

# High-End Headaches:

## Why High-End Home Construction Litigation Is So Difficult To Resolve

**Article by Pete Fowler**

On paper, it was a perfect match. A wealthy family wants to build their dream home. The owner's spouse knows the spouse of a small local builder. The owner and builder meet after their spouses connect them. They hit it off. They quickly reach an "agreement." The construction begins with excitement. The builder receives the first few progress payments. The process seems to be humming along. But then things take a turn for the worse. It turns out the "contract price" was really a budget. Each selection the owner makes, including roofing, siding, windows, doors, cabinets, and flooring, is more expensive than the "allowance" in the budget, so the price increases weekly.

The honeymoon is over. There is palpable tension. The owner and builder barely speak.

Adding insult to injury, the owners catch mistakes. They ask for changes to bathroom six, but the builder forgets. The subcontractors seem incompetent: Wrong plumbing fixtures are installed. Electrical outlets are in wacky places. The owners are so worried that they audit the invoices. They find discrepancies. They hope it's negligence but are concerned because each "mistake" benefits the builder.

Construction limps toward completion. A certificate of occupancy is issued.

The owners finally move in, but the home took twice as long to build and cost twice as much as promised. Even worse, more problems emerge. Those wood doors facing the sun that the owner insisted on, despite the builder's warning they would warp, begin to warp. The home automation system never works. Cooling bedroom four to a comfortable temperature turns bedroom five into a meat locker. The first rains come, and the roof and windows allow water to pour into the home.

The owners insist the builder immediately fix everything. As a precaution, the owners withhold final payment. The builder then stops responding to complaints. That causes the owners to go ballistic and instruct their personal lawyer—who has no construction law experience—to file a lawsuit. The owner and builder are now engaged in a kind of litigation—high-end home construction litigation—that is notoriously difficult to resolve.

**Here are four reasons why.**



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# Emotions run high

The parties to a high-end home construction lawsuit tend to be emotional. These emotions will cloud their judgment and trump logic.

Owners will be emotional because they will feel betrayed. For one, owners often believe their builders violated the trust the owners put in them by hiring them to build a home. Additionally, when owners build custom homes, they're building their dream homes. They've invested time and money in developing a concept that feels personal to them. After all, it is where they will live with their families and where they'll entertain their extended family, friends, and business associates. When builders get something wrong, owners may feel like the defect is an affront to them personally because of the close connection we as humans have to our homes. No matter how unrealistic their expectations may have been, owners are likely to feel defrauded if their builders do not give them exactly what they wanted.

For these reasons, experienced mediators and lawyers for builders and insurers know that giving owners an opportunity to vent, to feel heard, and to release pent-up anger and frustration is a necessary first step toward resolving this kind of litigation.

Builders will be emotional, too. Their work is a reflection of who they are. When that work is attacked, their sense of worth suffers. They'll likely feel as though they're being unfairly criticized. Most builders have never been sued. When they are, they're worried about their reputations, their ability to continue in business, and their ability to feed their families. Because builders often have close relationships with owners, they, too, will feel betrayed when owners file lawsuits because they'll feel the nature of their relationship with an owner should have led them to resolve their differences without turning to the court system.





## The lack of formalized agreements means no one thinks they're wrong

Contracting negligence is common in high-end single-family home construction. Many small builders do not have the time, interest, or sophistication to formalize their agreements with their clients. Deals get done on handshakes, specifications are hastily jotted down on random pieces of paper, and formal budgets are never agreed to. When things go awry, this lack of contractual formalities—which may have been a factor in why things went awry in the first place—allows the parties to double down on their positions.

With no formal, centralized agreement between a builder and an owner memorializing, in detail, what they both agreed to regarding dimensions, finishes, hardware, paint, etc.; there is no objective standard that either party can be held to.

Both the builder and the owner can point to the absence of any documents contradicting their stance as proof they're not wrong when insisting something was or was not done correctly. This ambiguity allows both parties to further dig their heels in and make resolving their legal dispute that much more difficult.

# The lawyers involved may not know how to litigate construction lawsuits

It might sound like marketing hyperbole, but it is not: When the lawyers who are involved in construction litigation understand how the process will play out, because they've been through it before, that process tends to go smoother than when lawyers without that knowledge and experience are involved. Most lawyers representing builders and insurance companies in construction litigation tend to have experience litigating such cases. But frequently, the lawyers representing owners do not. That can be a problem.

As we alluded to in our introduction, the lawyers representing owners in these cases are often hired because of their relationship with an owner and not because of their experience with construction litigation. Because of this, they're in a tough spot. They do not know the dynamics of construction litigation, but they're representing emotional clients who are used to getting whatever they want in life and in business. So, in an effort to be the zealous advocate their clients want them to be, owners' lawyers will likely make a number of irrational demands that prolong the resolution process and show their lack of knowledge about how construction litigation tends to play out.

This lack of knowledge can be helped by experienced lawyers for the builder and the insurer in a lawsuit educating the owner's lawyer in a collegial way that benefits all parties. By dropping the inflammatory rhetoric and explaining to an owner's lawyer that a breach of warranty claim may not be available in their particular situation, or that no homeowners in their state get 100 cents on the dollar in connection with a claim like the one their client lodged, experienced counsel can help an owner's lawyer get the owner in line so that settlement discussions can be more rational and productive.

Sometimes, lawyers for a builder or an insurer may not be in a position to educate an owner's lawyer. In that case, a mediator with construction law experience could play that role—and more. In addition to educating a lawyer or two, a strong, assertive, and experienced mediator can bring the owner into line and credibly make clear that if they want to resolve the dispute, they'll need to come to the table ready to give in on some of their demands.



# The insurance situation can present challenges

Insurance will be a driving factor in the settlement of high-end construction litigation. Restrictions or limitations with builders' insurance coverage, combined with the challenges of maintaining appropriate documentation of risk transfer avenues, can lead to roadblocks on the path to resolution.

Small builders building high-end homes may potentially have restrictive insurance coverage. Securing expansive coverage can be cost prohibitive. Additionally, the insurance marketplace can be challenging for small builders to navigate without a risk manager or lawyer on staff. More restrictive coverage can present challenges in the resolution of construction litigation due to limitations or exclusions present in a small builder's insurance policy, which was likely bargained for at a cheaper rate.

Further complicating the situation, small builders can lack sophistication in understanding what coverage is available to them under their insurance policies or what they must do to comply with their policies' requirements. For example, even though small builders likely have contractor's warranty endorsements in their policies requiring their subcontractors to provide them with indemnity and other protections, many small builders may not understand what those endorsements require of

them or may simply choose not to comply with them. The penalties for noncompliance can range from applications of additional deductibles all the way to coverage limitations or denials. This can further impact the availability of insurance proceeds to resolve a claim. Adding to an already complex situation can be the presence of policy restrictions or exclusions that larger builders may have the purchasing power to negotiate away.

Insurance funds may further be limited by builders failing to contract with their subcontractors with appropriate indemnification and additional insured requirements. This would provide the kind of risk transfer, commonplace in large construction jobs between sophisticated general contractors and their subcontractors, that expands the pool of available insurance funds. However, some builders do not want their subcontractors to be sued or pulled into litigation because they want to protect those business relationships. In these situations, when builders are willing to bite the financial bullet for the sake of preserving a relationship, they end up both further reducing the amount of insurance money available and potentially causing a rift between them and their insurers.



On top of all this, high-end home litigation can present many challenges to insurers—both from an investigation and resolution standpoint. Naturally, claims representatives want to make sure they're making reasonable payments for legitimate claims that are covered under an insurance policy. The assigned claims representatives will want to see reports from the owner and the builder, reports from their experts, a comprehensive case analysis, site inspection/visit reports, destructive testing reports, and any other materials that support a claim.

Construction litigation is always a drawn-out process, but high-end home construction litigation can seem even more so when coupled with the hurdles outlined in this article. The fact that this kind of litigation can take years to resolve, which can boost the parties' expectations and tenacity, does not help.

But there are proven strategies parties to high-end home construction litigation can use to surmount those hurdles and resolve their disputes.



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