CONTRACTOR AND SUB-CONTRACTOR'S CONSTRUCTION CLAIMS – LITIGATION DEFENSE STRATEGIES

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INTRODUCTION

It is not likely a “news flash” to most trial attorneys; but, I’ll restate it anyway… construction defect litigation is "complex litigation".

There are two reason for that… the first is because of the numbers of parties typically involved, the volumes of paper that can be generated and the statutory regulatory schemes and case law which apply.

The second is because these cases will involve the technical opinions of a potentially wide variety of professional expert witnesses and these opinions require some level of specialized knowledge on the part of the attorney of the professional or scientific field involved and the technical analysis and testing being done. Sometimes it is like an Agatha Christie mystery, trying to figure out just “who did what to whom?”

However, there are some simple and straightforward "truths" that can be kept in mind for most CD cases.

Defense strategies will differ, depending upon who your insured or client is ... design professional, contractor, sub-contractor or materialman and the nature of the project (public vs. private, single family vs. multi-unit vs. mass-produced).

While in most cases it is readily apparent, ***it is always important to understand the strategies and end goals of the other players*** in the litigation game.

- The **design professional**, for the most part, will defend by arguing that any problems experienced on a project are due to construction errors, not design flaws. If design flaws are established, he may then look to his own sub-consultants for indemnity (an architect, for example, may work with a sub-consultant structural engineer, in much the same way a general contractor retains sub-contractors to build the project).

- The **general contractor** [GC] will always be intent upon involving as many sub-contractors and suppliers as possible in the defense of the litigation (and keeping them involved through settlement or trial), in order to spread the risk and share the cost of any settlement or judgment. It

will argue that there were no defects of construction... but, if any are proven by the plaintiff(s), they were the responsibility of the sub-contractors.

A secondary goal of the GC often seen is to resist separate settlements between the claimant(s) and a sub-contractor, so as to avoid building a litigation fund for the claimant(s).

Third, the GC and its counsel will aggressively seek to rely upon written indemnity agreements and additional Insured [AI] Endorsements to force its subcontractors to assume and bear the burden of the expense of the litigation

There are times, however, when the GC's own independent negligence is to blame and not any error by a sub. It is, after all, "in overall responsible charge" of the project.

- **The subcontractor's** first line of defense is always 1) to show that the w*ork* was done in accordance with the plans and specifications, through the construction documents, through course of construction inspection records, photographs, change orders, etc., and to 2) limit or narrow its scope of work on the project.

  Secondarily, it must develop evidence to challenge the legal issue of causation and factually eliminate or minimize the defects or damages claimed and the costs of repair/remediation. In many cases it can be shown that damage manifested to the insured's work was the result of outside influences, such as defects in work done by other subs, subsequent homeowner changes, lack of maintenance, acts of God, etc.

  Different laws will sometimes apply to those who supply a service (design professionals, for example), rather than a product (materialmen, for example) and that can change the ultimate defense strategies used.

  Finally, defense strategies will, of course, depend upon the "real-world" considerations such as available insurance for covered claims, non-covered claims, jury verdict potential and settlement value.

LITIGATION DEFENSE STRATEGIES

1. As early in the claim process as possible, obtain complete and legible copies of all construction project documents, including requests for bids, bids, awards, contracts, change orders, change estimates, requests for information and any other documents which could serve to define:

   a. The project[1]

   b. The scope of work of the insured / client.

[1] Public Works projects are heavily regulated by statute and subject to special considerations. See: Public Contract Code, Section 1100 through 9203.

c. The relative relationships between the parties (owners, developers, design professionals, contractor, sub-contractors and materialmen).

d. The terms and conditions of any indemnity agreements.

2. Review the file for possible absolute/technical defenses (statute of limitations, licensing, etc.), e.g.,

In California, for example, there is a 3 year statute for injuries to real property[2], measured from when the damage was first known or first should have been known through reasonable investigation. There is a 4 year statute for "patent" construction defects[3] and an outside 10 year limit, or "statute of repose" for latent defects[4].

"Substantial compliance" with State contractor's licensing laws is no longer sufficient and a technical gap or deficiency in the licensing of a claimant GC may be a basis for a defense.

3. Claims supervisors and counsel should immediately and aggressively pursue a meaningfully detailed "defect matrix" from the claimant(s), itemizing the specific location(s) and character of each claimed defect or problem and the claimed cost of replacement/repair. This documentation of the claim should be obtained at the earliest possible moment.

Faced with a dilatory or obstructive plaintiffs' counsel, early consideration should be made for a joint defense motion for the appointment of a Special Master, if the court has not already done or if no stipulated Case Management Order by the parties exists dealing with such an appointment. The Sepcial Master can impose a time-specific discovery order on the parties, setting forth, amongst other things, precisely when the defect list is to be delivered and when defense experts can inspect those defects.

4. The insured/client is a built-in expert witness. Use him or her. They should be invited to do an informal site inspection with counsel as soon as possible to review the problems claimed. Doing so often provides early information regarding the underlying project which can be used to lay a foundation for important defenses.

5. Where there is a realistic potential for liability and express indemnity cross-claims from the GC or others are not an issue, serve a reasonable "statutory" offer early in the case. Keep in mind, however, that a "good faith" settlement order does not extinguish a cross-action based upon an express indemnity contract provision.

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[2] Code of Civil Procedure, Section 338.

[3] Code of Civil Procedure, Section 337.1.

[4] Code of Civil Procedure, Section 337.15.

6. Where the insured is a "peripheral" defendant or cross-defendant, seek a nominal cost-of-defense "issue release" settlement with the plaintiff and a dismissal from the general contractor or other cross-complainant. Where separate settlement is not agreed to by the general contractor or other cross-complainant, advise them in writing that their refusal to agree to your settlement with the plaintiff/owner could constitute bad faith and further pursuit of their cross-action could constitute malicious prosecution. Not infrequently, counsel for general contractors resist separate settlements with subs, because it would serve to fund the plaintiff's continued prosecution of the lawsuit against the general or (unstated) they wish to continue to receive the Additional Insured (AI) defense costs back from the sub's carrier. Those, however, are not legitimate basis to keep a sub-contractor in the litigation.

If all parties are acting in good faith, it should be possible to draft a mutual "scope-of-work" release agreement, in a separate settlement for a sub-contractor, through which both the sub and the GC are released and protected from any and all claims arising from the scope of work of the released sub-contractor. Therefore, a GC or developer truly has nothing to lose in agreeing to a 3 way issue release settlement between a minor subcontractor and the plaintiff, where the release also releases the general for any and all related claims. The added benefit, of course, is that the number of parties and issues are narrowed, rendering settlement with the remaining parties more likely or, barring that, resulting in a shorter, more focused trial.

7. In the appropriate case, counsel should endeavor to lay a foundation for a Summary Judgment motion.

8. Carriers should, of course, monitor counsel's hours and hourly rates on a periodic basis. Construction defect litigation is paper and time intensive but there is much work which can be better accomplished by an expert witness, a paralegal or someone other than counsel. Counsel need not attend every deposition in most cases and, while he or she may wish to attend a portion of a visual site walk through to familiarize himself or herself with the project, generally there is no need for counsel to be present all day, every day during multi-day site visits or destructive testing.

9. Carriers should also work together with counsel at all stages to make mutual decisions as to the defense plan and what discovery needs to be done and what can be avoided to save defense costs, without compromising the client's interests or counsel's ethical standards.

10. Counsel should not "shot-gun" discovery by rote habit, of course.

11. Counsel should make every effort whenever possible to share costs with similarly interested co-defendants.

12. Finally, counsel and his or her principal should undertake early exploration of all settlement possibilities, including formal alternative dispute resolution (ADR). The two most common ADR mechanisms are arbitration and mediation. It is important in each case to keep in mind the purposes and distinctions

of each of these tools. Arbitration is an alternative to a trial as a fact finding mechanism and judgment/award. Mediation, on the other hand, is simply a formalized process of settlement discussion.

ARBITRATION

In the absence of a contractual obligation compelling arbitration, in our experience, arbitration is not desirable in all cases; rather, a decision to arbitrate should be made on a case by case basis. The decision process should include close scrutiny of the following:

a. Who the insured is.

Sometimes the arbitration process, being less formal and structured than trial, could favor one party over another or could tend towards a "split-the-difference" result, based upon a desire for "equity", rather than adherence to the technical law and/or the objective evidence.

b. The size of the case.

If the case exposure is smaller, say less than $100,000, then perhaps simple economics of size would mandate serious consideration to arbitration to reduce defense expenses of trial.

c. The arbitration forum available.

Some attorneys and insurance companies claim to have had excellent results using the large multi-discipline commercial ADR services for arbitration. Our experience has been more mixed and again I would suggest that each strategy be determined on a case by case basis. Focus should be on the proposed arbitrator, individually, rather than simple reliance upon a large ADR conglomerate. Ideally, your arbitrator should be an experienced CD litigator, sensitive to an adherence to the Rules of Evidence and possessed with a degree of knowledge about the construction industry and design/construction issues.

d. Cost

Finally, there is cost. Many of the larger ADR businesses seem to be bent upon charging the parties fees of $600 per hour and up. I would suggest that such fees are unconscionable and that every effort should be made between the parties to find qualified hearing officers, who are satisfied with a more responsible fee.

MEDIATION

Though mediation may not appropriate in every construction case, nowadays it is usually ordered or “encouraged” by the courts in one way or another. It clearly is desirable in the larger, multi-party litigation, which otherwise can become self-generating and explosively out of control (the same type of case in which a Special Master may be particularly effective). Past experience suggests, though, that it is only truly effective where the parties come into the discussions with a mutual motivation for settlement.

My comments above, regarding selection of arbitrators and fees, also apply to mediation. Choices should be made on the basis of knowledge, experience and, frankly, personality. A good mediator is one who can encourage discussion and avoid the building of walls between the parties. He or she is someone who can trigger the appropriate "pressure points" of the respective parties and, perhaps, make them aware of the true strengths, weaknesses and exposures in the case.

Counsel and their clients should never rely entirely upon the mediator to do the work to hammer out an agreement. Rather, counsel must fully prepare for the hearing and be ready to present evidentiary support for his or her positions, in the form of photographs, charts, plans, extracts of salient deposition testimony, etc. The mediator in every instance is looking for reasons to progress the discussions towards resolution and the more factual reasons counsel can supply, the more leverage the mediator will have to use with the claimants to settle their case.

And the ultimate “truth?” … it is normally in every party’s interest to compromise and settle litigation sooner, rather than later. But that requires all parties to be willing to perhaps make some concessions and to be realistic.

For the defense, an early settlement reduces the potential for exposure to a larger-than-expected verdict and eliminates or at least significantly reduces what are typically huge defense costs.

From the plaintiffs’ perspective, their costs too are reduced by an early settlement; but, beyond that, money in hand now, in an amount certain for necessary repairs, rationally must be preferred over only the possibility of an unknown amount of money sometime in the future, sometimes 1-2 years away.