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There's No Place Like Home ... Until You Discover Defects: Do Prelitigation Statutes Relating to Construction Defect Cases Really Protect the Needs of Homeowners and Developers

Melissa C. Tronquet
THERE'S NO PLACE LIKE HOME . . . UNTIL YOU DISCOVER DEFECTS: DO PRELITIGATION STATUTES RELATING TO CONSTRUCTION DEFECT CASES REALLY PROTECT THE NEEDS OF HOMEOWNERS AND DEVELOPERS?

Melissa C. Tronquet*

I. INTRODUCTION

Whether a person owns a starter home or a multi-million dollar mansion, discovering a construction defect in that house can be a traumatic experience.1 In the last two decades, residential construction defect litigation throughout the United States has increased dramatically.2 While the flood of litigation in the construction defect arena has kept lawyers busy, these cases have burdened developers, builders, and in-
urers, and the impact of such cases has been particularly pronounced in California. The economic impact on builders, developers, and insurers receives the most notoriety of all the problems relating to construction defect litigation. In response to the large numbers of claims and the high cost of defending construction defect lawsuits, insurers have either drastically limited the coverage they offer or withdrawn altogether from insuring new residential construction projects.

This trend has been particularly pronounced in the condominium market. Faced with soaring rates or no insurance at all, condominium developers either pass on the high insurance costs to buyers or simply elect not to build new housing projects. These problems have led to a void in the condominium market that threatens the availability of affordable housing. The large expenditure of both money and time required to bring a construction defect lawsuit is similarly burdensome


5. Courts have established that insurers of development projects have a duty to defend builders in construction defect lawsuits. See Montrose Chemical Corp. v. Admiral Ins. Co., 897 P.2d 1 (Cal. 1995); Wendy A. Gable, Note, Constructing a Solution to California's Construction Defect Problem, 30 MCGEORGE L. REV. 299 (1999).


In interviews, builders and insurers consistently report that California is more prone to construction-defect litigation relating to condominiums and attached housing units than other states, and that the plaintiff-friendly characteristics of California's legal environment tend to encourage greater numbers of such lawsuits, thereby reducing the number of such units being built.

Id. at 17.

7. There are some astounding statistics about changes insurers have made in response to the flood of construction defect litigation. See, e.g., Gavin, supra note 3 ("[N]ear San Diego, there were 20 to 30 insurers in the late 1980s; now there are no more than four... 17 insurers have pulled out of the state [of Washington] over the past year.").


9. See, e.g., Golden, supra note 4; Wedner, supra note 1.
to owners of single family homes. Courts faced with managing these cases are encumbered by the significant amount of time they demand from the judicial system.

In response to the burdens imposed on all parties, courts and states began developing policies to help mitigate the negative impacts of residential construction defect litigation. Courts in many states have limited tort recovery for economic losses related to residential construction defects. At the forefront addressing problems associated with construction defect litigation, the California legislature has created statutes requiring pre-claim compliance with mandatory dispute resolution procedures. The concepts behind these “prelitigation” statutes have inspired other states to address residential construction defects with similar types of statutes. This comment analyzes whether prelitigation requirements encouraging early resolution of residential construction defect claims can meet the needs of homeowners, developers and builders, insurers, and states.

First, this comment examines traditional legal theories on which construction defect cases may be based, highlighting recent case law developments in California. Next, it outlines problems that construction defect litigation creates for developers, builders, purchasers, and insurers of new homes and reviews two California statutes that require parties involved in construction defect claims to complete specific prelitigation steps before filing formal action. Finally, the comment analyzes the efficacy of those prelitigation requirements.

14. See infra Part II.A.
15. See infra Part II.B.
16. See infra Part II.C.
17. See infra Part II.D.
18. See infra Part III. One statute establishes guidelines for claims of defects in condominium housing, and the other applies specifically to defects in single family residential construction.
requirements and suggests ways for California to improve and adapt the prelitigation process for construction defect claims to more effectively encourage early settlement or other resolution of those claims.19

II. BACKGROUND

A. Theories of Liability in Construction Defect Cases

Construction defect litigation developed in the last half-century as a result of changes in the character of real estate sales.20 Today, homebuyers have several legal remedies available to compensate them for construction defects.21 The theories of liability available to a party alleging construction defects will depend on the circumstances of the claim, and the theories a party chooses can determine both the existence of defects and the extent of recovery allowed for those defects.22 This section describes the most common theories of liability in construction defect actions and their recent treatment by California courts.23

1. Contract: Express Warranty

Under the theory of express warranty, a homeowner may hold a developer or builder liable based on representations made about the quality of a product.24 Either words or actions may create an express warranty,25 and claims of express warranty are commonly based on contract warranties with re-

19. See infra Part IV (discussing ways in which the prelitigation process for condominium defect cases could be improved in California).
21. See Dunstan & Swenson, supra note 2, at 4 (noting that “[i]n both California and the nation, construction defect law has, to a great extent, been created as a result of judicial decisions. . .”).
23. See infra Part II.A.(1)-(4) (outlining four common theories of liability used in construction defect cases).
25. BLACK'S LAW DICTIONARY 1582 (7th ed. 1999).
spect to the performance of work or on warranties provided by manufacturers.\textsuperscript{26}

Warranty claims can be difficult to apply in the context of construction defect claims because a construction contract is not generally viewed as a contract for the sale of goods.\textsuperscript{27} However, some courts have allowed home buyers to sue builders for breach of contract when products included in the sales contract fail to meet express manufacturer warranties.\textsuperscript{28} In such cases, buyers may sue manufacturers for breach of express warranties\textsuperscript{29} and may also be able to sue builders who fail to honor warranties for products that were included in a sales contract.\textsuperscript{30}

2. Contract: Implied Warranty

Until the 1960s, real estate sales were characterized by the principal of caveat emptor—"let the buyer beware."\textsuperscript{31} Generally, this theory insulated sellers from liability because it placed the burden of ensuring quality on the buyer.\textsuperscript{32} However, the dramatic increase in housing construction following World War II\textsuperscript{33} led to both a change in attitude toward buyer/seller relationships\textsuperscript{34} and, unfortunately, a decline in

\begin{itemize}
\item \textsuperscript{26} See id.; see also Castro, supra note 20, at 119.
\item \textsuperscript{27} See Castro, supra note 20, at 119.
\item \textsuperscript{28} See Presiding Bishop v. Cavanaugh, 32 Cal. Rptr. 144, 156-57 (1963) (holding that manufacturer’s express warranty to a contractor applied to the owner of a building for whom the contractor was working because the purpose of the warranty was to encourage consumers to ask their contractors to use the manufacturer product).
\item \textsuperscript{29} See Herman v. Bonanza Bldgs., 390 N.W.2d 536 (Neb. 1986) (holding that a manufacturer brochure purporting to replace or repair defect, when given to an owner, created an express warranty for which the manufacturer could be held liable).
\item \textsuperscript{30} See id.
\item \textsuperscript{31} See SAN DIEGO ASS’N, supra note 20, at 2; Castro, supra note 20, at 100 ("For three centuries, the "maxim" of caveat emptor insulated the home seller from liability for construction defects.").
\item \textsuperscript{32} See SAN DIEGO ASS’N, supra note 20, at 2 (observing that real estate transactions in the caveat emptor era were generally entered into by parties who knew one another, in contrast to buyers and sellers in recent decades who usually know little about each other).
\item \textsuperscript{33} See Castro, supra note 20, at 101 ("Before 1945 new construction was estimated at $2 billion annually. In 1945 new housing starts jumped to $15 billion annually and increased to $18 billion by 1950.").
\item \textsuperscript{34} See SAN DIEGO ASS’N, supra note 20, at 2 ("The common law rule of caveat emptor originated in an environment of repeat transactions between buyers and sellers who knew one another. Modern markets, however, usually involve buyers and sellers who have limited information about one another and
the quality of new homes. As a result, purchasers of defective homes turned to the courts for relief, and the caveat emptor rule was gradually abrogated.

With the rejection of the caveat emptor doctrine, courts began to recognize breach of implied warranty as a valid claim in construction defect cases. The concept of implied warranty originated from the Uniform Commercial Code “sale of goods” rules and involves two policy rationales: (1) buyers rely on the skill of the builder and are not in a position to adequately inspect the construction; and (2) builders have some duty to produce habitable housing and are likely better positioned than buyers to bear economic losses. Because those UCC provisions deal with sales of goods and not real property, the UCC concepts of implied warranty apply to construction cases only by analogy.

The warranties of “fitness for intended purpose” and “reasonably workmanlike construction” apply most commonly in construction defect cases. The implied warranty doctrine benefits plaintiffs because warranties are based on expectations or reliance on builder work; therefore, recovery does not necessarily require a showing of physical property damage. However, the implied warranty doctrine is limited in con-

35. See Castro, supra note 20, at 101 (observing that poor quality and defects were inevitable results of the huge quantities of new housing being produced in such a short time).
36. See SAN DIEGO ASS’N, supra note 20, at 2; Castro, supra note 20, at 101 (citing the Colorado case of Carpenter v. Donohoe, 388 P.2d 399, 402 (Colo. 1964) as the first case to reject caveat emptor, and noting that “since Carpenter, an avalanche of appellate decisions throughout the nation have rejected the doctrine of caveat emptor . . .”).
37. See Castro, supra note 20, at 102.
38. See id.
39. See Pollard v. Saxe & Yolles Dev. Co., 525 P.2d 88 (Cal. 1974) (applying implied warranty theory to design and construction of apartment buildings); Schipper v. Levitt & Sons, Inc., 207 A.2d 314 (N.J. 1964) (holding that a builder should be liable for burn injuries caused by improper installation of a hot water valve because the buyer relied on the skill of the builder in presuming that the house would be “reasonably fit for habitation”); Kuitems v. Covell, 231 P.2d 552 (Cal. 1951) (holding that a contractor could be liable for improper installation of a roof because there is a good-faith duty to perform contractual obligations with reasonable skill).
40. See Castro, supra note 20, at 105; ACRET, supra note 22, § 8.23; see also Pollard, 525 P.2d 88.
41. See ACRET, supra note 22, § 8.24-.25.
struction defect claims. Plaintiffs must give builders reasonable notice of a defect, and file claims within time periods required by statutes of limitations. In some jurisdictions, plaintiffs may only apply the doctrine of implied warranty in cases involving new construction.

3. Tort: Negligence

Until recently, plaintiffs often included negligence as a cause of action in construction defect cases, alleging that home builders have certain duties of care to home buyers. In construction defect cases involving negligence claims, plaintiffs must establish the basic elements of the tort: duty, breach of duty, causation, and harm. The most contentious element of negligence claims for construction defects is often the extent of harm necessary for recovery because it can be

43. See id. at 773 (suggesting that plaintiffs must show that claimed defects are inherent and “substantially certain” to malfunction).
44. See Pollard, 525 P.2d at 90.
45. Statutes of limitation for construction defects can be fairly complicated. See, e.g., CAL. CIV. PROC. CODE § 337 (West 2000). This statute offers no definitions of construction defects, but distinguishes between “patent” and “latent” defects. Patent defects are apparent or easily discoverable, and there is a four year statute of limitations for such defects. Id. § 337.1. Latent defects are not visible or easily discoverable, and there is a ten year statute of limitations for these defects. Id. § 337.15. California also has a ten year statute of repose specifically for construction defects, which applies to latent defects. Id. Unlike statutes of limitations, which run from the time the injury is discovered, statutes of repose run from the time of substantial completion of a structure. For a discussion of California’s statutes of limitation and repose and a comparison to such statutes in other states, see KROLL ET AL., supra note 6, at 19-21.
46. See E. Hilton Drive Homeowners Ass’n v. W. Real Estate Exch., 186 Cal. Rptr. 267 (1982) (holding that plaintiffs could not use a theory of implied warranty when they purchased their homes from a vendor who purchased them four years prior to selling them to plaintiffs); see also Castro, supra note 20, at 107-08 (discussing the fact that the definition of “new construction” is not settled, and the viability of the implied warranty defense in such cases will often depend on the positions of the parties involved).
difficult to define the "harm" that poor construction causes.\textsuperscript{49} A defect can substantially reduce the value of a home without causing actual physical damage.\textsuperscript{50} Builders argue that even if a defect violates construction standards, no real harm occurs if the defect has not caused physical damage or injury.\textsuperscript{51} From a homeowner’s perspective, however, defects can cause harm by creating physical damage that will require repair, and potentially reducing the value of the home.\textsuperscript{52}

Several states limit negligence liability for defects that have not caused tangible harm.\textsuperscript{53} Known as the "economic loss rule," this principle bars tort recovery in cases where a defect has not caused physical damage to the property or actual injury.\textsuperscript{54} In jurisdictions that apply the economic loss rule, plaintiffs suffering solely from negative economic impacts of faulty construction cannot recover for negligence.\textsuperscript{55}

\textsuperscript{49} See SAN DIEGO ASSN, supra note 20, at 3-4.
\textsuperscript{50} See id. (observing that any defect "reduces the value of the structure; and clearly, it seems absolutely necessary to repair it. But in the law of tort, something that is merely defective, but has not caused physical harm to people or property, has only caused 'economic damage,' which is not true damage in the tort sense").
\textsuperscript{51} See Wedner, supra note 1 (noting a common belief held by builders that owners often include claims for "frivolous" defects because lawyers convince them to include those defects, not because those owners are truly concerned about potential damage).
\textsuperscript{52} See id. (giving examples of construction defects that cause physical damage, physical injury, and economic harm, and noting that all defects are potentially harmful from the homeowner perspective).
\textsuperscript{53} See KROLL ET AL., supra note 6, at 20.
\textsuperscript{54} See Alan C. Eagle & Frank J Giliberti, Economic Loss Rule Limits Plaintiff’s Ability to Recover Damages, 1 MEALEY’S LITIG. REP.: CONSTRUCTION DEFECTS 11 (Dec. 2000). The authors discuss negligence claims in construction defect cases:

A lawsuit over alleged construction defects may assert... claims for negligence that contend that the plaintiffs suffered property damage, property damage and economic loss, or economic loss alone. It is generally well accepted that a defendant that negligently injures a plaintiff may be liable for all proximately caused harm, including economic losses. However, a virtually per se rule in courts across the country, known as the economic loss rule, bars recovery for economic loss unless the negligent conduct also caused physical harm.

Id. (citations omitted).
\textsuperscript{55} See, e.g., KROLL ET AL., supra note 6, at 20 (reporting that twelve of twenty-one states surveyed in a construction defect litigation study apply the economic loss doctrine, including Arizona, California, Colorado, Florida, New York, and New Jersey). See generally AM. B. ASSN COMMITTEE ON CONSTRUCTION DEFECT LITIG., STATE-BY-STATE SURVEY OF THE ECONOMIC LOSS DOCTRINE IN CONSTRUCTION LITIGATION: A REPORT OF THE SUBCOMMITTEE ON DAMAGES AND THE SUBCOMMITTEE SURVEY OF STATE LAWS
Homeowners argue that this rule excuses careless builders from responsibility for repair of potentially serious defects. Builders, however, support application of the rule and argue that it reduces "frivolous" claims for defects that may never cause damage.

4. Tort: Strict Liability

Strict liability allows plaintiffs to hold manufacturers responsible for damage caused by products regardless of fault, so that plaintiffs need not prove that a manufacturer violated the standard of reasonable care. Like product manufacturers, housing developers and designers are in a better position to assume the risk of loss than home buyers. When strict liability is applied in construction defect actions, courts generally limit it to cases involving mass-produced or multiple-unit housing.

A. Recent Judicial Treatment of Theories of Liability in California

1. Limits on Tort Recovery for Defects: Aas v. Superior Court

In the 2000 case of Aas v. Superior Court, the California
Supreme Court upheld the economic loss rule in California, limiting tort claims in construction defect cases to defects that had already caused physical damage.62

In Aas, homeowners sued the developer and general contractor for negligence, strict liability, breach of contract, and breach of implied and express warranty.63 The plaintiffs sought damages for the cost of repairing the defects as well as damages for diminution in the value of their homes.64 With respect to the negligence claim, the trial court granted the defendant's motion in limine to exclude evidence of the defects that had not caused property damage.65 The court of appeals upheld this ruling.66

The court held that without property damage or physical injury, the plaintiffs in Aas could not recover in negligence for economic losses alone.67 After analyzing the different theories of tort liability and their application to construction defect claims, the court concluded that actions for defects that have not yet caused damage are more appropriate for the field of contract law.68 Finally, the court applied the economic loss rule to bar negligence claims for defects that had not caused damage.69

Chief Justice George agreed with the majority that "minor defects"70 which do not create sufficient risk of injury or damage to property should not be included in negligence ac-

62. Id. at 1130.
63. Id. at 1128.
64. Id.
65. Id. at 1129.
66. Id.
67. Aas, 12 P.3d at 1130.
68. The court noted,
Speaking very generally, tort law provides a remedy for construction defects that cause property damage or personal injury. Focusing on the conduct of persons involved in the constructions process, courts in this state have found such a remedy in the law of negligence. Viewing the home as a product, courts have also found a tort remedy in strict products liability . . . . Any construction defect can diminish the value of a house. But the difference between price paid and value received, and deviations from standards of quality that have not resulted in property damage or personal injury, are primarily the domain of contract and warranty law or the law of fraud, rather than of negligence.
69. Id.
70. Id. at 1138 (citing "doors that are out of plumb, discolored drain stoppers, and inoperable garbage disposals" as examples of such "minor" defects).
But the Chief Justice also dissented, arguing that some serious defects pose significant potential risks, and that a homeowner should be allowed to maintain a negligence action for serious defects even when they have not manifested damage. Although the Chief Justice argued that the distinction between major and minor defects appealed to common sense and sound economic policy, the majority thought that it would be an unworkable distinction in practice.

Developers and builders praised the Aas decision as a positive step in the direction of limiting frivolous construction defect claims. However, home buyers, their attorneys, and some legislators criticized the decision as an inappropriate solution to the problems of excessive construction defect litigation. The Aas decision helped clarify California's perspective on economic loss and negligence claims, but did not address the extent of damage required for recovery under other theories of liability in construction defect actions.

71. Id. at 1143.
72. Id. (citing improperly constructed walls that would create risks of collapse in earthquakes or high winds, or that would allow a fire to spread rapidly as examples of serious defects).
73. Aas, 12 P.3d at 1143 (arguing that allowing negligence recovery "would not require [the court] to break new ground . . . [and] also best comports with rational economic policy, as well as common sense").
74. Id. ("It obviously is preferable to pay a relatively few dollars at an early date to correct a serious safety risk that may cost millions or billions of dollars to redress if the inhabitants are forced to wait for disaster to strike and for death, personal injury, or physical property damage to ensue.").
75. Id. at 1140-41. The author noted that "the proposal entails serious difficulties . . . . The distinction between serious and minor defects has a superficial theoretical appeal that evaporates in practice" because it would force courts and experts to speculate on the "potential seriousness of possible property damage" and that such speculation would "insulate from demurrer and summary judgment virtually all complaints containing allegations of building code violations." Id.
76. See Cynthia A. R. Woollacott, In the Land of Aas: The California Supreme Court has Ruled that Damages from Construction Defects Must be Manifest in Order to Bring a Tort Cause of Action, 24 L.A. LAWYER 35 Jan. 2002.
77. See id. at 35-36 (noting that even though Aas was considered a "victory" for builder/defendants, plaintiffs and defendants in defect cases may still have several effective claims). Courts in other states have also applied the economic loss doctrine to construction defect claims; see also Calloway v. City of Reno, 993 P.2d 1259 (Nev. 2000).
78. Aas, 12 P.3d 1125.
79. See Woollacott, supra note 76, at 42 (observing that "whether contract related damages constitute property damage under insurance policies might be the next subject of appellate scrutiny").
2. Express and Implied Warranty as Alternatives to Tort Recovery

The *Aas* ruling was only a partial victory for developers and builders in limiting defect claims.\(^{80}\) Although the decision foreclosed negligence recovery for purely economic losses, the *Aas* court noted explicitly that it did not preclude recovery under theories of contract or warranty.\(^{81}\) In the 2001 case of *Hicks v. Kaufman & Broad Homes Corp.*,\(^{82}\) the California Supreme Court allowed recovery under an implied warranty theory for defects that had not yet caused damage, and cited *Aas* as support.\(^{83}\)

Homeowners in *Hicks* sued the developer for the cost of replacing defective concrete slabs that had not yet displayed damage.\(^{84}\) The court allowed the plaintiffs to use theories of breach of express and implied warranty to recover for defects that had not manifested physical damage by proving that the slabs contained "an inherent defect which is substantially certain to result in malfunction during the useful life of the product."\(^{85}\) The court held that the product's defect was enough for recovery, reasoning that the plaintiffs had a right under warranty to a product free of defects.\(^{86}\) The remedy was the cost of replacing the defective slabs.\(^{87}\)

Although *Hicks* primarily addressed the right to recover for defects in the context of class action certification, the decision is important because it also reveals the court's view that actual physical damage from defects is not a condition prece-
dent to recovery. While the terms “inherent defect” and “substantially certain to malfunction” can be debated in future cases, Hicks preserves a plaintiff’s right to recover for defects that have not caused damage.

C. New Home Construction and Construction Defect Litigation

The condominium market has absorbed many of the effects of construction defect litigation. In the 1980s, condominiums became popular among developers and homebuyers because they were more affordable to construct and purchase than single family homes. Often, builders could not find enough skilled construction workers to complete the large numbers of projects. Shoddy construction resulted and, consequently, unhappy homebuyers.

Single family homeowners also sue over construction defects, but cases involving condominium and common interest development projects have probably received greater attention because condominium defects are frequently more pronounced. Lawsuits by condominium homeowner associations often require more money, resources, and effort than suits by single family residence homeowners. Particularly

88. Id. (stating “we see no reason why a homeowner should have to wait for the inevitable injuries to occur before recovering damages to repair the defect and prevent the injuries from occurring”).
89. Hicks, 107 Cal. Rptr. 2d 761.
90. See, e.g., Dunstan & Swenson, supra note 2, at 1 (stating that “construction defect litigation has been blamed for destroying the condominium market”); SAN DIEGO ASS‘N, supra note 20, at 2 (stating that “the surge of condominium construction defect litigation in the last 20 years has significantly reduced condominium construction”).
91. See SAN DIEGO ASS‘N, supra note 20, at 4-5 (describing how a thriving economy led to an increase in residential construction, how both experienced and inexperienced builders could easily obtain loans, and how projects were frequently constructed by unskilled workers); see also Dunstan & Swenson, supra note 2, at 1-3 (describing the builder-friendly real estate market of the 1980s).
92. See, e.g., Dunstan & Swenson, supra note 2, at 1-2 (presenting a graph of multi-family permit data from 1980-1999; while multi-family permits include apartments and condominiums, the graph shows a major increase in multi-family projects in the 1980s, followed by a sharp decline in the 1990s).
93. See id. at 1.
94. See, e.g., Kenneth Harney, New Dispute-Resolution Law Helps Avoid Suing the Builder, BALTIMORE SUN, June 23, 2002, at IL; see also Wedner, supra note 1.
95. Condominium owners have a larger resource pool than single family homeowners and therefore have more leverage in making defect claims. In
in large condominium defect cases, claims by homeowner associations utilizing multiple theories of liability can lead to enormous costs for developers who must defend the claims. Builders argue that both condominium and single family homeowners exacerbate defect actions when they include claims for defects that have little or no impact on the structure or the homeowner. Homeowners and their attorneys point out that litigation is an important measure for preserving homeowners' rights against defects in poorly constructed homes. Homeowners simply want problems fixed, and litigation is often a "last resort" to which discouraged owners turn when builders or developers fail to respond adequately.

The full effect of construction defect litigation is difficult to quantify because many other factors influence the housing market. In response to the flood of defect lawsuits in the 1990s, insurers began to increase premiums for builders of condominium developments, or refuse to insure condominum associations’ rights against defects in poorly constructed homes. California, the Davis-Stirling Common Interest Development Act gives homeowner associations the right to make claims on behalf of all owners in their communities. In addition, owners in common interest developments are well-positioned to file class action claims. See Dunstan & Swenson, supra note 2, at 1, 5; see also SAN DIEGO ASS'N, supra note 20, at 3 (noting that condominium associations not only have more resources to sue than individual homeowners, but also have a fiduciary duty to investigate and correct certain construction problems).

96. See Wedner, supra note 1 (citing examples of cases in which plaintiffs complained of fairly minor defects that builders finally settled for amounts far exceeding the cost of the actual problem).

97. See, e.g., Pierce, supra note 10; Wedner, supra note 1; Zito, supra note 3.

98. See Pierce, supra note 10 (quoting a consumer-advocate who claims that "if builders responded promptly to requests for repairs, the defects wouldn't mushroom into the larger problems that force frustrated homeowners into lawsuits").

99. See id. That construction defect cases are commonly taken on a contingent fee basis is an additional factor that also might explain why they go to trial so often.

100. For a full explanation of factors impacting research on construction defect litigation and the condominium market, see Dunstan & Swenson, supra note 2. See also KROLL ET AL., supra note 6. These authors observe that data collection for both condominium construction, and the multitude of other factors influencing the condominium market, are inadequate to formulate conclusive observations about the exact impact of defect litigation on condominium development.

101. See, e.g., Montrose Chem. Corp. v. Admiral Ins. Co., 897 P.2d 1 (Cal. 1995) (holding insurer responsible for any potential liability for continuous and progressive damages when insurer had a policy in effect during the period of damage). For full analysis of insurer indemnity and construction defect claims, see Gable, supra note 5.
ium developments altogether. Coupled with the risk of lawsuits, the increased cost of insurance discouraged developers from constructing new condominium projects. The lack of condominium construction has seriously impacted the housing market—most notably the affordable housing market.

Theorizing that builders who face less defect litigation will be more able and willing to apply their time and resources to new construction, and that homeowners will stop turning to the courts if they have a greater opportunity to get defects fixed, state legislatures have targeted statutory reform as one way to combat the problems of construction defect litigation. Therefore, legislatures have begun to formulate statutes designed to encourage negotiation and promote settlement before homeowners file defect actions.

D. The California “Calderon Process” for Common Interest Developments

In 1995, the California legislature added section 1375 to the Davis-Stirling Common Interest Development Act. Known as the “Calderon Process,” this law established a detailed set of requirements for homeowners’ associations to fulfill before proceeding with formal defect claims against builders. Section 1375 is limited to cases involving common

102. See SAN DIEGO ASS’N, supra note 20, at 6 (citing a California Research Bureau study that concluded that the number of insurers for condominium projects in California declined from more than 40 in the 1980s, to less than 3 today); see also Zito, supra note 3 (citing California construction insurance data stating “for every $1 insurers collected in 1998, they paid out nearly $1.87; in 2000, insurers paid out about $2.95 for every dollar in premiums”).

103. See Jesus Sanchez, Ruling by Court Unlikely to Spur Condo Constructions Housing: Despite New Limits on Negligence Lawsuits, California Builders Still Face High Cost of Defect Insurance, L.A. TIMES, Dec. 9, 2000, at A2 (“[A]s a result of litigation, condo builders have seen liability insurance premiums on such [condominium] projects soar, making it economically infeasible to build all but the most expensive condos.”).

104. See, e.g., Pierce, supra note 10; Sichelman, supra note 10; Wedner, supra note 1; Zito, supra note 3.

105. See, e.g., Pierce, supra note 10; Sichelman, supra note 10; Wedner, supra note 1; Zito, supra note 3.


107. Id. For a general discussion of section 1375 as originally enacted, see KROLL ET AL., supra note 6, at 29-30.

108. The Calderon Process was named for Senator Calderon, who introduced the bill and was its main proponent.

109. See KROLL ET AL., supra note 6, at 29; see also ACRET, supra note 22, at § 8.45.
interest developments of more than twenty units and therefore applies mainly to defect claims initiated by homeowners’ associations.

The original goal of the Calderon Process was to encourage more efficient resolution of construction defect disputes by providing a mandatory period for settlement negotiation before trial. As originally enacted, section 1375 required plaintiffs to give builders notice of defects and results of testing for defects. It also mandated a ninety-day settlement period before a formal claim could be filed. However, the process was criticized as an ineffective way to limit litigation. Industry experts argued that the ninety-day period required by the act was too short to promote meaningful negotiation, that the lack of penalties for noncompliance with section 1375 requirements made the guidelines ineffective, and that the statute did not effectively discourage litigation because subcontractors were not required to participate.

The California legislature responded to criticism of the original Calderon Process and the 2000 Aas decision by amending the Calderon Process in 2001. The new provisions took effect for actions filed after July 1, 2002. The revised Calderon Process is designed to include all parties and make the prelitigation process more efficient.

Under the new process, a homeowners’ association must first serve builders or developers with a “Notice of Com-

111. See KROLL ET AL., supra note 6, at 29.
112. See CAL. CIV. CODE § 1375.
113. See id.; see also KROLL ET AL., supra note 6, at 29.
114. For a full discussion of the shortfalls of the original Calderon Process, see Leslie Steven Marks & Ryan P. Eskin, Defective Solutions: Legislation Intended to Encourage the Resolution of Condominium Defect Disputes May Inhibit Effective Association Management, L.A. LAWYER, Jan. 2003, at 39 (remarking that the section 1375 dispute resolution process “often seemed to be nothing more than a speed bump on the road to full-blown litigation”).
115. Id.; see also KROLL ET AL., supra note 6, at 29 (remarking that “without being legally compelled to participate, subcontractors and their carriers rarely volunteered to contribute toward pretrial settlement offers, thereby increasing plaintiffs’ motivation to pursue larger awards through a trial”).
116. CAL. CIV. CODE § 1375.
117. Id. § 1375.05(h).
118. See id.; see also KROLL ET AL., supra note 6, at 29 (noting that the revisions to section 1375 are the result of compromise between builders, homeowners, and attorneys, and are thus likely to be fairly balanced in the burdens those provisions impose).
mencement of Legal Proceedings. Service of this notice begins a 180-day period for the parties to attempt to resolve the problems, which may be extended with the consent of all parties. Alternatively, if the parties fail to reach a settlement by the end of the original or extended period, the association may then file an official complaint.

Upon receipt of the notice, the builder must comply with the timeline and requirements set forth in section 1375. Within twenty-five days of receipt, the builder may request a meeting with the association. Within sixty days, the builder must (1) give the association access to relevant documents, and (2) send written notification to all subcontractors, design professionals, and insurers (collectively, “respondents”). Following these disclosures, the parties must select a dispute resolution facilitator.

The parties are required to attend a meeting with the facilitator and develop a case management plan within one hundred days of the initial notice. The main duty of the

119. CAL. CIV. CODE § 1375(b) (1996 & Supp. 2003). This notice should describe the project, provide an initial list of defects and an explanation of the damage arising from those defects, and provide summaries of testing and homeowner surveys about the relevant defects. *Id.*

120. *See id.* § 1375(c). This change doubled the settlement period.

121. *Id.*

122. *See id.* Parties may extend the original 180-day period for one additional period of 180 days; when the second period expires, the mandatory prelitigation requirements are complete. *Id.*

123. *See id.* § 1375(d).

124. *See id.* § 1375(d) (specifying that the meeting request must be made in writing, and the meeting itself must take place not more than ten days after the written request is made).

125. The association must provide the builder with the same access. CAL. CIV. CODE. § 1375(e)(1). The goal of this section is to facilitate the discovery process, as it requires each party to make available “all files reasonably calculated to lead to the discovery of admissible evidence regarding the defects claimed.” *Id.* Further, each party is required to prepare a privilege log for any documents withheld based on the privilege. *Id.*

126. *Id.* § 1375(e)(2). The language regarding additional parties in this provision is fairly broad, requiring notice to “all subcontractors, design professionals, their insurers, and the insurers of any additional insured whose identities are known to the respondent or readily ascertainable by review of the project files or other similar sources and whose potential responsibility appears on the face of the notice.” The additional parties must then provide information about their own insurers. *Id.*

127. *See id.* § 1375(f)(1). This selection meeting should occur not later than twenty days after the respondent notifies subcontractors and other parties. CAL. CIV. CODE. § 1375(f)(1).

dispute resolution facilitator is to set case management guidelines, and help the parties establish guidelines for fulfillment of required elements of the prelitigation process. With the help of the facilitator, the parties will set deadlines for submitting requests and settlement offers. Respondents are entitled to (1) request one meeting with the homeowners’ association board to discuss a settlement offer, and (2) make a written settlement offer that includes an explanation of the terms and reasons for the offer.

Within ten days of receiving a settlement offer, the association board must hold a meeting to decide whether to accept or reject the offer. If the board decides to reject the offer and file an action for damages, it must hold a meeting open to all members of the association before beginning the action, and provide all owners with written notice fifteen days prior to that meeting. Upon completion of these requirements, and assuming no resolution is reached, the homeowners’ as-

129. See id. § 1375(h)-(j). The dispute resolution facilitator also has an overall duty to resolve the conflict in a “fair manner.” See id. § 1375(f)(1)-(3).
130. See id. § 1375(h). These elements include (1) a “document depository,” (2) a more detailed list of defects the association claims, (3) provisions for non-intrusive and invasive testing by the association and respondents (when necessary), (4) a “comprehensive” demand by the association (and appropriate allowances for modification of that demand), and (5) provisions for “facilitated dispute resolution of the claim” requiring parties with settlement authority to attend dispute resolution sessions. Id.
131. See CAL. CIV. CODE § 1375(k).
132. See id. § 1375(k)(1)(A).
133. See id. § 1375(k)(C).
134. See id. § 1375(k)(D) (requiring the meeting to occur at least fifteen days before the claim is filed).
135. See id. § 1375(k)(D). Notice of the meeting must be given at least fifteen days before the meeting occurs, and must include the time and place of the meeting, identification of the problems that lead to the settlement negotiations and potential action, options/alternatives to address the problems, a discussion of how the association can pay for those alternatives, and finally, the text of the settlement offer and the explanation of the reasons for the terms of the offer. Id. § 1375(k)(E).
136. Note that a respondent may petition the court to allow additional testing if the respondent shows all of the following: (1) the insurer for that respondent did not have notice of the 1375 claim at least thirty days prior to the time inspections/testing began, (2) the insured party of that insurer did not participate in the inspections/testing, (3) the insurer retained separate counsel after receiving notice that the formal complaint was filed and that counsel did not participate in the section 1375 process, (4) the insured party is reasonably likely to suffer prejudice if additional testing is not allowed, and (5) information the party would obtain in the testing is not available from any other source. Id. § 1375.05(c).
sociation may then file a formal action.\textsuperscript{137} The homeowners’ association may also file suit if the respondent elects not to provide a written statement.\textsuperscript{138} When the association files a formal complaint, section 1375.05 provides that the action will be given trial priority, so that associations do not feel time spent on settlement negotiations was a penalty.\textsuperscript{139}

Section 1375.05 also creates penalties for noncompliance with the prelitigation procedures.\textsuperscript{140} Parties who had notice of the settlement negotiations but failed to participate will be bound by any settlement reached.\textsuperscript{141} Once the action is filed, any party may allege that another did not comply with the section 1375 procedures by the association.\textsuperscript{142} If the court finds substantial noncompliance, it will stay the action for ninety days to allow the delinquent party to establish compliance.\textsuperscript{143}

\textbf{E. Senate Bill 800: Construction Defects in Single Family Homes}

In September 2002 Governor Gray Davis signed into law Senate Bill 800.\textsuperscript{144} Like the Calderon Process, Senate Bill 800 sets new standards governing construction defect claims, yet it applies only to single family, non-condominium residences purchased after January 1, 2003.\textsuperscript{145} Codified in California Civil Code sections 895-945.5, Senate Bill 800 incorporates

\textsuperscript{137} See \textit{CAL. CIV. CODE} § 1375.05(a).
\textsuperscript{138} See \textit{id.} § 1375 (k)(B). If the respondent either fails to submit, or elects not to submit, an offer by the deadline established by the dispute resolution facilitator, the plaintiff/association is excused from satisfying the remaining requirements of section 1375(k), and is free to file a formal complaint. \textit{Id.}
\textsuperscript{139} See \textit{id.} § 1375.05 (a). Further, section 1376.05(b) provides that, in assigning this trial priority, the court must consider the date of service of the notice on the builder as the filing date of the complaint, and assign the earliest possible trial date.
\textsuperscript{140} See \textit{id.} § 1375.05(g).
\textsuperscript{141} See \textit{id.} § 1375.05(d).
\textsuperscript{142} \textit{Id.} § 1375.
\textsuperscript{143} See \textit{CAL. CIV. CODE} § 1375.05(g). When a party makes an allegation of noncompliance, the court will schedule a hearing to determine whether or not there was “substantial noncompliance” with the prelitigation procedures. \textit{Id.} § 1375.05(g)(2)-(3). Remedies for noncompliance are within the discretion of the court, determined in part by the extent of compliance with the section. \textit{Id.} § 1375.05(g)(3)(B).
\textsuperscript{144} The law was codified as Civil Code section 895-945.5 (West 2004), but is commonly referred to in recent articles addressing construction defects as “Senate Bill 800.” See, e.g., Marks & Eskin, \textit{supra} note 114.
\textsuperscript{145} \textit{CAL. CIV. CODE} § 895(f).
and expands upon the prelitigation requirements that were originally developed in the Calderon Process. The prelitigation procedures in Senate Bill 800 provide owners of residences to which the law applies with three options for dispute resolution before they can file a defect claim, including repair of the alleged defects, mediation, or a cash settlement.

The sale of a new home triggers the provisions of Senate Bill 800. The statute requires builders to choose at the time the home is sold whether they will use a dispute resolution method other than the procedures outlined in the statute in the event of a dispute over a defect in the home, and to notify the buyer of that choice no later than close of escrow. This choice of dispute resolution methods is binding on the builder, buyer, and buyer's successors in interest, and if the builder does not choose an alternative process at the time of sale, he will be bound to the statutory requirements.

Under Senate Bill 800, a homeowner initiates the claim process by sending written notice of the defect or defects to the builder, stating that the owner is alleging a defect, and describing the character, nature, and location of that defect. The builder then has fourteen days to acknowledge receipt of the homeowner's notice in writing. The builder may inspect the alleged defects (but must request to perform tests) and complete that inspection within fourteen days after acknowledg-

146. Essentially, this statute applies only to single family residential construction because defects in condominium projects are governed by the Calderon Process. Id.
147. Id. § 914(a) describes the goal of the dispute resolution process required by the statute. "This chapter establishes a non-adversarial procedure, including the remedies available under this chapter which, if the procedure does not resolve the dispute between the parties, may result in a subsequent action to enforce the other chapters of this title." Id.
148. Id. § 938.
149. The choice of dispute resolution is binding on the builder:
At the time the sales agreement is executed, the builder shall notify the homeowner whether the builder intends to engage in the non-adversarial procedure of this section or attempt to enforce alternative non-adversarial contractual provisions. If the builder elects to use alternative non-adversarial contractual provisions in lieu of this chapter, the election is binding, regardless of whether the builder's alternative non-adversarial contractual provisions are successful in resolving the ultimate dispute or are ultimately deemed enforceable.

Id. § 914(a).
150. Id.
151. CAL. CIV. CODE § 910.
152. Id. § 913.
edging receipt of the homeowner's notice of defects.\textsuperscript{153} If the builder determines that additional testing is necessary, he must request an additional inspection within three days of the initial inspection, and complete the second inspection within forty days of the initial tests.\textsuperscript{154} The builder is responsible for all costs of the inspections and must also provide adequate assurance that any damage caused during the tests will be promptly repaired.\textsuperscript{155}

Within thirty days of the final inspection, the builder must choose one of three options: (1) make no settlement offer at all and allow the litigation to proceed, (2) make a cash settlement offer, or (3) make an offer to repair the defects.\textsuperscript{156} Obviously, a builder who elects not to make any offer at all chooses to accept the costs and consequences of litigation. Similarly, a homeowner who receives a cash settlement offer has the unqualified right to either accept the cash payment or reject the offer and proceed to litigation.\textsuperscript{157} As a result, builders who offer cash settlements take the risk of allowing the homeowner to decide whether or not to litigate.\textsuperscript{158} In contrast, offering to repair the problem may lower a builder's risk of litigation because the statute gives builders an absolute right to repair the defects before the homeowner can initiate the process of litigation.\textsuperscript{159}

The offer to repair must contain "a detailed, specific, step-by-step statement identifying the particular violation that is being repaired, explain[] the nature, scope, and location of the repair, set[] a reasonable completion date for the repair,"\textsuperscript{160} and must be accompanied by a statement offering to mediate if the homeowner so chooses.\textsuperscript{161} Builders who de-

\textsuperscript{153} Id. § 916(a).
\textsuperscript{154} Id. § 916(c).
\textsuperscript{155} Id. § 916(a).
\textsuperscript{156} See CAL. CIV. CODE §§ 916-917.
\textsuperscript{157} The statute allows the builder to obtain a reasonable release from the homeowner for a cash settlement. Id. § 929(B).
\textsuperscript{158} Since the homeowner is only required to allow repair efforts, builders who make offers that do not include repair take the risk of owners rejecting those offers simply because they are not required to accept them. See id. § 929(a).
\textsuperscript{159} See id. § 919 (allowing builders to repair defects if mediation fails to resolve disputes over the builder's settlement/repair offer); see also discussion infra Part II.B.
\textsuperscript{160} Id. § 917.
\textsuperscript{161} Id. § 919.
cide to repair only some of the claimed defects must include a
detailed explanation of the reasons the offer does not provide
for repair of every defect. If homeowners choose to allow
the builder to repair, they have thirty days after receiving the
offer to either authorize the repairs set forth or request that
the builder provide the names of up to three additional con-
tractors to complete the repair work. The builder must pro-
vide the names of additional contractors within thirty-five
days of such a request, and a homeowner then has twenty
days to choose one of those contractors and notify the builder
of that choice.

Alternatively, the homeowner can respond to an offer by
requesting mediation of the dispute. The mediation session is
limited to four hours and must occur within fifteen days of
the date of the homeowner request. The mediator should be
selected and paid for by the builder; homeowners who want
to participate in choosing the mediator must pay half the cost
of the mediation session. However, the statute gives the
builder the right to repair even if the parties do not reach a
mutually agreeable result at the mediation: “If a builder has
made an offer to repair a violation, and the mediation has
failed to resolve the dispute, the homeowner shall allow the
repair to be performed either by the builder, its contractor, or
the selected contractor.”

Finally, builders may be penalized for failing to comply
with the prelitigation requirements. A builder’s failure to
respond to homeowner concerns or complete any of the pre-
litigation requirements within the specified time frames will
constitute a waiver of all rights to which builders are entitled;
a homeowner may dispense with the prelitigation require-
ments and file a formal claim as soon as the builder fails to
comply with any statutory requirement. In contrast, if a

162. CAL. CIV. CODE § 924.
163. Id. § 918.
164. Id.
165. Id. § 919.
166. Id. However, the statute does not define “nonaffiliated mediator.”
167. Id.
168. CAL. CIV. CODE § 919.
169. See id. § 915.
170. See id. § 919 (releasing homeowner from further compliance with pre-
litigation requirements if builder fails to acknowledge the notice or request an
inspection within the required timeframe); id. § 916(d) (releasing the home-
owner from prelitigation requirements if builder fails to actually complete the
homeowner fails to comply with the requirements before filing a formal claim, builders may only request a stay of the action until the requirements have been satisfied.171

From an evidentiary standpoint, all communications occurring during the prelitigation process between homeowners and builders, with the exception of the four hour mediation, are admissible in subsequent proceedings.172 The fact that the builder makes efforts to repair the defect will not prevent the homeowner from offering evidence of the condition of the property before the repair.173 Similarly, the fact that the builder attempted repair is also admissible. Further, the statute specifies that “evidence of both parties’ conduct during this process may be introduced during a subsequent enforcement action, if any.”174

The prelitigation requirements of both the Calderon Process as well as Senate Bill 800 highlight two significant issues facing parties in residential construction defect disputes. First, although prelitigation statutes exist to encourage settlement, and the primary interests of the parties involved in these cases are quite divergent, it is unclear whether the statutes will in fact achieve this goal or simply delay formal litigation.175 Homeowners want to be compensated for shoddy construction affecting the value of their homes; builders want to minimize litigation costs and avoid paying large awards; the government wants to ease the burden that prolonged defect cases create for the court system.176 Second, given the various theories of liability available to homeowners in construction defect actions, as well as the ambiguities that remain after recent decisions such as Aas,

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171. Id. § 930(b).
172. See id. §§ 933-934.
173. Id.
174. CAL. CIV. CODE §§ 933-934.
175. See, e.g., John Boyden, Chapter 40 and Construction Defect Litigation—Boom or Bust?, NEV. LAWYER, Jan. 2002 (arguing that the Nevada prelitigation procedures may, in fact, encourage litigation because homeowners have little to lose in taking their claims to court); Marks & Eskin, supra note 114 (arguing that mandatory homeowner association disclosure of settlement offers to owners may have a chilling effect on defect litigation because required disclosure could compromise the association’s position of authority).
176. See discussion supra Part II.C.
many prelitigation statutes provide no clear guidelines for judging what kind of damage should be actionable, creating an additional barrier to meaningful settlement negotiations.\(^{177}\)

### III. Problem

Both the Calderon Process revisions and Senate Bill 800 were designed to address the main concerns about construction defect litigation in California.\(^{178}\) Several other states have enacted similar laws with a similar goal of minimizing litigation.\(^{179}\) However, the newness of the statutes, particularly the fact that they have not yet been extensively tested in court or otherwise, makes it difficult to determine whether the statutes will generate any meaningful benefits.\(^{180}\)

States drafting or revising prelitigation statutes for construction defect actions must consider several factors. Statutes of limitation specifically designed to address construction defect actions vary among states.\(^{181}\) In some states, the extent of damage required for valid claims is not clearly defined.\(^{182}\) In addition, the timing and extent of pre-trial or prelitigation procedures is often not clearly defined.\(^{183}\) Given the increas-

\(^{177}\) See Cal. Civ. Code § 1375; see also supra Part II.A-B.

\(^{178}\) For a summary of the original Calderon process, criticism of that process, and the revised elements, see Marks & Eskin, supra note 114, at 39-46.


\(^{180}\) See, e.g., Boyden, supra note 175, at 10 (arguing that a Nevada prelitigation statute for construction defect cases may be unfavorable to homeowners); Ronald M. Sandgrund et al., The Construction Defect Action Reform Act, COLO. LAW., Oct. 2001, at 121 (summarizing a Colorado prelitigation statute and raising issues that still need to be addressed).

\(^{181}\) For a summary of statutes of limitation for construction defects in California, see supra note 46.

\(^{182}\) Many states are slowly recognizing the problems of construction defect litigation, and courts are increasingly applying the economic loss doctrine, as the California Supreme Court did in Aas. See, e.g., Calloway v. City of Reno, 993 P.2d 1259 (Nev. 2000) (applying economic loss doctrine to limit negligence claims for construction defects in Nevada). Definitions of "construction defect" in state statutes vary dramatically. See, e.g., Nev. Rev. Stat. § 40.615 (2003) (defining "constructional defect" as including "a defect in design, construction, manufacture, repair, or landscaping ... "); COLO. Rev. Stat. 13-20-804 (2002) (limiting negligence claims for construction defects if claim arises from failure to construct in substantial compliance with building codes and standards, subject to exceptions for actual and probable damage and personal injury); Cal. Civ. Code §§ 896-897 (containing an extensive list of types of defects California will consider "actionable" in defect cases).

\(^{183}\) Supplying an initial list of defects to a builder or developer is fairly
ing popularity of prelitigation statutes and the different approaches states take to address the construction defect problem, California's experience in developing and revising such statutes is an important factor to consider when formulating an effective prelitigation process for residential construction defect cases.

IV. ANALYSIS

In practice, there has been little time to test the effectiveness of prelitigation statutes for construction defects. To the extent that the prelitigation provisions of the Calderon Process and Senate Bill 800 were designed to address problems related to construction defect litigation, they certainly improve the opportunity for early settlement of claims. However, both the Calderon Process and Senate Bill 800 may not be efficient or effective enough to meet the needs of homeowners and developers in resolving construction defects.


186. California's experience with the original Calderon Process and revisions is perhaps the most extensive among states with prelitigation procedures, and even though the process has been revised, the original statute was only enacted in 1995. See, e.g., Marks & Eskin, supra note 114.

187. See id. at 40-41; see also Roger Haerr, A Condo Divided: New Law Means Big Changes for Construction Defect Litigation, RECORDER, June 26, 2002, at 4 ("The only real winners were plaintiffs' contingency lawyers and their experts."); KROLL ET AL., supra note 6, at 29-30.

188. See discussion infra Part IIC.
A. Strengths and Weaknesses of the Revised Calderon Process

Several elements of the revised Calderon Process effectively address concerns about condominium defect cases. By requiring participation of all subcontractors and interested parties in defect investigations and settlement discussions, the process encourages more thorough analysis of claims and helps increase the parties’ chances of reaching a settlement before formal litigation is initiated. Early involvement of subcontractors and insurers can only make the negotiation process more efficient, given the great likelihood of their eventual involvement.

The revised Calderon Process also allows a longer period to resolve disputes and achieve settlements. The revisions not only doubled the settlement period (from 90 to 180 days), but also created additional flexibility for the parties to extend the 180-day minimum settlement period. The longer time period for dispute resolution gives respondents time to identify and notify the other parties that should be involved, and allows for more detailed inspection and testing of defects and claims. The section 1375 provisions giving respondents ad-
ditional time to investigate and test the defect allegations can meet this need.196

The revised guidelines for testing and investigation in section 1375 will also help facilitate the dispute resolution process.197 Investigation and testing of defects is a critical part of the settlement process because investigation allows both homeowners and respondents to assess the magnitude of the claims.198 Section 1375 addresses this component by allowing both parties to investigate defects and requiring them to share the results of any tests.199 Full disclosure of testing results can assist both respondents and homeowners’ associations because all parties will have the same information with which to prepare and evaluate settlement offers.200 Investigation and information-sharing gives both sides in a dispute equal access to information as well as the opportunity to make practical and informed decisions about the most effective way to proceed with defect claims.201

Provisions requiring homeowner associations to disclose settlement agreements to owners and meet with those owners to discuss settlement options may also help promote settlement.202 Builders may be able to use the offer to argue the benefits of settlement because section 1375 requires respondents to give reasons for their offer.203 Clearly articulated reasons for each component of a settlement offer can also give associations and owners better insight into the builder’s perspective on specific defect claims,204 and help them evaluate their defect claims and weigh the costs and benefits of settlement.205

196. See CAL. CIV. CODE § 1375(c).
197. See KROLL ET AL., supra note 6, at 29-30.
198. See id.
199. See CAL. CIV. CODE § 1375(e).
200. See id. § 1375(k) (requiring respondents to include an explanation of reason for the terms of any settlement offer).
201. See Marks & Eskin, supra note 114, at 41 (noting that the same rules for document disclosure apply to all parties).
202. See Dunstan & Swenson, supra note 2, at 5 (observing that associations were previously not required to notify homeowners, and many builders perceived that the associations were pressured to file suits by attorneys).
203. See CAL. CIV. CODE § 1375(k) (requiring respondents to include explanations for the terms of their settlement offers, and requiring associations to disclose the full text of those offers to homeowners).
204. See id.
205. The section 1375 requirement of homeowner participation in a meeting.
The greatest strengths of the revised Calderon Process lie in the components that give both sides of the dispute equal opportunities to obtain and evaluate information related to the defects. This balanced discovery and exchange of information can help ease respondent concerns about extensive lists of defects. Even so, the Calderon Process may not address all concerns about the resolution of condominium defect claims.

Section 1375 sets no standards for defects and damages that should merit reasonable claims, and contains no provisions to discourage associations from making claims about minor defects. Under the Calderon Process, builders can only defend against claims for inconsequential defects by excluding such claims from a settlement offer. Furthermore, the statute lacks any clear incentives for homeowners' associations to accept such offers in lieu of litigation. Because the Calderon Process does not clearly define which defects will be actionable if a case proceeds to litigation, builders gain only limited benefits from the dispute resolution require-

to analyze the costs and benefits of taking the claims to court provides an additional layer of “review” for associations to consider their claims. See id. § 1375(k)(D)-(E).

206. See KROLL ET AL., supra note 6, at 30.

207. The provisions allowing respondents to conduct testing on the homes can help ease builder concerns about extensive lists of defects by allowing them to investigate the defects first hand, and by allowing—and even requiring—them to explain the components of their settlement offers. See CAL. CIV. CODE § 1375(e), (h), (k).

208. See KROLL ET AL., supra note 6, at 29 (characterizing the dispute resolution provisions of the Calderon Process as “relatively weak”); see also SAN DIEGO ASS’N, supra note 2, at 8-10 (discussing factors that may be needed to reduce unnecessary defect litigation, including clear statutory definitions of construction defects and warranty programs).

209. From a legal standpoint, the broad definition of damages in CAL. CIV. PROC. CODE § 337.15 as “any deficiency in the design, specifications, surveying, planning, supervision or observation of construction or construction of an improvement to, or survey of, real property” is favorable to homeowners making claims for any defect, regardless of the damage that defect has caused.

210. Respondents have discretion over which items they include in settlement offers. See CAL. CIV. CODE § 1375(k).

211. Association refusal to settle may be attributed to a number of factors and choices. See Wedner, supra note 1, at 2 (quoting homeowner attorney, “these lawsuits are worth it because homeowners are stuck with a choice: either pay for the damages out of their pockets, or make the builder responsible. . . . The average consumer doesn’t have the expertise to investigate the cause of defects or make proper repairs.”).
Without guidelines to describe reasonable claims for defects, the Calderon Process does little to assist developers and builders who view claims for "incidental" defects as one of the greatest problems with construction defect litigation. Although the procedures encourage communication and settlement, the realities of judicial treatment of defect claims may outweigh the incentives for homeowner associations to settle in the prelitigation phase.

As a result of those weaknesses, associations may still have the "upper hand" in condominium defect cases because neither the Calderon Process nor the decisions in Aas and Hicks substantially discourage claims for minor defects. While prelitigation procedures encourage thorough evaluation of settlement offers, homeowner associations retain full discretion in deciding whether to accept or reject an offer and proceed with litigation. In this sense, plaintiff homeowners' associations may have little to lose by rejecting settlement offers and proceeding to court when offers fail to include all of the claimed defects.

Finally, although the Calderon Process has fairly strict penalties for parties who do not participate, the penalties for noncompliance—a stay of the action merely to establish compliance—with the procedures are relatively weak. Without penalties for noncompliance, respondents often try to impede or delay the process. Until the scope of "substantial

212. See SAN DIEGO ASS'N, supra note 21, at 9 (noting that "some feel that the lack of a precise, carefully limited definition of construction defect allows litigation for merely cosmetic defects as well as more serious problems.").
213. ID. at 5.
214. See Sandgrund et al., supra note 180, at 123 (commenting on a similar law in Colorado and the fact that no clear understanding of the concept of "damage").
215. See Castro, supra note 20 (discussing how the decisions in Aas and Hicks affect the theories of liability plaintiffs use in defect cases, but not necessarily the types of claims they allege).
217. See Wedner, supra note 1 (discussing the fact that, in many cases, homeowners choose to make formal claims after receiving inadequate settlement offers because they do not have the expertise or resources to resolve defects themselves).
218. See CAL. CIV. CODE § 1375.05(d) (specifying that any party who had notice of but failed to participate in the dispute resolution process will be bound by any settlement reached and will be included in the allocation of the settlement).
219. See id. § 1375.05 (g)(3)(A).
220. See id.
221. See Marks & Eskin, supra note 114, at 45 (noting tendency of respon-
compliance" with the Calderon Process is defined, noncompliance and delays remain a risk in the prelitigation phase.222

B. Senate Bill 800 Prelitigation Process

1. Time Limits

The time limits in Senate Bill 800 for investigation of and response to defects were likely developed to prevent parties from prolonging cases. In practice, however, the actual timeframes for complying with the prelitigation requirements may not provide enough time for parties to investigate and fully consider the merits of defect claims.223 Because the builder has only fourteen days to complete testing and investigations, the right to repair elements of the statute will likely benefit the homeowner because the builder will have less time to evaluate the severity and intricacies of defect claims.224 Although the builder may request a time extension for additional testing, the pressure will remain on the builder to meet the time limits or lose the right to repair. In some cases, it may simply be easier for the builder to offer to repair, even if the extent of the defect is questionable, than risk losing the right to repair.225

Further, the burdens of the prelitigation time limits may not be evenly allocated, because the builder is responsible for meeting deadlines after the homeowner sends notice.226 After the homeowner initiates the process by giving notice, the builder alone is responsible for coordinating investigations and testing, and formulating the offer to repair in the required time.227 Arguably, this burden on builders could be balanced by the fact that they have an absolute right to repair after complying with the requirements, regardless of any

222. Id. at 41.
223. See Mark Cameron, Change to Spare: The New California Construction Warranty and Defects Law, 13 MILLER & STARR REAL ESTATE NEWS ALERT (Jan. 2003) (observing that "builders may find it difficult to meet the new statutory deadlines.... [and] homeowners may be shocked to learn that to pursue court claims their new homes may first be entered and repaired whether they like it or not").
224. See id.
225. See id.
227. See id. §§ 916-917.
dispute a homeowner has with the repair offer.\textsuperscript{228} However, if the times allowed do not provide enough time for gaining adequate information, builders may feel that the process is not entirely fair because they do not have time to gather adequate information to make informed decisions.

\section*{2. Offer to Repair}

The Senate Bill 800 requirement for submitting the offer to repair could potentially foreclose negotiated solutions that might be more successful or easier for both builders and homeowners.\textsuperscript{229} Senate Bill 800 gives the builder the right to specify the repairs that will be completed, and to propose a completion date and contractor to perform those repairs—a process that makes it easier for the homeowner to obtain repairs because the problem can be resolved without litigation and the builder will organize the repair attempt.\textsuperscript{230} However, the fact that Senate Bill 800 encourages builders to repair all defects that might be actionable,\textsuperscript{231} and requires homeowners to accept those offers to repair, also tends to reduce or eliminate the opportunity for those parties to develop other solutions that might meet their needs more effectively.\textsuperscript{232} Proponents of prelitigation might argue that a dispute resolution method in addition to repair is unnecessary because the main goal of most homeowners is to get the problems fixed, but the required procedures allow only minimal flexibility, which may discourage parties from negotiating a personalized solution more appropriate to their needs.\textsuperscript{233}

\textsuperscript{228} Id. § 919.

\textsuperscript{229} See Cameron, supra note 223 (noting one difficulty that might arise in the mandatory right to repair: “The trust and cooperation usually required for successful repair efforts are often lost early in the claims process, yet the right to repair will survive that loss as long as other requirements are met”).

\textsuperscript{230} See CAL. CIV. CODE § 917.

\textsuperscript{231} The extent of this requirement remains somewhat vague. For example, a homeowner might give notice to a builder of specific claims, but additional defects could be uncovered in the course of investigation and testing. Since the statute is meant to be broadly construed, a builder would likely have to offer to repair the newly discovered defects, even though the homeowner did not include those problems in the original complaint.

\textsuperscript{232} See Carrie Menkel-Meadow, Mothers and Fathers of Invention: The Intellectual Founders of ADR, 16 OHIO ST. J. DISP. RESOL. 1 (2000) (“The morality of mediation lies in optimum settlement, a settlement in which each party gives up what he values less, in return for what he values more.”).

\textsuperscript{233} Because of the goal and importance already discussed of increasing parties’ satisfaction with the repairs, it will be important to preserve mediation as
3. Mediation

Senate Bill 800 requires builders to make an offer to mediate, but homeowners alone choose whether to actually participate in mediation. Because the parties will likely enter mediation with diverging interests and attitudes, attempts to compromise through mediation might be frustrated. For example, homeowners may request mediation because they are unhappy with the contents of a repair offer, but builders may be disillusioned when their offer to fix the alleged problem does not satisfy those homeowners. Further, the fact that builders retain the right to repair, regardless of mediation, creates little incentive for them to actively participate and creates a real risk of defeating both the purpose and the potential of mediation. The factors preceding the mediation still seem to weigh in favor of the builder because the builder will still get to attempt repair and thus has little to lose by ignoring concerns that the homeowner raises in mediation about the offer to repair.

Assuming that the prelitigation requirements of Senate Bill 800 prove too restrictive for homeowners and builders, or otherwise do not meet the needs or desires of builders, the statute also gives the builder the choice of opting out of its prelitigation requirements by choosing an alternative dispute resolution effort. Mediation seems particularly suited to promoting the feeling of a fair and personally satisfying process, because the job of a mediator can be described as “assisting parties to clarify issues, to develop agendas, to communicate ‘reasonable and fair’ offers, and to work on easy issues first seem to pay off in better settlements.” Deborah M. Kolb & Jeffrey Z. Rubin, Mediation Through a Disciplinary Kaleidoscope, 4 DR FORUM 3, 7 (1989).

234. The fact that homeowners make the decision unilaterally suggests that in many cases mediation will not necessarily be a mutual choice because the builder is required to offer it, but may not sincerely want to participate.

235. See Owen M. Fiss, Against Settlement, 93 YALE L.J. 1073 (1984) (“[T]he distribution of financial resources, or the ability of one party to pass along its costs, will invariably infect the bargaining process, and the settlement will be at odds with a conception of justice . . . .”).

236. See generally id.

237. The builder will, of course, be subject to any applicable legal and ethical requirements to negotiate in good faith. See generally John Lande, Using Dispute Design System Methods to Promote Good Faith Participation in Court-Connected Mediation Programs, 50 UCLA L. REV. 69 (2002).

238. See Roger B. Coven, California Attempts to Resolve Residential Construction Defect Claims Without Litigation, 23 CONSTR. LAWYER 35 (2003) (observing that “unless the builder is successful in satisfying the homeowner, SB 800 may do little more than delay the inevitable).
resolution method at the time of sale. While this may seem to allow for greater flexibility in choosing a method of dispute resolution, the fact that the builder must choose a method at the time a house is sold rather than when a dispute arises may not maximize the dispute resolution potential. For example, the value of the claim and the type of defect would likely be factors influencing the choice of dispute resolution method, but the builder has no real way of knowing the exact nature of potential disputes at the time the house is sold.

On the other hand, the fact that the Senate Bill 800 process is prelitigation may ease concerns about time limits and alternative processes as long as builders have enough time to gather the resources they need to make an informed offer. Because the statute is so new, it is probably too early to tell whether or not efforts to resolve claims under the Senate Bill 800 prelitigation process will be hampered by the restrictions on time and process. If the provisions prove workable, both owners and builders will benefit from because defects will be repaired and full litigation will be avoided.

IV. PROPOSAL

The prelitigation requirements in the revised Calderon Process and Senate Bill 800 improve the dispute resolution

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241. Essentially, the prelitigation process is only a starting point for parties litigating such claims. Both laws allow homeowners to file formal claims after the prelitigation process is completed. See CAL. CIV. CODE §§ 926, 1375.05.
242. The defect definitions and the builder right to repair are new. Litigation is often drawn out for extended periods of time because parties fight over whether or not certain defects should be actionable. The definitions in SB 800 will help eliminate this ambiguity. Further, builders have never had an absolute right to repair a defect; the hope for this provision is that repair would go directly to the main goal of homeowners, that is, fixing the defect.
   The legislature worked with both the building industry and trial lawyers to devise a law that would give both groups more protection. The result is a law that establishes extensive new rights, obligations, and remedies, representing a compromise between both groups. The two sides worked right up to the end of the legislative year to obtain this compromise . . . .
   Id. at 106.
potential for construction defect claims. By encouraging communication between parties and within the homeowners' associations themselves, the Calderon Process helps increase the chances of settlement. Similarly, the mediation and offer to repair provisions of Senate Bill 800 promote communication and encourage parties to address repair directly and early.

The requirement of the right to repair is a fairly narrow solution for residential construction defect claims which may initially limit the scope of remedies that parties might otherwise consider. Repair, dictated as the final remedy in the prelitigation stage, should not bar parties from trying to negotiate a settlement that can more effectively accommodate their needs.

The repair remedy is valuable because repair is easy for both parties; it offers the builder a quick resolution of the defect claim and, in most cases, will meet homeowner goals of correcting the construction defect. However, where homeowners request mediation, builders may find the homeowners' dissatisfaction irritating. Negotiating a settlement may be frustrated by the fact that the two parties have only a limited interest in preserving an ongoing relationship.

244. See generally Haerr, supra note 187; Marks & Eskin, supra note 114; Wedner, supra note 1.
246. See Marks & Eskin, supra note 114, at 40-41.
247. Dispute resolution in construction defect could potentially lead to a wide range of solutions if there were no repair requirement. This paper focuses only on dispute resolution within the context of the SB 800 and Civil Code section 1375 prelitigation provisions, analyzing the potential interaction of the right to repair and other dispute resolution mechanisms.
248. The goal is, after all, to promote settlement. Since the statutes do not bar further litigation, the success of any resolution under this statute will necessarily be dictated by the satisfaction of parties involved and final resolution at the prelitigation stage. See CAL. CIV. CODE §§ 926, 1375.05.
249. See Cameron, supra note 223. This author predicts the future of Senate Bill 800 by stating:

As a practical matter, SB 800 should expedite repairs on some construction claims, bar homeowners from the courthouse during the repair period, ease consumer burdens of proof, impose on builders statutory obligations to deliver residential units which meet minimum system performance standards, and foster constructive dialogue before attorneys take over the process of determining appropriate repair needs.

Id.

250. For the most part, homeowners want compensation for the problems, while builders may be interested in limiting expensive litigation. See Jeffrey W.
Allowing for additional dispute resolution techniques in both Senate Bill 800 and the Calderon Process might help facilitate early settlement, depending on the severity and extent of claims. Although additional dispute resolution for small defect claims that are relatively easy and inexpensive to repair might not promote efficiency, expansion of dispute resolution options for larger claims would likely be worthwhile because the parties would have a greater opportunity to reach an amicable settlement. In disputes over repair offers that are related to defects with a larger value, the four hour limit that Senate Bill 800 imposes on mediation may not be enough to allow homeowners to be sufficiently satisfied with the prelitigation result.²⁵¹ Supplementing the current Senate Bill 800 provisions to provide additional opportunities for builders and homeowners to reach settlements may increase the chances of satisfying the parties and preventing further litigation.²⁵²

Since Senate Bill 800 gives the builder an absolute right

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²⁵¹ See supra note 233 and accompanying text.
²⁵² Several authors suggest that the parties' satisfaction with the process can matter just as much as the result. This idea seems particularly relevant when the result is essentially already dictated by statute. See, e.g., John Lande, Using Dispute Design Methods to Promote Good Faith Participation in Court-Connected Mediation Programs, 50 UCLA L. REV. 69, 119 (2002). Although this article primarily addresses court-connected mediation, some ideas about the interest of parties could apply to the preliminary stages of construction defect claims:

Parties are more likely to feel satisfied if their actual mediation experience meets or exceeds their expectations. Parties are more likely to feel satisfied with mediation when they feel that they have opportunities for meaningful self-expression and participation in determining the outcome. Parties are also more satisfied when they believe that the mediation process is fair, understandable, informative, attentive to their interests, impartial, uncoerced, and private.

Id. at 118 (citations omitted).
to repair, homeowners may feel that they have less leverage in ensuring that the repair efforts are acceptable to them.\textsuperscript{253} Defect statutes are premised on the idea that repair will appease homeowners and discourage them from pursuing litigation.\textsuperscript{254} Recognizing and protecting the interests of homeowners can make these statutes more successful. Quite simply, limiting the mediation for complex defect cases to four hours may not be enough to ease homeowner concerns about proposed repairs, and may create a risk of truncating discussions that could be beneficial.

Dispute resolution in construction defect cases should more fully promote open discussion of repair proposals to encourage builders to look beyond the fact that they have a right to repair regardless of the mediation outcome.\textsuperscript{255} Requiring parties to split mediation costs would perhaps impose a slightly greater financial burden for homeowners, but could also create a better sense of neutrality for both parties and a greater sense for homeowners that their interests are being protected during the mediation.\textsuperscript{256}

Another way to ensure that builders actively participate in mediation would be to set an arbitration date before the mediation occurs.\textsuperscript{257} By setting a date for arbitration before the mediation begins, or by agreeing to a mediation/arbitration, builders will know that if they cannot reach an agreement a neutral party will make a decision that could potentially affect their repair offer. Although expanding the dispute resolution process to include arbitration might seem excessive at the prelitigation stage, particularly given that the subject of mediation is essentially limited to the terms of a builder’s repair offer, the goal of the statute is also to make

\textsuperscript{253} See generally CAL. CIV. CODE § 895-935.
\textsuperscript{254} See Harney, supra note 94.
\textsuperscript{255} See Lande, supra note 253, at 123 (noting that “mediation programs are likely to promote productive behavior when participants are ready to mediate seriously and if the mediation techniques address the participants’ interests”).
\textsuperscript{256} See Thomas J. Stipanowich, Reconstructing Construction Law: Reality and Reform in a Transactional System, 1998 Wis. L. REV. 463, 505 (1998) (noting that “homeowners’ lack of technical expertise may place them at a real or perceived disadvantage in negotiations with builders”).
\textsuperscript{257} This is apparently a common practice in construction defect cases. One attorney stated that he refuses to attend mediation if an arbitration date is not set first because builders simply will not participate fully in mediation unless they know that a “real decision” may be made by someone else if the parties do not reach agreement.
sure that both parties are happy with repairs so that the cases do not proceed to litigation.\textsuperscript{258} For homeowners, the benefit of making both processes available is that the mediation will allow them to articulate their problems directly to the builder and discuss the merits of the repair offer with the builders,\textsuperscript{259} but if those discussions do not result in a solution, a neutral expert's decision about the most appropriate repair strategy can make the process seem less dominated by the builder's repair terms.\textsuperscript{260} The most efficient process would likely be a mediation/arbitration proceeding, so that the whole process could be decided and completed in a day, and particularly so that the entire process can be completed within the original timeframe contemplated by a prelitigation statute.\textsuperscript{261}

V. CONCLUSION

Construction defect cases involve complicated claims, is-

\textsuperscript{258} See Hibberd & Newman, ADR and Adjudication in Construction Disputes 60 (1999) ("[A]s facilitator the mediator does not become pro-active by proposing or attempting to impose a solution, but rather promotes a realistic understanding by each party of the other's interest."). Because statute dictates and mandates the "rights" of each party, the mediation in Senate Bill 800 cases will likely focus almost exclusively on the interests of the parties.

\textsuperscript{259} Some authors argue that mediation is valuable to parties because the neutral or other mediator helps them assess their case. This idea supports the proposition that the parties might benefit from the opinion that they might receive in arbitration. See, e.g., Stempel, supra note 249, at 266-67:

\textquote{[M]ediation adds value to the disputing transaction by providing the parties with information and structured evaluation that parties themselves cannot provide. This view... suggests parties benefit significantly from being accorded a relatively timely, reasonably formal opportunity to present their case to a neutral third party and to receive a fair and reflective hearing of the matter... both economic and sociological analysis tends to suggest that more value is added to the process when the mediator not only gives the parties a forum and assists them in new ways of assessing the dispute, but also provides some yardstick for assessing the options...}

\textbf{Id.} (citations omitted).

\textsuperscript{260} See generally id.

\textsuperscript{261} The mediator could take a facilitative or evaluative approach, depending on the attitude and needs of the parties. Hibberd & Newman describe the approach of the Construction Disputes Resolution Group, a British organization: "The Construction Disputes Resolution Group (CDRG) mediation service sets out in its guidelines that the mediator has the discretion to adopt any procedure that suits the parties and may at any stage make proposals for the settlement of the dispute. This provides a high degree of flexibility..." Hibberd & Newman, supra note 258, at 61.
sues, and interests, and California’s statutory solutions that address these complex problems should carefully consider the many factors and interests involved in residential construction defect claims. Homeowners and builders need a construction defect resolution system that works to minimize litigation, and also encourages builders to provide a better product for the homeowner. The prelitigation provisions California Civil Code sections 1375 and 875 through 945.5 strive to limit litigation by encouraging settlement before homeowners’ associations file formal complaints. However, the settlement incentives in both statutes may not provide a dispute resolution system that is effective enough to overcome homeowners’ desires to test claims in court.

Because the statutes focus on resolving defects prior to formal litigation, the parties’ satisfaction with the resolution they reach at that stage is critical in fulfilling the goals of the statutes. If the parties are more satisfied with the prelitigation solution, they will be less likely to feel the need for litigation. Ultimately, the goals of any resolution system for residential construction defect claims should include encouraging better workmanship; indeed, “[g]ood construction and design have always been the best defenses.” A home without defects is a happy and litigation-free home.

262. See discussion supra at Part II.C.
263. Id.
264. Although the legislative focus on construction defects is the abundance of litigation, poor construction is the root of this litigation. Consequently, use of legislation to solve defect problems should include measures to resolve current problems as well as discourage future problems. Seeinfra Part III.
265. See discussion supra Part IV.
266. Cameron, supra note 223, at 7.