

**SUBJECT:** Revising operation of the Texas Residential Construction Commission

**COMMITTEE:** State Affairs — committee substitute recommended

**VOTE:** 6 ayes — Swinford, Van Arsdale, Christian, Flynn, Parker, Veasey  
1 nay — Farrar  
2 absent — Paxton, B. Cook

**WITNESSES:** For — Pamela Bolton, Texas Watch; Jeffrey Brooks, Texas Public Interest Research Group; John Burchfield, Greater Houston Builders Association, David Weekley Homes; Patricia Cabrera, Villa De Fortuna; J.C. Calcote, Texas Panhandle Builders Association; Jerry Carter, Texas Association of Builders; Paul Cauduro, Home Builders Association of Greater Dallas; W.T. Little, Southeast Texas Builders Association; Rick McGuire, West Texas Home Builders Association; Rick Montelongo, Greater San Antonio Builders Association; Michael Moore, Greater San Antonio Builders Association; Scott Norman, Texas Association of Builders; Edward Ocampo, Villa De Fortuna Subdivision, KB Homes; Dorina Corrente; Pat Egert; Sherry Freeland; (*Registered, but did not testify:* Carol Baker, Home Builders Association of Greater Austin; Brooke Bulow, Home Builders Association of Greater Austin; Ron Connally, Texas Panhandle Builder Association; Ned Muñoz, Texas Association of Builders; Bob Stout, Newland Communities Texas; Kathryn Wood, Greater Houston Builders Association; Susan Wright, Greater San Antonio Builders Association

Against — Connie Hudson; Alfonso Peña; Stephanie Thompson

On — Geoff Bracken, Perry Homes, A Joint Venture; John Cobarruvias, Homeowners Against Deficient Dwellings; Carlos Contreras, KB Home; Mark Eberwine; A. Duane Waddill, Texas Residential Construction Commission; (*Registered, but did not testify:* Gary Poenisch)

**BACKGROUND:** In 2003, the 78th Legislature enacted HB 730 by Ritter, et al., the Texas Residential Construction Commission Act (TRCCA). The TRCCA requires home builders to register with the Texas Residential Construction Commission (TRCC). It also defines the state-sponsored inspection and

dispute resolution process (SIRP) to resolve homeowner and builder disputes over construction defects. The TRCCA includes requirements for limited statutory warranties and building performance standards for new homes.

DIGEST:

CSHB 1038 would add a variety of violations for which a builder could be subject to disciplinary action. Additional disciplinary remedies would be added, and administrative penalties would be increased. The bill would make several changes to the state-sponsored inspection and dispute-resolution process and to TRCCA general provisions.

**Disciplinary action.** CSHB 1038 would allow the commission to obtain injunctions and issue cease and desist orders for violations of the TRCC rules. A person subject to a cease and desist order could appeal directly to the district court within 30 days of the decision. The commission could assess a fine of \$1,000 a day for failure to comply with a cease and desist order. Before issuing a cease and desist order, the commission would hold a hearing to determine if a violation had occurred.

CSHB 1038 would clarify the class of people eligible for disciplinary action to include a builder, builder's representative, or a person who controlled a majority ownership interest in a builder. TRCC could take joint action against any of these parties, and they would be jointly and severally liable for any amount due the commission.

The bill would add the following acts to those subject to disciplinary action:

- misapplication of trust funds ;
- paying a fee by a credit card or electronic transfer that was declined or returned;
- failure to pay a fee to register a home ;
- engaging in fraud or misappropriation of funds as determined in a hearing;
- failing to participate in the state-sponsored inspection and dispute resolution process if required to do so;
- failing to register as a builder;
- using or attempting to use an expired or revoked registration;
- falsely representing that the person holds a registration;
- acting as a builder using a name other than the name on the registration;

- aiding, abetting, or acting as an agent of someone that did not hold a registration to evade provisions of the TRCCA;
- allowing another person to use one's registration;
- failing to repair a home as recommended by a third-party inspector, continuous or repeated failure to comply with the statutory warranties or building performance standards established by the TRCC as established at a hearing; and
- violation of any TRCC rule.

The commission could not revoke a registration unless the misconduct occurred within the preceding 12 months and involved the greater of four homes in one year or 2 percent of the homes registered by the builder. TRCC could not revoke a registration for fraud or misappropriation of funds unless the determination of these offenses had been made in a final nonappealable judgment by a court. Appeals to a district court regarding revocations or suspensions of registration would be determined based upon the preponderance of evidence standard.

In addition to other disciplinary actions, TRCC could assess an administrative penalty of up to \$10,000 for each violation. To impose an administrative penalty for failure to comply with statutory warranties or building and performance standards, the commission would be required to show at hearing that the violations were repeated or continuous. The TRCC could request a continuance of a hearing even if the applicant did not agree. Fraud, misappropriation of funds, or misappropriation of trust funds would be punishable by a higher administrative penalty of up to \$100,000.

**State-sponsored inspection and dispute resolution process.** In a non-structural matter, an inspector would have 30 days rather than 15 to issue a recommendation. The recommendation of a third-party inspector or a panel of state inspectors would be considered admissible as evidence as a business record. TRCC could not report inspection findings against a builder if the builder made or offered to make the repairs before or after the inspection. TRCC could not require a builder to reimburse fees or inspection expenses if the builder made an offer to repair the home before the inspection if the offer was substantially similar to the inspector's recommendations. The bill would exempt the homeowner from going through the TRCC if the builder was not registered when the homeowner filed a complaint.

If a SIRP request was accepted by the commission, a party to the dispute who did not file the request could respond to the request with evidence not later than the 15th day after receipt of a copy of the request. If the response alleged a defect not stated in the initial request, then the third-party inspector also would make a determination regarding the alleged defect.

A person who responded to a request for an inspection would disclose in the response the name of the person who inspected the home prior to the request submission. If the name of the inspector was not disclosed, the person could not be used as a witness in an action arising from a construction defect.

The bill would decrease the minimum number of years of experience required of third-party inspectors inspecting issues involving workmanship and materials from five years experience to three years experience. If the inspector inspected issues involving structural matters, the minimum years experience would be reduced from 10 years to five years. All third-party inspectors would have to receive training on state-sponsored inspection and dispute resolution and take annual continuing education.

A third-party or state inspector would not be liable for civil damages associated with the inspector's duties if the inspector did not act with wanton and willful disregard for the rights, safety, or property of another. TRCC could reimburse an inspector for travel expenses whether or not the expenses exceeded the amount collected for the inspection and dispute resolution process. The TRCC no longer would have to provide a mechanism to submit SIRP requests by e-mail.

**Builder registration, rights, and duties.** Municipalities would verify that a builder was registered with TRCC before issuing a building license to that builder. CSHB 1038 would exempt only those licensed by the state or a state agency to practice a profession related to residential construction from the definition of builder. It would also add to the definition of a builder a person who builds a home with the intent to immediately re-sell. Such individuals would be liable as builders under construction warranties. The bill would lower the value of interior home improvements subject to the TRCC from \$20,000 to \$10,000.

A builder could not sue for enforcement of a residential construction contract unless the builder held a certificate of registration at the time the contract was signed and throughout the time the contracted work was performed. If a contract for a home improvement contained a binding arbitration clause, the homeowner would sign an additional space on the contract acknowledging awareness of it. The contract would contain the contractor's certificate of registration number from the TRCC if registration was required, as well as the address and telephone number at which the owner could file a complaint with the TRCC.

The bill would require a builder to register a home at the earliest of the date of substantial completion of construction, the date the home was occupied, or the date of the issuance of the certificate of completion or occupancy. Colonia builders would register homes even if they were not subject to the building requirements established by the TRCC. A homeowner in a colonia who claimed a post-construction defect would go through the SIRP. Warranties established by the TRCC would not supersede other warranties established to protect homes built in colonias.

**TRCC composition and responsibilities.** The bill would prohibit an officer of a company involved in the building industry or an officer's spouse from being a member of the TRCC or being employed in an executive, administrative, or professional capacity.

TRCC could procure and distribute to consumers informational materials and promotional items that contained commission outreach and general information. The commission would make available to the public information about each complaint that resulted in a disciplinary action by the commission but in doing so would not disclose the address of an individual home.

The commission could charge late fees up to the amount of the fee due and could charge a reasonable fee for:

- open records requests;
- state-sponsored inspections; and
- producing and distributing printed materials for use by builders.

Fees for application for registration, registration renewal, and late charges would be nonrefundable. The commission could seek reimbursement for any amounts due or restitution for any dishonored payment.

**General provisions.** The House Committee on State Affairs would conduct an interim study on the creation of a fund to reimburse aggrieved persons who had experienced damages from a builder's actions. Recommendations from the study would be provided by September 1, 2008.

CSHB 1038 would take effect September 1, 2007, and would apply only to an application for a building permit, an application to be a Star Builder, or a SIRP request submitted on or after that date. New disciplinary action and related punishment provisions would pertain only to violations that occurred on or after September 1, 2007. Finally, provisions regarding restrictions on builders issuing suits based upon whether or not they were registered while performing work would apply only to work performed on or after September 1, 2007.

**SUPPORTERS  
SAY:**

CSHB 1038 would give the TRCC the tools necessary to increase its effectiveness in protecting homeowners. In the comptroller's homeowner study released in January 2006, 86 percent of homeowners who had construction defects verified by the state inspection and dispute resolution process reported that their construction defects were never fixed. The bill would give the TRCC the enforcement authority it now lacks to hold builders accountable for shoddy building practices.

The bill would include significant increases of TRCC disciplinary power. The TRCC would have the authority to take disciplinary action for continuous or repeated failure to comply with statutory warranties and building and performance standards as cited by third-party inspectors. Other critical violations against which the TRCC could take disciplinary action would include fraud, misappropriation of funds, failure to register as a builder, or otherwise violating the TRCCA or a TRCC rule.

CSHB 1038 would expand the parties against whom a homeowner could take action. The builder's agents and those who had a majority interest in the builder would be subject to disciplinary action, so these individuals could not evade their shared responsibility to homeowners. These parties would be jointly and severally liable for any amounts due to the TRCC, giving the TRCC more means to collect on amounts owed. The bill also would provide remedies for homeowners who had been harmed by unregistered builders. Municipalities could not issue building permits to builders not registered with the TRCC. If a builder performed work

without registration, a homeowner could disregard the SIRP process and go directly to court.

Remedies for these violations would be enforceable because the TRCC could issue cease and desist orders against those violating the TRCCA and could get court-ordered injunctive relief if builders did not comply. In addition, the administrative penalty for misappropriation of funds and fraud could be as much as \$100,000, and the maximum for all other administrative penalties would be doubled. These appropriately severe penalties would be an incentive for homebuilders to perform work properly the first time and to address quickly any issues that were identified after construction.

The bill would arm consumers with more information and increase responsiveness to consumer complaints. It would strengthen the homeowner's presumption of a defect in subsequent civil actions by making an inspector's recommendation self-authenticating. This would save time and money for the homeowner in court.

The bill simultaneously would maintain appropriate protections for builders. The bill would ensure that a revocation of registration could not occur unless violations involved the larger of four or more homes registered by the builder or at least 2 percent of the homes registered by the builder. This would recognize that some builders conducted more business than others and would ensure that a very large builder would not have its registration revoked for isolated incidents in a much larger business. If the builder was a bad actor, there would still be multiple violations upon which to base a revocation.

TRCC could not assess administrative penalties for failure to comply with statutory warranties unless TRCC had shown at a hearing that the violations were repeated and continuous. A builder's license could not be revoked in a fraud or misappropriation of funds case until these offenses were determined in a final, nonappealable judgment by a court. Allowing suspensions while a builder awaited a final court judgment would be acceptable because suspensions would be temporary. To reach the point of appeal to a court, the builder already would have been proven at fault in a hearing. This would be enough evidence to assess a suspension because of the increased likelihood the individual could cause harm to other homeowners.

The bill appropriately would disallow a builder from filing suit against a homeowner if a builder was not registered at any time during which work was performed under a contract. If a builder had performed work while not registered, the builder would have forfeited his right to suit because the builder was in violation of the TRCCA and was falsely representing himself to the homeowner.

CSHB 1038 would not drop experience requirements below what would be necessary to fulfill the professional duties of an inspector. The bill would maintain certification and training requirements that an inspector could not achieve if the inspector were not experienced enough to do so.

CSHB 1038 would not address warranties because the TRCCA already contains appropriate flexibility for the TRCC to define warranty standards. Minimum standards for warranties have been established, and TRCC has rulemaking authority to create more stringent warranty standards if research on residential construction practices indicates changes to warranties would be appropriate. For example, TRCC has a rule that if the manufacturer of an appliance has an independent warranty that the builder would adhere to a warranty standard that was the greater of the two years defined in statute or the life of the manufacturer warranty.

Finally, the bill would make the commission more impartial by making it unlawful for the officers of a builders' trade association to be members or employees of the TRCC. The TRCCA includes the standard sunset provisions governing membership of a commission, so conflict of interest provisions for the commission would be consistent with other Texas regulatory bodies.

CSHB 1038 is a balanced bill that would make the TRCC a stronger, more effective agency with more power to protect homeowners and punish the bad actors in the residential construction industry.

**OPPONENTS  
SAY:**

In trying to amend the TRCCA in favor of homeowners, CSHB 1038 would ignore the rights of homebuilders. Most builders are responsible workers trying to fulfill their contracted duties, and these individuals deserve due process as much as homeowners if and until it was proven that the builder was at fault.

Determining whether a builder could file suit to enforce a construction contract should be based only upon whether the builder was registered at

the time the contract was entered into. Further requiring that the builder be registered during the time work was performed under the contract could provide opportunities for homeowners to dodge legitimate suits by arguing about when work was or was not performed.

CSHB 1038 would prevent the TRCC from revoking a builder's registration in a fraud or misappropriation of funds case until the case was determined in a final nonappealable judgment by a court, but there would be no similar protection from registration suspension until such a court opinion had been issued. Given that the TRCCA does not allow a builder to work while his license is suspended, such a suspension would keep a builder from earning a living until a court decision was made. In particular, if a court found that a builder was not liable for fraud or misappropriation of funds, then the builder unjustly would have gone without work for the period of time in which a suspension was sustained.

Finally, because the bill would not specify the jurisdiction of the court at which a judgment could be made regarding the commission of fraud or misappropriation of funds, it would be possible that builders that operated across the nation could be unaware they had been sued in a different state. If the builder incurred a default judgment in such a case, the judgment would be sufficient to revoke a registration even though a builder could contend that the court had no jurisdiction over that builder.

OTHER  
OPPONENTS  
SAY:

Although many of the provisions in the bill would be positive, CSHB 1038 would not go far enough to help homeowners and would decrease consumer protections in some areas.

The bill should not decrease the number of years of experience required to be an inspector. It is imperative that inspectors are sufficiently experienced to make expert assessments regarding alleged construction defects. This expertise is of benefit to both the builder and the homeowner.

In addition, the bill could shelter a builder's substandard work practices because TRCC would not have to report inspection findings against a builder if the builder offered to make substantially equivalent repairs to the inspector's recommendation. A builder's offer to make repairs would not guarantee follow-through, and the public would have a right to know about obligations that a builder did not fulfill.

One of the most critical reforms needed for the TRCCA was not addressed in CSHB 1038. The bill at a minimum should extend the warranty periods from one year to two years for workmanship and from two years to three years on electrical and appliances. For example, it is uncommon for tiles to loosen after the first year if shoddy work was performed, yet the warranty would not address repairs after a year. In addition, a homeowner should not anticipate that an appliance would fail after two years, yet after this time period, the homeowner's only recourse would be the manufacturer. When confronted with an appliance failure, most manufacturers would point a consumer back to faulty installation on the part of the builder. Such short warranties create a frustrating cycle that leaves no remedy for the homeowner. Ideally, the bill would not dictate warranty periods in statute so that the commission could use its judgment to set appropriate warranty periods. This would be especially critical if the manufacturer warranty was shorter than the warranty in statute.

The bill would not go far enough to ensure unbiased representation on the commission. Currently, there are limited restrictions on who can be appointed by the governor to serve as one of the three TRCC public members. CSHB 1038 only would add the requirement that members of the commission or their spouses not be officers of a Texas trade association related to residential construction. This would not prevent a biased party from serving as a public commission member. For example, no aspect of the TRCCA would prevent an attorney who represented homebuilders from filling one of the public membership positions. Without unbiased representation, the TRCC would continue to favor the building industry.

Finally, the report on the TRCC study released by the comptroller in January 2006 made 16 recommendations for changes that should be made to the TRCC. CSHB 1038 would not implement the full set of recommendations. It would be better for the TRCC to be abolished and provide homeowners immediate access to the court system than to continue the TRCC without the appropriate authority and impartiality.

NOTES:

Significant changes made by the committee substitute to the filed version of HB 1038 include:

- requiring the homeowner to sign an additional space on the contract acknowledging awareness of a mandatory arbitration clause;

- lowering the value of home improvements subject to the TRCCA from \$20,000 to \$10,000;
- giving the TRCC authority to issue cease and desist orders for violations of the TRCC rules;
- allowing the commission to assess a fine of \$1,000 a day for failure to comply with a cease and desist order;
- allowing the commission to charge for an open records request, an inspection request, or bulk print materials for builders;
- requiring the commission to make public every complaint that resulted in disciplinary action;
- prohibiting a builder from suing a homeowner to enforce a contract if the builder was not registered when it entered into the contract and built the home;
- adding to the list of things for which builders could be disciplined, including misapplication of trust funds and failing to repair a home as recommended by a third-party inspector;
- prohibiting the commission from revoking a registration unless the misconduct involved the greater of four homes in one year or 2 percent of the homes registered by the builder;
- making inspector's recommendations business records for evidentiary purposes;
- making decisions on appeals based upon a preponderance of the evidence;
- increasing maximum administrative penalties;
- exempting the homeowner from going through the TRCC if the builder was not registered when the homeowner filed his complaint;
- permitting an inspection as evidence only if the inspector had been named in the SIRP request or response;
- decreasing the minimum number of years of experience required of third-party inspectors;
- exempting inspectors in certain instances from civil liability;
- permitting a response to a SIRP request from a party that did not initiate the request;
- prohibiting the TRCC reporting a finding against a builder if the builder made or offered to make repairs; and
- commissioning the House State Affairs Committee to conduct an interim study.

The companion bill, SB 210 by Fraser, has been referred to the Senate State Affairs Committee.

The LBB estimates it would cost \$503,803 a year to implement the changes in CSHB 1038, including six additional FTEs, travel costs for inspectors, and costs associated with hearings and judicial actions. These costs would be covered by fees raised by TRCC.