

# ProNetwork News

## Risk Management Tools for the Design Professional



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### **If You Build It, They Will Sue: Condominium Projects – Part I**

*by Trevor O. Resurreccion, Esq. & Peter L. Stacy, Esq., Weil & Drage, APC<sup>1</sup>*

#### **I. Introduction**

Do architects owe a “duty of care” to the homeowners of a condominium project with whom the architects have no contractual privity? According to the California Supreme Court, they do. What does this mean in practical terms? The answer is that architects are now more than ever exposed to potential future claims and lawsuits brought by homeowners and the homeowners’ associations years after the project has been completed even where the architect’s design decisions are trumped by those of the project developer, and the architect’s role in the construction phase of the project is limited.

The purpose of this paper is to provide background on an architect’s potential liability to its client and third parties on condominium projects as well as guidance on how to prospectively address the concerns highlighted by a recent California Supreme Court decision and many other lawsuits in which architects have been sued by third parties. Specifically, we address the following topics: assessing your owner client, important contract provisions, and insurance issues. The intent is to provide a roadmap for architects in assessing their risks on condominium projects and a practical approach to addressing those risks. While it may not be possible to fully insulate architects from all risks, it is certainly a good practice to have a firm understanding of those risks and to address the risks up front. Benjamin Franklin is attributed with the statement: “In this world nothing can be said to be certain, except death and taxes.” For architects who design condominium projects, unfortunately, lawsuits should be added to that list.

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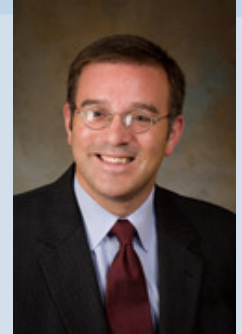
### II. The *Beacon* Case – A Bellwether for Future Court Decisions?

In July 2014, the California Supreme Court declared that an architect owes a duty of care to future homeowners where the architect is a “principal architect” on the project. (*Beacon Residential Community Association v. Skidmore, Owings & Merrill LLP, et al.*, 59 Cal.4th 568, 327 P.3d 850 (2014) (“Beacon”).)<sup>2</sup> The Court held that this duty applies “even if the architect does not actually build the project or exercise ultimate control over construction decisions.” (*Id.* at 581, 327 P.3d 850, 859.) Shocking? Yes! The more significant question is whether YOU are prepared to provide design services on a condominium project in light of the California Supreme Court’s recent decision. The *Beacon* case is particularly apropos to this paper because it involved a condominium project.

It is important to understand the context and facts upon which the *Beacon* case was decided before we address best practices for providing design services for condominium projects. The plaintiff was a homeowners’ association, which sued the project developer and various other parties, including two project architects, for alleged construction defects that purportedly make the homes unsafe and uninhabitable during portions of the year due to high temperatures. According to the Association’s complaint, the architects “played an active role throughout construction, coordinating efforts of the design and construction teams, conducting weekly site visits and inspections, recommending design revisions as needed, and monitoring compliance with design plans.”<sup>3</sup> (*Id.* at 572, 327 P.3d 850, 853.)

The architects filed a motion challenging the plaintiff’s complaint with the trial court on the grounds that the architects did not owe a duty of care to the Association or its members under the facts alleged. Although the architects prevailed on their motion, the Association appealed and the Court of Appeal reversed the trial court’s decision, holding that the architects owed a duty of care to the Association. The case eventually percolated its way up to the California Supreme Court. The Court framed the legal issue as follows: “Here we consider whether design professionals owe a duty of care to a homeowners association and its members in the absence of privity [of contract].” (*Id.* at 573, 327 P.3d 850, 854.) In answer to this question, the Court noted that the importance of contractual privity “has been greatly eroded over the past century.” (*Id.* at 574, 327 P.3d 850, 854.) In other words, the California courts have recognized that even in the absence of contractual privity, architects may owe a duty to a non-client such as a homeowners’ association.

In particular, the Court focused on three factors: (1) the closeness of the connection between the architects’ conduct and the Association’s injury; (2) the limited and wholly evident class of persons and transactions that the architects’ conduct was intended to affect; and (3) the absence of “private ordering” options that would more efficiently protect homeowners from design defects and their resulting harms. (*Id.* at 581, 327 P.3d 850, 859.)



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Peter has drafted and negotiated complex contracts concerning multi-million dollar public works projects and private hotels, casinos, resorts, horse racing organizations, mixed-use developments, and multi-family subdivisions. He represents a wide variety of clients, including architects and engineers, contractors, investment advisors, horse racing association, horse owners, entrepreneurs, entertainers, manufacturing and fabrication companies, property managers, and retail businesses.

With respect to the first factor, the Association's complaint alleged that the architects' primary role in the design of the project bore a close connection to the Association's injury. The Court agreed with the Association that, "even if an architect does not actually build the project or make final decisions on construction, a property owner typically employs an architect in order to rely on the architect's specialized training, technical expertise, and professional judgment." (*Id.* at 582, 327 P.3d 850, 859.) As such, the architects could not avoid liability concerning their professional judgment on architectural issues such as adequate ventilation or code-compliant windows on the grounds that the client made the final decision.

Perhaps more alarming was the Court's pronouncement that, "it would be patently inconsistent with public policy to hold that an architect's failure to exercise due care in designing a building can be justified by client interests at odds with the interest of prospective homeowners in safety and habitability." (*Id.* at 582, 327 P.3d 850, 859.) The Court characterized the architects' services as taking a "lead role" in both the design and implementation of the design for the project. Notably, the Court acknowledged the architects' claim that the developer's independent decision and authorization of the alleged defect may prove to be a defense as to whether the architects were the cause of the Association's claim injury, but not whether the architects owed a duty to the Association. (*Id.* at 583, 327 P.3d 850, 853.)

The second factor the Court considered is the class of persons the architects' services were ultimately intended to benefit or affect. The Association alleged that the architects knew their services were being provided on a project intended to be sold as condominiums and used as residences. Accordingly, the Court concluded that the architects were well aware that the architects' services would necessarily affect the homeowners. (*Id.* at 584, 327 P.3d 850, 854.)

The third and final factor the Court considered was the prospect of so-called private ordering (hiring a third party professional to provide an independent assessment of the structure and its component parts) as an alternative to negligence liability. The Court analogized the average homebuyer to the "presumptively powerless consumer" in a product liability case. (*Id.* at 584, 327 P.3d 850, 861.) The Court explained:

A liability rule that places the onus on homebuyers to employ their own architects to fully investigate the structure and design of each home they might be interested in purchasing does not seem more efficient than a rule that makes the architects who designed the homes directly responsible to homebuyers for exercising due care in the first place. This seems especially true in 'today's society' given the 'mass production and sale of homes' . . . such as the 595-unit condominium project in this case."

(*Id.* at 585, 327 P.3d 850, 862.)

The Court in *Beacon* summarized its conclusion as follows:

1. The architects' work was *intended to benefit the homeowners* living in the residential units that the architects designed and helped construct;
2. It was *foreseeable* that these homeowners would be among the limited class of persons harmed by the negligently designed units;
3. The Association's members *suffered injury* because the design defects made their homes unsafe and uninhabitable during certain periods;
4. Based upon the nature and extent of the architects' role as the sole architects on the project, there is a *close connection* between the architects' conduct and the injury suffered;
5. Significant "*moral blame*" attached to the architects' conduct because of their "unique and well-compensated role" in the project in addition to their awareness that future homeowners would rely on the architects' specialized expertise in designing safe and habitable homes; and
6. The *policy of preventing future harm* to homeowners reliant on architects' specialized skills supports recognition of a duty of care.

(*Id.* at 586, 327 P.3d 850, 862.)

In light of the *Beacon* decision, architects are forewarned regarding the potential minefield of liability issues they may face if they choose to provide architectural services on a condominium or other residential project, including exposure to claims by future homeowners and the homeowners' associations (HOA). The following are a few tips for taking a proactive approach when considering taking on the inherent liability risks involved in designing a condominium project:

- An iron-clad scope of services, clearly designating the roles of owner, contractor, architect and other consultants, may prove helpful in educating a court on how broad a prime consultant's services really are. We are all very aware that lead consultants on a project can only do so much. Your contract becomes the first line of defense in articulating how much control you really have.
- An indemnity and/or limitation of liability provisions that includes third party claims are generally enforceable. You can negotiate reasonable language with your client that will protect both parties fairly, and require your client to protect you from third party claims, or provide insurance to cover such claims. Even if that protection has its limits, it is worth fighting for. Better yet, insist that the indemnity obligations are with the parent company developer as opposed to the subsidiary/LLC that only owns the one development property.
- As lead consultant, you are generally the scrivener of meeting minutes, responses to inquiries and change order requests, etc. Use these



opportunities to include notations as to the parties involved in certain discussions and decision-making. These documents may become key in a subsequent lawsuit, as they will likely shed light on how much power a “principal architect” really has throughout the course of a project.

- Propose contract provisions to your client requiring language in the Purchase and Sales Agreements and CC&Rs, (Covenants Conditions and Restrictions), that force the HOA and homeowners, if they are to be considered legitimate third party beneficiaries, to be subject to any and all contract defenses that you have within your agreement with your client.
- Insist upon additional, protective contract language that has your client agree to write into the Declaration, the Bylaws and Purchase & Sales Agreements a requirement that the recommended maintenance be the responsibility of the HOA, and that homeowners undertake additional maintenance measures for their own residences.

With *Beacon* as our starting point, let’s now turn to more specific contractual and other liability considerations to assist architects who are considering designing a condominium project.

### III. Assessing Your Owner Client

In light of the *Beacon* decision, client selection/evaluation could not be more important for a condominium project. The client that you execute a contract with is looking to transfer ownership to a HOA and individual unit owners as soon as possible. This means that instead of just the client as a likely claimant against the design professional for project delays and/or defects, you now also have the HOA and individual unit owners as potential plaintiffs that can sue the design professional directly. Is the client developer going to be there when the claims of the HOA and/or unit owners arise? Often times, a single purpose entity is formed by the client developer for the particular project. The contract may very well limit your remedy only against this single purpose entity that has little if any assets once the project is complete and units sold. Will the client developer even be in existence at the time of a claim? You may heavily negotiate an owner indemnity provision for HOA/homeowner claims. However, unless there is some parent company guaranty to such an indemnity obligation, this may be a hollow provision. What is the client developer’s litigation history and/or track record in addressing HOA and unit owners’ claims? Will the client developer entertain making repairs to mitigate the damages, or at least have hired reputable contractors and required such contractors to carry appropriate insurance to cover HOA and unit owner claims? Is the client developer willing to address maintenance obligations of the HOA and unit owners in the drafting of the HOA’s CC&Rs, bylaws and other documents? Reputation of your client developer in this regard should not be

overlooked. All of the above should be carefully considered in addition to the specific key protective contract provisions.

Be on the lookout for *If You Build It, They Will Sue: Condominium Projects – Part II*, the next bi-monthly issue of *ProNetwork News*, which will include sections on important contract clauses and insurance issues resulting from Beacon.

### Endnotes

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<sup>2</sup> The Court defined “principal architect” as an architect, in providing professional design services, who is not subordinate to any other design professional. (*Id.* at 581, 327 P.3d 850, 859.)

<sup>3</sup> For purpose of the motion, the Court accepted as true the facts as alleged in the Association’s complaint. Importantly, the architects would have the opportunity to challenge the factual allegations at a later stage in the lawsuit, including trial.

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