

Real Construction Problems: Real Solutions

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CASE STUDIES¹

I. CASE STUDY #1 – COLLAPSED BUILDING.

A. Relevant Facts.

1. Cost of the facility approximately \$1,000,000.
2. One-Page Purchase Order (with no warranty disclaimers).
3. Buyer and Seller are commercial entities.
4. Structure is for business purposes.
5. Seller said product would meet Buyer's needs *and represented product could perform for its intended use which was discussed prior to purchase.*²
6. The seller is in the business of constructing these types of structures, *the buyer is in manufacturing business.*
7. *Within three months of construction partial failure begins, and within six months there is total collapse making the structure unusable.*
8. Collapse of building resulted in substantial business interruption and consequential damages far exceeding the cost of the structure itself.

B. Point - Counterpoint. *I will move through the columns of the Summary Guide, first as the Plaintiff and then as the Defendant for each of the case studies.*

1. Plaintiff's Claims.
 - (a) Breach of Contract.
 - (i) Nature of the Claim.
 - (ii) Elements. *Elements seem to be satisfied for a claim.*
 - (iii) Damages. *Plaintiff is entitled to damages to place it in the same position it would have enjoyed had the contract been fully performed through either the cost of reconstruction in accordance with the contract or the difference in value of the building as constructed with the value as actually built. Damages cannot be unreasonable.*

¹ This outline relies heavily on a presentation made at the 2003 Real Estate Institute entitled "Bless This Mess Sorting Out Construction Claims" presented with my partner, Tim Hassett.

² Text in italics represents editorial comments not contained in the Powerpoint presentation.

- (iv) Statute of Limitations. *Not a problem here. Two years from discovery of the breach, so not applicable here because the problem occurred almost immediately after construction.*
- (v) Potential Defenses. *Will be addressed by the Defendant.*
- (vi) CONCLUSION? **YES. PUT IT IN THE COMPLAINT.**

(b) Negligence.

- (i) Nature of the Claim. *Plaintiff alleges that the builder breached the duty of care. There has been a common misconception through the reading of the Lesmeister v. Dilly case that the presence of a construction breach of contract claim precludes a negligence claim. This is wrong. Both can be asserted.*
- (ii) Elements. *A builder has a duty independent of the building contract itself to construct in a reasonably good and workmanlike manner.*
- (iii) Damages. *Generally under negligence theory, the measure of damages is either the cost of reconstruction in accordance with the contract, or the difference between the value of the building as contracted for and as actually built.*

However, as will be discussed from the Defendant's perspective, the Economic Loss Doctrine as adopted in Minn. Stat. § 604.101 limits a Plaintiff's tort recovery.

- (iv) Statute of Limitations. *Claim must be brought within two years of discovery of the breach, and in any event, within ten years of substantial completion of construction (the Statute of Repose). Not applicable in this case because the problem occurred almost immediately.*
- (v) CONCLUSION? **YES, BUT DAMAGE RECOVERY MAY BE MORE LIMITED AS A TORT**

(c) Misrepresentation.

- (i) Nature of the Claim. *Here, the owner is arguing the builder made specific misrepresentations concerning the*

ability of the building to perform, when the builder knew or reasonably should have known the building would fail.

(ii) *Elements. The Defendant will discuss these elements in greater detail, but suffice the Plaintiff can initially satisfy the claims by demonstrating specific representations made concerning performance which at least create a question of whether they were false.*

(iii) *Damages. The measure of damages is the difference in value between the actual value of the property with the misrepresented condition and the price paid for it, together with other damages which naturally and proximately are caused by the misrepresentation.*

Here again, as Defendant will discuss, damages can be limited by the Economic Loss Doctrine for negligent misrepresentations.

(iv) *Statute of Limitations. The statute of limitations for fraud and misrepresentation is six years and does not begin to accrue until discovery of the misrepresentation. Here again, the claim was brought promptly.*

(v) **CONCLUSION? YES.**

(d) Uniform Commercial Code.

(i) *Nature of the Claim. The owner is bringing a claim against the builder arguing that the product, in this case the building itself, was sold in violation of the Uniform Commercial Code claim.*

(ii) *Elements. The primary question is whether the construction of the building is a “good” and thus covered under the Uniform Commercial Code or a “service.” Minnesota uses the “predominant factor” test to determine whether it is a good or service. In this case, the construction of a specific building which is marketed for commercial purposes would likely result in the building being considered a “good” under the Uniform Commercial Code.*

Moreover, the legislature has adopted the economic loss doctrine in Minn. Stat. § 604.101, which has blurred the distinction between goods and services and limited tort

based claims by funneling lawsuits to the UCC and common law breach of contract.

(iii) Damages. *The measure for damages under the Uniform Commercial Code is the difference between the value of the goods accepted and the value they would have had if they had performed as warranted.*

(iv) CONCLUSION? **YES.**

(e) Statutory Warranties For New Homes and Improvements Under Chapter 327A.

(i) NO.

(f) Express and Implied Statutory Warranties for Common Interest Communities Under Chapter 515B.

(i) NO.

2. Defendant's Defenses. *I am only repeating those sections which are relevant to the defenses. I will not bother to repeat all of the individual items repeated by the Plaintiff in the interest of focusing on the relevant issues. Once again, stepping through the Summary Guide, one column at a time, we come to the relevant sections for the Defendant's analysis of the case.*

(a) Breach of Contract.

(i) Statute of Limitations. *This is a dead-end issue for the Defendant because the claim was brought promptly.*

(ii) Defenses.

(1) Contract Limitations. *Carefully analyze the language itself. Any limitations clauses? Is the Plaintiff trying to impose terms that do not exist?*

(2) Owner Supplied Plans & Specs. *Who supplied the specs? If the Plaintiff did, its claim may be limited. An owner is responsible to the extent the defects are the result of the owner's faulty specifications.*

(3) Owner Interference. *Did the owner interfere with the construction sufficient to explain the collapse?*

- (4) Doctrine of Substantial Performance. *Likely inapplicable here because the project was completed and then it collapsed. However, if an owner refuses to pay, even though the project was "substantially completed," that can be a defense to a claim by a Plaintiff.*
- (5) Acceptance of Defects. *Inapplicable here, unless there is some evidence in discovery that the Plaintiff was aware of the defects when construction was completed and the Plaintiff accepted the defects without objection.*
- (6) Doctrine of Impossibility. *Inapplicable here. That would apply where the contractor is excused because of unanticipated problems. Here the building was completed.*
- (7) Failure to Mitigate. *Did any actions of the Plaintiff contribute to the damages? In this case, did the Plaintiff continue to use the structure when it began to fail, thus aggravating the condition? If so, the Plaintiff's may be barred or limited. OR Once the failure began to occur, did the Plaintiff fail to act in a manner which could have limited the damages suffered by the Plaintiff?*
- (8) Spoliation of Evidence. *Did the Plaintiff destroy evidence which is relevant? If a party spoils evidence which could have been relevant in the case, generally the courts will construe the spoiled evidence against the party who destroyed the evidence.*

(b) Negligence.

- (i) Damages. *The Plaintiff is seeking substantial damages far exceeding the cost of the original structure itself. Specifically, when it is not possible to restore the building, the owner is entitled to the remaining diminution in value of the building, so long as the total damages awarded do not exceed the difference in value before and after or the costs of restoring the building to substantially its former condition, whichever is less. Other damages which are a direct and proximate result to their injury are recoverable. However, there is a reasonableness limitation.*

Most significantly, the buyer's ability to bring a negligence or tort claim is limited by the economic loss doctrine embodied in Minn. Stat. § 604.101, which bars a buyer's claim against a seller for compensatory damages for sale of goods, unless those goods damage other personal property. Here, the economic loss doctrine permits recovery for damage to real or personal property. As to the goods themselves (the collapsed building), there is no common law recovery in tort. Must look to contract or UCC themselves.

(ii) Statute of Limitations. *Once again, this is a dead-end.*

(iii) Defenses.

(1) Economic Loss Doctrine. *We have just discussed how the Economic Loss Doctrine can limit severely a Plaintiff's ability to recover for a tort-based claim.*

Additionally, the UCC is the exclusive remedy where both the buyer and seller are merchants of a good in the kind which is the subject matter of the dispute. Not relevant here because Buyer is not a "merchant" in the good purchased.

(c) Misrepresentation.

(i) Elements. *There are many elements to maintain a misrepresentation claim. A good defense should attack as many of these elements as possible. Failure of a Plaintiff to sustain all of the elements is fatal to the claim.*

For example, the defendant may deny that the specific representations were made.

The Defendant can also assert that the Plaintiff does not reasonably rely on the representations, thus undermining the elements of the Plaintiff's claim.

(ii) Damages. *Unique damage rule, which could hurt the Plaintiff.*

(iii) Statute of Limitations. *Inapplicable*

(iv) Defenses.

- (1) Failure to Plead Fraud with Particularity. *This is a pleading issue often overlooked by Plaintiffs. Minnesota Rule of Civil Procedure 9.02 requires that the specific what, where and who be specified for any claims of fraud. Generalized representations can result in the Plaintiff's claims being dismissed.*
- (2) Plaintiff's Claims Relate to Future Performance. *This is an interesting defense to fraud claims. A misrepresentation must involve a past or present representation of facts. The false statement cannot relate to future predictions or contingencies.*

Therefore, a defense which can be asserted by Defendant is that promises concerning how a product will perform is a "future" representation and therefore not actionable as a fraud claim. While this seems both counterintuitive and ridiculous, some courts have actually agreed and dismissed misrepresentation claims because they involve future predictions.

Obviously, the way to respond to such arguments is that while the performance of the product may relate to an action in the future, there is a current promise regarding its characteristics which is not a future prediction, rather a current statement of its functional capacities, and therefore is actionable. In any event, this is a good defense for a defendant to argue because it "muddies the waters."

- (3) Economic Loss Doctrine. *The Economic Loss Doctrine does limit damage recovery for merely "negligent" misrepresentations. However, if the misrepresentation is intentional or reckless as it relates to the goods sold, the buyer is not limited by the Economic Loss Doctrine.*
- (v) Additional Comment Consumer Fraud. *In virtually every consumer or construction misrepresentation claim, a plaintiff always included a consumer fraud allegation under Minn. Stat. § 325F.69, because it also permitted attorneys' fees under Minn. Stat. § 8.31. However, since the Ly v. Nystrom decision, such claims have been severely restricted and are routinely dismissed by district*

courts. That is, for a plaintiff to maintain a claim, it must demonstrate more than there is a specific representation to the harmed plaintiff, but also a generalized misrepresentation to the public which can result in harm. Courts are following the Supreme Court's lead in Ly and happily dismissing consumer fraud based on misrepresentation claims. This is taking away the "hammer" of attorneys' fees which plaintiffs were using to great effect.

(d) Uniform Commercial Code.

- (i) Elements. *The Defendant may attempt to argue that the Uniform Commercial Code does not apply, because the transaction is a "services" as opposed to a "goods" hybrid analysis.*
- (ii) Damages. *Because of the Economic Loss Doctrine Statutes Minn. Stat. § 604.101, the recovery by plaintiffs under tort-based theories have been substantially diminished, and the type of recoveries have also been shunted to contract and UCC based claims.*
- (iii) Statute of Limitations. *Inapplicable.*
- (iv) Defenses.
 - (1) Predominant factor test. *See my discussion above regarding whether it is a "good or service."*

C. Conclusion Point - Counterpoint. *There are plenty of theories for recovery, defenses and interesting facts as presented by skilled lawyers that will determine the outcome.*

II. CASE STUDY #2 - RESIDENTIAL WET BASEMENT

A. Relevant Facts

1. Residential home completed in December 2002.
2. Homeowner hired another contractor to landscape and construct patio and retaining wall.
3. Exterior landscaping and grading completed in Spring 2003.
4. Leaks in the house began to occur in Summer 2003.

5. No leaks in the surrounding homes.
6. In September 2003, Homeowner provides written notice of leaks and commenced the lawsuit.

B. Point – Counterpoint.

1. Plaintiff's Claims.

(a) Breach of Contract.

- (i) Elements. *Clearly parties do not intend there to be a leak.*
- (ii) Damages. *Same analysis as our discussion above with respect to other breach claims.*
- (iii) Statute of Limitations. *Lawsuit was timely.*
- (iv) CONCLUSION? **YES.**

(b) Negligence.

- (i) Elements. *Res Ipsa Loquitur. In the absence of negligence, houses don't leak, especially when surrounding homes show no signs of leakage.*
- (ii) Damages. *Same analysis as our discussion above with respect to other breach claims.*
- (iii) Statute of Limitations. *Lawsuit was timely.*
- (iv) CONCLUSION? **YES.**

(c) Misrepresentation.

- (i) Elements. *Plaintiff can identify no specific representations by builder concerning the water tight nature of the home. In the absence of a specific representation, Plaintiff is not asserting a claim.*
- (ii) CONCLUSION? **NO.**

(d) Uniform Commercial Code.

- (i) Elements. *Hybrid test. No Minnesota case has directly ruled on whether a residential home is subject to the*

Uniform Commercial Code. There are good arguments both ways.

- (ii) Damages. *See discussion above regarding damages under the Uniform Commercial Code. The Economic Loss Doctrine will apply if the sale of the home is found to be a “good.” If the home is found to be a “good” then the statutorily imposed warranties will apply under the Uniform Commercial Code (e.g. applied warranty of merchantability and implied warranty of fitness for a particular purpose). By the same token, if the Economic Loss Doctrine Applies, damages for tort-based claims will be severely limited.*

On the other hand, if the product is found to be a “service” and not a “good” then there will not be a limitation of damages under the Economic Loss Doctrine and the Uniform Commercial Code will be inapplicable as well.

- (iii) Statute of Limitations. *Lawsuit was timely.*

- (iv) CONCLUSION? **YES.**

(e) Statutory Warranties for New Homes under Chapter 327A.

- (i) Elements. *Plaintiff is asserting a claim for defective construction resulting in the leak in the basement. Such a defect shortly after construction would appear to be covered under the statute.*

- (ii) Damages. *The purchaser can choose between specific performance or damages. Damages are limited to the amount necessary to repair the defect or the difference in value of the dwelling as promised and as exists with the defect.*

- (iii) Statute of Limitations. *Lawsuit was timely.*

- (iv) CONCLUSION? **YES.**

(f) Statutory Warranties for Home Improvements under Chapter 327A.

- (i) Elements. *Plaintiff is asserting a claim relating to the initial construction and not subsequent improvements. Therefore, the Plaintiff is not asserting a claim under Minn. Stat. § 327A for improvements.*

- (ii) CONCLUSION? **NO**.
- (g) Express and Implied Statutory Warranties for Common Interest Communities Under Chapter 515B.
 - (i) Elements. *This is not a project involving common interest communities. Therefore claims for express and implied warranties under Minn. Stat. § 515B are inapplicable.*
 - (ii) CONCLUSION? **NO**.

2. Defendant's Defenses

- (a) NEW FACT. Once sued by Plaintiff, Defendant reviews the site and discovers that the cause of the leak is exterior landscaping and retaining walls which were installed by Plaintiff and are directing water toward the home.
- (b) Breach of Contract.
 - (i) Elements. *No causation/no breach.*
- (c) Negligence.
 - (i) Elements. *Defendant had no duty to perform exterior landscaping and Plaintiff caused the problem not Defendant's work.*
 - (ii) Economic Loss Doctrine. *Again, even if the Plaintiff is able to maintain its claim, its damages are limited by the Economic Loss Doctrine.*
- (d) Uniform Commercial Code.
 - (i) Potential Defenses.
 - (1) Not a Sale of Goods.
 - (2) No Breach of Warranty. *No breach of the implied or express warranties of the Uniform Commercial Code because Defendant has determined that Plaintiff's exterior landscaping caused the problem, and therefore Defendant breached no duty implied by the Uniform Commercial Code.*
- (e) Statutory Warranties for New Homes Under Chapter 327A.

- (i) *Definitional Defense. Chapter 327A does not apply to detached garages, driveways, walkways, patios, boundary walls, retaining walls and other structures which are not necessary for the structural stability of the dwelling, including landscaping fences and non-permanent construction materials. See Minn. Stat. § 327A.01, subd. 3. The exterior landscaping is not covered by the statute.*

C. Conclusion? *Homeowner will probably lose.*

III. CASE STUDY #3 - THE METROPOLITAN CENTRE (A/K/A LINCOLN CENTRE) CASE

A. Relevant Facts.

1. This is a general factual discussion of Metropolitan Life Insurance v. M.A. Mortenson Co., 545 N.W.2d 394 (Minn. App. 1996).
2. There are two different problems with this building, both related to the windows:
 - (a) Problem 1 Water Leak Beginning in 1987. Leaks were found inside the windows of the building. These leaks were continuous and never stopped prior to the commencement of the lawsuit. When the chief engineer discovered the leaks in 1987, he immediately notified the owner, who in turn notified the general contractor.
 - (i) In 1988 payment was withheld to Mortenson and a report was prepared concluding condensation was the cause.
 - (ii) In 1991, another report was prepared, again concluding condensation.
 - (iii) In 1992, another report was prepared, concluding that there was a defect in the vapor barrier.
 - (iv) In April 1994, the owner commenced a lawsuit.
 - (b) Problem 2 The spandrel defect.
 - (i) Window Washer early 1990. *The building's spandrel were designed to be opaque. In early 1990, a window washing crew informed the owner that the windows were beginning to delaminate.*

- (ii) Owner Requests Manufacturer Replace all Windows in 1992. *The owner hired a consultant who recommended that all of the windows needed to be replaced. The owner notified the window manufacturer in March 1992 regarding the problem.*
- (iii) Manufacturer Denies Claim. *The manufacturer initially denied the problem and then refused to repair the problem.*
- (iv) Lawsuit is commenced in April 1994.

B. Point - Counterpoint.

1. Plaintiff's Claims.

(a) Breach of Contract.

(i) Elements. *Both the leaking windows and spandrel constitute a breach of the parties' intent and appears actionable.*

(ii) Statute of Limitations.

(1) Leaks. *There were continuous leaks from 1987 until the commencement of the lawsuit in April 1994, but the Plaintiff did not know the true cause of the leak until April 1992. Once the owner was aware of the cause of the leak, it did commence the lawsuit within two years.*

(2) Spandrel. *The window manufacturer did refuse to fix the problem within two years of commencement of the lawsuit; however, the window sales contract included an express 10 year statute of limitations. The Plaintiff can argue that the 10 year statute of limitations applies.*

(iii) CONCLUSION? **YES (BUT NOW KNOW WRONG)**
Plaintiff brings claim (you will see that under the Mortenson case, Plaintiff now will commit Rule 11 if it brings the case).

(b) Negligence. The Court did not analyze the case from a negligence perspective

- (i) Elements. *Again, elements appear to be satisfied because the windows were negligently constructed.*
- (ii) Statute of Limitations. *Same analysis as breach of contract applies (although the court did not analyze claims from a negligence perspective).*
- (iii) CONCLUSION? **YES (BUT NOW KNOW WRONG)**
Plaintiff brings claim (you will see that under the Mortenson case, Plaintiff now will commit Rule 11 if it brings the case).
- (c) Misrepresentation. *Inapplicable.*
- (d) Uniform Commercial Code.
 - (i) *Statute of Limitations. Claims are barred because actions must be brought within four years of delivery*
- (e) Statutory Warranties for New Homes and Improvements under Chapter 327A. *Inapplicable.*
- (f) Express and Implied Statutory Warranties for Common Interest Communities Under Chapter 515B. *Inapplicable.*

2. Defendant's Defenses.

- (a) Defendant prevailed on dismissing Plaintiff's claims on statute of limitations.
 - (i) Is the spandrel problem a "defective and unsafe" condition under the statute? *The Plaintiff tried to argue that because it is a mere cosmetic issue, the statute does not apply. The Court rejected this argument, concluding that the reflective nature of the windows provides privacy and limits light. Therefore the statute of limitations revision requiring a "defective" or unsafe condition still triggered the statute of limitations.*
 - (ii) Does the two year statute of limitations apply when the warranty period has not expired? *There was a 10-year warranty on the windows contained in the manufacturer's contract. The Plaintiff argued that the 10-year warranty, and not the 2-year warranty contained in the statute should apply.*

The Court concluded that the manufacturer specifically refused to repair the work and denied the claim. Because the Plaintiff failed to commence the action within two years, all claims were barred.

Effectively, the Defendant's refusal to repair the problem constituted notice to the Plaintiff of a breach requiring it to act to satisfy both the two year statute and the 10-year warranty. The Plaintiff's failure to commence an action within two years barred both the claims under the statute and under the express warranty.

IV. CASE STUDY #4 - MOLD IN A COMMON INTEREST COMMUNITY

A. Relevant Facts.

1. The CIC townhome community was completed in July 1991.
2. Builder/Declarant written statement in promotional material said: "These are the best built homes in the state. . .We have been building for twenty years and have never had a leak you will not have a leak either!"
3. The exterior of the townhomes is stucco.
4. A group of townhomes began to have problems with leaks in February 1992.
5. The Builder/Declarant was notified by telephone and it promptly came and repaired the leak.
6. Every other year, from 1992 through 2001, a leak would be discovered in middle of winter and was repaired. The Builder/Declarant would come and repair the problem, engaging in increasingly elaborate repairs (including substantial improvements to the property at the Builder/Declarant's expense), and each time telling the homeowner and the Association management that the problem had been fixed.
7. The Builder/Declarant told the homeowners and the management of the CIC that the leak had been repaired.
8. One disgruntled homeowner then contacted an outside service. Outside service to come and examine the problem and discovered huge mold problems which caused structural damage.
9. Written notice February 2001. The homeowners, through the Association, provided written notice to the Builder/Declarant within six

months of the discovery of the mold in February 2001. The cost of repairing to the leaks was many thousands of dollars.

10. The Builder/Declarant refused to make the repairs in March 2001.
11. The insurance company has denied the Association's claim for coverage based on a mold exclusion.
12. A lawsuit was commenced in June 2001.

B. Point - Counterpoint.

1. Plaintiff's Claims.

(a) Breach of Contract.

- (i) Nature of Claim. *For purposes of analysis, this assumes that the Declaration for the Association provides that the Association, as opposed to the individual unit owners, is responsible for the repairs of the leaks. It further assumes that the Association hired the builder and was responsible for all coordinating the repairs. It is, therefore, the Association, and not the individual unit owners, that would have standing to bring claims against the Builder/Declarant.*
- (ii) Elements. *The Plaintiff entered into the contract with the Defendant Builder/Declarant. The Builder/Declarant breached the contract through its negligence during initial work and repairs.*
- (iii) Damages. *The standard for breach of contract damages is the same as we discussed in our first case study.*
- (iv) Statute of Limitations. *The Plaintiff commencing this action, the Plaintiff faces significant problems with the statute of limitations. The Plaintiff must argue claims are equitable tolled by Defendant's promises or that it did not run because notice was not given of the Builder's refusal to repair until March 2001.*
- (v) CONCLUSION? **YES** *In light of new Vlahos case.*

(b) Negligence.

- (i) Nature of Claim. *All three of these issues involve the same analysis as we had in the first situation. That is, a*

duty exists, there is an apparent breach of the duty, and the damages are going to be circumscribed by the Economic Loss Doctrine.

- (ii) Statute of Limitations/Statute of Repose. *The statute of limitations requires an action be commenced within two years of the discovery of the defect.*³ *Here, a defect was discovered in February 1992. A lawsuit was not commenced until June 2001. Vlahos case says statute does not run until written notice by builder refusing to repair.*

Additionally, the Plaintiff will argue that it did not “discover” the nature of the injury until the unit owner hired an outside contractor, who revealed the full nature of the problem precipitating the notice of breach to the contractor and the commencement of the lawsuit.

- (iii) Comment – Violation of the UBC. *To the extent the work by the Defendant violated the Uniform Building Code or other governmentally prescribed construction requirements, this provides the Plaintiff with a substantial additional argument that there is a “per se” negligence by the Defendant in construction.*
- (iv) CONCLUSION? **YES.** *As discussed below, the underlying Vlahos v. R&I Construction, 676 N.W.2d 672, 2004 WL637569 (Minn. April 1, 2004),⁴ case requires a written refusal by the contractor to repair the claimed defect. In this case, no such refusal was made by the contractor until the March 2001 written notice. A lawsuit was then commenced within two years of the builder’s refusal and before the expiration of the ten year statute of repose.*

(c) Misrepresentation.

- (i) Nature of Claim/Elements. *Two potential misrepresentations: (1) As to the quality of the original work and (2) continual misrepresentations concerning the condition of the work when the repairs occurred.*

³ The absolute bar of the Statute of Repose is ten years, which is not implicated in this fact pattern.

⁴ The Court of Appeals Vlahos decision was cited in Footnote 1 in the Summary Guide to Construction Claims. The new Vlahos decision places a substantially greater burden on the builder to act to trigger the running of the statute of limitations. See attached analysis of the case – Section V.

- (ii) Statute of Limitations. *Best vehicle to avoid statute of limitation problems.*
 - (iii) Damages. *If it is mere negligent misrepresentations by the Defendant, the Economic Loss Doctrine will limit damages.*
 - (iv) CONCLUSION? **YES.**
- (d) Uniform Commercial Code.
- (i) Nature of Claim/Elements. *Hybrid test. Does the construction of the townhomes and the subsequent repair constitute a “good” or a “service?” Because this work was completed long before the new Economic Loss Doctrine statute (Minn. Stat. § 604.101), we are subject to the old economic loss doctrine statute of Minn. Stat. § 604.10 which focuses on the nature of the transaction and the predominant factor.*
 - (ii) Damages. *Because this transaction occurred prior to August 2000, the Economic Loss Doctrine, as articulated under the old statute (Minn. Stat. § 604.10), provides that a party in a commercial transaction cannot pursue a negligence cause of action if the damage sought resulted from damages to the goods at issue. However, a party was able to pursue a negligence action in non-commercial transactions, or any other transactions involving damage to other personal property or personal injuries.*

In this case, the test would be whether the townhomes constructed constitute a “commercial transaction” subjecting the parties to the limitation of the Economic Loss Doctrine. Conversely, if it was determined that it is not a “commercial transaction,” then the Association is not subject to the limitations of the Economic Loss Doctrine and may maintain a negligence-based claim.
 - (iii) Statute of Limitations. *The Uniform Commercial Code contains a harsh statute of limitations provision. That is, it provides that the statute of limitations is four years from the delivery of the goods (although the parties may lower that statute of limitations to one year). In this case, the goods were delivered over 10 years ago. Even in the presence of fraud, it will be difficult to maintain a claim under the strict requirements of the Uniform Commercial Code. Perhaps the only argument which may also be*

asserted is that that new and subsequent repair constituted new “improvements” which become the new controlling date for the claims for breach of that subsequent work.

- (iv) **CONCLUSION? NO.** *The vulnerability of the statute of limitations, especially given the requirement under the Uniform Commercial Code that the triggering date is the date of delivery, as opposed to the discovery of the breach. Hence, a claim under the Uniform Commercial Code is more vulnerable than some of the other causes of action. By asserting a Uniform Commercial Code action, in the face of the other claims, its weakness would likely undermine the viability of the other claims and it is best not asserted, because it is already weak.*

- (e) **Statutory Warranties for New Homes under Chapter 327A .**
 - (i) **Nature of Claim.** *Despite the fact that this is a townhome, the Plaintiff still has rights to claims under Chapter 327A.*

 - (ii) **Elements.** *There are both structural (rotting of supporting members) and general warranty defects of faulty construction could support a violation of the statute.*

 - (iii) **Damages.** *For violation of the statute a buyer can choose between a cause of action for damages or specific performance. Damages are limited to the amount of money necessary to repair the defect, or the difference between the value of the dwelling without the defect and the value of the dwelling with the defect. The fact that the Builder is now out of business may still permit the Association to recover up to \$50,000 under the recovery fund administered by the Department of Commerce.*

 - (iv) **Statute of Limitations.** *Even in the absence of the recent underlying Vlahos decision, there is a strong case for equitably tolling the statute of limitations. See Rhee. While the statute provides that a claim must be commenced within two years of discovery of the breach, if the builder provides repeated assurances that a claim has been repaired, courts have found that there is at least a fact question sufficient to avoid summary judgment and to permit the case to go to the trier of fact whether the statute of limitations should be equitably tolled and the Plaintiff can proceed with its claim.*

- (v) CONCLUSION? **YES.**
- (f) Statutory Warranties for Home Improvements Under Chapter 327A.
- (i) Nature of Claim. *Minn. Stat. § 327A applies to both the construction of dwellings themselves and also to subsequent repairs. If there is a new “improvement” the statute of limitations runs from that improvement.*
 - (ii) Statute of Limitations. *Once again, the question is whether the assurances by the builder that the “improvements” solved the problem should equitably toll the statute of limitations, or whether a reasonable buyer, in that situation should have known that the problem was not fixed and written notice of a violation should have been provided and a lawsuit should have been commenced.*
 - (iii) CONCLUSION? **YES.** *An action should be brought to the extent the “improvements” in addition to the underlying work were defectively performed supporting a cause of action for breach of improvements under Minn. Stat. § 327A.*
- (g) Express Statutory Warranties for Common Interest Communities Under Minnesota Chapter 515B.
- (i) Nature of the Claim. *An action can be brought by the owner of a common interest community based on express warranties made by the Declarant/Builder to the Association.*
 - (ii) Elements. *If a statement is made by the Declarant/Builder, it is actionable if it is more than a mere opinion and it must be a statement on which the Association can reasonably rely. Here the builder told the Association members that you can rely on the fact that “you will not have a leak either!”*
 - (iii) Damages. *Remedies are liberally administered to benefit the injured party, but consequential, special and punitive damages are generally not available. The court may award reasonable attorneys fees.*
 - (iv) Statute of Limitations. *A cause of action must be commenced within six years after the cause of action*

accrues, although the parties may reduce the accrual period to two years. A cause of action accrues at the earlier time of the conveyance of the unit or the time the purchaser enters into possession. If the warranty extends to future performance, the cause of action accrues at the time the breach is discovered or at the end of the period in which the warranty explicitly states it extends.

In this situation, it was an express warranty as to future performance, and the question will, again, be when the Association reasonably discovered the breach. Once again, the issue will turn on whether the discovery of the breach should be equitably tolled based on the builder's assurances or it can be it did not accrue until a written refusal was made under Vlahos. .

(v) CONCLUSION? **YES.**

(h) Implied Statutory Warranties for Common Interest Communities Under Minnesota Chapter 515B.

(i) Nature of the Claim. *A unit owner can also bring an action for implied warranties relating to the sale of a CIC.*

(ii) Elements. *A warranty is implied in a CIC sale that the unit is in at least as good of a condition at the time of conveyance as at the time of contracting, and that the unit would be suitable for the ordinary uses of real estate of its type and that it would be free from defective materials and would be constructed in a workmanlike manner, and that the unit would be available for residential purposes and comply with applicable law at the time of delivery. In this case, the Plaintiff can argue there was a breach of implied warranty, because the unit was not constructed in a workmanlike condition, and not suitable for its intended residential purpose because of its extensive leaking.*

(iii) Damages. *Damages are the same standard as for express warranties.*

(iv) Statute of Limitations. *The statute of limitations is the same standard as express warranties.*

(v) CONCLUSION? **YES.**

2. Defendant's Defenses.

(a) Breach of Contract.

- (i) Statute of Limitations. *The main argument will be that there is no basis to toll the statute of limitations. A reasonable person should have known that a breach occurred and their failure to commence an action within two years as required under the statute prevents them from asserting their claim. In particular, the statute requires an action to be commenced upon exercise of due diligence. Their failure to engage in an investigation, in the face of these continuing problems, prevents them from asserting their claim. Additionally, the case law has held that it is not a matter of knowing the entire defect, but rather having a general idea that a problem exists. See Pamida Inc. v. Christenson.*

This was the predominant argument until April 1, 2004. The Vlahos decision makes an argument that the statute begins to run, in the absence of a written refusal by the builder, much more difficult.

(ii) Potential Defenses.

- (1) Contractual Limitations. *Hopefully, Defendant has carefully drafted contract and sale documents.*
- (2) Owner Supplied Plans & Specs. *Inapplicable.*
- (3) Owner Interference. *Likely inapplicable in a CIC.*
- (4) Substantial Completion. *Inapplicable.*
- (5) Acceptance of Defects. *Inapplicable in a CIC.*
- (6) Doctrine of Impossibility. *Inapplicable.*
- (7) Failure to Mitigate. *Inapplicable given the frequent calls to Builder/Declarant.*
- (8) Spoliation of Evidence. *Did the investigators engage in any spoliation of evidence? What is the impact of the repeated substantial repairs on evidence of a construction defect?*

(b) Negligence.

- (i) Statute of Limitations. *The Vlahos does not specifically address the issue of whether the statute of limitations begins to run in a negligence claim or a claim under 327A. Nevertheless, in the absence of the statute of repose being triggered, there can be a strong argument that the Vlahos case also extends to negligence-based claims for defects. The awareness of the defect by the homeowner (or in this case the CIC) did not occur until there was an explicit refusal by the Builder to repair the defect. In this case, the builder can attempt to argue (consistent with Pamida discussed above) that the Association was on notice of the defect and should have commenced the claim, that prior written notice was provided in some manner, or that the Vlahos case should not be extended to either negligence or CIC claims. Given the Supreme Court's pronouncement in Vlahos, all such arguments are difficult to sustain.*
- (ii) Potential Defenses.
- (1) Economic Loss Doctrine. *As discussed extensively above, a Plaintiff's damages for negligence are severely limited under the Economic Loss Doctrine which was in effect prior to August 2000. That is, if the transaction was found to be a "commercial transaction" then damages cannot be recovered for the goods at issue and only limited damages including those to other tangible personal property. Conversely, if the case is found to be a matter which is not a "commercial transaction" then the Association will be free to proceed with a common law negligence claim without such limitations.*
- (2) UCC Exclusive Remedy. *Inapplicable.*
- (3) Spoliation of Evidence. *Discussed above.*
- (4) Failure to Mitigate. *Discussed above.*
- (iii) Comment. *If the initial construction was contrary to the Uniform Building Code, or other governmental requirements, it provides the Plaintiff with a strong argument of a per se evidence of negligence. The best defense a defendant has in light of a violation of the*

Uniform Building Code, would be to focus on the Economic Loss Doctrine to limit damages and the statute of limitations to avoid the claim in total.

(c) Misrepresentation.

- (i) Elements. *Challenge the specific elements of the misrepresentation. What representations were made? When they were made? Was reliance reasonable? In this situation, the defense is often that, in the face of these repeated problems, the owner should have known better and should not have reasonably relied.*
- (ii) Statute of Limitations. *Once again, the best defense the Defendant has is to argue that the Plaintiff's continued reliance on the assurances that the problem had been repaired were not "reasonable." The hard part about such an argument is that, the builder is, in essence, arguing that the CIC should have known that the builder was "lying."*
- (iii) Potential Defenses.
 - (1) Failure to Plead Fraud with Particularity. *As discussed above in the first case study, the Defendant should try to force the Plaintiff to identify of the specific representations made where these alleged "assurances" were provided by the Defendant to the Plaintiff, thus justifying the tolling of the statute of limitations. If the Plaintiff cannot identify the specific instances where such assurances were made, then the grounds for equitable tolling begin to evaporate.*
 - (2) Plaintiff's Claims Relate to Future Performance. *Probably inapplicable here.*
 - (3) Failure to Mitigate. *Discussed above.*
 - (4) Spoliation of Evidence. *Discussed above.*
 - (5) Economic Loss Doctrine. *The Economic Loss Doctrine does limit damage recovery for merely "negligent" misrepresentations. However, if the misrepresentation is intentional or reckless as it relates to the goods sold, the buyer is not limited by the Economic Loss Doctrine.*

- (iv) Comment/Consumer Fraud. *As discussed above, any claim predicated on consumer fraud is likely to be dismissed under the court's increasingly broad reading of Ly v. Nystrom.*
- (d) Uniform Commercial Code. *As the Plaintiff has conceded, there are substantial statute of limitation problems with the Uniform Commercial Code given its harsh four year statute of limitations from the delivery of the product.*
- (e) Statutory Warranties for New Homes under Chapter 327A. *Again, skipping to the most relevant issue, we turn to:*
 - (i) Statute of Limitations. *The best defense to be asserted by the Defendant is that equitable tolling is not reasonable. The increasingly serious repairs required by the builder should have alerted the Association that a problem existed sufficient to prevent equitable tolling. This argument is increasingly difficult to make in light of the Vlahos decision which requires a written notice to the homeowner of the refusal to repair the defect by the builder to begin the running of the statute of limitations.*
 - (ii) Potential Defenses.
 - (1) Exclusive Remedy. *While no case has directly ruled on this issue, it is at least arguable that a case predicated upon statutory warranties under Minn. Stat. § 327A bars all other theories. See Minn. Stat. § 327A.06.*
 - (2) Definitional Defenses. *Minn. Stat. § 327A only applies to "dwellings" as defined under the statute. That is, a home which was previously occupied by someone other than the builder may bar the statutory warranties. Additionally, if the seller is not a "vendor," that is – someone in the business of constructing dwellings, the statutory warranties may be inapplicable and there are specific types of repairs (e.g. exterior work) which are not included under the statutory warranties. Unfortunately for the Defendant, none of those exclusions appear to apply in this case. The Builder is in the business of building such homes, and the dwelling was a newly-occupied structure to be used for residential uses.*

- (3) *Specific Statutory Exclusions. There is a list of fifteen specific statutory exclusions which can be used for the basis of avoiding liability. Unfortunately, again for the Defendant, they do not apply here. The statutory home improvement warranties do not cover the following: (1) loss or damage which is not reported by the owner to the contractor, in writing, within six months after the owner discovers or should have discovered the loss or damage; (2) loss or damage caused by defects in design, installation, or materials which the vendee or the owner supplied, installed, or had installed under his directions; (3) secondary loss or damage such as personal injury or property damage; (4) loss or damage from normal wear and tear; (5) loss or damage from normal shrinkage caused by drying of the swelling or the home improvement within tolerances of building standards; (6) loss or damage from dampness and condensation due to insufficient ventilation after occupancy; (7) loss or damage from negligence, improper maintenance or alteration of the dwelling or the home improvement by parties other than the vendor or the home improvement contractor; (8) loss or damage from changes in grading of the ground around the dwelling or the home improvement by the parties other than the vendor or the home improvement contractor; (9) landscaping or insect loss or damage; (10) loss or damage from failure to maintain the dwelling or the home improvement in good repair; (11) loss or damage which the vendee or the owner, whenever feasible, has not taken timely action to minimize; (12) loss or damage which occurs after the dwelling or the home improvement is no longer used primarily as a residence; (13) accidental loss or damage usually described as acts of God, including, but not limited to: fire, explosion, smoke, water, escape, windstorm, hail or lightning, falling trees, aircraft and vehicles, flood, earthquake, except when the loss or damage is caused by failure to comply with building standards; (14) loss or damage due to soil conditions where construction is done upon land owned by the vendor or the owner and obtained by him from a source independent of the vendor or the*

home improvement contractor; and (15) in the case of home improvement work, loss or damage due to defects in the existing structure and systems not caused by the home improvement. See Minn. Stat. § 327A.03(a-p).

(4) Failure to Mitigate. *Discussed above.*

(5) Spoliation of Evidence. *Discussed above.*

(f) Statutory Warranties for Home Improvements Under Chapter 327A.

(i) Elements. *Issue of whether it is an “improvement” or a “repair.” Mere repair work relates back to the original date of the work and the statute of limitations continues to run from the original date of the improvement unless there is action supporting equitable tolling (e.g. assurances by the builder). Conversely, if the builder is engaged in new and substantive “improvements” of the property, then the statute of limitations runs from the date of the improvement.*

(ii) Statute of Limitations. *One of the best defenses to a Minn. Stat. § 327A claim is that the homeowner failed to provide written notice of the defect within six months of its discovery as required under Minn. Stat. § 327A.03(a). That is, even if a homeowner has contacted the builder verbally and asked him to repair the problem, it still must provide written notice of the breach, or the claim can be barred. In this case, the Association did provide that notice, but if it had failed to do so, the Association’s claim could have been vulnerable.*

(iii) Potential Defenses. *Discussed above.*

(g) Express Statutory Warranties for Common Interest Communities under Chapter 515B.

(i) Elements. *The Association argues that an express warranty existed based on promotional materials regarding claims that leaks have never occurred in the past. The builder can attempt to argue that this is not a promise as to future performance and, most importantly, that the representations constitute mere “puffery.”*

(ii) Statute of Limitations. *Case law is untested for equitable tolling for Minn. Stat. § 515B. However, the statute is supposed to be liberally interpreted and it is likely courts would find the Vlahos decision instructive.*

(h) Implied Statutory Warranties for Common Interest Communities under Chapter 515B.

(i) Statute of Limitations. *Case law is untested for equitable tolling for Minn. Stat. § 515B. However, the statute is supposed to be liberally interpreted and it is likely courts would find the Vlahos decision instructive.*

C. Conclusion. *Prior to April 1, 2004, the Association would have had an uphill battle to support its argument for equitable tolling. The recent Vlahos decision will probably allow the statute of limitations to be tolled because of the absence of a written refusal by the builder to repair the problem.*

V. Analysis of Vlahos, et al. V. R & I Construction, et al., 676 N.W.2d 672, (Minn. April 1, 2004)

Comment [DSM1]: Numbering scheme in use: General Numbering (1) (Firm-standard scheme) Applied via Payne Numbering Assistant using Heading styles linked to outline numbering.

A. Facts. *Vlahos involved a purchase of a luxury home by Dean and Michelle Vlahos in 1999 from Roger and Carol Rovick. The Rovicks hired R & I Construction to build their home on Lake Minnetonka in 1990. From 1992 through 1999, the Rovicks experienced repeated water and moisture-related problems in the home.*

The Rovicks fully disclosed the existence of the known water problems and the Vlahoses engaged in extensive inspection of the home prior to purchase. Following the purchase of the home, the Vlahoses discovered even more extensive water problems, including water infiltration which compromised structural elements of the home.

In May 2000, the Vlahoses provided notice to R & I of the defects and demanded R & I cure. R & I and its insurer inspected the property and refused. Vlahoses commenced an action under the ten year “structural” provision under 327A.02.

R & I successfully moved for summary judgment which held that the Rovicks were aware of the defects between 1992 and 1999, any claim was barred by the two year statute of limitations. The Court of Appeals affirmed. The Supreme Court reversed the District Court and Court of Appeals and remanded the case.

B. Summary of Supreme Court Opinion. *In reversing and remanding the case, the Supreme Court held that the lower courts had incorrectly applied the statute of limitations (Minn. Stat. § 541.051) and misdefined the scope of the structural warranty under 327A.02, subd. 1(c).*

1. Statute of Limitations. *The Supreme Court applied Minn. Stat. § 541.051, subd. 4 in determining when the statute of limitations for violation of 327A.02 begins to run. The Court held these provisions require an action “be brought within two years of discovery of the breach of warranty.”*

The Supreme Court rejected prior decisions which have relied upon Minn. Stat. § 541.051, subd. 1 which held an action must be commenced within two years of discovery of the injury. Compare Minn. Stat. § 541.051, subd. 1(b) and subd. 4. The Supreme Court found that the statute of limitations does not begin to run when the homeowner (or its predecessor owners) discovered or should have discovered an “injury or damage,” rather the statute of limitations runs “when the homeowner discovers, or should have discovered, the builder’s refusal or inability to ensure the home is free from major construction defects.”

Apparently the Rovicks never requested in writing (under 327A.03(a)) that R & I repair the load-bearing portions of the home. Rather, they focused on other “non-structural” water damage. It was the Vlahoses who first made a “structural repair” demand in May 2000. When R & I refused to repair the structural problems, a “breach” occurred commencing the statute of limitations period. Thus, the Court held “the question of when the Rovicks or the Vlahoses discovered or should have discovered R & I’s refusal or inability to ensure the home was free from major construction defects” was a factual question to be decided on remand.

2. Definition of “Major Construction Defect.” *The Vlahoses contended that the ten year statutory warranty (Minn. Stat. § 327A.02, subd. 1(c)) covers their claims because the persistent water intrusion damaged the load bearing portion of the home during the ten year warranty period. In contrast, R & I contended that to make a claim the “alleged construction defect must be created during and be present upon completion of construction.” Therefore, R & I argued that to the extent that the problem occurred after the completion of construction, the warranty does not apply.*

The Supreme Court unequivocally rejected R & I’s argument and held that the legislature intended to broadly define the term “major construction defect” to include problems that occur “from and after” the warranty date. That is, because the statute includes the word “after,” the Court concluded the legislature intended to permit defects which arose “after” the construction is completed.

C. Practical Considerations.

1. Notice of Defect from the Owner. *The case does not directly address the requirement that an owner provide the builder with written notice of damage within six months of discovery of the problem under Minn. Stat. § 327A.03(a). However, the case does imply that such notices were given by both the Rovicks and Vlahoses.*

A written notice by a homeowner must be taken very seriously by a builder. Such a “written notice” can be a mere e-mail or even an informal handwritten note from an owner. Once a builder has received such a notice, the builder must act if it wants the statute of limitations period to run.

2. Response to a Claim of Defect. *Even in the absence of receipt of a written notice, if a builder determines there is a potential claim, the builder now must provide a written refusal to repair to the owner to cause the statute of limitations to begin to run. Practically, this means that the builder should provide a written notice to the homeowner indicating that the builder is either: a) refusing to correct a defect; or b) is unable to correct the home in such a way that it will be “free from major construction defects.” If a builder continues to work with a homeowner, and never “refuses” or demonstrates an “inability” to repair a defect, then the homeowner can argue (under Vlahos) there was never a “breach” causing the statute of limitations to begin to run.*

D. Significance of Decision. *Once again, the Minnesota Courts are further burdening builders and broadening the statute of limitations. The Courts already expanded the statute of limitations through the doctrine of “equitable tolling” to permit owners to delay (sometimes called “toll”) the statute of limitations if builders continue to work with homeowners to address their problems. See Rhee v. Golden Home Builders, Inc., 617 N.W.2d 618 (Minn. App. 2000). In Vlahos, the Supreme Court is also requiring builders to make explicit their refusal to respond to a homeowner’s claim in order to permit the running of the statute of limitations. The Supreme Court is shifting the burden to the builder to commence the statute of limitations by focusing only on the “breach,” rather than “injuries” that could or reasonably should have been discovered by the homeowner.*

Builders should be proactive in providing written notice that they are refusing or unable to fix problems to order to start the running of the statute of limitations. The practical “problem” is that such written refusals will trigger litigation and place a further burden on builders.