Key Legal Issues In Construction Defect Claims

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Recent Development: The California Supreme Court has ruled that contractors cannot be held liable in negligence for either cost of repair or diminution in value for "pure" construction defects, i.e., those that have caused no property damage. Aas v. Superior Court, 24 Cal. 4th 627, 101 Cal. Rptr. 2d 718 (2000).

I. BASIC THEORIES OF LIABILITY

The identity of the defendant determines the type of suit that may be brought against it.

A. Theories of Liability Against a Developer

A developer builds improvements for sale to the public. He is either a subdivider who improves the raw land and then constructs buildings for sale, or one who buys improved lots and builds the buildings on speculation for sale to the public. In either case, he builds and sells his products in the same manner as any other manufacturer of a product. (Miller & Starr, Cal. Real Estate 2d at § 25.1 (1990)).

1. Breach of Contract/Warranty.

Developers are liable for breach of contract or breach of any express warranty.

In addition, a developer may be liable for breach of an implied warranty. The developer holds himself out to the public as being knowledgeable and qualified to manufacture buildings. Therefore, courts have concluded that the developer who constructs buildings for sale to the public impliedly warrants that the improvements have been constructed in a reasonably workmanlike manner, that they are free from serious defects, and that they are fit and proper for the uses intended. If the property contains serious defects, the developer breaches this implied warranty, and the owner of the property can recover his damages from the developer. (Miller & Starr, Cal. Real

Estate 2d at § 25.18 (1990) (citing Pollard v. Saxe & Yolles Development Co., 12 Cal. 3d 374, 377-380 (1974))).

2. Negligence.

When a developer undertakes the development of property for sale to the public, he assumes the duty to construct the improvements properly, in a careful manner, and without defect. If he builds the improvements negligently, he is liable to the purchaser for any damages suffered which were proximately caused by the developer's negligent construction. His liability extends not only to correction of the defective improvements, but also to the repair of other portions of the property damaged by the defective portion or the improvements, and to any personal injuries caused by the defect. (Miller & Starr, Cal. Real Estate 2d at § 25.16 (1990)).

In addition, the developer's duty extends to third persons who foreseeably may be endangered by his negligence. Thus, any person who is within the area of foreseeable risk may recover for the personal injuries or property damages proximately caused by the developer's negligent construction, whether or not they are in privity of contract. (Miller & Starr, Cal. Real Estate 2d at § 25.17 (1990)

3. Strict Liability.

Courts have found little distinction between the "mass production and sale of homes and the mass production and sale of automobiles, and the pertinent overriding policy considerations are the same." Kriegler v. Eichler Homes, Inc., 269 Cal. App. 2d 224, 227 (1969). Consequently, the developer of mass-produced, or tract homes may be held strictly liable on basic product liability theories whether or not there is privity of contract. Id. at 227.

4. Other Theories of Liability.

Developers may also be held liable on fraud or nuisance theories.

B. Theories of Liability Against a Contractor or Subcontractor

As opposed to a developer who builds improvements on his own land, a contractor is a person who enters into a contract with a landowner to build improvements on the landowner's property. The contractor (general contractor or sub-contractor) enters into a construction contract and agrees to

construct the improvements described in the contract in a good and workmanlike manner according to the contract documents.

1. Breach of Contract/Warranty.

Contractors are liable for breach of contract or breach of any express warranty.

Generally speaking, the contractor does not impliedly warrant the merchantability of the final product if he follows the contract plans and specifications. If there are defects in the completed improvements because of some error or omission in the contract documents, a design professional may have some liability, but generally the contractor has none. (Miller & Starr, Cal. Real Estate 2d at § 25.3 (1990)). However, a contractor who also prepares the plans and specifications necessary to accomplish the contracted work is held to the standards of care of a design professional. (Miller & Starr, Cal. Real Estate 2d at § 25.5 (1990)). Similarly, a sub-contractor who agrees to select the methods and materials to be used to complete a portion of a contract is considered a seller of labor and materials, and he impliedly warrants that both his workmanship and materials will be fit and proper for the intended use. (Miller & Starr, Cal. Real Estate 2d at § 25.12 (1990)).

2. Negligence.

A contractor who builds improvements with poor workmanship, or uses insufficient or improper materials for the job, or deviates from the plans and specifications, or otherwise fails to exercise due care in the construction of the improvements, is liable for negligence to the owner for the damages proximately caused by his negligent performance. (Miller & Starr, Cal. Real Estate 2d at § 25.4 (1990)). The contractor is also liable for the damages caused by the negligence of his subcontractors even though the contractor himself was not negligent. (Miller & Starr, Cal. Real Estate 2d at § 25.5 (1990))

3. Strict Liability.

There is no strict liability against contractors or sub-contractors. See, Ranchwood Communities v. Jim Beat Construction, 57 Cal. Rptr. 2d 386 (1996); La Jolla Village Homeowners' Association, Inc. v. Superior Court, 261 Cal. Rptr. 146 (1989).

4. Fraud.

Although rare, a contractor is liable for fraud in the construction of improvements, such as when a contractor intentionally fails to build improvements according to the contract requirements. (Miller & Starr, Cal. Real Estate 2d at § 25.6 (1990) (citing Balfour, Guthrie & Co. v. Hansen, 38 Cal. Rptr. 525 (1964)).

C. Theories of Liability Against a Design Professional

1. Breach of Contract/Warranty.

Design professionals (e.g., architects or engineers) are liable for breach of contract or breach of any express warranty.

However, like the contractor, a design professional is not generally held liable on a theory of breach of implied warranty. (Miller & Starr, Cal. Real Estate 2d at § 25.22(1990) (citing Huang v. Garner, 157 Cal. App. 3d 404, 412 (1984)); Matthew Bender, Construction Law, ¶ 5A.04[3]). Also, a design professional cannot be found liable for breach of warranty under the Uniform Commercial Code (U.C.C.) since plans are not goods within the meaning of the U.C.C. (Matthew Bender, Construction Law, ¶ 5A.04[3]).

2. Negligence.

A design professional assumes a duty to perform his services in a skillful and careful manner. "The standard is that set by the learning, skill and care ordinarily possessed and practiced by others of the same profession in the same locality, at the same time." Paxton v. Alameda, 119 Cal. App. 2d 393, 399 (1953). The design professional, therefore, is under a duty to exercise such reasonable care, technical skill, ability and diligence as is ordinarily required of design professionals in the course of their plans, inspections and supervision to any person who foreseeably and with reasonable certainty may be injured by their failure to do so. (Matthew Bender, Construction Law, ¶ 5A.06[2].)

3. Strict Liability.

No liability attaches to a design professional on a theory of strict liability. See, Huang v. Garner, 147 Cal. App. 3d 404, 412, fn. 5 (1984).

II. LIMITATIONS ON RECOVERY: STATUTES OF LIMITATIONS AND REPOSE

A. Statutes of Limitations

Construction defect claims are subject to both the four year statute of limitations for breach of contract actions (California Code of Civil Procedure ("CCP") § 337, two years if based on an oral contract (CCP § 339)) and the three year statute of limitations for actions based on injury to property (CCP § 338). Breach of warranty claims are governed by the statutes of limitations for contracts in general, and therefore must be brought within four or two years, depending upon which type of contract is involved. See, e.g., Fundin v. Chicago Pneumatic Tool Company, 199 Cal. Rptr. 789, 795 (1984).

When a construction defect is "patent," the three year statute of limitations for injury to property of CCP section 338 and the four year statute of limitations for breach of contract of CCP section 337 begin to run from the date of "substantial completion of the property." (CCP section 337.1). A patent defect is one which "is apparent by reasonable inspection." Geertz v. Ausonio, 6 Cal. Rptr. 2d 318, 320 (1992) (internal quotation omitted). If a reasonable inspection would reveal only signs of the defect, but not its actual cause, then the defect is not usually considered to be patent. Id.

If, on the other hand, the construction defect is "latent," the three year statute of limitations for injury to property of CCP section 338 and the four year statute of limitations for breach of contract of CCP section 337 do not begin to run until the latent defect is, or should have been discovered. North Coast Business Park v. Nielsen Construction Co., 21 Cal. Rptr. 2d 104 (1993). Courts will consider a defect to be "discovered" when "the damage is sufficiently appreciable to give a reasonable man notice that he has a duty to pursue his remedies." Id. at 107.

Finally, the statutes of limitations will be tolled by an attempt to effect repairs by the defendant. Winston Square Homeowner's Association v. Centex West, Inc., 261 Cal. Rptr. 605 (1989). Mere notification, however, will not toll the statute. Mack v. Hugh W. Comstock Associates, Inc., 37 Cal. Rptr. 466 (1964).

B. Statute of Repose

California Code of Civil Procedure ("CCP") section 337.15 imposes "an absolute requirement that a suit . . . to recover damages for a construction defect be brought within ten years from the date of substantial completion of construction, regardless of the date of discovery of the defect." Regents of

University of California v. Hartford Accident and Indemnity Co., 21 Cal. 3d 624, 631. CCP section 337.15(g) provides in part: "The ten-year period specified . . . shall commence upon substantial completion of the improvement." The ten year statue applies to defects which are latent, and were never discovered. It also will preclude suits for discovered defects which are not brought within its ten year time limit.

III. UNIQUE DEFENSES

A. As-Is Clauses

An as-is clause in a contract may relieve a seller of real property from certain types of liability for defects in the condition of the real property. For example, in Shapiro v. Hu, 188 Cal. App. 3d 324,332 (1986), the court held that absent express warranty, fraud or misrepresentation, the law governing the selling of an old building was "caveat emptor, with the buyer assuming the risk on quality or condition of the property . . . ." Similarly, claims based on trespass, nuisance, and equitable indemnity may be barred by the inclusion of an as-is clause in a sale agreement. See, Galen v. Mobil Oil Corp., 922 F.Supp. 318, 324, 327 (C.D. Cal. 1996).

However, where the sale of real property involves a new building, the California Supreme Court has held that "the builder or seller of new construction . . . makes implied representations, ordinarily indispensable to the sale, that the builder has used reasonable skill and judgment in constructing the building." Pollard v. Saxe & Yolles Development Company, 12 Cal. 3d 374, 379 (1974). Thus, an as-is clause does not bar claims on breach of warranty in all circumstances. Likewise, claims based on strict liability (Seely v. White Motor Company, 63 Cal. 2d 9, 19 (1965)), negligence (Shapiro v. Hu, 188 Cal. App. 3d 324 (1986)), fraud (Loughrin v. Superior Court, 15 Cal. App. 4th 1188 (1993)), or intentional misrepresentation or concealment (Shapiro v. Hu, 188 Cal. App. 3d 324 (1986)) are still available, despite the presence of an as-is clause in a contract. See also, Lingsch v. Savage, 213 Cal. App. 2d 729, 742 (1963).

B. Compliance with Plans and Specifications

As noted above, a contractor who receives plans and specifications from another party, such as an architect, does not assume responsibility for the suitability of those plans and specifications. So long as the contractor performs his work in compliance with the plans and specifications of the contract, the contractor is not liable. (Miller & Starr, Real Estate 2d at ¶ 25.2).

However, this defense is not available where the contractor also acts as the design professional, preparing the plans and specifications, or when he agrees to construct the finished product in accordance with performance specifications. In such cases, the contractor is seen to warrant construction methods and materials and cannot rely on a defense of having followed the plans and specifications. (Cushman & Cushman, Construction Litigation: Representing the Owner (1984), at § 3.12).

IV. MEASURE OF DAMAGES

Where property is damaged by the negligence of a contractor or subcontractor, absent unusual circumstances, the recoverable damages are either the cost to repair the damage or the diminution in value. Mozetti v. City of Brisbane, 136 Cal. Rptr. 751, 756 (1977). There is an exception if the personal loss in value is greater to the owner and the repairs will definitely be made. In that case, the owner can recover the costs of repair in excess of the diminution. (Miller & Starr, Real Estate 2d at ¶ 25.8, fn. 74).

Likewise, damages against a developer or design professional are generally the lesser of the costs to repair or the diminution in value. (See, Miller & Starr, Real Estate 2d at ¶ 25.21, 27). In addition, damages for loss of use may be available, though purely economic losses such as lost profits are not generally available. (Miller & Starr, Real Estate 2d at ¶ 25.21).