

How COVID Could Worsen The US Construction Defect Crisis

By **James Prichard, Adele Ridenour and Robert Wilkinson** (June 8, 2021)

Central to the American Dream — the notion that equality of opportunity is available to any American — is owning a home, a warm, safe, well-lit place of one's own.

For generations, Americans have come of age with the impulse and belief that we should study diligently to do well in school, secure a good job, and work hard at that job, all of which will enable us to buy a house that will become the home where we raise our family, make memories and live out our days satisfied that we have done our part and earned our fair reward.

No doubt this traditional concept of American homeownership has been corrupted over the years. In the runup to the Great Recession, for example, homeownership was central to the get-rich-quick mania that seduced tens of thousands of Americans into believing real property can only appreciate — quickly — and purchasers could therefore confidently finance 100% or more of a house's appraised value.

This perception led thousands of those people to finance multiple house purchases, believing rental income and appreciation would allow them to pay down the massive debt and strike it rich. Ultimately, the economy collapsed, and a heartbreakingly large number of Americans lost their homes to foreclosure.

In the wake of the Great Recession, as lending standards tightened and Americans recognized the housing market was susceptible to volatility and sharp decline, demand for apartments soared. While this phenomenon has been documented and commented on in the financial news and by academics, most of us need only stroll through our city streets to see gleaming new apartment buildings that did not exist 10 years ago.

Then, suddenly, in 2020 everything changed again. As the COVID-19 pandemic took hold in the U.S., high-density residential environments like apartment buildings, high-rise condominiums and nursing home facilities were associated with a greater risk of infection.

The shared amenities that once attracted renters — gyms, business centers, social facilities — were now viewed as public health hazards, along with shared elevators, mail rooms and hallways.

Similarly, as COVID-19 surged in America's cities, some residents moved to smaller towns and suburbs, seeking the physical distance from others that public health officials advised was critical to prevent infection. Simply put, COVID-19 jolted the traditional view of American homeownership back into focus.

Presently, demand for houses is historically high.[1] From coast to coast, headlines trumpet demand for housing in the wake of COVID-19.[2] In the Pacific Northwest, for example, the average sales price in Portland, Oregon, increased by 19.1% over the last calendar year.[3] Likewise, demand is so high in Orlando, Florida, that the inventory of homes for purchase is



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the lowest ever recorded.[4]

During the pandemic, many Americans have come to see a house as a symbol of safety and security — a refuge — in a dangerous world. A house can be a castle, perhaps more literally than ever before. In a typical house the residents can control their interactions with neighbors, there is room to move and play outdoors, there is space to care for sick family members, and there may be room to comfortably work and study.

The Construction Defect Pandemic in Housing

Home is where the heart is. We know the adage, and likely agree with it. Yet, for too many Americans, and for too long, homeownership is a story of heartbreak.

While rising demand and low inventory, skyrocketing home prices, and lack of affordable housing during the pandemic have received significant media attention, there is another crisis in American housing that has persisted for decades.

A strikingly large number of newly built houses contain defects in construction that will result in significant property damage or otherwise impair how the house performs over time. Most of these defective conditions are concealed behind the attractive new home's exterior. Typical examples include leaks behind siding, under roof assemblies or through window installations.

Over time, however, water from these leaks will cause damage to other components of the house, and what may have been a hidden condition will reveal itself. These hidden defects may cause a variety of troublesome conditions affecting the owner's ability to comfortably and safely reside in the house.

The construction defect crisis has ravaged the American housing market for decades. Most large cities across the country have experienced periods of intense population growth and new home construction. With very few exceptions, these periods of growth and new home construction are closely followed by many years of intense litigation arising from deficiencies in the new home construction.[5]

The housing market was changed by COVID-19, and the resulting high prices and historic demand have added fuel to the national construction defect crisis. Homebuilders across the country have been forced to work quickly to meet spiking demand, and are scrambling to complete projects, start new projects and keep costs as low as possible.

Skilled construction labor is in short supply across the country, particularly in the smaller cities and suburbs that have become destinations for home buyers during the pandemic.

On one hand, these labor shortages create opportunity for new businesses to enter a thriving market, or for smaller businesses to grow. For example, specialty subcontractors may expand their business operations to undertake new home construction or significant remodels as existing owners choose to renovate instead of entering the overheated market for a new house.

On the other hand, consumers have more and more reasons for concern when it comes to the quality of the new home construction.

Under ordinary circumstances, historic demand and labor shortages alone would negatively impact the quality of construction as project supervision and oversight by homebuilders are

put to the test, and mistakes by subcontractors and others go uncorrected.

But these problems are amplified in the current housing market due to supply chain disruptions caused by COVID-19 closures; severe weather events such as hurricanes, tornadoes and wildfires; and impacts to global shipping infrastructure such as the recent Suez Canal blockage by the container vessel Ever Given.

These supply chain disruptions significantly impact the cost of new home construction by slowing the process and increasing the amount of administrative time invested in each project, and by driving up the cost of raw materials and manufactured goods.

According to the National Association of Home Builders, lumber prices have increased more than 300% since April 2020. Other materials and products including steel, millwork, windows, plumbing fixtures and metal hardware have experienced significant price escalation, raising homebuilder costs by around 20% on a mid-market home in most locations.[6]

In many instances, homebuilders are forced to absorb rising costs on their own, decreasing or eliminating the opportunity to profit on each project. Rising housing prices may not be enough to cover these additional costs.

Understandably, such market conditions create an incentive for homebuilders to save money at every opportunity. This may result in downgrades to materials or building methods that put the finished home's long-term performance at risk. Local permitting authorities and plan reviewers are similarly impacted by high demand for new housing and COVID-19 closures that slow the process.

Building departments throughout the country have been asked to serve the public interest by safeguarding certain aspects of new home construction through plan review, permitting and inspections, yet they have limited time, limited personnel and a huge volume of applications to review.

Taking into account homebuilders rushing to bring projects to market and manage costs, the confluence of factors affecting skilled labor, raw material and manufactured product supplies, and the pressures on plan review, permitting, inspections, project review and supervision, it's not surprising that the quality of new home construction continues to decline.

Across the country, some proactive homebuilders have, of course, implemented processes and are working to control quality and avoid construction defects. These homebuilders have embraced superior building methods through training and supervision and have committed to spend the money necessary to attract and retain skilled labor.

Similarly, these builders avoid the temptation to downgrade materials or incorporate inferior designs despite shortages and the high cost of materials. Increasingly, homebuilders are engaging outside consultants to help manage risk.

For example, many builders use building envelope consultants to assure compliance with energy codes and prevent water intrusion when assembling the walls and roofs of a house. Such consultants may help design siding, roofing, and deck systems.

During construction, these consultants may supervise test assemblies called mockups to train construction crews, and perform periodic field observation to call out any deviations

from the consultant's design. Although costly and time-consuming, these precautions help homebuilders avoid expensive and time-consuming litigation, and the negative impact it can have on business or reputation.[7]

Meanwhile, the responsible purchaser should research a homebuilder's reputation, seeking references if possible.

For an existing home, a purchaser should consider retaining a qualified home inspector and carefully reviewing the written report. A purchaser should request all records of renovation work, including permitting and contractor documents.

For newly built homes, the purchaser should be sure to ask questions about the construction process, including what quality control measures were employed during construction, and what kind of labor and material warranties are in place.

Be sure to read the purchase and sale agreement. It is a legal contract, and buried within the pages of standard provisions may be provisions that attempt to limit a purchaser's ability to pursue legal action for construction defects, including broad form releases and waivers of liability.

Finally, the COVID-19 pandemic has also impacted how construction defects in newly built homes are resolved. Legal claims are subject to time limitations. These time limitations are often controlled by statute and vary from state to state.

Many owners do not discover construction defects for years, and often their discovery occurs when legal claims may be about to expire. This has been a particularly challenging problem during the pandemic, during which people have sought refuge in their houses and have been reluctant to meet with professionals, including doctors, dentists, and attorneys, but also inspectors, contractors, engineers and others who might help identify and address construction defects.

Moreover, civil courts have experienced closures and changes to procedure that confuse both members of the legal field and the public at large. As a result, many Americans have struggled to gain access to civil justice during the pandemic.

Thankfully, some states have recognized this challenge, and have taken action to protect access to the courts. In the case of construction defects, Oregon's Legislature responded to the pandemic by passing S.B. 4212, which provides extra time to bring many claims.

There are efforts to clarify that the legislation is retroactive to March 2020, when Oregon's governor first declared a state of emergency in response to COVID-19.

Conclusion

As the COVID-19 pandemic triggered a shift in how many Americans view homeownership, it also created market conditions that may worsen the decadeslong construction defect pandemic in housing. At a time when the notion of home has become more essential to feelings of safety and security, the prevalence of construction defects and property damage presents a genuine risk to the housing market.

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[1] <https://www.forbes.com/advisor/mortgages/new-home-construction-forecast/>.

[2] Construction Spending Rises 1.4% in August as Residential Boom Outweighs Private Nonresidential Decline and Flat Public Categories, Associated General Contractors of America, October 1, 2020, <https://www.agc.org/news/2020/10/01/construction-spending-rises-14-percent-august-residential-boom-outweighs-private>.

[3] <https://www.oregonlive.com/realestate/2021/04/portlands-median-home-price-jumps-8900-in-a-month-as-rock-bottom-inventory-remains.html>.

[4] <https://www.orlandosentinel.com/business/real-estate/os-bz-orlando-real-estate-inventory-hits-record-low-20210517-me3zkvxiongz5cfn2qscfumirq-story.html>.

[5] This paper focuses on recent changes to the American housing market, and the impact of COVID-19 on the construction defect crises. A forthcoming article [REFER TO LAW 360 SERIES IF APPLICABLE] analyzes the traditional response purchasers and homebuilders have had to construction defects, and recommends practices and policies to prevent both construction defects and litigation.

[6] <https://www.cnbc.com/2021/04/30/soaring-lumber-prices-add-36000-to-the-cost-of-a-new-home.html>.

[7] Beyond the construction practices described here, homebuilders and developers throughout the United States can employ many legal strategies to reduce, manage and transfer risk on a project. For a broader discussion of these strategies, see Balancing Opportunity and Risk: How Developers and Contractors can Prepare for Exposure to Construction Defect Litigation, J. Prichard and M. Picataggio, Law 360, October 2020 <https://www.law360.com/articles/1321027/mitigating-pandemic-prompted-construction-defect-risk>.