

HOUSE BILL REPORT

SSB 6385

As Reported by House Committee On:
Judiciary

Title: An act relating to real property.

Brief Description: Concerning real property.

Sponsors: Senate Committee on Consumer Protection & Housing (originally sponsored by Senators Weinstein, Kauffman, Fraser, Marr, Pridemore, Fairley, Brown, McAuliffe and Kohl-Welles).

Brief History:

Committee Activity:

Judiciary: 2/26/08, 2/28/08 [DPA].

**Brief Summary of Substitute Bill
(As Amended by House Committee)**

- Creates statutory implied warranties for the construction of improvements upon residential real property.
- Allows a current owner to sue for a breach of warranty and recover damages if the breach "adversely affects" the performance of the property.

HOUSE COMMITTEE ON JUDICIARY

Majority Report: Do pass as amended. Signed by 6 members: Representatives Goodman, Vice Chair; Flannigan, Kirby, Moeller, Pedersen and Williams.

Minority Report: Do not pass. Signed by 4 members: Representatives Rodne, Ranking Minority Member; Warnick, Assistant Ranking Minority Member; Ahern and Ross.

Staff: Edie Adams (786-7180).

Background:

A homeowner who suffers losses due to defects in the construction of the home may be able to seek redress through a cause of action for breach of contract or for breach of an implied

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warranty of habitability. There are no statutory warranties governing residential construction, except in the case of condominiums, and there is no statutory or common law negligence cause of action for construction defects.

Common Law Implied Warranty of Habitability. Under the common law, the buyer of a new home may sue the builder of the home for a breach of an implied contractual "warranty of habitability." This warranty covers structural defects in the house and its foundation that make the home unfit for its intended purpose. The warranty extends only to the first purchaser who occupies the home, and the home must have been purchased soon after the completion of construction. In addition, the sale must be of a commercial nature and the relative bargaining positions of the parties must be inherently unfair to the buyer. The implied warranty of habitability may be disclaimed by the seller if the disclaimer is conspicuous, known to the buyer, and specifically bargained for.

Statutory Warranties for Residential Construction. There are no statutory warranties applicable to new home construction except in the case of condominiums. The Washington Condominium Act (WCA) establishes the following implied warranties with respect to condominiums (condos): the condo is suitable for the ordinary uses of real estate of its type and is free from defective materials; and the condo has been constructed in accordance with sound engineering and construction standards, in a workmanlike manner, and in compliance with all applicable laws. Damages are recoverable only if the breach had an adverse effect that is more than technical and that would be significant to a reasonable person. Damages that may be awarded are the cost of repairs unless those costs are clearly disproportionate to the loss in the condo's market value caused by the breach, in which case damages are the loss in market value.

A cause of action for breach of an implied warranty under the WCA must be brought within four years after the cause of action accrues. For an individual condo unit, accrual occurs when the purchaser takes possession, and for common areas, accrual occurs upon the later of occupancy of a unit or completion of the common area.

Negligence-Based Actions for Construction Defects. There is no statutory cause of action for negligence in the construction of improvements to real property. Washington courts have declined to recognize a negligent construction cause of action by adopting the economic loss rule in the context of construction claims. The economic loss rule is used by the courts to maintain the boundary between tort claims and contract claims when a claim has the potential to be remedied under either theory. The economic loss rule bars a plaintiff from recovering in tort where a contractual relationship exists between the parties and the damages are "economic losses." "Economic losses" in this context mean losses related to the property subject to the contract, as opposed to losses resulting from personal injury or damage to other property.

Right to Cure Statute. In 2002 the Legislature enacted the contractor right to cure statute. This statute prohibits a homeowner from filing suit against a construction professional for alleged construction defects until the homeowner has given the construction professional notice of the alleged defect and an opportunity to cure the defect within time lines set out in the statute. Any suit filed before the owner provides the right to cure notice must be dismissed by the

court. "Construction professional" is defined as an architect, builder, builder vendor, contractor, subcontractor, engineer or inspector, including condo dealers and declarants, performing or furnishing the design, supervision, inspection, construction, or observation of the construction of any improvement to real property.

Construction Statute of Repose. A cause of action must be brought within a specified time limit from when the action "accrues." A cause of action accrues when facts sufficient to allow a lawsuit exist. A statute of limitations says how long a plaintiff has to bring a lawsuit after a cause of action has accrued. A statute of repose sets a time limit within which a cause of action must accrue. Construction claims are governed by a six-year statute of repose, beginning on the later of substantial completion of construction or termination of the project. This means that any claim against a construction professional must accrue within that six-year period or it is barred. If the claim accrues within the six-year period, the claimant then must bring the action within the applicable statute of limitation period.

Summary of Amended Bill:

Statutory implied warranties are created for the construction of improvements upon residential real property. "Residential real property" means a single-family house or a duplex occupied by the owner as a residence. A construction professional making improvements to residential real property warrants that the work will be:

- suitable for the ordinary uses of real estate of its type;
- free from defective materials;
- constructed in accordance with sound engineering and construction standards;
- constructed in a workmanlike manner; and
- constructed in compliance with all laws then applicable to the improvements.

A current owner may bring an action against a construction professional for a breach of any of these warranties. In order to recover damages, the owner must show that the breach adversely affects the performance of the property. An "adverse effect" must be more than technical and must be significant to a reasonable person, but need not render the property unfit for occupancy.

The damages that are awarded for a breach are the cost of repairs. However, if the cost of repairs is clearly disproportionate to the loss in market value, the damages are limited to loss in market value. The court may award costs and reasonable attorneys' fees to the prevailing party.

An action for breach of a warranty must be brought within four years after the date the cause of action accrues. The cause of action generally accrues: (1) in the case of newly constructed residential real property, on the date the first owner takes possession; and (2) in the case of improvements on existing residential real property, upon the later of substantial completion of construction or termination of the construction project. If the cause of action is for a breach based on a latent structural defect or latent water penetration defect, the discovery rule applies and the cause of action accrues when the claimant discovers or reasonably should have

discovered the defect. However, the action must accrue within the six-year statute of repose or the claim is barred.

Condos and nonprofit housing developers are exempt from the act. The existing definition of "construction professional" in the right to cure statute, which is the definition that applies to this act, is amended to exclude local government inspectors.

Amended Bill Compared to Substitute Bill:

The substitute Senate bill created a cause of action against construction professionals for negligence in the construction of improvements to real property intended for residential use.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date of Amended Bill: The bill takes effect July 1, 2009.

Staff Summary of Public Testimony:

(In support) A homeowner who buys a house that has major construction defects deserves an adequate remedy or mechanism to force the contractor to take care of the defects. Currently there is no remedy. There is no negligence action and there are no statutory warranties. The implied warranty of habitability provides little protection and usually it is disclaimed by the builder in exchange for a third party warranty. These third party warranties are so limited and require the homeowner to jump through so many hoops that they are really worthless.

Subsequent owners particularly have no rights or remedies. The average home turns over in less than four years and those subsequent owners have just as much right to a home that is habitable as the first purchaser.

The striking amendment will make builders responsible for their work. It provides to homeowners the same warranties and remedies that apply to condo owners. It creates a fair balance and will be good for the good contractors and bad for the bad contractors. It will not have the dire consequences predicted. The building industry is doing fine in other states that have strong homeowner protections.

Allowing builders to get away with shoddy construction is not the way to create affordable housing. The biggest hidden cost of home ownership is the cost to fix the house the buyer just paid good money for.

One change that should be made is to allow a discovery rule for latent defects that cause structural or water damage that may not show up within six years.

(In support with concerns) Local government inspectors should be exempted because they have a different type of duty that doesn't fit within this bill. Suppliers also should not be included.

(Opposed) The bill is bad for an industry that is already hanging on by its fingertips. Ninety-eight percent of builders have never had a claim. Most builders are small, building fewer than 12 homes a year, and if there is a problem they have to deal with it or they lose their client base. There are already remedies available to homeowners.

The bill will have a devastating impact on the insurance market. It will result in a lack of predictability, which will lead to less affordable and less available liability insurance, which will increase the cost of homes. This will also impact nonprofit housing because those builders also have to buy insurance.

The striking amendment tries to place the condo system on the very different single-family residence situation. The type of insurance currently required for condo builders just isn't available to home builders and it is much more costly. The striking amendment doesn't include all of the WCA changes that were part of the agreed package. Key components, such as mediation, arbitration, and an offer of settlement provision, are not included.

This type of major policy change shouldn't be rushed through on such short notice with little time to examine its impact. You need to evaluate the information that is out there to determine what the problem is and how it should be addressed. There is a need to establish a process to ensure the competency of contractors and evaluate complaints against contractors. There should also be greater accountability of inspectors.

Persons Testifying: (In support) Senator Weinstein, prime sponsor; George and Edward Robison; M. Jayne Freitag-Koontz; Sandy Levy; and Karen Veldeer, Cooper Crest Community.

(In support with concerns) Derek Young, Cities of Lakewood, Pasco, and Spokane Valley; and Margaret Hyneman, National Association of Credit Managers.

(Opposed) Kevin Coker, American Institute of Building Design; Amy Brackenbury and Shelli Lucus-Kennedy, Building Industry Association of Washington; Daimon Doyle; Cliff Webster, Architects and Engineers Legislative Council; Mel Sorensen, Washington Defense Trial Lawyers; and Stan Bowman, American Institute of Architects of Washington Council.

Persons Signed In To Testify But Not Testifying: None.