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***"IGNORANCE IS NO EXCUSE: ACCEPTANCE BY OWNER,  
BY OWNER'S AGENT OR BY FAILURE TO INSPECT AS A  
BAR TO PERFORMANCE CLAIMS."***

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## **"IGNORANCE IS NO EXCUSE: ACCEPTANCE BY OWNER, BY OWNER'S AGENT OR BY FAILURE TO INSPECT AS A BAR TO PERFORMANCE CLAIMS."**

We are all too familiar with situations in which an owner/obligee of a bond has failed to inspect work performed by a contractor, or has inspected and failed to find any obvious defects in the work, and accepts it, only later to claim some of the work on the project is defective. In substantially all jurisdictions, the obligee can still demand performance under the bond if the defect is found by the trier of fact to be latent. In the majority of jurisdictions, however, an obligee cannot make a successful claim under the bond if the defect is found to be patent, i.e., one that is discoverable by reasonable inspection, and the owner or the owner's agent has conducted an inadequate inspection or no inspection. However, at least one jurisdiction, Illinois, permits obligees to make a claim for patent defects as long as the obligees have not expressly accepted the defects.

Naturally, the obligee, after accepting a patent defect, always alleges that the defect is latent in an attempt to absolve himself of responsibility. In a perfect world, the courts would uphold the general rule that acceptance of a patent defect absolves the bonded principal-- and the surety -- from liability. Unfortunately, this is not a perfect world, and the courts are often willing to carve out exceptions to reach the results they want. An examination of these concepts and some examples from various jurisdictions will illustrate the extent of the problem for the surety, and hopefully expose some of the more common pitfalls encountered in trying to bind an obligee to its acceptance of a patent defect.

### **I. Latent Defects**

The general rule is that an obligee cannot be held responsible for accepting work which contains defects which the trier of fact determines are not detectable by reasonable inspection.<sup>1</sup> In other words, an owner may make a performance bond claim for defects appearing after acceptance if they would not have been discoverable by reasonable inspection. Such defects are, by definition, latent.

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<sup>1</sup> See, e.g., *Dial v. Graves*, 351 So.2d 598 (Ala. Civ. App. 1977); *Phenix-Georgetown v. Chas. H. Tompkins Co.*, 477 A.2d 215 (D.C. 1984); *Forte Towers South, Inc. v. Hill York Sales Corp.*, 312 So.2d 512 (Fla. 3d DCA 1975); *Savannah Indus. Constructors v. Sumner*, 375 S.E.2d 486 (Ga. Ct. App. 1988); *Five M. Palmer Trust v. Clover Constr.*, 513 So.2d 364 (La. Ct. App. 1987); *Foley v. Horton*, 780 P.2d 638 (N.M. 1989); *Trenton Constr. Co., Inc. v. Straub*, 310 S.E.2d 496 W. Va. 1983); *Stevens Constr. Corp. v. Carolina Corp.*, 217 N.W.2d 291 (Wis. 1974).

In *Trenton Construction*, for example, a building contract called for a visqueen vapor barrier to be installed under the flooring.<sup>2</sup> After construction was completed and the work accepted by the owner's architect, the owner began to experience problems with moisture in several areas of the home.<sup>3</sup> In the process of relocating certain bathroom fixtures, the owner removed parts of the flooring and discovered that the visqueen barrier was not present.<sup>4</sup> Core samples taken from other parts of the house revealed that the visqueen barrier was never installed.<sup>5</sup> The contractor sued for enforcement of its mechanic's lien and the owner counterclaimed against the contractor for breach of contract.<sup>6</sup> The contractor claimed that the architect's acceptance of the work waived any claim for the failure to install the visqueen, but the West Virginia Supreme Court found that "damages may be recovered for concealed defects which could not have been discovered by due diligence even after the owner (or his agent) have accepted the completed construction and approved of all work as having been done in a workmanlike manner."<sup>7</sup>

Similarly, in *Foley v. Horton*, the buyer of a home sued the contractor for breach of contract after the house became structurally unstable.<sup>8</sup> The evidence adduced at trial revealed the contractor had used green timbers in the construction of the house which warped as they dried.<sup>9</sup> The contractor argued that the acceptance of the house effectively waived such a claim, but, the court found:

[t]hese defects were not readily identifiable to the [owners], but became known over time. We have previously held that if defects are latent, acceptance does not constitute waiver...Since substantial evidence showed the defects in the house were latent, we affirm the trial court's rejection of [the contractor's] requested findings on waiver.<sup>10</sup>

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<sup>2</sup> 310 Se.2d at 497.

<sup>3</sup> *Id.* at 498.

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> *Id.* at 497.

<sup>7</sup> *Id.* at 499 (citing *Steinbrecher v. Jones*, 153 S.E.2d 295 (W. Va. 1967)).

<sup>8</sup> 780 P.2d at 638.

<sup>9</sup> *Id.* at 639.

<sup>10</sup> *Id.* at 639 (citations omitted).

Accordingly, as a general rule, if the defect is latent and not detectable to the owner, no claim is waived against the contractor for defective work merely because the owner accepts the work.

## II. Patent Defects

The majority of cases dealing with the classification of a defect, however, are not so clear cut and the factual issue of what is or is not a patent defect can become contentious. Generally, if the defect complained of is so obvious that a reasonable inspection would have uncovered it, then the contractor is absolved of liability for that defect because of the owner's acceptance. Courts in some instances have recognized that the standard of reasonableness might be relative to the knowledge and experience of the owner or his agent. In at least one jurisdiction, acceptance of the defect must be express, and we will also see some examples of this concept being stretched too far, where the court rules in favor of the owner strictly on the basis of the insufficiency of the contractor's performance.

### A. The General Requirement of a Reasonable Inspection

In order to uphold a claim for defective performance, most jurisdictions require that a defect must not be discoverable by a reasonable inspection.<sup>11</sup> One court has defined the test of whether a defect is patent as, "not whether a particular condition is obvious but whether the defective nature of the condition is obvious with the exercise of reasonable care."<sup>12</sup> In *Mastor*, after accepting the work of a contractor for the construction of a bowling alley, the owner filed suit against the contractor when an engineer's inspection revealed that the project was riddled with defects.<sup>13</sup> Despite the general rule, the court, finding that an issue of material fact existed as to whether the owner had actually accepted the work, reversed summary judgement on behalf of the contractor.<sup>14</sup>

Similarly, in *Florida Ice*, a Louisiana appellate court held "the law is settled that even if defects or omissions and the costs of repairing them are proved by an owner or contractor, he is nevertheless barred from recovering the costs of the defects or omissions if he accepted the

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<sup>11</sup> See, e.g., *Phenix-Georgetown v. Chas. H. Tompkins Co.*, 477 A.2d 215 (D.C. 1984); *Mastor v. David Nelson Constr. Co.*, 600 So.2d 555 (Fla. 2nd DCA 1992); *Eastover Corp. v. Martin Builders*, 543 So.2d 1358 (La. Ct. App. 1989); *Florida Ice Machine Corp. v. Branton Insulation, Inc.*, 290 So.2d 415 (La. Ct. App. 1974); *Spartan Mech. v. St. Paul Fire & Marine*, 414 N.W.2d 476 (Minn. Ct. App. 1987); *Lindsay Mfg. Co. v. Universal Sur. Co.*, 519 N.W.2d 530 (Neb. 1994); *Stevens Constr. Corp. v. Carolina Corp.*, 217 N.W.2d 291 (Wis. 1974).

<sup>12</sup> *Mastor*, 600 So.2d at 557 (citing *Kala Inv., Inc. v. Sklar*, 538 So.2d 909 (Fla. 3rd DCA 1989)).

<sup>13</sup> *Id.* at 556.

<sup>14</sup> *Id.* at 557.

work despite patent defects or imperfections discoverable upon reasonable inspection."<sup>15</sup> In that case, a contractor filed suit against one of its subcontractors for the latter's faulty installation of refrigeration pipes.<sup>16</sup> Apparently, the subcontractor's faulty installation destroyed the insulation surrounding the refrigeration pipes causing them to fail.<sup>17</sup> The court found that the defect easily could have been discovered by an inspection and that the plaintiff accepted the work in writing.<sup>18</sup>

In *Phenix-Georgetown*, the District of Columbia Court of Appeals found:

The general rule is 'where defects in the work of construction of a building are known or readily discoverable by the purchasers of the property, and no complaint about the quality of the work is promptly made by them, their acceptance of the property discharges any right to damages which they might have had for the defects.'<sup>19</sup>

In that case, the owner brought suit against a construction manager who had been hired to supervise and warrant the work to be performed on the air conditioning unit of a commercial building.<sup>20</sup> The trial court granted summary judgement to the construction manager because the owner had accepted the building without objection, but the decision was overturned because "whether or not an owner has accepted defective performance is generally a question of fact...as is the latent or patent character of a defect."<sup>21</sup> Because there was a question of fact as to the character of the defect, the court found the summary judgement inappropriate and remanded the case to the trial court.<sup>22</sup>

## **B. The Illinois Standard (Beware)**

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<sup>15</sup> 290 So.2d at 422.

<sup>16</sup> *Id.* at 416.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> 477 A.2d at 222 (citations omitted).

<sup>20</sup> *Id.* at 220.

<sup>21</sup> *Id.* (citing 5 WILLISTON ON CONTRACTS Sec. 724 (3d Edition 1961)).

<sup>22</sup> *Id.* at 227.

At least one jurisdiction construes the existence of a patent defect extremely narrowly. Illinois appellate courts have held that in certain contexts patent as well as latent defects may provide the basis for a cause of action against the contractor unless the defects are expressly waived by the owner at acceptance.<sup>23</sup> In *Shaw*, for example, the owner sued the contractor for breach of contract because it used improper materials and failed to construct a slaughterhouse roof in a workmanlike manner.<sup>24</sup> Even though the owner was at the site and actually helped to install the roof, the court explained that "the facts must indicate that the injured party intentionally relinquished a known right...The injured party must also express 'assent to accept defective performance in satisfaction and as a complete discharge.'" <sup>25</sup> The general acceptance of the roof after it was built did not waive the owner's subsequent claim for defective performance because there was no express waiver of the defective condition.<sup>26</sup>

Similarly, in *Kansas*, the agent of the owner was present when the contractor poured the concrete floor in the basement of a house, and, in fact, agreed that the contractor should pour less concrete than required by the contract.<sup>27</sup> When the owner subsequently terminated the agreement and sued for defective performance, the contractor claimed that the assent of the owner's agent (and thus, the owner) as to the amount of concrete poured waived any claim for defective performance.<sup>28</sup> The court found, however, that even with actual knowledge of the defect and consent to continue the work, the owner had not waived its claim for defective performance: "For a voluntary acceptance of defective performance to work a complete discharge, the acceptance must be absolute and unconditional...based on facts and circumstances indicating the owner intentionally relinquished a known right."<sup>29</sup> Therefore, the courts in Illinois will relieve the contractor of liability for defective performance only upon the owner's express acceptance of a known defective work.

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<sup>23</sup> See, e.g., *Shaw v. Bridges-Gallagher, Inc.*, 528 N.E.2d 1349 (Ill.App. 1988); *Kangas v. Trust*, 441 N.E.2d 1271 (Ill.App. 1982); *Broncata v. Timbercrest Estates, Inc.*, 241 N.E. 2d 569 (Ill.App. 1968).

<sup>24</sup> 528 N.E.2d at 1350.

<sup>25</sup> *Id.* at 1354 (citing *Kangas*, 441 N.E.2d at 1271).

<sup>26</sup> *Id.*

<sup>27</sup> 441 N.E.2d at 1273.

<sup>28</sup> *Id.* at 1275.

<sup>29</sup> *Id.* at 1275 (citations omitted).

### C. The Experience of the Owner or Inspector

In some cases, the test of whether the defect could reasonably have been discovered is predicated on the experience -- or lack thereof -- of the obligee or agent who is doing the inspection.

In *Mastor*, for instance, the Florida Second District Court of Appeal raised the specter of the owner's inexperience:

Mastor asserted in his deposition and affidavit that he was unfamiliar with reading plans and specifications and that he eventually hired a licensed engineer and general contractor to inspect the building. It was after that inspection that he realized an additional thirty instances of defects or failure to follow the plans and specifications. Based on this record, it was improper for the trial court to enter summary judgement under the theory that Mastor accepted the building, knowing of its defects.<sup>30</sup>

In *Florida Ice*, the Louisiana Court of Appeals recognized that: "In the present case, as the supervision of the work was performed by experts in the field of architecture and engineering, it is clear that the laying of a pipe across a rigid joist is not a defect which cannot be discovered upon reasonable inspection."<sup>31</sup> In other words, because the inspectors were experts, the court was less willing to find fault with the trial court's determination that the defect could not be reasonably overlooked.

In *Stevens Construction*, the Wisconsin Supreme Court recited the general rule: "If the defects are hidden or latent and thus under the exercise of reasonable diligence unknown to the owner or architect, there cannot be implied a waiver on the part of the owner of construction defects."<sup>32</sup> The reference to the limits on the expertise of the inspector, however, was far less oblique:

The general contractor was herein aware of the limitations of the architect's duty to inspect the construction. He knew the architect was unqualified to detect design engineering defects. Likewise, the general contractor was informed that his plans were approved only insofar as they were in conformance with the architectural concept. The plaintiff was not, therefore, lured into believing, as a result of the architect's actions, that his design engineering was acceptable only to later discover that such

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<sup>30</sup> 600 So.2d at 557.

<sup>31</sup> 290 So.2d at 422.

<sup>32</sup> 217 N.W.2d at 299 (citations omitted).

was not the case. Such not being the case, it would be improper to imply a waiver of the owner's right to remedial action on the part of the general contractor resulting from his breach of a contractual duty to design.<sup>33</sup>

The court explicitly recognized the need to take into consideration the expertise of the inspector when applying the general rule and seemingly looked to contract language to determine the scope of the duty to inspect.

#### **D. Failure of the Contract in Extreme Examples**

In some instances, the performance of the contractor is found to be so materially deficient as to not satisfy the essential elements of the contract. When faced with this type of situation many courts have been unwilling to find that the contractor has met the threshold test of substantial performance, a prerequisite for recovery under the contract, and thus the issue of acceptance and waiver of defects becomes moot.

For example, in *M.S. Rau Inc. v. Gibson Roofer, Inc.*,<sup>34</sup> the Louisiana Court of Appeals held that although the contractor had proven that the owner accepted a patent defect, the performance was so deficient as to make the contractor liable for breach of contract.<sup>35</sup> In that case, the owner of a French Quarter antique shop hired a contractor to replace the roof of his building.<sup>36</sup> The contractor replaced the front half of the roof only, and the owner paid him without inspection.<sup>37</sup> Upon the discovery that the rear portion of the roof had never been replaced, the owner sued for breach of contract.<sup>38</sup> The trial court ruled in favor of the contractor on the grounds that, "[p]laintiff had an opportunity to inspect the [d]efendant's work and that an inspection would not have been inconvenient nor impractical. The failure of the Plaintiff to make the inspection precludes the Plaintiff from later questioning the completeness of Defendant's work."<sup>39</sup> In reversing the lower court, the appellate court noted that the defendant "itself breached the primary terms of the contract by failing to fulfill its express obligations under the contractual provisions...the fact that (plaintiff) paid for the work without inspection

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<sup>33</sup> *Id.* at 299.

<sup>34</sup> 657 So.2d 102 (La. Ct. App. 1995).

<sup>35</sup> *Id.* at 105.

<sup>36</sup> *Id.* at 103.

<sup>37</sup> *Id.* at 104.

<sup>38</sup> *Id.*

<sup>39</sup> *Id.* at 104-105.

does not negate (defendant's) liability for the damages caused by (defendant's) breach of contract."<sup>40</sup> Here the court relied on the lack of performance to overturn what was otherwise a typical acceptance of a patent defect.

Similarly, in *O.W. Grun Roofing & Constr. Co. v. Cope*<sup>41</sup>, the Texas Court of Appeals held that the significantly deficient performance of a contract cannot give rise to a successful claim for payment under the doctrine of substantial performance.<sup>42</sup> In that case, the contractor replaced the roof of a house with shingles that did not match.<sup>43</sup> When the contractor could not correct the problem by replacing some of the shingles, the owner sued for breach of contract.<sup>44</sup> The contractor contended that the owner's continued occupancy of the house represented acceptance of a patent defect and waiver of any claims.<sup>45</sup> In rejecting that argument, the court found that, although the roof was perfectly functional, the jury was justified in finding that the discoloration represented a failure to substantially perform on the contract.<sup>46</sup> The court noted: "We are not prepared to hold that a contractor who tenders a performance so deficient that it can be remedied only by completely redoing the work for which the contract called has established, as a matter of law, that he has substantially performed his contract obligation."<sup>47</sup>

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<sup>40</sup> *Id.* at 105.

<sup>41</sup> 529 S.W.2d 258 (Tex. Ct. App. 1975).

<sup>42</sup> *Id.* at 261.

<sup>43</sup> *Id.*

<sup>44</sup> *Id.* at 260.

<sup>45</sup> *Id.* at 262.

<sup>46</sup> *Id.* at 263.

<sup>47</sup> *Id.*

In *J.R. Sinnott Carpentry, Inc. v. Phillips*,<sup>48</sup> the Illinois Appellate Court refused to reverse the trial court on the basis of a similar rule.<sup>49</sup> The trial court had previously found that a contract for the construction of a three story house called for the third floor to be habitable and that builder failed to satisfy that requirement.<sup>50</sup> The court held that as a condition precedent to recovery the builder needed to show "substantial performance of the work required by the contract and a good faith performance of the essential points of the contract."<sup>51</sup> Rejecting the contractor's argument that the owner's occupation of the house constituted acceptance and waiver of the defects, the court noted that the trial court was justified in finding there was no substantial performance given the builder's failure to construct a third floor.<sup>52</sup> Although the opinion is unclear, the builder's original claim was for the amount due under the contract, which is generally based on a claim that the owner accepted a patent defect. If that was the case, the builder was clearly barking up the wrong tree, because, as we have seen, the Illinois courts do not accept arguments based on less than an express waiver.<sup>53</sup> In fact, the trial court found -- and the appellate court agreed -- that the contractor did not even meet the next lowest standard for recovery, that of substantial performance, in which the contractor is generally entitled to the price of the contract minus the cost of fixing the defects.<sup>54</sup> The lesson of these cases is that in a situation of failure to perform substantial elements of the contract, any claims based on the owner's acceptance are difficult to win. Therefore, with some exception, the general rule is that acceptance of work with a defect which is or could be reasonably observed by the owner acts to waive any claim the owner might later bring for defective performance. The courts in Illinois have taken a narrower view, denying waiver even when the owner has actual knowledge of a defect before acceptance, so long as he does not expressly waive his rights. Further, courts in most jurisdictions have shown some degree of flexibility to both sides when dealing with more or less sophisticated actors by adapting the "reasonable" standard to take into account the particular level of knowledge of the owner or inspector, and have even rejected the whole doctrine of waiver where the breach is so egregious that the contractor completely fails to substantially perform the essential elements of the contract.

### III. Acceptance by Agents and the Liability for It

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<sup>48</sup> 443 N.E.2d 597 (Ill. App. Ct. 1982).

<sup>49</sup> *Id.* at 602.

<sup>50</sup> *Id.* at 600.

<sup>51</sup> *Id.* at 601

<sup>52</sup> *Id.* at 602.

<sup>53</sup> See, e.g., *Shaw v. Bridges-Gallagher, Inc.*, 528 N.E.2d 1349 (Ill.App. 1988); *Kangas v. Trust*, 441 N.E.2d 1271 (Ill.App. 1982); *Broncata v. Timbercrest Estates, Inc.*, 241 N.E. 2d 569 (Ill.App. 1968).

<sup>54</sup> *J.R. Sinnott Carpentry*, 443 N.E. 2d at 602.

An agent of the owner -- an architect, engineer, or other representative -- can accept a project, and bind the owner to such acceptance, whether by operation of contract or through explicit authorization by the owner. Additionally, even without the agent's participation in the acceptance, his knowledge of patent defects can be imputed to the owner and may be sufficient to waive claims for such defects.

## A. Agency Status

It is well established that an agent's actions can generally bind the owner, but the key to the extent of the agent's authority lies in the origin of its status as an agent. The agent may act pursuant to a contractual provision which specifically grants the agent authority to represent the owner or the agent may act by some other designation of the owner.<sup>55</sup> An agent's acceptance of work generally can bind an owner as to any patent defects which may exist and, similarly, can relieve the owner as to latent ones in the same manner as if the owner itself accepted the project.<sup>56</sup> The agent's decision controls if it is not found to be fraudulent, the product of gross mistake, or arbitrary and capricious.<sup>57</sup>

In resolving disputes arising out of an agent's acceptance of defective work, the first determination a court will make is the status of the agent.<sup>58</sup> In *First-Wichita*, an individual was appointed as the agent of a trust to oversee improvements to a private home.<sup>59</sup> Various letters to, and activities of, the individual were used to establish his status as the agent for the trust, prompting the court to find that he

was appointed by the Trustee to oversee and supervise the reconstruction work done by the Contractor, that he did have Trustee's permission and authority to finally approve the work of the contractor (sic) on behalf of Trustee, and that [he] in fact did so approve the labors, materials and workmanship furnished by

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<sup>55</sup> See *Midsouth Land Co. v. A.E. Hughes, Jr., Inc.*, 434 So.2d 239 (Ala. 1983); *Hart and Son Hauling, Inc. v. MacHaffie*, 706 S.W.2d 586 (Mo. Ct. App. 1986); *Transamerica Ins. v. Victoria Housing Auth.*, 669 S.W.2d 818 (Tex. Ct. App. 1984); *First- Wichita Nat'l Bank v. Wood*, 632 S.W.2d 210 (Tex. Ct. App. 1982). See also *Southern Sch. Bldgs. v. Loew Elec., Inc.*, 407 N.E.2d 240 (Ind. Ct. App. 1980).

<sup>56</sup> See *City Nat. Bank of Miami v. Chitwood Constr. Co.*, 210 So.2d 234 (Fla. 3rd DCA 1968). But see *City of Okeechobee v. La Grow Irrigation, Inc.*, 434 So.2d 995 (Fla. 4th DCA 1983); *Burke Cty. Public Sch., Etc. v. Juno Constr.*, 273 S.E.2d 504 (N.C. Ct. App. 1981); *City of Midland v. Waller*, 430 S.W.2d 473 (Tex. 1968).

<sup>57</sup> See *Sarnoff v. De Graf Bros., Inc.*, 554 N.E.2d 335 (Ill. App. Ct. 1990); *Acmat Corp. v. Daniel O'Connell's Sons, Inc.*, 455 N.E.2d 652 (Mass. App. Ct. 1983); *J.J. Finn Elec. v. P & H Gen. Contractors*, 432 N.E.2d 116 (Mass. App. Ct. 1982); *Welborn Plumb. & Heat. Co. v. Randolph Co. Bd. of Ed.*, 150 S.E.2d 65 (N.C. 1966); *Top Line Constr. v. J.W. Cook & Sons*, 455 S.E.2d 463 (N.C. Ct. App. 1995); *City of Midland v. Waller*, 430 S.W.2d 473 (Tex. 1968); *Transamerica Ins. v. Victoria Housing Auth.*, 669 S.W.2d 818 (Tex. Ct. App. 1984).

<sup>58</sup> See *First Wichita*, 632 S.W.2d at 210.

<sup>59</sup> *Id.* at 210.

Contractor, and that such approval was binding on Trustee.<sup>60</sup>

The court analogized the letters of authority to a standard contractual designation:

it is clear that if the letters did not expressly grant to [agent] the final authority to approve Contractor's work, certainly that was the intent of the parties..." (*Id.*), concluding that, "... if the contract designates an architect, or other person, to supervise and approve the work, in the absence of fraud or bad faith, his decision is binding on the principal and is a waiver of all defects and of the principal's right to defend the action of the contractor or builder to recover the contract price."<sup>61</sup>

This case also demonstrates that absolute responsibility for an agent's decision can exist outside of the contract between owner and contractor.

However, two other cases, *Midsouth* and *Southern School Buildings*, show that the extent of an agent's responsibility may be wholly dependent upon the specific agreement. In each of these cases, an agent was designated in the contract to oversee and approve some portion of the work, and in each of them, the courts found that the contracts also required something further to bind the owner to final approval. In *Midsouth*, for instance, the court cited 17A, C.J.S. Contracts Sec. 498(8) (1963), for the proposition that, "Even though the contract provides that specified questions shall be determined by the architect or engineer, his decision is not final and conclusive unless the parties have so provided in plain and unequivocal language."<sup>62</sup> In that case, topographical information was to be supplied by an engineer in the performance of a contract to fill in and grade a vacant lot, and the contract specified that his approval was a necessary condition to final acceptance.<sup>63</sup> It also provided, however, for the necessity of the performance of all the contractual obligations by the contractor, leading the court to find that "matters within the knowledge of the parties, particularly performance within the specified time period, was not to be determined by the engineer..."<sup>64</sup> Accordingly, because the owner complained that the terms of the contract were not fully met as to time, the decision of the engineer as to performance was not held to be determinative, and the trial court was

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<sup>60</sup> *Id.* at 213.

<sup>61</sup> *Id.* (citations omitted).

<sup>62</sup> 434 So.2d at 244.

<sup>63</sup> *Id.* at 241.

<sup>64</sup> *Id.* at 244.

reversed.<sup>65</sup>

Similarly, in *Southern School Buildings*, a contractor was hired to complete all of the electrical work for a new high school, and an architectural firm was appointed to certify its work.<sup>66</sup> The court held that, "[t]hat the effect of an architect's or engineer's certificate is wholly dependent upon its contractual context is axiomatic."<sup>67</sup> Based on this principle, the court, in examining the contract in question, found "subsection 'd' of paragraph 2 entitled Southern to withhold ten percent of the contract price if it determined that Loew's work did not conform to specifications."<sup>68</sup> Southern's right to retain final payment existed independent of K.M. Associate's certification, for the parties indicated in paragraph 2 that the ten percent retainage could be withheld until "all of the...conditions are fully met."<sup>69</sup> Having thus found the contract to require more than the architect's certificate for final approval, the contractor's claim on appeal for final payment was denied.<sup>70</sup> Therefore, in an action based on the acceptance of work by an agent of the owner, the extent of the specific authority for the agent's status as such is critical to the determination of the finality of his decision, whether based specifically in the contract between the parties or elsewhere.

It is also clear that an agent's acceptance, if valid, binds the owner in precisely the same way as the owner's own acceptance waives any claims for patent defects. In *City of Midland*, the court found that latent defects -- in this case, leaks in a swimming pool not discovered until some twenty months after acceptance -- were not waived by an architect's approval and that the contract's express twelve month warranty period -- as opposed to the general statute of limitations on latent defects -- was not applicable.<sup>71</sup> The court noted that "The architect's certificate is binding on all parties as to the actual physical final completion of the work in erecting the structure or making the improvement called for by the construction contract. Insofar as defects are concerned which are unknown and could not have been discovered by ordinary care, the four-year statute of limitations applies."<sup>72</sup> In *Burke*, although the court eventually found that other contractual provisions in the case limited the effect of the architect's

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<sup>65</sup> *Id.* at 243-245.

<sup>66</sup> 407 N.E.2d at 243.

<sup>67</sup> *Id.* at 244.

<sup>68</sup> *Id.*

<sup>69</sup> *Id.* at 245.

<sup>70</sup> *Id.* at 255.

<sup>71</sup> 430 S.W.2d at 478.

<sup>72</sup> *Id.* (citations omitted).

certificate, the general rule was upheld as to defects found in a roof after acceptance.<sup>73</sup> The court explained:

Where the contract between the parties makes the final certificate of the architect conclusive as to the completion of the work in accordance with the contract, the parties may not question it or impeach it as to observable defects or those which were or could have been discovered by the architect in the proper performance of his duties, except in cases of fraud or mistake so substantial as to indicate bad faith or gross neglect.<sup>74</sup>

Therefore, if an agent is otherwise authorized to accept work on behalf of an owner, the same standards of whether a defect is latent or patent will apply to determine whether a claim has been waived by the owner through his agent.

Finally, as mentioned in *Burke* and *First-Wichita*, an otherwise valid determination of the agent as to performance has been held to be valid in all circumstances short of fraud or some other form of bad faith. In Texas, for instance, the standard applied is fraud or bad faith.<sup>75</sup> In North Carolina, it is fraud or gross mistake.<sup>76</sup> In Massachusetts, the exercise of the decision by the architect must not be arbitrary and capricious.<sup>77</sup> In Illinois, a showing of bias or fraud must be made.<sup>78</sup>

## **B. The Imputation of Knowledge**

Even where the owner maintains direct control over the acceptance of the project, the knowledge of the agent as to patent defects can be imputed to him and can operate to waive later claims for defective performance.<sup>79</sup> In *City of Gering*, for example, the City voted to

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<sup>73</sup> 273 S.E.2d at 508.

<sup>74</sup> *Id.*

<sup>75</sup> See *Transamerica*, 669 S.W.2d at 822.

<sup>76</sup> See *Welborn*, 150 S.E.2d at 68.

<sup>77</sup> See *Acmat*, 455 N.E.2d at 656.

<sup>78</sup> See *Sarnoff*, 554 N.E. 2d. at 340.

<sup>79</sup> See *Eastover Corp. v. Martin Builders*, 543 So.2d 1358 (La. Ct. App. 1989); *City of Gering v. Patricia G. Smith Co.*, 337 N.W.2d 747 (Neb. 1983); *South Union v. George Parker & Assocs.*, 504 N.E.2d 1131 (Ohio Ct. App. 1985).

accept work done by a contractor on a sewer line at the suggestion of the engineering firm they had hired to oversee the construction.<sup>80</sup> A defective sag was thereafter discovered in the line, but the court held that it was in the nature of a patent defect which was or should have been known to the City at acceptance:

While the City officials testified that they did not know of the defect before they voted to accept the work and had not seen the 'as-built plans' which showed the existence of the sag, the uncontroverted evidence in the case established that the existence of the sag was at least known to the engineering firm before it prepared the certificate and urged acceptance of the work by the City. Gene Ackie, a project engineer for Schaff (the firm), testified that he personally knew of the existence of the sag before certification and that his knowledge was based upon a survey done by other employees of Schaff. Knowledge of the agent Schaff was knowledge of the principal, the City of Gering.<sup>81</sup>

Similarly, in *Eastover*, a slightly more confusing scenario yielded the same result. Farnet, an architect and part-owner of LMI, a motel chain, was hired by the chain to oversee a construction project.<sup>82</sup> He in turn hired an agent named Vivien who hired another agent named Lauto to inspect the completed work.<sup>83</sup> The subsequent discovery of a problem with the hanging of some pipes gave rise to a claim by the successor owner for a latent defect, but the court rejected the claim, holding:

The evidence is clear that either Vivien or Lauto or both visually observed the number and spacing of the pipe hangers. The work was approved by [contractor's] chief inspector and no one voiced objection or complaint about the underground plumbing system. If Farnet did not have actual knowledge of the hanger placement, he should have since his agents and representatives did. The placement of the hangers was easily observable. At the time of the plumbing inspection, the 'defective' hanger placement was clearly a patent and not a latent one.<sup>84</sup>

The court also noted that, because of his status as part owner of the company, "Common

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<sup>80</sup> 337 N.W.2d at 750.

<sup>81</sup> *Id.* at 750-751.

<sup>82</sup> 543 So.2d at 1359.

<sup>83</sup> *Id.*

<sup>84</sup> *Id.* at 1362.

sense necessitates the conclusion that knowledge obtained by Farnet, or knowledge which he should have obtained, whether as an architect or a layman, is knowledge by LMI, the owner."<sup>85</sup> Because there was no complaint registered prior to acceptance, the court held, "It would be unfair to allow them or their transferee to now complain about something they were aware of and approved."<sup>86</sup> Thus, the successor-owner of a motel was bound by the imputed knowledge of the previous owner's partner/architect and his agent's agent as to the existence of defects in the spacing of pipe hangers.<sup>87</sup>

Therefore, where the agent of an owner has knowledge of a defect -- or even where, as in *Eastover*, the agent should only reasonably have knowledge of a defect -- the knowledge is imputed to the owner, and acceptance will work to bar claims for defective performance later on. Overall, the actions of the agent can be critical to the claim for defective performance for the owner. If the agent acts to accept defective work which is reasonably obvious -- or even if he only has knowledge or reasonably should have knowledge of such patent defects -- then his acceptance or knowledge can bind the owner and thus work to create a valid defense for the contractor.

#### IV. Conclusion

There are thus many problems the surety must be aware of in these actions. While the acceptance of the work can act as a fig leaf for the contractor under ideal conditions, it often results in decisions adverse to contractors in cases the facts are unusual; the owner has no experience in inspecting, the defect is unusual, the defects are unreasonably large: or where the action is brought in Illinois. The actions or knowledge of an agent of the owner can also be a useful defense to some of these claims; however, in some cases the specific terms of the agency contract can act to upset what would otherwise be the legitimate acceptance of a defect. In the end, it seems that the ideal situation for a surety to defend one of these actions would involve the reasonable inspection of the work by a qualified agent of the obligee who has the contractual authority to act as such -- and hopefully, one where the builder has put on the whole roof.

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<sup>85</sup> *Id.*

<sup>86</sup> *Id.* at 1363.

<sup>87</sup> *Id.*