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Notice and Opportunity to Repair Construction Defects: An Imperfect Response to the Perfect Storm

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By Alice M. Noble-Allgire*

“There are no easy solutions to problems that simultaneously affect one person’s home and another’s livelihood ...”\(^1\)

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I. Introduction

The nation's home building industry is in crisis. During the past two decades, insurance carriers have pulled out of the market in many areas of the country or raised premiums precipitously, blaming increased risks from construction defect litigation.\(^2\) With insurance either unavailable or prohibitively costly, many builders have gone out of business, stopped building certain types of housing projects, or passed the increased costs along to consumers – all of which threatens the availability and affordability of housing.\(^3\)

For these and other reasons,\(^4\) state legislatures have acted swiftly to stem the tide of construction defect litigation. A common response has been to enact legislation requiring homeowners to provide builders with notice and opportunity to repair construction defects before
the homeowners can bring legal action. Since 2000, more than two dozen states have adopted notice and opportunity to repair (NOR) statutes, bringing to 33 the total number of states with NOR legislation on the books.5

This article analyzes the efficacy of NOR legislation as a solution to the housing construction crisis and concludes that the legislation is an incomplete and imperfect remedy to a complex problem. Section II of this article describes the combination of factors that led to the housing construction crisis. Section III gives an overview of NOR statutes enacted to curb construction defect litigation. Section IV examines some of the weaknesses of NOR legislation – most notably that such legislation addresses only part of the problem and, in many states, is biased towards the needs of industry at the expense of consumers. Section V concludes with a call for a more comprehensive solution that would include a uniform statutory warranty act – one that clearly defines construction defects and establishes the parties rights – along with improved quality control measures and insurance claims practice reforms.

The issues raised in this article affect homeowners in a variety of settings, from standalone, single-family residences to condominiums, town homes, and other common interest communities. They also affect contractors across the entire spectrum of the construction industry, from architects and other design professionals to general contractors to electricians, plumbers, HVAC, and other building trades. For simplicity, however, this article generally uses the term “homeowner” to describe the parties who bring construction claims and “builder” to describe the parties subject to those claims.

II. Anatomy of a Housing Construction Crisis

The construction industry is suffering the effects of a housing boom much like the one that sparked a revolution in property law following World War II. Prior to that war, caveat emptor ruled the day, placing the burden upon home buyers to determine for themselves the quality and fitness of a dwelling. Courts found that rule untenable, however, when the post-war housing boom led to a burst of litigation over the poor quality that resulted from “hurried construction and skimping on materials” – circumstances that home buyers were ill-equipped to discover.6 Through an evolutionary process, courts began recognizing an implied warranty of good quality and fitness in residential construction contracts.7

Recent events in the housing construction industry have prompted a new call for legal reforms. Similar to the post-war housing boom, the market has experienced a rapid increase in home construction during the past two decades.8 Not surprisingly, industry experts reported a corresponding surge in litigation alleging construction defects.9 In this current boom/litigation cycle, however, it is the builders who are feeling the pinch – particularly when insurance companies began reporting substantial losses on contractor liability policies10 and reacted to those losses by pulling out of the market, raising premiums, or adding exclusions to their insurance policies.11

In short, there is clear evidence of a crisis. What is less clear – but critical for purposes of identifying an appropriate resolution – is the precise cause. While many in the insurance
industry have been quick to blame construction defect litigation for their woes, a closer analysis suggests that a combination of factors are involved, including some of the insurance industry's own practices and economic issues. Moreover, to the extent that construction defect litigation has contributed to the problem, there are several factors at work there as well. This "perfect storm" of contributing factors is discussed below.

A. A Rise in Construction Defect Litigation

Given the very nature of the insurance business, any significant increase in construction defect litigation is reason for concern in the insurance industry. There is a perception, if not reality, that there has been an explosion of construction defect lawsuits in the past two decades. While the California condominium boom appears to be at the epicenter of the explosion, the impact has rippled throughout high-growth states like Nevada, Texas, Colorado, Washington, and Florida and beyond. Indeed, as one industry source reported, “even states that have kept a relatively low profile in terms of construction defect litigation are not immune to the effects of runaway lawsuits on insurers' appetites to take on construction risks in the housing sector.”

The insurance crisis often takes center stage in debates concerning construction defect litigation, but legislatures also have expressed concern that such litigation offers an inefficient remedy for construction problems in general. Although most homeowners presumably would want the defect fixed, a lawsuit typically results in an award of monetary damages that is often insufficient to pay for the repair. At the same time, builders and insurers complain that the expenses of litigation often far exceed the costs of repairs and homeowners often do not perform the repairs with the recovery but instead spend the insurance check on other things. Litigation also poses non-monetary burdens, such as lost time of the litigants, harm to the builder's reputation, the homeowner's inability to sell or refinance while the suit is pending, and the demands that such litigation places upon the courts.

Of particular concern to builders and insurers are massive lawsuits involving condominium, town home, or other residential complexes. Builders contend that multifamily developments – particularly condominiums – are "prime targets" for aggressive lawyers because of “the sheer number of units . . . and the potential for systemic defects in the building.” Condominium and homeowner associations also have a fiduciary duty to investigate and correct construction defects, as well as the resources to pursue litigation, which is not often the case with the owner of a single-family home. As a result, lawsuits involving condominium or homeowner associations present substantial exposure for builders and their insurers, and give associations considerable leverage to force settlements.

But what is the root cause of the rise in construction defect litigation? Although the home building and insurance industries are blaming lawyers who bring construction defect lawsuits, lawyers are pointing back at the home builders for building defective housing in the first place. Ultimately, however, the evidence suggests that both defective construction and aggressive litigation have been contributing factors.
1. Defective construction

It is logical to assume that the number of defects (and lawsuits) would increase at a rate equal to the number of new houses being built. An unusually rapid expansion in the market exacerbates the problem. Thus, in the Sunbelt’s construction boom, demand in some areas severely strained the pool of trained, talented construction workers as well as municipal housing inspection budgets, which is a recipe for consumer complaints of shoddy construction.

The shortage of skilled workers is not limited to the fastest growing areas of the country, however; it is being felt nationwide as the baby boom generation reaches retirement age and younger generations seek careers in computers and other high-tech industries. At the same time, the construction industry nationwide is facing severe economic pressures from abnormally inflated construction costs, tightened credit, more complex construction techniques, and increased government regulation – all of which may create incentives to cut corners to cut costs.

Logic further suggests that if there is a rise in claims for defective housing, then insurance rates will rise as well. “If you crash your car three times a year, your rates are going up,” said one Nevada attorney, adding: “If everybody else in Las Vegas crashes their car three times a month, everybody’s insurance rates will go up.”

2. Aggressive litigation

Multiple factors have similarly combined to create an aggressive litigation environment, leading to industry complaints of frivolous or overblown lawsuits. One factor is enhanced consumer expectations due to their financial and emotional investment in their homes and a growing awareness of construction issues, e.g., mold, from media coverage. For the average American, the financial stakes are high because the purchase of a home is the single largest investment they will make. “While business owners tend to treat a leaky roof or window like any other commercial expense, homeowners react quite differently when the leak is in their new bedroom,” observed two Kansas City attorneys, adding, “When a retired couple’s life savings are invested in a high-end condominium (the ‘dream home’ overlooking the bay), they may expect their home to be perfect.”

A second factor helping to create an aggressive litigation environment is “plaintiff-friendly” legal regimes, such as those that: allow homeowners to recover attorney fees and litigation costs on top of the costs of repairs or damages; permit recovery on the basis of strict liability; recognize joint and several liability; or offer long statutes of limitation or repose. As one Nevada construction defect attorney observed, his state’s regime unabashedly creates a system that nearly guarantees litigation – because the plaintiff has almost nothing to lose.

At a more fundamental level, there is considerable uncertainty and ambiguity in the law, which “giv[es] homeowners greater bargaining power and increas[es] the overall threat of
Depending on the jurisdiction, homeowners may sue builders for a construction defect under one of as many as nine different theories of liability. One of the most glaring uncertainties, however, relates to the very essence of the lawsuit: what constitutes a construction defect in the first place? Without an industrywide standard, states have been left to fashion their own definition — largely as a result of judicial rulings on a case-by-case basis.

The final, but perhaps most contentious, factor is the development of a “cottage industry” of construction defect lawyers and experts, some of whom have engaged in aggressive tactics to attract business and build lawsuits. Builders complain that once lawyers become involved and employ experts to inspect the home, the defects multiply; thus, what may have started as a simple complaint about cracking drywall turns into a laundry list of problems “many of which were not known to the homeowner, or even considered a problem by the homeowner.” From a builder's perspective, these additional claims are “frivolous” even though, in a purely legal sense, a court would not dismiss the claims on that ground. Builders also contend that when lawyers get involved, the parties’ positions become polarized: homeowners' lawyers demand “Cadillac” repairs while builders' attorneys propose that a “Chevy” will do. Finally, one writer has observed that the contingent fee structure for plaintiffs’ attorneys may encourage more cases to go to trial for monetary damages, rather than settling for actual repair of the defect.

In sum, the proliferation of construction defect litigation is attributable in part to natural causes (a rise in housing construction that naturally leads to increased claims of construction defects) and in part to bad apples on both sides of the transaction (a rise in construction defects by some builders in the first place as well as the existence of a litigious environment in which some lawyers escalate and compound the problems perceived by consumers with unrealistic expectations of perfection). As discussed below, there is also evidence that a few recalcitrant insurance companies are impeding settlements, thereby forcing disputes into litigation.

B. Insurance Industry Practices and Economic Problems

Observers point to at least three problems within the insurance industry that have contributed to a contraction in the liability insurance market for contractors. One of these problems is a shortcoming in the industry’s own underwriting and claims practices; the other two are based upon economic issues that have affected the insurance industry generally.

1. Underwriting and claims practices

To some extent, the construction litigation crisis is caused by deficiencies in the insurance industry's own practices – at both the underwriting and claims processing stages. An analysis prepared by consultants for the National Association of Home Builders (NAHB) explains part of the underwriting problem as follows:

Knowledgeable observers . . . indicate that over the past decade, insurers have been charging premiums which were too low to support the risk being insured and that
insurers were and are under-reserved (not setting adequate reserves for anticipated claims). This phenomenon is industry-wide, not limited to the small group of insurers writing builder policies. As a result, the builder segment of the insurance industry continues to suffer loss ratios far in excess of premiums charged.54

Some of the underwriting challenges can be attributed to the difficulties of predicting potential losses from construction defects. Actuaries typically “look to the past to predict the future,”55 but a number of factors make it difficult to analyze construction defect claims.56 One of those factors is the unpredictability of the law itself. As noted earlier, courts have recognized as many as nine different causes of action for construction defects57 and there is considerable ambiguity as to what constitutes a construction defect in the first place.58 There is also substantial variation between states on a number of legal issues governing construction defect litigation.

In the insurance context alone, for example, this divergent case law regarding coverage of construction defect claims under commercial general liability policies.59 The traditional view, based upon a 1973 version of the standard CGL form, held that faulty construction was excluded from coverage under the so-called “business risk” exclusions in the policy.60 After the standard forms were modified in 1986, however, courts began reaching differing conclusions about whether such coverage exists.61 Thus, in recent interpretations of these documents, courts have divided on such critical issues as: (1) whether the policy covers the defective condition itself, or only when other property is damaged as a result of the defect; (2) whether the policy covers the contractor's liability under contract or just liability for tort damages; (3) whether the policy covers “economic loss” or just property damage; and (4) whether construction defects constitute an “occurrence” under the policy.62

These rulings have had an obvious impact upon the insurance industry, as illustrated in a study conducted for the Oregon Task Force on Construction Claims:

When courts began to find that the coverage grant of the CGL policy extended to construction projects, the insurance industry was taken by surprise. During the period from 1998 through 2005, loss and claim expense data provided by eleven insurers offering liability coverage to Oregon contractors indicated that construction defect claims accounted for approximately 46.6% of total claim losses and approximately 60.9% of total claim settlement expenses. Providing coverage for these defects represented an unintended and unexpected exposure to loss.63

Other factors cited by an industry expert as complicating the claims analysis process include: the lag in reporting construction defect claims because of long statutes of limitation; the involvement of multiple claimants, defendants, and insurance companies; and a continuously changing environment, which raises an “[o]verall concern that [the] past may not be predictive of the future.”64
Compounding the problem is the tendency by insurers to assess the risk of the industry as a whole, rather than on a builder-by-builder basis. Thus, when insurance companies began suffering significant losses from construction defect lawsuits, many pulled out of the industry as a whole or raised rates across the board. Although many builders are “doing it different and better” and have a better claims history, they traditionally have not received any benefit from that “unless the underwriters believe the entire industry is doing it better.”

While these underwriting issues create obvious problems at the front end of a construction defect dispute, some observers contend that insurance companies create problems for themselves on the claims management end as well. As a practical matter, one construction law expert observed, the insurance industry “isn't savvy” in selecting defense attorneys who can effectively deal with homeowner associations. In addition, the insurers' claims management structure often impedes settlements, rather than facilitating them. The attorney noted that insurers “often get bogged down in technical details – such as what percentage of the defect should be covered under the policy – and end up paying more to litigate the problem than they would have to spend to simply pay for repairs.” These problems are compounded when a defect claim involves multiple defendants, each with its own insurer.

One construction litigation expert attributed this phenomenon to the way that construction defect cases are typically litigated: “They sue everybody and have all of the insurance companies chip in. They should sue only the person who is responsible for the defect.” Things become even worse when one or more of the parties or their insurers are uncooperative.

2. Reinsurance market

A second problem insurers have faced is a contraction of the reinsurance market. The availability of reinsurance shrunk sharply after the September, 11, 2001, attacks on the World Trade Center and the Pentagon, but observers suggest that the contraction “was well underway” even prior to the attacks. An analysis by the NAHB explains: “As losses have matured in recent years and large claims paid, loss ratios turned upside down and reinsurers began to feel the effect of insufficient premiums. The reinsurance market contracts as a result.” When the reinsurance market contracted, so did the commercial liability insurance market.

3. Reduced investment income

The third general issue facing the insurance industry was the stock market decline, which had a negative impact on the industry's investment returns. As explained by a report to the Oregon Task Force, “During the 1990s insurers enjoyed double digit investment returns which more than offset underwriting losses. After the market collapse in 2001, investment income shrunk substantially.” This reduced investment income, coupled with large losses on claims, “translates directly into reduced capacity.”

In sum, the availability of commercial liability insurance contracted nationwide because of the combination of underwriting losses, lack of reinsurance, and a reduction in investment income.
income. “These broader forces alone likely would have meant higher rates and tighter coverage,” one industry reporter observed. “But the addition of construction claims has turned an insurance crunch into a crisis.”77 Moreover, all of these issues were converging “during the hard market portion of the normal insurance cycle” when premiums are ordinarily higher and coverage more difficult to obtain simply because of normal market fluctuations.78

III. Legislative Responses to Construction Defect Litigation

Construction defect legislation has taken several twists and turns since the days of caveat emptor. A few states have acted to strengthen consumer protections through the enactment of New Home Warranty Acts, which impose an implied or express warranty against specified construction defects.79 More recently, legislatures have acted to protect the building industry from threats posed by construction defect litigation, first through statutes of repose that set absolute limits on the time for homeowners to bring construction defect lawsuits80 and later through notice and opportunity to repair (NOR) statutes.

At last count, thirty-three states have some type of NOR requirement for construction defect litigation.81 Although five of those provisions existed prior to 1996, the remainder have been added in quick succession since 2001, largely in response to intense lobbying by the NAHB.82 In most states, these statutes apply only to construction defects involving residential property – sometimes only newly constructed homes, but often substantial remodeling projects as well – but a handful apply to both residential and commercial property or to commercial property alone.83

NOR legislation can be generally categorized into one of three formats: (1) A “pure NOR template developed at the behest of the NAHB;84 (2) cursory NOR provisions within a new home warranty act or licensing act; and (3) a more comprehensive regime unique to that particular state. These formats can be briefly described as follows:

A. “Pure” NOR Statutes (NAHB Template)

Twenty-two of the most recently enacted statutes appear to be based upon a format developed at the NAHB's request.85 The primary function of these statutes is to establish a procedure for homeowners to provide builders with notice of a construction defect and an opportunity to cure it – or at least offer to cure – before the homeowner initiates legal action. Among the statutes utilizing this standardized format, wide variations exist in the components of the process, the level of detail in which the procedure is proscribed, and the effects of noncompliance, but the basic concept is quite simple:

- The homeowner must file a written notice with the builder within a specified number of days before a lawsuit can be filed. If a lawsuit is filed before such notice is given, the lawsuit is dismissed or stayed.
- The builder has a specified number of days to respond to the notice by offering to inspect the alleged defect, offering a monetary settlement, or stating that the builder disputes the claim.
If the homeowner permits an inspection, the builder has a specified time period after the inspection to offer to repair the defect, offer a monetary settlement, or indicate that the builder will proceed no further to remedy the defect. If the homeowner accepts the builder's offer, the matter presumably is resolved. If the builder fails to respond to the notice or to make an offer acceptable to the homeowner, however, the homeowner can proceed with a lawsuit.

Six of the states have gone beyond this basic template to incorporate limitations on builder liability into their NOR statutes and a few incorporate alternative dispute resolution provisions, but most focus simply on the notice and repair procedure. A twenty-third state, North Dakota, has some of the procedural requirements of the NAHB template, but at four sentences in length, is considerably less detailed than the statutes in the other twenty-two jurisdictions.

**B. Warranty/Licensing Acts**

In six states, NOR requirements are only briefly stated in a New Home Warranty Act and in a seventh state, such requirements are included in a contractor licensing act. Four of the warranty acts have NOR provisions that are no more than one paragraph in length, such as Virginia's statute, which states: "such vendee must provide the vendor, by registered or certified mail at his last known address, a written notice stating the nature of the warranty claim. After such notice, the vendor shall have a reasonable period of time, not to exceed six months, to cure the defect that is the subject of the warranty claim." Minnesota's provision is only slightly longer, spanning three paragraphs. Michigan has incorporated several paragraphs of NOR provisions within its administrative process for complaints against licensed contractors.

**C. More Complex Regimes**

Three states have more elaborate statutory regimes that appear to be the product of extensive negotiation and compromise among the competing interest groups. California has combined extensive NOR procedural requirements with a statutory warranty, building standards, a mediation process, and limits on recoverable damages. Nevada's statute similarly combines damage limitations with an NOR process that is perhaps the most detailed of all the states and includes an option to submit construction defect issues to the state's contractor board. Texas has a two-tiered system: (1) for residential property in general, the state has a fairly typical NOR process that gives the builder notice and opportunity to inspect and repair; (2) for single-family residences and duplexes, Texas has combined statutory warranties with a mandatory state-sponsored inspection process. If a claim involving a single-family residence or duplex is not resolved during the state-sponsored inspection, the homeowner must then follow the general NOR statute.

In summary, three states that are perceived to be among the most litigation-intensive in the nation have developed the most comprehensive plans to address the problem, while a handful
of others included NOR provisions in statutes that address construction defects through statutory warranty plans or licensing. The vast majority, however, have adopted the industry-driven response, hoping that NOR procedures alone will create a “cooling off” period that discourages litigation. The following section analyzes some of the weaknesses of this latter approach.

IV. Pure NOR Statutes: A Partial, but Imperfect Solution

The basic premise of NOR statutes has considerable common sense appeal; indeed, the initial reaction of most homeowners who discover a construction defect is to report it to the builder and request repairs. Similarly, many courts have required notice and opportunity to repair as an element of a common law cause of action for construction defects. Thus, NOR statutes would merely codify this common sense practice. As discussed below, however, pure NOR statutes are an imperfect response to the construction defect issue because they provide only a partial remedy to a complex problem. Moreover, legislators face significant challenges in attempting to draft legislation that appropriately balances the interests of builders and homeowners and provides sufficient detail without becoming overly complicated. These issues are discussed below, along with alternative solutions to the problems that NOR statutes are attempting to address.

A. Why Pure NOR Statutes Are Only a Partial Solution

Part I of this article described many factors that have combined to create the housing construction liability crisis. Although a rise in construction defect litigation is one of the factors, some of the insurance industry's own practices and problems are also partly to blame. Ultimately, resolution of the problem requires addressing three primary components: improving quality control (i.e., prevention of construction defects in the first place); reducing litigation (which has salutary effects beyond the insurance crisis); and promoting healthy insurance underwriting, reinsurance, and investment practices. As demonstrated below, pure NOR statutes, by themselves, address only a small portion of the problem.

1. Prevention of Construction Defects

One of the primary shortcomings of pure NOR statutes is that they are “curative rather than preventative in nature. The legislation provides no incentive to build a home correctly in the first place.” Although one builder suggested that it is “naïve to say that an increased commitment to better quality will solve the problem,” it is equally naïve to think that the problem will be solved solely through notice and opportunity to repair.

One could argue that pure NOR statutes do attempt to reduce construction defects by giving builders the opportunity to make repairs as part of the construction process. But most pure NOR statutes do not require homeowners to allow the builder to make such repairs. Instead, the statutes give builders the opportunity to offer to make a repair; it is up to the homeowners to determine whether to accept the offer or proceed to litigation. Homeowners who lack confidence in their builder are unlikely to accept the builder's offer to repair.
Some builders also contend that the market will provide optimum quality control because consumers will decline to give their business to disreputable builders. But buyers lack reliable information to make educated determinations about a builder’s qualifications because there are no public records of construction defect claims against builders. Moreover, it is questionable how useful such claims information would be. Quite often, many contractors and subcontractors are brought into a lawsuit primarily as a settlement strategy even though they were not the responsible party. Thus, the claims record does not accurately identify the truly bad actors. Moreover, even if consumers know the record of the builder they hire, there is no guarantee that the contractor won’t end up with a bad subcontractor on a particular job. Finally, there is a sense that home buyers are not in the best position to insist upon quality because they often lack a long-term economic perspective in making this purchase. Thus, one government report suggests that "forces other than consumers (either the government, insurance companies, or a regulatory association composed of the firms themselves) must intervene and mandate the level of investment in housing construction that results in the least cost in the long run."

There are a variety of steps that have been suggested to reduce construction defects through better quality control. Builders could develop and implement quality control programs themselves, voluntarily or by government mandate. Government can help improve the quality of the workforce through licensing, certification, and education requirements, and can improve the quality of the work through building inspections. Insurance companies can also play a role by making more detailed inspections for projects they underwrite and by encouraging builders to implement better risk management practices.

2. Insurance Practices

Pure NOR statutes also do little, if anything, to address the insurance industry practices and problems that have contributed to the construction liability insurance crisis. Of course, NOR legislation could theoretically remedy part of the insurance crisis if NOR procedures help to reduce the number of lawsuits that are filed, as discussed in the next section. But they do not address problems with the industry’s underwriting and claims management practices, the availability of reinsurance, or investment losses caused by stock market declines.

To the extent that reinsurance and investment losses affect the entire insurance industry and not just contractor liability insurance, resolution of these problems is largely beyond the scope of this article. But there are some steps that can be taken to promote a healthier insurance environment with respect to construction defects by addressing underwriting and claims management issues. First, as suggested above, insurance underwriters face substantial challenges in analyzing construction defect claims because of ambiguity and uncertainty in the law, beginning with the fundamental question of what constitutes a “construction defect” for which builders are liable. Addressing this uncertainty – and developing some uniformity in construction defect law among various states – will go a long way toward resolving several of the factors that have contributed to the construction liability crisis.
Second, insurers can develop best practices for management of construction defect claims. To avoid some of the problems inherent in claims against multiple defendants, for example, insurers might encourage all contractors and subcontractors to agree to a joint defense. The defense team should also develop a process to resolve disputes among themselves, which would “allow the team to cooperatively address legitimate claims and to jointly defend baseless claims without suing each other.” The American Institute of Architects has embraced this cooperative model in its newest set of form contracts, which are based upon a new “integrated project delivery” model of construction.

Third, government and industry can explore alternatives to the traditional commercial general liability insurance policy. A report to the Oregon Task Force on Construction Claims suggested that “wrap” policies and policies offering specific loss control discounts held some promise for major projects. First Party Warranty and Third Party Warranty Insurance programs are another alternative, as discussed in greater detail below.

Finally, state insurance regulators should take steps to improve data collection regarding construction defects. Data availability was “a significant concern” to consultants who studied the insurance issues for the Oregon legislature. Better data could not only “help clarify the nature and magnitude” of the insurance crisis, but also assist legislators in monitoring the effectiveness of legislative actions to address the crisis.

In short, insurance reforms should not be overlooked in attempting to address the housing construction issue. As a report to the Oregon Task Force on Construction Claims observed: “A healthy insurance environment actually supports all three aspects of the task force objective. A properly structured insurance program reduces losses, lowers insurance costs, and expands consumer protection.”

3. Prevention of Construction Defect Litigation

Although legislators have been somewhat vague in identifying their ultimate objective in enacting pure NOR statutes, observers suggest that the basic concept is to promote “efficient correction of construction deficiencies without need for litigation.” The hope is that by preventing lawsuits, NOR statutes will solve a variety of ills, such as:

- alleviating litigation costs for homeowners and builders;
- controlling the cost of insurance premiums and keeping housing affordable;
- relieving courts of the burdens of litigation;
- improving customer satisfaction by addressing defects with a more personal dispute resolution process;
- providing homeowners with a better result (because the consumer gets the problem fixed instead of compensation that is likely insufficient after costs and attorney fees are
deducted);137 and

- protecting builders from frivolous and unnecessary lawsuits.138

It is questionable, however, how far pure NOR statutes can go toward reaching these goals. There have been anecdotal reports that lawsuits have declined after enactment of NOR legislation in Colorado,139 while builders in Nevada reported a positive change in the ability to get insurance quotes (even though pricing was still prohibitive) and a home builders’ attorney in Arizona observed a “positive effect” on smaller claims.140 Ultimately, however, most commentators have suggested that the “actual realities and ramifications of the [NOR] legislation remain to be seen.”141

Analytically, NOR statutes are not designed to counteract the primary forces that have been blamed for construction defect litigation. As noted above,142 three factors have combined to create an aggressive litigation environment: consumer expectations of the “perfect” home, plaintiff-friendly legal regimes, and aggressive litigators. For reasons described more fully below, pure NOR statutes are an ineffective response to those causes.

a. Consumer expectations

Pure NOR statutes have little, if any, impact upon consumer expectations of acquiring a perfectly constructed home. Some commentators suggest that the NOR process provides a “cooling off” period to simmer the homeowner's emotional response to the defect, giving the builder time to fix the problem before the dispute escalates into a lawsuit.143 However, this process works well only when reasonable parties want to solve the problem. Indeed, as indicated above, the average homeowner's first response to a defect is to notify the builder and ask to have it fixed.144 Thus, for the vast majority of cases, imposition of an NOR statute is unnecessary; such a statute merely formalizes what most reasonable homeowners and builders would do informally on their own.

Conversely, the NOR process is unlikely to succeed when any party is being unreasonable – whether the homeowner, builder, subcontractor, or insurer.145 In those cases, a statutorily imposed “cooling off period” merely imposes unnecessary and expensive hurdles to the inevitable lawsuit. Most NOR statutes do nothing to force or encourage homeowners to be more realistic; nor do they provide greater incentives for builders to be reasonable in addressing homeowner complaints.

A few states have attempted to inject reasonableness into the process by imposing penalties upon homeowners who unreasonably refuse the builder's offer to inspect or repair the defect.146 Some jurisdictions, for example, limit the damages and attorney fees that a homeowner may recover in a subsequent lawsuit.147 Others would require the homeowner to pay the builder's attorney fees and costs.148 A couple of states are more even-handed in their approach; they impose a reciprocal “reasonableness” requirement upon the builder149 or award attorney fees and costs to the “prevailing party.”150
Although these penalty provisions have the laudatory purpose of encouraging homeowners (and sometimes builders) to act reasonably, they pose some practical difficulties for the courts and the parties themselves. Most statutes imposing a “reasonableness” requirement provide no standard for determining whether an offer is “reasonable” or if it was “unreasonably” rejected; two provide simply that “the trier of fact” shall determine the reasonableness of the offer. 151 This puts an attorney in a difficult position when trying to advise a client; the attorney must consider not only whether the offer is satisfactory to the client in general, but also whether a trier of fact might second-guess that decision in litigation.

There are similar concerns about a “prevailing party” standard, which imposes sanctions only if the judgment in the subsequent litigation is “more favorable” than the builder's offer. 152 This standard is relatively easy to apply if the builder offers a monetary settlement to the homeowner. It is more difficult to apply, however, when the builder has offered to make repairs because that offer requires the fact finder to determine the “value” of builder's proposed repair.

More fundamentally, these penalty provisions do not effectively address the underlying problem – i.e., that consumers expect “perfectly constructed” homes. These provisions merely require a litigant to consider whether the homeowner's own expectations are likely to be substantially different than those of the trier of fact. Because there are no clear standards as to what constitutes a construction defect, both the homeowner and the trier of fact are left to their own subjective expectations. Removing this uncertainty about expectations would go much further toward reducing litigation than merely imposing the purely procedural requirements of a pure NOR statute.

In short, better consumer education is critical – i.e., helping homeowners understand that some imperfections are to be expected in the normal construction process. One strategy suggested by industry observers is for builders to prepare home maintenance manuals, which “offer an opportunity for education, for disclosure, and for management of homeowner expectations.” 153 Another suggestion is for builders to develop a more effective customer service program. 154

b. Aggressive litigators

Pure NOR statutes have no impact upon the aggressive tactics that some litigators have used to solicit clients and build lawsuits. Two statutes have gone beyond pure NOR procedures to include provisions that make it unlawful to offer an association officer anything of monetary value to encourage or discourage a construction defect action – or for an association officer to accept such a gift. 155 But even those measures do not deter lawyers from reaching out to potential clients in other ways, such as educational workshops or targeted mailings; indeed, attempts to completely prohibit the latter forms of advertising are likely to face First Amendment challenges. 156 Nor do they deter the aggressive lawyer bent on litigation.

At best, there is a hope that NOR statutes can prevent litigation by helping homeowners and builders resolve their disputes before litigators get involved. As one commentator explained, NOR statutes are an attempt “to foster constructive dialogue before attorneys take over the
process of determining appropriate repair needs." Thus, from a builder's perspective, the NOR process is designed to address defects within the homeowner-builder business relationship, rather than in the courts:

The whole right to repair concept came out of practical experience that I, and some other lawyers representing builders, had in this community. We found that when we got our clients back out in the community when we knew there were problems, clients typically make the right business decision and homeowners typically make an intelligent consumer decision.

In short, the building industry views the NOR process as a way to “improve overall customer satisfaction by making the repair process less clouded by legal formalities and, therefore, more personal.”

This argument has some merit; given the polarizing effect that litigators often have upon negotiations, it makes sense to suggest that the best way to avoid litigation is to avoid lawyer involvement in the first place. Doing so, however, comes at a potential cost: one might argue that homeowners (or builders) who are negotiating without the assistance of a lawyer are likely to make poor decisions because they are uninformed of their legal rights or perhaps vulnerable to the superior bargaining power of the other party. Moreover, as discussed in further detail below, there is a concern that some NOR statutes are too complex for homeowners to understand without legal assistance. Thus, to the extent that the NOR process is designed to encourage communication between homeowners and builders before lawyers get involved, some statutes are having exactly the opposite effect.

Once a litigator becomes involved, the common perception is that the NOR process becomes “nothing more than a speed bump on the road to full-blown litigation.” There is still some hope that requiring a homeowner to participate in the NOR process will result in an amicable settlement with the builder. For that to occur, however, the builder's offer to repair must be equal to or better than the result that the homeowner believes that he can obtain through litigation. Otherwise, forcing the homeowner to comply with the NOR procedures merely expands the litigation process, imposing additional costs upon the litigants. Indeed, some commentators have noted that there is a potential for the NOR process to “become as costly as protracted litigation, while still leaving open the possibility of litigation.” These increased costs will merely place additional burdens on the insurers, exacerbating the liability insurance crisis.

An Oregon study of NOR legislation suggested two final impediments to successful negotiation under the NOR process. One is the builder's reluctance to make an offer or to undertake repairs “that could later be viewed as an admission of fault if the matter proceeds to litigation.” Some NOR statutes address this disincentive by providing that certain conduct or information shared in the NOR process is inadmissible in any subsequent legal action. The second impediment is the involvement of insurers. “Builders are often required to let their insurer take over the defense of the case and are not allowed to make repairs they might have
normally performed. The end result is that homeowners face delays and claims still end up in litigation. This problem relates back to issues discussed above regarding the insurance industry's own claims management practices.

In short, pure NOR statutes offer some hope that the NOR process can keep homeowners from seeking the assistance of aggressive litigators in the first place or can redirect the interests of homeowners who have sought legal assistance without exploring the builder's desires to make repairs or before the builder has made an offer that is palatable to the homeowner. Ultimately, however, these hopes rely on the assumption that both parties are acting reasonably and can reach an amicable solution. As a practical matter, it is unclear how frequently those forces are likely to align – particularly when an aggressive lawyer is involved.

c. Plaintiff-friendly legal regimes

Pure NOR statutes have no impact on substantive laws that make construction defect lawsuits an attractive option for homeowners. The NOR process by itself is unlikely to deter a homeowner from filing a lawsuit if, as suggested above, the homeowner “has almost nothing to lose” because the state’s legal regime allows the homeowner to recover attorney fees and expert witness fees for even the most minor construction defect. The NOR process also offers nothing to resolve the substantive uncertainties or ambiguities in construction defect law that create incentives for plaintiffs to pursue litigation.

A few states have sought to address some of these issues by adding provisions to their NOR statute that would limit the builder's liability. The Kentucky statute, for example, limits the types of conduct or defects that are actionable. Other statutes limit the amount or type of damages that a homeowner may recover. The Colorado statute, for example, limits a homeowner to “actual damages” unless the homeowner recovers under the state's Consumer Protection Act, in which case the aggregate of treble damages under that act and attorneys fees may not exceed $250,000. The Alaska statute lists specific types of damages that homeowners may recover, which include: the reasonable cost of repairs to cure a defect or actual damages that result from a defect; the expenses of temporary housing; and fees for consultants and attorneys.

These provisions help to bring some certainty to the law, but leave much to be desired. On the one hand, some might argue the provisions are one-sided and go too far in restricting a plaintiff's recovery. Attorney fees and expert costs, for example, are at the center of this debate. Plaintiffs' lawyers contend that homeowners must be allowed to recover these fees to be made whole. Builders, however, contend that the ability to recover attorney and expert fees is a root cause of the construction defect litigation boom because recovery of those costs makes it profitable to pursue litigation no matter how trifling the defect may be.

On the other hand, the provisions fall short in defining what constitutes a construction defect. Although they eliminate some obviously improper claims (such as normal wear and tear or shrinkage), they provide only minimal guidance on homeowner rights and builder
responsibilities – the most critical components in the construction litigation equation.

Several commentators and analysts have suggested that state legislatures can remedy the uncertainty by adopting statutory warranties with clear performance standards. 177 About a dozen states already have such acts, with varying degrees of coverage and specificity, as discussed in further detail below. 178 Indeed, there is considerable room for disagreement on how long the warranty should last and how precisely to define the builder's responsibilities. Nonetheless, it seems reasonable to expect that with appropriate input from the affected constituencies, state legislatures can negotiate an appropriate compromise that balances “the goal of protecting homeowners from construction defects against the goal of keeping housing costs down.” 179 Such an undertaking would obviously require some time and effort, but it would make much more sense to expend that effort at this stage – to reduce the uncertainties about the parties' rights and responsibilities – than in trying to develop an elaborate NOR process to manage the multitude of lawsuits that attempt to identify those rights and responsibilities on a case by case basis.

B. Other Weaknesses of Pure NOR Statutes

While the preceding analysis suggests there is some merit to a notice and repair requirement, 180 legislative attempts to codify this requirement have raised a number of drafting concerns that undermine the efficiency of pure NOR statutes as a solution to the construction defect crisis. One concern is the constitutionality of particular NOR statutes or components thereof. Other concerns relate to the complexity and one-sided nature of many NOR statutes, as well as wide variation among statutes from state to state.

1. Constitutionality

Like other efforts at litigation reform, NOR statutes are susceptible to challenge on constitutional grounds. While the basic concept of requiring homeowners to give notice and opportunity to repair seems relatively unremarkable, particular aspects of an NOR statute may give rise to constitutional challenges. Limits on the amount of damages recoverable in construction defect litigation are a primary concern, but other provisions have been questioned on constitutional grounds as well.

a. Limitations on damages

Colorado's provisions limiting damages were challenged but upheld by a district court in Staufer v. Richmond American Homes of Colorado. 181 The homeowners alleged that the damage limitations in the NOR statute violated the equal protection clause of the state constitution because the provisions apply only to suits against construction professionals and not to other tort defendants or violators of the state's consumer protection act. 182 The homeowners also alleged that the NOR law violated their due process rights by prohibiting the recovery of non-economic damages. 183 Although one court has rejected those claims, commentators have also questioned whether Colorado's statute violates the equal protection clause because it treats
damages recoverable by residential and commercial property owners differently.\textsuperscript{184}

In Pennsylvania, Governor Edward Rendell cited a damages limitation provision as one of the reasons he vetoed a NOR bill in 2006.\textsuperscript{185} Pennsylvania Attorney General Tom Corbett had issued an opinion that the limitation on recovery would violate Article III of the state Constitution, which states that “in no other cases shall the General Assembly limit the amount to be recovered for injuries to property.”\textsuperscript{186}

b. Abatement or abrogation of claims

Some commentators have questioned the constitutionality of requiring trial courts to “abate” an action if the homeowner fails to comply with the pre-litigation notice and repair requirements.\textsuperscript{187} A Florida construction litigation attorney suggested that Florida's abatement requirement may violate the state supreme court's constitutional authority to promulgate the rules of civil practice.\textsuperscript{188}

In Arizona, Governor Janet Napolitano vetoed an NOR bill that would have required a majority of homeowners to vote in favor of filing construction defect litigation against the builder.\textsuperscript{189} Governor Napolitano suggested that for homeowners who could not obtain majority consent, their rights would abrogated in violation of Article 18, Section 6 of the Arizona Constitution, which provides: “the right of action to recover damages for injuries shall never be abrogated.”\textsuperscript{190} This type of NOR provision is particularly troublesome when the developer maintains voting rights within the association. If the developer still owned two-thirds of the project, for example, the developer could thwart efforts by other homeowners to bring suit against the developer.\textsuperscript{191}

c. Alternative dispute resolution provisions

A mandatory mediation provision raised constitutional questions for former Missouri Governor Bob Holden, who vetoed a 2004 version of the bill with that provision.\textsuperscript{192} He noted that the procedural hurdles delay homeowners from filing lawsuits, thereby violating Article I, section 14 of the Missouri Constitution, which provides: “That the court of justice shall be open to every person, and certain remedy provided for every injury to person, property, or character, and that right and justice shall be administered without sale, denial or delay.” Missouri later enacted a statute with a voluntary mediation option.

There may be similar constitutional questions about a provision in the Kansas statute permitting a homeowner, as an alternative to accepting or rejecting a builder's offer, to “elect an arbitration process pursuant to K.S.A. 5-201 et. seq.”\textsuperscript{193} A construction law attorney in that state suggested that the homeowner's unilateral election to select arbitration would, in some situations, violate the builder's “inviolate right” to a jury trial under the Kansas Constitution's Bill of Rights.\textsuperscript{194}

d. Other special provisions in NOR statutes
Observers have noted a handful of other provisions in NOR statutes that pose potential constitutional issues, including:

- Retrospective/special legislation – The *Staufer* lawsuit alleged that Colorado’s NOR statute should not be applied to the plaintiffs’ case because the cause of action had accrued before the statute took effect.195 The plaintiffs also challenged the statute as special legislation because it benefits only construction professionals.196

- Inspections and testing – Another potential infirmity in the Colorado statute is its requirement that homeowners permit builders to conduct inspections or destructive testing. Commentators suggest that these requirements may violate a homeowner's right to privacy or constitute a taking without just compensation.197

- “Deemed accepted” provisions – The 2003 version of the Florida statute provided that a builder's written offer to settle a claim or make repairs “must contain a statement that the claimant shall be deemed to have accepted the offer" if the homeowner/claimant failed to serve a written rejection of the offer on the builder within 15 days.198 A Florida construction litigation attorney opined that “[a] homeowner faced with this scenario may seek to challenge the statute on constitutional grounds by arguing that the ‘deemed acceptance’ provision unduly restricts access to the courts . . . ”199 The provision was subsequently removed from the Florida statute the following year, but at least two states – Georgia and Tennessee – have similar language in their laws.200

- Discovery rules – The Florida statute also may encroach upon the Supreme Court's powers by permitting trial courts to impose discovery sanctions upon a party who fails to produce discoverable evidence to the party before a lawsuit has been filed.201

2. Lopsided Requirements

Critics have complained that much of the NOR legislation is largely one-sided, imposing procedural requirements upon homeowners without any reciprocal requirements of builders. As noted above, many of the statutes enacted since 2002 have been based upon the NAHB template. It is not surprising, then, that the core elements of those statutes focus on what is required of *homeowners* – i.e., that homeowners must (1) provide notice of an alleged defect to the builder; (2) allow inspections of the alleged defect; and (3) give the builder an opportunity to make the repair (or to offer to make a repair).202 Some statutes go further to require homeowners to provide documentary evidence or permit destructive testing of the premises.203 Most statutes also provide sanctions for a homeowner's noncompliance, such as dismissing, abating, or staying any legal action alleging a construction defect until the homeowner complies with the NOR requirements.204 An “unreasonable rejection" of a builder's proposed settlement can result in a limitation of the homeowner's damages in a subsequent lawsuit and/or an award of costs and attorney fees to the builder.205

There has been significantly less attention paid to the builder's obligations under the
Some NOR statutes make no provision for a builder's failure to respond to the homeowner's notice; most of the others provide simply that if the builder fails to respond within a specified time, the homeowner may proceed with litigation without further notice. Commentators have also noted other deficiencies in many statutes, such as:

- No time limits for a builder to make the actual repairs.
- No remedies or procedures to follow if a builder fails to honor a settlement.
- No “reasonableness requirement” upon builders’ offers or guarantees that the repairs will be effective.
- No provision addressing damages caused by inspections or destructive testing.
- No “cooling off” period for builders to bring lawsuits for contractual payments withheld pending the dispute (and no exception for the homeowner to bring a counterclaim in the builder's suit).
- No ability for a homeowner to mitigate damages (such as a leaking roof) or make emergency repairs during the “cooling off” period.

One commentator has suggested that some of the disproportionate effects can be explained by the nature of the problem that NOR legislation is designed to solve:

To the extent that ‘right to cure' laws affect homeowners disproportionately, they do so because of a need to persuade homeowners to seek other remedies prior to commencing costly lawsuits. In contrast, the vast majority of suits filed by contractors against homeowners are simple contract claims for unpaid sums. “Right to cure” legislation purposefully targets the types of lawsuits that cause the greatest burden on the judicial system and the resources of the parties involved.

Notwithstanding this observation, however, the commentator conceded that NOR laws could achieve more balanced reform “by exempting individual litigants with single-family homes from the prelitigation requirements or by exploring other consumer-friendly amendments.”

3. Complexity

Developing NOR legislation presents a drafter's dilemma: There is a desire for making the statutes sufficiently detailed to spell out the parties' obligations and the procedures to be followed. Doing so, however, presents a risk that the statute will become too complex for the average homeowner to comprehend without legal assistance. Thus, to the extent that NOR statutes are designed to encourage communication between homeowners and builders before lawyers get involved, some NOR statutes are creating just the opposite effect.

One commentator notes that “the ‘procedural hoops' that most ‘right to cure' statutes put in place are often equally as complicated as the pleadings phase of litigation.” This concern is particularly applicable to statutes that require specific, detailed information in the notice to the
builder. Most statutes simply request that the notice describe the defect in "reasonable detail sufficient to determine the general nature of the alleged defect and results of the defect if known. 217 Some, however, require that the homeowner assert that the claim is made pursuant to the NOR statute; 218 provide disclosure of the homeowner's evidence of the defect (provided that such evidence is discoverable under the state's rules of civil procedure); 219 identify the method used to calculate damages; 220 and even (in one state), include the "legal theory of recovery. 221 Similar concerns apply to the requirements of how the notice is to be served, disclosure of other prelitigation discovery, participation in alternative dispute processes, and so on. Indeed, when statutes reach the level of complexity of some regimes, even the average lawyer would have some difficulty diagramming the requirements. 222

One could argue that compliance with the NOR procedures becomes an issue only if the homeowner actually attempts to bring a lawsuit, at which time the homeowner will probably need to hire an attorney anyway. 223 But this view ignores the reality that many homeowners, upon encountering the intricacies of some NOR statutes, will engage the services of a lawyer sooner in the process rather than later. In fact, given the detail required in the homeowner's notice to the builder, some lawyers have suggested that homeowners may want to employ construction experts to identify and analyze defects before filing the notice of claim. 224 As indicated above, 225 however, getting lawyers and experts involved will defeat the purpose of the NOR statute – particularly if the lawyer's advocacy causes positions to harden and creates a "greater gulf of distrust" 226 or the lawyer is motivated to obtain a monetary judgment or settlement under a contingent fee arrangement. 227

In many states, the only sanction for failure to comply with the NOR procedures is that the homeowner's lawsuit is stayed or dismissed until the procedures are followed. 228 Thus, the only consequence an unwary homeowner suffers is the delay inherent in the NOR process. In some cases, however, a homeowner's failure to understand the interrelationship between the NOR process and the statutes of limitation or repose may prove fatal to the claim. Some states have included tolling provisions in their statutes, 229 but one attorney has observed a serious potential for confusion – even for lawyers – as to how the tolling provision works. 230 Thus, homeowners could lose their claims if they fail to file a lawsuit before a statute of limitations expires, even though the NOR statute very clearly requires that the homeowner give notice and submit to the prelitigation process before filing suit. 231

In short, there is a fine line between developing a statute that is sufficiently detailed (to address the rights and responsibilities in an even-handed way) and one that is so overly complex that it imperils homeowners who proceed on their own or creates traps for unwary practitioners. To the extent that an NOR statute merely codifies what the average homeowner would do anyway – i.e., hand deliver a notice to the builder and wait a reasonable time for the builder to respond – the risks to consumers are minimized. The benefits of including additional requirements and extensive details should be weighed against the burdens of doing so, with an eye toward what is truly necessary to achieve the underlying goals of the legislation.
4. Lack of uniformity

There is considerable variation among the NOR statutes in existence. The length ranges from a couple of sentences tucked within a warranty act, as in Louisiana and Virginia,232 to more than forty sections in Nevada's act, which spans thirty pages in Michie's Nevada Revised Statutes Annotated.233 Significant deviations exist even among the statutes that are based upon the “pure NOR” template developed by the National Association of Home Builders.234

Although some variation is inevitable, the wide disparity is problematic for a building industry that is quickly becoming dominated by large companies that operate in multiple geographic locations. During 2006, the top 100 builders accounted for 43.8% of the closings on new homes, with more than a quarter of the new homes being built by just the top ten builders—all in a year that saw a significant overall drop in new home sales.235 Industry analysts have predicted that those numbers will continue to rise, with the top ten companies alone controlling forty to fifty percent of the market within the next decade.236

Most of the top 100 builders have increased their geographic diversity during the past two decades, and “[g]eographic expansion features prominently in the current growth plans” of these companies.237 One California company, KB Home, for example, “builds in 40 of the top 75 markets[.]”238 Another company, D.R. Horton, “began using some of its existing 77 markets as springboards to smaller satellite markets three years ago. The strategy—modeled after Wal-Mart's expansion across the country—enables the company to use much of the same staff and hold overhead down while capturing market share from small- and medium-sized builders[.]”239

As more builders adopt this strategy, there is an increasing desire for uniformity in the laws that govern the industry. To that end, the National Conference of Commissioners on Uniform State Laws (NCCUSL) appointed a study committee in 2006 to explore the possibility of developing a uniform NOR act. Although more than a dozen states had already enacted a version of the NAHB template by that time, the Joint Editorial Board on Uniform Property Acts predicted that the NAHB bill would not get universal acceptance because of substantial objections from trial lawyers, but a “more balance[d] and well-drafted act may be able to obtain substantial additional enactments.”240

After analyzing the existing statutes, the study committee expressed concerns about the significant lack of uniformity in the law.241 The committee ultimately determined, however, that an attempt to draft a uniform act would be futile without the political support of the building industry and/or consumer groups.242 Accordingly, NCCUSL declined to pursue the matter at that time. If legislatures are inclined to pursue a more comprehensive strategy as suggested below, however, NCCUSL’s assistance would be invaluable as a means of bringing uniformity to some components of that strategy.

V. A More Comprehensive Solution is Needed

As the foregoing analysis illustrates, pure NOR statutes are, at best, only a partial remedy
to the construction defect litigation problem. An Oregon study summed up the situation well when it stated that: “In general, the NOR laws have not had the positive impact that was intended and the laws passed in isolation, as they often have been, do not address the fundamental cause of construction defect claims.” Instead, a more comprehensive solution is needed that will:

- Clearly establish what constitutes a construction defect and the homeowner’s rights and builder’s responsibilities with respect to a defect;
- Improve the quality of construction through builder incentives, education, and oversight; and
- Improve insurance underwriting, claims processing, and investment practices.

Several states have already taken steps to develop a more comprehensive approach, with varying components in their package. What follows is a discussion of some of the most promising components, beginning with perhaps the most critical element: a statutory warranty act that establishes clear liability and performance standards.

A. Statutory Warranty with Clear Performance Standards

As indicated throughout this paper, the failure to clearly define construction defects (and homeowner rights and builder responsibilities) is at the root of the insurance liability crisis:

There is a clear need to give definition to construction defect litigation. Builders need guidelines under which to build. Homeowners need parameters within which they can know whether to demand repair or sue. Insurers need some assurance that they will not be underwriting themselves into certain liability for many construction defect claims. A new home warranty act can significantly diminish this uncertainty by delineating the builder’s responsibility for construction defects, setting precise limits on how long the warranty lasts with respect to different components of the home, and, most importantly, providing a clear definition of what constitutes a defect. About a dozen states currently have warranty acts for new homes in general or, in some states, special provisions for condominiums. Although a complete analysis of these statutes is beyond the scope of this article, the following discussion considers some of the key issues that would need to be addressed.

1. What Constitutes a Construction Defect?

Existing warranty acts provide varying degrees of specificity in defining construction defects and setting performance standards. Some contain only general definitions that provide little, if any, additional guidance beyond common law standards. Indiana, for example, provides a two-year warranty that the new home will be free from defects caused by faulty workmanship or defective materials. This type of definition leaves considerable room to litigate what constitutes faulty workmanship and would almost invariably require expert testimony.

Virginia provides a generalized test with substantially more specificity. It provides that new homes shall be “sufficiently (i) free from structural defects, so as to pass without objection
in the trade; (ii) constructed in a workmanlike manner, so as to pass without objection in the trade; and (iii) fit for habitation." Most importantly, the statute defines “structural defect” as “a defect or defects that reduce the stability of safety of the structure below accepted standards or that restrict the normal use thereof.” This definition ties the defect to performance or functionality, which is a concept that the average factfinder could apply in many cases without need for expert testimony. A hairline crack in the drywall, for example, does not reduce the safety of the wall or restrict its normal use; conversely, a factfinder could easily understand how how a three-inch separation between the wall and ceiling (leaving exposure to the outdoors) would demonstrate that the wall is not serving its normal use.

Other states have tied their warranties to compliance with local building codes, while a handful have developed specific performance standards that go beyond building codes. California's statute, for example, contains a comprehensive list of building standards. The list contains 45 specific requirements that cover most building components, including the integrity of doors, windows and other aspects of the exterior envelope, foundations and other structural issues, soil structure, plumbing, electrical, fire protection, and other systems.

A detailed list of performance standards obviously provides significant guidance as to what constitutes a construction defect. However, there have been criticisms that California's standards are both too detailed and not detailed enough. Builders are also concerned that California's list of building standards might “supplant the 'standard of care'” for construction professionals, requiring courts to measure the professional's conduct against the statutory standards, rather than against the performance of professional peers. At the very least, one construction litigation attorney suggested that the law imposes a negligence per se standard, which shifts the burden of proof to the construction professional to establish compliance with the standard. To the extent that the industry is involved in developing the performance standards, however, one might argue that such standards simply codify the industry's standard of care, rather than supplanting it.

2. Limitations on liability, damages

Some of the existing statutes supplement their liability standards by expressly excluding certain types of damage or defective conditions. Mississippi, for example, has a detailed list of exclusions that include damage from improper maintenance by anyone other than the builder, loss or damage that the homeowner has not taken timely action to minimize, normal deterioration, insect damage, mold (unless builder's negligence was a contributing cause), and consequential damages.

Some statutes also limit the extent of the builder's monetary liability. New Jersey, for example, limits the builder's liability to “the purchase price of the home in the first good faith sale thereof or the fair market value of the home on its complete date if there is no good faith sale.” Indiana provides that damages may not exceed the actual and consequential damages plus attorney fees. The act defines actual damages as “the amount necessary to effect repair
of the defect" or "the difference between the value of the new home without the defect and the value of the new home with the defect[.]

3. Length of warranty, statutes of limitation

Existing statutes vary considerably with respect to the length of the warranties, although they commonly require "one year for labor and materials, two years for delivery systems and appliances, ten years for structural." Builders benefit from having such clear limits on how long a building’s components are expected to be defect-free, as compared with common law rules that employ a much looser "reasonableness" test. Homeowners, however, are concerned that the standard one-year coverage for labor and materials is not long enough. Most statutes provide that the warranty extends to subsequent purchasers as well as the original purchaser of the home, thereby eliminating confusion that exists in the common law.

Many warranty acts also have their own statutes of limitation, but others are silent on the issue and implicitly invoke statutes of general application. When drafting a statute, legislators should ensure that the warranty terms are consistent with the state’s statute of limitations and statute of repose – i.e., that the warranty action is not time-barred before it has even accrued. The interrelationship between these two statutes presents a potential trap for litigants – particularly with respect to third-party claims.

4. Waiver

Some warranty acts provide that the parties may waive or disclaim the statutory warranty, provided that the disclaimer is sufficiently conspicuous in the parties' contract. In some states, this waiver is permitted only if the builder provides a substitute warranty that offers substantially the same protections as the statutory warranty. Louisiana, by contrast, provides that its warranty provisions "establish minimum required warranties and shall not be waived by the owner or reduced by the builder provided the home is a single or multiple family dwelling to be occupied by an owner as his home."

5. Exclusive or non-exclusive remedy

Louisiana provides that its warranty act provides the “exclusive remedies, warranties, and peremptive periods [statute of limitations]” concerning construction defect claims between homeowners and builders. Conversely, Maryland provides that its warranty provisions “are in addition to all other implied or express warranties provided by law or agreement.” Others take a middle ground, preserving the homeowner's right to pursue remedies based upon contract but otherwise preempting implied or express warranty claims other than those brought pursuant to the warranty act.

6. Notice and opportunity to repair
Although Section IV of this article was critical of relying solely upon pure NOR statutes as a resolution to the construction liability crisis, there is some benefit to requiring notice and opportunity to repair as part of a more comprehensive solution. Indeed, many of the existing warranty acts include some type of NOR provision. Most of these statutes include only cursory provisions, ranging from a couple of sentences to a couple of paragraphs. Some states, however, have enacted more detailed NOR provisions based upon the NAHB template.

7. Who backs the warranty?

Some warranty acts simply mandate that the builder warrants against the covered defects and do not address whether and how the builder will back that warranty. This raises some concerns about homeowner protection if the builder is insolvent or no longer in business when a defect claim arises. Even if the builder is not insolvent, the builder may lack insurance coverage for claims brought under a warranty act. As one study explained: “Since the cause of action is breach of warranty (contract), recovery from a liability policy is not available.”

Some states address the problem by requiring or permitting builders to carry insurance to cover their warranty exposure. Other states permit builders to satisfy their warranty obligation with a third-party warranty – i.e., one issued by a home warranty company. Although some homeowners prefer third-party warranties because a neutral party is guaranteeing the builder's performance, other homeowners have expressed great dissatisfaction with home warranty companies. New Jersey offers a New Home Warranty Security Fund, which allows homeowners to file their claims through a state agency and provides payment if the builder refuses or is unable to make repairs.

8. Alternative Dispute Resolution

Legislators have incorporated varying degrees of alternative dispute resolution into their warranty acts. Several states provide for mediation of claims. California, for example, has an elaborate mediation process for construction defect claims brought by a homeowners association. Maryland's statute simply provides that home warranty security plans shall “[p]rovide for mediation of disputes between an owner and a builder before a claim will be paid . . . .” Other states, such as Mississippi, permit arbitration, which is often a more expeditious method of resolving disputes but is viewed by some homeowners as “slanted against consumers.”

New Jersey has a combined mediation and arbitration process. Its claims resolution procedure begins with a basic notice and opportunity to repair process, but if the parties cannot achieve resolution on their own, a neutral third party steps in to mediate the claim and, if that fails, to arbitrate the claim (with the parties' consent). If the parties do not agree to arbitration, the dispute proceeds through an administrative review, ultimately appearing before an administrative law judge. Alternatively, a homeowner may choose to opt out of the
program and file suit in a court of law; doing so, however, precludes the owner from subsequently filing a claim with the state warranty plan.292

When arbitration is involved, one of the key considerations is the arbitrator's knowledge of the field in dispute. “You want a construction expert doing the arbitration; not a retired judge or a lawyer,” observed one construction litigation expert.293 To further this goal, Texas submits the construction dispute process to a nine-member commission dominated by members of the building trades.294 Some critics, however, have likened the process to “putting the foxes in charge of the henhouse.”295

9. Uniformity

Although home building was once a local trade, practiced by builders largely within their own home towns, the industry has become increasingly national in operation during the past several decades.296 The industry would benefit, therefore, from greater uniformity in the laws that govern builder responsibilities. Similarly, the insurance industry has many companies that operate nationwide and would gain efficiencies in its underwriting and claims management practice if laws were more uniform from state to state. These efficiencies would benefit consumers, in turn, because they would reduce the costs that builders and insurers incur in researching and complying with a multitude of variations in state laws.

One of the most obvious ways to achieve uniformity is to draft a uniform or model act through the National Conference of Commissioners on Uniform State Laws (NCCUSL). The organization has already drafted uniform acts that provide warranty protections to homeowners in condominium and other common interest developments.297 While some contend those uniform acts can be strengthened,298 they provide a good starting place for extending warranty protections to new homes outside common interest developments.

B. Better Quality Control

A second component of a comprehensive plan should seek to avoid construction defects in the first place by improving quality control. Government, insurance companies, builders, and homeowners can collectively structure a system that will encourage and reward good construction while deterring and punishing the bad actors.

Builders can start by implementing their own quality control programs299 and by structuring their contracts in a way that ensures that the party that created the defect takes responsibility for fixing it, rather than spreading the risk among multiple codefendants through third-party lawsuits.300 Indeed, one of the newest developments in the industry – integrated project delivery – holds substantial promise for improving quality by encouraging collaboration and cooperation between the key parties from the design phase to completion.301

The industry can also benefit from improved oversight. Local governments, for example
can do more to improve their building inspection practices. Insurance companies can also play a more active role by performing more detailed inspections for projects they underwrite and by offering financial incentives for quality construction.

If these market forces are insufficient, states can take additional steps to improve the quality of the workforce through licensing, certification, and education requirements. New Jersey, for example, has combined a builder registration requirement with its new home warranty program. The registration component supports the warranty program by providing for revocation or suspension of the builder’s registration for a variety of improprieties, including failure to participate in the dispute settlement process or to correct or settle a claim after a determination is made that the defect is the builder’s responsibility. To register, a builder must disclose whether the builder is enrolled in the state’s warranty plan or, alternatively, in a private warranty plan approved by the state. Under either program, the builder pays a warranty premium that is used to compensate homeowners in the event that the builder fails to repair or pay compensation for a defect. Under the state’s plan, the premium is determined by the builder’s claims history and length of time registered with the state, thus rewarding builders with good track records and imposing greater costs upon inferior builders. The builder’s liability under the warranty is limited to the purchase price of the home or its fair market value on the completion date.

Texas has combined builder registration and statutory warranties with a state-sponsored inspection process for single-family homes. Before the builder can obtain a registration certificate, the Texas Residential Construction Commission must be satisfied with the person’s honesty, trustworthiness, and integrity based on information supplied or discovered in connection with the person’s application. The statute also requires builders to comply with continuing education requirements to maintain their registration.

C. Insurance Reform and Other Litigation Control Strategies

A detailed analysis of the reforms necessary to address the reinsurance and investment practices of insurance companies is beyond the scope of this article. However, as discussed above, states should explore alternatives to the general liability policy as a means of insuring construction defects and should improve their data collection on construction defect claims. Insurance companies should also be encouraged or mandated to improve their underwriting and claims management practices. One of the most significant steps that insurers can take is to promote a unified defense when claims involve multiple defendants by amending construction and design contracts to provide for (1) a joint defense of all contractors and subcontractors; and (2) a process to resolve disputes between co-defendants as to their respective levels of responsibility for the defect.

D. Political Considerations

The preceding analysis suggests that there is room for debate on some of the best ways to
achieve the various components of a comprehensive plan. Therefore, one of the most critical factors in developing the plan is to ensure that all stakeholders are involved in the legislative process to ensure a fair and workable compromise.\textsuperscript{317} In Oregon, for example, the legislature established an independent task force to study the construction defect issue and offer recommended solutions.\textsuperscript{318}

This process can work, however, only if state legislatures resist the political pressures of the building and insurance industries' lobbies after a compromise has been reached.\textsuperscript{319} The Oregon legislature ultimately enacted only two of the eight task recommendations that required legislative action; defeat of the others was blamed largely upon lobbying efforts of special interest groups – notwithstanding the fact that these groups had been "well represented on the task force."\textsuperscript{320} One construction litigation attorney observed that the failure to act upon the task force's independent recommendations will cause a "serious setback" to attempts to resolve the construction industry crisis.\textsuperscript{321} "The most likely next step will be further special-interest legislative proposals favoring one party at the expense of another. Not only will this lead to contentious legislation, it will also likely result in simple and narrow proposals being advanced to solve a very complex problem."\textsuperscript{322}

VI. Conclusion

The construction defect crisis requires a solution that goes beyond the pure "notice and opportunity to repair" statutes that the building industry has heavily promoted for several years. As this article demonstrates, the construction defect crisis stems from a variety of causes, including builder error, insurance practices, and aggressive litigation. Although notice and opportunity to make repairs is an appropriate response to part of the problem, state legislatures should not rely solely on NOR statutes at the risk of failing to develop a more effective strategy that addresses the various factors contributing to the crisis.

Several states have already begun formulating more comprehensive solutions, and other states should follow this lead. This article highlights some of the more promising strategies, emphasizing that perhaps the most critical element is the development of a statutory warranty act that establishes clear liability and performance standards. Moreover, given the nationwide operations of both builders and insurers, greater uniformity in these laws would be desirable and could be achieved with the assistance of the National Conference of Commissioners on Uniform

*Professor of Law, Southern Illinois University School of Law. Professor Noble-Allgire served as the reporter for a study committee appointed by the National Conference of Commissioners on Uniform State Laws to examine notice and opportunity to repair statutes. Although this article is based in part upon research prepared for that committee, the views expressed in the article are entirely those of the author and not of NCCUSL. Professor Noble-Allgire thanks Robert M. Diamond, R. Wilson Freyermuth, Wenona Whitfield, and William Drennan for their thoughtful comments on earlier drafts of this article. She is particularly grateful to have Mr. Diamond's practical knowledge of the construction industry and construction defect litigation. She also acknowledges the research and editorial assistance of Amber Jeralds, Class of 2008, Southern Illinois University, as well as the helpful comments of faculty colleagues who attended an oral presentation of this work.


3Aalberts, supra note 1; 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?, 44 Santa Clara L. Rev. 1249, 1250 (2004); Nat’l Ass’n of Home Builders & NERA Econ. Consult., Construction Defect Disputes – Getting to Yes Without Going to Court 1 (2005)[hereinafter NAHB Report], available at http://www.nera.com/Publication.asp?p_ID=2529&login=6923124. These problems have been compounded by other economic pressures, such as dramatic construction cost increases associated with the depressed dollar and a credit crunch caused by the subprime lending predicament, as well the aging and retirement of many skilled construction workers. See infra notes 31-32 and accompanying text.

4See infra notes 17-23 and accompanying text.

5See infra notes 84-98 and accompanying text for a summary of the statutes.


7Id. at 543. This legal theory is one of nine potential causes of action available to address construction defects in some jurisdictions today. See infra note 44 and accompanying text.


9There are no official statistics available on the number of lawsuits alleging construction defects. See Cynthia Kroll et al., The Impact of Construction-Defect Litigation on Condominium Development, Cal. Pol’y Research Ctr. Brief, Vol. 14, No. 7 (Oct. 2002), at 2. Informal surveys, however, have demonstrated a dramatic rise in such litigation in some parts of the country. See, e.g., Michael M. Edwards, Jr., et al, A Defense Perspective to Construction Defect Litigation and the Upcoming Legislative Session, Nev. Law., Jan. 2001, at 30 (informal survey showed number of cases filed by 10 prominent Nevada plaintiffs’ attorneys involving condominiums/townhouses rose ten-fold in a four-year period – from five in 1996 to 53 in 1999); NAHB Report, supra note 3, at 2, n.20 (reporting that the number of cases filed by the three firms most active in construction litigation in Colorado rose 10% per year for the three-year period starting in 2000).

10Zito, supra note 2 (stating that in 2000, California “insurers collected $15.2 million and paid out $44.8 million" for construction liability claims, which includes construction defect claims as well as other liabilities, such as personal injuries during the construction process)(citing statistics from the Insurance Services Offices, which provides research for the insurance industry).

11See, e.g., Roger Dunstan & Jennifer Swenson, Construction Defect Litigation and the Condominium Market, Cal. Res. Bureau Note, Vol. 6, No. 7 (Nov. 1999)(reporting that more than 40 admitted companies wrote this type of insurance in California in the early 1980s, but only a couple did so in 1999); Am. Actuarial Consulting Group, Insurance Analysis: Reforms,
Alternatives, and Pricing 10-14 (Sept. 2006) [hereinafter Oregon Ins. Report] (report to Oregon Task Force on Construction Claims; cites surveys that found that insurance premiums increased between 50% and 143% for Oregon builders from the late 1990s to early 2000s); NAHB, supra note 3, at 2 (citing anecdotal reports of insurance costs rising as much as 60% or more in one year); Robert Gavin, Home Builders Face Insurance Woes – Coverage Scarce, Premiums High After an Increase in Construction Suits, Wall. St. J., Feb. 2002, at B7 (reporting cases in which insurance premiums were as much as 12 times higher than the previous year, with reduced coverage).


13 As indicated earlier, supra note 9, there are no official statistics on the number of construction defect lawsuits or settlements.

14 See Dunstan & Swenson, supra note 11, at 1, 3 (discussing litigation that followed condominium construction boom in California in the 1980s); Aalberts, supra note 1, at 686 (noting that some observers contend that Nevada's rising numbers of construction defect lawsuits in the mid-1990s was due in part to the arrival of construction defect attorneys from California); Andree J.B. Swanson, Las Vegas: Boom Town for Construction Defect Litigation, Nev. Law., Dec. 1997, at 15, 16 (observing that Nevada's construction defect litigation is booming as California's market "is drying up").

15 Stephanie K. Jones, Construction Defects Burning a Hole Through the Residential Contractors Market, Ins. J., July 19, 2004; G. William Quatman & Heber O. Gonzalez, Right-to-Cure Laws Try to Cool Off Condo's Hottest Claims, Constr. Law., Summer 2007, at 13, 20 (listing Arizona, California, Colorado, Florida, Louisiana, North and South Carolina, Oregon, Texas, and Washington as “high claims” states); Masters et al., supra note 12, at 15 (stating that the crisis first hit builders in "states with heavy construction defect exposures" such as California, Texas, and Florida, but has spread to Colorado, Arizona, Utah, and Nevada and "insurance industry sources indicate that builders nationwide will, to a greater or lesser degree, experience the same difficulty with availability, affordability, and restrictive coverage").

16 Jones, supra note 15. Paul Norman of the Norman-Spencer McKernan Agency (NSM) in Dayton, Ohio, told the magazine that some insurance companies have modified their underwriting practices because of the “actual or perceived” exposures to construction defect liability. As he explained: “In some states, it's construction defects and in other states it's the fear of construction defects[. . .]. Construction defects is not in every state, there are just fears of it. Because of that some companies have some very stringent underwriting practices for this class of business.” Id.

17 Anna Amundson & Jessica Thompson, Litigation Alternative – Does “Fix-It” Legislation Really Fix It?, For the Defense, Sept. 2006 (noting that in many cases, when the costs of litigation – including attorney and expert fees – are removed, homeowners are left “with an inadequate monetary settlement that prevents them from repairing or replacing the very subject of the litigation”); NAHB Report, supra 3, at 4 (citing NAHB-sponsored study that found that after legal fees and court costs are deducted, “approximately half of the homeowners are left with a net recovery inadequate to make repairs”).

18 See Oregon Ins. Report, supra note 11, at 9 (“For the insurers, the legal cost often equals or exceeds the cost of repair.”); see also Center for Democratic Culture, The Law and Politics of
Tort Reform, 4 Nev. L.J. 377, 406 (2003) [hereinafter Tort Reform] (describing Nevada case in which homeowners were awarded $7.8 million for the defect but the attorney fee request in the case was $9.3 million).

Builders have expressed concern that “the claimed ‘defects’ in some suits in highly litigious states were fictitious – having no consequence for the homes’ integrity – and that the homeowners never perform the repairs post-suit.” NAHB Report, supra note 3, at 5-6. An NAHB-sponsored study looked at several large-scale projects in which settlements were reached, but in most cases, no building permits were filed for repairing the alleged defect; in a handful of cases, the study found permits for unrelated remodeling work or additions – including construction of pools and spas. Id. “The lack of evidence of repair work is inconsistent with plaintiffs’ demands for damages.” Id. at 6.

Tronquet, supra note 3, at 1250-51.


See Steve Hill, Op-Ed, Should Construction-Defect Laws be Overhauled – Yes, Las Vegas Sun, Jan. 3, 2003, at 1D (stating that “the FHA and VA will not refinance a loan for a home in a lawsuit, nor will they loan money to a potential buyer” and “[r]eal estate agents often will not show the home to potential buyers.”). But see Sullan Sandgrund, Smith & Perczak, P.C., Construction Defect FAQs, http://www.vssss.com/CM/Custom/Construction-Defect-FAQs.asp#14 (asserting that a construction defect lawsuit “should have no greater [e]ffect on property values than the existence of those defects already has had on property values”).

Tronquet, supra note 3, at 1250-51.

Tort Reform, supra note 18, at 386; NAHB Report, supra note 3, at 1.

Quatman & Gonzalez, supra note 15, at 14; John Frith, Builders Battle Trial Lawyers Who Carpet Bomb Their Communities, Cal. Bldrs. Magazine, Sept./Oct. 2004 (noting that suits against condominium builders were “an efficient way to do business” because “the lawyers could deal with a homeowners' association board of directors and there were usually dozens of units involved”). Although condominium and townhouse projects were particularly problematic at an early stage, the NAHB-sponsored study asserts that “[t]his successful formula for class action solicitations is now being applied with greater frequency to communities with single- family homes.” NAHB Report, supra note 3, at 2.

See San Diego Ass’n of Gov’ts, Condominium Construction Defect Litigation and Affordable Housing: The Anatomy of a Problem, with Strategies for a Solution 3 (July 20, 2001) [hereinafter San Diego Report]. When an individual is suing on a single- family home, he is paying his own legal fees and, therefore, has an economic incentive to sue only for serious problems, not minor or speculative concerns. By contrast, condominium and homeowner associations have the ability to pool the resources of many homeowners by levying assessments to pay for litigation. The boards of these associations also have an economic incentive to make claims on behalf of other owners – even for minor defects – rather than risking personal responsibility for breach of their fiduciary duties.

Tronquet, supra note 3, at 1261 n.95; Darin T. Allen, Construction Defects Litigation and the “Right to Cure” Revolution, Constr. Briefings, March 2006, at 3.

For a good example of the polarized positions, see Tort Reform, supra note 18, passim (transcript of one-day symposium discussing construction defect litigation and medical
malpractice).

29Oregon Ins. Report, supra note 11, at 2 (“Consumer Reports indicates that 15% of new homes have at least one major defect. If this number is correct, the total number of defects would be increasing just based on the yearly increase in housing starts.”); Debra Pogrund Stark & Andrew Cook, Pay It Forward: A Proactive Model to Resolving Construction Defects and Market Failure, 38 Val. U. L. Rev. 1, 6 (2003)(citing New Jersey statistics suggesting that “valid claims were raised against builders/developers in approximately ten percent of the new homes built”).

30Michael J. White, Arizona Defect and Mold Litigation: Parties and Theories of Liability *1 (Nat'l Bus. Inst. 2004); San Diego Report, supra note 26, at 4-5 (“The demand for new construction [during San Diego's economic boom in the 1970s and 1980s] soon tied up the supply of experienced, reputable building companies. New companies – from the inexperienced with good intentions to the truly fly-by-night – entered the market and built many condominiums during this boom period.”).


32The depressed value of the dollar has increased the price of fuel and construction materials, according to Ken Simonson, chief economist for the Associated General Contractors of America, observing that “[c]umulative construction cost increases since the end of 2003 have far outstripped inflation, despite the housing slump and recent declines in some construction input prices.”See Matt Hudgins, Fed Rate Cut May Accelerate Rising Construction Costs, Natl Real Est. Investor, Oct. 11, 2007, available at http://nreionline.com/strategies/corporate/rising_construction_costs/. Builders also suffered a loss in sales and a tightening of their own ability to get credit during the subprime mortgage crisis. See Claire Koltko, Credit Crunch – Credit tightening is now reaching builders, Builder, Jan. 1, 2008, at 88 (“The subprime-induced tightening of credit conditions in home mortgage markets now is being joined by tightening in credit markets where builders and developers raise funds – the markets for land acquisition, land development and construction loans . . . .”).

33Tort Reform, supra note 18, at 389 (statement of Scott Canepa). Canepa added that when the state’s insurance commissioner asked insurers for input on why rates had risen so sharply for contractors, one of the insurance companies said that “while the high cost of litigation is one reason for claim severity, it believes the most critical cost driver, from a claims perspective, is the substandard construction practices and poor workmanship by the contractors.” Id.; see also Am. Ass'n Ins. Servs., Poor Construction – Legal Rulings in Construction Defect Cases Threaten Fundamental Insurance Principles, AAIS Viewpoint (Summer 2001) (“Make no mistake, the principal reason for the rise in construction defect cases is the discovery of genuine
defects in construction. The trend cannot be dismissed as the work of greedy plaintiffs' attorneys. 

34Quatman & Gonzalez, supra note 15, at 13; Marianne Sparks, Construction Defect Resource Guide 2 (2005) ("From the foundation slab to the roof . . . home buyers have sought to make the general contractor the guarantor of the perfection of each of these items."), available at http://www.munichreamerica.com/content/rl/construction_defect.htm.

35See Sparks, supra note 34, at 2 (noting an increased awareness of construction defect claims, "thanks to several high-profile and highly publicized court battles over construction defects and mold allegations"); Masters et al., supra note 12, at 5 (same).

36See John G. Steinkamp, A Case for Federal Transfer Taxation, 55 Ark. L. Rev. 1, 74 (2002) ("For most Americans, their principal residences are their single largest investment, constituting approximately 60% of all assets held by the middle 60% of households in 1998.") (citing Edward N. Wolff, Recent Trends in Wealth Ownership, 1983-1998, 13, tbl.5 (Jerome Levy Econ. Inst. Working Paper No. 300, 2000)).

37See Quatman & Gonzalez, supra note 15, at 13.

38See John Boyden, Chapter 40 and Construction Defect Litigation – Boom or Bust?, Nev. Law., Jan 2002, at 10, 11 (discussing Nevada provision allowing plaintiffs to recover attorney fees as well as the fees of experts hired to investigate defects); Amundson & Thompson, supra note 17, at 28 (describing recovery of attorney fees as well as double or treble damages under suits brought under Texas Deceptive Trade Practices Act prior to the state's enactment of its Residential Construction Liability Act in 1989). Defense attorneys contend that attorney fees and expert fees increase the exposure to defendants and insurers, making it more difficult to settle the litigation. See Tort Reform, supra note 18, at 392 (comments of Elizabeth Goff Gonzalez). But plaintiffs' attorneys contend that recovery of such fees are necessary to make the homeowner whole. See Robert Maddox, In Defense of Chapter 40: Homeowner's Rights, Nev. Law., April 2002, at 28-29.

39Kroll, supra note 9, at 3 (noting that California is among only a handful of states applying strict liability to construction defect claims); Masters et al., supra note 12, at 5.

40See Quatman & Gonzalez, supra note 15, at 20 (listing states).

41Masters et al., supra note 12, at 5.

42Boyden, supra note 38, at 11.

43Allen, supra note 27, at 3.

44See Sparks, supra note 34, at 6 (listing as possible theories: strict liability or negligence per se (for violation of a building code or other law); negligence; breach of contract; breach of implied or express warranty; fraud and negligent misrepresentation; breach of fiduciary obligation (by directors or officers of a homeowner's association); negligent and intentional infliction of emotional distress; nuisance; and products liability); see also Tronquet, supra note 3, at 1252-57; White, supra note 30, at 14-50.

46See Sparks, supra note 34, at 3. One construction industry resource suggests that defects recognized by the courts fall into one of four general categories:

- **Design deficiencies** – buildings and systems do not work as intended from a design standpoint (e.g., a roof system prone to leaks because of a poor design);
- **Material deficiencies** – use of inferior building materials or installed components (e.g., windows that fail to function adequately, even when properly installed);
- **Construction deficiencies** – poor quality or substandard workmanship (e.g., water infiltration because of poor construction); and
- **Subsurface/geotechnical problems** – soil conditions that are not properly addressed during construction, causing cracked foundations, etc.

Id. at 3.

47See, e.g., Masters et al., supra note 12, at 4-5; Allen, supra note 27, at 3 (discussing rise in number of attorneys specialized in this area of practice).

48See, e.g., Andrea Adelson, *The Great Nevada Litigation Rush*, N.Y. Times, Dec. 4, 1996, at 1 (discussing lawyers who trolled for clients at trade shows and a condominium manager who was courted with free gifts); Masters et al., supra note 12, at 5 (discussing lawyers who share information via the internet about pending claims, emerging builder liability issues, and particular builders); Frith, supra note 25 (describing targeted mass mailings sent to condominium and townhouse communities); *Construction Defects: The View from the Other Side* – Why your client doesn’t believe in Right to Cure, only Right to Sue, N.M. Home Bldrs. Ass’n Housing J., Feb. 2004, at 8 (describing practice called “deconstruction” in which lawyers allegedly “purchase one home in a tract and take it apart in order to find every little defect or code violation possible” and then file class action lawsuits alleging that those defects exist throughout the development); Meg Green, *A Hole in the Wall: Soaring Construction-Defect Litigation is Shaking the Foundation of the Commercial General Liability Market* – and Residential Contractors are Getting Hammered, Best’s Review, July 1, 2003, at 51 (reporting observation of attorney Robert M. Diamond that “lawyers are hiring forensic engineers to examine properties to find defects”).


50See *Tort Reform*, supra note 18, at 389-90 (comments by plaintiffs’ attorney Scott Canepa, who observed that contrary to the frequent claims of frivolous lawsuits, he knew of no cases in which the contractor walked away with a complete defense verdict).

51*Tort Reform*, supra note 18, at 438 (comments of defense lawyer Mark Ferrario).

52Tronquet, supra note 3, at 1262 n.99.

53See infra note 74 and accompanying text.

54Masters et al., supra 12, at 3-4.

55Kozlowski, supra note 45, at 11.

56Id. at 10.

57See supra note 44 and accompanying text.

58Kozlowski, supra note 45, at 10-11. The ambiguity regarding what constitutes a construction defect not makes it difficult for insurers to predict losses, but also complicates negotiations between homeowners and builders. As a San Diego study observed: “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." San Diego Report, supra note 26, at 9.


61 Wielinski & Young, supra note 59; Shapiro, supra note 60.

62 See Robert E. Frankel, Insurance Recovery: Advanced Issues in Real Estate Law, Nat'l Bus. Inst. – Real Estate Law: Advanced Issues and Answers (2007), available on Westlaw at 38823 NBI-CLE 67; see also Wielinski & Young, supra note 59 (analyzing the division among the courts and concluding: “Despite similar fact patterns, results are so divergent that they are impossible to reconcile, and even an explanation is difficult to achieve.”); Shapiro, supra note 60.

63 Oregon Ins. Report, supra note 11, at 10. Courts are still divided over whether the CGL policy covers construction defects (thereby requiring insurers to pay to repair the defect itself) or only damages to other property caused by such defects. See, e.g., Lamar Homes, Inc., v. Mid-Continent Cas. Co., 239 S.W.3d 236 (Tex. 2007)(recognizing split of authority and concluding that “allegations of unintended construction defects may constitute an ‘accident’ or ‘occurrence’ under the CGL policy” triggering the insurer’s duty to defend the contractor against a construction defect lawsuit).

64 Kozlowski, supra note 45, at 10.


66 Green, supra note 48, at 51. Attorney Robert Diamond observed that insurance companies often hire attorneys who lack experience with community associations and residential construction defect claims.

Negotiating with homeowners associations isn't like dealing with a commercial entity, Diamond said. “We're dealing with peoples' homes, and there's a big emotional attachment. You can throw out money, and put in its place game theory... How insurance companies' claims departments deal with these claims is one of the reasons why there [are] significant claims and losses.”

Id.

67 Id; see also Dunstan & Swenson, supra note 11, at 8 (“Attorneys for insurance companies argue that a few uncooperative insurance companies complicate defense and settlements.”).

68 Green, supra note 48, at 51. Diamond cited one case in which several insurance companies – and dozens of attorneys – ended up in the courtroom. “You'll never get them to reach a settlement," he said. Id.


70 See, e.g., Dunstan & Swenson, supra note 2, at 8 (“Attorneys for insurance companies argue that a few uncooperative insurance companies complicate defense and settlements. They argue that the ability to bring bad faith lawsuits against these companies would allow recovery of attorney's fees and would facilitate settlement or defense of these cases.”).

71 As explained in a report to the Oregon Task Force on Construction Claims:
Commercial liability insurance is heavily reinsured. The reason for the reinsurance is the nature of the very broad coverage offered by commercial policies, and is not specifically related to a single exposure, such as construction defects. Exposure to unexpected catastrophic perils such as asbestos underlies this requirement.

Oregon Ins. Report, supra note 11, at 10.

72Id.
73Masters et al., supra note 12, at 6.
74Id.
75Oregon Ins. Report, supra note 11, at 10.
76Masters et al., supra note 12, at 6.
77Gavin, supra note 11.
78Wielinski & Young, supra note 59.
79See Oregon Ins. Report, supra note 11, at 17-19, app. I (discussing states that have enacted New Home Warranty Acts). Although the specific provisions vary from state to state, the acts commonly provide warranties of “one year for labor and materials, two years for delivery systems and appliances, and ten years for structural” components.; see also Randy Sutton, Validity, Construction and Application of New Home Warranty Acts, 101 A.L.R.5th 447 (2002).
80A statute of repose bars a plaintiff’s cause of action after a specific time from the date construction is completed – even if the cause of action has not accrued for purposes of the statute of limitations. Legislatures began enacting statutes of repose in the mid-1960s in response to industry concerns about a series of judicial opinions that eliminated the privity of contract requirement for construction defect lawsuits and held that the cause of action accrued when the injury was discovered; the cumulative effect of these decisions was to expose the building industry to liability many years after construction had been completed. Martha Ratnoff Fleisher, Validity, as to Claim Alleging Design or Building Defects, of Statute Imposing Time Limitations Upon Action Against Architect, Engineer, or Builder for Injury or Death Arising Out of Defective or Unsafe Condition of Improvement to Real Property, 5 A.L.R. 6th 497 (2005); see also George Anthony Smith, Comment, Recent Statutory Developments Concerning the Limitations of Actions Against Architects, Engineers, and Builders, 60 Ky. L.J. 462, 463-64 (1972) (noting that 30 states enacted such legislation from 1965 to 1967 at the urging of the American Institute of Architects, the National Society of Professional Engineers, and the Associated General Contractors).
81See infra notes 84-98 and accompanying text for a list of statutes.
84Most of the laws passed since 2001 are based upon a model developed by the American Legislative Exchange Council at the request of the National Association of Home Builders. Bradford, supra note 82.

86 Most statutes permit the builder to make an offer to repair, which the homeowner may accept or reject. See, e.g., Mo. Rev. Stat. § 436.356. This is not to say that homeowners may arbitrarily reject such offers; some statutes impose sanctions upon homeowners for rejecting a reasonable settlement offer. See infra notes 146-152. By comparison, two states with complex statutory regimes require the homeowner to allow repairs to be made if the builder so elects. See Cal. Civ. Code § 918 (but homeowner may request that a different builder perform the repairs); Nev. Rev. Stat. § 40.6472(3).

87 See, e.g., Wash. Rev. Code §§ 64.50.005–.060.


94 Minn. Stat. §§ 327A.02, 327A.03(a).


99 Id. §§ 401.001–438.001 (statutory warranties and state-sponsored inspection process for new single-family homes and duplexes).