

# HOUSE BILL REPORT

## ESSB 5536

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**As Reported by House Committee On:**  
Judiciary

**Title:** An act relating to condominiums.

**Brief Description:** Resolving claims relating to condominium construction.

**Sponsors:** Senate Committee on Judiciary (originally sponsored by Senators Finkbeiner, Reardon, Roach, Hale, Horn, Benton, Morton, Hewitt, Schmidt, Kastama, Sheahan, Mulliken, Johnson, Parlette, Stevens, West and Esser).

**Brief History:**

**Committee Activity:**

Judiciary: 3/27/03, 4/4/03 [DPA].

**Brief Summary of Engrossed Substitute Bill**  
**(As Amended by House Committee)**

- Allows arbitration of condominium disputes with a right of a jury trial on an appeal on the arbitrator's record, and with limited authority to supplement the record on appeal.
- Limits implied warranties to failures that have a material effect on structural integrity, unit safety, or use of a unit, or that substantially impair the sale of a unit.
- Allows disclaiming of specified defects that are known to exist at the time of the disclaiming and that have become a part of the bargaining for the sale of the condominium.
- Creates a committee to make recommendations to the Legislature on matters relating to condominium, including third-party inspections which will be required beginning July 1, 2005.

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### HOUSE COMMITTEE ON JUDICIARY

**Majority Report:** Do pass as amended. Signed by 9 members: Representatives Lantz, Chair; Moeller, Vice Chair; Carrell, Ranking Minority Member; McMahan, Assistant Ranking Minority Member; Campbell, Flannigan, Kirby, Lovick and Newhouse.

**Staff:** Bill Perry (786-7123).

**Background:**

The Washington Condominium Act (WCA) controls the creation, construction, sale, financing, management, and termination of condominiums.

A condominium consists of real property that has individually owned units and also has commonly held elements in which all the individual unit owners have an undivided common interest. A condominium may be created for any of a number of purposes, including residential use. A condominium is created by the recording of a "declaration." The person creating a condominium is referred to as the "declarant." The declarant or other seller of a condominium is required to prepare a "public offering statement" which must be delivered to a purchaser before sale. The public offering statement must contain a variety of information about the condominium, the declarant, and the management of the condominium.

The WCA also creates specific rights and responsibilities. The WCA creates implied warranties, and authorizes the use of express warranties, regarding the quality of materials and construction in a condominium. It gives certain rights to owners and their associations regarding these warranties.

**Warranties.**

Express warranties are assertions that are made by a declarant with respect to the condominium and that are relied upon by a buyer.

Implied warranties are statutorily created in the WCA. Implied warranties by the seller of a condominium include warranties of quality that:

- the units and common areas are suitable for the ordinary uses of real estate of that type;
- any construction is free from defective materials; and
- construction has been done in accordance with sound engineering and construction standards and has been done in a workmanlike manner and in compliance with applicable laws.

Implied warranties in non-residential condominiums may be waived by the written agreement of the parties or by a general disclaimer such as declaring that the sale of a unit is to be "as is" or "with all faults." Implied warranties in the sale of a residential unit, however, may not be waived by such a general disclaimer. A disclaimer of implied warranties regarding a residential unit must:

- be signed by the purchaser;
- specify the defect or noncompliance with the law that is the subject of the waived

- warranty; and
- be with respect to a defect or failure to comply that became a part of the basis of the bargain between the seller and buyer.

Under a 2001 decision, *Marina Cove Condominium Owners Association v. Isabella Estates*, the Washington State Court of Appeals (Court) held that a defect may be disclaimed even if the defect is in fact not known to exist at the time of the disclaimer so long as the disclaiming of the defect has become a part of the bargain for the sale of the condominium.

### **Arbitration.**

The *Marina Cove* decision also held that binding arbitration clauses in condominium agreements are unenforceable under the WCA. A separate statute outside the WCA does authorize the use of binding arbitration if parties to a dispute agree to it. Under this procedure, the decision of an arbitrator, if appealed, is reviewable by a court only for procedural errors. However, in *Marina Cove*, the Court ruled that this kind of binding arbitration cannot be used in condominium disputes. The Court reached this conclusion based on its reading of the WCA. The Court noted that the WCA states that the Act is "enforceable by judicial proceedings" and that provisions of the WCA may not be varied by agreement of the parties unless the WCA expressly allows such a variance. Since there is no allowance for waiving the right to a judicial determination of a dispute under the act, the Court held that arbitration clauses are unenforceable.

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### **Summary of Amended Bill:**

Several changes are made to the WCA with respect to warranties and the use of arbitration to settle disputes. A committee is also created to study various issues related to condominiums, including drafting implementing legislation for requiring third party inspections of condominiums for water penetration problems.

### **Warranties.**

The implied warranties are limited to failures in the construction of a condominium that:

- have a material adverse effect on structural integrity;
- result in a unit being materially unsafe;
- substantially impair the sale of the unit; or
- materially impair the use of the unit.

The declarant may disclaim liability for an implied warranty with respect to a specified defect if the disclaimer becomes a part of the bargain for the sale of the condominium, and if the defect was known to exist at the time of the disclaimer. Otherwise, a declarant may replace or modify an implied warranty only through the use of an express written

warranty, and only if there is no reduction in the protection of the implied warranties.

**Arbitration.**

Arbitration may be agreed to in the declaration or by other agreement of the parties for resolution of any claim under the WCA. However, arbitration is required for disputes involving alleged breaches of warranties under the Act. Procedures are provided for the selection of an arbitrator and for conducting arbitration hearings and appealing arbitration decisions regarding warranty claims.

Following arbitration, a party may appeal the decision of the arbitrator to the superior court. The appeal includes the right to demand a jury trial. The appeal is on the record of the arbitrator, and only limited kinds of new claims may be introduced on the appeal. Those claims must relate to disqualification of an arbitrator, improper exclusion of matters by the arbitrator, or matters that were outside the jurisdiction of the arbitrator. Introduction of new material facts regarding already arbitrated claims is permissible on appeal only if the facts were unknown and not reasonably knowable or discoverable.

**Condominium Construction Defect Dispute Resolution Committee.**

An 18 member committee, including four legislators, is created to make recommendations regarding various issues relating to condominiums. The committee is to deliver recommendations to the Legislature by December 31, 2003, regarding:

- legislation to implement required third-party inspections of condominiums for water penetration problems;
- shared insurance pooling or other mechanisms for providing additional insurance to declarants; and
- the use of single-entity corporations for condominium development.

**Third-Party Water Penetration Inspections.**

Beginning on July 1, 2005, all condominiums must be inspected by an independent third party with respect to water penetration prevention. If the Legislature does not enact laws regarding the performance of these inspections, they are to be done in accordance with rules adopted by the Office of Community Development.

**Application of the Act.**

The Act applies only to condominiums created by declarations recorded on or after July 1, 2003.

**Amended Bill Compared to Engrossed Substitute Bill:**

- The Senate bill required binding arbitration in cases involving more than one condo unit. The amendment allows arbitration, but also allows a jury trial on the record on appeal with limited ability to supplement the arbitration record.
- The amendment rewords the language of the Senate bill regarding limitation of

implied warranties to those defects or failures that have some material or substantial effect on the structural integrity, safety, value or use of a condo.

- The Senate bill allows an implied warranty to be replaced by an express warranty that meets certain federal standards or that is set forth in the public offering statement and declaration and acknowledged by the purchaser. The amendment allows disclaimer of a specific defect only if known to exist at the time of the disclaimer, and otherwise prohibits an express warranty from reducing the protections of the implied warranties.
- The Senate bill increases the statute of limitations to six years. The amendment leaves the statute of limitations at four years.
- The amendment adds provisions relating to the creation of a study committee, third-party inspections, and application of the act to condos created on or after the effective date of the Act.

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**Appropriation:** None.

**Fiscal Note:** Not Requested.

**Effective Date of Amended Bill:** The bill contains an emergency clause and takes effect on July 1, 2003.

**Testimony For:** The bill provides the right balance between creating a more fair insurance climate for builders and paying attention to the owners' need for adequate protections. Many builders have simply stopped building condominiums because insurance is either too expensive or not available. The bill is a reasonable way to afford some risk reduction for builders and some predictability for insurers. Condos are necessary if local governments are to meet the requirements of the Growth Management Act. Condominiums are critical for meeting the need for affordable housing. Arbitration should be allowed as an efficient way of handling condo disputes. There may have been problems with the quality of condo construction in the past, but condos today are better built than they were five years ago.

(With concerns, original bill) If the bill is not clear, it will require a great deal of time and money to litigate just to find its meaning. The bill is poorly drafted. It provides no meaningful alternative to implied warranty protection and could result in the sale of condominiums "as is." The real need is for changes that will help those builders who do quality work. The bill should address the ways the current law allows unscrupulous builders to cut corners in construction quality, dump ownership of the project, and walk away from the problems. Just adding layer upon layer to the law will not reduce litigation.

The statute of limitations should not be increased from four years. The reason for the four year period is that the condo law contains warranty protections not generally applicable in other kinds of construction.

**Testimony Against:** Poorly constructed buildings are the problem. That problem cannot be solved by taking away homeowners protections and rights. A good builder who does not cut corners, and who follows the building codes, will not end up in court. Some poorly built condos have rotted in as little as three years. The bill rewards poor construction and puts the good builder at a competitive disadvantage.

The bill does nothing to reduce risk. It just shifts the risk of poor construction to the homeowner.

Builders are complaining about insurance costs, but the owner of a poorly built condo had insurance premiums of \$18,000 before the insurer cancelled the policy completely.

A task force is needed to carefully study the problem.

**Testified:** (In support) Senator Finkbeiner, prime sponsor; George Pilant, Tacoma-Pierce County Association of Realtors; Ron Fowler, Washington Association of Realtors and Seattle-King County Association of Realtors; Tony To, Home Sight; Mark Johnson, National Federation of Independent Business; and Suzanne Dale Estey, Office of the King County Executive.

(In support, with amendments) Representative Fromhold; Bob Drewel, Snohomish County Executive; Ron Meyers, Condominium Alliance; Todd Bennett, Master Builders Association of King and Snohomish Counties; James C. Middlebrooks, David Rockwell, and Vincent DePillis, Washington State Bar Association; and Tim Harris, Building Industry Association of Washington.

(In support, with concerns) Cliff Webster, Architects and Engineers Legislative Council; and Tim Layton and Mel Sorenson, Contractors Bonding and Insurance Company.

(Concerns) Genessee Adkins, 1000 Friends of Washington.

(Opposed) Carl Wilson and David Merchant, Washington Homeowners Association; Peter Salidino, Charter Construction Incorporated; Lesley Rockney; Ryan Spiller, Washington Homeowners Coalition; Marion Morgenstern and Stan Sales, Washington State Community Associations Institute; Mark Minie, Riverfront Landing; Cheryl Lee, Kelsey Lane; Phil Culver, Bostonian Condominium Association; Norma Jean Craig, Bayview Townhomes and Washington State Community Associations Institute; Mary Beth Barbour; Dee and Edris Gluek, Rivendale Owners Association; Nancy Wall, English Cove Condominium Association; Yvonne Walden, Edward Konarzewski, and Keith Sprott, Victoria Park Condominium Association; Elaine Gregory, Plum Grove Homeowners Association; Barbara Holst; Lester Haase, Harbor Place Condominium Association; Mark Taylor and Stacey Long, Windward Cove Homeowners Association; John Siegel and Richard Levin, Levin and Stein Attorneys at Law; Valerie Rountree, Harbor Place; Celeste Siebol; and Deborah Bullock, Bayview Townhomes.

