

CALIFORNIA DECISION ERODES CERTAINTY OF 10 YEAR LIMIT ON POTENTIAL LIABILITY FOR CONSTRUCTION DEFECTS

(2005)

by Gregory R. Shaughnessy

For many years now practioners of construction law in California have understood that a “bright line” exists with regard to potential liability for construction defects – no liability 10 years after substantial completion of the project. The recent decision by the California Court of Appeal in *Acosta v. Glenfed Development Corp.* (2005) 128 Cal.App. 4th 1278, took a narrow exception to the 10 year rule, for actions based on “willful misconduct or fraudulent concealment,” and expanded the exception to the point where the exception swallows the rule. In so doing, the Court took a statute intended to provide certainty and reduce risk and created a great deal of uncertainty and potential added risk.

Background. Code of Civil Procedure Section 337.15 provides a statute of repose that bars the bringing of any action to recover damages for construction defects more than 10 years after substantial completion of the work of improvement. Case law has clarified that this 10 year bar does not apply to personal injury claims. See *Geertz v. Ausonio* (1992) 4 Cal.App.4th 1363.

In *Acosta* the court granted summary judgement in favor of a developer/contractor on the grounds that 47 of the 59 named plaintiffs had been brought into the case more than 10 years after the recordation of notices of completion on each of their single family homes. The plaintiffs argued that an exception to the 10 year rule under Section 337.15 applied, namely subdivision (f), which provides:

(f) This section shall not apply to actions based on willful misconduct or fraudulent concealment.

In opposition to a Motion for Summary Judgment by defendants, counsel for the plaintiffs attempted to apply this exception to the facts of the case.

Opposition to Defendant’s Motion

The Plaintiffs opposition to the Defendants’ motion for summary judgment consisted of two declarations from expert witnesses that listed defects which are commonly found in almost any report by an expert witness in any substantial construction defect litigation, including:

1. horizontal attachments for vertical truss supports in the garages were missing;
2. lack of adequate shear transfer;
3. missing or inadequate holdowns;
4. missing or inadequate straps and hangers on load bearing members;
5. some driveways were short by as much as 3.5’;
6. stucco defects;
7. the windows leaked; and
8. less expensive kraft paper was used to flash around the windows instead of the asphalt polyethelene sheeting specified on the plans approved by the City.

The experts opined that most of the defects undermined the structural integrity of the homes and created a substantial risk of injury to persons and/or property. They also opined that the

defects: (1) involved conspicuous failures to comply with applicable building code provisions, with the city-approved building plans, and with basic construction industry practices; (2) were of a type that inevitably would have been recognized by any competent construction supervisor conducting even minimal day-to-day inspections of the type required in a construction project such as the one involved here, and would have caused the construction supervisor to require the responsible subcontractors to remedy the defects immediately, before work could proceed on the houses; and (3) had the financial impact of producing, in defendants' favor, substantial cost savings.

The experts stated that the defects appeared to be the result of willful misconduct by defendants in that they were "so serious and prevalent that they were either the result of [a] deliberate decision to 'cut corners' for cost savings or the result of a near total, virtually reckless, failure by the developer to adequately supervise subcontractors."

Analysis

The *Acosta* court recognized that other case law had emphasized that the purpose of Section 337.15 was to "provide a 'firm and final' outside limitation period for construction suits involving claims for latent defects." Nonetheless, the court held that the "willful misconduct exception" applied, holding that the term encompassed "not only intentional wrongdoing, but negligence of such a character as to constitute reckless disregard for the rights of others." The Court of Appeal reversed the trial court's order granting summary judgment in favor of the developer/contractor.

The *Acosta* court was able to locate only one other decision applying the exception in Section 337.15(f), *Felburg v. Don Wilson Builders* (1983) 142 Cal.App.3d 383, 390. In *Felburg* a defendant builder had sold plaintiffs a home that had been built over an oil sump. After subsidence caused considerable damage to the

home, the plaintiffs filed suit about 12 years after substantial completion of the home. In opposition to the defendant's motion for summary judgment, the plaintiffs submitted an expert declaration that stated that "it would have been impossible to pour the foundation of the home without seeing the evidence, in plain view, that the lot was over an oil sump." The plaintiffs also offered evidence that indicated that the builder had actually received a boring report from a soils engineer that showed the existence of the oil sump on or near the plaintiff's lot.

The *Acosta* court found that the facts in *Felburg* were "remarkably similar" to those in the *Acosta* case. It is submitted that the obvious knowledge in *Felburg* that a house was being built on a woefully deficient construction site with total disregard of a soils report showing the existence of the oil sump, is not remotely, much less remarkably, similar to the garden variety construction defects that were present in the *Acosta* case. Indeed, the principal defects in *Acosta* appeared to be defects which undermined the structural integrity of the houses and which created the RISK of injury, but which had not actually caused any injury.

Importantly, the *Acosta* court held that the developer/contractor could be found to have engaged in willful misconduct, even if it did not have actual knowledge of the defects, for example, where the work was performed by subcontractors. The court reasoned that the developer/contractor was liable to the buyers for the acts of the subcontractors because developers/contractors "have supervision over the construction, including the work of the subcontractors," and found that this duty was non-delegable. The court also found that imposing supervisory obligations on developers/contractors was consistent with the Contractors License Law. Finally, the court found that under the exception in subdivision (f), which states that it applied to "actions based on willful misconduct," "it is only necessary that the action be based on and arise from willful misconduct by *someone*. It does not matter

whether defendants committed such misconduct directly or it was done by subcontractors hired by them.”

This language suggests that where there was willful misconduct by ANYONE involved in a project that led to construction defects, the 10 year statute of repose cannot be invoked by anyone else involved in the project. Taken further, the logic of *Acosta* suggests that where there was willful misconduct on ANY defect, the 10 year statute cannot be invoked for any OTHER defect, even if the other defect was not caused by willful misconduct or fraud.

Comment

A petition for review by the California Supreme Court was filed on May 25, 2005. It is likely that the petition will be granted, to allow the Supreme Court to clarify the significant uncertainty the *Acosta* decision has created. However, plaintiffs lawyers now have authority that will allow the 10 year statute of repose to be overcome in most construction defect cases. The 10 year statute of repose will no longer be seen as an almost insurmountable barrier.

It is difficult to imagine a case where a creative plaintiff’s lawyer, with a “flexible” expert witness, will be unable to come up with a declaration that the construction defects were the result of a deliberate decision to cut corners for cost savings and that there must have been a near complete failure by the developer to exercise even minimal supervision. In such cases, it may be difficult for a defendant to escape from the case by a motion for summary judgment that relies on the 10 year statute of repose. Thus, plaintiffs will frequently be able to get cases before a jury that would otherwise have been disposed of by summary judgment. Whether the conduct by the developer/contractor was willful misconduct will normally be a question of fact for the jury. *Colich & Sons v. Pacific bell* (1988) 198 Cal.App.3d 1225.

The *Acosta* decision is not remarkable in its application of the “willful misconduct” exception, but rather in the manner in which it applied the exception. It allowed expert declarations which were not remarkable, and which did not remotely approach the egregious facts in the *Felburg* decision, to create a triable issue of fact, even against a developer/contractor where there was no direct evidence that the developer/contractor had knowledge of the defects. In effect, the *Acosta* decision creates strict liability by the developer/contractor for any willful misconduct by the subcontractors, or where the defects were the result of a lack of supervision.

Some steps can be taken by developers/contractors to try and keep the 10 year limitation period intact. This includes conducting special inspections and keeping good records of such inspections. This would tend to show that proper supervision was provided, and that attention to quality control was given, perhaps enough to overcome the conclusory and self-serving declarations of the plaintiff’s experts on a motion for summary judgment. Notably, there was no discussion in *Acosta* of the fact that the allegedly grossly defective work had all presumably passed the inspections by the local building officials.

Special inspections have actually been fairly common for the past five years or so on condominium projects in California, as most such projects were built with wrap OCIP insurance policies, which typically required such inspections as part of the OCIP program. However, such OCIP policies typically also have a ten year “tail” coverage following substantial completion. Under *Acosta*, construction defect actions can be brought AFTER the expiration of the 10 year tail, leaving developers, contractors and subcontractors completely exposed to liability for construction defects, with absolutely no insurance coverage, with the effect of further chilling the market for construction of single family housing in California.

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