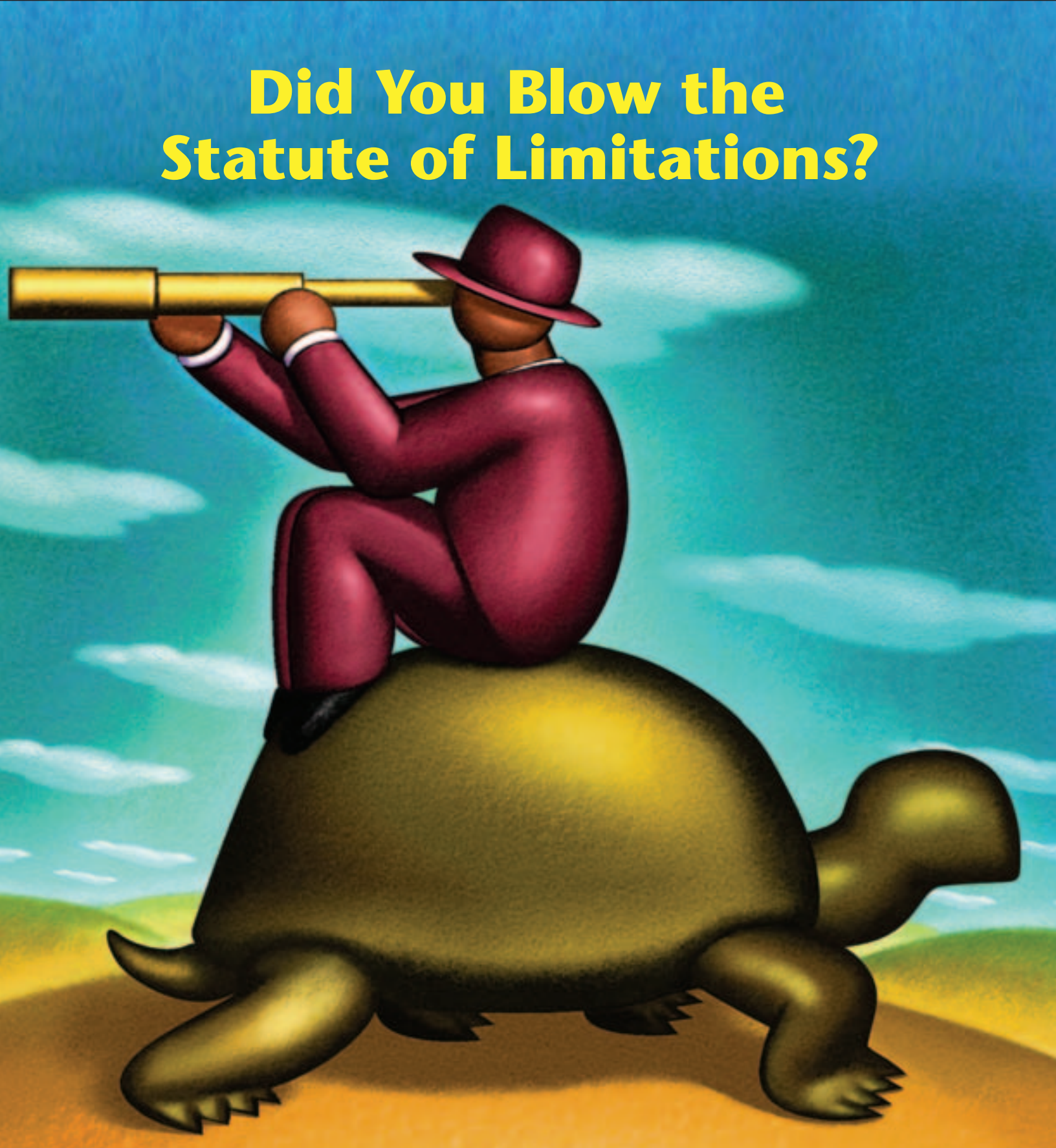
Did You Blow the Statute of Limitations?



The Effect of Title 7 on a Community Association's Right to Sue for Construction Defects

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It's 1998. The plumbing in your association's 5-year old condo project has started to leak. You hire a plumber who discovers that the plumbing lines are made out of imported galvanized pipe and it is corroding from within, leaving pinhole leaks throughout. Further investigation reveals that this pipe was withdrawn from the market years ago because of this tendency to corrode and leak. You also have a serious noise problem between units. Owners can hear the neighbors above them walking around. Your architect discovers that there are no resilient channels in the ceiling as required. Finally, numerous trees around the complex begin to die. Your landscape contractor investigates and finds that they were planted in holes that were too small for the root ball. Your letters to the developer for assistance are ignored. A few months later, you decide to file suit. Later your attorney is able to settle the matter for enough money to replace the damaged pipes, fix the ceilings and replace the trees.

It's 2008. Same facts as above, except that the condominiums were built in 2003. Although your attorney files suit within a year after you discover all of these problems, this time the suit is dismissed by the court as being untimely filed. What happened? How can two identical suits, filed 10 years apart by two community associations succeed for one and completely fail for the other?

Title 7 of the California Civil Code is what happened. Originally known as SB800, it was passed by the Legislature in 2002. It applies to new residential construction first sold after January 1, 2003. It contains three essential parts: performance standards for building components; revised alternative dispute procedures, including an enhanced right given to builders to make repairs to defective projects; and new, often shorter, limitations on a community association's right to bring an action against the developer.

In the examples above, there were three defective components: plumbing, acoustics and landscaping. In the first example, the project was sold before 2003 and was not subject to the provisions of Title 7; so the association had as long as ten years to bring suit as long as they filed the action within three years from the time they discovered the problem. In the second example, the project was first sold after January 1, 2003; so Title 7 applied and the time to file actions to recover for defects in those same three components is only four years, one year, and two years, respectively, regardless of when the problem was discovered. Therefore in our examples, a project that was just 7 years old has already lost the right to recover for significant defects in key components even though the owners had no notice of the existence of these problems! We'll discuss these new limitation periods imposed by Title 7, but first, a primer on various limitations on actions in construction defect cases.

Statutory Limitations on Actions

An "action" is a lawsuit—initiated by a complaint filed in a California Superior Court. Statutory limitations on the right to bring an action (commonly, "statutes of limitation") by a community association asserting its claims vs. the developer/builder of a project, appear in several places in California law. Applicable statutes can be divided into two categories: those imposing time limits on actions that are triggered by the discovery of damage or the occurrence of some event that leads to damage; and those that impose outside limits on the right to sue regardless of when the damage occurs or is discovered. The former are loosely termed "discovery" statutes, and the latter are "statutes of repose." Either or both types of time limit, if allowed to expire, can effectively deprive a community association plaintiff of its legal right to bring an action against a developer or others involved in the construction of a project.

Statutes of Repose

Notwithstanding when a negligent act or a breach of contract occurred or when damages were discovered, no action may be brought later than the dates established by various statutes of repose. These are "outside" time limits and depend upon when a project was first sold or upon other enumerated events. For many years, this was primarily California Code of Civil Procedure (CCP) 337.15, which applied a limitation period of 10 years starting with the earliest of four different definitions of the "substantial completion" of a project. A new statute, Title 7 of the California Civil Code (CC), provides shorter statutes of repose for actions for damage to certain specific components of a building. Therefore, the first task is to determine which statute applies, and thereafter, how its provisions govern the right to bring an action against the builder.[1]

"New" California Civil Code Title 7, Section 938 states that its provisions apply "to new residential units where the purchase agreement with the buyer was signed by the seller on or after January 1, 2003." If a home or a building was the subject of a purchase agreement signed prior to that date, the "old" rule of ten years for all components would apply. For projects that qualify

1. California Civil Code, Title 7, commencing with Section 895, was the result of SB800, passed in 2002. It is enormously dense and convoluted and, hence, difficult to interpret. It will undoubtedly give rise to many disputes over its application and meaning, which the courts will eventually have to unravel. We have given its provisions the interpretation that we understand was the intent of the drafters of the legislation and the Legislature. There are many pitfalls for the unwary in its application, however, and we cannot always be sure that our interpretations will prevail. Therefore, wherever we can, we recommend the most conservative course of action.

under the "new" statute, the general rule is that an action must be brought no later than a fixed period, depending upon the component, from either the date of "close of escrow" or "substantial completion." For community association claims, "close of escrow" is defined as " …the date of substantial completion, as defined in Section 337.15 of the Code of Civil Procedure (see above), or the date the builder relinquishes control over the association's ability to decide whether to initiate a claim under this title, whichever is later." [CC 895(e)] However, this "close of escrow" trigger date only applies to certain specifically stated components, and the balance of the components, in actions brought under this statute, fall under the provisions of CC Section 941, which states: "(a) Except as specifically set forth in this title, no action may be brought to recover under this title more than 10 years after substantial completion of the improvement but not later than the date of recordation of a valid notice of completion."[2]

Apply either the date of relinquishment of builder majority control or "substantial completion," whichever is later, as the trigger date for the limitation periods which commence on "close of escrow."[3] The period of limitations for all other components commenced on either "substantial completion" of the project or upon the recording of a Notice of Completion, whichever is later.[4] Let's assume that the developer of a particular project relinquished majority control as of September, 2004. Based on that, the periods of repose for those specified components that commence on "close of escrow" would start to run as of September, 2004, except in those rare instances where a developer relinquishes majority control of the association before the project is finished. For all other components, those that are subject only to the general, ten-year period of limitation, that period commences, as stated, upon the date of recording of a Notice of Completion or upon the date of "substantial completion." That date is not defined by the statute. It is defined, however, elsewhere in the code.[5]

"Discovery" Statutes

Notwithstanding the "outside" time limits provided under the applicable statutes of repose, an association's claim may also be subject to potentially shorter limitation periods dating from "discovery" of a claim or other events that constitute the commencement of a legal claim.[6] The length of time to bring an action allowed by the various statutes depends upon the legal theory or "cause of action" being applied to the facts of the claim. Those causes of action traditionally available to a community association for construction problems are: Strict Liability; Negligence; Implied Warranty; Express Warranty; Negligent Misrepresentation; and Intentional Acts, such as Fraud. Title 7 of the Civil Code, however, provides only for a single, statutory cause of action in the event that a component does not meet the standards set forth in that code. Certain contract or fraud claims are made exceptions to the coverage of the new statute.[7]

Other time limits for bringing actions based on construction defect claims are found in the California Code of Civil Procedure. CCP 337 governs actions for damage arising from the breach of a written contract, which must be brought within four years from the date of the breach. CCP 339 governs actions for breach of an oral contract that must be brought within two years from the date of breach.

CCP 338 governs actions for property damage and is three years from date of the claimant's "discovery" of the facts supporting the claim. Determining what constitutes "discovery" of a claim

2. This is similar to, but not exactly, the same as the language of the existing 10-year limitation period set forth in CCP 337.15 that also defines "substantial completion" but this statute does not. Also, it is written in such a way as to suggest that the recording of a valid notice of completion could cut off the rights of a claimant. We are confident, however, that a court would interpret that phrase as meaning the 10-year period starts at substantial completion or upon the recording of a valid notice of completion, whichever is earlier. The existing statute (CCP337.15) would appear to continue to apply to any causes of action that are exceptions to the "new" statute; i.e., contract claims and claims for intentional torts. However, since it also provides that it is tolled during periods of builder control, the net effect on all association claims is the same.

3. Certain specifically enumerated building components have special periods of limitation which are triggered upon "close of escrow" (CC 896) that, for a community association, is defined as the date of surrender of builder control or "substantial completion," whichever is later. (CC 895)

4. An action brought on any building component for which Title 7 does not assign a specific period of limitations on actions is governed by the 10-year limitation period specified in CC 941.

5. CCP 337.15 defines "substantial completion" for the application of the existing 10-year statute of repose and that definition was recognized by the new statute [CC895(e)] for at least some purposes.

such that it will trigger the start of a limitation period is not a simple matter. Various cases have held that "discovery" occurs when the potential plaintiff has sufficient knowledge of the damage, the cause of the damage, and the fact that the cause is related to the defendant's negligence. Ultimately, only a judge can make that determination, but counsel, analyzing the facts of each case, can usually make a reasonable assessment of when a limitation period is triggered.

If these shorter limitation periods apply, regardless of what the "outside" time limit may be in a particular case, an action brought by a community association (or any other plaintiff) has to meet these time requirements even though the applicable statutes of repose may be longer. Of course, the most prudent course is to act to suspend all limitation periods well before their expiration.

Illustrations

Example 1: Let's assume that an association building is "substantially completed" in September, 2004, and it is notified of a roof leak for the first time in October, 2006. During the course of repairs, it discovers that the problem is due to a defect in the original construction. It knows this because the contractor who repaired that specific location provided an analysis of the problem along with his invoice dated October 31, 2006. The roofer states in his report that this problem appears to be systemic and will likely be found throughout the project. The builder is immediately notified but refuses to respond. Finally, in November, 2011, the association hires an attorney and files suit against the builder for the defects in the roof. What result?

Under the provisions of Title 7, Section 896, the roof component is not the subject of a special, shorter period of repose; so the limitation on the right to file an action is ten years from the date of "substantial completion" (undefined) or the recording of a Notice of Completion, whichever is later, meaning the association would otherwise have an outside limit—until September, 2014—to bring a claim vs. the builder. However, since the association is suing for damage to property, its claim may be barred by the provisions of the statute that applies the rule of Discovery—CCP 338, which provides that claims for property damage must be brought within three years from the date the association discovered the defect and its cause, negligence by the builder—to the association's claim. A Breach of Contract claim, which must be brought within 4 years of the date of breach, presumably when the roofs were installed, or at best, 4 years from the date the builder denied the claim, would also be barred. So notwithstanding that the association's claim was filed within the 10-year statute of repose, it failed to bring its action within the shorter period triggered by its "discovery" of the problem.

Example 2: Change the facts in Example 1 to read that the association "discovers" the damage and its claim against the builder on October 31, 2012. It files its action on April 1, 2015, well within the three-year "discovery" period. What result? The claim is barred since the association failed to adhere to the 10-year outside limit on actions.

Contractual Limitations on Actions

All of the above limitations on actions are of the statutory variety. That is, they have been adopted by the Legislature and appear in the California Codes. There are other periods of limitation that can also affect an association's right to sue—private agreements contained in contracts that are unaffected by Title 7. These are rarely an issue in the typical construction defect case, but they do exist. They can appear in sales agreements, management documents, or other agreements between the community association or individual owners, on the one hand, and the developer/builder on the other. The most common contractual limitation on actions is found in the surety bonds posted by developers to satisfy the requirements of the California Department of Real Estate. These can be Common Area Completion bonds; Assessment Payment bonds; or bonds to secure the developer's performance in some other way. Bonds of this type are deposited with the DRE and serve as a guarantee that the developer will complete the project and will pay all of the assessments to the association that it is obligated to pay under the law.

These surety bonds usually prescribe a period of time by which a potential claimant must sue to enforce the bond. These periods vary, but usually are two years from the date of the completion of the various improvements specified in the bond form. Since a bond of this type is just a guarantee of performance and not an insurance policy, it is usually not considered a source of recovery for an association's construction defect claims. Consequently, they are rarely called upon. This is especially true since, by the time the average association becomes aware of defects in its project, the normal two-year contractual limitation on the right to enforce the bond has expired.

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6. There is an ongoing debate among attorneys as to whether the general statutory limits on actions that are based on the "discovery" of a claim apply to actions brought under Title 7 of the California Civil Code. Some would argue that they do not, since the statute states that an action based on its provisions is "exclusive" and hence the limitation periods to be applied are only those that appear in its provisions. Others argue that all of the limitation periods in the statute are outside limits only, and that the claim is still subject to other statutory limitations in the Code of Civil Procedure, which may be shorter in duration. Where there is such ambiguity, we advise a client to adhere to and plan for the shortest period of limitation.

7. It is unclear whether other legal theories, such as strict liability or negligence, may be pled separately in an action involving a project that falls under Title 7.

Methods of Avoiding the Expiration of Limitation Periods

Limitation periods on the right to bring an action, even the new, shorter periods imposed by Title 7, can be suspended or "tolled," but early detection of any actionable problems is necessary and advisable. The right to bring an action can be protected from the lapse of a limitation period by filing an action; voluntary agreements; or the use of statutory tolling, but advance knowledge of construction problems insures that the association has time to use them.

Conduct an Early Inspection

New associations, those less than a year or two old, should consider conducting a comprehensive investigation of all components that have been the subject of either repairs or owner complaints and, in general, to ascertain the condition of all building components and the extent of any defects. This is especially true for those components that, under Title 7, have been assigned shorter periods of limitation.[8] This will give the association adequate time to evaluate its position before being compelled to do so by some limitation on the association's right to bring a claim. Such an inspection could be an extension of the reserve study that all associations have to conduct every three years. Reserve studies are typically limited to components that have a recognized "service life."[9] The inspection we recommend would include other components as well, with some spot testing of all components to give the board information on their condition. The bulk of this inspection can be conducted before the association is three years old. The inspection of some components, however, including acoustics, irrigation, drainage, landscaping and untreated wood, should occur in the association's first year to avoid the one and two-year limitation on claims relating to those components. The association, with legal counsel's help, should also calendar deadlines for decisions relative to tolling the limitations periods for claims on any other components by one of the methods discussed below.

Suspending the Limitation Periods

There are various ways to suspend the running of the various limitations on actions, including the following:

Reach an Agreement. Tolling agreements can be used to suspend a period the running of the statutes of limitation. These are usually entered into by the association and the developer, and specify a period of time during which both agree that the statute of limitations will be suspended. This is useful in small matters where it is clear that no one but the developer/builder will be involved. But in a typical construction case, numerous parties are usually involved which requires that all potential parties (including some that may not yet be identified) agree to the tolling or it will not be effective as to any non-signing party. Since unanimous agreement is usually unlikely, contractual tolling agreements in large construction cases are unusual.

Use Statutory Tolling. Under the old "Calderon" statute (CC1375) and pursuant to the provisions of the new statute (CC910) the applicable statutes are tolled by serving a document entitled: "Notice of Commencement of Legal Proceedings." This document, when served, "…shall toll all applicable statutes of limitation and repose, whether contractual or statutory, by and against all potentially responsible parties…" This method remains the most efficient way to "buy time" in order to do further investigations or begin negotiations before an action must be filed.

File an Action. The most direct way of avoiding the loss of rights to a limitation on actions (contractual or statutory) is to file an action prior to the lapse of all applicable time periods. In the two illustrations this was not done, and the statute of limitations "ran" (expired) before the action was filed. The filing of a court action is the most certain way to avoid the loss of legal rights to statutes of limitation. If it has not already expired, any limitation period that relates to the matters alleged in the complaint is suspended upon filing.

Title 7 of the Civil Code has imposed an additional overlay of rules that give new meaning to the phrase, "A trap for the unwary." No longer can we wait until a problem is "discovered" or ten years from the completion of the project—the standard that was universal just a couple of years ago. New projects are governed by more complex rules on construction defect recoveries and the association that waits for a component to fail before investigating its physical plant could very well forfeit substantial legal rights.

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8. To obtain a chart of building components, standards, and limitations on the right to sue for each covered building component, contact the author at tberding@berding-weil.com.

9. Generally, these components appear in the regulations of the California Department of Real Estate and are included in the pro forma reserve budget submitted by the developer as part of its application for a Final Public Report.

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