

HOUSE BILL REPORT

HB 1420

As Reported by House Committee On:
Civil Rights & Judiciary

Title: An act relating to lien priority of mortgages and deeds of trust.

Brief Description: Concerning lien priority of mortgages and deeds of trust.

Sponsors: Representatives Hackney, Corry, Walen and Ormsby.

Brief History:

Committee Activity:

Civil Rights & Judiciary: 1/31/23, 2/10/23 [DP].

Brief Summary of Bill

- Establishes the first in time, first in right rule of lien priority for mortgages and deeds of trust.

HOUSE COMMITTEE ON CIVIL RIGHTS & JUDICIARY

Majority Report: Do pass. Signed by 11 members: Representatives Hansen, Chair; Farivar, Vice Chair; Walsh, Ranking Minority Member; Graham, Assistant Ranking Minority Member; Cheney, Entenman, Goodman, Peterson, Rude, Thai and Walen.

Staff: Matt Sterling (786-7289).

Background:

The common law rule for mortgage priority is that the first party to obtain a mortgage has first priority if multiple parties seek to collect on their security during a foreclosure, also known as first in time, first in right. Under the common law rule, if a mortgage secures optional future advances, any future advances are subordinate to any intervening encumbrance made between the initial mortgage and the advance when the advance is made

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with actual knowledge of the intervening encumbrance.

Statutory law provides priority to a party who obtains a mortgage later in time to a previous mortgage if that party records the mortgage first and does not have actual or constructive notice of the previous mortgage. Except for mechanics' liens and construction financing, any mortgage or deed of trust takes priority over all liens, mortgages, deeds of trust, and other encumbrances that are not recorded prior to the recording of the mortgage or deed of trust.

The Washington Supreme Court held in *Commencement Bank v. Epic Solutions, Inc. (In re EM Property Holdings, LLC)*, 511 P.3d 1258 (2022), that the lien priority statute only applies to construction loans and liens as opposed to being generally applicable to mortgages and deeds of trust. The court found that the placement of the lien priority statute in the chapter pertaining to mechanics' liens indicates that the Legislature intended the provisions to apply only to construction loans.

Summary of Bill:

A new section is added to the chapter on foreclosure of mortgages and liens to provide that a mortgage or deed of trust has priority to all liens, mortgages, deeds of trust, and other encumbrances that have not been recorded before the recording of the mortgage or deed of trust. All sums secured by the mortgage or deed of trust are allocated in this priority, regardless of when the secured sums are disbursed or whether the disbursements are mandatory or optional.

The bill applies to all causes of action that are commenced after the effective date of the bill regardless of when the cause of action arose.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect 90 days after adjournment of the session in which the bill is passed.

Staff Summary of Public Testimony:

(In support) This bill is about principles of lien priority and the main foundational principle is first in time, first in right. This has been enacted in Washington law that a recorded mortgage or deed of trust is superior to a future encumbrance if it is secured by the mortgage or deed of trust regardless of when funds are disbursed. The interpretation that

lenders and lawyers have held for decades is that this principle applies to all loans. The Washington Supreme Court recently held that this principle should only be applied to construction loans. What this means is that for loans that make an optional disbursement of funds with the knowledge of an intervening encumbrance, those loans are now subordinate to the intervening encumbrance. So, for non-construction loans, common law would prevail which would require the parties to go to court to determine if the disbursement was mandatory or optional. The *Commencement Bank* decision introduces uncertainty for loans and increases costs, particular for lines of credit. Under the current situation, there is a risk of financing being denied for individuals who would otherwise be eligible for it. Maintaining confidence in lien priority is essential for opening lines of credit. The bill would restore the system we were operant under for decades and applies the first in time, first in right principle to all loans which would relieve a lot of confusion. The foundation of the *Commencement Bank* case was bad behavior from a market player and while this is a good bill, there is still an opportunity for that same type of bad behavior in the future so it would be a good idea to make additional changes to prevent that type of bad behavior.

(Opposed) None.

Persons Testifying: Representative David Hackney, prime sponsor; Brad Tower, Community Bankers of Washington; Mike Kot, Washington Mortgage Bankers Association; and Trent House, Washington Bankers Association.

Persons Signed In To Testify But Not Testifying: None.