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IT BYTES

ANSWERING YOUR COMMON IT CONTRACT LAW QUESTIONS

WHAT IS THE DIFFERENCE BETWEEN A WARRANTY AND A REPRESENTATION?

WHEN DOES THIS QUESTION TEND TO ARISE?

You are negotiating a contract to procure some important technology tools for your business. During the due diligence process, the seller provides a number of statements about the features and functionality of the technology tools, including whether they are fit for purpose and if the tools meet the specifications you originally agreed upon with the supplier. You are relying heavily on these statements in deciding whether to go ahead with the purchase. However, unsurprisingly, you are worried about what recourse you may have if those statements turn out to be false, after you have already paid for and started using the technology tools in your business. This will, in part, depend on the extent to which those statements have been incorporated as terms of the contract under which you purchased the technology tools or if they remain only pre-contractual representations.

WHAT DOES THE LAW SAY?

The distinction between a 'warranty' and a 'representation' is a recurring issue in commercial contract negotiations and disputes. It is important to understand the difference as warranties and representations can allow for different remedies for breach.

A 'representation' is a statement of fact made by one party to another upon which the other party may rely upon in deciding whether to enter a contract. Representations are often made during pre-contractual negotiations but will not necessarily be incorporated into the contract itself. If any representations not incorporated into the contract turn out to be false, the aggrieved party will not be able to seek damages or other relief by bringing a claim for breach of contract. However, other common law, equitable or statutory remedies may be available depending on the circumstances. These could include:

- Rescission of the contract, with other orders to restore the parties to their pre-contractual positions (to the extent possible).
- Damages in negligence, where the representation involves negligent statements or a degree of recklessness as to whether they are correct or not.
- Damages or other remedies under the Australian Consumer Law for misleading conduct.

A 'warranty' on the other hand, is a contractual term which functions as a promise or undertaking and for which contractual damages, aimed at putting the aggrieved party in the position they would have been if the contract had been properly performed, along with other usual contractual remedies, will be available if there is a breach. Depending on the circumstances, failure to comply with a warranty may also trigger a right for the aggrieved party to terminate the contract, either at common law or under a contractual termination framework. The starting position at common law is that a breach of a warranty (as opposed to an essential term or 'condition' of the contract) will not trigger a right to terminate. However, if the breach is sufficiently material so as to deprive the aggrieved party of substantially the whole benefit of the contract, then a right to terminate may still arise at common law (you can find out more on common law termination rights in this IT Bytes article).

Accordingly, the treatment of a statement as either a pre-contractual representation or as a contractual warranty may have significant implications for the various causes of action and associated remedies that may be available to an aggrieved party in the event of a breach. In each case, the position may also be affected by the liability provisions of the contract, including liability caps and exclusions and non-reliance provisions (like entire agreement clauses, which seek to negate reliance by either party on statements made before entering the contract that have not been converted into contractual terms).

WHAT ARE THE PRACTICAL IMPLICATIONS FOR YOUR CONTRACT?

The difference between a warranty and a representation can have a material impact on the rights and remedies available to contracting parties.

Where a party wishes to rely on pre-contractual statements, the best approach will usually be to convert those statements into contractual terms. This may be done either by drafting appropriate provisions into the contract directly or else by incorporating documents exchanged as part of the pre-contractual negotiations (e.g. a tender response) into the contract by reference. In doing so, consideration should be given to:

- How the terms are framed – a statement that is described in the contract as both a 'warranty' and a 'representation' may preserve remedies for both breach of contract and for misrepresentation if the statement turns out to be false, particularly if supplemented by an express provision to the effect that the relevant party has relied upon the 'representation' in entering into the contract.
- The operation of the contractual termination framework – to avoid uncertainty as to whether a breach will trigger a right to terminate, this will ideally be explicitly addressed in the contract itself.

On the other hand, if the parties wish to draw a line under their pre-contractual exchanges, the contract should include express statements to the effect that representations made prior to entering the contract do not form part of the contract and that the parties have not relied upon any pre-contractual representations in deciding to enter the contract. This should also be made consistent with the entire agreement clause in the contract. While there are limits to the extent to which liability for pre-contractual misrepresentations can be excluded, clear disclaimers can help to show that, as a matter of fact, the parties did not rely upon pre-contractual statements in deciding to enter the contract, which may negate liability that may otherwise arise in respect of such statements.

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We would like to acknowledge the contributions of Easha Malik and Zoe Mitchell to this article.

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