

# HOUSE BILL REPORT

## HB 1534

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### As Reported by House Committee On:

Labor & Workplace Standards

Appropriations

**Title:** An act relating to strengthening protections for consumers in the construction industry.

**Brief Description:** Strengthening protections for consumers in the construction industry.

**Sponsors:** Representatives Orwall, Berry and Fosse.

### Brief History:

#### Committee Activity:

Labor & Workplace Standards: 2/7/23, 2/14/23 [DPS];

Appropriations: 2/23/23, 2/24/23 [DP2S(w/o sub LAWS)].

#### Brief Summary of Second Substitute Bill

- Raises the required bond amounts for contractor registration from \$12,000 to \$30,000 for general contractors and from \$6,000 to \$15,000 for specialty contractors.
- Requires the Department of Labor and Industries to deny an application for registration when the applicant is a successor to a business entity with an unsatisfied final judgment against it.
- Raises the fine for failure to register as a contractor from a range of \$1,000 to \$5,000 to a range of \$1,200 to \$6,000.
- Requires fines and penalties collected under the Contractor Registration Act to be deposited into the Homeowner Recovery Account.
- Establishes the Homeowner Recovery Program for eligible homeowners to receive recovery payments of up to \$25,000 from the Homeowner Recovery Account based on unsatisfied final judgments brought against registered contractors, subject to certain requirements and limitations.

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*This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not part of the legislation nor does it constitute a statement of legislative intent.*

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## HOUSE COMMITTEE ON LABOR & WORKPLACE STANDARDS

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 9 members: Representatives Berry, Chair; Fosse, Vice Chair; Robertson, Ranking Minority Member; Schmidt, Assistant Ranking Minority Member; Bronoske, Connors, Doglio, Ormsby and Ortiz-Self.

**Staff:** Kelly Leonard (786-7147).

### **Background:**

The Contractor Registration Act requires general and specialty contractors to register with the Department of Labor and Industries (Department). A general contractor works in more than one building trade or craft in a single job, project, or building permit, whereas a specialty contractor works in one trade or craft. To register as a general or specialty contractor, an applicant must submit an application, file a bond and proof of insurance, and pay a fee.

*Application information.* An application for contractor registration must include the following information: (1) employer social security number; (2) unified business identifier number; (3) evidence of workers' compensation coverage meeting specified requirements; (4) Employment Security Department number; (5) type of contracting activity; and (6) the name and address of each partner if the applicant is a firm or partnership; the name and address of the owner if the applicant is an individual proprietorship; the name and address of the corporate officers and statutory agent, if any, if the applicant is a corporation; or the name and address of all members of other business entities.

*Contractor bonds.* The required bond amount is \$12,000 for a general contractor and \$6,000 for a specialty contractor. The bond is conditioned upon the contractor paying persons performing labor for the contractor, persons furnishing material or renting or supplying equipment to the contractor, amounts adjudged against the contractor for breach of contract, and taxes due to the state. A contractor may file an assigned savings account in lieu of a bond. A person with a claim against a contractor may bring a lawsuit against the contractor and the bond in superior court. If claims exceed the amount of the bond, the claims are satisfied in the following order:

1. employee labor;
2. breach of contract;
3. subcontractors, material, and equipment;
4. taxes; and
5. any court costs, interest, and attorneys' fees.

One-half of the bond amount is protected for residential homeowners. For a claim against a specialty contractor, the protected amount is one-half the bond amount or \$4,000, whichever is greater. If a residential homeowner prevails in a claim for breach of contract,

the homeowner is entitled to costs, interest, and reasonable attorneys' fees.

*Applicants with prior judgments.* The Department is required to deny an application for registration under certain circumstances, including for example, when the applicant has an unsatisfied final judgment against him or her relating to work governed under the Contractor Registration Act or when the applicant owes the Department money for penalties resulting from a final judgment. Further, the Department may require an applicant applying to renew, reinstate, or apply for a new registration to file a bond of up to three times the normal amount if it determines that the applicant, or a previous registration of a corporate officer, owner, or partner of a current applicant, has had a final judgment involving a residential single-family dwelling on two or more different structures in the previous five years.

*Fees and penalties.* The Department is required to charge fees for issuance, renewal, and reinstatement of certificates of registration, among other transactions under the Contractor Registration Act. The Department sets the amount of the fees by rule. Revenues from those fees and other charges, excluding penalties, pertaining to contractor registration and other programs are deposited into the Construction Registration Inspection Account. Revenues from the Construction Registration Inspection Account are used for administering those related programs; however, until July 1, 2023, 7 percent of the revenues are transferred into the State General Fund.

*Certain penalties apply for violations of the Contractor Registration Act.* The Department must assess a fine of not less than \$1,000, nor more than \$5,000, for failure to register as a contractor. However, the Department may reduce the fine to \$500 for a first violation if the person registers within 10 days of receiving notice. For other violations, the Department must assess a penalty of not less than \$200, nor more than \$5,000. This includes, for example, violations involving: (1) advertising, offering to do work, submitting a bid, or performing any work as a contractor without being registered or with a suspended registration; (2) transferring valid registration to an unregistered contractor or allowing an unregistered contractor to work under a registration issued to another contractor; or (3) using an unregistered subcontractor. Revenues from penalties are deposited into the State General Fund.

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### **Summary of Substitute Bill:**

Several changes are made to the Contractor Registration Act.

*Application information.* An applicant may provide an individual taxpayer identification number, in lieu of a employer social security number, with his or her application for contractor registration.

*Contractor bonds.* For initial registrations and renewal contractor registrations occurring on

or after July 1, 2024, the required bond amount is increased to \$30,000 for general contractors and \$15,000 for specialty contractors. One-half of the bond amount is protected for residential homeowners.

*Applicants with prior judgments.* The Department is required to deny an application for registration when the applicant is a successor to a business entity with an unsatisfied final judgment against it relating to work governed by the Contractor Registration Act, or a business entity that owes the Department money for penalties assessed or fees as a result of a final judgment. A "successor" means an applicant operating with all or part of the assets of another entity previously registered as a contractor, where the applicant is under substantially common ownership, management, or control of the other entity. There is a rebuttable presumption that a successor knew or should have known of the relevant unsatisfied final judgment. If a successor demonstrates by a preponderance of the evidence that he or she did not know of the unsatisfied final judgment, by having exercised due diligence and timely verifying with the Department that the other contractor was in good standing, then the Department may grant the application for registration. The Department must adopt rules for the purposes of implementing this provision.

The Department is also required to deny an application for registration when the applicant is under 18 years old at the time of application.

*Fees and penalties.* The expiration date for the transfer of 7 percent of the revenues from the Construction Registration Inspection Account to the State General Fund is removed, thereby making that transfer ongoing.

Beginning July 1, 2024, the fine for failure to register as a contractor is increased to a range of \$1,200 to \$6,000. The Department may reduce the fee to no less than \$600 for a first violation if the person registers within 10 days of receiving notice.

The Homeowner Recovery Account is established. Revenues from all fines and penalties collected by the Department under the Contractor Registration Act must be transferred into the Homeowner Recovery Account. Expenditures from the Homeowner Recovery Account may only be used for the Homeowner Recovery Program established in the bill.

*Homeowner Recovery Program.* Subject to a specific appropriation, the Homeowner Recovery Program (Program) is created and administered by the Department. Beginning July 1, 2026, a claimant is eligible to recover from the Program after making a claim, provided that each of the following conditions is satisfied:

- the claimant has a final judgment in a court of competent jurisdiction against a registered contractor on the claimant's primary residence;
- the judgement specifies the actual damages suffered as a consequence of the claim;
- the claimant has proceeded against any existing bond covering the contractor;
- the judgment has not been satisfied in full; and
- the claim for recovery under the Program is made within 90 days after the conclusion

of any civil action.

Payments for an eligible claim are made from the Homeowner Recovery Account. Payment is limited to actual damages awarded in a final judgment after recovery against the bond. Payments for other costs related to or pursuant to civil proceedings, such as attorneys' fees, court costs, or punitive damages, are prohibited. Payments may not exceed \$25,000 per contractor per parcel, or the amount unpaid on the judgment, whichever is less.

If a claimant is issued payment, the claimant must assign his or her right, title, and interest in any final judgment to the Department to the extent of such payment. The Department may pursue reimbursement from the contractor, the insurer, or any third party for the amount paid from the Homeowner Recovery Account. The Department may establish reimbursement payment plans up to 36 months, but any payment plan longer than 12 months must assess interest. Reimbursements must be deposited into the Homeowner Recovery Account.

The priority of payment for eligible claims must be by the order of receipt by the Department. Total payments from the Homeowner Recovery Account for a fiscal year may not be greater than 80 percent of the account balance calculated at the end of the previous fiscal year. The Department must create and maintain a waitlist for any eligible claims unpaid due to insufficient funds in the Homeowner Recovery Account. The waitlist must preserve the order of receipt, and the Department may carry over a waitlist and authorize payments to eligible claims from previous fiscal years.

From 2024 through 2030, the Department must submit to the Legislature an annual report on the total applications to and payments made under the Program and the status of the Homeowner Recovery Account.

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### **Substitute Bill Compared to Original Bill:**

The substitute bill defines "successor" as an applicant operating with all or part of the assets of another entity previously registered as a contractor, where the applicant is under substantially common ownership, management, or control of the other entity, rather than a contractor who acquires through sale, lease, gift, or any process, all or part of the operating assets of another business entity, where the contractor is under substantially common ownership, management, or control of the other business entity. The substitute bill adds the rebuttable presumption provision, allowing a successor to an entity with an unsatisfied final judgment to register in some instances. The substitute bill requires the Department to adopt rules to implement the rebuttable presumption provision.

The substitute bill:

- allows an applicant to submit an application for registration with an individual taxpayer identification number, rather than requiring an employer social security

- number in all instances;
  - specifies that payments to claimants other than residential homeowners from a specialty contractor's bond or deposit may not exceed one-half of the bond or deposit, rather than specifying that those payments may not exceed one-half or \$4,000, whichever is greater;
  - restricts total payments under the Program for a fiscal year to no greater than 80 percent of the account balance calculated at the end of the previous fiscal year, rather than specifying total payments may not exceed 20 percent of the account balance at the end of the current fiscal year;
  - requires interest on payment plans exceeding 12 months to be calculated based on current applicable state law, rather than the prime rate plus 2 percent;
  - removes language providing that the Department may suspend or revoke registration based on missed payments to the Program, since the Department is required to suspend or revoke registration through other provisions under the Contractor Registration Act; and
  - adds internal cross-references to improve clarity.
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**Appropriation:** None.

**Fiscal Note:** Available. New fiscal note requested on February 14, 2023.

**Effective Date of Substitute Bill:** Section 10 of the bill contain an emergency clause and takes effect June 30, 2023. The remainder of the bill contains multiple effective dates. Please see the bill.

**Staff Summary of Public Testimony:**

(In support) The bill addresses serious issues caused by bad actors in the construction industry. There are numerous instances where homeowners have been financially devastated by bad and fraudulent contractors. In one example, a veteran couple saved over \$67,000 to remodel their home and paid the contractor, but no work was ever done. The contractor never showed up, and they lost their life savings. In another example, a homeowner paid a contractor \$100,000 with the same result, only to then have to finance an additional \$100,000 to pay another legitimate contractor to complete the project. These homeowners did their due diligence. They verified the contractor was registered. However, they discovered later that the contractors were deceptive and predatory. Bad actors often target seniors and vulnerable persons. They use deceptive advertising, refuse to give detailed estimates, request large down payments, and offer discounts for cash payments. Thousands and thousands of dollars have been stolen and never recovered. The state must act to protect the public.

The bill is a product of many years of work involving the input of businesses, homeowners, and the Department. In 2020, a work group developed recommendations, many of which

are reflected in the bill, but the project was shelved due to the COVID-19 pandemic. Before then, the work group conducted comprehensive research with the input of bonding and insurance companies, and it looked closely at models in other states. The bill is a great example of a successful stakeholder process. It is time to move forward.

The bill raises the bond amounts for the first time in over 20 years, which will pose minor costs to contractors while yielding significant protections for homeowners. Businesses and homeowners support increasing the bond amounts. It is long overdue. The bill also establishes the Homeowner Recovery Program, which will go a long way toward providing relief to homeowners. The recovery amount is capped at \$25,000, which will not make people whole, but it is still the right thing to do. Importantly, the Program will be funded by the bad actors, not legitimate contractors.

The bill should be amended to address some technical concerns, especially with respect to the definition of successorship. It is important not to penalize persons who purchase businesses while being unaware of outstanding claims. The bill should also modify the application requirements to allow someone to apply with a taxpayer identification number. Yet stakeholders are supportive of advancing the bill and perfecting it through the legislative process.

(Opposed) None.

**Persons Testifying:** Representative Tina Orwall, prime sponsor; Tina Heavener; Bobbi Cussins; James King, Independent Business Association; Tom Kwieciak, Building Industry Association of Washington; Jimmy Matta; and Nina Martinez, Latino Civic Alliance.

**Persons Signed In To Testify But Not Testifying:** None.

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## HOUSE COMMITTEE ON APPROPRIATIONS

**Majority Report:** The second substitute bill be substituted therefor and the second substitute bill do pass and do not pass the substitute bill by Committee on Labor & Workplace Standards. Signed by 30 members: Representatives Ormsby, Chair; Bergquist, Vice Chair; Gregerson, Vice Chair; Macri, Vice Chair; Stokesbary, Ranking Minority Member; Chambers, Assistant Ranking Minority Member; Corry, Assistant Ranking Minority Member; Berg, Chandler, Chopp, Connors, Couture, Davis, Dye, Fitzgibbon, Harris, Lekanoff, Pollet, Riccelli, Rude, Ryu, Sandlin, Schmick, Senn, Simmons, Slatter, Springer, Steele, Stonier and Tharinger.

**Staff:** Emily Stephens (786-7157).

**Summary of Recommendation of Committee On Appropriations Compared to Recommendation of Committee On Labor & Workplace Standards:**

The second substitute bill modifies provisions pertaining to the Homeowner Recovery Program (Program) by:

- providing that a person files an "application" under the Program, rather than makes a "claim" under the Program;
- replacing references to "claimant" with "applicant" or "person," when referring to payments under the Program, but otherwise retaining relevant references when referring to claims against contractors;
- specifying that eligibility under the Program does not create a right to payment under the Program, and that payments under the Program are discretionary;
- specifying that the bill does not create an entitlement to payment or services, and does not create a right of action; and
- removing language expressly providing that the waitlist of applicants be carried over from a previous fiscal year, but otherwise requiring the Department of Labor and Industries (Department) to create, maintain, and preserve a waitlist for any eligible applications unpaid due to insufficient funds.

The second substitute bill also extends the requirement for the Department to submit annual reports on the Program from 2030 to 2034, and requires those reports to also include information on the status of any waitlist under the Program and the solvency of the Homeowner Recovery Account. From 2035 onward, the Department is required to report to the Legislature if the Department finds there is a significant waitlist or there is insufficient funds to sustain the Program.

The second substitute bill requires 3.5 percent of revenues from the Construction Registration Inspection Account to be transferred to the General Fund on a quarterly basis, rather than requiring 7 percent of those revenues to be transferred on a quarterly basis.

A severability clause is added.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date of Second Substitute Bill:** Section 10 of the bill contains an emergency clause and takes effect June 30, 2023. The remainder of the bill contains multiple effective dates. Please see the bill.

**Staff Summary of Public Testimony:**

(In support) This is an important bill for construction consumers. The issues identified in the bill have been around for decades. This bill is designed to make bad contractors pay for harming consumers. Increasing the bond amount for contractor registration would benefit families and individuals in the complicated construction industry. Contractors who are less than honorable harm residential homeowners, and this bill provides protections to them.

(Opposed) None.

**Persons Testifying:** James King, Independent Business Association; and James Richards.

**Persons Signed In To Testify But Not Testifying:** None.