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How Condo Law Change Will Impact New Development

Are Twin Cities' Developers Finally Going To Break Ground On New Condos?

By Kristin Rowell, Esq.

Newsflash Minnesotans: our state laws governing condominiums and townhomes changed at the conclusion of the 2017 legislative session. For a business litigator who emphasizes a significant portion of her practice representing real estate developers in complex business disputes, I've been particularly interested in the evolution of these changes. Why? Because condominium development has stalled in recent years, and the prevailing belief amongst experts in the field (including my clients) is that the dearth in condominium development has little to do with our economy (indeed, there is no shortage of demand for condos), but rather the influx of construction defect litigation in this state. Those who know of this cottage industry of litigation know what I am talking about—litigation commenced by homeowners' associations, often with minor or meritless construction defect complaints, where the attorney's fees and other costs are excessive, making the potential costs associated with the condominium development project not worth the risk.

That litigation risk—largely in the form of the cost of defending against claims brought by homeowners' associations years after the development was constructed and sold—made even the most confident and well-respected developers gun shy about spending millions of dollars on a quality project. The problem with the law is that the statute of limitations, often referred to as the "liability tail" for construction defect claims, means that developers (and most or all of those in the developer's chain of command) can be sued for the most minor infraction as much as a decade or more after the project is completed. The majority of developers decided that the cost to defend itself against litigation, often meritless, wasn't worth the risk.

Are there legitimate claims by homeowners' associations for defective construction? Absolutely. But the reality is that the Minnesota legislature did not intend by its law to create a cottage industry of construction defect litigation by aggressive plaintiff's attorneys shopping for claims. As you may have deduced by now, I am fiercely protective of my developer clients. And, as beautiful and successful as my clients' luxury apartment projects are, I am personally ready for developers to start building condominiums again. Jim Stanton's recent passing has left yet another hole in condo market. It is finally time for condo development to recommence.

Here's the good news: after tireless work by numerous stakeholders, the 2017 legislative session resulted in a number of changes to the Minnesota Common Interest Ownership Act ("MCIOA") codified in Minnesota Statutes § 515B that affect our state's construction defect laws (primarily found in Minnesota Statutes Chapter 327A). The changes to Minnesota Statutes § 515B went into effect just a few weeks ago—on August

1, 2017—so I thought it was the perfect time to summarize them. With a few exceptions, the changes apply to all condominium and townhome associations created on or after that date.

The following is a summary of the 4 primary changes to the MCIOA affecting construction defect claims in Minnesota. Lawyers representing condominium developers, construction companies, homeowners' associations and others associated with new condominium developments should take note of these changes.

Change 1: Definitions of "Construction defect claim" and "Development party"

For the first time, the terms "construction defect claim" and "development party" are defined in MCIOA. Specifically:

> "Construction defect claim" means a civil action or an arbitration proceeding based on any legal theory including, but not limited to, claims under [Minnesota Statutes] chapter 327A for damages, indemnity, or contribution brought against a development party to assert a claim, counterclaim, cross-claim, or third-party claim for damages or loss to, or the loss of use of, real or personal property caused by a defect in the initial design or construction of an improvement to real property that is part of a common interest community, including an improvement that is constructed on additional real estate pursuant to section 515B.2-124. "Construction defect claim" does not include claims related to subsequent maintenance, repairs, alterations, or modifications to, or the addition of, improvements that are part of the common interest community, and that are contracted for by the association or a unit owner.

Minn. Stat. §§ 515B.1-103(11a). As is clear from the language of this provision, the purpose is to define what is included in the bucket of construction defect claims and perhaps more importantly, what is not. The same is true for the new definition of "development party," which states:

> "Development party" means an architect, contractor, construction manager, subcontractor, developer, declarant, engineer, or private inspector performing or furnishing the design, supervision, inspection, construction, coordination, or observation of the construction of any improvement to real property that is part of a common interest community, or any of the person's affiliates, officers, directors, shareholders, members, or employees.

Minn. Stat. §§ 515B.1-103(16a). Now the list of professionals against who construction defect claims may be sought is more clearly defined.

Change 2: Authorization Before Homeowner's Association Can Sue

Another important change is that a homeowner's association ("HOA") board cannot just launch into litigation without obtaining approval from HOA membership. Now, "before instituting litigation or arbitration involving construction defect claims against a development party," the HOA must:

> (1) Mail or deliver notice of the anticipated commencement of the action to each unit owner, and the notice must "specify the nature of the construction defect claims to be alleged, the relief sought, and the manner in which the association proposes to fund the cost of pursuing the construction defect claims," and
>
> (2) Obtain approval of the majority of unit owners in the association. Votes may be obtained at an annual or special meeting of the members of the HOA or by electronic means if allowed by the association documents.

Although there are exclusions for votes allocated to units owned by foreclosure mortgagees or persons related to the declarant, the purpose of this added provision is to make sure that the majority of the HOA is on board with pursuing the construction defect claims so that the HOA has some say in the process.

Minn. Stat. §§ 515B.3-102(d).

Change 3: HOA Must Maintain And Adhere To Preventative Maintenance Plan

New to the "Upkeep of Common Interest Community" section in the law is Minn. Stat. § 515B.3-107(b), which requires the HOA's board of directors to "prepare and approve a written preventative maintenance plan, maintenance schedule, and maintenance budget for the common elements." It also requires the HOA to follow it, and all owners in the HOA must be provided with a copy of the plan and maintenance schedule. "If a common interest community was created on or before August 1, 2017, the association's board of directors shall have until January 1, 2019, to comply with the requirements of this subsection."

The purpose here is to limit a development party's damages if the HOA or its owners do not prepare or comply with the plan. Specifically:

> A development party shall not have liability under this section for loss or damage caused by the failure of the association or a unit owner to comply with obligations imposed by section 515B.3-107, unless the loss or damage is caused by failure to comply with section 515B.3-107 while the declarant controlled the board.

Minn. Stat. § 515B.4-113(h).

Change 4: Pre-Litigation Mediation Requirement

Last but certainly not least is the new pre-litigation mediation requirement. I think of this provision as a compromise between leaving the MCIOA's attorney's fees provision in the law and taking it out. The new mediation provision states:

> As a condition precedent to any construction defect claim, the parties to the claim must submit the matter to mediation before a mutually agreeable neutral third party under Rules of Civil Procedure, rule 114.02(7). If the parties are not able to agree on a neutral third-party mediator from the roster maintained by the Minnesota Supreme Court, the parties may petition the district court in the jurisdiction in which the common interest community is located to appoint a mediator. The applicable statute of limitations and statute of repose for an action based on breach of a warranty imposed by this section, or any other action in contract, tort, or other law for any injury to real or personal property or bodily injury or wrongful death arising out of the alleged construction defect, is tolled from the date that any party makes a written demand for mediation under this section until the latest of the following:
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> (1) five business days after mediation is completed; or
>
> (2) 180 days.
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> Notwithstanding the foregoing, mediation shall not be required prior to commencement of a construction defect claim if the parties have completed home warranty dispute resolution under section 327A.051.

Minn. Stat. § 515B.4-116(c). In short, before an HOA can sue a development party for a construction defect claim, the parties have to sit down and determine whether they can resolve their dispute through mediation. One of the primary purposes of this added provision is to ferret out meritless claims and resolve legitimate claims early in the process, before both parties spend a significant amount of money on litigation.

It remains to be seen how these changes will affect future construction defect litigation in Minnesota. I am personally excited about these changes and look forward to new condominium projects coming in the spring of 2018.

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"Buying real estate is not only the best way, the quickest way, the safest way, but the only way to become wealthy."

– Marshall Field