

Quality knows *no borders*

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CONSTRUCTION PAPERS



Complying with more than just the contract?

There are two useful phrases that help avoid all sorts of construction disputes: express and implied technical specifications.

In the first article of a four-part series, we discuss what contractors should pay attention to in the examination of the technical specifications of construction contracts. We also address the distinction between express and implied specifications. The article will also discuss contractors' liabilities and obligations associated with design flaws, non-excluded standards, and the principles of reasonable expectations and fitness for the purpose. We will also analyse the key characteristics of guarantee and warranty liabilities. Finally, we will make a few proposals that might help you avoid disputes involving technical specifications, both during contracting and when the enforcement of claims is sought.

Express and implied specifications

- [1] A contractor must perform all works that are expressly stated and listed in the contract, and typically in the performance and prescriptive specifications ("express specifications"), as well as those that are necessary to perform the listed items and/or indispensable for the use of the facility for the purpose intended, without being specifically listed ("implied specifications").

In addition to the contract, some of the express specifications are stated in the design and technical documentation. As the analysis of any technical documentation is primarily an engineering matter, the only legal dilemma that usually arises in this regard is the scope of the requirement for contractors to assess the design documentation and to recognise any flaws in the designs.

Matters associated with implicit specifications tend to generate more disputes and are usually rooted in the same question: can requirements that were never specified

but are demanded by the developer after the start of the construction (standards, quality requirements, requirements deriving from the Taxonomy Regulation, etc.) become a part of the contract? To put it another way, the question is what matters should the contractor understand to be included in the contract without being specific listed. Before digging deeper, it is important to note that once a contract is in place, the developer cannot make additional requirements that go beyond the fitness for purpose standard.

Issues associated with express specifications

- [2] **Contractor's obligation to review designs and discoverability of design flaws.** The contractor has an obligation to review, before the contract is signed, the design documentation delivered by the developer, and warn the developer about all visible design flaws. If a design flaw is discovered during the construction phase, the contractor is required to inform the developer about immediately. **The contractor must review the design documentation with the due care reasonably expected from a specialist** (Supreme Court, judgment GK 54).
- [3] *Design flaws that the contractor cannot be reasonably expected to identify: The standard of due care does not mean that the contractor should carry out engineering calculations to verify the correctness of the design.* Based on this principle, courts ruled that contractors were not expected to identify the following design flaws:
- The contractor cannot be faulted for implementing a flawed design if the identification of the design flaw requires a calculation that it does not have an obligation to perform (judgment BH1983. 207).
 - For example, judgment BH1984. 366 held that *only the designer was solely liable for flaws stemming from heat transfer calculations*, and such flaws could not serve as the basis for joint liability for damages with the contractor. According to the facts of the case, the structure had thermal bridges along various concrete beams. Another design flaw was that dry plaster was used in indoor areas. The court ruled that the identification of both flaws would have required heat transfer calculations that were not within the scope of the contractor's design review obligations.
 - In judgment BH1984. 234, the court held that the contractor *did not have to recognise the design flaw*, because it *could only have been discovered with detailed heat transfer and vapour diffusion calculations*.
- [4] *Design flaws that the contractor must be able to identify:*
- According to judgment BH2021. 257, a contractor specialising in the construction of homes should have realised that the structure of the building should have been reinforced due to the *low structural integrity of the adobe bricks* used in the construction. Another important aspect is that this recent judgement (also) treated the developer as a non-expert, and therefore the contractor cannot argue that the developer could also have discovered the flaw due to their expertise – even if this could be a reasonable expectation for a developer.
 - Judgment BDT2016. 3426 is interesting in that the contractor in the case, in compliance with its obligations, warned the developer about *waterlogged undersoil, and proposed soil replacement as a solution*. The developer ordered the soil replacement as extra work. However, if the contractor believed that the soil was

still *unsuitable for bearing the load of the tracks* even after the replacement, it should have warned the developer again, but it did not comply with that obligation.

- The court held in judgment BDT2021. 4326 that the contractor should have recognised that *track height should have been raised* and an adaptation plan should have been prepared *due to high soil water levels*, and it should have warned the developer about the same.

If the contractor discovers a flaw in the design documentation, it must inform the developer about it. It follows from this general rule that the contractor must warn the developer if it gives an unfeasible or technically wrong instruction. If the developer still insists on proceeding with the instruction or the flawed design documentation, the contractor may choose to rescind the contract or perform the work in accordance with the developer's instructions and at its risk. However, the contractor must refuse to perform an instruction if it would result in the violation of a statute or a regulatory resolution, or jeopardise any third party's life, limb or property. [Civil Code, Section 6:240,(2)]

- [5] **Specified standards.** The standards specifically listed in the construction contract are incorporated into the technical specifications. If a listed standard and the technical specifications do not match or contradict each other, the main rule says that the specific requirements will override general ones. However, it is always a good idea to request information from the developer if there is any doubt about the interpretation of the technical specifications.

Issues associated with implied specifications

- [6] **Standards not excluded by the parties are incorporated into the contract.** In the past, there was a distinction between mandatory and non-mandatory standards, but the application of standards cannot be statutorily mandated since 1 January 2002. However, this does not mean that standards cannot become a part of the contract – they can, even without a specific contractual provision.

Non-mandatory standards operate in the same way as permissive statutes: parties may deviate from them or exclude their application. However, if this is not done, standards that are widely used in the given industry will be incorporated into the contract without a specific provision.

This follows from Section 6:63(5) of the Civil Code, which states that all of the customs that the parties agree on, and all of the practices that they develop, in their business relationship will be incorporated to the contract that is in place between them. The contract will also include practices that would be considered generally applicable and widely known by parties to similar contracts in the given industry, unless the application of such practices would be unreasonable between them in the light of their earlier business relationship.

Therefore, if the practices that are developed by the parties or generally used on the market include the application of a standard (which is otherwise not mandatory), that standard will be incorporated to the contract without a specific provision. It might even be sufficient if the parties regularly use the rules of a particular standard as a guideline in their disputes concerning quality requirements, and their declarations make it clear that they apply such rules.

- [7] **Relevant statutes are also incorporated into contracts.** It is important to note that the provisions of all relevant statutes will become a part of a contract even if the parties do not state this expressly in it. Under the main rule, the application of statutory provisions may not be excluded (unlike standards). Certain permissive rules in the Civil Code are an exception, because the parties can modify them or rule out their application – on the other hand, if this is not done expressly in the contract, they will become a part of the contract just as any other provision. As far as technical specifications are concerned, the most important permissive rule is Section 6:123 of the Civil Code, which defines a general standard for the quality of contractual performance. If the parties want to deviate from the standard level of quality, for example because the developer wants to implement a lower quality (and therefore cheaper) solution, this must be clearly and expressly stated in the contract. If the contract does not state that Section 6:123 will not apply, the contractor's performance will have to meet the general standard of fitness for purpose. Consequently, whatever the contractor supplies must be fit for purpose, if the developer stated that purpose to the contractor before the contract was signed. It must also be fit for the purposes for which similar services are generally used. Additionally, it must be of the quality and have the same performance characteristics that similar services have and that the developer can reasonably expect in the light of public statements made by the contractor or, if the service is supplied by someone else, by the actual supplier, about the specific characteristics of the service. The service must have the attributes that are stated in a description delivered by the contractor, or otherwise must match the attributes of a service that was presented by the contractor to the developer as a sample. Finally, it must meet the quality requirements specified in any applicable regulations.
- [8] **Standard of reasonable expectations and use for the purpose intended.** In broadest sense, Section 6:123 of the Civil Code states the quality requirements that must be met in the performance of a contract. Additionally, the customary practices and expectations that prevail in the relevant industry or market will also have a role in determining the conditions that the developer can reasonably expect the contractor to meet without an express contractual stipulation (as long as the same are not expressly excluded). It is important to note that according to court opinion 1/2012. (VI. 21.) PK, a service can still be flawed if no specific standard or requirement applies to its quality at all, and it meets the relevant contractual provisions and statutory requirements but it is not fit for purpose, i.e. it is otherwise flawed. Therefore, if the flaw in the service can in fact be established on the basis of the principle of reasonable expectations, it is not necessarily advisable for the contractor to restrict its defence to claiming that there is no applicable statutory requirement or standard or that not statutes were violated.
- [9] *The requirement to ensure fitness for purpose* imposes a similar requirement on contractors and creates a similar dilemma for them. In addition to all specifically listed works, a contractors must also carry out all other works that are needed in order for the relevant facility to be fit for its intended purpose. The question of what exactly is included in the meaning of fitness for purpose and what conditions should be met to ensure it can be a minefield of varying interpretations and misinterpretations, which is best avoided by defining the technical specifications as accurately as possible. The situation can be made worse if the developer does not commission a stand-alone facility but orders the construction of a part of facility and completes the rest itself.

When this is the case, special attention should be paid to the statement of activities and the technical specifications, and to the conditions that must be met for the contractor's part of the facility to function properly (in conjunction with the rest completed by the developer itself). It is also advisable to make warranty and guarantee clauses more detailed to adequately reflect the allocation of tasks. For example, it is a good idea to state that the contractor warrants that its own part will only be fit for purpose if the rest of the facility is properly completed by the developer.

Proving flaws / flawlessness

[10] **Warranties and guarantees.** If a contractor's performance is flawed, it has a warranty or guarantee obligation. The warranty or guarantee obligation can be based on the contract or on a statute. In the case of a contract-based obligation, the relevant details will be determined by the contract: the deadlines for making complaints and repairs, the claims that can be made and terms of how they can be made. If a contract does not include provisions on a particular matter, the situation can be resolved on the basis of the general warranty / guarantee rules stated in the Civil Code. In the case of a statutory obligation, the rules will be determined by the relevant statute. These rules tend to focus on specific details, and therefore any gaps will be filled by the general provisions of the Civil Code. Section 6:159 (2) of the Civil Code defines general warranty claims as follows, (and the definition also applies to guarantees, *mutatis mutandis*): the obligee has the option a) to choose either repair or replacement, unless compliance with the chosen warranty right is impossible or would result in disproportionate expenses on the part of the obligor as compared to the alternative remedy, taking into account the value the service in a flawless state, the significance of the non-performance, and the harm caused to the obligee upon compliance with the warranty right, or b) to ask for a commensurate reduction in the consideration, repair the flaw or have it repaired at the obligor's expense, or to rescind the contract if the obligor refuses to provide repair or replacement or is unable to fulfil that obligation within the applicable deadline and without harming the obligee's interests, or if the obligee no longer has interest in the repair or replacement.

[11] **Distinction between warranties and guarantees:**
The key difference between a warranty and a guarantee is in the burden proof, which is to say that in the case of a warranty, the developer has to prove that the performance was flawed, while in the case of a guarantee (if a flaw is discovered), the contractor has to prove that its performance was flawless.

In the case of a *warranty-based claim* the developer will have to prove that the flaw existed at when the contractor performed its service. For the contractor, on the other hand, it might be sufficient to demonstrate other causes beyond its control that could also have resulted in the flaw. If it is plausible that such alternative causes may have contributed to the existence of the flaw, the contractor might be able to successfully defend itself against the developer's warranty claim. In summary, in the case of a warranty, the developer is responsible for the assessment of the flaw, for the identification of its causes and, generally, for the presentation of the relevant evidence.

The situation is reversed when it comes to guarantees: if the developer identifies a flaw, the contractor will be liable for the flaw until it proves

otherwise. The contractor can only be exempted from the liability if it proves beyond reasonable doubt that its service was not flawed at the time when it was supplied, and the cause for the flaw is not rooted in its performance but in some other, post-performance cause that was beyond its control and that can be clearly identified. Consequently, it is not sufficient to claim that the flaw could have been caused by some other factor; in fact, the contractor will not be exempted if the cause for the flaw cannot be identified. With regard to guarantees, any uncertainty concerning the evidence will be held against the contractor.

Examples for difference in the burden of proof in the case of warranties and guarantees: If the developer discovers water damage in a facility built by the contractor but cannot identify its cause, the parties' position in a dispute will be radically different depending on whether the rules of warranties or guarantees apply. In the case of a warranty, the developer will not win the case just by identifying the problem (water damage). If it cannot prove the existence of a specific cause (such as a problem in the roofing), its warranty claim will be denied. A lawsuit brought by the developer can also be rejected if the contractor offers convincing evidence that the water damage could have equally been caused by the mismanagement of maintenance tasks. In contrast, in the case of a guarantee, both of the situations described above will result in the contractor losing the case if it cannot prove that the water damage was not a result of a flaw in its performance. In order to avoid that fate, it will have to prove in some way that its performance was flawless or that the flaw was solely attributable to a cause beyond its control, such as inadequate maintenance. Consequently, it will not be enough for the contractor to prove that maintenance problems may have contributed to the water damage, it will have to demonstrate that such problems were the only cause of the damage.

Finally, it is worth noting that the contractor will have a guarantee liability if it expressly agrees to it or if it is imposed on it by a statute. If neither is the case, the contractor will not have a guarantee liability. This is in contrast with the warranty liability, which, under the Civil Code, will generally apply to the party that has the relevant obligation under a contract that imposes obligations on both parties, such as a construction contract.

- [12] **Statutes that impose mandatory guarantee and warranty obligations:** Mandatory guarantee applies to certain structural elements and the installation of the same in newly built apartments, homes and public facilities under Government Decree No. 181/2003. (XI. 5.) on mandatory guarantees in home construction. Mandatory warranty applies to structural elements and equipment, whether pre-fabricated or fabricated on site, in path-like structures and facilities, and to certain products and materials used in the fabrication, under Joint Decree No. 12/1988. (XII. 27.) of the Ministry of Construction and City Development, the Ministry of Industry, the Ministry of Commerce, the Ministry of Agriculture and Food, and the Ministry of Environmental Protection and Water Management on the mandatory useful life of certain path-like structures.

OUR RECOMMENDATIONS

The correct description of the technical specifications is the best way to avoid disputes in the contracting phase

- [13] **Detailing the specifications:** Most disputes arise from misunderstandings surrounding the technical specifications of a contract. For example, when there is a dispute about extra work, the parties usually disagree about whether the relevant works were part of the contract from the outset. On the other hand, in warranty-related disputes, misunderstandings tend to be associated with required level of quality. Therefore, the accurate determination of the parties' obligations and the technical specifications is very important during the contracting stage. In this regard, the most important issue, as discussed above in greater detail, is that the contractor has to implement more than what is expressly stated in the contract. It is required to carry out any other work that are necessarily part of the relevant facility or the listed tasks, or that are necessary to meet all non-excluded standards, and the requirements of reasonable expectations and fitness for purpose. The question of what the contract implies in the developer's mind and in the contractor's mind will always create uncertainties, which tends to expose the contractor to risks. Uncertainties involving technical specifications are usually seen as a liability for the contractor; for example, if a provision is ambiguous in terms of the required quality, the contractor is typically expected to perform the relevant task at a higher level of quality.
- Consequently, contractors have a strong interest in eliminating uncertainties and regulating the underlying matters expressly and clearly. Requesting a specific declaration from the developer can be an effective strategy** – for example about the developer's choice between two possible solutions that both meet the specifications. It is advisable for the contractor to have a **record of the uncertain interpretation**, its own interpretation of the issue, and the fact that it contacted the developer in connection with the matter. Documenting the developer's response or the lack thereof is also a good idea.
- [14] **Managing risks associated with standards:** As noted above, standards that are not excluded may become a part of the contract. Therefore, it is eminently possible that the developer will demand satisfaction of a standard that the contractor never reckoned with; whereas in a lawsuit, a forensic expert and the court will examine the contractor's performance in the light of that standard. In order to avoid such risks, it might be useful to specifically and exhaustively list all standards that the contractor agrees to meet. If possible, it is worthwhile to list every standard that is excluded, or otherwise use language that makes it clear that only the listed standards are to be applied.

Treatment and examination of flaws

- [15] As discussed above, in the case of a warranty the developer must prove that the contractor's performance was flawed, i.e. that the cause for the flaw existed at the time of the performance. On the other hand, the contractor might be exempted from the warranty obligation if it cites (with evidence) alternative causes for the flaw that are beyond its control, such as poor maintenance. Judgment BDT2001. 538 is a good example for what role alternative causes can play: the court held that the client should have provided evidence that the causes for the relevant flaws were part of the machinery at the time of the performance. This had relevance because the flaws could also have been the result of the client's use of the machinery. Consequently, the client should have proved that the flaws did not arise because the machinery was not used for the purpose intended.

Consequently, it can be a useful strategy for contractors to identify and present alternative causes for a flaw. Obviously, it will only strengthen the contractor's position if it can show that its performance was not flawed and the cause for the flaw did not exist at the time of its performance.

[16] In the case of guarantees, the contractor is required to prove that the flaw arose after its performance, and therefore citing alternative causes that are beyond its control will not be sufficient. The contractor will not be exempted from liability even if the specific cause of the flaw cannot be established, whether because the unavailability of the required technology or the passage of time (BH2015. 62.). Similarly, simply listing potential causes is insufficient; the contractor will have to demonstrate the existence of a specific cause for the flaw that is unrelated to it. The contractor will also not be exempted from liability if the cause of the flaw could not be discovered at the time with state-of-the-art technology (BDT2016. 3492.).

In the case of a guarantee, every uncertainty will be held against the contractor, and therefore the contractor should document its performance and examine complaints about flaws as thoroughly as possible so that it can prove beyond doubt that its performance was flawless or that the flaw cited by the developer was due to a cause beyond its control. **For these reasons, documenting structural elements that are covered up is particularly important.**

[17] It is advisable to give a detailed account of the method used to examine the flaws, what flaws were discovered, what potential causes were identified and what actions the parties agreed to take in order to eliminate the flaws. It is a good idea to record these matters in writing so that any misunderstandings and issues can be later clarified easily.

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