SENATE BILL REPORT
EHB 1848

As Reported By Senate Committee On:
Judiciary, March 30, 2005

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: Passed House: 3/14/05, 97-0.
Committee Activity: Judiciary: 3/23/05, 3/30/05 [DPA, w/oRec].

SENATE COMMITTEE ON JUDICIARY

Majority Report: Do pass as amended.
Signed by Senators Kline, Chair; Johnson, Ranking Minority Member; Carrell, Esser, Hargrove, McCaslin and Rasmussen.

Minority Report: That it be referred without recommendation.
Signed by Senator Weinstein, Vice Chair.

Staff: Aldo Melchiori (786-7439)

Background: The Washington Condominium Act (WCA) controls the creation, construction, sale, financing, management, and termination of condominiums. A condominium (condo) 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 creates implied warranties and authorizes the use of express warranties regarding the quality of materials and construction in a condo.

In a 2001 decision, *Marina Cove Condominium Owners Association v. Isabella Estates*, the Washington State Court of Appeals held that binding arbitration clauses in condo agreements are unenforceable. 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 condo legislation passed in 2004, a Condominium Study Committee was created to look at: (1) the use of independent third-party inspections during the construction of condos in order to reduce water penetration problems; and (2) the use of alternative dispute resolution procedures in condo cases.

Summary of Amended Bill: Building enclosure design documents must be submitted with any application for a building permit for the construction of a multiunit residential building. The documents must address waterproofing, weatherproofing, and other protections of the building from water or moisture intrusion. A building department may not issue a building

permit unless the design documents have been submitted, but the department need not review or approve the documents.

Inspection provisions apply to construction for which an initial or rehabilitative building permit is issued on or after August 1, 2005. The building enclosures of all multiunit residential buildings must be inspected during the course of construction. The periodic inspections must determine whether the construction is in compliance with the enclosure design documents and must also include testing windows and window installations for water penetration problems. The inspections must be performed by a person who has training and experience in design and construction of building envelopes, who is free of improper interference or influence, and who has not been an employee of the developer. The inspections may be done by the architect or engineer who prepared the design documents or who is the architect or engineer of record on the project. A building department may not issue a certificate of occupancy for a multiunit residential building until a building enclosure inspection report has been submitted. However, the department need not determine the adequacy of the inspection.

The design document and inspection requirements do not create a right of action or any liability against any architect, engineer, or inspector. However, the developer and any architect, engineer, or inspector on a project may contractually agree on the extent of possible liability to the developer. No evidentiary presumption is created regarding an inspection report. No condominium unit can be sold without the required enclosure design documents and inspection report.

Every condo conversion requires an intrusive inspection of the building envelope with testing for construction quality and for water penetration. A conversion inspection must include a report of the findings of the inspection and any recommended repairs. The report must be made a part of the public offering statement for the condo. Any recommended repairs must be completed before the condo units can be sold.

The alternative dispute resolution provisions of the WCA apply to any such lawsuit that is filed and served on or after August 1, 2005. At least 10 days after filing and service, the parties must meet and confer on a case schedule to be proposed to the court. The proposed plan must cover schedules for the mandatory mediation process, possible selection of arbitrators, joinder of parties, investigations of the case, disclosure of repair plans and estimated costs, and each party's settlement demand or response.

Unless the parties agree otherwise, mediation must begin within seven months of filing and service. The court or arbitrator appoints the mediator unless the parties agree otherwise. Before mediation, the parties must meet and confer to attempt to resolve or narrow disputed issues. If, after the parties have met and conferred, issues still remain, any party may request the court or arbitrator to appoint a neutral expert. Unless the parties agree otherwise, the neutral expert may not have been employed as an expert by a party within the previous three years. The court, the arbitrator, or the parties by agreement select the neutral expert and determine matters such as the scope of the neutral expert's duties, the timing of inspections of the property by the neutral expert, and coordination of inspections by the neutral expert and the parties' experts. Absent an agreement by the parties, the neutral expert does not decide the amount of damages or the costs of repair. A neutral expert is not liable to the parties regarding

his duties. There is no evidentiary presumption created regarding a neutral expert's report. Each party must agree to provide a decision maker who has the authority to settle the dispute. Mediation ends upon written notice of termination by any party.

Any party may demand arbitration not less than 30 nor more than 90 days after the lawsuit has been filed and served. Subcontractors may be joined in an arbitration upon the demand of any party who has a legal claim against the subcontractor if the work performed by the subcontractor is an issue in the arbitration. Absent agreement by the parties, the case is heard within 14 months by a single court-appointed arbitrator if the case involves less than $1 million or by three court-appointed arbitrators for larger cases. Within 20 days after the arbitrator's decision is filed, either party may demand a trial de novo on appeal.

Different rules apply regarding payment of arbitrators, mediators, and neutral experts depending on whether a condominium was built pursuant to a building permit issued before or after August 1, 2005. For the earlier built cases, the party who demands arbitration pays for both the arbitrator and the mediator, and the party who requests a neutral expert pays for the expert. If arbitration has not been demanded, the court decides on payment of the mediator. These payments are not subject to the cost shifting offer of judgment provisions discussed below. For later cases, the same parties under the same situations must "advance" payment, but those payments are subject to possible shifting under the offer of judgment provisions.

The ultimate responsibility for the fees and costs of trial or arbitration may be affected by the acceptance or rejection of offers of judgment. Within 60 days after mediation is terminated, a condo declarant, condo association, or condo unit owner who is a party to the dispute in trial or arbitration may make an offer of judgment. Any offer not accepted within 21 days is considered rejected and withdrawn. A declarant's offer must include a demonstration of the ability to pay the judgment and any costs and fees, including reasonable attorney fees, within 30 days of entry of the judgment. If an association is a party to the dispute, then the association has sole responsibility for accepting or rejecting offers with respect to common elements of the condo. An association or owner who accepts an offer is considered the prevailing party and is entitled to the judgment and costs and fees.

Generally, if the judgment of the court in a trial de novo is not more favorable to the appealing party than the arbitration award, the appealing party must pay the respondent's costs and fees, including reasonable attorney fees. If the judgment is more than the arbitration award, the court may award those costs and fees to the appealing party. If an offer or offers of judgment have been made, and the final judgment of the court or arbitrator is not more favorable to the offeree than was the last offer, then the offeror is considered the prevailing party. If the final judgment is more favorable to the offeree, then the court is to decide any award of costs and fees in accordance with otherwise applicable law.

If a condo association has brought a claim, no award of costs and fees against the association may exceed 5 percent of the assessed value of the condo as a whole. If an individual unit owner has brought a claim, no such award against the owner may exceed 5 percent of the unit's assessed value.

Amended Bill Compared to Original Bill: All condominium conversions are made subject to building inspections for water penetration problems, regardless of whether the building had been made subject to a non-conversion covenant. The conversion inspection must include

testing such as the removal of siding to determine the manner in which the building was constructed. The inspection must also include an evaluation of water penetration issues, and the inspection report must also recommend any needed repairs. The inspection must be disclosed in the condo public offering statement. In addition, in the case of a building that is converted to a condo before the expiration of a 5-year covenant not to convert, any recommended repairs must be performed before the units may be sold as condos.

Builders and developers who are not required to comply with the course of construction requirements of the bill are given the option of electing to do so. This option applies to residential condominiums without attached units, to buildings which have attached units on separately platted lots, and to any buildings with two attached dwelling units. The inspections remain mandatory for multi-unit residential buildings of three or more units. Additional testing of window assemblies is not required if the same assemblies have already been tested on the same project site within two years.

The applicability provisions of the bill with respect to when building permits are issued and when legal actions are filed are clarified. The definitions of terms "multi-unit residential building" and "building enclosure" are clarified a definition for a "sale prohibition covenant" is provided.

Parties to a dispute are required to attempt to agree on a case schedule plan that includes specific deadlines for various events in alternative dispute resolution or trial. The interaction among the prevailing party cost and fees provisions of the bill with respect to arbitration, trial de novo, and offer of judgment are clarified.

Appropriation: None.

Fiscal Note: Not requested.

Committee/Commission/Task Force Created: No.

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

Testimony For: This is a unanimous recommendation from a broad group of representatives who represented very divergent perspectives. This legislation should reduce the number of disputes by helping assure quality construction. The dispute resolution provisions provide many incentives and avenues to divert these cases from trial. This is the result of a lot of compromise by all of the parties. Everyone gave a little to gain some assurances of quality construction and better dispute resolution. Affordable housing is a huge issue in Washington and this bill will help assure the availability of quality condominiums affordable by first time buyers. If the parties know that they can go to trial de novo, they are less likely to use alternative dispute resolution procedures fully. Giving these cases "priority" just puts them in line with a number of other issues for which the legislature has designated priority. Architects have some technical issues with the time lines and definitions in the legislation. Architects want to be involved more in the inspection process.

Testimony Against: None.

Who Testified: PRO: Representative Springer, prime sponsor; Steve Seward, study committee chairman; Todd Hobert, Washington Homeowner's Coalition; Sandi Swarthout,

Washington Homeowner's Coalition; Angela Song, Realtors; Martha Harden Cesar, Superior Court Judge's Association; Scott Hildebrand, Master Builder's Association; Jeff Hamlett, Arai Jackson Architects.