New Home Warranties

by Kathleen O'Brien

If you don't offer your customers a written new home warranty, that doesn't mean you haven't provided a warranty. According to the law, when you build a home, you make an "implied warranty" that it meets certain standards of construction and service. The trouble is, without a written warranty, the courts decide what those standards are and whether you've met them. To avoid the risk of leaving your financial future in the hands of a judge, you need an explicit warranty.

An explicit warranty can also provide marketing appeal in a slow market. But providing your own is expensive and risky. In today's quick-to-sue atmosphere, a small firm is better off relying on "third-party" warranty programs. They're relatively inexpensive and take a lot of the guesswork out of standing behind your work.

What's Available?

Home warranties got their start in 1973, when Home Owners Warranty (HOW) was established by the National Association of Home Builders (NAHB) to deter federally legislated home warranties. In 1981 HOW became an independent operation. Other national programs, including HomeBuyers Warranty (HBW) and Residential Warranty Corporation, as well as some smaller statewide programs, have been established in the meantime.

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The basic premise for all of these programs is the same: In return for meeting certain guidelines and paying a per house fee, builders can offer their clients a limited warranty. But all warranty programs are not exactly alike, so one may suit you better than another. For example, if you choose a program with a large enrollment, such as HOW or HBW, you may benefit from its national identity. On the other hand, if you believe "smaller is better," you may opt for a statewide program that may provide more personalized service. Some states have more than one program. Florida, for example, offers the Preferred Builders Warranty and the Bonded Builders Home Warranty.

Who Qualifies?

Keep in mind that all of these programs have a right to "refuse service." If you don't meet the standards they have set, you won't be able to enroll in their warranty program. Usually, they look at financial reliability and the quality of your work. They talk with lenders, suppliers, and your past customers, and they sometimes look at projects under construction.

What to Look For

There are several things to consider when you're shopping for a warranty program.

What does the program cost? The average cost for a warranty is $300 per home. Check to see if the rate schedule is competitive and straightforward. Sometimes rates fluctuate in a particular area relative to the performance of other builders. There may also be add-on fees or hidden costs — for example, for special construction design requirements.

Is the warranty understandable? If you don't understand the warranty, then your customer won't either. That can lead to some serious disagreements down the road.

What exactly does the warranty cover? Compare coverage. Check the length of coverage for electrical and mechanical (nonstructural) systems, as well as for structural repair. Nonstructural repairs are generally covered for a short term only, usually one or two years. Also find out what your liability is if things go wrong. Can the warranty program collect money from you to cover repairs it believes you are responsible for?

How selective is the enrollment? You probably don't want to be a member of a program that accepts everybody. A program that is extra selective limits its risk and yours. It is also less likely to generate bad press and poor public relations by being associated with fly-by-night builders.

What kind of dispute resolution services does the program provide? Does the warranty include a provision for mediation between you and the owner? Does the warranty have an arbitration provision? If so, does the program provide an independent arbitration service and is it reputable? An arbiter who is an employee of the warranty program might have trouble being objective. Also find out who pays for the arbitration.

Does the program provide educational services? Some programs conduct seminars for builders on construction techniques to reduce the possibility of structural or other problems. Even if you don't personally need such a seminar, it's a good sign when the company uses education as a means of reducing risk and maintaining quality.

Is the program financially strong? New home warranties provide coverage for ten years, so you want to be certain that the company backing it will be around for at least that long. Warranty programs are regulated like any insurance company, and are required to register with the insurance commissioners in the states in which they operate. Check to see if your state insurance commissioner's office knows of any problems with the warranty programs you're interested in. You should also read any information generally available on a program's financial status, such as an audited public financial statement.

If you want to dig further, have your insurance broker or accountant review the detailed statements filed by the warranty program with the state insurance commissioner's office. These statements are lengthy and dense, but in addition to information about the financial status of the warranty company itself, they can provide information on "reinsurance" coverage — backup insurance by another company that will take over claims if the original insurance company can't afford them or goes bankrupt.

How long has the program been around? You should think twice about signing up with a program that hasn't been tested in the field. Many of the programs have been around for awhile and have had a chance to work out some kinks, but this isn't necessarily true of all of them.

What is the program's service record? Find out how many claims have been made on the warranty, and how many of the claims were resolved without going to court. Are there consumer complaints about the program on record? Unhappy customers tell their friends, and a program with a shaky reputation doesn't have half the marketing appeal of one with a solid one. Check this out with your builder friends, too. If they use the program, what do they think?

Can the program adequately serve its builders? If the program is national, find out where the branch offices are. You don't want to work long distance if you don't have to. The ratio of enrolled builders (or covered homes) to field staff is important, too. The lower the ratio, the greater the likelihood of a timely response to your questions and problems. Actually, you can get a good idea from your first contact with a warranty company. Did you get through to the right department quickly? Were your questions answered professionally and thoroughly? Were the company's representatives interested in you and did you get the information you needed in a timely manner?

Is the program recognized by VA and FHA Financing Programs? If it is, this could save some time. Some VA and FHA inspection requirements are waived if you carry a recognized warranty.

What marketing support does the program provide? A warranty program should be a part of your marketing plan. Find out if the program provides personalized brochures, signs, and other materials. Look them over if you can to see if they are attractive and well written. Ask other builders enrolled in the program if they're satisfied with the support.

Who administers the warranty program? Many warranty programs are run by people who are builders themselves, and it certainly helps to have people who understand construction on your side. Don't forget, however, that their real business is to run a home warranty program. They need to have a solid understanding of warranty and insurance issues.

Is the warranty endorsed and by whom? If you're having a difficult time choosing between programs, knowing that the program is endorsed by a trade association or other organization that you respect may help you make your decision. ■

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