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Construction Defect Liability in California: How Reform Could Increase Affordable Homeownership Opportunities

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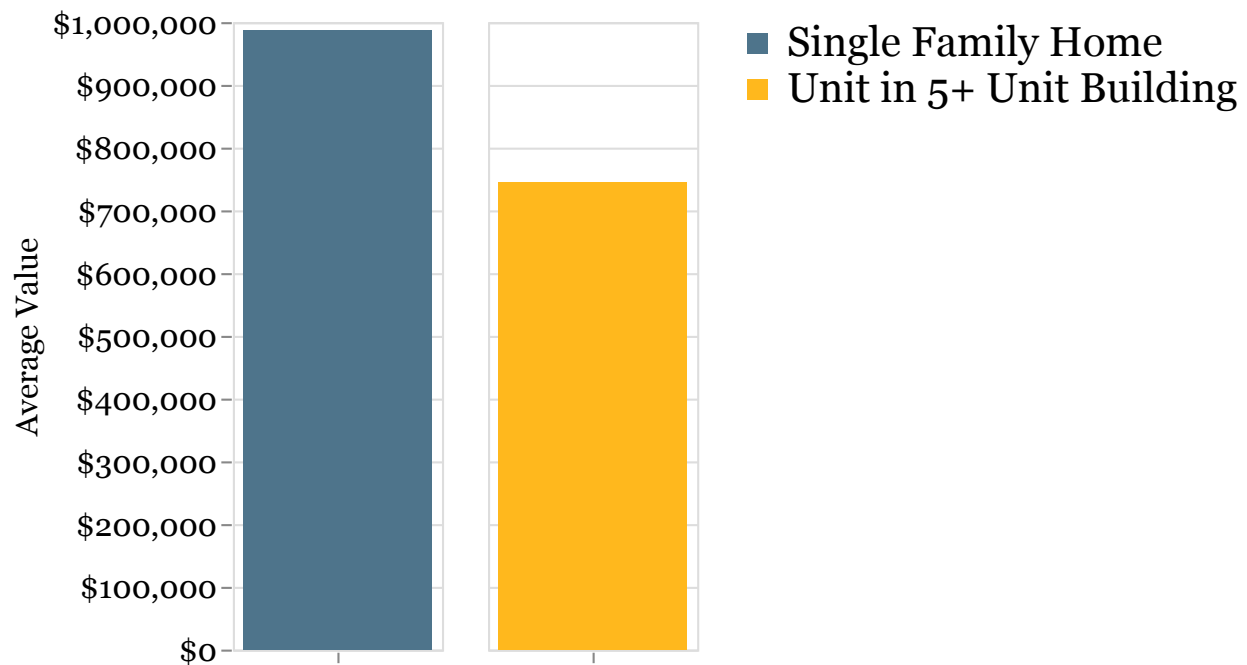
Introduction

Condominiums—homes for purchase in multifamily buildings—have long been one key entry point for homeownership. Due to their smaller square footage, they are generally less expensive than single-family homes (Figure 1).¹ Yet despite their importance to the market as a source of entry-level homes for purchase, condominium development has significantly diminished across California in the past several decades, reducing the ability of middle-income households to achieve homeownership. The homeownership rate in California has declined from around 50 percent in 2000 to around 44 percent in 2021, with younger Californians aged 35 to 45 experiencing the steepest decrease. As previous Turner Center research has shown, the share of adults who own their home in California is more than 15

percentage points lower than in the rest of the country—the widest the gap has ever been.² The undersupply of condominiums has a disproportionate impact on BIPOC (Black, Indigenous, People of Color) households, as they are more likely than their White counterparts to access homeownership by buying a condominium.³

This policy brief examines one particular challenge facing new condominium development in California: the state’s construction defect liability laws. Construction defect liability laws are intended to protect home buyers from bearing the cost of fixing defects in newly built homes. However, the scope of California’s construction defect liability laws pose a significant disincentive for developers and contractors to build new condominiums. They apply for ten years once construction is complete, versus only four years for rental housing. They

Figure 1. Average Unit Price Estimate for California, 2022



Source: Data from Turner Center analysis of 2022 one-year American Community Survey (ACS) from Integrated Public Use Microdata Series (IPUMS). We excluded group quarters from our analysis. This data also excludes mobile homes and group housing. Additional analysis of some major counties are broken down in the Appendix.

also cover non-structural problems such as bubbling paint, nail pops in drywall, and improper paint application. Homeowners Associations (HOAs) frequently initiate class-action lawsuits representing numerous plaintiffs for construction defects, which particularly affect townhomes and condominiums. The long time frame and expansive coverage has led to a legal environment in which homeowners are encouraged to seek settlements rather than allowing the developer and/or contractor to fix (or “cure”) the defect. Because all of this increases a developer’s risk, many choose to avoid building new multifamily homes for sale.

This policy brief is part of a body of work by the Turner Center and partner organizations dedicated to exploring the costs of building for-sale apartments. We explore the history of such laws in California and provide a comparative

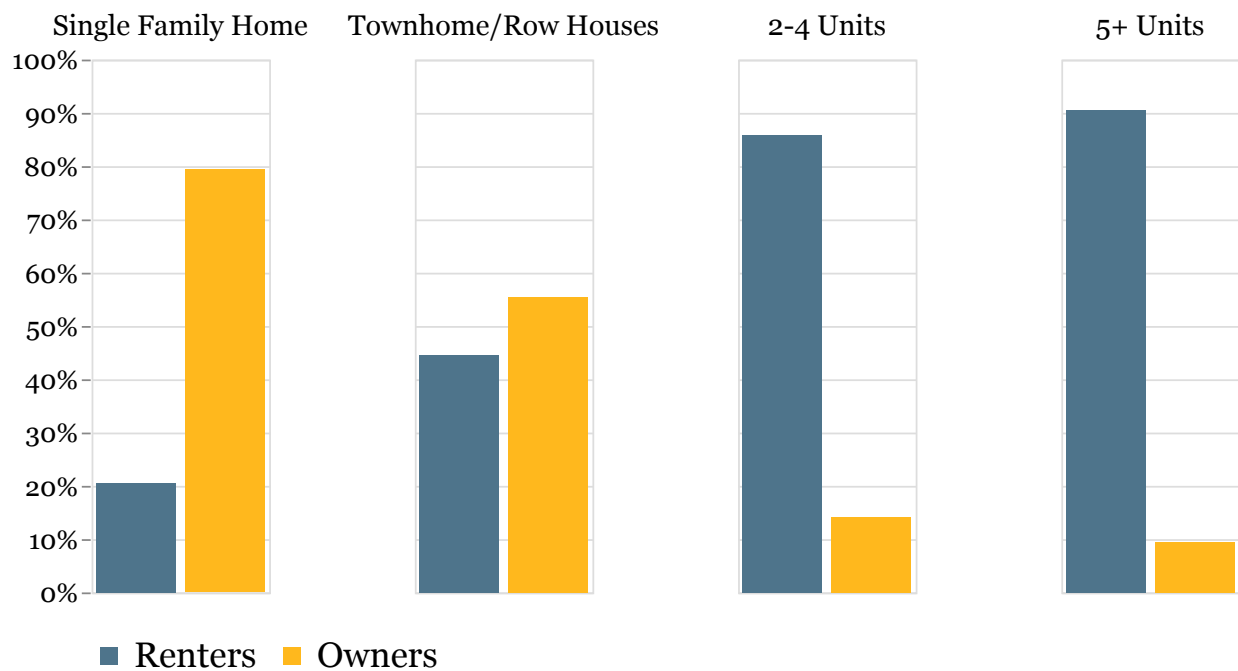
analysis of approaches to construction defect liability in other states and Canada. Our findings illuminate opportunities for legal reform and identify further avenues of research.

Background

The Decline in Condominium Construction in California

Over the last two decades, California has experienced a significant decline in homeownership. Between 2000 and 2021, the share of adults who owned their home dropped from 50 to 44 percent, with the most significant reductions occurring among Californians aged 35 to 45.⁴ These decreases are not just the result of changing preferences for homeownership—they are a direct result of the state’s high housing costs.⁵ One key driver of rising housing costs is home size. Over

Figure 2. Ownership Status by Building Size in California, 2022



Source: Data from Turner Center analysis of 2022 one-year ACS from IPUMS. We excluded group quarters from our analysis. This data also excludes mobile homes and group housing.

the past few decades, the number of new homes that are smaller than 1,400 square feet has decreased steadily. In 2020, less than ten percent of all new homes built were smaller than 1,400 square feet.⁶

Despite the fact that condominiums generally offer lower-cost entries into homeownership, the share of homes in multifamily units being offered for sale has been declining, particularly in California. An estimated 3 percent of all multifamily homes built in California between 2011 and 2021 were for sale rather than rental.⁷ In 2022, homeowners occupied less than 10 percent of units in existing structures with more than 5 units (Figure 2). As a result of these trends, the majority of households seeking to own their home buy single-family structures.

In Figure 3, we show condo construction trends in four major California submarkets: Los Angeles/Orange County, San Jose, San Diego, and San Francisco. In each market, condominium starts peaked in 2006 prior to the Great Recession and have not returned to even half the level of previous production. In Santa Clara County, more condominium units were created in 2006 and 2007 respectively than in the entire period from 2011 to 2023. Nearly 60,000 units were produced in San Diego from 2005 to 2006—more than the last 15 years in the county combined. Between 2005 and 2006, more condominiums were produced in San Diego than in the entire state in 2022.

Although financing challenges drive some of the condo production declines, developers have pointed to construction defect liability laws as a key factor in their decision to pursue rental instead of ownership multifamily development.

What is Construction Defect Liability?

California state law provides home buyers protection from bearing the cost of fixing construction defects in newly built homes. Construction defects can include problems with workmanship, design, and materials, as well as issues that arise from the architectural and engineering plans used to build the home. The period of construction defect liability is four years for rental products and ten years for for-sale products.⁸ Builders, architects, and engineers are more likely to be sued for construction defects for new homeownership units than for rental units due to this longer period of liability. The law also allows for legal action for non-structural items, such as bubbling paint, nail pops in drywall, and improper paint application.

While holding a builder responsible for addressing errors is an important consumer protection, California laws may inadvertently incentivize homeowners to take legal action against builders, architects, and engineers for problems that the builders could otherwise fix. The next section addresses the history of California's construction defect liability laws and efforts to make reforms.

Figure 3a. Annual Multifamily (5+ units) Condominium Starts in Los Angeles and Orange Counties

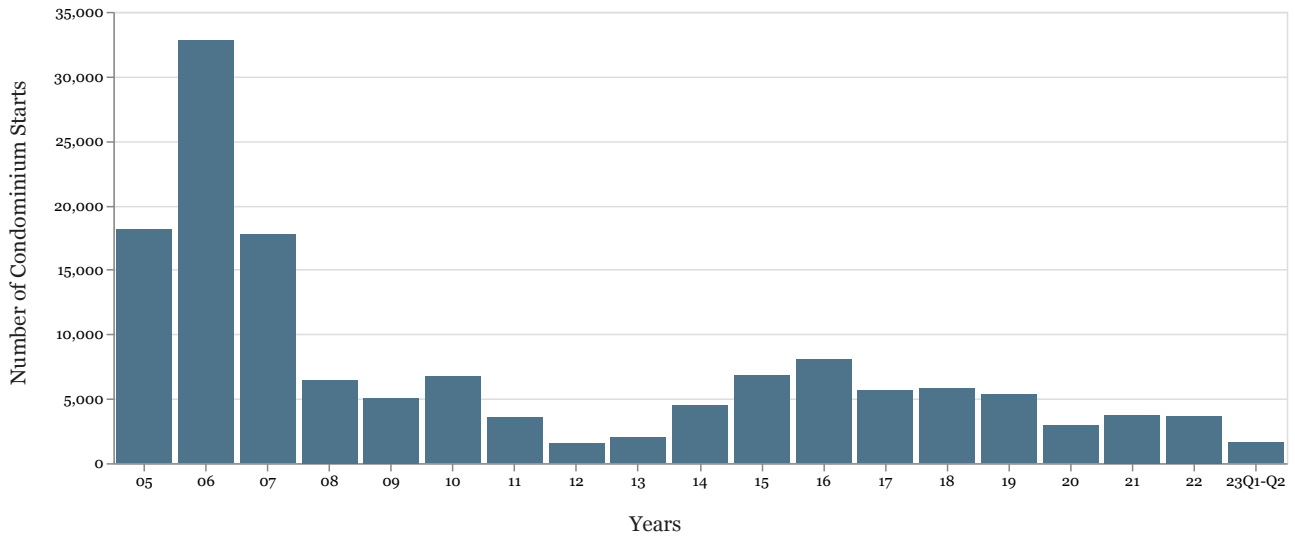
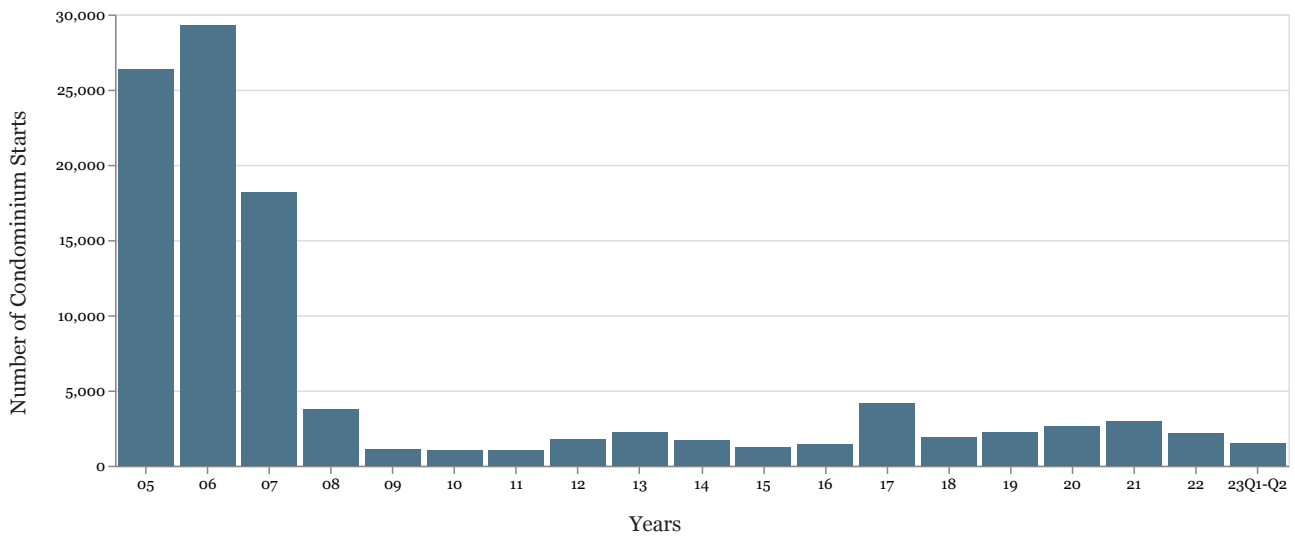


Figure 3b. Annual Multifamily (5+ units) Condominium Starts in San Diego County



Source: Analysis of Zonda data by Peak Economics Research and Consulting. Analysis of county-level data for 5+ unit condominiums starts annually.

Figure 3c. Annual Multifamily (5+ units) Condominium Starts in Bay Area⁹

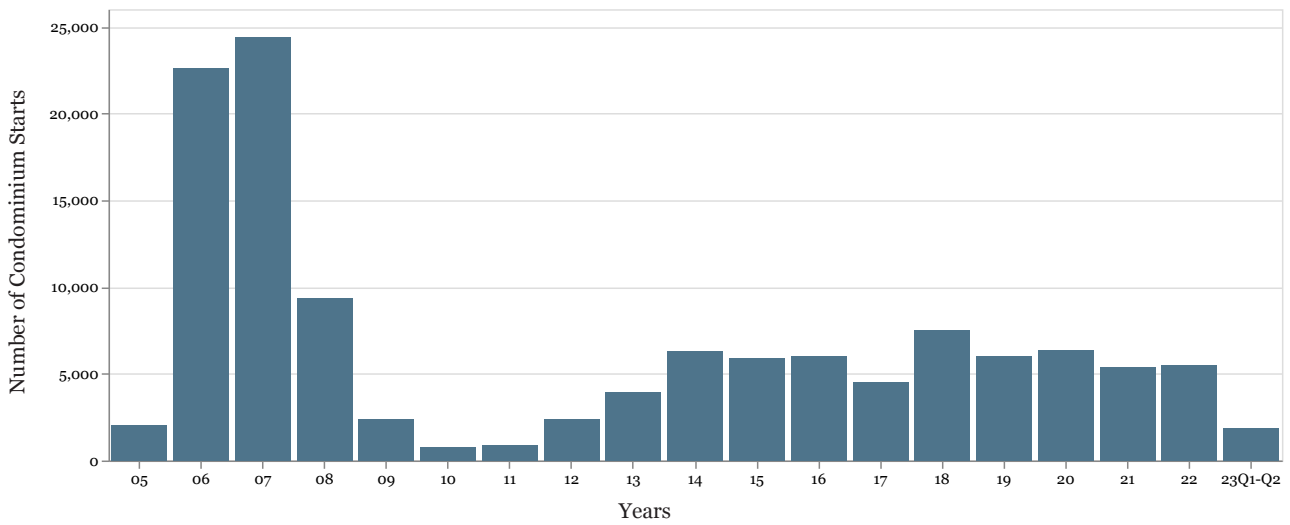
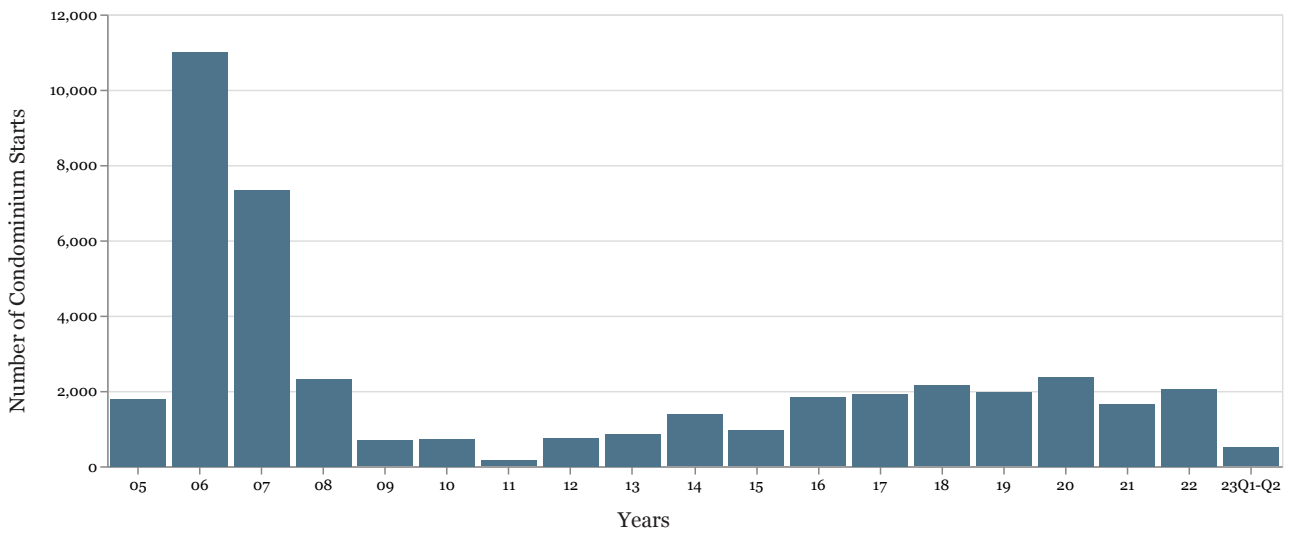


Figure 3d. Annual Multifamily (5+ units) Condominium Starts in Santa Clara County



Source: Analysis of Zonda data by Peak Economics Research and Consulting. Analysis of county-level data for 5+ unit condominiums starts annually.

How have California's construction defect liability laws changed over time and what do they say?

California's construction defect liability law dates back to the 1970s and 1980s, when a building boom brought many new developers, builders, and workers into the residential development and construction sector, many of whom designed and built relatively inexpensive multifamily for-sale homes. During this period, the influx of new developers and workers led to inconsistent construction quality, often resulting in defects that posed significant risks to homeowners.¹⁰ Addressing these issues through construction defect liability law was essential to protect consumers from major defects and financial losses.

A 1974 California Supreme Court case¹¹ found that home builders should be held responsible for construction defects under an "implied warranty"¹² attached to the sale of real property. This decision created a precedent for implied warranties which in turn gave rise to a wave of construction defect claims in the 1980s and 1990s.¹³ As a result of this increased litigation risk, developers began to turn away from the production of for-sale multifamily products.

In an effort to clarify the responsibilities of developers to future homeowners, the California State Legislature passed legislation in 1995 which established pre-litigation and dispute resolution procedures that owners needed to follow when confronting a construction defect. The law, known as the Calderon Process, asserted that an HOA in a common-interest development¹⁴ of 20 or more units must follow certain processes before the HOA can sue the developer over construction defect claims. In 2002,

the California Supreme Court found that homeowners do not have the right to sue for construction defects that had not yet caused actual damage to other property or parts of a home. This created a major gap in consumer protections for new for-sale multifamily homes.

In 2002, the California State Legislature went a step further and adopted Senate Bill 800,¹⁵ known as the "Right to Repair Act." The act established the homeowner's right to receive damages or repairs for defective construction, even if there was no actual property damage yet.¹⁶ The intention of SB 800 was to catalyze more production by reducing the legal uncertainty caused by the 2002 court case when developing multifamily condos while still standardizing the legal process to ensure consumer safety. SB 800¹⁷ mandated two things. First, it created a statute of limitations for lawsuits whereby homebuyers can have up to ten years to file claims. This ten-year limitation period includes defects that range from more cosmetic issues like nail pops to subsurface defects such as structural or drainage issues. Second, when mutually agreed upon by the plaintiff and defense, it allows builders the opportunity to first repair the issue rather than be obligated to pay a cash settlement.

Challenges with California's Existing Construction Defect Framework

Townhomes and condominiums are particularly susceptible to construction defect liability litigation, often initiated on behalf of multiple plaintiffs organized by HOAs in class-action lawsuits. This is because multifamily condominium projects are more complex to construct than single-family homes. Condos fall under the more restrictive International Building Code rather than the Interna-

tional Residential Code (which applies to 1-2 family homes and townhomes). Condominium owners are easier to organize for joint lawsuits than other types of homeowners because they live in greater proximity and are often already organized by HOAs. While SB 800 envisioned a non-litigious resolution through right to repair, in practice, the ten-year period has opened up more opportunities for defects to be identified, particularly as the line between natural wear and tear and errors of craftsmanship become blurred. Moreover, the absence of standardized definitions for defects has led to varying interpretations by construction experts, often former general contractors, architects, and subcontractors, who are hired by both owners and developers to assist in the litigation process.

Although SB 800 and Calderon were meant to reduce lawsuits, the reality falls short because plaintiffs' lawyers have little incentive or accountability to agree to early resolutions. For example, SB 800 currently prohibits homeowners from waiving their claims as consideration for repairs made under the Right to Repair process. Moreover, the practice of plaintiffs' counsel charging contingency fees (which can take up to one-third of a cash settlement) disincentivizes settlements for repairs alone.

The end result is often protracted litigation, where the high costs of discovery and trial preparation mean insurers pay substantial settlements, ultimately driving up both insurance and housing costs.¹⁸ This consequence has reduced the number

of companies that will insure for-sale buildings. When they do, they charge extremely high rates, which fewer builders, architects, and engineers can pay. These insurance costs can add substantially to the cost of producing a new unit and can compromise the financial feasibility of new ownership projects.

California's defect liability also places burdens on general contractors (GCs), and subcontractors. An indemnity clause is a legal provision in contracts, designed for risk management by obligating one party to compensate the other for certain losses or damages that might occur during their agreement. Indemnity clauses for GCs and subcontractors in construction contracts with developers transfer significant financial risks to them, making them hesitant to participate in condominium projects. Citing high legal risks and insurance costs, GCs and subcontractors place higher bids on building new condominium units or decline to bid at all, reducing the pool of available labor.

This dynamic has skewed the new for-sale ownership units towards luxury condominium towers in downtown areas, which are more likely to be able to bear the costs of higher insurance and contractor bids, or detached single-family developments, which are less likely to experience costly lawsuits.¹⁹ That leaves a gap in the homeownership market for smaller housing projects such as townhouses, cottage clusters, and three- to five-story developments. Alternative forms of homeownership, such

as co-housing products (e.g. co-ops), are stifled by the construction defect liability issue as well. Insurance providers require the same costly coverage for subcontractors and GCs, on the assumption that the liability is the same as condominiums—even if property owners forgo using a developer and build the product directly with the GC.

How Other Places Handle Construction Defect Liability

Other states have different approaches to construction defect liability that may do a better job of balancing consumer protections with encouraging condominium construction. We examine construction defect liability legal frameworks in four states: Minnesota, Utah, Hawaii, and New Jersey. We also look at Canada’s system, which is highly effective and may offer valuable insights for California.

Minnesota

In 2017, the Minnesota legislature adopted²⁰ reforms to make it easier to build for-sale, attached homes. These changes were part of a broader legislative effort to balance the interests of homeowners and builders and to encourage the construction of for-sale multifamily units. Instead of a ten-year period to address all repairs, the state adjusted timelines to give homeowners one year to identify and raise litigation for defects caused by faulty workmanship or materials, two years for defects caused by faulty installation of heating, cooling, electrical, or plumbing systems, and ten years for “major construction defects” such as foundation or roof defects. Mediation is required before a lawsuit can be filed.²¹

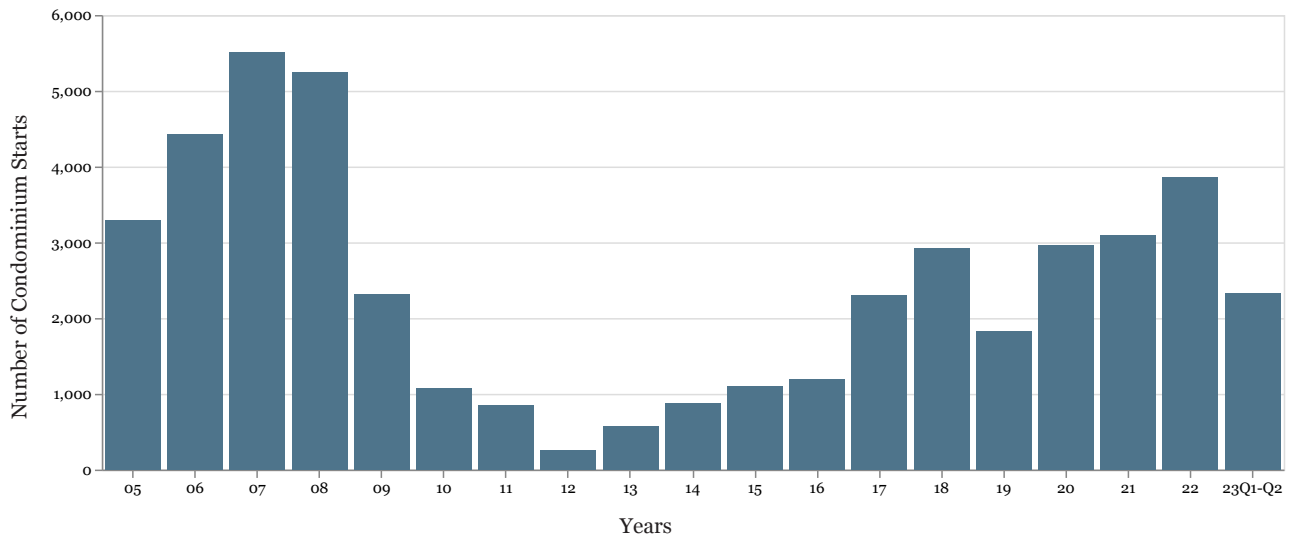
Utah

Salt Lake City is one metropolitan region that has seen their condominium starts recover somewhat following the Great Recession (Figure 4) but its overall construction defect laws have reduced consumer protections to spur development. To start, Utah’s construction defect law is more narrow than California’s, particularly when it comes to who can bring a claim. Under Utah Code,²² an “action for defective design or construction may be brought only by a person in privity of contract with the original contractor, architect, engineer, or real estate developer.” This requirement means that only those in direct contractual relationships can pursue construction defect claims. For example, if a homeowner hires a contractor to build their home and there are defects, the homeowner can sue the contractor. However, if the homeowner sells the home and the new owner discovers defects, the new owner typically cannot sue the contractor directly because they do not have a direct contract with them. There are some limited exceptions to this rule, such as claims based on fraud or certain statutory protections. In contrast, California does not have the same “privity of contract” barrier, allowing a broader range of parties to bring such claims to protect homeowners.

Additionally, Utah has a six-year statute of limitations for construction defect claims, which cannot be extended.

There is also no “right to repair” law that requires property owners to notify the construction professional of alleged defects and allow them an opportunity to repair the issue before filing a lawsuit.

Figure 4. Annual Multifamily (5+ units) Condominium Starts in Salt Lake County



Source: Analysis of Zonda data by Peak Economics Research and Consulting. Analysis of county-level data for 5+ unit condominiums starts annually.

New Jersey

New Jersey has taken a different approach to defect liability. In 1977, it created the New Home Warranty Program—a ten-year warranty protection plan²³ against construction defects for new homeowners. As in Minnesota, for the first two years the warranty covers any defects in workmanship and materials as well as systems. Up to year ten, it covers major defects that affect the home’s structural integrity, such as problems with the foundation, load-bearing walls, and other structural components. It places significant responsibilities on builders, designating them as the primary warrantors for new homes. Builders are obligated to repair any defects that fall under the warranty coverage. The process for handling claims under the New Home Warranty Program is structured to facilitate efficient resolution of construction defects. Homeowners are required to file claims directly through

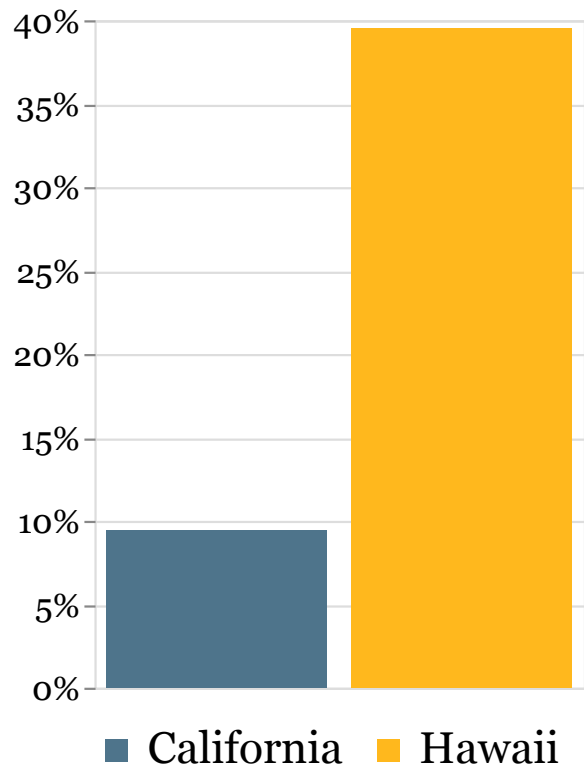
the program, adhering to specific procedures and timelines based on the nature of the defect. This system is designed to provide a clear pathway for homeowners to seek redress while giving builders the opportunity to rectify issues within a stipulated time frame. If the builder does not make the necessary repairs promptly, the state warranty program that the developer paid into during initial construction steps in to cover the costs, ensuring that the defects are addressed without undue delay or additional cost to the homeowner.

Hawaii

In 2022, 40 percent of multifamily units in Hawaii were owner-occupied (Figure 5), in part due to the limited amount of land for development.²⁴ However, Hawaii has also created a framework for defect liability that makes it easier to build ownership condos. Like California, it has a 10-year limit from the date of completion for legal actions to be initiated for construction defects. Hawaii also has specific educational and regulatory frameworks to support condominium management and dispute resolution, funded by the Condominium Education Fund (CETF). Through its support of mediation services, the CETF plays a pivotal role in the resolution of disputes, including those related to construction defects. Mediation offers a less adversarial and more cost-effective alternative to litigation.

Under Hawaii statute,²⁵ mediation is mandated if requested by a condominium owner or the HOA for disputes concerning the enforcement of the association's rules. The fund helps cover the costs, making it financially feasible for parties to engage in mediation rather than pursuing more expensive and time-consuming litigation. The first hour costs \$375 (paid for by the condominium owner or the HOA), and the CETF subsidizes the remaining cost, with a cap on the maximum amount per mediation. The CETF also supports voluntary binding arbitration between parties in condominium-related disputes.²⁶ This provides an alternative avenue for dispute resolution, offering a binding decision from an arbitrator, which can be a quicker and less adversarial process than going to court.

Figure 5. Ownership Rate for Units in Buildings with 5+ Units in California and Hawaii, 2022



Source: Data from Turner Center analysis of 2022 one-year ACS from IPUMS.²⁶ We excluded group quarters from our analysis. This data also excludes mobile homes and group housing.

Canada

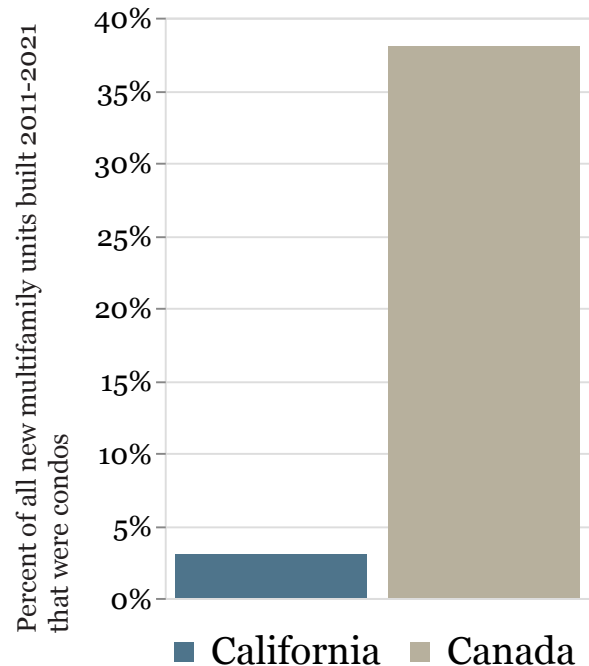
Canada has a different set of risk management strategies and safeguards in place to protect stakeholders in condominium construction, which has made the industry more robust than California's (Figure 6). Between 2011 and 2021, Canada added 1.66 million multifamily (5+) units, of which 38 percent were condominiums. In comparison, California added 987,476 multifamily units, but only 27,836 (or 3 percent) were condos.

In Canada, a comprehensive system shields consumers from construction defects at every stage. Residential builders are subject to stringent licensing requirements that demand both high professional standards and continuous skills development. The associated licensing fees also fund worker training.

In addition to robust licensing, Canada enforces warranty coverage similar to New Jersey's model. This coverage mandates that builders or warranty providers rectify certain construction defects for up to ten years, with terms varying by province. Initially voluntary, these warranty programs are gradually becoming the standard—they are mandatory in four provinces and remain optional in three.²⁸

Tarion, a nonprofit agency operating in the province of Ontario, illustrates Canada's proactive approach. Funded solely by licensing fees and home sales, Tarion manages defect resolutions and ensures homes comply with consistent warranty standards. This streamlined system emphasizes efficiency and cost-effectiveness, minimizing the need for litigation by providing affordable warranty coverage—usually costing a few thousand dollars per unit annually for ten years. Notably, this warranty comes without deductibles,

Figure 6. Condo Units as a Share of New Multifamily (5+) Production, 2011-2021



Source: Home Ownership in Transition – A Canada-California Comparison 2023 page 2. Analysis of California Building Permits 2012–2021. AHS 2011, 2019. Canada Census. May 2011, May 2021.

removing barriers for consumers needing repairs. It covers both individual units and common areas, offering broad protection for homeowners. Tarion also guarantees swift action on issues, with a process in place to start repairs within 30 days of a claim being filed, ensuring the builder's right to undertake necessary repairs.²⁹

Recommendations

Stimulating lower-cost homeownership opportunities should be a priority for California legislators, and advancing changes to the state's construction defect liability laws could support that goal.

Lessons from reforms in other states and Canada offer guidance for where California lawmakers might focus their efforts. The examples presented above underscore a variety of approaches to addressing construction defect liability, with states like Hawaii, Minnesota, and New Jersey spearheading reforms. Utah chose the path of less overall regulation, potentially at the expense of consumer protections. The Canadian model provides a path forward without government subsidies and has a similar warranty period to California's. Other states have undertaken or attempted to reform construction defect liability as well, including Colorado,³⁰ Florida,³¹ and Washington.³²

California legislators have also made attempts at reforming the state's construction defect liability law. In 2024, California Senator Steve Glazer introduced Senate Bill 1470,³³ which aimed to amend construction defect liability regulations in an effort to revitalize the condominium construction sector. The bill was meant to create an unbiased third-party inspector for the repair process—typically the person in charge of issuing the building permit—to verify the repairs are up to code. However, the bill did not move forward in the 2024 legislative session due to opposition.

Below we offer key recommendations, drawn from the examples of other states, for policy efforts to improve California's construction defect liability law and encourage condominium construction:

Implement the Right to Repair with Mandatory Mediation

Following Canada's and Hawaii's examples, integrating a right-to-repair framework that mandates mediation before litigation could reduce legal costs and promote amicable resolution between homeowners and builders. This would require a new fee for new home construction to be used to resolve construction defect issues found later. While this fee would add a cost, the establishment of greater accountability in the mediation process would provide significant benefits in de-risking the cost of insurance for sale construction for GCs and subcontractors. As in Hawaii and Canada, this process could be managed by a nonprofit or through a state agency like California's Department of Real Estate. This approach would aim to not only foster collaborative problem-solving but also would lessen the adversarial nature of defect resolutions with improved timelines for repairs.

Develop Effective Warranty Programs

Drawing from the practices in New Jersey and Canada, establishing comprehensive and mandatory warranty programs managed by nonprofits or insurance pools can offer robust consumer protection. Funded by licensing fees and home sales, these programs provide a sustainable and efficient way to handle defect repairs with little to no deductible to the homeowner, ensuring quick and fair repairs and resolutions without overburdening any party.

Establish Appropriate Attorney Incentives

Allowing homeowners to settle and release claims in exchange for builder repairs as part of the right-to-repair process would encourage acceptance of repair offers or early cash settlements rather than litigation. This could also be done through a voluntary arbitration agreement between both parties, similar to Hawaii. This reform—along with possibly requiring plaintiffs to pay defendants’ legal fees if they lose—may reduce the tendency of plaintiffs’ lawyers to rely on contingent fee agreements.

Adopt a Graduated Statute of Limitation

Inspired by Minnesota’s approach, implementing a graduated statute of limitations could significantly enhance fairness in construction liability. This model allows shorter periods for resolving cosmetic defects and extends the timeframe for major structural issues, thus acknowledging the varying severity and detectability of construction defects. Utah’s narrower six-year statute of limitations also supports a more streamlined legal process and could be a model for states seeking simplicity and efficiency.

Strengthen Licensing Requirements

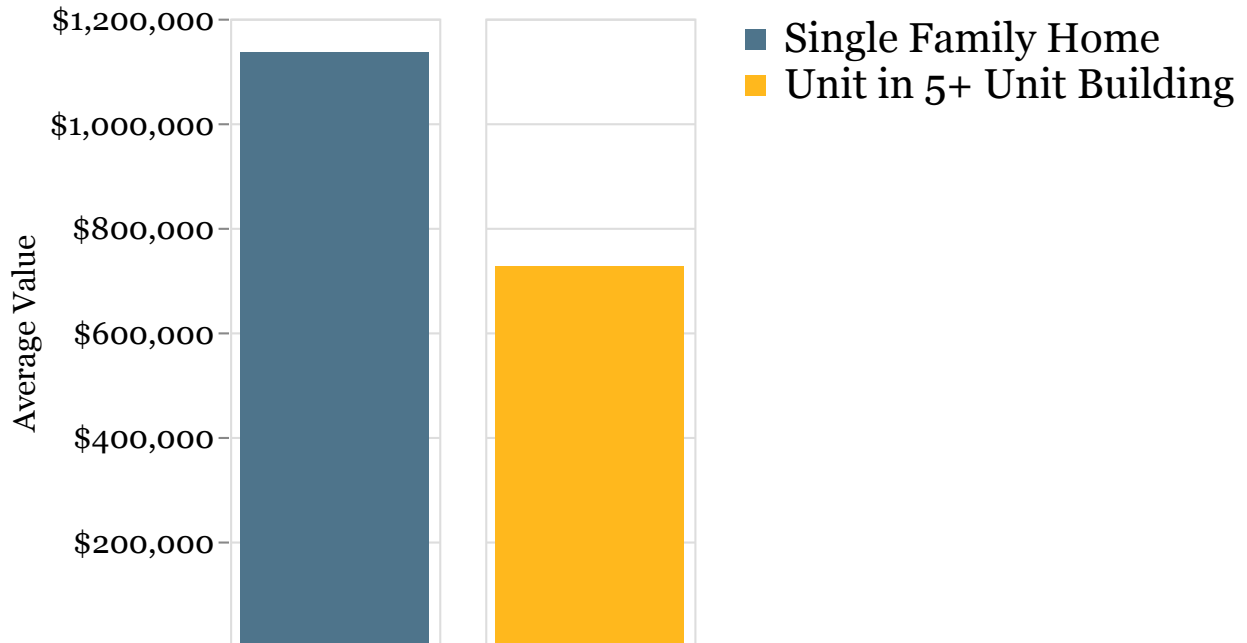
Canada’s rigorous licensing standards for contractors ensure high competency and reduce the likelihood of construction defects. Coupled with mandatory continuous professional development, such standards can raise the industry’s bar for quality and ensure that construction meets high safety and quality standards. However, there is some risk that this would further limit the labor pool and drive up construction costs.

Conclusion

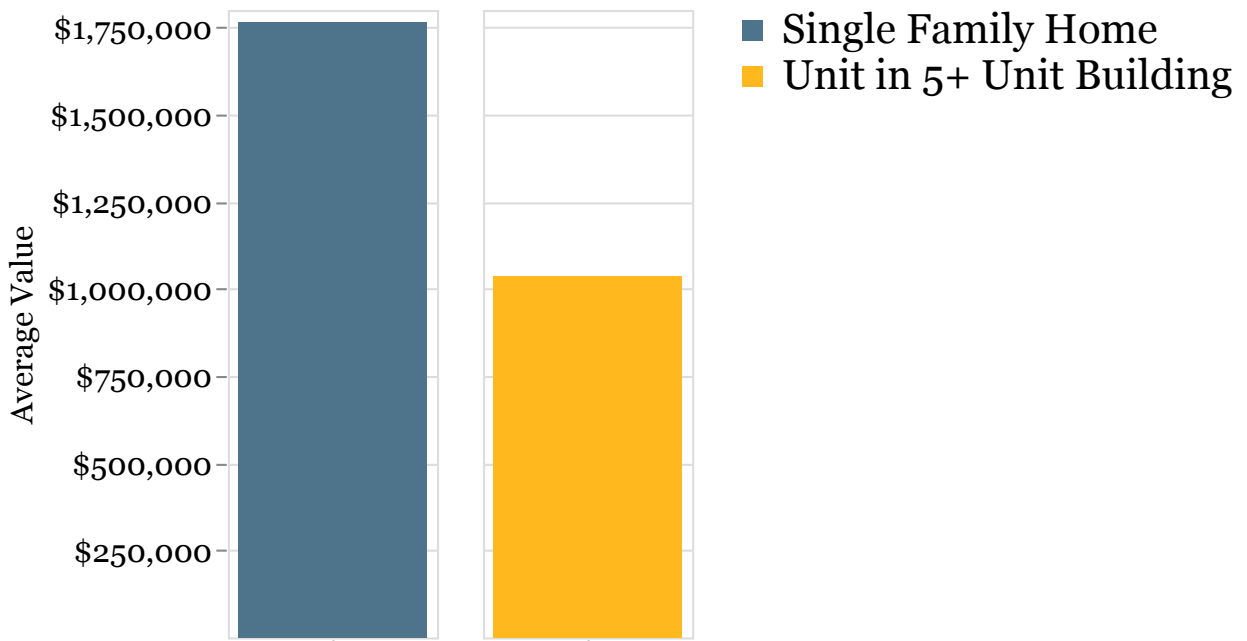
The lack of lower-cost, for-sale housing options³⁴ in California locks many out of homeownership. Multifamily units for sale could help to fill that gap, and—when coupled with infill development patterns—could satisfy the growing share of households who want to live in dense, mixed-use areas.³⁵ As the state prioritizes urban infill development to reach its climate goals, there is a compelling public interest in revisiting the construction defect laws set forth by SB 800 more than 20 years ago. Re-examining California’s current approach to handling construction defect liability with an eye to reducing litigation, lowering costs, and encouraging consumer trust is a crucial step towards creating much-needed homeownership opportunities for Californians.

Appendix: Average Unit Value of Condominiums and Single-Family Homes in Four California Counties

Average Unit Value for Los Angeles and Orange Counties, 2022

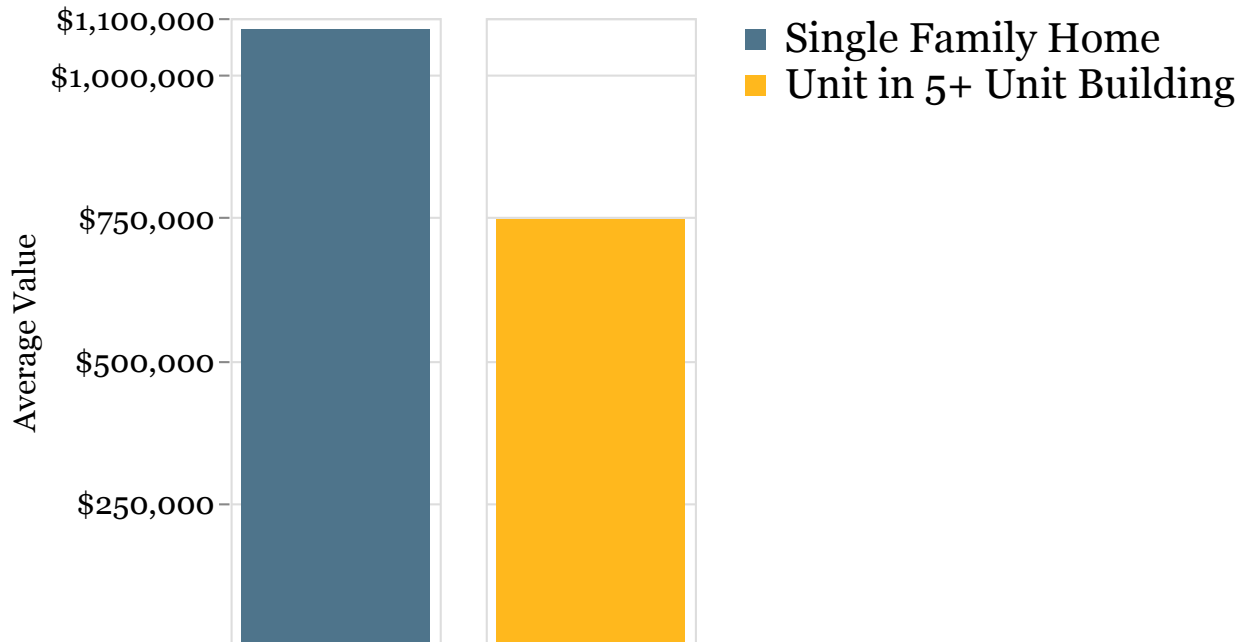


Average Unit Value for San Francisco County, 2022

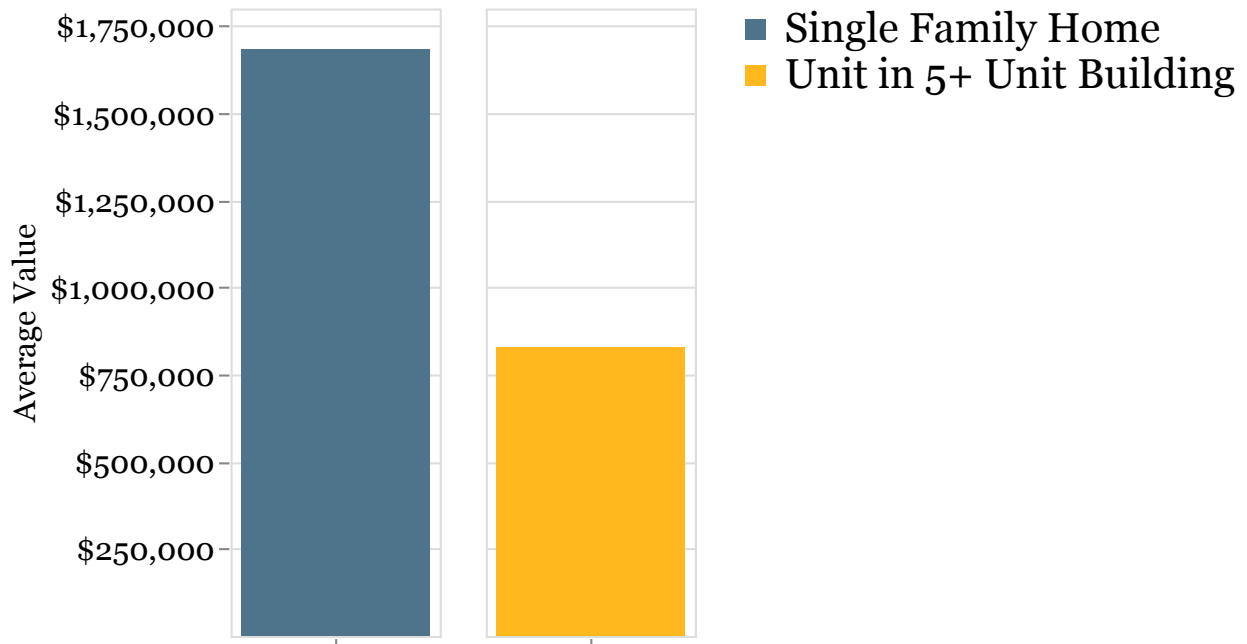


Source: Data from Turner Center analysis of 2022 one-year ACS from IPUMS.³⁶ We excluded group quarters from our analysis. This data also excludes mobile homes and group housing.

Average Unit Value for San Diego County, 2022



Average Unit Value for Santa Clara County, 2022



Source: Data from Turner Center analysis of 2022 one-year ACS from IPUMS. We excluded group quarters from our analysis. This data also excludes mobile homes and group housing.

Endnotes

1. Garcia, D., et. al. (2022). “Unlocking the Potential of Missing Middle Housing.” Turner Center for Housing Innovation, UC Berkeley. Retrieved from: <https://turnercenter.berkeley.edu/wp-content/uploads/2022/12/Missing-Middle-Brief-December-2022.pdf>.
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3. Schafran, A., et. al. (2024). “California’s Missing Middle: Middle-Income California is Large, Diverse, and Left Out of the Housing Conversation.” California Community Builders. Retrieved from: <https://www.ccbbuilders.org/moderate-middle-income-california-racial-wealth-gap>.
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7. Cameron, K., Cook, R., & Youmans, T. (2023). “Home Ownership in Transition – A Canada-California Comparison.” Global Initiatives Committee of Lambda Alpha International. Retrieved from: https://www.lai.org/sites/default/files/KeyNotes/GlobalProgramming/lai_webinar_discussion_paper_-_home_ownership_in_transition-ro.pdf.
8. Meisenhelder, Gregory E., & Windust, Paul W. (2022). “Claims for Construction Defects on Commercial and Multifamily Rental Properties.” Retrieved from: <https://members.aagla.org/news/claims-for-construction-defects-on-commercial-and-multifamily-rental-properties>.
9. This chart includes data for the 9-county Bay Area, (Alameda, Contra Costa, Marin, Napa, San Francisco, San Mateo, Solano, Sonoma) except for Santa Clara County, which is broken out in chart 3d.
10. Arditi, David & Günaydın, Hüsnü. (1997). “Total quality management in the construction process.” *International Journal of Project Management*. 15. 235-243. 10.1016/S0263-7863(96)00076-2.

11. Pollard v Saxe & Holles Dev. Co., 12 Cal. 3d 374, 525 P.2d 88, 115 Cal. Rptr. 648.
12. An implied warranty is a legal principle that automatically holds builders liable for construction defects, despite no explicit mention in a contract. This warranty applies even without the builder's explicit assurance, providing a layer of protection to buyers against latent defects that may not be immediately apparent at the time of purchase.
13. California USLAW Construction Law Compendium. USLAW Network, Inc., 2021, https://new.uslaw.org/wp-content/uploads/2022/02/California_USLAW-Construction_Compendium_2021.pdf.
14. A "Common Interest Development" (CID) refers to a type of real estate arrangement where individual owners have exclusive ownership rights to their specific units or lots, along with shared ownership and responsibility for the common areas and facilities.
15. "Right to Repair Act, AB 800, California Civil Code § 895-945.5 (2002). Retrieved from: http://www.leginfo.ca.gov/pub/01-02/bill/sen/sb_0751-0800/sb_800_bill_20020920_chaptered.html.
16. Wolff Law Office. Retrieved from: <https://www.wolfflaw.com/the-california-builders-right-to-repair-act-sb800-and-homebuyers.html>.
17. Right to Repair Act, AB 800, California Civil Code § 895-945.5 (2002).
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