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Minnesota's Moisty, Moldy Morass: A Comment on Construction Defect Claims in Minnesota

Terri A. Tersteeg

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MINNESOTA'S MOISTY MOLDY MORASS: A COMMENT ON CONSTRUCTION DEFECT CLAIMS IN MINNESOTA

Terri A. Tersteeg[†]

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I. INTRODUCTION

Today, the home building industry is plagued with a rise in construction defect litigation.¹ The problem has pitted homeowners, home builders, and the insurance industry against each other. It is an extremely emotional issue with no easy compromise because it impacts one party's home and another's livelihood.

Construction defect problems in the home building industry are not a new phenomenon. The longevity of the problems is evidenced by Elizabeth Dole's 1979 speech to the National Association of Home Builders.² In her speech, she noted that "most of the homes built in this country are of sound, lasting quality."³ But she also emphasized that "for too many Americans, the dream home has turned into a nightmare."⁴

The homeowner's dream home can become a nightmare when the homeowner discovers a mold and moisture intrusion problem, often due to a construction defect, and learns that the process and legal remedies for resolving the problem do not work very well.

While the construction defect problem exists across America, this comment will focus on the problem in Minnesota. Part II examines the events that likely set the stage for today's construction

1. Author's conclusions from interviews with J. Scott Andresen, Attorney, Bassford Remele in Minneapolis, Minn. (June 6, 2006); Rich Dahl, Attorney, Madigan, Dahl & Harlan, in Minneapolis, Minn. (June 5, 2006); Julie Doherty, Attorney, Fabyanske Westra Hart & Thomson, in Minneapolis, Minn. (June 12, 2006); Rob Moschet, Attorney, McCollum, Crowley, Moschet & Miller, LTD., in Bloomington, Minn. (June 20, 2006); Brenda Sauro, Attorney, Hammargren & Meyer, P.A., in Edina, Minn. (June 23, 2006).

2. Elizabeth Hanford Dole, Comm'r, Fed. Trade Comm'n, Address at the National Association of Home Builders Annual Convention, Home Warranties: Construction a Good Foundation for Builder/Consumer Relations (Jan. 21, 1979), http://www.hobb.org/index.php?option=com_content&task=view&id=390&Itemid=142.

3. *Id.*

4. *Id.*

defect problem. Part III explores the legal theories that form the basis for construction defect claims. Part IV outlines statutory law and reviews recent homeowner cases that have interpreted the law. Part V examines the recovery theories that provide funding sources for construction defect claims. Part VI outlines the societal impact of Minnesota's current approach to addressing construction defect claims. Finally, Part VII offers recommendations for addressing Minnesota's construction defect plight.

II. MINNESOTA'S HOME BUILDING INDUSTRY AND THE CONSTRUCTION DEFECT PROBLEM

A. *Construction Defects—Defined*

Construction defects can range from complex foundation and framing issues, which threaten the structural integrity and habitability of a building, to aesthetic issues such as improperly painted surfaces.⁵

Construction defects that threaten a building's structural integrity and habitability generally can be grouped into four major categories.⁶ The first category encompasses design deficiencies.⁷ A defect in this category often manifests in the roof system, which has a design complexity prone to leaks.⁸ The second category, material deficiencies, results from the use of inappropriate or inferior building materials and products.⁹ The universe of material deficiencies is large, and can range from windows that, despite proper installation, do not function properly to building materials that are inappropriate for the climate.¹⁰ The third category, construction deficiencies, includes poor quality or substandard workmanship.¹¹ It often manifests as water infiltration into the building structure, rotting plywood or wood-based products or creating pest or mold infestation or growth, electrical or

5. C-Risk, Construction Defect, What is a Construction Defect?, http://www.c-risk.com/Construction_Risk/CR_CDs_01.htm (last visited Apr. 3, 2007).

6. *Id.* These four categories arose from construction defect litigation and are generally recognized by trial courts handling construction defect cases. *See id.*

7. *Id.*

8. *Id.*

9. *Id.*

10. *Id.*

11. *Id.*

mechanical problems, or lack of appropriate, sound insulation.¹² Subsurface and geotechnical problems, which comprise the fourth category, are typically found in parts of the United States that have expansive soil conditions, such as California or Colorado.¹³ Examples of this fourth category include slope failures and settlement, and such defects can ultimately result in cracked floor slabs and foundations.¹⁴

B. Minnesota Homeowners—“The Consumer”

According to the United States Census Bureau’s 2003 American Community Survey, over seventy-six percent of Minnesota residents own their home, earning Minnesota the highest ranking in the nation.¹⁵ While the census data do not identify what percentage of these Minnesota homeowners are part of the Baby Boomer generation, given the size and span of the generation, it seems reasonable to postulate that they comprise a large portion of it. Furthermore, the “Baby [B]oomers make up a large majority of today’s work force and wealth component, with significant buying power.”¹⁶ Unlike their parents and grandparents, “they did not live through the depression, are not afraid of spending money, and are often credited with keeping the economy afloat.”¹⁷ Moreover, they “often have a hurried lifestyle and were brought up to be individualistic.”¹⁸

This financially free-flowing and individualistic lifestyle spawned a demand for homes that were expansive, flowing, and perceived as different from those of the neighbors. The original concept embodying this demand became known as the “McMansion.” These homes were intended to fill a gap between the modest suburban tract home and the upscale custom-designed

12. *Id.*

13. *Id.*

14. *Id.*

15. Minn. Housing Finance Agency, The Emerging Markets Homeownership Initiative: A Business Plan to Increase Homeownership in Minnesota’s Emerging Markets 14 (June 30, 2005), *available at* http://www.mhfa.state.mn.us/about/EMHI_Business_Plan.pdf.

16. See OnPoint Marketing & Promotions, Baby Boomer Marketing Defined, <http://www.onpoint-marketing.com/baby-boomer-marketing.htm> (last visited Apr. 3, 2007).

17. *Id.*

18. *Id.*

home found on large residential properties.¹⁹ Inherent in this lifestyle was an expectation that the home would be perfect and easily maintained.

C. Minnesota's Home Building Industry

In order to build or remodel residential property in Minnesota, a home builder (general contractor) must be licensed, comply with state building codes, and carry liability insurance.²⁰ The general contractor must pass one or more initial exams, although they are not as rigorous as the state medical, accounting, and bar exams.²¹ General contractors must also meet annual continuing education requirements and must actively renew the license each year.²²

Historically, general contractors had employees or "crews" to perform the work on their residential building projects.²³ Today, as in recent years, all or most of the work performed on a residential building project is done by subcontractors.²⁴ While the general contractor is ultimately accountable for the completed product, the current homebuilding business model provides the general contractor little management control over the manner and methods used by the subcontractors.²⁵ The general contractor must rely on subcontractors, building product manufacturers, and suppliers, who in some instances do not stay current on building practice changes or do not fully comprehend the impact of the changes.²⁶ To complicate matters, many of the subcontractors, manufacturers, and suppliers view their work or product as an

19. The definition of McMansion: "A modern house built on a large and imposing scale, but regarded as ostentatious and lacking in architectural integrity." 1 SHORTER OXFORD ENGLISH DICTIONARY 1727 (William R. Trumble & Angus Stevenson eds., 5th ed. 2002).

20. See MINN. STAT. §§ 326.83–.992 (2006); Contractor's License Reference Site, Minnesota, <http://www.contractors-license.org/mn/Minnesota.html> (last visited Apr. 2, 2007).

21. See MINN. STAT. §§ 326.84, .87, .89, .97 (2006).

22. *Id.*

23. Author's conclusions from interviews with Rich Dahl, Attorney, Madigan, Dahl & Harlan, in Minneapolis, Minn. (June 5, 2006); Rob Moschet, Attorney, McCollum, Crowley, Moschet & Miller, in Bloomington, Minn. (June 20, 2006); Don Sivigy, Sr. Rep., Minn. Dept. of Labor & Ind., in St. Paul, Minn. (June 21, 2006); Nick Wojtowicz, Owner, Olinda Contracting, Inc., in Hugo, Minn. (June 29, 2006).

24. *Id.*

25. *Id.*

26. *Id.*

independent unit.²⁷ Consequently, they do not view their segment of the homebuilding project as part of a coordinated and integrated system.²⁸ Finally, for a variety of reasons, one of which is consumer pressure, the general contractors and subcontractors place a high priority on completing the project on time.²⁹

In 1972, Minnesota adopted a state-wide building code.³⁰ As a result of the 1973–74 Arab Oil Embargo and consumer concerns about dwindling energy sources, Minnesota amended the code in 1976 to include energy conservation in buildings.³¹ Due to this energy conservation amendment,³² Minnesota homes built in the past thirty years are much more energy efficient.³³ While these energy code changes were a welcome improvement for homeowners because they kept homeowners warmer in the cold Minnesota winters and cooler in the hot and humid Minnesota summers, such changes created durability issues with the homes.³⁴ The Minnesota homes built in this era are much tighter, with a lower level of air exchange between the inside and outside air.³⁵ Consequently, the buildings must be properly engineered and adequately ventilated to ensure good performance.³⁶ The home must be viewed as a dynamic system with a focus on moisture management.³⁷ The presence of excess moisture in a home can result in condensation on walls and windows, decay, wood rot, and mold growth.³⁸

A home that has been properly engineered has integrated building materials, products, and practices that are appropriate for

27. *Id.*

28. *Id.*

29. *Id.*

30. See Minn. Dep't of Labor & Indus., History of Building Codes and Standards Division, http://www.doli.state.mn.us/bc_contact_us_history (last visited Apr. 2, 2007).

31. *Id.*

32. *Id.*

33. See Minn. Lath & Plaster Bureau, Stucco in Residential Construction: 2003 Minnesota State Building Code Update 3 (Aug. 2004), <http://www.mnlath-plaster.com/listing/StuccoResidConstr.pdf>, at 3.

34. *Id.*

35. *Id.*

36. Patrick Huelman, Minn. Dep't of Commerce, Building Science Primer, available at http://www.state.mn.us/mn/externalDocs/Commerce/Building_Science_Primer_111202035139_BuildingPrimer.pdf 1 (last visited Apr. 3, 2007).

37. *Id.*

38. *Id.* at 12.

the regional climate.³⁹ The construction of the home has integrated both a barrier and a drainage approach to managing and controlling moisture.⁴⁰ In plain language, the home has been constructed with attention to detail so that all of the components, windows, doors, wall systems, decks, roofs, and exterior cladding interact to manage moisture levels either by keeping moisture out or by draining it from the structure.

It is also important to understand that the state building code is a minimum standard.⁴¹ A best practice standard is better.⁴² To date, however, best practice does not appear to be clearly defined or accepted for residential building practices. This lack of definition makes it ambiguous to interpret and enforce best practice.

Building materials and products have changed in the past thirty years,⁴³ and three product changes seem to have had the most impact on the moisture intrusion problem. Those changes are sheathing, windows, and stucco products. In the 1980s, the residential building industry stopped using plywood as sheathing.⁴⁴ Plywood was predominantly replaced with oriented strand board ("OSB").⁴⁵ This changed the wetting and drying capacity of the structure.⁴⁶ Plywood is wood with its natural composition still intact.⁴⁷ Nature's capillaries are still present and, within limits, can

39. See Building Science Corp., House Design Recommendations by Climate Region, <http://www.buildingscience.com/designsthatwork/default.htm> (last visited Apr. 3, 2007) (providing links to home designs integrated and specialized for different climates).

40. See Building Science Corp., Water-Managed Wall Systems 8 (2003), http://www.buildingscience.com/resources/articles/water-managed_wall_systems.pdf (last visited April 6, 2007).

41. Author's conclusions from interview with Don Sivigy, Sr. Rep., Minn. Dept. of Labor & Ind., in St. Paul, Minn. (June 21, 2006).

42. *Id.*

43. Author's conclusions from interviews with Steve Pedracine, Exec. Dir., Minn. Lath & Plaster Bureau, in St. Paul, Minn. (June 8, 2006); Paul Ellringer, Owner, Air Tamarack, in St. Paul, Minn. (June 16, 2006).

44. *Id.*

45. *Id.*

46. Author's conclusions from interview with Paul Ellringer, Owner, Air Tamarack, in St. Paul, Minn. (June 16, 2006). In addition, according to Paul Ellringer, during the 1980s and 1990s, the building industry changed not only the type of vapor retarders used but also how they used them. This change, in combination with the OSB sheathing, was a major contributor to the moisture problem in wall systems. *Id.*

47. *Id.*

move moisture and dry themselves out.⁴⁸ OSB is manufactured wood.⁴⁹ It is chipped pulp wood that has been mixed with adhesives and formed into wood sheets.⁵⁰ In contrast to plywood, when OSB gets wet, the OSB tends to retain moisture and not dry out.⁵¹

Similarly, homes built before the 1980s had all-wood window frames.⁵² During this timeframe, window manufacturers began producing metal and vinyl-clad windows that were made from a combination of products.⁵³ While they were easier to maintain than wood windows, due to their artificial properties, they expanded and contracted at different rates than plywood or OSB.⁵⁴ In contrast, the homes built before 1980 contained all-wood components that seemed to more naturally work in unison.⁵⁵

Lastly, stucco has been used as cladding on buildings for centuries.⁵⁶ It was used in many old European buildings as well as early buildings in the Eastern United States.⁵⁷ As evidenced by the life of these buildings, the stucco was attractive and long-lasting.⁵⁸ It was labor intensive to apply, however, and limited in terms of color and texture.⁵⁹ Likely as a part of the demand for McMansions, stucco composition and processes evolved and, much like sheathing and windows, stucco became a manufactured component of the structure.⁶⁰ As such, it was limited in its natural ability to interact with other components.⁶¹

These three product changes have resulted in homes that have openings at the joints where the components come together.⁶² Initially, the general contractors, subcontractors, and product manufacturers did not realize the impact of these openings.⁶³

48. *Id.*

49. *Id.*

50. *Id.*

51. *Id.*

52. Author's conclusions from interviews cited *supra* note 43.

53. *Id.*

54. Interview with Steve Pedracine, Exec. Dir., Minn. Lath & Plaster Bureau, in St. Paul, Minn. (June 8, 2006).

55. *Id.*

56. Minn. Lath & Plaster Bureau, *supra* note 33, at 1.

57. *Id.*

58. *Id.*

59. Author's conclusions from interview with Steve Pedracine, *supra* note 54.

60. *Id.*

61. *Id.*

62. *Id.*

63. *Id.*

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Consequently, homes were constructed without effective moisture management systems.⁶⁴

D. *Minnesota's Failing Homes*

Much has been written and published about Minnesota's construction defect problem.⁶⁵ Many homeowners have been unhappy to discover that they have more consumer protections for a fickle \$20 toaster than for a home that turns out to be flawed.⁶⁶ The Executive Vice President of the Builders Association of Minnesota estimates that "less than one percent of the homes built in Minnesota since 1990 may fail. While this is a small number, it involves people's homes, so it is an emotional and costly issue."⁶⁷

Statewide validated data on the magnitude of the problem is not readily available. The City of Woodbury is the only known Minnesota community that has documented the problem and is collecting data.⁶⁸ From 1990 to 2000, Woodbury issued approximately 11,200 building permits.⁶⁹ According to Woodbury's documented figures, 276 of Woodbury's stucco homes failed

64. Author's conclusions from interviews with Steve Pedracine, Exec. Dir., Minn. Lath & Plaster Bureau, in St. Paul, Minn. (June 8, 2006); Paul Ellringer, Owner, Air Tamarack, in St. Paul, Minn. (June 16, 2006); Patrick Huelman, Assoc. Professor, Univ. of Minn. Cold Climate Housing, in St. Paul, Minn. (June 8, 2006).

65. See, e.g., Martin Holladay, *Energy Design Update: Minnesota's Rotting Stucco Walls*, 5 MINN. BUILDER 32 (2006); Paul J. Ellringer, Air Tamarack, Inc., *Why Are New Masonry Stucco Houses Rotting in Minnesota?*, June 2005 (on file with author); City of Woodbury, Minn., "Stucco in Residential Construction," A Position Paper by the City of Woodbury Building Inspection Division, Update (Feb. 9, 2005), <http://www.ci.woodbury.mn.us/planning/hmstucco.html>; Tim Carter, *EIFS Stucco Systems Prone to Water Problems*, STAR TRIB. (Minneapolis), Oct. 14, 1998, available at <http://www.startribune.com/397/story/36129.html>.

66. Dee DePass, *Exposed to the Elements: When Windows Leak or Are Improperly Installed, Homeowners Often Are Left Waiting as the Blame, Costs and Legal Remedies Get Hashed Out*, STAR TRIB. (Minneapolis), Apr. 15, 2006, at 1H; KARE-11 News, *A Quirk in the Law That Could Cost Homeowners Everything*, Feb. 3, 2006, http://kare11.com/news/news_article.aspx?storyid=117836; CONSUMER REPORTS, *Housewrecked*, Jan. 2004, <http://www.consumerreports.org/cro/personal-finance/shoddy-home-construction-104/overview/>. While this *Consumer Reports* article is not speaking specifically about Minnesota, it is speaking to the problem. *Id.* Minnesota homeowners who spoke on the condition of confidentiality made similar comments.

67. Interview with Pam Perri Weaver, Executive Vice President, Builders Association of Minnesota, in St. Paul, Minn. (June 29, 2006).

68. Author's conclusions from interview with Ron Glubka, Chief Building Official, City of Woodbury, in Woodbury, Minn. (June 22, 2006); email from Ron Glubka (July 27, 2006) (on file with author).

69. *Id.*

during this period.⁷⁰ And while home repair costs were not validated prior to the year 2002, to date, the City of Woodbury estimates home repair costs resulting from construction defect problems to be in excess of \$22,000,000.⁷¹

All the parties involved—general contractors, subcontractors, window manufacturers, building inspectors, insurance companies, homeowners, and attorneys—are pointing fingers and playing the “blame game.” All parties do agree, however, that the construction defect problem seems to be most catastrophic in homes built between 1990 and 2000 in the fastest-growing outer-ring suburbs of Minneapolis and St. Paul.⁷² Nonetheless, all parties believe they have a valid argument. And they probably do. Minnesota’s construction defect problem is a complex issue with no easy compromise.

III. LEGAL THEORIES OF CONSTRUCTION DEFECT CLAIMS

A. *Tort—Negligence*

“Broadly speaking, a tort is a civil wrong, other than breach of contract, for which the [legal system] will provide a remedy in the form of an action for damages.”⁷³ A cause of action founded on negligence, which is one category of torts, is comprised of four elements.⁷⁴ The first element is a duty “to conform to a certain standard of conduct, for the protection of others against unreasonable risks.”⁷⁵ The second, a failure of the party to conform to the required standard, is a breach of that duty.⁷⁶ The third is “a

70. City of Woodbury, Minn., *supra* note 65.

71. Email from Ron Glubka, Chief Building Official, City of Woodbury (Feb. 12, 2007) (on file with author).

72. Author’s conclusions from interviews with J. Scott Andresen, Attorney, Bassford Remele in Minneapolis, Minn. (June 6, 2006); Rich Dahl, Attorney, Madigan, Dahl & Harlan, in Minneapolis, Minn. (June 5, 2006); Julie Doherty, Attorney, Fabyanske Westra Hart & Thomson, in Minneapolis, Minn. (June 12, 2006); Brenda Sauro, Attorney, Hammargren & Meyer, P.A., in Edina, Minn. (June 23, 2006); Paul Ellringer, Owner, Air Tamarack, in St. Paul, Minn. (June 16, 2006); Ron Glubka, Chief Building Official, City of Woodbury, in Woodbury, Minn. (July 28, 2006); Kevin Schmieg, Building Official, City of Eden Prairie, in Eden Prairie, Minn. (June 13, 2006).

73. W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 1 (5th ed. 1984).

74. *Id.* § 30.

75. *Id.*

76. *Id.*

reasonably close causal connection between the conduct and the resulting injury.”⁷⁷ The fourth and final element is actual loss or damage resulting to another.⁷⁸ The party asking the legal system for relief has the burden of proof to establish that a duty existed, the duty was breached by the defendant, the breach resulted in an injury or damages to the plaintiff, and the plaintiff is due relief.⁷⁹

Under the doctrine of negligence, the general contractor must exercise reasonable care in the construction of the house.⁸⁰ The homeowner has the burden of proving that the general contractor breached his or her duty of reasonable care, which resulted in personal injuries or property damage, and the homeowner is due relief for those damages.

B. *Contract—Breach of Contract*

The most quoted definition of the term “contract” is that found in Section One of both the First and Second Restatements of Contracts: “A contract is a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty.”⁸¹ Further, “[a] promise may be expressed in the form of a warranty,”⁸² and “[i]f a warranty is made, it is believed that what is being promised and what the promisee is being led to expect on the part of the promisor, is indemnification against loss, in case the facts turn out to be not as represented.”⁸³

“A breach of contract may be large or small, total or partial.”⁸⁴ A contractor may fail to start excavation for the building’s foundation or may erect the entire building per specifications, but fail to use the brand of sewer pipe required by the contract.⁸⁵ In either case, the contractor has committed a breach of contract, but the two breaches are of different size and importance.⁸⁶

77. *Id.* § 30.

78. *Id.*

79. *Id.* § 38.

80. 13 AM. JUR. 2D *Building, Etc., Contracts* § 144.

81. 1 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1.3 (Joseph M. Perillo ed. 1993) (quoting RESTATEMENT (SECOND) OF TORTS § 1 (1965)).

82. *Id.* § 1.14.

83. *Id.*

84. ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS, ONE VOLUME EDITION 925 (1952).

85. *Id.*

86. *Id.*

Nonetheless, where a breach has occurred, “an action can be maintained and the law will give an appropriate remedy.”⁸⁷

When the general contractor and homeowner enter into a contract, a warranty is created.⁸⁸ The general contractor has expressly committed to build a product for the homeowner that meets the specifications attached to the construction purchase agreement. The general contractor must stand behind his or her product.

C. *Breach of Statutory Warranties*

The early American legal system adopted the notion of caveat emptor (“let the buyer beware”) so that there was no liability on the part of a seller of a product to the purchaser.⁸⁹ Over the years, however, considerable pressure for the protection of the consumer resulted in the development of the warranty theory of recovery.⁹⁰ “[This] law, as it stands today, is very largely statutory.”⁹¹ Minnesota addressed consumer complaints surrounding new home construction and home improvement construction in 1977.⁹² Accordingly, the legislature enacted a statute that created warranties for homeowners.⁹³

IV. THE LAW AND RECENT HOMEOWNER CASES

A. *Statutory Law*

Over the years, several states have adopted legislative actions designed to protect homeowners from construction defects in new and remodeled homes.⁹⁴ As noted above, Minnesota adopted a new body of consumer protection law largely focused on home

87. *Id.* at 930.

88. 25 A.L.R. 3D 383 § 5.

89. KEETON ET AL., *supra* note 73, § 95A.

90. *Id.*

91. *Id.*

92. *See* MINN. STAT. §§ 327A.01–.08 (2006).

93. *Id.*

94. ARIZ. REV. STAT. ANN. §§ 12-1361 to -1366 (2001); CONN. GEN. STAT. ANN. §§ 47-116 to -121 (West 2002); IND. CODE ANN. § 32-27-2-8 (West 2007); LA. REV. STAT. ANN. §§ 9:3141–:3150 (2001); MD. CODE ANN., REAL PROP. §§ 10-201 to -205 (West 2003); MINN. STAT. ANN. §§ 327A.01–.08 (West 2004); N.J. STAT. ANN. §§ 46:3B-1 to -20 (West 2003); N.Y. GEN. BUS. LAW § 777-a (McKinney 1996); VA. CODE ANN. § 55-70.1 (2003).

warranties.⁹⁵ These legislative actions are codified in Chapter 327A of the Minnesota Statutes.⁹⁶ The legislative motivation for the statute is best described as “residence protection,” a desire to insulate homeowners from egregious construction defects.⁹⁷

While an examination and analysis of Chapter 327A is not the purpose of this comment, a brief description of the statute is necessary for the reader’s understanding.

Minnesota Statutes section 327A.02 outlines the basis of the statutory warranties that are provided within the law.⁹⁸ Under subdivision 1 of section 327A.02, the general contractor must warranty a new home from the date of closing or passage of title to a homeowner for (a) one year on defects caused by faulty workmanship and defective materials, (b) two years from defects caused by faulty installation of plumbing, electrical, heating, and cooling systems, and (c) ten years from major construction defects.⁹⁹ Subdivision 2 of the statute states that the warranty stays with the dwelling.¹⁰⁰ This provision of the statute provides warranty protection to all owners of the home during the dwelling’s initial ten years.¹⁰¹ Under subdivision 2a, an incorporated or limited liability general contractor is precluded from escaping the warranties through dissolution.¹⁰² Subdivision 3 of the statute extends the warranty to any major structural changes or additions done on the dwelling.¹⁰³ The time limit on the home improvement warranty is extended for one, two, and ten years for new home construction.¹⁰⁴ In the event of a construction defect remediation on the home, the statute restarts or extends the warranty for the

95. *Koes v. Advanced Design, Inc.*, 636 N.W.2d 352, 356–57 (Minn. Ct. App. 2001) (holding that homeowners may bring an action under Minnesota Statutes section 327A.02 after the warranty period expires if the action is brought within the two-year limitations period in Minnesota Statutes section 541.051, subdivision 4 and meets the six-month written notice requirement of Minnesota Statutes section 327A.03(a)).

96. *Id.* at 356.

97. Note, *Minnesota Statutory Warranties on New Homes: An Examination and Proposal*, 64 MINN. L. REV. 413, 430 (1980) (examining the nature and coverage of Minnesota’s Home Warranty statute).

98. See MINN. STAT. § 327A.02 (2006).

99. See *id.* § 327A.02, subdiv. 1(a)–(c).

100. See *id.* § 327A.02, subdiv. 2.

101. See *id.* § 327A.02, subdivs. 1(c), 2.

102. See *id.* § 327A.02, subdiv. 2a.

103. See *id.* § 327A.02, subdiv. 3(a).

104. See *id.* § 327A.02, subdiv. 3(a)–(c).

parts of the dwelling that were repaired.¹⁰⁵ The statute also provides that the homeowner must give the general contractor an opportunity to inspect and repair the construction defect.¹⁰⁶

Another key component of Minnesota Statutes Chapter 327A is section 327A.03, titled “Exclusions.”¹⁰⁷ One important exclusion from recovery falls under this portion of the statute. This exclusion states that the homeowner must notify the general contractor, in writing, within six months after the homeowner discovers or should have discovered the damage or loss.¹⁰⁸ Failure to do so results in an exclusion from recovery under the statute.¹⁰⁹

Finally, the statute of limitations for initiating a construction defect legal action on a home is codified in Minnesota Statutes section 541.051.¹¹⁰ One portion of this statute applies to non-warranty claims,¹¹¹ and a different portion applies to warranty claims.¹¹² The statute of limitations is two years for both types of claims.¹¹³ The application of the limitation, however, is slightly different in each instance.¹¹⁴

B. *Recent Minnesota Homeowner Cases*

As stated earlier, Minnesota’s construction defect claims are typically brought under a breach of statutory home warranty claim or as a non-warranty claim under a negligence or breach of contract cause of action.¹¹⁵ Pursuant to the Minnesota General Rules of Practice, Rule 114, homeowner claims can be mediated.¹¹⁶ Mediated claims are unreported. Additionally, the Minnesota legal

105. *See id.* § 327A.02.

106. *See id.* § 327A.02, subdiv. 4.

107. *Id.* § 327A.03.

108. *See id.* § 327A.03, subdiv. (a):

The liability of the vendor or the home improvement contractor . . . does not extend to . . . loss or damage not reported by the vendee or the owner to the vendor or the home improvement contractor in writing within six months after the vendee or the owner discovers or should have discovered the loss or damage.

Id.

109. *Id.*

110. *See id.* § 541.051.

111. *See id.* § 541.051, subdiv. 1.

112. *See id.* § 541.051, subdiv. 4.

113. *Id.* § 541.051, subdivs. 1, 4.

114. *See id.*

115. *See supra*, Part III.

116. MINN. R. GEN. PRAC. 114 (2006). This rule governs alternative dispute resolution in Minnesota civil cases; *see id.* R. 114.01.

system tracks statistics by case file number and party name(s), which does not make the gathering of homeowner and general contractor construction defect data straightforward. Nonetheless, a few landmark decisions seem to be changing statutory law or developing common law rulings on the subject.

In *Camacho v. Todd & Leiser Homes*, the Minnesota Supreme Court ruled against homeowners who brought a warranty claim because their claim was time-barred.¹¹⁷ Before the homeowners initiated suit, the defendant general contractor had voluntarily dissolved the corporation, time-barring the claim under Minnesota's dissolution statute.¹¹⁸ The Court went on to say that the only remaining entity from which the homeowners could potentially recover damages was the general contractor's insurer.¹¹⁹ But because Minnesota has a longstanding common-law rule that courts will not allow third parties to maintain a direct action against the insurer until the third party has a judgment against the insured, any claim against the insurer would also, therefore, be time-barred.¹²⁰ The court concluded that "[i]t is the province of the legislature, not this court, to provide a remedy to those homeowners who may be foreclosed from bringing an action."¹²¹

While the homeowners did not win their case, the decision prompted the Minnesota Legislature to seriously consider amending the Home Warranty statute.¹²² With the support of other homeowners, plaintiffs' attorneys, and several legislators, the legislature amended the Minnesota Home Warranty statute to preclude incorporated and limited liability general contractors

117. 706 N.W.2d 49, 55 (Minn. 2005). The conflict in this case was between two competing statutes of limitations: the Home Warranty statute with a ten-year limitation would have allowed the homeowners to proceed with their claim, but the Corporate Dissolution statute only had a two-year limitation, which had already passed. See MINN. STAT. § 327A.02, subdiv. 1(c) (2006) (Home Warranty); MINN. STAT. § 302A.7291, subdiv. 3(a) (2006) (Corporate Dissolution); *Camacho*, 706 N.W.2d at 54 (discussing the conflict between the above statutes).

118. *Camacho*, 706 N.W.2d at 52, 55.

119. *Id.* at 56.

120. *See id.* (citation omitted).

121. *Id.* at 55.

122. *See* Senate Judiciary Committee Hearings on Home Warranty Statute, S.F. No. 1287, Mar. 8, 2005 (Judiciary, 00:55:30–02:23:05) & Mar. 22, 2005 (Judiciary Part 2, 00:03:45–02:10:00), available at <http://www.senate.leg.state.mn.us/media/archive/2005/committee/audio/index.shtml#March2005> (last visited Apr. 15, 2007) & Apr. 4, 2006 (Judiciary Part 2, 00:12:00–00:15:00), available at <http://www.senate.leg.state.mn.us/media/archive/2006/committee/audio/index.shtml#April2006> (last visited Apr. 15, 2007).

from escaping warranties through dissolution.¹²³

In *Vlahos v. R&I Construction of Bloomington, Inc.*,¹²⁴ the Minnesota Supreme Court overturned the trial court and the court of appeals decisions and ruled in favor of the homeowners.¹²⁵ The essence of the lower courts' rulings was that the statute of limitations barred the Vlahoses' claim because the previous homeowners had discovered the water problems more than two years before the Vlahoses commenced their action, and the previous owners' knowledge of the water problems could be imputed to the Vlahoses.¹²⁶ The supreme court, however, found that the statute of limitations begins to run not from the discovery of the *defect* but from the point at which the homeowner "discovers or should have discovered, the builder's refusal or inability to ensure the home is free from major construction defects."¹²⁷ Consequently, the court held that summary judgment was inappropriate.¹²⁸ And the court also clarified that a "major construction defect" in the home warranty statute¹²⁹ extends to damage to load-bearing portions of the dwelling occurring after the completion of construction.¹³⁰ The general contractor in this case, as well as general contractors in previous cases, argued that the definition required the defect both to exist at the time construction was completed and to persist thereafter.¹³¹ This ruling clarified the term "major construction defect" contained in the

123. See Act of 2006, ch. 202, §§ 5–6, 2006 Minn. Laws 110 (amending MINN. STAT. § 327A.02, subdiv. 2(a) (2004)).

124. 676 N.W.2d 672 (Minn. 2004).

125. *Id.* at 677. The issue in this case concerned another statute of limitations that bars claims two years after the homeowner has "discovered" the problem. See MINN. STAT. § 541.051, subdiv. 4 (2002).

126. *Vlahos*, 676 N.W.2d at 676; see also *Vlahos v. R&I Constr. of Bloomington, Inc.*, 658 N.W.2d 917, 921 (Minn. Ct. App. 2003).

127. *Vlahos*, 676 N.W.2d at 678. The court's holding was based on its decision that the applicable statute of limitations was contained in Minnesota Statutes section 541.051, subdivision 4, providing for the bringing of an action within two years of the discovery of the *breach of statutory warranty*, as opposed to section 541.051, subdivision 1, which provided that the cause of action accrued upon discovery of the *injury*. *Id.* at 677. This case also partially overruled *Hyland Hill North Condo Ass'n v. Hyland Hill Co.*, 549 N.W.2d 617 (Minn. 1996), which failed to apply subdivision 4 to a breach of statutory warranty claim and instead applied subdivision 1. *Vlahos*, 676 N.W.2d at 677.

128. *Vlahos*, 676 N.W.2d at 677.

129. See MINN. STAT. § 327A.02, subdiv. 1(c) (2006).

130. *Vlahos*, 676 N.W.2d at 681.

131. *Id.* at 680.

Minnesota Home Warranty statute.¹³²

In *Fuhr v. D.A. Smith Builders, Inc.*,¹³³ a trial court granted summary judgment against homeowners, the Fuhrs, on the ground that the statute of limitations barred their home warranty claim.¹³⁴ The Minnesota Court of Appeals, however, found that material facts were in dispute as to whether the moisture intrusion in question was a new injury, or was identical to a claim that the Fuhrs previously brought in conciliation court, and partially reversed the grant of summary judgment.¹³⁵ The court did, however, confirm the trial court's grant of summary judgment as to the Fuhrs' breach of statutory warranty claim because it agreed there was no factual dispute that the Fuhrs did not provide written notice to the home builder within the statutory period.¹³⁶

In 1998, the Fuhrs noticed and repaired damage to sheetrock apparently caused by water leaking through the below-grade stucco on the outside of their house.¹³⁷ In 2002, the Fuhrs again found water damage in their home and subsequently learned they had severe mold problems throughout the house.¹³⁸ They sued their homebuilder in order to recover the costs of repairing the extensive mold damage.¹³⁹ The trial court ruled that the Fuhrs' claim for moisture intrusion was time-barred because the statute of limitations began to run in 1998, when they first discovered a water damage problem.¹⁴⁰ The court of appeals noted the rule that "[i]f an injury is continuous and becomes more serious without appearing to be corrected, the limitations period begins to run upon the initial discovery"¹⁴¹ but held there was a question of fact as to whether the subsequent damage found in 2002 was part of the

132. *Id.* at 681. The court applied the plain meaning of the words of the statute and held that "subject to the specifically enumerated exclusions and exceptions provided in MINN. STAT. § 327A.03, the definition of 'major construction defect' in the statutory new home warranty extends to actual damage to load-bearing portions of the dwelling occurring after the completion of construction." *Id.*

133. No. A04-2457, 2005 WL 3371035 (Minn. Ct. App. Dec. 13, 2005), *rev. denied*, 2006 Minn. LEXIS 133 (Mar. 14, 2006).

134. *Id.* at *2.

135. *Id.* at *4.

136. *Id.* at *5; *see also* MINN. STAT. § 327A.03(a) (2006) (requiring written notice within six months of discovery of damage).

137. *Fuhr*, 2005 WL 3371035, at *1.

138. *Id.*

139. *Id.* at *2.

140. *Id.* at *3.

141. *Id.*

same or a different injury.¹⁴² Nonetheless, the court of appeals affirmed and upheld the trial court's dismissal of the homeowners' breach of statutory warranty claim because the homeowners did not provide written notice to the general contractor within six months after discovering the mold and moisture damage problem.¹⁴³

In many cases, homeowner suits continue to be frustrated by the strict time limitations and requirements for written notification to the general contractor. In a 2006 case, *Collins v. Buus*,¹⁴⁴ the Minnesota Court of Appeals affirmed the trial court's conclusion that the Collinses could not maintain an action for breach of statutory warranty because they failed to provide the general contractor with written notice of the construction problem within six months after discovery.¹⁴⁵ This finding was in spite of evidence in the record indicating that the homeowners did notify the general contractor via an oral conversation.¹⁴⁶ The general contractor, in turn, notified his insurer, who sent a claims representative to the Collinses' home to investigate the claim, interview them, transcribe their statements into a written report, and deliver the report to the insurer.¹⁴⁷ Judge Minge pointed out in his dissent that "the insurer had taken initial responsibility for handling the claim and the insurer was acting on behalf of [the general contractor]."¹⁴⁸ Judge Minge also believed that "the statute does not require that the writing is physically prepared by the homeowner," and he concluded that "the technical requirements of the statute [were] met."¹⁴⁹

C. Challenges of Homeowner Cases

The above cases are examples of the complexities homeowners and general contractors encounter when addressing construction defect problems. Long before the case ever gets to court, several

142. *Id.* The court noted that "summary judgment should not be granted when the homeowner initially discovers a problem and takes corrective action that is apparently appropriate to fix the defect, and then a new injury appears and there is evidence that the new injury is different in kind, location, cause, and appropriate corrective action." *Id.*

143. *Id.* at *5.

144. No. A05-1771, 2006 WL 1985431 (Minn. Ct. App. July 18, 2006).

145. *Id.* at *2.

146. *Id.* at *2-3.

147. *Id.* at *3 (Minge, J., dissenting).

148. *Id.*

149. *Id.*

scenarios will likely play out. The scenario often begins with the homeowner telephoning the general contractor about a construction defect problem the homeowner discovers in his or her home.¹⁵⁰

In the best-case scenario, the general contractor visits the home, investigates the problem, diagnoses the problem as minor, and repairs it. In many instances, the homeowner later has another problem. Again the general contractor responds and investigates the problem but now discovers the home has a mold and moisture intrusion problem with damage to the structure. If the general contractor has sufficient assets and has a small number of homes with moisture problems, the general contractor is likely to simply repair the problems in order to protect his or her reputation and relationship with customers. But if the general contractor built homes between 1990 and 2000 in the fast-growing suburbs, the general contractor may have a larger number of homes with moisture problems and structural damage. Hence, the general contractor likely would not have the financial wherewithal to remedy the problem without involving his or her insurance company. The general contractor's insurance company must be notified, allowed to manage the investigation, facilitate discussions with subcontractors and window manufacturers, and prepare a settlement offer. This adds another level of complexity as well as requiring additional time to solve the problem because more parties are involved. As one might expect, each of these parties wants the opportunity to prove that its product or workmanship did not cause the moisture problem. In the best-case scenario, the homeowner is offered and accepts a settlement that will completely repair the home. But it often takes six to twelve months to get through this part of the process. Then, the homeowner and general contractor sign a settlement release and repair contract and begin the repair process. Depending on the general contractor's schedule, the repair of the home may take another six to eight months.

150. The facts in the following paragraph are hypothetical and based on the author's conclusions from interviews with J. Scott Andresen, Attorney, Bassford Remele, in Minneapolis, Minn. (June 6, 2006); Rich Dahl, Attorney, Madigan, Dahl & Harlan, in Minneapolis, Minn. (June 5, 2006); Julie Doherty, Attorney, Fabyanske Westra Hart & Thomson, in Minneapolis, Minn. (June 12, 2006); Brenda Sauro, Attorney, Hammargren & Meyer, P.A., in Edina, Minn. (June 23, 2006); Barb Goodwin, State Representative, Minnesota House of Representatives, in Minneapolis, Minn. (June 12, 2006).

In the worst-case scenario, the general contractor either does not respond to the homeowner or the general contractor responds, but his or her insurance company is slow to respond or ineffective in investigating the problem, pulling in the subcontractors and window manufacturers, and developing a comprehensive settlement offer. Out of frustration, the homeowner may either accept the settlement offer, paying any additional repair costs out-of-pocket, or the homeowner may file a legal claim with the hope of obtaining a better settlement offer.¹⁵¹

As one might imagine, numerous scenarios exist between these best- and worst-case scenarios. If the homeowner was not aware of the strict legal time limitations or the legal written notice requirements that apply to construction defect claims, the homeowner may not have taken the appropriate steps along the way to preserve his or her legal rights. Consequently, the homeowner may file a legal claim, only to find that the case is time-barred and no legal remedy is available. In contrast, the homeowner may find that the case is meritorious, but because the courts are still grappling with interpreting moisture intrusion cases,¹⁵² the homeowner may need to appeal the case to higher courts in order to obtain a legal remedy.

Furthermore, once the homeowner makes the decision to consult an attorney or file a legal cause of action, he or she starts incurring attorney fees and other associated fees. Under Minnesota law, each party to a civil lawsuit pays his or her own attorney fees unless a statute or contract provides otherwise.¹⁵³ The Minnesota Home Warranty statute does not contain any provisions for awarding attorney fees or other associated fees as part of the homeowner's remedy.¹⁵⁴ At the conclusion of all this activity, the homeowner may get a legal remedy that is sufficient to cover the

151. *Id.*

152. Author's conclusions from interviews with J. Scott Andresen, Attorney, Bassford Remele in Minneapolis, Minn. (June 6, 2006); Rich Dahl, Attorney, Madigan, Dahl & Harlan, in Minneapolis, Minn. (June 5, 2006); Julie Doherty, Attorney, Fabyanske Westra Hart & Thomson, in Minneapolis, Minn. (June 12, 2006); Brenda Sauro, Attorney, Hammargren & Meyer, P.A., in Edina, Minn. (June 23, 2006); *see also* Vlahos v. R&I Constr. of Bloomington, Inc., 676 N.W.2d 672 (Minn. 2004); *supra* Part IV.B.

153. *Barr/Nelson, Inc. v. Tonto's, Inc.*, 336 N.W.2d 46, 53 (Minn. 1983) (citing *Jacobs v. Rosemount Dodge-Winnebago South*, 310 N.W.2d 71, 79 (Minn. 1979)); *see also* MINN. STAT. § 327A.05 (2006) (discussing the remedies).

154. Author's conclusions from interviews cited *supra* note 150; *see also* MINN. STAT. §§ 327A.01–.08 (2006).

construction defect repairs. The homeowner, however, must also pay his or her attorney fees and other associated fees out of the settlement offer. Therefore, the homeowner still does not emerge financially whole.¹⁵⁵

V. RECOVERY THEORIES FOR CONSTRUCTION DEFECT CLAIMS

A. *Recovery Theories—Defined*

In many cases where an individual sustains a loss at the hands of another party, that individual must seek a funding source in addition to the injuring party in order to be fully compensated for the loss. In the case where Party *B* accidentally rear-ends Party *A*, Party *A* may file suit and obtain a judgment against Party *B*. And though the judgment requires Party *B* to compensate Party *A* for the losses resulting from the accident, Party *A* is unlikely to obtain recovery of those losses if Party *B* has no insurance (and has no significant personal assets). While this example is greatly oversimplified, the necessity of locating an outside funding source to compensate the injured party for its loss applies is a critical aspect of managing construction defect claims.

All of the homeowners, general contractors, subcontractors, and product manufacturers embroiled in the Minnesota construction defect morass are looking for a funding source in order to be compensated for losses caused by this problem. Homeowners are currently looking to the general contractors and to their own homeowner's insurance policies for recompense. General contractors are looking to their own insurance policies, the subcontractors and their insurance policies, and the product manufacturers and their insurance policies for recompense.

The rest of this Part of the Comment explores and explains four recovery theories or funding sources available to recompense homeowner's construction defect claims: commercial general liability insurance policies, homeowner's policies, the Minnesota Contractor's Recovery Fund, and Quadriga Builders Insurance. Of these recovery theories, Commercial General Liability insurance policies are currently the predominant funding source for mold and moisture intrusion construction defect claims.¹⁵⁶

155. Author's conclusions from interviews cited *supra* note 150.

156. Author's conclusions from interviews cited *supra* note 152.

B. Commercial General Liability Policies

Historically, general contractors and subcontractors have carried insurance coverage for liability claims under Commercial General Liability (CGL) policies. The basic insuring agreement of the CGL policy is that the insurance company will pay, on behalf of the general contractor or subcontractor, all claims that the general contractor or subcontractor becomes legally obligated to pay as damages because of bodily injury or property damage caused by an occurrence during the policy period.¹⁵⁷ The claims that arise are typically initiated by the homeowner, who is not a party to the general contractor or subcontractor's insurance policy.¹⁵⁸

1. Occurrences and Trigger Theories

Under the CGL policy, the date of the occurrence is very important.¹⁵⁹ The concept of an occurrence is also complicated because it can be considered a single event, such as the installation of a defective product, or it can be considered continuous, such as damage or injury that occurs to areas surrounding the defective product.¹⁶⁰ While the event need not happen during the policy period, the result of the event must happen during the policy period.¹⁶¹ In the case of a construction defect claim, the claim can result from a single event, such as the installation of defective stucco, or from the damage caused by continuous wetting over a period of time.¹⁶²

Each instance of injury or damage is an occurrence that may trigger a general contractor's or subcontractor's entitlement to benefits.¹⁶³ To date, American courts have provided four different

157. See ROBERT H. JERRY II, UNDERSTANDING INSURANCE LAW § 65(a) (2nd ed. 1996).

158. See *id.* § 51(a) (discussing the scope of obligations and how to identify the insured).

159. See *id.* § 65(e).

160. *Id.* § 65(d).

161. *Id.*

162. *Kootenia Homes v. Federated Mut. Ins.*, No. A05-278, 2006 WL 224162 (Minn. Ct. App. Jan. 31, 2006) (holding that damage was result of single, identifiable event of installation of faulty stucco), *rev. denied*, 2006 Minn. LEXIS 227 (Apr. 18, 2006); *Wooddale Builders, Inc. v. Maryland Cas. Co.*, 722 N.W.2d 283 (Minn. 2006) (holding that that damage was the result of continuous wetting and progressive damage and that damages were to be allocated among all insurers on risk from closing to date when insured received notice of claim).

163. JERRY, *supra* note 157, § 65(e).

trigger theories to determine which policies were on the risk: the manifestation rule, the exposure rule, the actual injury rule, and the multiple events (or continuous) rule.¹⁶⁴ The manifestation rule limits coverage only to those policies in effect when the damage or injury was discovered.¹⁶⁵ The exposure rule extends liability to the policies in effect when the property or claimant was exposed to the damaging or injurious substances.¹⁶⁶ The actual injury rule triggers the coverage of the policies in effect when the damage or injury occurred or was initiated.¹⁶⁷ The continuous rule combines aspects of the above-mentioned approaches and views the damage or injury as progressive.¹⁶⁸ All insurance companies that provided coverage are potentially on the risk for the period of time the respective policy was in effect.¹⁶⁹ Each insurance company is allocated damages relative to the total number of years coverage was provided.¹⁷⁰

Minnesota adopted the actual injury rule in 1976 in *Singsaas v. Diederich*¹⁷¹ when the court wrote, “[W]hile it is arguable that the liability of the insurer should attach at the time of the negligent act, the proper rule seems to be that the liability accrues when the cause of action arises.”¹⁷²

Because occurrences and trigger theories are complicated where a single injurious event is not readily identifiable, the Minnesota Court of Appeals in 1987 broadened its interpretation of the “actual injury rule.”¹⁷³ In *Industrial Steel Container v. Fireman’s Fund*,¹⁷⁴ the court recognized that situations may arise in which

164. *Id.*

165. *Id.*

166. *Id.*

167. *Id.*

168. *Id.*

169. *Id.*

170. *Id.*

171. 238 N.W.2d 878 (Minn. 1976). An injured worker brought an action against a construction company for bodily injuries suffered after cancellation of the CGL policy, although the injuries were caused by negligent work performed while the policy was still in effect. *Id.* at 879–80. The court held that the CGL policy did not provide coverage for injuries resulting after the policy was cancelled. *Id.* at 880.

172. *Id.* at 882 (quoting *Home Mut. Fire Ins. Co. v. Hosfelt*, 233 F. Supp. 368, 370 (D. Conn. 1962)).

173. *See Indus. Steel Container v. Fireman’s Fund Ins. Co.*, 399 N.W.2d 156 (Minn. Ct. App. 1987) (holding that there can be more than one occurrence where property damage results from continuous, long exposure to a toxic substance and that more than one policy can be on the risk).

174. *Id.*

there is more than one occurrence of injury because “property damage result[ed] from continuous or repeated conditions of exposure.”¹⁷⁵ The court held that all policies on the risk during the time of continuous exposure were triggered.¹⁷⁶ The Minnesota Supreme Court solidified this broad interpretation of the “actual injury” rule in *Northern States Power Co. v. Fidelity & Casualty Co. of New York*¹⁷⁷ by applying a “pro rata by time on the risk” allocation scheme to apportion damages.¹⁷⁸ Then, in *In re Silicone Implant Insurance Coverage Litigation*,¹⁷⁹ the court affirmed Minnesota’s use of the actual injury rule,¹⁸⁰ but found allocating risk to be reserved for difficult cases in which the injury’s origin could not be readily identified.¹⁸¹ The Court held that the injury was a “readily identifiable discrete event” and that liability should not be allocated.¹⁸²

2. Business Risk Doctrine and Exclusions

The CGL policy also looks to the business risk doctrine for interpretation.¹⁸³ This doctrine, which further complicates policy interpretation, states that defective workmanship is not insurable and that general contractors should manage their operations accordingly.¹⁸⁴

The Minnesota Supreme Court first discussed the relationship between the business risk doctrine and CGL policies in *Bor-Son Building Corp. v. Employers Commercial Union Insurance Co. of America*¹⁸⁵ and *Knutson Construction Co. v. St. Paul Fire & Marine*

175. *Id.* at 159.

176. *Id.*

177. 523 N.W.2d 657, 664 (Minn. 1994) (finding that actual injury was “continuous from the point of the first damage to the point of discovery or cleanup”).

178. *Id.* at 663.

179. 667 N.W.2d 405 (Minn. 2003) (finding insurance policies were triggered at the time of silicone gel breast implantation).

180. *Id.* at 416.

181. *Id.* at 421.

182. *Id.* at 422.

183. See Roger C. Henderson, *Insurance Protection for Products Liability and Completed Operations: What Every Lawyer Should Know*, 50 NEB. L. REV. 415, 434–41 (1971).

184. See *id.* at 438.

185. 323 N.W.2d 58, 63 (Minn. 1982) (holding that damages resulting from faulty workmanship in the performance of contracts were not within the coverage of the CGL policy).

*Insurance Co.*¹⁸⁶ In *Bor-Son*, the court said that the general contractor should ensure that quality products and services are supplied to their construction projects and that the consequence of not performing well is part of the business venture.¹⁸⁷ The court ruled that the cost of replacement or repair of faulty products and services is a business expense borne by the general contractor and is not the type of risk against which the CGL policy was meant to insure.¹⁸⁸ In *Knutson*, the court ruled in a similar fashion and went on to say that covering such business expenses presents an incentive for the general contractor to be less diligent in completing a project in a good, workmanlike manner.¹⁸⁹

But in later decisions, Minnesota courts made clear that *Bor-Son* and *Knutson* do not “serve as the foundation for a separate ‘business risk doctrine’ that operates to override the express language of policy exclusions.”¹⁹⁰ In *O’Shaughnessy v. Smuckler Corp.*,¹⁹¹ the court explained that under the express language of the policy’s exclusions, damage to the general contractor’s work is covered under the CGL policy if the damage results from work done by a subcontractor.¹⁹² In *Thommes v. Milwaukee Insurance Co.*,¹⁹³ the Minnesota Supreme Court held that a general contractor’s CGL policy provided coverage because the parties’ intent to exclude third-party property damage was not clearly and unambiguously demonstrated in the policy’s exclusions.¹⁹⁴ Finally, the Minnesota Supreme Court decided in *Wanzek Construction, Inc. v. Employers Insurance of Wausau*¹⁹⁵ that the general contractor’s

186. 396 N.W.2d 229, 234–35 (Minn. 1986) (finding that building damage caused by general contractor’s faulty workmanship or use of defective materials was business risk to be borne by contractor).

187. *Bor-Son*, 323 N.W.2d at 64 (quoting *Weedo v. Stone-E-Brick, Inc.*, 405 A.2d 788, 791 (N.J. 1979)).

188. *Id.*

189. *Knutson*, 396 N.W.2d at 234.

190. *Thommes v. Milwaukee Ins. Co.*, 641 N.W.2d 877, 880 (Minn. 2002).

191. 543 N.W.2d 99 (Minn. Ct. App. 1996).

192. *Id.* at 104.

193. 641 N.W.2d 877 (Minn. 2002).

194. *Id.* at 883 (Minn. 2002). The court further read the phrase “incorrectly performed” to mean work performed in a faulty or defective way. *Id.* at 883–84 (construing against the insurer the ambiguity of whether “incorrectly” meant faulty work or work performed on the wrong property). And since damage to a third party resulted from performing work in the wrong place, as opposed to performing the work in a defective manner, the court found the “incorrectly performed” exclusion inapplicable. *Id.*

195. 679 N.W.2d 322 (Minn. 2004).

business risk was determined by the express terms of the insurance contract¹⁹⁶ and that the policy did not exclude subcontractor work.¹⁹⁷

The history of Minnesota insurance law and policy interpretation is very important to construction defect claims. As stated earlier, CGL policies are currently the predominant funding source for construction defect claims. Equally important is the theory used to interpret the policy, because the theory helps to determine a homeowner's remedy.

3. *Trigger Theory Analysis*

Suppose, for example, that a general contractor builds homes for eight homeowners in the same calendar year. Six years after the homes are complete, all eight homeowners file claims for moisture intrusion. The total amount of each claim is \$150,000.

Now suppose that the court applies the actual injury rule, as in *In re Silicone*¹⁹⁸ and *Kootenia Homes*.¹⁹⁹ This would mean that only the CGL policy in effect at the time the homes were built, and a defective product was installed, is on the risk. Also, suppose the general contractor's CGL policy in effect at that time had an annual limit of \$1,000,000. The total amount claimed by all eight of the homeowners is \$1,200,000. This means the last homeowner to file a claim will not receive a remedy and the second-to-last homeowner will only receive a \$100,000 remedy.

In contrast, suppose the court applies the actual injury rule with pro-rata time on the risk allocation, as in *NSF*²⁰⁰ and *Wooddale Builders*.²⁰¹ This means all of the CGL policies in effect from the date the homes are built and the defective product is installed, up to the date the moisture intrusion damage is discovered, are on the risk. In this instance, suppose the general contractor has the following policies over the six-year period: year one, a policy with

196. *Id.* at 327.

197. *Id.* at 329 (construing the definition of "subcontractor" in favor of providing coverage).

198. *In re Silicone Implant Ins. Coverage Litig.*, 667 N.W.2d 405 (Minn. 2003); *see supra* note 179.

199. *Kootenia Homes v. Federated Mut. Ins.*, No. A05-278, 2006 WL 224162 (Minn. Ct. App. Jan. 31, 2006); *see supra* note 162.

200. *N. States Power Co. v. Fid. & Cas. Co. of N.Y.*, 523 N.W.2d 657 (Minn. 1994); *see supra* note 177.

201. *Wooddale Builders, Inc. v. Maryland Cas. Co.*, 722 N.W.2d 283 (Minn. 2006); *see supra* note 162.

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XYZ insurance company; year two through five, a policy with ABC insurance company; and year six, a policy with HJK insurance company. Again, assume the annual limit of each policy is \$1,000,000. In this case, all eight homeowners will receive a remedy because the risk is allocated across all three insurance companies over the period of time that the damage caused by continuous wetting was occurring. For simplicity, assume all eight homeowners discover the moisture intrusion damage in year six. Each homeowner will receive a settlement of \$25,000 from XYZ insurance company, \$100,000 from ABC insurance company, and \$25,000 from HJK insurance company.

This example is *greatly* oversimplified. Typically, the general contractor, the framer, the stucco or other cladding installer, and the window manufacturers *all* have CGL policies that come into play. Additionally, the remedy may also be affected by how broadly or narrowly the court interprets exclusions in the CGL policy in connection with the business risk doctrine. But this example is a representation of the policy interpretation and legal mathematics with which the courts are grappling in recompensing mold and moisture intrusion construction defect claims.

4. *Implications*

Until the Minnesota Supreme Court has the opportunity to issue an unambiguous ruling on CGL policies as applied to construction defect claims, decisions on the topic will continue to be a moving target. Mold and moisture intrusion claims are extremely complex and emotional for homeowners, general contractors, and subcontractors. Consequently, each party uses the above-mentioned case law and policy interpretations to argue its case in the most beneficial way.

Finally, although CGL policies have always contained exclusions, as a result of the number and magnitude of construction defect claims, insurance companies are adding policy endorsements that narrow or eliminate coverage for a general contractor's construction defect claims.²⁰² These endorsements contain exclusions that range from total elimination of coverage for construction defect claims to elimination of coverage for work

202. See Timothy P. Tobin, *Update on Commercial General Liability Policy Coverage Issues*, in RESIDENTIAL CONSTRUCTION DEFECT CLAIMS § 1, at A-1 to -3 (Minn. Continuing Legal Educ. ed., May 2006).

performed by a subcontractor on behalf of the general contractor, elimination of coverage for mold-related claims, and elimination of coverage for claims that should have been known by the general contractor when a new policy first became effective.²⁰³

C. *Homeowner's Policies*

Homeowner's property insurance is designed to protect homeowners from the risks and activities associated with owning a home.²⁰⁴ Standard homeowner policies typically contain exclusions for errors, omissions, and defects that would apply to negligent construction and exclusions for wear and tear that would apply to wet or dry rot and mold.²⁰⁵ Homeowners' policies were not designed to protect homeowners from water intrusion damage to their homes.²⁰⁶ But out of frustration with the general contractors, subcontractors, product manufacturers, and CGL policies' recovery remedies, homeowners are turning to their own insurance companies for reimbursement on the damages to their home.²⁰⁷

In two recent Minnesota cases, the homeowners brought claims against their insurance companies and prevailed at the trial court level. In *Bloom v. Western National Mutual Insurance Co.*,²⁰⁸ the trial court found the homeowner's policy language ambiguous and determined that damages resulting from rot and mold were not excluded because they were covered as ensuing losses.²⁰⁹ But the Minnesota Court of Appeals reviewed the case, reversing the trial court's order and concluding that damages from water intrusion were excluded from coverage under the "errors, omissions, and defects" or "wear and tear" exclusions.²¹⁰

On the other hand, the United States District Court for the District of Minnesota, in *Buscher v. Economy Premier Insurance Co.*,²¹¹ concluded that the construction defect exclusion did not exclude coverage for water loss or mold that resulted from the covered

203. *Id.*

204. See JERRY, *supra* note 157, § 13(c).

205. Julian C. Janes, *First Party Coverage for Residential Construction Defect Damages*, in RESIDENTIAL CONSTRUCTION DEFECT CLAIMS § 2, at 4 (Minn. Continuing Legal Educ. ed., May 2006).

206. *Id.* at 1.

207. *Id.*

208. No. A05-2093, 2006 WL 1806415, at *3 (Minn. Ct. App. July 3, 2006).

209. *Id.* at *3.

210. *Id.* at *5.

211. No. 05-544, 2006 WL 268781 (D. Minn. Feb. 1, 2006).

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water loss.²¹² Both cases, however, are unpublished opinions, so it is yet unclear whether any Minnesota courts will find them persuasive.

D. Minnesota Contractor's Recovery Fund

In 1994, Minnesota created the Contractor's Recovery Fund (Fund).²¹³ From a regulatory perspective, the Fund was designed to regulate licensed contractors engaging in construction activities that require a license, contractors engaging in construction projects without obtaining the proper building permits, and other similar actions.²¹⁴ From a consumer perspective, the Fund's purpose is to compensate residential property owners or renters who have lost money due to a licensed contractor's fraudulent, deceptive, or dishonest practices, conversion of funds, or failure to perform.²¹⁵

The contributions to the Fund are collected from Minnesota's licensed contractors through fines and fees.²¹⁶ In order to build or remodel residential property, a contractor must be licensed.²¹⁷ As a part of the annual license renewal requirements, the contractor must pay an annual fee into the Fund.²¹⁸ The contractor's annual fee payment is based on the contractor's gross receipts for the previous fiscal year.²¹⁹ Fines collected result from levies against contractors as a result of consumer complaints.²²⁰

The Commissioner of Labor and Industry administers the Fund.²²¹ The Fund is limited and restricts the dollar amount of losses that are eligible for reimbursement.²²² A homeowner

212. *Id.* at *5. The federal district court noted, however, that the policy excluded claims attributable to the cost of correcting defective workmanship. *Id.* at *6.

213. See MINN. STAT. § 326.975, subdiv. 1(a) (2006).

214. Author's conclusions from email from Charlie Durenberger, Manager, Enforcement Servs., Minn. Dep't of Labor and Indus. (July 27, 2006) (on file with author).

215. See MINN. STAT. § 326.975, subdiv. 1(a)(2).

216. Author's conclusions from email from Charlie Durenberger, Manager, Enforcement Servs., Minn. Dep't of Labor and Indus. (July 26, 2006) (on file with author); see also MINN. STAT. § 326.975, subdiv. 1(a)(1).

217. See *supra* Part II.C.

218. See MINN. STAT. § 326.975, subdiv. 1(a).

219. *Id.* § 326.975, subdiv. 1(a)(1).

220. E-mail from Charlie Durenberger, *supra* note 216.

221. How the Fund Works, http://www.doli.state.mn.us/pdf/rbc_contractors_recoveryfund.pdf, (last visited April 6, 2007).

222. See MINN. STAT. § 326.975, subdiv. 1(a)(3).

applying to the Fund may be paid up to \$50,000.²²³ But no more than \$75,000 may be paid from the Fund on behalf of any one licensed contractor.²²⁴ If the total amount of valid claims against a contractor exceeds \$75,000, the reimbursement amounts are prorated. For example, suppose five homeowners file valid claims of \$100,000 each against a contractor. Each homeowner would receive a reimbursement award of \$15,000.

In order for a homeowner to obtain a reimbursement award from the Fund, the homeowner must obtain a judgment against the licensed contractor.²²⁵ The homeowner can apply to the Fund for losses actually incurred as a result of a licensed contractor's fraudulent, deceptive, or dishonest practices, conversion of funds, or failure to perform. The statute governing the Fund, however, does not make any provisions for reimbursement of attorney's fees, court costs, or other costs associated with applying to the Fund.

A small number of homeowners submit mold and moisture intrusion construction defect claims to the Fund. Due to the statutory limit on losses available from the Fund and the typical loss amount of a mold and moisture intrusion claim, the Fund is not very useful for these claims.²²⁶ The Fund was designed and adopted before the mold and moisture construction defect problems began surfacing.²²⁷ While there has been no formal research into changing the premise of the Fund, there has been limited support for such a change.²²⁸ The biggest stumbling block to such a change is the need to increase the payout limits of the Fund, which in turn requires larger contributions from contractors.²²⁹

E. Minnesota Builders Risk Retention Group—Quadriga

In November 2005, the Builders Association of Minnesota (Association) created Quadriga Builders Insurance (QBI),²³⁰ a risk retention group designed to provide general contractors with a more comprehensive liability insurance option at an affordable

223. *Id.*

224. *Id.*

225. *See id.* § 326.975, subdiv. 1(a)(2)(i).

226. Author's conclusions from email from Charlie Durenberger, Manager, Enforcement Servs., Minn. Dep't of Labor and Indus. (July 31, 2006) (on file with author).

227. *Id.*

228. *Id.*

229. *Id.*

230. *See* Quadriga Builders Insurance, <http://www.qbimn.org>.

price.²³¹ QBI is a replacement CGL policy that was born out of the general contractors' frustration with steeply rising insurance costs and recently expanded or added exclusions that restricted the existing CGL coverage.²³²

The Association did not take the development or introduction of QBI lightly.²³³ It spent eighteen months planning, developing, and securing regulatory approvals and financing for QBI.²³⁴ While the Association estimates that "less than one percent of the homes built in Minnesota since 1990 may fail,"²³⁵ it also recognizes that, because of the impact the mold and moisture intrusion problem has on people's homes, the problem has been harmful to many of the Association member's reputations.²³⁶

QBI requires each general contractor who purchases a policy to adhere to the required building practices of the QBI agreement.²³⁷ The building practices of the QBI agreement address many of the products and practices that caused or contributed to the existing mold and moisture construction defect problem.²³⁸ QBI considers the monitoring and enforcement of these required building practices a very serious business concern.²³⁹ Consequently, each QBI policyholder must agree to an annual three-hour interview with a risk management consultant, as well as three annual, unannounced jobsite investigations.²⁴⁰ If a general contractor fails repeated investigations and refuses to obtain the continuing education that would help the general contractor understand and integrate the required building practices, QBI will deny the general contractor's claims or drop the general contractor's coverage.²⁴¹ To date, most general contractors have been very willing to adopt QBI's required building practices and, if

231. Author's conclusions from e-mail from Pam Perri Weaver, Executive Vice President, Builders Ass'n of Minn. (July 28, 2006) (on file with author); interview with Pam Perri Weaver, in St. Paul, Minn. (June 29, 2006).

232. E-mail and interview with Pam Perri Weaver, *supra* note 231.

233. *Id.*

234. *Id.*

235. *Id.*

236. *Id.*

237. *Id.* For QBI-required building practices, see *Special Report: Minnesota's Rotting Stucco Walls*, ENERGY DESIGN UPDATE, May 2006, reprinted in MINN. BUILDER, Summer 2006, at 32, 38.

238. E-mail and interview with Pam Perri Weaver, *supra* note 231.

239. *Id.*

240. *Id.*

241. *Id.*

necessary, to alter their own building practices.²⁴²

As an added incentive, each general contractor who holds a QBI policy has an ownership stake in QBI.²⁴³ In the first year of the general contractor's policy, the general contractor is required to pay a policy premium and purchase QBI stock.²⁴⁴ In the end, if QBI is successful, the general contractors who are policyholders will realize a return on their investment.²⁴⁵ This return on the general contractors' investment will be twofold: first, and perhaps most importantly, the general contractor will realize a rehabilitation of his or her reputation; second, the general contractor will realize an increase in his or her investment assets.

VI. RECOMENDATIONS

Generally, society and public policy frown on consumers being disadvantaged or harmed. Yet there are numerous stories of homeowners caught in the tangle of construction defect litigation.²⁴⁶ Although homeowners are not the only injured parties, this information does seem to indicate that the current approach to solving mold and moisture intrusion construction defect claims is not working very well. The following recommendations are proposals that, while not comprehensive solutions, are intended to open a dialogue that will allow homeowners and homebuilders to begin addressing these problems.

A. *Develop a "Step Up" Program*

Most homeowners do not want adversarial relationships with their general contractors. Similarly, the homeowners do not want

242. *Id.*

243. *Id.*

244. *Id.*

245. *Id.*

246. See Dee DePass, *Exposed to the Elements*, STAR TRIB. (Minneapolis), Apr. 15, 2006, at H1; KARE-11 News: *A Quirk in the Law that Could Cost Homeowners Everything* (KARE-11 Minneapolis television broadcast Feb. 2, 2006), available at http://kare11.com/news/news_article.aspx?storyid=117836 (last visited March 22, 2007); Larry Wills, *Broken Homes: Legislature Will Host Heated Debate over Construction Defect Law*, LAS VEGAS MERCURY, Jan. 30, 2003, available at <http://www.lasvegasm Mercury.com/2003/MERC-Jan-30-Thu-2003/20551900.html>; CONSUMER REPORTS, *Housewrecked: Serious Hidden Defects Plague Many Newer Homes* (Jan. 2004), <http://www.consumerreports.org/cro/personal-finance/shoddy-home-construction-104/overview/index.htm>.

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to litigate in order to obtain settlement offers that will repair the mold and moisture intrusion problems in their homes. But many homeowners are finding they have no other options.

General contractors, subcontractors, product manufacturers, insurance companies, and their legal counsel should pull together and develop a mandatory "Step Up" program. The key premise of a "Step Up" program is for the homeowners to get their homes repaired without all of the above-mentioned parties spending time and money establishing fault.

Given the history of the Minnesota mold and moisture intrusion problem, most general contractors probably have a good idea of how many "problem homes" they have, where those homes are located, and when they were built. Arguably such a program would be costly. But it may not be as costly as the existing approach. Currently, general contractors, subcontractors, product manufacturers, insurance companies, and their legal counsel are spending significant financial resources to determine if homes should be repaired and who should repair them. Then, once that decision is made, the general contractors, subcontractors, and product manufacturers are spending additional dollars to repair the homes. As stated earlier, if the homeowners do not receive reasonable settlement offers, they must turn to the legal system in order to obtain a remedy. When this happens, the general contractors, subcontractors, product manufacturers, insurance companies, and their legal counsel are incurring costs to prepare for and attend arbitrations, mediations, and trials. While anecdotal, if all of these aforementioned costs were redirected to a "Step Up" program, the actual costs of such a program could be less than the costs of the existing approach.

Finally, a "Step Up" program has benefits for all parties. First, such a program would keep most homeowners out of the legal system. Second, a "Step Up" program would begin to rehabilitate general contractors,' subcontractors,' and product manufacturers' reputations.²⁴⁷ Lastly, such a program would assist general contractors, subcontractors, product manufacturers, and insurance companies in identifying the scope and duration of the mold and

247. Homeowners' most frequent complaint about contractors is lack of communication. Telephone interview with Charlie Durenberger, Manager, Enforcement Servs., Minn. Dep't of Labor and Indus., in St. Paul, Minn. (July 25, 2006); see also *News from the Builders Association of the Twin Cities*, STAR TRIB. (Minneapolis), July 8, 2006, at H3.

moisture intrusion problem and would allow these parties to plan for an end to the problem.

B. Require Improved Building Practices and Inspections

The Association has realized the need for improved building practices.²⁴⁸ Consequently, the Association integrated a building practice standard into the QBI agreement.²⁴⁹ But to ensure full compliance with a higher standard of building practices, the Minnesota Department of Labor and Industry should consider upgrading the residential building code from a minimum standard to best practice. Updating the code and several other actions should be considered in a new “Step Up” program. Best practice should be unambiguous so that state and local building inspectors can more effectively interpret and enforce the building code. Furthermore, building inspectors currently have no liability for homes with building code violations.²⁵⁰ State and local building inspectors should be trained to actively enforce the residential building code and should be held liable for negligent inspections. The proper sequence of events would be as follows: (1) update the residential building code so that it is unambiguous and enforceable; (2) modify state law to hold state and local authorities, including building inspectors, accountable for their performance on residential building inspections; (3) train state and local building inspectors on the substance of the updated code and on the proper application of the code in residential building inspections. Finally, to avoid a negative impact on the building practice changes already being advanced by the Association, the Minnesota Department of Labor and Industry should work collaboratively with the Association and homeowners’ groups to reach a solution that is palatable to all.

248. See *supra* Part V.E.

249. See *supra* Part V.E.

250. See MINN. STAT. § 466.03, subdiv. 6 (2006); PHILIP L. BRUNER AND PATRICK J. O’CONNOR, BRUNER & O’CONNOR ON CONSTRUCTION LAW, § 13:20 (2002) (“A significant impediment to recovery against building officials for negligent inspection is the ‘public duty’ doctrine. This doctrine exempts municipalities and their building inspectors from liability for negligent approval of building plans and negligent enforcement of building codes.”).

C. Adopt Legislative Amendments

1. Include Attorney Fees

Homeowners are the only parties in the Minnesota construction defect problem whose personal assets are directly placed at risk. In response to this issue, several legislators and attorneys have drafted amendments to the Home Warranty statute and testified before the Minnesota Legislature.²⁵¹ To date, however, the amendments that would create provisions in the statute for awarding attorney fees and other associated fees, as part of the homeowners' remedy, have either been withdrawn or have not passed.

Perhaps if the amendment delineated when reimbursement of the above-stated fees is appropriate, as well as the fees that are considered reasonable for the case, the amendment would be more likely to pass. For example, if a homeowner has complied with the intent of the Home Warranty statute and twelve months later the homeowner is still waiting to receive a settlement offer to repair the home, perhaps the homeowner is entitled to a legal claim with all reasonable attorney and other fees paid by the opposing parties, regardless of who prevails. While a statute may provide for the prevailing party to be eligible for attorney fees, more often a statute will specify a particular kind of prevailing party.²⁵² Public policy may seek to discourage bad faith or uncooperative conduct by identifying the factors that make the legal claim more legitimate. A statute may authorize attorney fees for a particular class of winners such as employees or homeowners, but not the employers or general contractors, subcontractors, product manufacturers, or insurance companies.²⁵³ Additionally, the amount of awarded attorney fees is sometimes curtailed by the use of the word "reasonable."²⁵⁴ Given that the homeowner is the only party in the Minnesota construction defect problem with personal assets at risk, perhaps the amendment should specify a fee formula or an actual maximum billable amount that may be awarded as attorney fees.²⁵⁵

251. Senate Judiciary Committee Hearings, *supra* note 122.

252. Deborah K. McKnight, Minn. House of Rep. Research Dept., Attorney Fee Awards in Minnesota Statutes 1 (Feb. 2004), <http://www.house.leg.state.mn.us/hrd/pubs/attyfee.pdf>.

253. *Id.* at 2.

254. *Id.*

255. *See id.* It is considered good business practice for legal professionals and

Furthermore, if general contractors, subcontractors, product manufacturers, and insurance companies are paying homeowners' legal fees, these parties may have more incentive to offer timely and comprehensive settlements. Thus, this action may keep the homeowners out of the legal system.

2. *Require Mandatory Catastrophic CGL Coverage*

Currently, the predominant funding sources for residential construction defect claims are CGL policies.²⁵⁶ Additionally, insurance companies are adding policy endorsements that narrow or eliminate coverage for general contractors' construction defect claims.²⁵⁷ These actions promote another roadblock to homeowners' receiving a comprehensive remedy.

Minnesota insurance regulations should be amended to require mandatory, catastrophic CGL coverage for construction defect claims. Perhaps this is another area in which the scope and effects of the amendment could be limited with a sunset provision. For example, as a result of the data gathered for the "Step Up" program, the insurance companies would know the scope and duration of the existing construction defect problem, and the amendment could be limited accordingly and phased out at a termination point. Hence, if the "problem" homes are being repaired and eliminated from the system and the general contractors' and subcontractors' building practices are changing, there is no longer a need for catastrophic CGL coverage on construction defect claims.

D. *Create a Construction Law Court*

The American fault-based legal system does not appear to work very well for homeowners' construction defect claims. The legal system has already recognized that some disputes, such as tax problems and traffic tickets, are handled more effectively in systems specifically designed to address those problems.

While a construction law court would encompass more than

service providers to provide a customer with a proposal that details the value and cost of the services, explores both parties' objectives and expectations of the services, and outlines how and when the services will be invoiced. A paradigm shift toward project billing or contingent billing, versus straight hourly billing, may help advance the argument for enacting such a provision.

256. *See supra* Part V.B.

257. *Id.*

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homeowners' construction defect claims, this could make the creation of such a legal system more economically defensible. Construction disputes have existed for centuries, in all types of residential and commercial construction. A system of judges and support staff with construction law expertise and a specific step-by-step process for bringing disputes to closure would eliminate some of the ambiguity for homeowners. Similarly, while not validated, it may also simplify contractors' non-homeowner disputes.

VII. CONCLUSION

Too many Minnesota homeowners have discovered that the homes they purchased are damaged goods, and the current legal remedies for fixing the problem are not working. Furthermore, many homeowners are voluntarily entering or being pushed into the American legal system in order to get reasonable settlement remedies on their homes.²⁵⁸ Many of these homeowners step into the system believing that, because they did not bargain for the mold and moisture problems in their homes, they will be treated fairly and emerge whole. Through the experience, they learn that the American legal system stands for "justice" that does not always equate to "fairness." In the end, they return home to their "sick" houses emotionally upset, anguished, and disillusioned.

Minnesota's construction defect problem urgently needs an innovative solution. Homeowners, home builders, and the insurance companies are locked in a battle that has no real winners. In sum, Minnesota's construction defect problem is the result of three elements' failure to function properly: people, products, and processes. Moreover, the problem requires a solution that integrates accountability, uniformity, and cooperation. Just as the home should be viewed as a dynamic system that must be managed to achieve efficient performance, so must the solution to Minnesota's mold and moisture construction defect problem.

258. See interviews cited *supra* note 152.