New Developments Related to SB 800

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The Right to Repair Act, more commonly known as SB 800, applies to all new residential construction sold after January 1, 2003. It establishes a process to resolve certain construction defect claims prior to the filing of any lawsuit by a homeowner of new residential construction. Few cases discuss or provide clarification about SB 800 until recently.

<u>SB 800 Is Not the Exclusive Remedy</u>

The *Liberty Mutual Co. v. Brookfield Crystal Grove, LLC* (2013) and *Burch v. Superior Court* (2014) cases provide that SB 800 is not the sole remedy for construction defect claims for homes to which SB 800 applies.

In *Liberty Mutual*, a case involving a subrogation claim by an insurer, the California Court of Appeal held that SB 800 does not provide the "exclusive remedy" for construction defect claims involving "actual" as opposed to mere "economic" damages in new residential construction.

In *Burch*, the Court of Appeal reaffirmed that SB 800 is not the exclusive remedy for homeowners – in fact, this decision broadened the previous *Liberty Mutual* decision beyond subrogation claims by an insurer. The Court of Appeal held that the *Liberty Mutual* case applies to claims by a homeowner directly against a builder and allows the homeowners to pursue claims against the builder for negligence and breach of implied warranty.

<u>Notice Requirements to Builder Under SB 800</u>

The Court of Appeal in *KB Home Greater Los Angeles, Inc. v. The Superior Court of Los Angeles County* held that failure to give timely notice, or an opportunity to inspect, under the Right to Repair Act prior to effectuating a repair is fatal to the cause of action. The Right to Repair Act requires that a homeowner subject to SB 800 provide notice of the claimed defects to the builder *before* any repairs are made to the home. The purpose of this notice is to allow the builder an opportunity to correct the alleged defects and to make an offer of repair to avoid litigation. Therefore, where notice was not given before the repairs were undertaken, an insurance company that paid for such repairs will not recover the amounts it paid in any subrogation claim against the builder on a cause of action for the violation of the Right to Repair Act.

<u>Parties Can Opt Out of SB 800 to Adopt Their Own Prelitigation Procedure So Long as the Terms Are Not Unconscionable</u>

Most recently, it was determined that parties can adopt their own prelitigation procedure, so long as the terms are not unconscionable. The homeowners in *The McCaffrey Group, Inc. v. Superior Court of California, County of Fresno* filed suit against the builder, McCaffrey, without complying with the terms of the non-adversarial prelitigation procedures outlined in the purchase agreements.

The prelitigation procedure included a process that would replace SB 800 to address construction defect disputes.

The first step required the homeowner to provide the builder with written notice of the claimed defects and to provide an opportunity for inspection, thereafter, the builder has a "reasonable period of time," not to exceed 60 days, to meet and confer to discuss the claim. The second step required the parties to submit the claim to nonbinding mediation, and if mediation was unsuccessful, the parties could file suit.

McCaffrey filed a motion to compel the homeowners' compliance with the prelitigation procedures, but the trial court denied the motion, finding that the terms of the sales agreements were procedurally unconscionable, the agreements are adhesive, and the procedures lack the strict timelines integral to the Right to Repair Act.

Turning to unconscionability, the appellate court required a showing of procedural and substantive unconscionability on a sliding scale basis. That is, the more procedurally unconscionable a contract term, the less substantively unconscionable it needed to be. Procedural unconscionability requires oppression or surprise. The appellate court found that the purchase agreements had a low level of procedural unconscionability, therefore, for the homeowners to prevail, they needed to establish a high level of substantive unconscionability.

The substantive element of unconscionability pertains to the "fairness of an agreement's actual terms and to assessments of whether they are overly hard or one sided" (quoting *Pinnacle Museum Tower Assn v. Pinnacle Market Development LLC* (2012) 55 Cal.4th 223). The appellate court found that while the purchase agreement provisions did not have set deadlines wherein the builder must take corrective action, a reasonable time to perform was implied. Moreover, the purchase agreements contained an implied covenant of good faith and fair dealing, which the builder risks breaching if it fails to conduct itself in good faith.

The court previously explained in *Baeza v. Superior Court* (2011) 201 Cal.App.4th 1214 that if a builder opts out of the statutory procedures in favor of its own contractual procedures, the builder opts out of all of Chapter 4 (which prescribes the non-adversarial prelitigation procedures a homeowner must initiate before bringing a civil action against the builder; see also Civ. Code §§910-938). Tellingly, the court pointed out that if the Legislature intended to require a builder's contractual provisions to include certain deadlines, it could have so stated within Civ. Code §914 (which allows for the builder to commence non-adversarial contractual provisions other than those set forth in Chapter 4). Moreover, the Legislature could have made the deadlines of Chapter 4 applicable to a builder's contractual provisions by setting the deadlines as a minimum standard. Instead, the Legislature intended that all deadlines be included in Chapter 4, and that builders be permitted to opt out of Chapter 4 by way of Civ. Code §914. Therefore, the builder can prescribe its own non-adversarial prelitigation procedure.

The appellate court dismissed arguments that the agreement was unconscionable because it required more specific notice of defects than required under the Right to Repair Act. While the act required notice of the defect to the extent known by the homeowner, the lack of that precise language in the purchase agreement did not imply that the homeowner did not need to provide the nature and location of the known

defects. The appellate court also dismissed an argument that the contractual provisions that required sharing in prelitigation mediation fees was unconscionable. Other courts have ruled that it is not unconscionable for a homeowner to pay half the costs of judicial reference as outlined in a purchase agreement. Moreover, the homeowners here failed to show paying the mediation fees in this case would place any unreasonable burden on them, or how the mediation here was likely to last an undue amount of time.

The appellate court concluded that the contractual prelitigation provisions were not substantively unconscionable and were enforceable in this case.

Conclusion

SB 800 is not the sole remedy to a homeowner who purchased a home after January 1, 2003. However, if SB 800 is pursued, it needs to be followed strictly, and any anticipation for repair work needs to be timely reported to affected parties. Lastly, for builders, it is possible to completely eliminate the SB 800 process by opting out and, instead, carefully crafting a prelitigation procedure that balances procedural and substantive unconscionability.