

SENATE BILL REPORT

E2SSB 5258

As Amended by House, April 20, 2023

Title: An act relating to increasing the supply and affordability of condominium units and townhouses as an option for homeownership.

Brief Description: Increasing the supply and affordability of condominium units and townhouses as an option for homeownership.

Sponsors: Senate Committee on Ways & Means (originally sponsored by Senators Shewmake, Gildon, Billig, Lias, Lovick, Nguyen, Nobles, Randall and Wellman).

Brief History:

Committee Activity: Law & Justice: 1/23/23, 2/16/23 [DPS-WM, w/oRec].

Ways & Means: 3/09/23, 3/16/23 [DP2S, w/oRec].

Floor Activity: Passed Senate: 3/31/23, 48-0.

Passed House: 4/20/23, 98-0.

Brief Summary of Engrossed Second Substitute Bill

- Adds additional requirements for construction defect actions.
- Modifies deposit requirements and local government planning related to the construction of condominiums.
- Exempts certain sales of condominium units and townhouses from the real estate excise tax.
- Creates the Down Payment Assistance Account and specifies that moneys in the account may only be used for payment toward a person's down payment assistance loan offered by the Washington State Housing Finance Commission
- Requires, subject to appropriation, all real estate excise tax revenue collected on sales of condominiums or townhouses to a person using a down payment assistance program offered by the Washington State

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.

Housing Finance Commission be deposited into the Down Payment Assistance Account.

SENATE COMMITTEE ON LAW & JUSTICE

Majority Report: That Substitute Senate Bill No. 5258 be substituted therefor, and the substitute bill do pass and be referred to Committee on Ways & Means.

Signed by Senators Dhingra, Chair; Padden, Ranking Member; McCune, Pedersen, Salomon, Torres, Valdez and Wilson, L..

Minority Report: That it be referred without recommendation.

Signed by Senators Trudeau, Vice Chair; Kuderer and Wagoner.

Staff: Ryan Giannini (786-7285)

SENATE COMMITTEE ON WAYS & MEANS

Majority Report: That Second Substitute Senate Bill No. 5258 be substituted therefor, and the second substitute bill do pass.

Signed by Senators Rolfes, Chair; Robinson, Vice Chair, Operating & Revenue; Wilson, L., Ranking Member, Operating; Gildon, Assistant Ranking Member, Operating; Schoesler, Ranking Member, Capital; Warnick, Assistant Ranking Member, Capital; Billig, Boehnke, Braun, Conway, Dhingra, Hasegawa, Hunt, Keiser, Muzzall, Nguyen, Pedersen, Saldaña, Torres, Van De Wege and Wellman.

Minority Report: That it be referred without recommendation.

Signed by Senator Wagoner.

Staff: Alia Kennedy (786-7405)

Background: Construction Defect Claims. Before a lawsuit can be filed alleging a defect in the construction or substantial remodel of a residence, the homeowner must serve notice on the construction professional alleged to be responsible for the defect. For construction defect claims brought by a board of directors of a condominium or homeowners' association, the board of directors must also substantially comply with a requirement to mail or deliver written notice of the commencement or anticipated commencement of the action to each homeowner. The claimant's notice must be given at least 45 days before a suit is filed and must describe the claim in reasonable detail.

Within 21 days of receiving the notice, the construction professional must respond to the homeowner. In the response, the construction professional must do one of the following:

- offer to inspect the alleged defect and then, based on the inspection, either remedy the

- defect, pay for it, or dispute the homeowner's claim;
- offer to settle the claim by paying for the defect, including possibly buying the residence back from the homeowner; or
- dispute the claim.

If the construction professional fails to respond, or disputes the claim, or the homeowner rejects an offer of inspection or settlement, then the homeowner may file a lawsuit.

If a homeowner does not comply with the statutory requirements prior to filing a lawsuit, the lawsuit is subject to dismissal without prejudice and may not be recommenced until the requirements have been complied with.

Warranties for Construction of Condominiums. The Washington Uniform Common Interest Ownership Act (WUCIOA) contains provisions relating to express and implied warranties that apply to the construction of condominiums. These provisions specify how express warranties are created, warranties that are implied to a purchaser, how these warranties are disclaimed, and the time limit for commencing a cause of action for breach of warranty. These warranty provisions apply specifically to condominiums.

Warranty Insurance Applicable to Condominiums. If a condominium developer purchases warranty insurance that meets certain requirements, the developer and any construction professional are no longer liable to a condominium unit owner for breach of a warranty under the Washington Condominium Act. Instead, the condominium owner's recourse for a warranty breach is to file a claim under the warranty insurance policy. If a construction professional agrees to indemnify the insurer for loss due to construction defects caused by the construction professional, the liability of the construction professional is limited to the insurance limits of the warranty.

Deposits for Purchase. Under WUCIOA, when a purchaser enters into an agreement to purchase a unit from the developer of the community, any earnest money deposit or reservation deposit must be placed in escrow. The amount of the deposit may not exceed 5 percent of the purchase price.

Deposit funds for the purchase of a unit in a common interest community may be used for the construction costs of the unit if the developer obtains and maintains a surety bond in favor of the purchaser in an amount adequate to cover the amount of the deposit to be withdrawn.

Real Estate Excise Tax. The real estate excise tax is imposed on each sale of real property, which includes both the transfer of ownership and the transfer of controlling interests. Real property includes any interest in land or anything affixed to land.

Down Payment Assistance Programs. The Washington State Housing Finance Commission (HFC) is required in statute to provide a down payment assistance program to veterans and

a housing finance program for income eligible first-time homebuyers. The HFC homeownership programs offer below-market-rate loans and down payment assistance, allows homebuyers to qualify for mortgages with higher loan ratios, and pay less closing costs than under conventional loan programs. Although not required in statute, the HFC periodically develops supplemental programs to provide additional assistance to specific targeted populations including teachers, low-income rural residents, residents of a specific area, and individuals with disabilities.

Multifamily Property Tax Exemption. The Multifamily Property Tax Exemption (MFTE) exempts the value of real property associated with the construction, conversion, or rehabilitation of qualified, multi-unit residential structures located in residential targeted areas contained within an urban center. The tax exemption applies only to the value of the construction, conversion, or rehabilitation projects, and does not exempt the value of the underlying property or other improvements on the property.

Impact Fees. Planning jurisdictions may impose impact fees on development activity as part of financing public facilities needed to serve new growth and development.

Approval of Short Plats and Short Subdivisions. City, town, and county legislative authorities may adopt regulations and procedures for the approval of short plats and short subdivisions.

Summary of Engrossed Second Substitute Bill: Construction Defect Claims. A condominium association created after the effective date of this act must include a written report from a construction defect professional in a construction defect claim. The written report must include a description of the defect, the construction defect professional's qualifications, the type of inspection that served as the basis for the report, and the general location of the defect.

Within 14 days after service of the notice of claim, a construction professional may serve a written response demanding a meeting with a claimant and the claimant's expert to confer regarding the report and its contents. The meeting shall take place within 14 days of service of the construction professional's demand or another date as agreed to by the parties.

Within 14 days of the meeting, or within 21 days after service of the claim in the absence of a demand for such a meeting, whichever is later, the construction professional shall serve a written response on the claimant.

If the claimant is an association, the association may incur expenses to prepare and serve a notice of claim and any related reports notwithstanding any contrary provisions in the association's governing documents. The association must provide a copy of the construction defect professional's report to each unit owner upon request, and also provide a summary of the construction professional's response.

A declarant, association, or party unit owner may offer to allow judgment to be entered in a construction defect dispute involving multiunit residential buildings following the filing and service of the complaint.

Deposits for Purchase. Escrow requirements are limited to earnest money deposits for the purchase of a common interest community property from a developer subject to WUCIOA. The amount of deposit funds that can be used in construction costs may not exceed 5 percent of the purchase price.

Warranty Insurance Applicable to Condominiums. Condominium developers subject to WUCIOA may purchase warranty insurance

Real Estate Excise Tax. The sale of a condominium or townhouse that is constructed in a building qualifying for the multifamily property tax exemption, is exempt from the real estate excise tax.

The Down Payment Assistance Account is created. Moneys in the account may only be used for payment toward a person's down payment assistance loan offered by the Washington State Housing Finance Commission.

Beginning in fiscal year 2025, subject to appropriation, the State Treasurer must transfer from the state general fund to the Down Payment Assistance Account all real estate excise tax revenue collected in the prior calendar year from sales of condominiums or townhouses to persons using a down payment assistance program offered by the Washington State Housing Finance Commission, as determined by the Department of Revenue (DOR). The Washington State Housing Finance Commission must provide certain data to DOR to enable DOR to determine the transfer amount each fiscal year.

The real estate excise tax exemption, Down Payment Assistance Account, and revenue transfers from the general fund to the Down Payment Assistance Account expire January 1, 2034.

Impact Fees. Impact fee schedules shall reflect the proportionate impact of new housing units, including multifamily and condominium units, based on the square footage and number of bedrooms, or trips generated, in the housing unit, to produce a proportionally lower impact fee for smaller housing units. Any changes to the impact fee schedule take effect six months after the next periodic comprehensive plan update adopted by a city or county.

Approval of Short Plats and Short Subdivisions. All cities, towns, and counties shall include in their short plat regulations procedures for unit lot subdivisions allowing division of a parent lot into separately owned unit lots.

Appropriation: None.

Fiscal Note: Available.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: The bill contains several effective dates. Please refer to the bill.

Staff Summary of Public Testimony on Original Bill (Law & Justice): *The committee recommended a different version of the bill than what was heard.* PRO: Condos are a missing piece of Washington's housing market. Insurance costs for condos are often so high that only high-end condos are built instead of condos for regular people. Missing middle housing must be part of the housing solution. Less than one percent of multifamily units being built in the state are condominiums, which leads to generations of renters and not owners. Home ownership is an anchor to help families weather storms, provides economic stability in communities, and creates generational wealth. This bill removes barriers to attainable home ownership. Condominium reform unlocks the potential for other housing efforts. There is systemic litigation for condominium construction that are not seen in other construction projects due to the complexities of statutory warranties. Clarification of the right to cure and exclusion from the statutory warranty should be adopted. This bill will incentivize condo owners to work with builder to get to a solution that works for both. This bill will protect consumers and encourage first time home buyers by waiving excise taxes, reducing impact fees, and rolling back some of the red tape to build them.

CON: There are things in this bill that are laudable because of their goals, but there are problems. This bill requires an under-oath inspection by a court-qualified inspector before a homeowner can invoke their right to seek a cure of a defect. If the owner rejects a reasonable offer from the contractor, they can recover the fair market value of the contractor's offer, but the bill does not define a reasonable offer and is not limited to situations where the owner loses in court. This bill eliminates the statutory warranty of quality construction for condominiums with 12 or fewer units or three or fewer stories which would reverse decades of progress under the condominium statutes that have avoided really costly special assessments that end up putting people out of their homes. It is much cheaper to put in a little work in the front end to ensure that a condominium does not have water intrusion problems than to impose special assessments years later.

OTHER: There are issues with Section 13 of this bill. The one size fits all approach is complicated and not cost effective. Preapproved designs may be less expensive, but materials and construction costs will likely be contrary to the purpose of using statewide preapproved plans because of different design criteria in climate zones in different areas of the state. The requirements in the bill would exceed the current State Building Code Council authority. The Council is tasked with adopting policy, but neither the Council nor the Council staff has the subject matter expertise or knowledge to prepare architectural engineering plans, conduct approvals, and regulate enforcement. There will be significant fiscal impact to the Council and would likely require that the Council contract with third parties capable of completing designs and reviewing designs.

Persons Testifying (Law & Justice): PRO: Senator Sharon Shewmake, Prime Sponsor; Councilwoman Betsy Wilkerson, City of Spokane; Alex Hur, Master Builders Association of King and Snohomish Counties; Andrew Rolwes, Downtown Spokane Partnership; Bill Clarke, WA REALTORS; Bill Riley, Riley Communities (Condo/Townhouse Builder); Josie Cummings, Building Industry Association of Washington; Mike Ennis, Association of Washington Business; Briahna Murray, Cities of Tacoma, Bellevue, Redmond, and Kent; Spencer Gardner, City of Spokane.

CON: Anthony Rafel, Washington State Chapter of Community Association Institute.

OTHER: Stoyan Bumbalov, State Building Code Council.

Persons Signed In To Testify But Not Testifying (Law & Justice): No one.

Staff Summary of Public Testimony on First Substitute (Ways & Means): *The committee recommended a different version of the bill than what was heard.* PRO: The bill is partly the outcome of reports issued by the Department of Commerce and Homeownership Disparity Taskforce. Condominiums make up less than 1 percent of new construction in the state. The biggest obstacle to homeownership, especially for people of color, is the availability of down payment assistance. The REET rebate is directly tied to the Housing Finance Commission's income based down payment assistance programs. Condominiums have traditionally provided a more affordable, entry-level option for first-time homebuyers and are an attractive option for empty nesters seeking to downsize while staying in their community. The costs and fees associated with building condominiums in Washington are too high. Construction defect lawsuits are expensive and time consuming. The bill provides important changes to construction defect actions by requiring condominium owners to provide important information from a consultant to a builder, which will make this process more efficient and prevent lawsuits.

CON: It is challenging for first-time homebuyers to get legal representation and figure out the financial details associated with a construction defect lawsuit. The bill as it relates to construction defects will devastate the economy of first-time homebuyers who will be left with homes they cannot repair. Many first-time homebuyers are unable to navigate this increasingly complicated process. This bill makes homeownership more restrictive for first-time buyers.

Persons Testifying (Ways & Means): PRO: Councilmember Sarah Rumbaugh, City of Tacoma; Bill Clarke, WA REALTORS; Bill Cornell, Preg O'Donnell & Gillett; Andrew Rolwes, Downtown Spokane Partnership; Joe McCarthy, Stoel Rives LLP.

CON: Sarah Schacht, None.

Persons Signed In To Testify But Not Testifying (Ways & Means): No one.

EFFECT OF HOUSE AMENDMENT(S):

- Removes the real estate excise tax exemption for sales of condominiums and townhouses that are constructed in buildings qualifying for the multifamily property tax exemption.
- Limits the amount the Legislature must appropriate from the General Fund to the Down Payment Assistance Account to the lesser of (1) the total amount of real estate excise tax revenues attributable to sales of condominiums and townhouses to persons using down payment assistance programs in the prior calendar year, or (2) \$250,000 per fiscal year.