

Recent Jury Decision Makes the Case for Alternate Dispute Resolution for Condominium Warranty and Construction Claims

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In November, 2012, an Anne Arundel County, MD Circuit Court jury awarded damages in the amount of \$5.6 million to a condominium association in its claim against the builder/developer regarding alleged faulty construction of the condominium. In *Eden Brook Condominium, Inc. v. NVR Inc., Circuit Court for Anne Arundel County, Case No. 02C11158348*, the jury found in favor of the condominium association on claims for breach of express and implied warranties and negligent misrepresentation relating to alleged faulty construction that the condominium association claimed resulted in water penetration and substandard heating and cooling in the condominium.

The trial in the *Eden Brook Condominium* case lasted five weeks and included the testimony of multiple unit owners who described the need to keep buckets in their units to catch leaking water. It appears from case reports that the witnesses and evidence submitted by the condominium association also focused on the representations contained in marketing and sales materials provided by the developer. While a number of factors contributed to the verdict in this case, including substantial expert involvement and testimony, the testimony of numerous sympathetic witnesses likely captured the jury's attention. The costs associated with litigating complex construction cases, the amount of time it takes to try such cases and the empathy that jurors may have for impacted homeowners certainly raise the question whether alternate dispute procedures should be utilized by builders and developers of common interest communities, and whether such procedures should be dictated by the governing documents. When complicated warranty disputes are pursued through the court system, they are subject to the court's rigid rules and timelines with regard to discovery and experts and to the review of technical design and construction issues by lay persons. The complex nature of most construction defect cases require significant time for both sides to gather information, facts, opinions, and suggested remedies before disputes can be resolved. Less formal dispute resolution procedures often provide a better structure for the parties to fully examine alleged defects and come to a mutual and fair agreement as to the remedy.

Given the potential for juries to come back with sympathetic large verdicts, as in the *Eden Brook Condominium* case, builders/developers should give serious consideration to imposing alternate dispute resolution procedures in the documents governing new projects. The governing documents will guide the condominium association as to the procedures necessary to investigate and assert warranty and construction claims. Additionally, such documents may provide a

reasonable structure for the developer's exit from the project. A fair and detailed provision requiring procedures for investigation, notification and informal resolution of potential disputes regarding claims for breach of warranty and alleged construction defects may provide a good roadmap to avoiding significant jury verdicts such as the one issued in the *Eden Brook Condominium* case. Dispute resolution procedures that require joint inspections, informal settlement conferences and mediation before the parties may proceed with litigation or, better yet, arbitration, often force the parties toward a negotiated resolution as opposed to costly and risky litigation.

While arbitration does not necessarily guarantee a reasonable and less costly resolution, it does limit the review of complicated technical matters by lay persons easily swayed by emotional testimony. As a result, it is less likely that a parade of sympathetic homeowner witnesses will significantly impact the outcome. In a recent decision from the California Supreme Court, the court affirmed that a provision in a condominium declaration requiring arbitration is binding on a unit owners association, even though the association did not exist at the time, the declaration was recorded. *Pinnacle Museum Tower Association v. Pinnacle Market Development (US), LLC, et al., S186149 (Cal. Aug. 16, 2012)*. While this decision does not have precedential value in Maryland, its reasoning may be persuasive on the enforceability of alternate dispute resolution and, particularly, arbitration requirements contained imposed in the governing documents of the common interest community.

In the *Pinnacle* case, the community association filed suit against the developer seeking recovery for damage related to alleged construction defects. The developer then filed a motion to compel arbitration in accordance with the declaration provision that required construction disputes with the developer be solved through binding arbitration. Both the trial court and the Court of Appeals held that the arbitration requirement was unconscionable, however, the California Supreme Court reversed, upholding the mandatory arbitration provision in the declaration. As is typically the case in the formation of condominium projects, the developer drafted and recorded the declaration, setting forth the terms and conditions upon which the condominium project would be governed. Because no units had been sold prior to recordation of the declaration (nor could they have been under law), the association was not comprised of owners independent of the developer at the time the declaration was recorded. Nonetheless, the California Supreme Court stated that once the first buyer accepted the declaration by purchasing a unit, all terms of the declaration became enforceable,

unless unreasonable. Even though the association did not bargain with the developer regarding the terms of the declaration, the terms of the declaration reflect enforceable written promises. The Court found that the arbitration provision was not unconscionable in part because it was not overly harsh or one-sided so as to shock the conscience.

In the initial stages of project formation, it is important for the developer to consider how construction defect issues will be addressed. Dispute resolution procedures, including arbitration clauses are not uncommon and, in light of the significant judgment issued by a jury in the *Eden Brook Condominium* case, such requirements warrant serious consideration by developers. ■

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