
Commerce & Labor Committee

E2SSB 5773

Brief Description: Protecting homeowners who hire contractors to remodel or build their homes.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Fraser, Fairley, Kohl-Welles, Rockefeller, Kline and Pridemore).

Brief Summary of Engrossed Second Substitute Bill

- Establishes fiduciary duties and personal liability if a prime residential contractor does not show that funds paid by a homeowner to the contractor were paid by the contractor to persons who furnished labor or materials.
- Modifies various lien provisions, including giving persons who furnish labor or materials for a single-family residence a lien for the full price on the contractor's property and a lien for half of the price on the homeowner's property.
- Modifies various contractor registration provisions, including requiring additional information for contractor registration, increasing criminal penalties, and providing for increased bond amounts in certain circumstances.

Hearing Date: 3/28/05

Staff: Jill Reinmuth (786-7134).

Background:

I. LIEN LAWS

A. Definitions

Various terms are defined in lien laws, including "contract price" but not including "homeowner." "Contract price" is defined as the amount agreed upon by the parties, or if no amount is agreed upon, the customary and reasonable charge.

B. Liens

Persons who furnish labor or materials for residential construction projects have lien rights that are subject to certain requirements. For improvements to real property, these persons have a lien for the contract price on the improvements.

Such persons who do not contract directly with an owner must give the owner notice of their right to claim a lien. The notice protects the right to claim the lien for labor or materials supplied after a specific date. For most liens, the date is sixty days before the notice was mailed or delivered to the owner. However, for liens related to the new construction of a single-family residence (construction), the date is ten days before the notice was mailed or delivered to the owner.

Such persons claiming a lien must record a notice of claim of lien not later than ninety days after ceasing to furnish labor or materials or the last date on which employee benefit contributions were due. The notice of claim of lien must specify the principal amount of the lien. The person who signs the notice of claim of lien must state that they have read the notice of claim, and believe it to be true and correct.

Such persons may recover the full amount of most liens. However, for liens related to the repair, alteration, or remodel of a single-family residence or appurtenant garage (remodeling), the amount that may be recovered is limited to the amount not yet paid to the prime contractor at the time the notice is received.

Sales of real property may be forced in order to satisfy liens that are properly created and not otherwise discharged.

C. Informational Materials

Real property lenders and construction contractors are required to give informational materials on construction lien laws and available safeguards against lien claims to their customers. Lenders must give the document to persons who obtain loans to be used for construction or remodeling. Contractors must provide the document to certain customers, including those who contract for the construction or remodeling of four or fewer residential units when the price is \$1,000 or more.

The Department of Labor and Industries (Department) is required to prepare the master documents for the informational materials. The documents must include methods of protection that a consumer might use and sources of further information, including the Department and the Office of the Attorney General.

II. CONTRACTOR REGISTRATION LAWS

The Contractor Registration Act (Act) requires general and specialty contractors to register with the Department of Labor and Industries (Department). They are subject to criminal penalties for violations of the Act's registration requirements. They also must meet certain bonding requirements.

A. Definitions

Various terms are defined in contractor registration laws, including "residential homeowner." A "residential homeowner" is defined as a person who owns or leases real property upon which a single-family residence is to be built or improved, and the residence is one in which the person intends to reside upon completion of construction.

B. Registration

Applications for registration must include certain information, including the applicant's social security number and Unified Business Identifier account number, the type of contracting activity,

and the names and addresses the applicant's partners, owners, corporate officers and statutory agent, or members.

C. Criminal Penalties

It is a misdemeanor for contractors to violate certain registration provisions of the Act. These provisions prohibit persons from: (1) Advertising, offering to work, bidding, or performing work without being registered or while their registrations are suspended or revoked; (2) using false or expired registration numbers when purchasing advertising; and (3) transferring valid registrations to unregistered contractors. A misdemeanor offense is punishable by imprisonment in the county jail for a maximum term of not more than 90 days, or by a fine of not more than \$1,000, or both.

D. Bonds

Contractors are required to submit a bond to the Department. For general contractors, the bond must be for \$12,000. For specialty contractors, the bond must be for \$6,000. In specified circumstances, the director of the Department is permitted to increase the amount of the bond to up to \$36,000 for a general contractor and up to \$18,000 for a specialty contractor. These circumstances are if the contractor has had six final judgments involving a residential single-family dwelling on two or more different structures in the past five years.

Summary of Bill:

I. LIEN LAWS

A. Definitions

The definition of "contract price" is modified to specify that the "contract price" may include overhead and profit, but not amounts payable in the event of nonpayment or late payment.

A definition of "prime residential contractor" is added. A "prime residential contractor" is: (1) A prime contractor engaged in the business of constructing or remodeling a single-family residence of a homeowner; (2) the prime contractor's principals, partners, officers, directors, vice principals, and the employee with the greatest control over funds received by the prime residential contractor from homeowners; and (3) if different, the three persons who received or are entitled to receive the most compensation from the prime residential contractor during the term of the prime residential contractor's registration. "Residential subcontractor" is defined in a similar manner.

A definition of "homeowner" is also added. For most purposes of the lien laws, "homeowner" has nearly the same meaning as it does for purposes of the contractor registration laws. However, for purposes of the fiduciary duties and personal liability of the prime residential contractor and the lien rights of persons who furnish labor or materials, "homeowner" also means a person who has entered into a contract with a contractor, builder, or developer to purchase and occupy a single-family residence at when new construction, repair, alteration, or remodel of the residence or an appurtenant garage is complete.

B. Fiduciary Duties

Prime residential contractors must:

- act in the best interests of homeowners in the receipt, management, and disbursement of amounts paid by a homeowner to the prime residential contractor for labor or materials supplied by a supplier or subcontractor;
- defend homeowners against claims of liens for which the contractor was paid by the homeowner;
- maintain accounting records (but not separate accounts) to identify moneys received from homeowners and paid to suppliers and subcontractors;
- not use amounts paid by a homeowner for other purposes unless either the amounts owed to suppliers and subcontractors have been paid in full or the prime residential contractor provides written notice of its intent not to fully pay certain suppliers and subcontractors and its reasons for not doing so.

Similar provisions apply to residential subcontractors.

C. Personal Liability

Prime residential contractors are personally liable for the full amount of any liens if:

- the prime residential contractor fails to show that funds paid by the homeowner to the contractor were actually paid to suppliers or subcontractors;
- the prime residential contractor had knowledge of such use of funds (unless the prime residential contractor shows that he or she actually did not know); and
- the supplier or subcontractor records a notice of claim of lien against the prime residential contractor or the homeowner.

Similar provisions apply to residential subcontractors.

D. Liens

For improvements to an owner-occupied single-family residence, persons who furnish labor or materials have a lien for the contract price on real property owned by the prime residential contractor and a lien for no more than one-half of the contract price on the improvements to the residence.

Such persons do not have such a lien if they knew that, in the previous three years, the prime residential contractor was the prime residential contractor on a project in which a homeowner paid the prime residential contractor, the prime residential contractor failed to pay the subcontractors or suppliers, and the subcontractors or suppliers recorded liens or pursued collection actions against the homeowner. Such persons may preserve their right to lien if they provide written notice to the homeowner of the circumstances of the liens or the collection actions, and the homeowner requests the labor or materials in writing.

Such persons may give notice of late payment if they have not received payment from prime residential contractors within 30 days after the date specified in their contract, or within 60 days if no date is specified. Notice of late payment must be in writing and mailed or delivered to both the homeowner and the prime residential contractor.

The Department of Labor and Industries (Department) must notify the prime residential contractor if such a person presents to the Department evidence that a lien or other collection action has been commenced against the contractor, a notarized statement that the homeowner paid the contractor all amounts owed to suppliers and subcontractors and did not receive written notice that the prime residential contractor did not intend to pay suppliers or subcontractors, and a copy of the notice of late payment. Within five business days of the Department's notice, the prime residential contractor must provide a bond or other security in the amount of the claimed deficiency, or written documentation that the contractor informed the homeowner of the deficient payment.

For liens related to remodeling, the notice protects the right to claim the lien for labor or materials supplied ten days (rather than sixty days) before the notice was mailed or delivered to the owner. The notice of claim of lien must specify the principal amount of the lien, excluding interest, late fees, costs, attorneys' fees, and similar charges, and whether the claimant is an assignee. If the principal amount includes interest, late fees, costs, attorneys' fees or similar charges, the claimant waives any right to such charges. The person who signs the notice of claim of lien may state that they have either read the notice of claim or heard and understood it, and believe it to be true and correct. This person also must state that the lien is not frivolous and is not clearly excessive. The limitation on the amount that may be recovered (the amount not yet paid to the prime contractor at the time the notice is received) is deleted.

Sales of real property may not be forced unless the court finds that reasonable efforts were made to recover the amount not yet paid from the prime residential contractor and/or the residential subcontractor.

Subcontractors and suppliers must provide the Department with copies of judgments entered against any parties that are registered or licensed contractors or subcontractors.

E. Informational Materials

The types of master documents prepared by the Department are increased. The Department is required to prepare a master document that provides informational material about the basics of lien law relating to owner-occupied residential improvements and new construction projects. This document also must include a list of available safeguards against real property lien claims, which the homeowner must consider, reject, or select. The form of this document is specified.

A link between this master document and building permits for certain projects is established. Unless a homeowner has personally acknowledge receipt of this document, the permit issuing agency may not issue a building permit for the construction or improvement of a new owner-occupied single-family residence that involves an amount over \$1000 and the services of a prime residential contractor. The permit issuing agency must maintain a copy of the completed document in the same file as the homeowner's permit application.

II. CONTRACTOR REGISTRATION LAWS

The Contractor Registration Act (Act) is modified. Requirements relating to registration and bonding are changed. The criminal penalty for certain violations of the Act's registration requirements is increased.

A. Registration

The information required in applications for registration is modified to include whether the contractor engages or intends to engage in certain construction work on single-family residences of residential homeowners. If the applicant is a contractor engaging in such work, the information also must include the name and address of the three persons who received or are entitled to receive the most compensation from the prime residential contractor, and, if different, each principal, partner, officer, director, vice principal, and employee with the greatest executive, physical, or actual control over the accounting or disbursement of funds received by the contractor from residential homeowners. The additional names and addresses must be updated at least once every six months if the persons change. The additional names and addresses are not required if the applicant files a \$250,000 bond with the Department.

The Department must suspend a prime residential contractor's registration if, following notice of late payment, the contractor does not file a sufficient bond or other security.

B. Criminal Penalties

The criminal penalty for violating certain registration requirements under the Act is increased. It is a gross misdemeanor (rather than a misdemeanor) for such violations. A gross misdemeanor offense is punishable by imprisonment of not more than one year in jail, or by a fine of not more than \$5,000, or both.

C. Bonds

The provisions governing increased bond amounts are modified. In specified circumstances, the director of the Department of Labor and Industries is required (rather than permitted) to increase the amount of the bond to between \$24,000 and \$60,000 for a general contractor (rather than up to \$36,000) and between \$12,000 and \$30,000 (rather than up to \$18,000) for a specialty contractor.

These circumstances include if a contractor engaged in residential construction or remodeling, the contractor was a party to a lien action brought by a subcontractor or supplier, the claims against parties other than the residential homeowner were insufficient to satisfy the lien, and the subcontractor or supplier filed a lien against the residential homeowner. These circumstances are in addition to the circumstances in which the contractor has had six final judgments involving a residential single-family dwelling on two or more different structures in the past five years.

Rulemaking Authority: The Department of Labor and Industries is required to adopt rules establishing reasonable fees to cover the costs of processing certain documents.

Appropriation: None.

Fiscal Note: Available for 2SSB 5773; requested for E2SSB 5773 on March 22, 2005.

Effective Date: The bill takes effect on July 1, 2006.