

HOUSE BILL REPORT

HB 1848

As Reported by House Committee On:
Judiciary

Title: An act relating to managing construction defect disputes involving multiunit residential buildings.

Brief Description: Addressing construction defect disputes involving multiunit residential buildings.

Sponsors: Representatives Springer, Tom, Lantz, Priest, Hunter, Jarrett, Clibborn, Serben, Fromhold, Rodne, Williams, Flannigan, Kessler, O'Brien and Simpson.

Brief History:

Committee Activity:

Judiciary: 2/15/05, 3/1/05 [DP].

Brief Summary of Bill

- Requires course-of-construction inspections of the building enclosure of any multi-unit residential building, including condominium, specifically for water penetration around windows and more generally for compliance with the building's design documents;
- Allows any party in a condominium warranty dispute to demand arbitration after a lawsuit has been filed;
- Requires mediation and allows the use of neutral experts in all condominium warranty disputes, whether in a trial or arbitration;
- Allows any party in such a condominium dispute to make an offer of judgment which may result in the award of reasonable attorney fees to one party or the other depending on the ultimate outcome of the dispute in arbitration or trial; and
- Provides for a trial de novo upon appeal of an arbitration award in any condominium warranty dispute and for the allocation of fees and costs in the arbitration or trial.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: Do pass. Signed by 9 members: Representatives Lantz, Chair; Williams, Vice Chair; Priest, Ranking Minority Member; Rodne, Assistant Ranking Minority Member; Campbell, Kirby, Serben, Springer and Wood.

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." A condominium may be created at the time of the construction of a new condominium building, or a condominium may be created by the conversion of an existing building, such as an existing apartment building.

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. The WCA gives certain rights to owners and their associations regarding these warranties.

Express warranties are assertions that are made by the declarant with respect to a 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;
- free from defective materials;
- built in accordance with sound engineering and construction standards;
- built in a workmanlike manner; and
- built in compliance with applicable laws.

The WCA provides that any right or obligation under the WCA is enforceable by judicial proceeding. In a 2001 decision, Marina Cove Condominium Owners Association v. Isabella Estates, the Washington State Court of Appeals held that binding arbitration clauses in condominium agreements are unenforceable under the WCA. The Court held that the WCA does not authorize parties to agree to binding arbitration that prevents an appeal to a judicial process.

As part of condominium legislation passed in 2004, a Condominium Study Committee was created to look at two issues related to condominiums: (1) the use of independent third-party inspections during the construction of condominiums in order to reduce water penetration problems; and (2) the use of alternative dispute resolution procedures in condominium cases.

The Condominium Study Committee delivered its report to the Legislature at the beginning of the 2005 legislative session.

Summary of Bill:

Course-of-construction inspections are required for the building enclosures of all multi-unit residential buildings.

The WCA is amended to provide for alternative dispute resolution mechanisms including arbitration, mediation, and the use of neutral experts in disputes involving alleged breaches of condominium warranties.

INSPECTIONS.

The building enclosures of a multi-unit residential building for which a building permit is issued on or after July 1, 2005, must be inspected during initial construction or during rehabilitation work. The inspection must include a check for water penetration problems around the windows of the building and must also include ascertaining whether the construction is being done in accordance with building enclosure design documents. A building department may not issue a certificate of occupancy until the inspector has filed a letter indicating the required inspections have been performed.

"Multi-unit residential buildings" include condominiums and other residential buildings of more than two units. Hotels, motels, dormitories, care facilities, and floating homes are excluded, as are single ownership residential buildings with covenants preventing conversion to condominium status for at least 10 years.

"Building enclosures" are those portions of a building that separate interior and exterior environments from each other and also include balconies, decks, chimneys, garages, and other structures that interface with the building.

Design documents for the building enclosure must be submitted by an applicant for a building permit before construction starts. These documents must contain sufficient detail to allow construction of the enclosure. The documents must be prepared by or under the direction of an architect or engineer. The building department has no duty to review the documents.

Inspections must be done by a licensed architect or engineer or other person with verifiable training and experience in building enclosure design and construction. The inspector may, but need not be, the person who prepares the design documents or who is the architect or engineer of record on the building project, but the inspector may not be a person who otherwise has a monetary interest in the project. The inspector has no liability for the inspection to anyone other than the project developer. No evidentiary presumption is created regarding the use of an inspector's report or testimony in any arbitration or trial.

ALTERNATIVE DISPUTE RESOLUTION.

Once a lawsuit has been filed alleging a breach of a warranty under the WCA, several alternative dispute resolution provisions will apply.

The dispute will be referred to arbitration if within 90 days after a lawsuit is filed any party demands arbitration. Whether or not arbitration is demanded, mediation is required, and whether or not arbitration is demanded, either party may request the appointment of a neutral expert. Supreme Court rules will control the procedures for the use of any of these alternative resolution methods, including procedures for joining third parties in an arbitration. If the case is referred to arbitration, any party may appeal the arbitration award and demand a trial de novo, including demanding a jury trial. Whether the dispute is in arbitration or trial, within 60 days after the mandatory mediation, any party may make an offer of judgment.

- **Arbitration.** Any party may demand arbitration within 90 days after a lawsuit is filed. Unless the parties agree otherwise, one arbitrator will hear any claim of \$1,000,000 or less and three will hear larger claims. Unless the parties agree otherwise, the court will appoint all arbitrators. The party demanding arbitration must advance the arbitrator's fees. After an arbitration award, the non-prevailing party must pay the fees in cases involving condos built after July 1, 2005. In cases involving earlier-built condos, the arbitrator's fees continue to be the responsibility of the party demanding arbitration.
- **Mediation.** Mediation is mandatory in all cases. Unless the parties agree otherwise, the court or arbitrator will appoint the mediator. The parties and their experts are required to meet and to attempt to resolve or narrow the scope of their dispute. Mediation ends whenever one party notifies the other that mediation is terminated. In arbitrations, the party demanding arbitration must advance the fees of the mediator. In trials, the court will decide who advances the fees. After an arbitration award or a court judgment, the non-prevailing party must pay the fees in cases involving condos built after July 1, 2005. In cases involving earlier-built condos, the mediator's fees continue to be the responsibility of the party demanding arbitration, or if arbitration has not been demanded, the court will determine responsibility.
- **Neutral Expert.** Once the mandatory mediation is terminated, any party to the arbitration or trial may request the appointment of a neutral expert. The court or arbitrator decides whether or not an appointment will be made. A neutral expert must be a licensed architect or engineer with suitable experience and training. The court or arbitrator is to determine the scope of the expert's duties which, unless the parties agree otherwise, are not to include finding the amount of damages to be awarded or the cost of repairs. A neutral expert is not liable to the parties for his work as an expert. No presumption is created regarding a neutral expert's findings. The party who requests appointment of an expert is responsible for advancing the expert's fees. After an arbitration award or a court judgment, the non-prevailing party must pay the fees in cases involving condos built after July 1, 2005. In cases involving earlier-built condos, the expert's fees continue to be the responsibility of the party requesting the expert.
- **Trial de Novo.** Within 20 days after an arbitration award, any party may appeal the award and demand a trial de novo. If the judgment of the trial de novo is not more favorable to the appealing party than was the arbitration award, the appealing party must pay the other parties' costs and fees, including reasonable attorney fees, incurred after the filing of the appeal.

- **Offer of Judgment.** Within 60 days after the completion of mediation, any party may make an offer of judgment. The offer must include a demonstration of the ability to pay damages as well as any required costs and fees. If the claimant accepts the defendant's offer, the claimant is deemed the prevailing party and therefore entitled to recover not only damages but also costs and fees, including reasonable attorney fees. If an offer is not accepted and the final judgment is not more favorable to the non-accepting party, then the party making the offer is deemed the prevailing party. If an offer is not accepted and the final judgment is more favorable to the non-accepting party, then the court or arbitrator will determine who the prevailing party is. No costs and fees awarded against condominium owners pursuant to the offer of judgment provisions may exceed 5 percent of the assessed value of the condominium.
- **Application Dates.** The alternative dispute resolution provisions apply only to lawsuits filed on or after July 1, 2005.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect on July 1, 2005.

Testimony For: Multi-unit family housing is critical to many communities trying to meet their land use goals, especially in the Puget Sound area. There has been almost no such housing built in recent years. The bill will help with problems of water penetration which is one of the main causes in the decline of new housing. Owners with serious leaks often don't have the resources to fix the problem, can't afford to sue, and can't sell their homes or get insurance for their homes. Third party inspections during the course of construction will go a long way toward restoring consumer confidence in condos and other multi-unit housing. The alternative dispute resolution provisions of the bill will help with early settlements of disputes.

(With concerns) There are some technical issues with the bill that still need to be worked out. The requirement of filing of design documents with building permit applications is a concern for some building departments.

Testimony Against: None.

Persons Testifying: (In support) Representative Springer, prime sponsor; Representative Tom; Steve Seward and Marion Morgenstern, Study Committee; Angela Song, Washington Realtors; Ryan Spiller, Washington Homeowners' Coalition; Sue Dahlin, Sundance at Klahanie; and Scott Hildebrand, Master Builders' Association of King County and Snohomish County.

(With concerns) Mark Triplett, Washington Association of Building Officials.

Persons Signed In To Testify But Not Testifying: None.