agreements for which there will be a prohibition against the removal or limitation of implied warranties.