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RESIDENTIAL CONSTRUCTION LAW -- UPDATE AND CURRENT STATUS

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I. THE TEXAS RESIDENTIAL CONSTRUCTION LIABILITY ACT – PRACTICE AND PROCEDURE[1]

With the sunsetting of the Texas Residential Construction Commission Act, it is again crucial to understand practice and procedure under the Residential Construction Liability Act (the "RCLA"). This is again the primary governing statute in residential construction law. The RCLA's primary purpose is to give notice of the homeowner's complaint to the builder, and allow the builder to make an offer of settlement.

A. The RCLA Notice Letter

Under §27.004(a), a homeowner that is seeking damages from a contractor for construction defects must give sixty days written notice, via certified mail, return receipt requested, of his or her complaint(s) to the contractor before the homeowner may commence any litigation or arbitration action. The notice must specify the construction defects complained of in "reasonable detail," and must be sent to the contractor's "last known address." Tex. Prop. Code §27.004(a). If one also intends to assert a claim under the DTPA, one could include notice of the claims under that statute in the notice. Keep in mind, however, under *O'Donnell v. Roger Bullivant of Texas, Inc.*, 940 S.W.2d 411 (Tex. App. – Fort Worth 1997, writ denied) this may extend the contractor's time to make an offer to 60 days under the DTPA, rather than 45 days under the RCLA.

Although there is no case on point, in my opinion, sending the notice via certified mail, return receipt requested, to the contractor's last known address, is all that is required.[2] If the contractor does not retrieve its certified mail, this should not matter; the homeowner has complied with the statutory requirements.

B. Contractor's Opportunity to Inspect

The contractor may request, in writing, an inspection within 35 days of receiving the homeowner's RCLA notice. The statutory purpose of the inspection is to, "to determine the nature and cause of the defect and the nature and extent of repairs necessary to remedy the defect." Tex. Prop. Code §27.004(a). Upon receipt of the written request, the homeowner ***shall*** give the contractor a "reasonable opportunity" to inspect and have inspected the property that is the subject of the complaint." *Id.* During that inspection, "The contractor may take reasonable steps to document the defect." *Id.*

[1] The 2014 edition of the Texas Residential Construction Law Manual can be purchased at http://legalsolutions.thomsonreuters.com/law-products/Treatises/Texas-Residential-Construction-Law-Manual-2014/p/100277422. The 2015 edition should come out around June, with some minor updates.

[2] If the homeowner has been provided with written notice that the builder is represented by an attorney, the notice must be sent to that attorney. Tex. Prop. Code §27.004(o). The reverse is also true. If the builder is provided with written notice that the homeowner is represented by an attorney, notices and responses must be sent to that attorney. *Id.*

C. Contractor's Written Settlement Offer

Under the RCLA, the contractor has 45 days from the date notice was given to it to make a written offer of settlement.

> The offer must be sent to the claimant at the claimant's last known address or to the claimant's attorney by certified mail, return receipt requested. The offer may include either an agreement by the contractor to repair or to have repaired by an independent contractor partially or totally at the contractor's expense or at a reduced rate to the claimant any construction defect described in the notice and shall describe in reasonable detail the kind of repairs which will be made.

Tex. Prop. Code §27.004(b). Under this same section of the RCLA, the repairs, if the settlement proposal is accepted, must be completed within 45 days of the homeowner's acceptance. The only statutory exceptions are if, "completion is delayed by the claimant or by other events beyond the control of the contractor." *Id*. Also, the statute permits the Contractor and homeowner to agree, in writing, to extensions of any time periods. Tex. Prop. Code §27.004(h).

The contractor's offer should contain sufficient detail to allow the homeowner to effectively and accurately analyze the offer of repair and its consequences. It should also, in my opinion, be written with the understanding that it may be viewed by a trier of fact some day in the future, in litigation or arbitration, to determine reasonableness on the part of the contractor and/or the homeowner. If a contractor's offer of settlement is deemed to be unreasonable by a trier of fact, then the limitations on damages found in Tex. Prop. Code §27.004(e) (and set forth below) shall not apply. *See*, Tex. Prop. Code §27.004(f).

D. Homeowner's Response to Written Settlement Offer

Once the homeowner receives an offer of repair from the contractor, the homeowner must reject in writing or accept such offer within 25 days, or if the homeowner takes neither action, the offer will be deemed rejected. Tex. Prop. Code §§27.004(b)(1) and (i).[3] It is advisable, in my opinion, that if a homeowner is going to reject a contractor's offer of settlement, that he or she do so in writing, explaining in detail the reason(s) for the rejection. This letter should be written with a view to it being

[3] The two sub sections of Tex. Prop. Code §27.004 addressing this timing are slightly conflicting. §27.004(b)(1) provides that, "on or before the 25th day after the date the claimant receives the offer, the claimant shall advise the contractor in writing and in reasonable detail of the reasons why the claimant considers the offer unreasonable." As you can see, this subsection includes the 25th day, and appears to be mandatory, as it states the claimant "shall" give the written rejection notice. §27.004(i), on the other hand, states: "An offer of settlement made under this section that is not accepted before the 25th day after the date the offer is received by the claimant is considered rejected." A possible reading of this subsection is that on the 25th day, if the homeowner has not accepted or rejected the offer, it will be deemed rejected. The most cautious approach, therefore, is to accept by the 24th day, although practically speaking, acceptance on the 25th day should work.

read by the trier of fact in arbitration or litigation at some point in the future. Consequences flow from unreasonably rejecting a contractor's offer of repair:

> (e) If a claimant rejects a reasonable offer made under Subsection (b) or does not permit the contractor or independent contractor a reasonable opportunity to inspect or repair the defect pursuant to an accepted offer of settlement, the claimant:
>
> (1) may not recover an amount in excess of:
>
> (A) the fair market value of the contractor's last offer of settlement under Subsection (b); or
>
> (B) the amount of a reasonable monetary settlement or purchase offer made under Subsection (n); and
>
> (2) may recover only the amount of reasonable and necessary costs and attorney's fees as prescribed by Rule 1.04, Texas Disciplinary Rules of Professional Conduct, incurred before the offer was rejected or considered rejected.

Tex. Prop. Code §27.004(e).

If the homeowner accepts the offer, the Contractor has a 45 day window for completion of repairs. Tex. Prop. Code §27.004(b). The only statutory exceptions to this window are if, "completion is delayed by the claimant or by other events beyond the control of the contractor,"[4] or if both the Contractor and the homeowner agree in writing to extend this time period.[5] One can foresee some situations, for example in a complicated foundation failure, in which the Contractor simply cannot complete repairs within a 45 day window. It would seem two options are available to the Contractor to still be viewed as "reasonable." The easiest is if the homeowner will agree to the extended time period in writing. If this is not feasible, I would suggest the letter detail why the longer time period is an "event beyond the control of the contractor" under section 27.004(b).

E. The "Second Bite at the Apple"

If the homeowner rejects the Contractor's offer of settlement in writing, not later than the 10th day after the date the Contractor receives such written rejection, the Contractor, "may make a supplemental written offer of settlement to the claimant by sending the offer to the claimant or the claimant's attorney." Tex. Prop. Code §27.004(b)(2). The only logical reading of this right is that this supplemental offer is also considered by a tier of fact in determining the ***reasonableness*** of the Contractor's offer. Otherwise, it would appear that this provision would add nothing to the statute. It does

[4] Tex. Prop. Code §27.004(b).
[5] Tex. Prop. Code §27.004(h).

not appear that the parties' status during this ten day time period, of thereafter if a supplemental offer is made, is changed in any other way. In other words, once the initial rejection occurs, the homeowner appears to be free to proceed with suit or arbitration. Presumably the Contractor can still make an unlimited amount of settlement offers during that process. From the Contractor's perspective, I would argue the only way this provision adds anything to the process is if the trier of fact is allowed to also consider this supplemental offer in its analysis as to whether or not the parties were reasonable in their offers and rejections. This argument is bolstered by the language in Tex. Prop. Code §27.004(e) – "If a claimant rejects a reasonable offer made under Subsection (b)," the claimant may not recover certain elements of damages. The 10 day supplemental offer is part of Subsection (b), specifically Subsection (b)(2). Therefore, a homeowner should give any supplemental offer under Subsection (b)(2) as careful a consideration as the original offer under Subsection (b). If rejected, again I would suggest a rejection in writing, with detail, written with a view toward the trier of fact analyzing the rejection some day in the future in determining "reasonableness."

F. Miscellaneous Issues Under the RCLA

1. Threat to Health and Safety

Under Tex. Prop. Code §27.004(m), if there is an imminent threat to the homeowner's health or safety, then the contractor must take reasonable steps to cure the defect, or potentially suffer the statutory consequences. Specifically, subsection (m) states:

> Notwithstanding Subsections (a), (b), and (c), a contractor who receives written notice of a construction defect resulting from work performed by the contractor or an agent, employee, or subcontractor of the contractor and creating an imminent threat to the health or safety of the inhabitants of the residence shall take reasonable steps to cure the defect as soon as practicable. If the contractor fails to cure the defect in a reasonable time, the owner of the residence may have the defect cured and may recover from the contractor the reasonable cost of the repairs plus attorney's fees and costs in addition to any other damages recoverable under any law not inconsistent with the provisions of this chapter.

Tex. Prop. Code §27.004(m).

2. Limitations/Counterclaim Issue

Tex. Prop. Code §27.004(c) addresses the situation when the potential running of a statute of limitations keeps the homeowner from being able to give timely notice of his or her claim to the Contractor or Builder, as well as the situation in which the construction defect claim is asserted as a counterclaim.[6]

[6] Remember, with the sunsetting of the TRCCA the referenced Subtitle D, Title 16 will automatically not apply (unless, of course, you are dealing with a pre-sunset TRCCA case). This language has not been

> If compliance with Subtitle D, Title 16, or the giving of the notice under Subsections (a) and (b) within the period prescribed by those subsections is impracticable because of the necessity of initiating an action at an earlier date to prevent expiration of the statute of limitations or if the complaint is asserted as a counterclaim, compliance with Subtitle D, Title 16, or the notice is not required. However, the action or counterclaim shall specify in reasonable detail each construction defect that is the subject of the complaint. If Subtitle D, Title 16, applies to the complaint, simultaneously with the filing of an action by a claimant, the claimant must submit a request under Section 428.001. If Subtitle D, Title 16, does not apply, the inspection provided for by Subsection (a) may be made not later than the 75th day after the date of service of the suit, request for arbitration, or counterclaim on the contractor, and the offer provided for by Subsection (b) may be made not later than the 15th day after the date the state-sponsored inspection and dispute resolution process is completed, if Subtitle D, Title 16, applies, or not later than the 60th day after the date of service, if Subtitle D, Title 16, does not apply. If, while an action subject to this chapter is pending, the statute of limitations for the cause of action would have expired and it is determined that the provisions of Subsection (a) were not properly followed, the action shall be abated to allow compliance with Subsections (a) and (b).

Tex. Prop. Code §27.004(c). Essentially, then, if notice under the RCLA is not practical due to the running of the limitations period, or if the claim is being submitted as a counterclaim, then notice does not have to be given to the Contractor or Builder, however the Petition, Demand for Arbitration, Counterclaim, or other similar document setting forth the claim must specify in reasonable detail each construction defect that is the subject of the homeowner's complaint. The RCLA time period for inspection is then extended to the 75th day after the date of service of the suit, request for arbitration, or counterclaim on the Contractor. Note that despite the fact that in the limitations and counterclaim situation the RCLA provides a 75 day window for inspection, the Contractor has until the 60th day after service to give the settlement offer contemplated by Tex. Prop. Code §27.004(b). Presumably, therefore, the Contractor should do its inspection before the 60 days after service have run.

3. Statutory Right to Mediation

In 1999, the Legislature added a mediation provision allowing for mediation of construction defect cases in which the damages being sought by the homeowner exceeded $7,500.00. The key element (assuming the $7,500 threshold is passed) is that a suit has been filed. The provision, therefore, appears inapplicable in an arbitration proceeding. The provision, found at Tex. Prop. Code §27.0041, and its procedure are straightforward, and are as follows:

"cleaned up" to delete references to the TRCCA. Simply read the language with the assumption that Subtitle D, Title 16 does ***not*** apply.

(a) If a claimant files suit seeking from a contractor damages arising from a construction defect in an amount greater than $7,500, the claimant or contractor may file a motion to compel mediation of the dispute. The motion must be filed not later than the 90th day after the date the suit is filed.

(b) Not later than the 30th day after the date a motion is filed under Subsection (a), the court shall order the parties to mediate the dispute. If the parties cannot agree on the appointment of a mediator, the court shall appoint the mediator.

(c) The court shall order the parties to begin mediation of the dispute not later than the 30th day after the date the court enters its order under Subsection (b) unless the parties agree otherwise or the court determines additional time is required. If the court determines that additional time is required, the court may order the parties to begin mediation of the dispute not later than the 60th day after the date the court enters its order under Subsection (b).

(d) Unless each party who has appeared in a suit filed under this chapter agrees otherwise, each party shall participate in the mediation and contribute equally to the cost of the mediation.

(e) Section 154.023, Civil Practice and Remedies Code, and Subchapters C and D, Chapter 154, Civil Practice and Remedies Code, apply to a mediation under this section to the extent those laws do not conflict with this section.

4. Contractor's Right to Offer to Re-Purchase the Home

In the 2003 revisions to the RCLA, the Legislature provided for a Contractor's statutory right to repurchase a residence if certain conditions are met. This is found in Tex. Prop. Code §27.0042, titled "Conditional Sale to Builder." This statute provides as follows:

(a) A written agreement between a contractor and a homeowner may provide that, except as provided by Subsection (b), if the reasonable cost of repairs necessary to repair a construction defect that is the responsibility of the contractor exceeds an agreed percentage of the current fair market value of the residence, as determined without reference to the construction defects, then, in an action subject to this chapter, the contractor may elect as an alternative to the damages specified in Section 27.004(g) that the contractor who sold the residence to the homeowner purchase it.

(b) A contractor may not elect to purchase the residence under Subsection (a) if:

(1) the residence is more than five years old at the time an action is initiated; or

(2) the contractor makes such an election later than the 15th day after the date of a final, unappealable determination of a dispute under Subtitle D, Title 16, if applicable.[7]

(c) If a contractor elects to purchase the residence under Subsection (a):

(1) the contractor shall pay the original purchase price of the residence and closing costs incurred by the homeowner and the cost of transferring title to the contractor under the election;

(2) the homeowner may recover:

(A) reasonable and necessary attorney's and expert fees as identified in Section 27.004(g);

(B) reimbursement for permanent improvements the owner made to the residence after the date the owner purchased the residence from the builder; and

(C) reasonable costs to move from the residence; and

(3) conditioned on the payment of the purchase price, the homeowner shall tender a special warranty deed to the contractor, free of all liens and claims to liens as of the date the title is transferred to the contractor, and without damage caused by the homeowner.

(d) An offer to purchase a claimant's home that complies with this section is considered reasonable absent clear and convincing evidence to the contrary.

Tex. Prop. Code §27.0042.

As you can see, this part of the RCLA requires, preliminarily, that the contract between the Builder and the homeowner provide, in writing, for a right of repurchase. The contract should specify the agreed upon percentage by which the cost of repairs must exceed the current fair market value of the residence in order for the right to apply. The residence must not be more than five years old. If the Builder fulfills the foregoing and elects to repurchase the residence, it must pay the original purchase price of the

[7] Remember, this will no longer be applicable.

residence, closing costs incurred by the homeowner, the cost of transferring title to the Builder. The statute then states the homeowner ***may*** recover his or her reasonable attorney's and expert fees as identified in Section 27.004(g);[8] reimbursement for permanent improvements the owner made to the residence after the date the owner purchased the residence from the builder; and reasonable costs to move from the residence. Tex. Prop. Code §27.0042(c)(2). It is not clear what is meant by the statement that the homeowner ***may*** recover these items. I assume that this means that to the extent the homeowner has one or more of these types of damages, they should be part of the Builder's offer to repurchase. The other reading of this provision, that the homeowner "may" recover these, but does not have to, would seem to lead to the absurd result that no Builder's offer to re-purchase would include these damages. Why offer them if you are not required to do so?

Subsection (c) then provides that "conditioned on the payment of the purchase price, the homeowner shall tender a special warranty deed to the contractor, free of all liens and claims to liens as of the date the title is transferred to the contractor, and without damage caused by the homeowner." Again, I assume the phrase "conditioned on the payment of the purchase price" encompasses payment of all of the applicable elements of §27.0042(c), not solely the purchase price; otherwise an absurd result again follows.

The end result for the Builder complying with all of the foregoing is an offer that is presumptively reasonable. Such presumption can only be overcome with clear and convincing evidence. Tex. Prop. Code §27.0042(d).

5. Contractor's Affirmative Defenses under the RCLA

Tex. Prop. Code §27.003 provides five affirmative defenses to a contractor. The contractor is not liable, in a construction defects case, for any percentage of damages caused by: (1) the negligence of a person other than the contractor or an agent, employee, or subcontractor of the contractor; (2) failure of a person other than the contractor or an agent, employee, or subcontractor of the contractor to take reasonable action to mitigate the damages or take reasonable action to maintain the residence; (3) normal wear, tear, or deterioration; (4) normal shrinkage due to drying or settlement of construction components within the tolerance of building standards; or (5) the contractor's reliance on written information relating to the residence, appurtenance, or real property on which the residence and appurtenance are affixed that was obtained from official government records, if the written information was false or inaccurate and the contractor did not know and could not reasonably have known of the falsity or inaccuracy of the information. Essentially these statutory defenses state that the Contractor is not going to be liable for the negligence of others unrelated to the Contractor; is going to have a defense if the homeowner could and should have mitigated his or her damages and failed to do so; is not liable when the alleged defects fall within accepted industry tolerances; and that the Builder is not liable for reliance on government records, unless it

[8] Section 27.004(g)(6) merely references, "reasonable and necessary attorney's fees," so I am not sure what, if anything, this reference adds with respect to such fees. As to expert fees, Section 27.004(g)(3) allows recovery of, "reasonable and necessary engineering and consulting fees."

knew the information to be false or not accurate. These are ***additional*** defenses provided to a Contractor; they are not exclusive. *See*, Tex. Prop. Code §27.003(b)("Except as provided by this chapter, this chapter does not limit or bar any other defense or defensive matter or other defensive cause of action applicable to an action to recover damages or other relief arising from a construction defect").

6. Abatement/Dismissal for Failure to Give Notice and Opportunity to Inspect

As noted above, the 2003 amendments to the RCLA changed the procedure when a homeowner fails to give notice of his or her claims and/or fails to give a reasonable opportunity to inspect to the contractor. Prior case and statutory law provided for abatement. The 2003 amendments provided for ***dismissal***. The 2007 amendments to the RCLA included a return to ***abatement*** when notice or a reasonable opportunity to inspect has not been given. The current statute provides as follows:

> The court or arbitration tribunal shall abate an action governed by this chapter if Subsection (c) does not apply and the court or tribunal, after a hearing, finds that the contractor is entitled to abatement because the claimant failed to comply with the requirements of Subtitle D, Title 16, if applicable, failed to provide the notice or failed to give the contractor a reasonable opportunity to inspect the property as required by Subsection (a), or failed to follow the procedures specified by Subsection (b). An action is automatically abated without the order of the court or tribunal beginning on the 11th day after the date a motion to abate is filed if the motion:
>
> (1) is verified and alleges that the person against whom the action is pending did not receive the written notice required by Subsection (a), the person against whom the action is pending was not given a reasonable opportunity to inspect the property as required by Subsection (a), or the claimant failed to follow the procedures specified by Subsection (b) or Subtitle D, Title 16; and
>
> (2) is not controverted by an affidavit filed by the claimant before the 11th day after the date on which the motion to abate is filed.

Tex. Prop. Code §27.004(d).[9]

II. THE IMPLIED WARRANTIES OF GOOD AND WORKMANLIKE PERFORMANCE AND OF HABITABILITY

With the demise of the TRCCA, we are currently back to no statutory warranties on residential construction. As such, presumably we have returned to the common law with respect to warranties, including the implied warranties of good and workmanlike performance and of habitability.

[9] Tex. Prop. Code §27.004(c) addresses the situation where an impending statute of limitations creates problems in giving notice, as discussed in detail above.

A. The Common Law Implied Warranty of Habitability

The Texas Supreme Court recognized an implied warranty of habitability for the first time in 1968 in *Humber v. Morton*, 426 S.W.2d 554 (Tex. 1968). The key facts in *Humber* were as follows: "The widow Humber brought suit against Claude Morton, alleging that Morton was in the business of building and selling new homes; that she purchased a house from him which was not suitable for human habitation in that the fireplace and chimney were not properly constructed and because of such defect, the house caught on fire and partially burned the first time a fire was lighted in the fireplace." *Humber* at 554. To show you how far we have come in this area, Defendant Claude Morton actually defended on the following two grounds: "that an independent contractor, Johnny F. Mays, had constructed the fireplace and he, Morton, was not liable for the work done by Mays, and the doctrine of "caveat emptor" applied to all sales of real estate." *Id*.

Procedurally, Mrs. Humber prevailed at the first jury trial; the Court of Appeals reversed and remanded; upon remand competing motions for summary judgment were filed with the trial court, and the court held in favor of Morton; which judgment was affirmed by the Court of Appeals. The summary judgment for defendant was upheld on two grounds; "that Mays was an independent contractor and that the doctrine of implied warranty was not applicable to the case." *Id*. at 555. The case then went to the Texas Supreme Court, which held:

> [W]e are of the opinion that the courts below erred in holding as a matter of law that Morton was not liable to Mrs. Humber because the doctrine of caveat emptor applied to the sale of a new house by a "builder-vendor" and consequently no implied warranty that the house was fit for human habitation arose from the sale. Accordingly, we reverse the judgments of the courts below and remand the cause to the district court for a conventional trial on the merits.

Id. The Court noted that, "According to Morton, the only warranty contained in the deed was the warranty of title . . . and that he made no other warranty. . . ." *Id*. The Court then assumed "that no express warranties, either oral or written, were involved." Id. It then continued:

> However, it is undisputed that Morton built the house and then sold it as a new house. Did he thereby impliedly warrant that such house was constructed in a good and workmanlike manner and was suitable for human habitation? We hold that he did. Under such circumstances, the law raises an implied warranty.

Id. The Court then explored the history and doctrine of caveat emptor and how other states were treating it with respect to sales of residential property. It emphatically

rejected the doctrine of caveat emptor in the sale of residential property, and adopted an implied warranty of habitability.

> If at one time in Texas the rule of caveat emptor had application to the sale of a new house by a vendor-builder, that time is now past. The decisions and legal writings herein referred to afford numerous examples and situations illustrating the harshness and injustice of the rule when applied to the sale of new houses by a builder-vendor, and we need not repeat them here. Obviously, the ordinary purchaser is not in a position to ascertain when there is a defect in a chimney flue, or vent of a heating apparatus, or whether the plumbing work covered by a concrete slab foundation is faulty. It is also highly irrational to make a distinction between the liability of a vendor-builder who employs servants and one who uses independent contractors.

Id. at 561.

> The caveat emptor rule as applied to new houses is an anachronism patently out of harmony with modern home buying practices. It does a disservice not only to the ordinary prudent purchaser but to the industry itself by lending encouragement to the unscrupulous, fly-by-night operator and purveyor of shoddy work.

Id at 562.

The Supreme Court then, in 1983, extended the warranty of habitability to subsequent purchasers in *Gupta v. Ritter Homes, Inc.*, 646 S.W.2d 168 (Tex. 1983).

> On November 3, 1976, Ritter purchased the lot upon which the house was built and on July 27, 1977, sold the lot and finished house to James E. Wobig. Mr. Wobig and his family occupied the house for approximately three months and then sold it to Gupta. Gupta alleged that the slab foundation of the house had settled excessively causing the walls to crack, the roof to leak and the patio to pull away from the rest of the house. He also alleged that the garage slab and the driveway had cracked.

Gupta at 169.

> This Court held in *Humber v. Morton*, 426 S.W.2d 554 (Tex. 1968), that a builder/vendor impliedly warrants to his purchaser that a building constructed for residential use has been constructed in a workmanlike manner and is fit for habitation, thus rejecting the doctrine of caveat emptor. The question before us is whether that implied warranty extends to subsequent purchasers. We hold that it does cover latent defects not discoverable by a reasonably prudent inspection of the building at the time of sale. The reasons for this holding are: (1) a builder should be in

> business to construct buildings free of latent defects; (2) the buyer cannot, by reasonable inspection or examination, discern such defects; (3) the buyer cannot normally rely on his own judgment in such matters; (4) in view of the circumstances and the relations of the parties, the buyer is deemed to have relied on the builder; and (5) the builder is the only one who has or could have had knowledge of the manner in which the building was built. As between the builder and owner, it matters not whether there has been an intervening owner. The effect of the latent defect on the subsequent owner is just as great as on the original buyer and the builder is no more able to justify his improper work as to a subsequent owner than to the original buyer. The public policy upon which the *Humber* decision was based applies equally to both situations. See *id.* at 552.

The Defendant, Ritter, contended, "that an implied warranty arising out of a contract must fail as to a subsequent purchaser for lack of privity." *Id*. The Texas Supreme Court rejected this argument. "We hold that the implied warranty of habitability and good workmanship is implicit in the contract between the builder/vendor and original purchaser is automatically assigned to the subsequent purchaser." *Id*.

Justice Spears, in a concurrence, noted that:

> Texas is not the first state to extend the implied warranty of habitability to subsequent purchasers. The supreme courts of six states have recognized the cause of action and limited the implied warranty to latent defects which are not discoverable upon a reasonable inspection.

Id. at 170. He then noted the limitations and defenses inherent in the warranty:

> Our extension of liability is limited to latent defects which manifest themselves after the purchase, and are not discoverable by a subsequent purchaser's reasonably prudent inspection at the time of sale. The majority merely recognizes the cause of action, thereby reversing the summary judgment and allowing the cause to proceed to trial on the merits. In trial, the plaintiff has the burden of proving a latent defect which is attributable to the actions or inactions of the builder/seller. The builder has all the traditional contract defenses available to him including the defense that the defects are not attributable to original structural flaws. For example, the builder could escape liability by pleading and proving there has been substantial change or alteration in the condition of the house since the original sale, misuse, or that the defects could have been discovered by reasonably prudent inspection of the house.

Id. He concludes, however, by noting:

> Latent defects in a house often will not manifest themselves for some period of time, very likely, after the original owner has sold the property to a subsequent buyer. In our very mobile society a builder/seller should know a house he builds might be resold within a very short period of time; therefore, our extension of the implied warranty should not place any extra burdens on builders.

Id.

The most recent pronouncement by the Texas Supreme Court on the warranty of habitability is contained in *Centex Homes v. Buecher*, 95 S.W.3d 266 (Tex. 2002). The issue in that case was, "whether a homebuilder may disclaim the implied warranties of habitability and good and workmanlike construction that accompany a new home sale." *Buecher* at 268. The Texas Supreme Court held:

> We agree with the court of appeals that the implied warranty of habitability cannot be waived except under limited circumstances not implicated here. We disagree, however, that the implied warranty of good and workmanlike construction cannot be disclaimed. When the parties' agreement sufficiently describes the manner, performance or quality of construction, the express agreement may supersede the implied warranty of good workmanship. Although we do not agree in all respects with the court of appeals' reasoning, we affirm its judgment remanding this cause to the trial court.

Id. In *Buecher*:

> Michael Buecher and other homeowners purchased new homes built by Centex Homes or Centex Real Estate Corporation doing business as Centex Homes. Each homeowner signed a standard form sales agreement prepared by Centex. The homeowners allege that the agreement contained a one-year limited express warranty in lieu of and waiving the implied warranties of habitability and good and workmanlike construction.

Id. The Texas Supreme Court held that the implied warranty of habitability could not be waived by contract.

> In conclusion, we hold that the implied warranty of good workmanship may be disclaimed by the parties when their agreement provides for the manner, performance or quality of the desired construction. We further hold that the warranty of habitability may not be disclaimed generally. This latter implied warranty, however, only extends to defects that render the property so defective that it is unsuitable for its intended use as a home. Further, the implied warranty of habitability extends only to latent defects. It does not include defects, even substantial ones, that are known by or expressly disclosed to the buyer.

Id. at 274-275. (Below there is a discussion of the implied warranty of good and workmanlike construction issues in *Buecher*.)

The concept of the implied warranty of habitability was carried through in the TRCCA. Presumably, with the demise of the TRCCA, the common law implied warranty of habitability again exists. As *Buecher* tells us, this warranty cannot be disclaimed.

B. The Implied Warranty of Good and Workmanlike Construction

The Texas Supreme Court first recognized, "an implied warranty of good workmanship in the repair or modification of tangible goods or property" in *Melody Home Manufacturing Co. v. Barnes*, 741 S.W.2d 349 (Tex. 1987). Prior to this case, the Texas Supreme Court had not ruled on the existence of such an implied warranty:

> Melody Home next contends that repair services do not carry with them an implied warranty that they will be performed in a good and workmanlike manner. Implied warranties are created by operation of law and are grounded more in tort than in contract. *La Sara Grain v. First Nat'l Bank of Mercedes*, 673 S.W.2d 558, 565 (Tex. 1984); *Humber*, 426 S.W.2d at 556. A number of courts of appeals decisions have expressly or impliedly recognized such an implied warranty. In addition, several articles, comments, and notes have concluded that the doctrine of implied warranty should apply to services. Despite its importance, this court has never ruled on this issue. *But see Dennis v. Allison*, 698 S.W.2d 94, 96 (Tex. 1985) (Ray, J., dissenting).

Melody Homes at 352-353. The Court continued:

> An implied warranty arises by operation of law when public policy so mandates. *Dennis v. Allison*, 698 S.W.2d at 95; *Jacob E. Decker & Sons, Inc. v. Capps*, 139 Tex. 609, 164 S.W.2d 828, 829 (1942). Unlike the situations in *Nobility Homes of Texas, Inc. v. Shivers*, 557 S.W.2d 77, 78 (1977) and *La Sara Grain*, 673 S.W.2d at 565, consumers of services do not have the protection of a statutory or common law implied warranty scheme . . . The issue presented in this case is whether the protection of Texas consumers requires the utilization of an implied warranty that repair services of existing tangible goods or property will be performed in a good and workmanlike manner as a matter of public policy. *Nobility Homes of Texas, Inc.*, 557 S.W.2d at 78.
>
> During the last thirty-five years, the United States has shifted from a goods to a services oriented economy. With this change has come a marked decrease in the quality of services. Similar quality control problems and consumer protection interests led this court and the

> legislature to apply the theory of implied warranty to products, goods, and new houses. *See Humber*, 426 S.W.2d at 562; *McKisson v. Sales Affiliates, Inc.*, 416 S.W.2d 787, 789 (Tex. 1967); *Jacob E. Decker & Sons*, 164 S.W.2d at 832; *see also* Tex. Bus. & Com. Code Ann. § 2.314 (Vernon 1968).

Id. at 353. The Texas Supreme Court then held that, "an implied warranty to repair or modify existing tangible goods or property in a good and workmanlike manner is available to consumers suing under the [Deceptive Trade Practices Act]." *Id*. at 354. It defined "good and workmanlike" as, "that quality of work performed by one who has the knowledge, training, or experience necessary for the successful practice of a trade or occupation and performed in a manner generally considered proficient by those capable of judging such work." *Id*. The Texas Supreme Court also held that this warranty could not be disclaimed.

> Consistent with the trend in recent consumer protection legislation and sound public policy, we further hold that the implied warranty that repair or modification services of existing tangible goods or property will be performed in a good and workmanlike manner may not be waived or disclaimed. *See e.g.* Tex. Bus. & Com. Code Ann. § 17.42 (Vernon Supp. 1987) (DTPA waiver unenforceable and void); Tex. Rev. Civ. Stat. Ann. art. 5221f, § 18 (Vernon Supp. 1987) (waiver of the provisions of the Manufactured Housing Standards Act unenforceable and void). It would be incongruous if public policy required the creation of an implied warranty, yet allowed the warranty to be disclaimed and its protection eliminated merely by a pre-printed standard form disclaimer or an unintelligible merger clause. *See G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392, 394-95 (Tex. 1982) (Spears, J., dissenting).
>
> When disclaimers are permitted, adhesion contracts -- standardized contract forms offered to consumers of goods and services on an essentially "take it or leave it" basis which limit the duties and liabilities of the stronger party -- become commonplace. *See, e.g., King v. Larsen Realty, Inc.*, 121 Cal. App. 3d 349, 175 Cal. Rptr. 226, 231 (1981); *Wheeler v. St. Joseph Hosp.*, 63 Cal. App. 3d 345, 133 Cal. Rptr. 775, 783 (1976); *Star Finance Corp. v. McGee*, 27 Ill. App. 3d 421, 326 N.E.2d 518, 522 (1975); *Cushman v. Frankel*, 111 Mich. App. 604, 314 N.W.2d 705, 707 (1981); *Guthmann v. La Vida Llena*, 103 N.M. 506, 709 P.2d 675, 678 (N.M. 1985). The consumer continues to expect that the service will be performed in a good and workmanlike manner regardless of the small print in the contract. A disclaimer allows the service provider to circumvent this expectation and encourages shoddy workmanship. To the extent that it conflicts with this opinion, we overrule *G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392.

Confusion subsequently arose, as noted by the Texas Supreme Court in *Buecher*, over how this warranty differs or does not differ from the implied warranty of habitability, and in what instances, if any, was waiver permissible. "Subsequently [to *Humber v. Morton*], in *G-W-L, Inc. v. Robichaux*, we conflated the *Humber* warranties of good workmanship and habitability, concluding that the 'Humber warranty' could be disclaimed or waived if that intent were clearly expressed in the parties' agreement." *Buecher* at 270. The homeowner plaintiffs in *Buecher* responded, "that *Robichaux* is no longer the law in Texas because it was overruled in *Melody Home Manufacturing Co. v. Barnes*, 741 S.W.2d 349, 355 (Tex. 1987)." The Texas Supreme Court agreed. "Because *Melody Home* has cast doubt on the validity of *Robichaux*'s waiver holding, we re-examine our holding in that case." *Id.*

In *Buecher*, the Texas Supreme Court proceeded to note the differences between the two implied warranties:

> The implied warranty of good workmanship focuses on the builder's conduct, while the implied warranty of habitability focuses on the state of the completed structure. *See* Clarkson, Note, *Implied Warranties of Quality in Texas Home Sales: How Many Promises to Keep*?, 24 HOUS. L. REV. 605, 617-18 (1987). Through the implied warranty of good workmanship, the common law recognizes that a new home builder should perform with at least a minimal standard of care. *See* Jones, *Economic Losses Caused by Construction Deficiencies: The Competing Regimes of Contract and Tort*, 59 U. CIN. L. REV. 1051, 1059-60 (1991); Block, *As the Walls Came Tumbling Down: Architects' Expanded Liability Under Design-Build/Construction Contracting*, 17 J. MARSHALL L. REV. 1, 18 n.86 (1984); Greenfield, *Consumer Protection in Service Transactions - Implied Warranties and Strict Liability in Tort*, 1974 UTAH L. REV. 661, 666. This implied warranty requires the builder to construct the home in the same manner as would a generally proficient builder engaged in similar work and performing under similar circumstances. *See Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349, 354-55, 31 Tex. Sup. Ct. J. 47 (Tex. 1987). The implied warranty of good workmanship serves as a "gap- filler" or "default warranty"; it applies unless and until the parties express a contrary intention. *See* Davis, *The Illusive Warranty of Workmanlike Performance: Constructing a Conceptual Framework*, 72 NEB. L. REV. 981, 999-1009 (1993) (historical and intended purpose of good workmanship warranty was to serve as a gap-filler). Thus, the implied warranty of good workmanship attaches to a new home sale if the parties' agreement does not provide how the builder or the structure is to perform.
>
> The implied warranty of habitability, on the other hand, looks only to the finished product:

> The implied warranty of habitability is a result oriented concept based upon specific public policy considerations. These include the propriety of shifting the costs of defective construction from consumers to builders who are presumed better able to absorb such costs; the nature of the transaction which involves the purchase of a manufactured product, a house; the buyer's inferior bargaining position; the foreseeable risk of harm resulting from defects to consumers; consumer difficulty in ascertaining defective conditions; and justifiable reliance by consumers on a builder's expertise and implied representations.

Davis, 72 NEB. L. REV. at 1019 (footnotes omitted). This implied warranty is more limited in scope, protecting the purchaser only from those defects that undermine the very basis of the bargain. *Id.* at 1015. It requires the builder to provide a house that is safe, sanitary, and otherwise fit for human habitation. *Kamarath,* 568 S.W.2d at 660. In other words, this implied warranty only protects new home buyers from conditions that are so defective that the property is unsuitable for its intended use as a home. As compared to the warranty of good workmanship, "the warranty of habitability represents a form of strict liability since the adequacy of the completed structure and not the manner of performance by the builder governs liability." Davis, 72 NEB. L. REV. at 1015 (1993) (footnotes omitted).

These two implied warranties parallel one another, and they may overlap. For example, a builder's inferior workmanship could compromise the structure and cause the home to be unsafe. But a builder's failure to perform good workmanship is actionable even when the outcome does not impair habitability. *Evans*, 689 S.W.2d at 400. Similarly, a home could be well constructed and yet unfit for human habitation if, for example, a builder constructed a home with good workmanship but on a toxic waste site. Unfortunately, many courts, including this one, have not consistently recognized these distinctions.

Buecher at 273-274. The Court concluded:

> In conclusion, we hold that the implied warranty of good workmanship may be disclaimed by the parties when their agreement provides for the manner, performance or quality of the desired construction. We further hold that the warranty of habitability may not be disclaimed generally. This latter implied warranty, however, only extends to defects that render the property so defective that it is unsuitable for its intended use as a home. Further, the implied warranty of habitability extends only to latent defects. It does not include defects, even substantial ones, that are known by or expressly disclosed to the buyer.

Id. at 274-275.

In conclusion, presumably starting September 1, 2010, and likely even presently, the common law implied warranty of good workmanship again exists in the State of Texas with respect to residential construction. Assuming this is the case, this implied warranty will apply to those projects in which the warranty is not expressly disclaimed, and there is no express warranty provided.

> The implied warranty of good workmanship, however, defines the level of performance expected when the parties fail to make express provision in their contract. It functions as a gap-filler whose purpose is to supply terms that are omitted from but necessary to the contract's performance. *See* RESTATEMENT (SECOND) CONTRACTS § 204 (1981)(*Supplying an Omitted Essential Term*). As a gap-filler, the parties' agreement may supersede the implied standard for workmanship, but the agreement cannot simply disclaim it. *See generally Lenape Res. Corp. v. Tenn. Gas Pipeline Co.*, 925 S.W.2d 565, 570, 39 Tex. Sup. Ct. J. 496 (Tex. 1996) (interpreting UCC gap-filler).

Id. at 274. For those not wanting to fall under this implied warranty, it is essential that their contract expressly disclaim this implied warranty, and that they provide an express warranty.

III. COMPARE/CONTRAST OF RESIDENTIAL AND COMMERCIAL CONSTRUCTION LAW

A. Owner/General Contractor Relationship

- Contract between Builder and Homeowner really should be in writing, signed by all owners. Tex. Prop. Code §41.007 requires a written contract, signed by husband and wife, if applicable, in order to be able to lien homestead. (The same section, as amended in 2007, requires Builder's TRCC registration number to be listed. Presumably this is mooted by the sunsetting of the TRCCA, although the statute has not been cleaned up.) Additional disclosure requirements are outlined below.
- Traditionally little homeowner bargaining power
  - Exception – Upper end custom house ($1 million +)
  - During the recession, saw greater homeowner bargaining power; with the improving economy, this effect may be changing.
- Traditionally, majority of contracts contain an arbitration clause (same as commercial). This seems to be somewhat lessening.
- Warranty – For six years was been statutorily set in residential construction by the TRCCA – 1 yr/2yr/10yr + 10 year warranty of habitability. With the sunsetting of the TRCCA, this statutory warranty probably ceased at midnight 8/31/2009; and in any event, certainly ceased at midnight 8/31/2010. Will

then rely on express warranties, as in commercial arena; and if no express warranty, the implied warranties discussed above.

- Statutorily required notice provisions:
  - Tex. Prop. Code §53.255 – Extensive disclosure in contract – set forth in statute.
  - Tex. Prop. Code §41.007 – Homestead disclosure – "Know your rights under the law."
  - HB 1038 (eff. 9/1/07) – Added TRCC registration number disclosure requirement to Tex. Prop. Code §41.007; and arbitration clause disclosure requirement to Tex. Prop. Code §41.007 and to Tex. Prop. Code §420.002(2). Unclear whether disclosing TRCC registration number requirement applies during the "gap" period between 9/1/09 and 8/31/10; clear that no longer applies at this point, even though still referenced in statute.
  - Tex. Prop. Code §53.256 – "List of Subcontractors and Suppliers" – Disclosure of subcontractors used on project – Also, must be updated. Can be waived.
  - RCLA disclosure– Tex. Prop. Code §27.007. As stated above, RCLA has not been cleaned up, so it still states it applies of the TRCCA does not apply. Since the TRCCA has been sunsetted, it cannot apply, and the RCLA will apply.
  - For historical purposes, and because it may apply to construction defect litigation that you face over the next few years, the TRCCA required certain disclosures if it applied – Tex. Prop. Code Chapter 420 (including the arbitration clause disclosure mentioned above, if applicable). (Unclear whether applies during the "gap" period between 9/1/09 and 8/31/10; presumably no longer applies after 8/31/10.)
- Prompt Payment Act –
    - Owner can withhold 110% of disputed amount (as opposed to 100% in commercial construction context).
    - No statutory right to stop work for non-payment as there is in commercial construction. Can build, in my opinion, into contract.
- Texas Trust Fund Act (Tex. Prop. Code Chapter 162) – in residential homestead construction over $5,000, contractor must have dedicated construction trust bank account, with a number of management requirements. These requirements are set forth in Tex. Prop. Code §§162.006 and .007.

B. Subcontractors

- Rare to see written subcontract agreements.
- Rare to see retainage.
- Contingent Payment statute (Tex. Bus. & Com. Code §35.521) does ***not*** apply to residential construction.

C. Typical Causes of Action

- Breach of Contract – Typical fact patterns same as commercial construction projects – (a) from contractor's perspective – failure to pay; (b) from owner's perspective – defective, incomplete, and/or slow work.
- Breach of Warranty – Again, used to be statutorily set under the TRCCA, and performance of residence was measured against TRCC's performance standards. Probably as of 9/1/09, and certainly as of 9/1/10, will be either set by contract (express warranty) or by implied warranties of good and workmanlike performance and/or habitability, as discussed in detail above.
- Negligence – It is very typical to work in a negligence claim, primarily, in my opinion, to access insurance.
- Delay claims – Do not typically see the delay and impact claims that you encounter in commercial, especially governmental, project claims.
- Texas Deceptive Trade Practices Act – Historically used much more in residential construction disputes than in commercial ones. Ability to proceed under the DTPA seemed to be lessening under case law and the TRCCA. For example, a breach of the TRCCA warranties, by itself, did not support a DTPA action under Tex. Prop. Code §430.011(c). With the sunsetting of the TRCCA, I would not be surprised to see a resurgence of the use of the DTPA in homeowner litigation and arbitration.
- Texas Prompt Payment Act (Tex. Prop. Code Chapter 28) – As stated above, owner can retain 110% of disputed amount; and there is no statutory provision for demobilizing on project for non-payment, like there is in the commercial context.
- Uniform Declaratory Judgments Act – Use in voiding mechanic's liens (*see* below) (same for residential and commercial, just even easier in residential).

IV. MECHANIC'S LIENS IN RESIDENTIAL CONSTRUCTION

A. Definition of "Residential Construction"

Keys off who is owner of project. If performing construction or remodeling for homeowner, going to be residential. This is different from a volume builder that owns a large tract of land and builds houses on it to sell – this is not residential construction under the statute, even though is building houses. The pertinent definitions are as follows:

> "Residence" means a single-family house, duplex, triplex, or quadruplex or a unit in a multiunit structure used for residential purposes that is:
>
> (A) owned by one or more adult persons; and
> (B) used or intended to be used as a dwelling by one of the owners.

"Residential Construction Contract" means a contract between an owner and a contractor in which the contractor agrees to construct or repair the owner's residence, including improvements appurtenant to the residence.

"Residential construction project" means a project for the construction or repair of a new or existing residence, including improvements appurtenant to the residence, as provided by a residential construction contract.

Tex. Prop. Code §§53.001(9), (10), and (11).

B. Trapping Notice

1. 15th day of Second Month

2. If you are a Subcontractor or Supplier, must send to Owner and Original Contractor, regardless of what tier.

3. Additional requirement in notice if Homestead - "If a subcontractor or supplier who furnishes materials or performs labor for construction of improvements on your property is not paid, your property may be subject to a lien for the unpaid amount if: (1) after receiving notice of the unpaid claim from the claimant, you fail to withhold payment to your contractor that is sufficient to cover the unpaid claim until the dispute is resolved; or (2) during construction and for 30 days after completion of construction, you fail to retain 10 percent of the contract price or 10 percent of the value of the work performed by your contractor. If you have complied with the law regarding the 10 percent retainage and you have withheld payment to the contractor sufficient to cover any written notice of claim and have paid that amount, if any, to the claimant, any lien claim filed on your property by a subcontractor or supplier, other than a person who contracted directly with you, will not be a valid lien on your property. In addition, except for the required 10 percent retainage, you are not liable to a subcontractor or supplier for any amount paid to your contractor before you received written notice of the claim." Tex. Prop. Code §§53.252 and 254.

C. Mechanic's Lien Affidavit

1. 15th day of Third Month after indebtedness "accrues"

2. Homestead - (1) The original contractor and the owner must execute a written contract setting forth the terms of their agreement; (2) the contract must be signed before the material is furnished or the labor is performed; (3) if the owner is married, the contract must be signed by both spouses; (4) the contract must be filed with the county clerk of the county in which the homestead is located; and (5) the lien affidavit must contain the following notice conspicuously printed, stamped, or typed in a size equal

to at least 10-point boldface or computer equivalent, at the top of the page: "NOTICE: THIS IS NOT A LIEN. THIS IS ONLY AN AFFIDAVIT CLAIMING A LIEN."

3. Remember must send notice of lien filing to Owner and Original Contractor within five days of filing.

D. Foreclosure

The time period in which to file suit to foreclose a residential mechanic's lien is, "within one year after the last day a claimant may file a lien affidavit under Section 53.052 or within one year after completion, termination, or abandonment of the work under the original contract under which the lien is claimed, whichever is later." Tex. Prop. Code §53.158.

E. Removing

There is no difference in the mechanic's lien removal procedure between the residential and commercial context, however, you have many additional grounds for lien removal. As seen above, liening residential projects is more complex, and the time periods are shorter, thus allowing for even better chances of lien removal. Having said this, in my experience, people in the construction industry, in response to the recession and the need to ensure payment, have become much more sophisticated at lien perfection and filing.

The actual way to remove a lien is beyond the scope of this paper; however, there are generally two methods, both involving a lawsuit: (1) the summary lien removal process of Tex. Prop. Code §53.160; or (2) by summary judgment. These procedures are addressed in detail in the Texas Residential Construction Law Manual.

V. THE CONSTITUTIONAL LIEN – THE HOMESTEAD WRINKLE

There is an entire chapter in my book, the Texas Residential Construction Law Manual, on the Constitutional Lien. In that chapter, I have tried to distill everything I could find on the Constitutional Lien. That type of overview is beyond the scope of this paper, and if interested, I commend you to the Manual or to my paper at the Texas State Bar 27th Annual Construction Law Conference – 2014. However, I think the primary benefit of that Chapter is a chart that graphically shows the differences in the Constitutional Lien when you are in the homestead arena. Here is the chart:

Constitutional Lien Simplified Chart

<table>
<tr><th>Commercial</th><th colspan="3">Residential</th></tr>
<tr><td rowspan="2">Self-executing</td><td>Non-Homestead</td><td colspan="2">Homestead</td></tr>
<tr><td>Self-executing</td><td>New Construction</td><td>Remodel</td></tr>
<tr><td rowspan="8"></td><td rowspan="8"></td><td>Contract in writing[1]</td><td>Contract in writing[1]</td></tr>
<tr><td>Contract terms set forth[2]</td><td>Contract terms set forth[2]</td></tr>
<tr><td>Contract executed before material furnished/labor performed[3]</td><td>Contract executed before material furnished/labor performed[3]</td></tr>
<tr><td>Contract signed by both spouses (if married)[4]</td><td>Contract signed by both spouses (if married)[4]</td></tr>
<tr><td>Contract filed with County[5]</td><td>Contract filed with County[5]</td></tr>
<tr><td rowspan="3"></td><td>Contract cannot be signed until 5th day after apply for loan[6]</td></tr>
<tr><td>Three day out without penalty[7]</td></tr>
<tr><td>Contract signed at office of lender, attorney, or title company[8]</td></tr>
</table>

[1] Tex. Const. Art. XVI, § 50(a)(5)
[2] Tex. Prop. Code § 53.254(a)
[3] Tex. Prop. Code § 53.254(b)
[4] Tex. Prop. Code § 53.254(c)
[5] Tex. Prop. Code § 53.254(e)
[6] Tex. Const. Art. XVI, § 50(a)(5)(B)
[7] Tex. Const. Art. XVI, § 50(a)(5)(C)
[8] Tex. Const. Art. XVI, § 50(a)(5)(D

VI. PREPARING, MEDIATING, AND ARBITRATING THE RESIDENTIAL CONSTRUCTION CASE

A. Introduction

I have mediated (both as practitioner and as mediator) and arbitrated (both as practitioner and as arbitrator) construction defect cases, including residential construction defect cases, for over twenty years. The following are my experiences, thoughts, and opinions with respect to both common elements between residential construction cases and other types of cases, as well as things unique to residential construction cases. I hope you find the following admittedly colloquial thoughts and hints helpful in your future practice.

B. Preparation and Suggested Work Flow

The following is an overview of what one should typically expect the work flow to look like when representing a homeowner in a residential construction defect case. As the attorney representing the homeowner, when a residential construction defect case comes in, here is what I would do: (1) Sit down with the client, preferably at their home, and get a full understanding of their complaints. You must also take this opportunity to fully explain the upcoming process to the homeowner, including the RCLA process, the process after the RCLA, the timing aspect, and the cost.[10] (2) Have your client retain the expert or experts.[11] (3) Have the expert or experts do their inspection.[12] (4) Have the expert or experts prepare a well written report documenting, with pictures (and maybe video), the defects, remedial actions to be taken, and their cost.[13] (5) Prepare and send the RCLA demand letter. (6) Cooperate with the opposing party/counsel in arranging and

[10] The truth is that most residential construction defect cases, especially those with structural issues, are expensive and time consuming. In my experience, there is hardly ever a quick and easy settlement of these types of cases. There is typically simply too much at stake. It is best to let the homeowner know what they are facing from the very beginning.

[11] Please see the comments below as to my opinion on the importance of the expert(s) in a residential construction defect case. Also, if there is a structural issue, you are going to need an engineer, as well as a general construction expert.

[12] This has to be a thorough inspection. The experts should cover everything that could possibly be wrong. In many cases, this is going to require some destructive testing, such as brick removal, to see hidden conditions. As an advocate, I have tried in the past to do a cost-saving, two-prong attack – a general inspection/report leading to the RCLA letter, followed by mediation, to be followed by a more thorough (i.e. more costly) inspection/report if mediation is unsuccessful. I have also seen the same strategy as a mediator. In my experience, this strategy, though laudable from a cost-savings perspective, uniformly does not work in residential construction defect litigation. The truth is that if a defect is not thoroughly documented, the builder (and maybe more importantly – their insurance company or home warranty company) are not going to give much credence to this defect at mediation. Only fully documented defects are given weight at mediation.

[13] In preparing this report, you should approach this with the expectation that insurance and/or a third party home warranty company will be involved. Obviously if the homeowner has a third party home warranty, you should obtain and be familiar with the actual warranty. You may also be lucky enough to have a copy of the builder's insurance policy. If not, you should nevertheless be familiar with general insurance claim concepts, such as what is an occurrence, what is typically covered, and what is typically excluded from coverage. The expert should then work with the attorney to phrase the report in terms of maximizing coverage.

conducting the RCLA inspection. (7) Upon receipt of the RCLA offer, analyze same, with input from the client and the expert(s), and respond to the offer in a detailed, well-reasoned letter. Assuming the offer is not acceptable, this is the earliest point in the process in which it makes sense to consider teeing up the mediation. Again, it's unfortunate, but it also seems to be more effective to go ahead and have your arbitration action/lawsuit filed before teeing up the mediation.

Here is a typical work flow for the attorney representing the builder or a related responding party. Usually your introduction to the dispute will consist of being presented by your client with an RCLA notice. At this point, I would suggest you proceed along the following lines: (1) Have a detailed, face-to-face meeting with the client to develop their factual background. Sometimes it makes sense to divide this up into an initial meeting with the client's principal, immediately followed by bringing in one or more of the client representatives that were actually on the ground at the project, such as the project manager or superintendent. If the client is new to the process, then use the meeting with the principal to prepare his or her expectations as to how the process is likely to proceed. (2) Have the client retain your go-to expert(s). (3) Request an RCLA inspection of the project/property.[14] (4) Conduct the inspection with your client and expert(s). Make sure you attend. You need to have firsthand knowledge of the condition of the project. (5) Make sure your expert will give you a fast turn-around on their findings/report; you need this information for your RCLA offer of settlement. (6) Make a timely, well-written, well documented RCLA offer of settlement.[15] (7) If the offer is accepted, make sure repairs are completed in 45 day time period. If the offer is rejected, review the written rejection (assuming there is one), and give serious consideration to making the second bite at the apple offer. Generally, it is after these stages that the matter should most likely be ripe for mediation.

C. Mediation

If there is one, overarching theme that I would like to stress with respect to mediation, it is preparation. The truth is that over 85% of cases are going to end at mediation – in other words – they are going to settle at mediation. Mediation is the modern version of trial. Up to about twenty years ago or so, almost all cases either settled right before trial, often "on the courthouse steps" as we used to say, or were tried. With the advent of mediation, this is no longer true. Mediation has largely accomplished what its purpose was – to get cases resolved at a point before excess attorney's fees had been spent on the case. The truth is that mediation is the new trial. What I mean by this is that whereas traditionally trial, or the threat of imminent trial, was the paramount

[14] Remember, you have a 35 day window from the date of receipt of the written RCLA notice to request and conduct the inspection of the project/property, and 45 days from the date of the notice to make an RCLA offer of settlement. Do not procrastinate. Get the expert retained quickly; request the inspection quickly; conduct the inspection on the earliest date you can – give yourself as much time as you can to formulate your RCLA offer of settlement.

[15] Note that if the homeowner does not permit the statutorily required inspection, you are entitled to abate any litigation or arbitration until such is provided. Tex. Prop. Code §27.004(d). Also, be aware that there is a procedure for requesting extensions. In my experience, these are routinely granted. As in all such situations, request the extension as soon as you know you will need it. Tex. Prop. Code §27.004(h).

dispute resolution mechanism, mediation now takes this role for the vast majority of cases. As such, mediation should be taken very seriously, and a fair amount of preparation should go into the pre-mediation process. Obviously, like any other case, the attorney has to balance preparation with cost. It would make no sense to have all of the preparation needed for going to trial done prior to mediating – you would lose the paramount benefit of mediation – cost savings. On the other hand, in my experience, over the first decade or so of the prevalence of mediation, attorneys and their clients would simply show up at the mediation and "fly by the seat of their pants." Over the past decade, I have seen a definite shift – most attorneys and their clients appear at mediation pretty well prepared – in other words, they understand the strengths and weaknesses of the opposing parties case, and maybe more importantly, of their own case; and they do a good job of communicating these to the mediator and opposing parties. I still occasionally do encounter attorneys who appear at mediation with no real clue as to the value and weaknesses of their case, and with unrealistic expectations of settlement. If the attorneys appear in this mode, you can just imagine where their clients' thought processes are. These mediations are typically doomed to failure. This is unfortunate, as these cases are likely to settle at some point, but at a much higher cost to the parties.

The foregoing comments are largely true with respect to mediations in general, not just with respect to residential construction defect mediations. Where the residential construction defect mediation differs from other types of cases is in the type of preparation necessary, and the ideal time to mediate. The unfortunate truth is that it is highly unlikely that an early mediation of a residential construction dispute will result in a settlement. There are, in my opinion, three essential elements that have to be fulfilled before a mediation of a residential construction dispute has a good chance of settling; these are: (1) the homeowner must have a solid, credible expert; (2) the homeowner must have a solid, credible report from that expert detailing the defects, what is needed to fix them, and the cost; and (3) the responding party or parties should have a responsive report. I cannot over-emphasize, and it will be repeated below, the importance of the expert to residential construction litigation.[16] Other than the underlying facts, your expert is going to be the most important element of your case. He or she will likely make or break your case. If you practice in the area of residential construction defects, whether from the claimant's or respondent's side, you should have go-to experts on which you are comfortable relying. Ultimately the vast majority of these cases are a battle of the experts, and of those that are actually tried, the arbitrator, judge, or jury, as applicable, is likely to default to who they believe is the more credible expert. Similarly, the expert reports should be well thought out and written. This works well in residential construction litigation anyway, since you should comply with the requirements and provisions of the RCLA. Since the RCLA requires a homeowner to give a detailed listing of the homeowner's complaints to the builder; and since it allows the builder to inspect the complaints and provide a written offer of repair; and since there are serious ramifications with respect to how the parties handle this process; the RCLA process fits in very well with my following recommendation on preparing to mediate the residential construction defect case.

[16] Actually, my views here are true for construction defect litigation in general, not just residential.

As set forth above, in order for a residential construction defect case to have a good chance of settlement at mediation, one should have at least completed the RCLA process. There should be a well-grounded and documented expert report forming the basis of the complaints; an inspection by the builder (and any other applicable parties, like an insurance adjuster, a home warranty company representative, and their experts) should have occurred; and hopefully there is a well-grounded and documented response from the builder and any other parties. This enables everyone to have a good understanding of everyone's positions prior to the mediation session. In my experience, laying behind the log and springing issues and/or costs on the other side at mediation almost always leads to one result – a failed mediation.

With respect to preparation, prepare a mediation position paper and forward to the mediator at least three days prior to the scheduled mediation. This is imminently easy in a residential construction case, since all essential elements of such a paper are likely already set forth in RCLA letters – either the notice and rejection of settlement offer, if representing the homeowner(s), or in the settlement offer and "second bite at the apple," if representing the builder. These typically can be very easily converted into a mediation position paper for the mediator. I would also definitely forward your expert report(s), as well as your latest pleading, to the mediator. Help the mediator help you. Most mediators appreciate the opportunity to have a good feel for your case beforehand; it helps them mentally prepare for your mediation. Take advantage of this opportunity.

D. Arbitration

Probably not surprisingly, again the most important aspect of arbitrating a case is preparation. By preparation, I am not only talking about preparation for the hearing, but rather being prepared at every step of the arbitration. The key here is to understand that arbitration is your trial. Take it seriously. Too many people treat the arbitration procedure and its deadlines as mere guidelines that are easily ignored. Just because you are not faced with the formality of court proceedings does not mean you can be lulled into not taking the arbitration process seriously. (By the way, I have noticed over the past decade a definite trend toward attorneys treating arbitration equally as seriously as litigation, especially in the construction arena, where we tend to be more familiar with arbitration as a dispute resolution forum.) Docket all of your arbitration deadlines just as you would your court deadlines, and abide by them.

Typically the arbitration process commences with a prehearing telephone conference with the arbitrator and the parties' attorneys. Everyone knows (or should know) that the primary purpose of this conference is to schedule the hearing dates, and to schedule the other deadlines in the case. I cannot tell you how many times I have participated in such a conference in which one of the attorneys does not even have their own calendar, or does not know his or her clients'/experts' availability. It is not uncommon that I will be near the end of a half-hour scheduling conference, with all dates/deadlines filled in, when I hear something along the following lines: "OK, before you finalize these dates, I need to run them by my Client." Do not let this happen to you – know your clients' and experts' schedules ***before*** the preliminary conference. The

prehearing or preliminary conference is often your first chance to interact with your arbitrator – make a good impression by being prepared.

Related to the foregoing, here is a recipe for really impressing your arbitrator at the prehearing conference: submit a proposed agreed scheduling order beforehand. If you cannot reach agreement with your opposing counsel on all aspects of such an order, submit what can be agreed to, and argue over the rest. If you cannot reach agreement on any aspect of such an order with opposing counsel – submit the proposed scheduling order to the arbitrator stating that you have tried to reach agreement with opposing counsel but have been unable to do so, but you are submitting the proposed scheduling order for the arbitrator's convenience at least as a starting point.[17] (Which of the two attorneys involved is going to look better to the arbitrator in this situation? Be the proactive attorney who is trying to make the arbitrator's job easier.)

Also related to the foregoing – at the very least, try to provide, if at all possible, a range of hearing dates to the arbitrator before or at the commencement of the prehearing conference. Hopefully opposing counsel and you can either agree to a date or range of dates, or at least narrow the range to a couple of months to give the arbitrator something to work with. (Again, if you are simply not in the same ballpark as opposing counsel, then at the hearing all you can do is state that you attempted to reach agreed upon dates, were unsuccessful, and offer up your dates with argument as to why they make sense.)

If you are digitally/electronically adept (or someone on your staff is), at the prehearing conference, find out from your arbitrator what their preference is for hearing exhibits. Many still prefer notebooks with paper in them. Others commonly use laptops, and would prefer exhibits on a flash drive, especially for multi-day hearings with heavy documentation. Carrying a flash drive is much easier, than a slew of three-ring binders. (Most arbitrators will either request notebooks or advise the attorneys that the choice is up to them. When faced with the latter, I would provide the arbitrator with ***both*** notebooks and a flash drive.)

Treat your arbitrator with respect. You would think this would go without saying, after all this is the person that will determine your Client's fate in this dispute. Most attorneys adhere to this tenet. Nevertheless, I am surprised at the number of attorneys who will argue with (as opposed to arguing ***to***) their arbitrator, or raise their voice to their arbitrator. Arbitrators are impartial; they are also human. In my experience, the strength of an attorneys' argument is inversely proportional to how aggressively they make it. By all means one should be passionate, one can even get loud, but there is a line between advocacy, and just being obnoxious. Crossing the line does not do the client any favors.

On a related note, when trying your case to the arbitrator remember your audience. Generally you should not be trying the case to the arbitrator in the same manner that you might see a TV or movie lawyer character trying his or her case to a

[17] Obviously follow proper protocol in your submittal; *i.e.*, no *ex parte* contact. If there is a case administrator, such as through the AAA, submit to the case administrator. If there is not, copy opposing counsel on all communications to the arbitrator.

jury. Drama does not generally carry well with arbitrators. They want – "the facts, and just the facts" (well, and the law). For example, the classic "badgering the witness" is highly unlikely to help your cause at all in front of an arbitrator. Most likely it will get you an admonition with the arbitrator coming to the witness' defense. Again, I am not suggesting a lifeless, boring presentation. A little bit of drama, raised voice, incredulity, at the right time is part of effective advocacy. It is its overuse that will potentially lose you your audience in an arbitration.

If you are representing the homeowner (and sometimes when representing the builder), you are generally going to want a site visit to be part of your presentation. I would go ahead and put the arbitrator on notice, at the prehearing conference, that you will likely be requesting a site visit as part of your presentation of evidence at hearing. Be aware, arbitrators want to see the site. I do not think I have ever seen a situation where one of the parties has requested a site visit, and the arbitrator has denied same. If a picture is worth 1000 words, you can imagine what the site visit is worth.[18]

Somewhat related to the foregoing, at the hearing, arbitrators like demonstrative evidence – pictures, video, charts, plans, summaries, mockups, etc. Use these freely. They break up testimony (in a good way), and they help clarify what is being testified to.

Cross-examination – keep it short, targeted, and sweet. Prove your case through your direct testimony. I cannot tell you how many attorneys try to prove their case through an opposing witness by cross-examination (usually with open ended questions). These attorneys will commonly go, check list style, through every single statement the opposing witness made on direct, or through practically every single line of their report. Not surprisingly, the vast majority of this testimony simply confirms and affirms what the witness already testified to, and if the attorney does manage to get a good answer out of the witness, it is buried in the tedium of all the other questioning. We were all taught in law school to pick three or so key areas for cross examination, nail them, and move on. For some reason, at least in arbitration, a fear seems to take over that anything not questioned on cross will be taken as true by the arbitrator. Again, my suggestion to you is use ***your*** witnesses to prove your case and to rebut the other side's facts and arguments as much as possible; using opposing witnesses to do so is not likely to work.

Use opening argument for a general factual overview of what you expect the arbitrator to hear; use closing argument to argue the law. Do not use closing to recount to the arbitrator, in check list fashion, everything the arbitrator has heard for the past few days. Closing argument should be the time for you to argue and present the applicable legal concepts to the arbitrator (I would suggest with targeted, written briefing, citing statutes, cases, etc.), with a limited overview of key evidence, facts, and testimony heard previously by the arbitrator that support such legal arguments.

[18] In my experience, both parties are almost always in agreement on the propriety of a site visit. If you are opposing a site visit, you are putting yourself in a pretty awkward situation. Can you imagine – Mr. Arbitrator, I really do not want you seeing the site!

E. Typical Arbitration Process

Every arbitration has its own unique aspects. Procedures can be different depending on the provider used, or whether there even is a provider. Nevertheless, the following should give you a good starting point on what to typically expect in the arbitration process. (Rather than start each of the following with "Typically" or "Generally," keep in mind this is a typical arbitration work flow; each arbitration will likely have some unique aspects within this general framework.)

1. Demand for Arbitration – Arbitration is commenced with a written demand for arbitration. This is a simple, often one page, document outlining the parties and claims, and usually has a copy of the arbitration agreement attached.

2. Answering Statement – Within 15 days of the arbitration filing the responding party files an Answering Statement. Often if there is a counterclaim, it is at least generally addressed in the Answering Statement.

3. Choosing Arbitrator – If you are using an arbitration provider, you will be given a listing of arbitrators, their biographies and rates, and asked to strike any that are objectionable, and rank the rest in order of preference. The other party will do the same. Usually the highest, matching arbitrator will be appointed. If no arbitrator arises out of this process, each provider has a procedure for appointing an arbitrator. Conversely, the parties may agree to an arbitrator beforehand.

4. Prehearing conference – A prehearing conference is scheduled for the purpose of setting a hearing date, setting the other deadlines in the arbitration case, and addressing any other issues. This is almost always conducted by telephone. In my experience, only attorneys usually attend; although there is nothing wrong with also having your Client on the line if you so desire.

5. Specification of Claims/Counterclaims – One of the first deadlines after the prehearing conference is a deadline to specify claims and counterclaims. This is usually done in a pleading format, and is more detailed than the Demand for Arbitration/Answering Statement.

6. Joinder of Third Parties – Another fairly quick deadline is the one to join any third parties (usually subcontractors or suppliers who are also bound by an arbitration agreement). From the Claimant's perspective, this deadline should be relatively quick, as a late joinder is likely to lead to a continuance of the hearing date, and a pushing out of all deadlines, to accommodate the newly joined party.

7. Discovery – There will be an exchange of relevant documents. Discovery will generally be more limited compared to a court case. However, it is not uncommon to allow for deposition of experts, and maybe of the main parties – the homeowners and the builder's representative.

8. Deadline to designate experts and provide expert reports.

9. Exchange of Witness List and Exhibits – Shortly before the hearing, usually one to two weeks before, the parties will exchange witness lists and exhibits to be used at the hearing.

10. The hearing.

11. Typically the arbitrator has thirty days from the close of the hearing to render an award. In smaller damages cases, this may be two weeks.