

Perhaps Not Such A Great Victory After All: Court of Appeal Rules That
Common Interest Homeowners Association Cannot Be Considered
Third Party Beneficiary To Construction Contract Between Developer
And Subcontractor Where The Homeowners Association Did Not
Exist At The Time The Subcontractor Agreement Was Executed

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In a potential modification to an earlier published decision which permitted a homeowner to recover, among other things, significant attorney's fees from a subcontractor based upon a third party intended beneficiary theory, a California Court of Appeal has just ruled that a homeowners association for a condominium development cannot be considered to be a third party intended beneficiary to a construction contract between the developer of the common interest development and its subcontractor because the homeowners association did not exist at the time the contract was entered into.

As we reported in the July 2007 edition of *The Morrison Law Journal*, the Court of Appeal, Third Appellate District, ruled in Loduca v. Polyzos (2007) 153 Cal.App.4th 334 ("Loduca case") that an owner of a single family residence was entitled to recoup significant attorney's fees from a subcontractor based upon the homeowner's status as a third party intended beneficiary to the subcontractor's contract with the prime contractor (in the Loduca case, the contract between the general contractor and the subcontractor contained a clause whereby the prevailing party was entitled to recoup attorney's fees and the Court of Appeal ruled that the homeowner could recoup attorney's fees in his capacity as a prevailing third party intended beneficiary). However, the reach of the holding in the Loduca case has been apparently limited at least in the context of construction defect cases involving certain homeowners associations.

This apparent modification is a result of the California Court of Appeal, Second District's decision in Landale-Cameron Court, Inc. v. Petri Ahonen (2007) DJDAR 15613 ("Landale-Cameron case"). In the Landale-Cameron case, the California Court of Appeal in an opinion published on October 12, 2007 ruled that a construction contractor which had been sued on a third party beneficiary contract theory by a common interest homeowners association, and which later prevailed on a motion for summary judgment, could not be considered a "prevailing" party (and thereby entitled to attorney's fees) because the

condominium homeowners association was not an intended third party beneficiary to the subcontractor's agreement to begin with.

The facts of the Landale-Cameron case are common enough. In that case, the homeowners association of an eight unit condominium complex in Toluca Lake filed suit for construction defects. In an amended complaint, the homeowners association named Petri Ahonen doing business as Riteway Decking and Flooring ("Riteway") as a Doe defendant to causes of action for negligence and breach of a third party beneficiary contract. Riteway later filed a Motion for Summary Judgment on the basis that the homeowners association's claims were time barred. The trial court granted summary judgment to Riteway on the basis that the action was time barred but later denied Riteway's motion for attorney's fees (Riteway argued that it should be considered a prevailing party based on the breach of third party beneficiary contract cause of action).

The homeowners association appealed on the basis that there was a written tolling agreement under former Civil Code section 1375. Riteway cross-appealed on the basis that it should have been entitled to an award of attorney's fees as a prevailing party under contract.

In its decision, the Court of Appeal ruled that the homeowners association had submitted admissible evidence of a tolling agreement which complied with Civil Code section 1375 thereby satisfying the three year statute of limitations period for the negligence cause of action. However, the Court of Appeal went on to rule that, while the cause of action for breach of third party intended beneficiary contract also complied with the applicable statute of limitations period, the cause of action for breach of third party beneficiary contract had no merit because there was no evidence that the homeowners association existed at the time the Riteway contract was entered into and, therefore, there was no evidence of its being an intended third party beneficiary. The Court of Appeal acknowledged the homeowners association's argument that Riteway's principal was aware that his company's work would be performed for a condominium association but noted that (i) the Riteway principal testified that he only later learned that the building would be a condominium development, (ii) the Riteway contract did not mention the word "condominium" and (iii) the project could not have been considered to be a common interest development as a matter of law at the time the Riteway contract was executed because the Covenants, Conditions and Restrictions for the development had not yet been recorded. On those bases, the Court of Appeal concluded that there was no evidence to establish that Riteway intended to make the homeowners association an intended beneficiary to its contract and cited the decision in Gilbert Financial Corporation v. Steelform Contracting Company (1978) 82 Cal.App.3d 65.

The Court of Appeal further ruled that Riteway could not recover attorney's fees as a prevailing party based on its finding that the homeowners association was not an intended third party beneficiary to the Riteway contract.

The Landale-Cameron case provides an interesting twist to the earlier decision in the Loduca case which provides a path to attorney's fees for many property owner plaintiffs in construction defect cases. However, it should be noted that the decision in the Landale-Cameron case will likely be limited to homeowners association cases and there may be homeowners association cases which can be factually distinguished. For example, the Court in the Landale-Cameron case placed some emphasis on the fact that the Riteway subcontractor agreement did not mention the word "condominium" and noted that the subcontractor was not aware that the building would be constructed as condominiums. Also, in the Landale-Cameron case, the Covenants, Conditions and Restrictions for the common interest development had not yet been recorded. Therefore, while the Landale-Cameron case generally provides that a homeowners association may not bring suit as an intended third party beneficiary under the subcontractor agreements, and thereby potentially recoup attorney's fees, there are certainly scenarios where a third party intended beneficiary claim could be made by some homeowners associations.

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