CONSTRUCTION LAW

By Jason T. Shafron, Esq., Archer & Greiner, P.C. Attorneys at Law

Real estate developers in New Jersey: Navigating the minefield of personal liability

Real estate developers and construction contractors in New Jersey have long faced significant risks with respect to personal liability arising out of their companies' work. The New Jersey Supreme Court in Allen v. V & A Bros., Inc. recently confirmed that personal liability under New Jersey's Consumer Fraud Act ("CFA") for the principals and certain employees of contractors can be awarded based on regulatory violations. The risk of personal liability for such regulatory violations could now also be extended to real estate developers who previously were generally only concerned about personal liability under the New Jersey's Planned Real Estate Development Full Disclosure Act ("PREDFDA"), Real Estate Sales Full Disclosure Act ("RESFDA") and certain of New Jersey's environmental laws. Personal liability for CFA claims is of substantial and particular concern as the CFA provides for the award of triple damages and attorneys' fees to a prevailing plaintiff.

Jason T. Shafron

The Allen decision did not itself create a new cause of action under the CFA against individuals, but rather confirmed that contractors can be personally liable if they violate statutory protections for consumers, such as New Jersey's Home Improvement Practices ("HIP") regulations. While the Supreme Court in Allen specifically addressed violations under the HIP regulations, the Court may also have increased the threat of personal liability to individuals who develop a residential planned real estate development in New Jersey.

In Allen, the plaintiffs retained defendant V & A Brothers, Inc. ("V & A") to do some site work to enable plaintiffs to install a swimming pool. The work involved leveling the property and building a retaining wall. The owners of V & A were defendants Vincent and Angela DiMeglio, and they had one full time employee, defendant Thomas Taylor. After work was completed, the pool started tilting and various bulges and cracks appeared in the retaining wall. Ultimately, the Allens filed a complaint for breach of contract, and they also asserted CFA claims against V & A, and the DiMeglios and Taylor personally, alleging violations of New Jersey's HIP regulations which, as they are alleged in Allen, require written contracts, final approval before accepting final payment, and consent and knowledge of the consumer for substituting products or materials.

The trial court granted summary judgment for plaintiffs on the CFA claim based on V & A's failure to execute a written contract, but dismissed the claims against the individual defendants. The plaintiffs prevailed at trial on their breach of contract and CFA claims against V & A. Nevertheless, the plaintiffs then appealed the dismissal of their claims against the individual defendants, presumably because the substantial judgment could not be collected from V & A. The Appellate Division reversed, finding personal liability under the CFA could attach to individuals who directly participated in the regulatory violations at issue. The Supreme Court granted the individual defendants' petition for certification.

The Supreme Court examined both the CFA and the HIP regulations at issue. In reviewing the CFA's definition of a "person," the Court concluded that "there can be no doubt that the CFA broadly contemplates imposition of personal liability." Turning to the operative provisions of the CFA, the Court noted that it has long recognized that it protects consumers who have fallen prey to three separate kinds of unlawful practices: 1) affirmative acts, 2) knowing omissions, and 3) violations of regulations promulgated pursuant to statute. Specifically, by referring to "unconscionable commercial practice[s]," and by authorizing the Attorney General to promulgate regulations having the force of law, the CFA permits claims based on regulatory violations. Thus, the Supreme Court concluded that "it is clear that an individual who commits an affirmative act or knowing omission that the CFA has made actionable can be liable

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201-498-8510, email: jshafron@archerlaw.com

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CONSTRUCTION LAW

By Joshua C. Quinter, Kaplin Stewart

Think bigger when you plan your next project

As counsel to companies involved in construction at all levels, I routinely participate in the negotiation of the terms and conditions of my clients' construction contracts. I consider this a smart business practice because a small amount of time and resources invested in discussing the terms before a project begins can avoid much larger – and more expensive – conflicts after the project starts. Practically speaking, this should be the last step though. Consideration of a number of other interrelated things is often necessary before the contract negotiation even begins.

Joshua C. Quinter

Contracts are nothing more than an attempt to allocate risk on everything from nonpayment to work site injuries. Any intelligent plan or contract will properly address the risks for a particular job, so companies should start the process by identifying them. Next, figure out what entity or person is in the best position to control those risks and determine who actually controls them; and understand there is a difference. The party that controls the risk is not always the one most able to do so. Typically, the company that has the greatest ability to control a risk should bear it.

After the risks are catalogued and quantified, companies can more easily decide how to allocate them. Distribution of risk is primarily about control. A company taking responsibility for a certain part of a project must determine how to best mange that potential exposure. This dynamic is, in part, why identifying those who are in the best position to control the risk is so important. It is also why consideration of how the risk can be controlled should be part of that same discussion.

The contract language is only one part of risk management. Bonds and insurance can be purchased to address completion, payment, and casualty loss issues. Sound internal safety practices and corporate controls on procedure and finances also help. Even things as simple as the nature of the relationship with others on the work site, the personnel chosen for the project, and the equipment to be used can impact how risk is managed. These considerations are some of many that impact the contract and how you negotiate it.

Every worksite presents its own challenges and should be treated accordingly. Don't be lulled into thinking there is a "one size fits all" plan for every project. Variations of prior plans can be a good place to start, but the same structure should not necessarily be used on every occasion. When you start preparing for the next project, think bigger. It will help you plan your project better and avoid the trap of thinking that your "good contract" is all you need.

Joshua C. Quinter, Esq. is a principal in the Construction Law group of Kaplin Stewart in Blue Bell, PA. ■

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individually." Further, while a plaintiff might also pursue a veil-piercing approach to personal liability, nothing in the CFA or relevant cases suggests that, absent a veil-piercing, an individual employee or officer will be shielded from liability.

The Court appeared to have the greatest difficulty with the question of whether an employee or officer of a corporation can be found liable where the basis of the CFA claim is a regulatory violation rather than an affirmative act or a knowing misrepresentation. Such violations are particularly tricky since many regulatory violations are analyzed in terms of strict liability, thereby implicating issues of fairness where, as in Allen, regulatory violations are utilized to impose personal liability on corporate employees and officers. The Court therefore concluded that individual liability for regulatory violations ultimately must rest on the language of the particular regulation at issue and the nature of the actions undertaken by the individual defendant.

The Court reviewed in detail the three specific HIP regulations at issue: 1) requirement of a written contract, N.J.A.C. 13:45A-16.2(a)(12), 2) prohibiting submission of a final invoice in advance of issuance of a final

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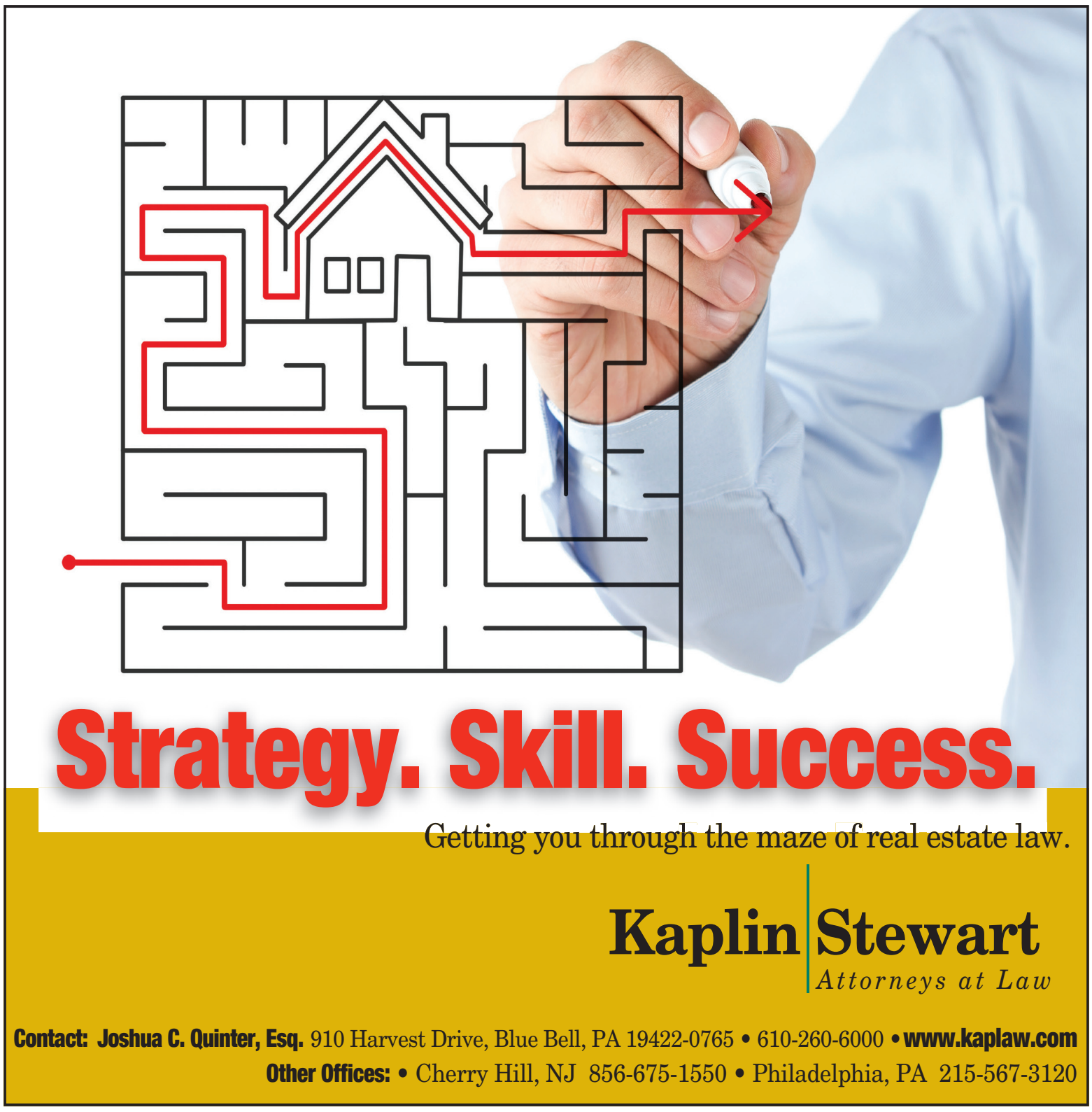

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inspection certificate, N.J.A.C. 13:45A-16.2(a)(10)(ii), and 3) substituting products or material for those in the contract or otherwise represented without consent, N.J.A.C. 13:45A-16.2(a)(3)(iv). After reviewing the regulations and the definition of "seller," the Court found a distinction between principals, who may be broadly liable, and employees, who in fairness cannot be held individually liable for an employer's policies over which they had no input or control. Thus, for example, if the principals in a corporation adopt a course of conduct in which written contracts are never used, an employee who merely complies with that policy should not be personally liable. But, where an employee substitutes an inferior product specified in the contract without the knowledge of the homeowner, the employee may be found personally liable under the CFA.

Jason T. Shafron

In addition to potential regulatory violations which may give rise to personal liability under the CFA for both contractors and developers, real estate developers may now also experience an increased risk of potential personal liability for any claim under the CFA. For example, the CFA was made specifically attributable to condominium development in Cybul v. Atrium Palaces Syndicate, 272 N.J. Super. 330 (App. Div.), certif. den., 137 N.J. 311 (1994) where the Court found that the plaintiff could recover pursuant to the CFA even though other remedies were available pursuant to PREDFDA. Likewise, in Lemendello v. Beneficial Management, 289 N.J. Super. 489 (App. Div. 1996), the court held that violations of the Consumer Loan Act could be used as evidence of conduct prohibited by the CFA and that the CFA was a remedy cumulative to those provided under the Consumer Loan Act.

Since its adoption in 1977, the PREDFDA also provides for personal liability of a partner, officer or director of a developer unless he or she did not know, and in the exercise of reasonable care, could not have known, of the existence of the facts by reason of which the liability is alleged to exist. N.J.S.A. 45:22A-37(c). Under the PREDFDA, a developer who makes a misleading statement or untrue statement of material fact, or omits a material fact from either the application for registration, any amendment thereto, or the public offering statement, with regard to the disposition of real estate, may be liable to the purchaser for double damages suffered, court costs and attorney's fees. N.J.S.A. 45:22A-37(a). Pursuant to the PREDFDA, "every general partner, officer, or director of a developer" is jointly and severally liable with the developer unless the individual "sustains the burden of proof that he did not know and in the existence of reasonable care could not have known of the existence of the facts by reason of which liability is alleged to exist." N.J.S.A. 45:22A-37(c).

This potential personal liability is limited to misrepresentations or omissions in the public offering statement or registration application and can be overcome if the purchaser knew of the untruth or omission, the purchaser did not rely on such information, or the developer did not know or, in the exercise of reasonable care, could not have known of the untruth or omission. Under the CFA, the purchaser is not required to show such reliance or deception. Likewise, the RESFDA provides a host of remedies and penalties related to deceptive advertising and sales of real estate, including fines of up to $50,000 per violation and provides for personal liability limited to the same extent as contained in the PREDFDA.

Real estate developers may now find that the limited areas of potential personal liability previously existing under the PREDFDA, the RESFDA and New Jersey's environmental laws may be greatly expanded by application of the Supreme Court's rationale in Allen for finding personal liability under the CFA for principals, officers and employees of contractors violating administrative regulations.

Jason T. Shafron, Esq. is a partner in Archer & Greiner, P.C.'s commercial litigation department. ■