



CALIFORNIA DECISION APPROVES SHORTENING STATUTES OF LIMITATION AND ELIMINATING THE DISCOVERY RULE VIA CONTRACT

In *Brisbane Lodging, LP v. Webcor Builders, Inc.*, No. A132555 BL 146042 (June 3, 2013), the California Court of Appeal (First District, Division Four) recently confirmed that parties can contractually agree to limit not only statutes of limitation, but can also agree to the date from which the statute of limitation will commence. This represents an important clarification to any party entering into a construction agreement where the statute of limitation is generally tolled for unknown (latent) defects until such time as the defects are discovered or should have been discovered through reasonable diligence (the “discovery rule”).

BACKGROUND AND SIGNIFICANCE OF *BRISBANE LODGING*

Construction defect cases in California have long operated under the statutes of limitation and repose dictated in California Code of Civil Procedure

sections 337.1 and 337.15. These sections provide a four-year window to bring suit for a “patent” defect and a 10-year window to bring suit for a “latent” defect—both periods commencing at the date of substantial completion. Patent and latent defects are defined in the Code of Civil Procedure:

CCP § 337.1(e): As used in this section, “patent deficiency” means a deficiency which is apparent by reasonable inspection.

CCP § 337.15(b): As used in this section, “latent deficiency” means a deficiency which is not apparent by reasonable inspection.

When a latent defect manifests itself (becomes patent to a reasonable observer), the statutory framework requires a suit to be filed on the newly discovered defect (arising out of a breach of contract) within four years of discovery. *Regents of the*

University of California v. Hartford Accident & Indemnity, Co., 21 Cal.3d 624, 630; see also CCP § 337 (four-year statute of limitation for breach of contract). This “discovery rule” effectively acts to toll the statute of limitation period on construction defects until they become reasonably apparent. *Id.*

The court in *Brisbane Lodging*, accepting the limitation periods identified above, has now held that parties can contractually manipulate the statute of repose on latent defects. The court validated a contractual clause that effectively eliminated the discovery rule tolling period for latent defects by stating that all statutes of limitation would run from the date of substantial completion for work performed prior to the substantial completion of the project. The relevant portion of the clause, cited by the court and taken from AIA A201 1997, reads:

As to acts or failures to act occurring prior to the relevant date of Substantial Completion, any applicable statute of limitations shall commence to run and any alleged cause of action shall be deemed to have accrued in any and all events not later than such date of Substantial Completion....

As a result, any party that entered into a contract incorporating the same portion of the A201 1997 general conditions (or similar language) should take this decision into consideration when evaluating contractual rights arising out of construction defects. As a broader result, *Brisbane Lodging* has solidified the contractual dynamic that two sophisticated parties jointly drafting and negotiating a contract can agree to modify the statute of limitation for construction defects. And, in fact, parties to a contract can now effectively eliminate the 10-year statute of repose for latent defects.

From a contractor or design professional standpoint, *Brisbane Lodging* would appear to be a victory; it sanctions their ability to negotiate the time period in which they may be liable for construction defects. In contrast, an owner might view this decision as eroding its ability to rely upon the workmanship of the designer and/or the builder up to a 10-year period. In reality, this opinion should be viewed as the court’s recognition that two sophisticated parties can

negotiate the duration of obligations to the owner and the amount that the owner is willing to pay for those obligations.

Taking a longer view of the effect of this decision is also important. Any party entering into an agreement that reduces the statutory limitation period will need to take the time and effort to contemplate a number of issues, including:

- Whether or not to include a flow-down provision or duplicate provision in subcontracts;
- How the inclusion of this clause will affect indemnity obligations (for the contractor and the subcontractors as indemnitors and the owner and design professionals as indemnitees) and what separate language may be necessary to clarify the indemnity obligations;
- What effect the waiver may have on equitable indemnity claims after the tolling period;
- Potential modifications or credits associated with costs normally assigned to contingency allowances for long-term defect obligations;
- The post-completion insurance requirements (commercial general liability insurance and additional insured obligations);
- Whether or not the subcontractors are third-party beneficiaries of the contractual limitation;
- Implications on subsequent purchasers or injured third parties without privity with the contractor; and
- Potential conflicts with the statutory time periods set forth by SB800 (CCP sections 895-945.5) in the case of negligence actions on residential construction.

In summary, while *Brisbane Lodging* provides some clarity regarding parties’ ability to define liability periods through contract, those limitations will have collateral effects that all parties should consider when negotiating or litigating a contract with similar limitations.

Note: The *Brisbane Lodging* case relied upon somewhat convoluted language in the AIA A201 1997 document that, based on the parties' initial responses and the willingness to file and appeal, may not have been fully appreciated or uniformly accepted. The current version of the AIA A201 (2007) has resolved an ambiguity related to the commencement of the limitation periods. It reads:

The Owner and Contractor shall commence all claims and causes of action, whether in contract, tort, breach of warranty or otherwise, against the other arising out of or related to the Contract in accordance with the requirements of the final dispute resolution method selected in the Agreement within the time period specified by applicable law, but in any case not more than 10 years after the date of Substantial Completion of the Work. The Owner and Contractor waive all claims and causes of action not commenced in accordance with this Section 13.7.

LAWYER CONTACT

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