

# SENATE BILL REPORT

## E2SSB 5773

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As Passed Senate, March 15, 2005

**Title:** An act relating to protecting homeowners who hire contractors to remodel or build their homes.

**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 History:**

**Committee Activity:** Labor, Commerce, Research & Development: 2/17/05, 3/1/05 [DPS-WM, DNP, w/oRec].

Ways & Means: 3/4/05, 3/7/05 [DP2S, w/oRec].

Passed Senate: 3/15/05, 28-20.

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### SENATE COMMITTEE ON LABOR, COMMERCE, RESEARCH & DEVELOPMENT

**Majority Report:** That Substitute Senate Bill No. 5773 be substituted therefor, and the substitute bill do pass and be referred to Committee on Ways & Means.

Signed by Senators Kohl-Welles, Chair; Franklin, Vice Chair; Brown, Keiser and Prentice.

**Minority Report:** Do not pass.

Signed by Senators Hewitt and Honeyford.

**Minority Report:** That it be referred without recommendation.

Signed by Senator Parlette, Ranking Minority Member.

**Staff:** John Dziedzic (786-7784)

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### SENATE COMMITTEE ON WAYS & MEANS

**Majority Report:** That Second Substitute Senate Bill No. 5773 be substituted therefor, and the second substitute bill do pass.

Signed by Senators Prentice, Chair; Doumit, Vice Chair; Fraser, Vice Chair; Brandland, Fairley, Kohl-Welles, Pflug, Pridemore, Rasmussen, Regala, Roach, Rockefeller and Thibaudeau.

**Minority Report:** That it be referred without recommendation.

Signed by Senators Hewitt, Parlette and Schoesler.

**Staff:** Paula Faas (786-7449)

**Background:** When equipment providers, material suppliers, subcontractors (potential lien claimants), or workers do not receive payment for the goods and services supplied to a construction project, including a homeowner's single-family residence construction or remodel project, those suppliers of goods and services can file a lien against the homeowner's property. When a potential lien claimant works through the "prime" or "general" contractor, the potential lien claimant must first notify the homeowner, in writing, that the potential lien claimant has the right to claim a lien. This notice establishes the potential lien claimant's rights with respect to goods or services that were supplied to a remodel project up to 60 days prior to the notice; or up to 10 days prior to the notice on a project for the construction of a new single-family residence.

A lien based on goods and services supplied to the repair or remodel of an owner-occupied single-family residence may only be satisfied from amounts not yet paid by the homeowner to the prime contractor at the time the notice of right to claim a lien is received by the homeowner.

To pursue a lien claim, a claimant that provided a "notice of right to claim a lien" must: (1) record the lien not later than 90 days after the claimant last provided services, materials, or equipment to the project; (2) commence an action to enforce the lien within eight months after the lien is recorded; and (3) complete the enforcement action within two years after the it was commenced.

**Summary of Bill:** Contractors owe a fiduciary duty to homeowners. A business acting as a prime contractor for a homeowner who occupies or will occupy a newly constructed or remodeled single-family residence owes a fiduciary duty to the homeowner with respect to funds paid by or on behalf of the homeowner to the contractor for suppliers, etc. A subcontractor owes a similar duty with respect to funds paid to it by the residential prime contractor.

Residential contractors are personally liable if funds paid by homeowner are misused. When a homeowner pays a contractor for goods or services supplied by potential lien claimants, those funds cannot be used for any other purpose, unless all amounts owed at that time on the potential lien claimants' contracts have been paid, or the contractor provides written notice otherwise. A subcontractor owes a similar responsibility with respect to funds paid to it by the residential prime contractor.

The contractor's fiduciary duty extends to all responsible members of the contracting business. If a contractor violates its fiduciary duty, all responsible members of the contractor business are personally liable for the resulting lien. Responsible members of the business are the contractor; any partners, principals or owners of the business; the business' chief financial officer; and the three persons who receive the greatest amount of compensation from the business, unless the members of the business show they did not know, and had no reasonable opportunity to know, that the funds were misused.

Lien claimants must pursue recovery from contractors before foreclosing against homeowners. A lien claimant that was not paid because of a fiduciary duty violation cannot foreclose on a lien against a homeowner until the lien claimant has exhausted efforts to recover the amount due from the contractor's bond, and from the assets of the personally liable members of the business. The maximum lien amount that can be foreclosed against a homeowner is one-half

of the claimant's contract price. The amount of the lien claimed cannot include interest, collection costs, etc., although a court may continue to award such amounts as part of a judgment.

Lien claimants must disclose if a contractor forced claimant to collect from a prior homeowner. A lien claimant is prohibited from filing a lien against a homeowner if the lien claimant pursued collection against another homeowner in the previous three years because the contractor retained by the current homeowner had failed to pay the lien claimant due to a fiduciary duty violation, unless the potential lien claimant informs the current homeowner about the prior violation.

Homeowners required to consider lien protection options before obtaining building permits. A building permit for the remodel or construction of owner-occupied single-family residence cannot be issued unless the homeowner provides the agency issuing the permit with a document indicating the lien protection option the homeowner selects, if any.

The Department of Labor and Industries (L&I) must track contractors that violate fiduciary duty. When registering with L&I, a contractor engaging in the new construction or remodel of single-family residences for homeowners must identify the members of the business who are potentially personally liable for the misuse of homeowner funds. If a lien involving a homeowner cannot be satisfied with the assets of these identified responsible parties, and recovery must be pursued against the homeowner, and L&I is notified, L&I must increase the bond of any contractor employing such identified person in a position of financial responsibility. In addition, if a lien claimant and homeowner notify L&I that a contractor has violated the fiduciary duty, and the contractor cannot show otherwise, L&I must suspend the contractor's registration when the contractor is finished work on any current job, unless the contractor submits security in the amount of the dispute caused by the violation.

The notice provision regarding the right to claim a lien notice for residential construction and remodel projects are made the same: ten days.

**Appropriation:** None.

**Fiscal Note:** Available for original bill; requested March 4, 2005 regarding substitute.

**Committee/Commission/Task Force Created:** No.

**Effective Date:** July 1, 2006.

**Testimony For:** If a homeowner pays a contractor in full for supplies and subcontractors, the homeowner should not have to worry about paying for them again. Contractors should be held personally responsible for misappropriating funds paid in good faith by the homeowner for supplies and subcontractors; that's better public policy than forcing homeowners to endure personal and financial horrors that occur when contractors fail to abide by rules of honest and fair dealings. A homeowner's dream home should not become a nightmare.

**Testimony Against:** Suppliers should not have to forego existing lien rights against homeowners if the pursuit of liens against contractors take longer than is currently allowed under existing lien law deadlines. Requiring trust accounts and other provisions will just increase construction costs, without providing any real benefit. What is really needed is better

consumer education to help homeowners avoid contractors who are unregistered, or who purposefully "low ball" bids.

**Who Testified:** PRO: Senator Karen Fraser, prime sponsor; Sandy Swarthout, WA Homeowners Coalition; Elizabeth Morse, Homeowner; Bob Gee, Western Building Materials Assoc.; Jeff Swan, Evergreen Lumber; Kerry Lawrence, Attorney.

CON: Brian Minnich, Building Industry Assoc. of WA; Bob Blayden, Blayden Design Build; John Bratten, JW Bratten Construction; Debbie deBoer, Janet Cole, National Assoc. of Credit Managers.