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FREEDOM TO CONTRACT IN TEXAS—
ENFORCEABILITY OF AN “AS IS”
CLAUSE IN A COMMERCIAL LEASE:
*GYM-N-I PLAYGROUNDS,
INC. V. SNIDER*

*Natalie Smeltzer**

TEXAS has long supported parties' freedom to contract.¹ Repeatedly, the Texas Supreme Court has upheld the right to contract as parties desire, unless the contract violates the law or public policy.² As a part of the bargaining process, parties may wish to allocate certain risks. In *Gym-N-I Playgrounds, Inc. v. Snider*, the Texas Supreme Court had to decide whether an “as is” disclaimer in a commercial lease waived breach of warranty and other claims founded on the property's condition by the tenant.³ The court correctly held that the “as is” disclaimer was effective during the holdover tenancy, precluding the tenant's claim for breach of implied warranty of suitability and negating the causation element of the tenant's other claims.⁴ This case extended the Texas Supreme Court's holding in *Prudential Insurance Company of America v. Jefferson Associates, Ltd.* that an “as is” clause is enforceable in a sales transaction to a commercial lease.⁵ The lower courts must follow this authority and foster the freedom of parties to contract, absent violation of public policy or law.

In 1983, Ron Snider constructed a 20,075 square foot building in New Braunfels, Texas, for his playground equipment business, Gym-N-I Playgrounds, Inc. (“Gym-N-I”).⁶ The fire marshal recommended, but did not require, that Gym-N-I install a sprinkler system in the building, but Snider never implemented this recommendation.⁷ Years later, Patrick

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1. *E.g.*, *Wood Motor Co. v. Nebel*, 238 S.W.2d 181, 185 (Tex. 1951).

2. *E.g.*, *In re Prudential Ins. Co. of Am.*, 148 S.W.3d 124, 129 (Tex. 2004); *Lawrence v. CDB Servs., Inc.*, 44 S.W.3d 544, 553 (Tex. 2001).

3. *Gym-N-I Playgrounds, Inc. v. Snider*, 220 S.W.3d 906, 908 (Tex. 2007).

4. *Id.* at 912.

5. 896 S.W.2d 156, 163–64 (Tex. 1995).

6. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 906.

7. *Id.*

Finn and Connie Caddell, two of Snider's employees, purchased the business and leased the building from Snider.⁸ Finn and Caddell, who were aware that the fire marshal's recommendation had not been implemented, did not inspect the property before leasing it because they had extensive knowledge of the building.⁹ Both parties were represented by counsel, and the lease was signed on September 30, 1993.¹⁰ Provisions in the lease stated that Gym-N-I would "(1) accept the building 'as is,' expressly waiving all warranties; (2) obtain insurance on the building to cover fire-related loss; and (3) perform maintenance and repairs."¹¹ Additionally, the lease contained a holdover provision stating that "[a]ny holding over without written consent of Landlord shall constitute a lease from month-to-month, under the terms and provisions of this Lease to the extent applicable to a tenancy from month-to-month."¹² The lease also contained provisions obligating Gym-N-I to insure the premises against fire damage and to maintain compliance with all building and fire codes and other applicable laws and regulations.¹³

Although the original lease term expired in September 1996, Gym-N-I continued to pay, and Snider continued to accept, monthly rent without executing a new instrument.¹⁴ On August 10, 2000, a fire destroyed the building. Snider received \$400,000, and Gym-N-I nearly \$1,000,000, from their respective insurance policies.¹⁵ Gym-N-I claimed that the fire was caused by defective electrical wiring and the absence of a sprinkler system.¹⁶

Gym-N-I brought a suit against Snider for negligence-related claims, Deceptive Trade Practices-Consumer Protection Act violations, breach of the implied warranty of suitability for commercial purposes, fraud, and other claims.¹⁷ Based on Snider's arguments that the claims were barred by the "as is" clause and the warranty disclaimer, the trial court granted summary judgment to Snider on all claims, except for a breach of contract claim which settled.¹⁸

On appeal, Gym-N-I argued that the "as is" clause was not effective during the holdover tenancy, and alternatively, that the clause was unenforceable.¹⁹ The court of appeals affirmed the judgment of the trial court, and Gym-N-I petitioned the Texas Supreme Court for review.²⁰

8. *Id.*

9. *Id.*

10. *Id.* at 906-07.

11. *Id.*

12. *Id.* at 907 n.4.

13. *Id.* at 907 nn.2-3.

14. *Id.* at 907.

15. *Id.*

16. *Id.*

17. *Id.* at 907-08, 914.

18. *Id.*

19. *Id.* at 908.

20. *Id.*

The Texas Supreme Court affirmed the judgment, holding that at the time of the fire the “as is” clause was effective, and the express warranty disclaimer waived the implied warranty of suitability and defeated the causation element of Gym-N-I’s other claims.²¹ The court held that per the plain and ordinary meaning of the words in the holdover clause, the “as is” clause was effective during the holdover tenancy.²² Because provisions of a lease that are expressly agreed upon control, and absent fraud in the inducement, a party that signs a contract containing an “as is” clause can waive property condition claims.²³ Thus, the court concluded that an express warranty disclaimer could, as a matter of law, effectively waive the implied warranty of suitability.²⁴ Further, the court noted that this conclusion supported strong public policy in Texas of freedom to contract.²⁵

The court reasoned that the “as is” clause was in effect during the holdover, because both parties agreed that their relationship portrayed a holdover as envisaged by the holdover provision, and because the plain and ordinary meaning of the words of the provision—“*under the terms and provisions of this Lease*”—meant exactly what they said.²⁶ Additionally, the court rejected Gym-N-I’s argument that the original terms of the lease did not apply to the holdover period as in *Bockelmann v. Marynick*, since the issue in that case was the liability of co-tenants who did not holdover, rather than whether the original terms applied during holdover.²⁷ In *Bockelmann v. Marynick*, Ms. Bockelmann, co-tenant in a residential lease with her husband, separated from her husband and vacated the leased premises before the lease term expired.²⁸ Mr. Bockelmann remained on the premises after the lease had expired as a holdover tenant, and subsequently, the landlords sued the tenants for past due rent, among other things.²⁹ The court held that Ms. Bockelmann was liable for rent and other damages during her husband’s holdover tenancy.³⁰ Not only did the *Gym-N-I* court distinguish the issue in *Bockelmann*, it also pointed out that in *Bockelmann* the court actually gave effect to the original lease by subjecting the new tenancy to the original terms.³¹

Once the court established that the “as is” clause remained effective during holdover, the court addressed the key issue of whether the clause

21. *Id.*

22. *Id.* at 908–09.

23. *Id.* at 912.

24. *Id.*

25. *Id.*

26. *Id.* at 908–09 (emphasis added).

27. *Id.*

28. *Bockelmann v. Marynick*, 788 S.W.2d 569, 570 (Tex. 1990).

29. *Id.*

30. *Id.*

31. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 909. The *Gym-N-I* court also noted that at least one court of appeals had identified this distinction and rejected a holdover tenant’s argument that *Bockelmann* supports the position that guarantees in the original lease were not effective during holdover. *Id.* (citing *Clark v. Whitehead*, 874 S.W.2d 282, 284 (Tex. App.—Houston [1st Dist.] 1994, writ denied)).

waived some or all of Gym-N-I's claims.³² Analyzing its holdings in *Davidow v. Inwood North Professional Group-Phase I*³³ and *Prudential Insurance Company of America v. Jefferson Associates, Ltd.*³⁴ in light of one another, the court concluded that when a lease expressly disclaims the implied warranty of suitability, it is waived as a matter of law.³⁵ In *Davidow*, a landlord brought suit for unpaid rent and other costs against a commercial tenant who offered the affirmative defense, among other defenses, that the landlord breached an implied warranty of suitability.³⁶ Extending the implied warranty of habitability in residential leases to commercial leases, the *Davidow* court held that there is an implied warranty of suitability by the landlord in a commercial lease, meaning that "at the inception of the lease there are no latent defects in the facilities that are vital to the use of the premises for their intended commercial purpose and that these essential facilities will remain in a suitable condition."³⁷ Although the *Davidow* court did not have the occasion to address whether the implied warranty could be waived, they did note that if "the parties to a lease expressly agree that the tenant will repair certain defects, then the provisions of the lease will control."³⁸

In *Jefferson Associates*, a purchaser of a commercial building alleged that the vendor violated the Deceptive Trade Practices Act and fraudulently concealed the existence of asbestos fireproofing in the building.³⁹ The contract for the sale included an "as is" clause which provided that "Purchaser is taking the Property 'AS IS' with any and all latent and patent defects and that there is no warranty by Seller that the Property is fit for a particular purpose."⁴⁰ Holding the "as is" clause negated the causation element of all the purchaser's claims, the court reasoned that a buyer agreeing to purchase something "as is" makes his own judgment of the bargain through the allocation of risks.⁴¹ The *Gym-N-I* court pointed out that in *Prudential* it did not consider the effect an "as is" would have on a breach of implied warranty of suitability claim in a lease because the transaction at issue was a commercial property sale, rather than a lease.⁴²

By combining its proposition in *Davidow*, that terms in the lease control when parties expressly agree the tenant is responsible for the repair of certain defects, with its holding in *Jefferson Associates*, that an "as-is"

32. *Id.*

33. 747 S.W.2d 373 (Tex. 1988).

34. 896 S.W.2d 156 (Tex. 1995).

35. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 912.

36. *Davidow*, 747 S.W.2d at 375.

37. *Id.* at 377.

38. *Id.* at 377. The *Gym-N-I* court noted that while several courts of appeals have addressed the scope of the waiver since *Davidow*, the Supreme Court had not since had a chance to address it. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 910.

39. *Jefferson Assocs.*, 896 S.W.2d at 158.

40. *Id.* at 160.

41. *Id.* at 161. The court noted that there could be exceptions to the enforceability of an "as is" clause in situations where there is fraud in the inducement of the contract or if the seller impairs the buyer's inspection of the property. *Id.* at 162.

42. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 912.

clause can waive claims founded on a condition of the property, the Texas Supreme Court in *Gym-N-I* concluded that the implied warranty of suitability is waived when it is expressly disclaimed in a lease.⁴³ Further, public policy in Texas strongly supports freedom to contract.⁴⁴ The court reasoned that this liberty allows the lessee and lessor to allocate risks regarding the suitability of the premises and to negotiate prices accordingly.⁴⁵ Citing to *Jefferson Associates*, the court stated that by leasing property “as is,” *Gym-N-I* agreed to make its own judgment of the physical condition of the property and, therefore, negated the causation element of the other claims.⁴⁶

Finally, the court acknowledged that the holding was in contrast to the implied warranty of habitability, which the court had previously held “can be waived only to the extent that defects are adequately disclosed.”⁴⁷ The court reconciled this conflict given that in most jurisdictions the warranty of habitability does not cover commercial tenancies, as the disparity of bargaining power in residential transactions is lacking in commercial transactions.⁴⁸

In *Gym-N-I* the Texas Supreme Court correctly upheld a waiver of the implied warranty of suitability when it was expressly disclaimed in a commercial lease. Unlike the implied warranty of habitability, which has a statutory foundation, the implied warranty of suitability is based solely on common law.⁴⁹ Consequently, the Texas Supreme Court, which established this warranty of suitability, is the mandatory authority on the law absent legislative action. By combining its previous opinions in *Davidow* and *Jefferson Associates*, the court logically concluded that the warranty can be waived in a commercial lease. The court took the opportunity presented by the facts of this case to extend its holding in *Jefferson Associates* from commercial sales to commercial leases and set forth the law regarding the waiver of the warranty of suitability.⁵⁰ More remarkably, examining the opinion from a broader viewpoint, the court seized the

43. *Id.*

44. *Id.* at 912–13. The court cited to recent decisions in which they have reaffirmed the long-standing policy in favor of the right to contract. *See, e.g.*, *BMG Direct Mktg., Inc. v. Peake*, 178 S.W.3d 763, 767 (Tex. 2005); *In re Prudential Ins. Co. of Am.*, 148 S.W.3d 124, 129 (Tex. 2004).

45. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 912–13.

46. *Id.* at 914.

47. *Id.* at 913–14 (quoting *Centex Homes v. Buecher*, 95 S.W.3d 266, 274 (Tex. 2002)). The *Gym-N-I* court also noted that after its decision in *Centex*, the Legislature formed a rulemaking authority called the Texas Residential Construction Commission. *Id.* at 914 (citing to TEX. PROP. CODE ANN. § 408.001(2) (Vernon 2007)).

48. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 913; 2 RICHARD R. POWELL, POWELL ON REAL PROPERTY § 233[2][b] (Michael A. Wolf ed., 2007).

49. TEX. PROP. CODE § 408.001(2); *Davidow v. Inwood IV Prof'l Group Phase I*, 747 S.W.2d 373, 377 (Tex. 1988).

50. Interestingly, the court in *Gym-N-I* explained that it had not had the occasion to determine whether the implied warranty of suitability could be waived when the court established it in *Davidow*, or in *Jefferson Associates* which dealt with a commercial sale rather than a lease. *Gym-N-I Playgrounds, Inc.*, 220 S.W.3d at 910, 912.

occasion to endorse Texas's long standing support of freedom to contract by enforcing the "as is" clause.

Notably, the court could have found that the warranty of suitability was ineffective without explicitly addressing the broader issue of enforceability of "as is" clauses. In fact, the Respondent argued in his brief that the warranty was not applicable.⁵¹ The warranty of suitability protects against *latent* defects existing at the commencement of the lease.⁵² A latent defect is defined as one which is "hidden, . . . concealed, . . . [cannot] be discovered by . . . observation or inspection made with ordinary care, . . . or which [the] owner has no knowledge."⁵³ Therefore, the lack of sprinkler system cannot be a latent defect because Gym-N-I knew there was no sprinkler system at the time the lease was commenced. Gym-N-I could have negotiated terms to address the issue, such as obligating Snider to install a sprinkler system. Both parties were represented by counsel and they chose to allocate risks in this manner as part of the bargaining process. Furthermore, Gym-N-I could have inspected the electrical wiring before commencing the lease, but chose not to inspect the premises. The court, obviously aware of the latent defect argument since it was made in Respondent's brief, wisely chose instead to use this case more expansively to support the freedom to contract policy.

The court's decision in *Gym-N-I* could have a significant impact on Texas common law regarding the freedom to contract. There have already been several appellate courts which have had the opportunity to address the *Gym-N-I* case, but to date there has not been a Texas case to explicitly follow the holding.⁵⁴ *El Sabor De Mi Tierra, Inc. v. Atascocita/Boone J.V.*, involving a commercial lease, distinguished *Gym-N-I* on grounds that the "as is" clause in *El Sabor* specifically applied to the "Deemed Premises," and the alleged claims related to matters outside the "Deemed Premises."⁵⁵ Therefore, the court held that the "as is" clause did not waive the allegations because they occurred outside the "Deemed Premises."⁵⁶ In *Kupchynsky v. Nardiello*, a case involving a dispute over a residential property sales contract, the dissent argued that the majority did not find that the buyers proved the fraud exception, expanding the *Prudential* exceptions to "negligent or unintentional misrepresentation."⁵⁷ Additionally, the dissent noted that this decision would permit

51. Respondent's Brief on the Merits at 25, *Gym-N-I Playgrounds, Inc. v. Snider*, 220 S.W.3d 906 (Tex. 2007) (No. 05-0197).

52. See *Davidow*, 747 S.W.2d at 377.

53. BLACK'S LAW DICTIONARY 456 (6th ed. 1990) (referring to "hidden defects").

54. See *El Sabor De Mi Tierra, Inc. v. Atascocita/Boone J.V.*, No. 05-05-01134-CV, 2007 WL 2417921, at *11-12 (Tex. App.—Houston [14th Dist.] Aug. 28, 2007, pet. filed); *Kupchynsky v. Nardiello*, 230 S.W.3d 685 (Tex. App.—Dallas 2007, pet. filed).

55. *El Sabor De Mi Tierra, Inc.*, 2007 WL 2417921, at *12.

56. *Id.*

57. *Kupchynsky*, 230 S.W.3d at 698. The majority held that whether the "as is" clause in a standard, preprinted residential contract was enforceable depended on the totality of the circumstances, and that in this case it was boilerplate language that was not an "important basis of the bargain." *Id.* However, the dissent believed that the burden was on the party trying to avoid the "as is" clause to plead and prove that the clause was unenforce-

courts and juries to reform contracts for parties by guessing what the parties “should have known,” which would be in opposition to the *Gym-N-I* holding reaffirming the freedom to contract.⁵⁸

In conclusion, Texas has yet to see to what extent the *Gym-N-I* holding will affect the common law freedom to contract principle. The court should be commended for making a step in the right direction as far as supporting freedom to contract, especially in light of recent appellate court decisions that have not upheld the enforceability of “as is” clauses.⁵⁹ As explained, the *Gym-N-I* case is not only important for commercial lease agreements, but it also has broader significance for “as is” and waiver of reliance clauses in commercial transactions of all types. Seeing that the court has extended its ruling from commercial sales to commercial leases, it is likely that the court will continue to uphold parties’ choice of risk allocation in various transactions. Furthermore, decisions such as this will impact the drafting and negotiating of contracts in Texas. Parties can negotiate and bargain with the assurance that their choice of risk allocation will be upheld. The significance of this holding permeates the common law of contracts. Practitioners will have to stay tuned to see what step the Texas Supreme Court will take next to uphold and promote this paramount policy of freedom to contract in Texas.

able per one of the *Prudential* exceptions. *Id.* at 690-91. Absent an exception, the clause negated causation. *Id.* at 693.

58. *Id.* at 698.

59. *See, e.g.,* Warehouse Assocs. Corporate Centre II, Inc v. Celotex Corp., 192 S.W.3d 225, 234 (Tex. App.—Houston [14th Dist.] 2006, pet. denied).

Articles

