

**STATE OF MARYLAND
OFFICE OF THE ATTORNEY GENERAL**

ANNUAL REPORT

**OF THE
HOME BUILDER REGISTRATION UNIT
CONSUMER PROTECTION DIVISION
OFFICE OF THE ATTORNEY GENERAL**

**SUBMITTED TO THE
GOVERNOR AND GENERAL ASSEMBLY
OF MARYLAND**

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TABLE OF CONTENTS

I.	Executive Summary	1
II.	Registration of Builders	3
	A. The Home Builder Registration Unit	3
	B. Builder Registration Under the HBRA	3
	C. Who Is a Builder?	4
	D. Who Are Maryland's Builders?	5
III.	Communication with Builders and Consumers	9
	A. Outreach to Builders	9
	B. Consumer Education Pamphlet	9
	C. Website Development	10
IV.	Coordination With Local Permit Offices	10
V.	Evaluating Consumer and Builder Dispute Resolution	11
VI.	Law Enforcement	12
VII.	Registration Fees Issue	14

I. EXECUTIVE SUMMARY

Prior to January 1, 2001, home builders were not required to be registered or licensed by the State of Maryland.¹ Existing laws provided partial protections for home buyers by focusing on protection of the buyer's deposit; required contract provisions and disclosures; and prescribed terms of non-mandatory home warranty security plans.² The General Assembly heard testimony from home buyers about problems they faced with their builders that were not being adequately prevented or resolved by the then current law. In response to this testimony, the General Assembly in the 2000 Session passed the Maryland Home Builder Registration Act (the "Act" or "HBRA"). The HBRA is designed to provide additional protections to new home buyers by requiring builders to register with the State and by providing an enforcement mechanism that will allow the State to prevent builders with a bad track record from building or continuing to build in Maryland.

The Home Builder Registration Unit (the "Unit") of the Consumer Protection Division of the Office of the Attorney General was created by the Act to administer and enforce the Act. The Act requires that the Consumer Protection Division make an annual report of its activities to the Governor and General Assembly on November 1st of each year. This is the first report since the law became fully operational on January 1, 2001.

The Unit's activities focus on five primary objectives, which are summarized in this report:

! Registration of Builders: 2,304 builders registered as of September 30, 2001. Half of the builders report building five or fewer houses during 1999 and 2000, which is 9% of the houses built. Conversely, 2% of builders report building more than 100 houses per year, which is 41% of the houses built in 1999 and 2000.

! Education of Builders and Consumers: The Unit has published and distributed 60,137 copies of *BUYING A NEW HOME - Consumer Rights and Remedies Under Maryland Law* as of September 30, 2001; met with home builders throughout

¹ Montgomery County and Prince George's County have varying forms of builder licensing or registration.

² New Home Deposits, Md. Code Ann., §10-301 et seq., Custom Home Protection Act, Md. Code Ann., Real Property §10-501 et seq., and New Home Warranty Security Plans, Md. Code Ann., Real Property §10-601 et seq.

Maryland; and constructed a website – www.oag.state.md.us/homebuilder – to give consumers, builders, permit offices and the public information about registered builders, building laws, and home building issues for consumers.

! Coordination with Local Building Permit Offices: The Unit has coordinated with local permit inspection offices to ensure that unregistered builders cannot obtain building permits and that builders with unresolved building code orders are reported to the Unit. Lists of registered builders are publicly available on the Unit's website.

! Evaluation of Consumer and Builder Dispute Resolution: While the program is too young to draw any firm conclusion, preliminary data suggests that the number of consumer complaints about builders filed with the Consumer Protection Division has remained relatively stable at about 200 complaints per year. However, consumers and builders are entering into resolutions through voluntary mediation at a significantly higher rate since the home builder registration program went into effect: 67% of consumer complaints that were mediated by the Consumer Protection Division were solved through mutual agreement, as opposed to 46% and 43% in the two years prior to when the Home Builder Registration Act went into effect.

! Law Enforcement: The Unit has opened 29 investigations through September 30, 2001 after receiving reports of unregistered builders or violations of the Consumer Protection Act. The Unit brought an enforcement action against an unregistered builder who had taken a \$31,000 deposit from a Prince George's County consumer but did not begin construction. A cease and desist order has been issued to stop the builder from continuing to build in Maryland, and a hearing is scheduled for December 7, 2001 to determine restitution for the consumer and penalties. Most of the investigations have been resolved by having the builder register or determining that the builder is no longer building in Maryland and not required to register. Ten cases are currently under investigation.

II. REGISTRATION OF BUILDERS

A. **THE HOME BUILDER REGISTRATION UNIT**

A central purpose of the HBRA is to require that all new home builders in Maryland register with the Unit. The Home Builder Registration Unit was created by the Act to administer and enforce the Act. A special fund was created to fund the Unit's activities, which is paid for through the collection of registration fees. The fees are limited by the Act to be no more than \$600 for a biannual registration period. HBRA §§4.5-201--203. The Unit has four positions: a Director/Assistant Attorney General, an Administrator, an Investigator, and a Secretary.

B. **BUILDER REGISTRATION UNDER THE HBRA**

The Act establishes a registration procedure that simply requires the disclosure by the builder of necessary information in an application form, and the payment of the required registration fee. The Act does not provide for competency testing or proof of financial responsibility. The Unit has implemented the registration requirements with an objective of making registration an easy and quick procedure.

To register, builders are required to complete an application form, provide information about the principals of the company and past legal proceedings involving the builder, and pay the registration fee of \$600. The registration by law lasts two years and expires on the second anniversary of the registration's effective date. HBRA § 4.5-305. The Unit will mail a renewal application to the builder's last known address at least 60 days before the registration expires.

The application provides the Unit with general information about the company or entity that is registering. It also provides the Unit with information about each "principal" of the company, which the HBRA defines to be the persons with at least a 10% ownership interest, directors, partners, officers and managers of the company. One of the purposes of the Home Builder Registration Act is to track builders who dissolve entities without meeting their financial obligations and then begin building again under a new company name. Such builders may be subject to denial or revocation of their registration under HBRA §4.5-308. To achieve this goal, the Unit must gather information from the applicants about the principals who own and operate building companies.

Predictably, there was a surge of builder applications in late 2000 and early 2001. During this time, all builders who completed the application process were

registered since the HBRA provides that any builders' acts or omissions occurring before January 1, 2001 shall not be interpreted to have any effect on the registration. By September 30, 2001, the Home Builder Registration Unit registered 2,304 builders and continues to receive registration applications on a daily basis.

C. WHO IS A BUILDER?

The HBRA defines "home builder" and "new home" broadly to ensure that all new home builders in Maryland must be registered. HBRA §4.5-101(f) and (k). The exceptions to the HBRA are narrowly drawn.³ Questions arose during the implementation of the HBRA as to whether certain types of companies or activities were covered by the HBRA. The Unit applied the Act and advised people that:

! There is no exemption in the HBRA for "construction managers," who are sometimes employed by consumers in lieu of hiring a general contractor/builder to manage the construction of the house.

! "Builders" who must register include non-profit organizations and vocational educational schools that construct homes for sale to consumers.

! Builders who install used mobile homes or industrialized buildings must register.

! The Home Builder Registration Act was not meant to require that a builder cross-register with the Home Builder Registration Unit as a new home builder and with the Maryland Home Improvement Commission (MHIC) for the same construction project. A builder would have to register with both agencies if any of its projects were building new homes and other projects were doing home improvements on pre-existing homes. The local permit office determines whether proposed construction is a "home improvement" or a "new home" for the purposes of issuing the construction permit.

³ The HBRA excludes from registration employees, subcontractors and vendors of a registered home builder; the manufacturer of industrialized building unless the manufacturer also installs the building; real estate developers who do not also construct homes; construction financiers; and builders who build solely in Montgomery County. HBRA §4.5-101(f)(3). Landowners who obtain building permits in their own name and who directly perform the construction on their own land for their own use are also exempted. HBRA §4.5-601.

D. WHO ARE MARYLAND’S BUILDERS?

Registering builders provides additional public information about builders in Maryland. The self-reports of the builders, combined with other available data, provides the following profile of Maryland Builders:

! Number of Builders: There are 2,304 registered builders in Maryland as of September 30, 2001.

! Size of Builders:

The following chart shows that the majority of Maryland’s home builders are small companies: almost half (49%) of the builders report building five or fewer houses per year in 1999 and 2000, which is 9% of the houses built. These small companies may be individuals who build a few houses each year, or may be LLCs that did not build any houses in the past year, intends to build an entire subdivision this year, and will cease to exist the following year. A builder’s legal identity and level of production is not necessarily static from year to year. Conversely, 2% of builders report building more than 100 houses per year, which is 41% of the houses built in 1999 and 2000.

Size of Maryland Builders And Number of Houses Built in 1999 and 2000								
Houses Built by Builder	1999				2000			
	Number of Builders	Percentage of Builders	Total Number of Homes Built	Percentage of Homes Built	Number of Builders	Percentage of Builders	Total Number of Homes Built	Percentage of Homes Built
Unknown	520	23%			454	20%		
0	118	5%	0	0%	74	3%	0	0%
1 to 5	1024	44%	2475	9%	1059	46%	2546	9%
6 to 10	239	10%	1874	7%	253	11%	1975	7%
11 to 20	166	7%	2539	10%	195	8%	2967	11%
21 to 30	86	4%	2193	8%	99	4%	2514	9%
31 to 40	45	2%	1658	6%	52	2%	1893	7%
41 to 50	25	1%	1155	4%	29	1%	1329	5%
51 to 100	45	2%	3188	12%	56	2%	3861	14%
101 and up	36	2%	11209	43%	33	1%	10829	39%
Total	2304		26291		2304		27914	

Source: Builder Registration Applications, Md. Dept. of Planning data.

! Type of Construction: The vast majority – 82% – of Maryland’s builders report that they build new homes, custom homes or condominiums. Another 8% report they build industrialized buildings, and 4% report they build mobile homes. (The

remaining 6% did not report).

! Form of Business: The majority (58%) of Maryland's builders use corporations as their form of business organization. Another 19% are sole proprietorships, and 17% are limited liability companies (LLCs).

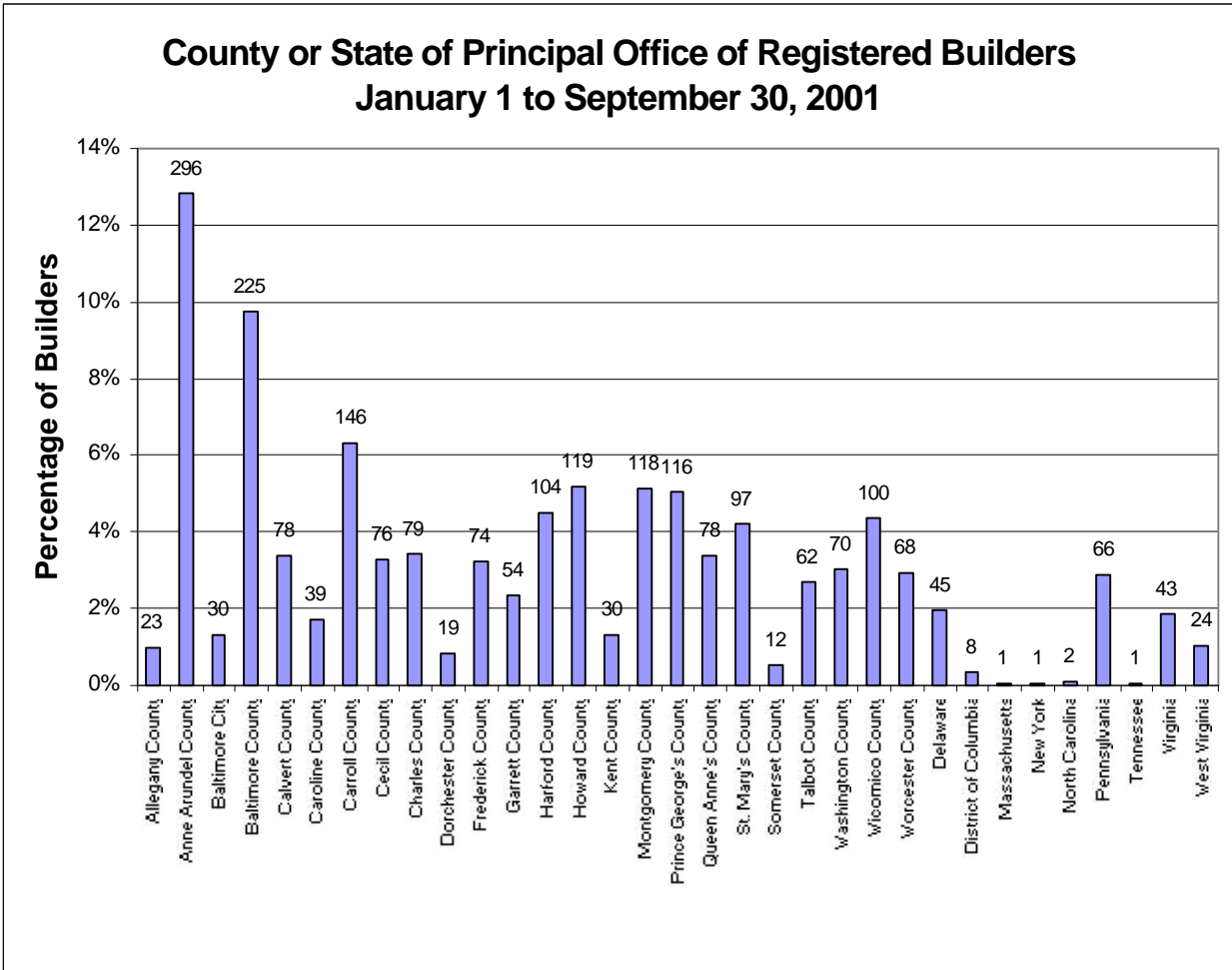
! Location of Builders and Housing Construction:

Not surprisingly, Maryland's builders are located in the regions of Maryland that are experiencing the most new home building activity, as measured by the number of single family housing permits issued: 71% of building permits for single family construction were issued in the Washington Suburban Region and in the Baltimore Region, where 52% of Maryland's builders are headquartered. Fourteen percent of builders who registered in Maryland are headquartered in other states. The following chart shows the headquarters of builders in each region, the number of single family housing permits issued in each region from January – September, 2001, and the percentage of the total number of single family housing permits issued in Maryland in each region from January – September, 2001.

Region	Percentage of Builders With Headquarters in Region	Number of Permits Issued in Region Jan - Sept. 2001)	Percentage of Permits Issued in Region
Baltimore Region (Anne Arundel, Baltimore City, Baltimore County, Carroll, Harford, Howard)	39%	9,281	37%
Out of State (Pennsylvania, Delaware, Virginia, West Virginia, Washington, D.C., Massachusetts, New York, North Carolina, Tennessee)	14%		
Suburban Washington Region (Frederick, Montgomery, Prince George's)	13%	8,805	35%
Upper Eastern Shore Region (Caroline, Cecil, Kent, Queen Anne's, Talbot)	10%	1,929	7%
Lower Eastern Shore Region (Dorchester, Somerset, Wicomico, Worcester)	9%	1,134	5%
Southern Region (Calvert, Charles, St. Mary's)	9%	3,092	12%
Western Region (Allegany, Garrett, Washington)	6%	891	4%
Totals	100%	25,132	100%

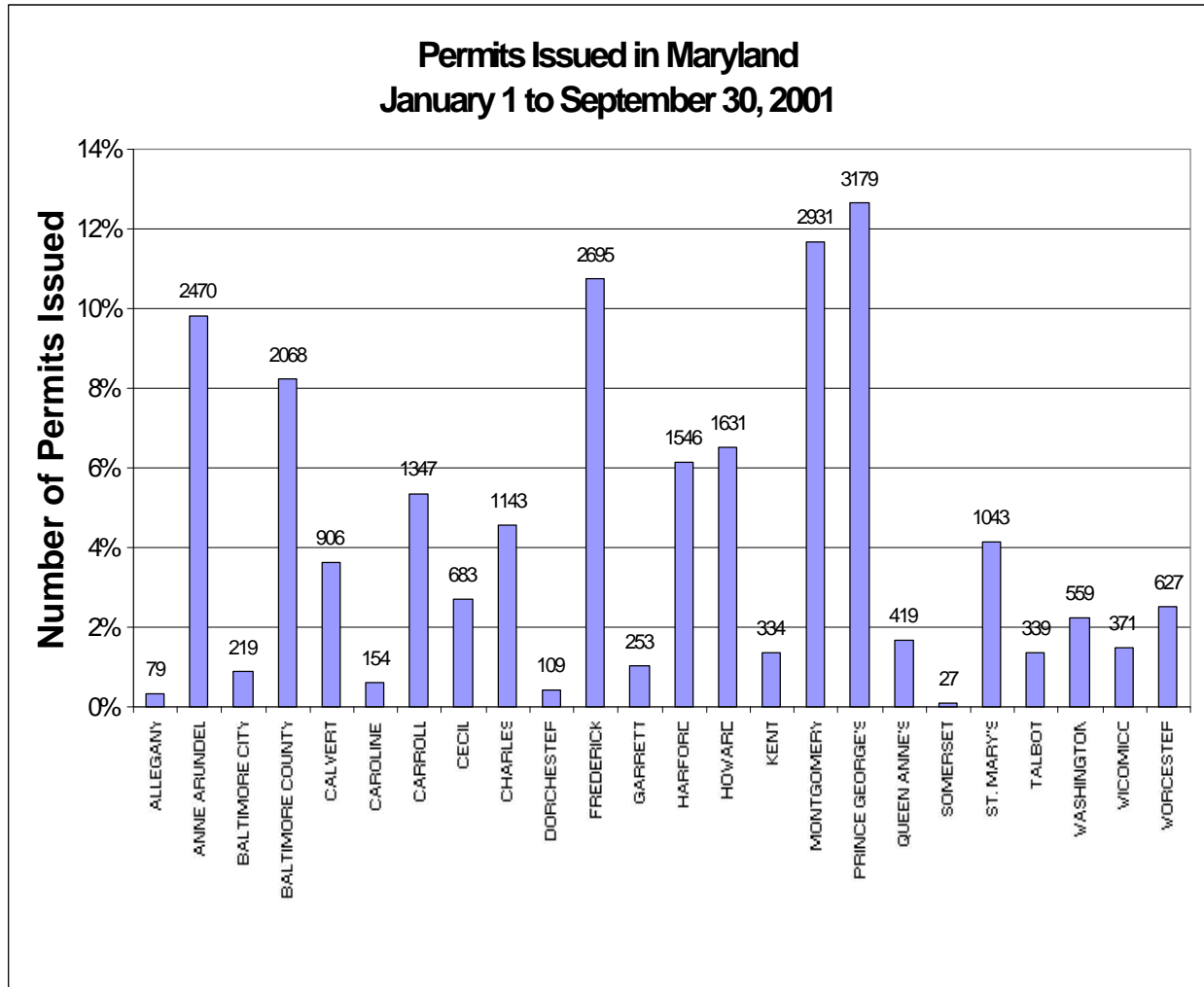
Source: Md. Dept. of Planning, for Single Family Permits Issued January through September, 2001.

The following graph shows the breakdown of builders' headquarters for each county and state:



Source: Md. Department of Planning data.

The following chart shows the number of permits issued in each county from January through September 2001.



Source: Md. Department of Planning data

III. **COMMUNICATION WITH BUILDERS AND CONSUMERS**

A. **OUTREACH TO BUILDERS**

The Home Builder Registration Unit traveled throughout the State to meet with builders prior to January 1, 2001 to talk with them about the Home Builder Registration Act and the actual process for registration. Meetings were held in Aberdeen, Baltimore, Hagerstown, Linthicum, McHenry, Rockville, Salisbury, Waldorf, and Woodlawn. Builders were given registration packets at these meetings and those builders who were unable to attend were able to obtain their applications by downloading them from the Home Builder Registration Unit's website (www.oag.state.md.us/homebuilder) or by calling the Unit.

The Unit also handled, and continues to handle, numerous builder inquiries by phone in regard to the Home Builder Registration Act and the registration process. The Act and the registration program were publicized by press releases in newspapers across the State, and televised appearances by the Attorney General.

B. **CONSUMER EDUCATION PAMPHLET**

The HBRA required that the Unit develop, in consultation with the industry, a consumer information pamphlet that describes the rights and remedies of consumers in the purchase of a new home and provides any other information that the Division considers reasonably necessary to assist consumers in the purchase of a new home. The law further requires that the consumer information pamphlet be given to consumers by builders before they sign a contract to purchase a new home. The receipt of the consumer information pamphlet shall be acknowledged in writing. HBRA §4.5-202(c).

The Division consulted with the industry, and developed and published a consumer education pamphlet, *BUYING A NEW HOME - Consumer Rights and Remedies Under Maryland Law*, in December, 2000. The Unit also drafted and distributed a model form for the consumer to sign to acknowledge receipt of the pamphlet. A copy of the pamphlet is attached.

The Unit has now distributed a total of 60,137 consumer information pamphlets to builders as of September 30, 2001.

C. **WEBSITE DEVELOPMENT**

The Home Builder Registration Unit developed a website to make information readily available to consumers, builders, permit offices and other entities requiring information about the home building industry. The website has been operational since January, 2001 and is updated regularly as information changes. Since the website can be accessed by anyone with Internet access, it is a significant mode of outreach and is an education resource for both consumers and builders. The website address is www.oag.state.md.us/homebuilder. On the website can be found:

- ! Information about the Home Builder Registration Unit, the Home Builder Registration Act, and the responsibility of builders pursuant to the Act.
- ! A list of currently registered builders that can be searched either alphabetically or by registration number.
- ! Registration materials including all the registration forms.
- ! The Home Builder Registration Act and other applicable laws.
- ! The consumer information pamphlet developed by the Home Builder Registration Unit, *BUYING A NEW HOME - Consumer Rights and Remedies Under Maryland Law*.

IV. **COORDINATION WITH LOCAL PERMIT OFFICES**

Permit offices have a pivotal role in the regulatory scheme of the Home Builder Registration Act. First, the building and permits department of a county may not issue a permit for home building unless the permit includes the home builder registration number of a registrant. HBRA § 4.5-601. This is the critical first line of defense against unregistered builders. Second, local permit offices are required to notify the Unit of any builder who, within a reasonable time, fails to correct a building code violation, so that the Unit may consider imposing registration sanctions. HBRA §§4.5-602(b), 4.5-308.

The Unit has communicated regularly with 91 local and municipal permit offices across the state. An informational letter and copies of the registration packets were provided to the offices for distribution to builders in need of registration. The Unit continues to send out regular printed copies of the lists of registered builders to local permit offices and communicates with them on a regular basis.

V. EVALUATING CONSUMER AND BUILDER DISPUTE RESOLUTION

The Home Builder Registration Act requires that the Unit “collect and maintain information on the resolution of consumer complaints involving new home builders.” HBRA §4.5-202(d). Although there is no central repository of information about consumer/builder disputes, consumer complaints filed with the Mediation Unit of the Consumer Protection Division are illustrative. Comparison of consumer complaints filed in past years with the complaints filed since the inception of the HBRA in January 1, 2001 shows that the number of consumer complaints has remained relatively steady, but the number of disputes successfully resolved through mediation has increased significantly.

Written consumer complaints filed with the Mediation Unit of the Consumer Protection Division about home builders has traditionally averaged about 200 complaints per year.⁴ In 2000 there were 237 complaints filed and by the end of 2001, more than 200 complaints will be filed.⁵

When a consumer complaint is filed with the Consumer Protection Division, a mediator from the Mediation Unit is assigned. The mediator contacts both the builder and consumer and assists them in resolving their dispute. A mediated agreement is possible only if both parties are willing to mediate and can reach mutually acceptable terms. A mediation is considered successful if it results in a mediation agreement.

The Home Builder Registration program has been in existence too short of a time to accurately assess whether builder registration and enforcement will have an effect on consumer/builder dispute resolution, although early data suggests it is having a positive effect in motivating voluntary mediation. In 1999 and 2000, before the Act was implemented, 43% and 47% of mediations were resolved through mediations in which mutual agreements were reached. This rate of agreements through mediation has climbed to 67% since January 1, 2001, when the Act was implemented.

⁴ Consumer also filed complaints against builders with the Montgomery County Office of Consumer Affairs (43 in 2000) and with the Howard County Office of Consumer Affairs (28 in 2000).

⁵ The number of consumer complaints projected for 2001 is an extrapolation from actual complaints closed from January 1 through September 30, 2001.

VI. LAW ENFORCEMENT

The Home Builder Registration Act provides an enforcement mechanism with the objectives of (1) keeping unregistered builders from building in Maryland and (2) preventing registered builders who establish a bad track record of unresolved disputes or legal violations from continuing to build in Maryland.

To accomplish these objectives, the HBRA prohibits unregistered builders from building and authorizes the Unit to use civil administrative proceedings to seek a cease and desist orders and a civil penalty of up to \$1000 per day of unregistered practice. HBRA §§ 4.5-501 and 4.5-502. In addition, the HBRA provides that the Unit may deny registration to an applicant, reprimand an registrant, suspend or revoke a registration, or impose a civil penalty if the Unit determines that the applicant or registrant has engaged in any of the specified practices stated in HBRA 4.5-308.

The Unit has opened 29 investigations since the inception of the Act on January 1, 2001 through September 30, 2001. These investigations have involved allegations of violation of the HBRA, other building related laws, or the Consumer Protection Act. Nineteen of these investigations have now been closed and ten remain under continuing investigation. The Unit receives information from many sources, including consumers, other builders, and permit offices about builders who were alleged to be building without being registered. Subpoenas for depositions and documents were issued in several cases. The results of these investigations are summarized as follows:

! The Unit sought and obtained a cease and desist order against a home builder who is not registered, but who took \$31,000 from a Prince George's County consumer to build a custom home. The builder never began construction, did not place the deposit in an escrow account, and did not refund the deposit, as required by law. The cease and desist order prohibits the builder from building in Maryland until registered. A hearing is set for December 7, 2001 to determine the amount of restitution and civil penalties due for the harm to the consumer and for acting as a builder without being registered.

! One investigation involved a builder who had initiated a fee it represented to consumers as a "Maryland Regulatory Fee" of one percent of the price of the house. The Unit alleged that this phrase misrepresented to consumers that the charge was a mandatory fee imposed by the State of Maryland rather than an additional charge imposed by the builder. The builder and the Unit

entered into a settlement agreement under which the description of the charge was accurately disclosed as a builder charge that was not required by law. Because no consumers had been harmed as a result of the misrepresentation, the builder was not required to pay restitution.

! Most of the investigations involved questions as to whether the builder was properly registered. Because the program was new and some builders had still not heard of the registration requirement, the program's initial objective was to register the builder rather than penalize the builder for not being registered, while also addressing any underlying consumer complaints. Investigations were closed where (1) the builder registered promptly or was already registered, or (2) the builder was not required to register because the builder was not engaging in home building since January 1, 2001 or were exempted because the builder was building homes only in Montgomery County.

VII. REGISTRATION FEES ISSUE

An issue that has been of concern during and since the passage of the Act has been the amount and method of charging builders to register and thus fund the administration and enforcement of the Act. The Act provides that the Division establish by regulation a fee schedule that may not exceed \$600 in a two-year registration period. The fees are paid to a special fund – the Home Builder Registration Fund – which is used solely to fund the direct and indirect costs of the Home Builder Registration Unit. HBRA §4.5-203, §4.5-303, §4.5-305. In part because the costs of the program were unknown at the inception of the program, the Division by regulation established an application/renewal fee of \$600 for a two-year registration. The Division's costs for the Home Builder Registration Unit include salary, benefits, and administrative costs for a four-person unit; production and distribution of the consumer education pamphlet; continued maintenance of the website and data systems; and perhaps most importantly, enforcement costs. The cost of law enforcement includes not just attorney and investigative resources, but expert witness fees, depositions, and other litigation related expenses.

The fee structure is particularly relevant given the profile of Maryland's builders presented in this Annual Report. First, we now know that there are many more builders in Maryland than anyone was able to predict when the legislation was passed. Second, we now have concrete knowledge that many of builders are small companies that construct only a handful of houses per year, whereas a small number of large companies construct a large percentage of the houses each year.

Under the present fee structure, a builder who builds 5 houses every year is paying \$60 (60 dollars) per house for HBRA registration fees, whereas a builder who builds 500 houses per year is paying \$0.60 (60 cents) per house for registration. Since all builders, large and small, pass their costs on to consumers, it is also true that the consumer who buys from the large builder, in the example here, is paying 60 cents for the State's protection afforded by this program, whereas the buyer from a small builder is paying 60 dollars for the same protection.

Methods of assessing graduated fees based on number of houses built – rather than a flat fee per registrant – were considered and rejected when the Act was first passed, in part because they are difficult to apply or enforce. For example, setting the fee based on the number of houses a builder built last year is not fair to the builder who did well last year but is building fewer houses this year, and it would undercharge the LLC who did not build any houses last year but will build an entire subdivision next year. The same issues would arise with any fee based on predicted future building. Trying to determine and enforce such fee calculations would be difficult, if not impossible, and would require additional staffing to investigate the

claims made on each application.

The only practical way to charge a fee based on housing production is to tie it to the one act that every builder must take – obtaining the building permit. The General Assembly may want to consider addressing the inequity of the current fee structure by restructuring the Act to provide that builders would be charged a fee for every housing permit they obtain. The builder would pay the HBRA fee, say \$25, to the local permit office at the time the builder pays for the permit. The local permit office would collect the HBRA fee along with its other customary charges. The local permit office would then forward the HBRA fees it collected to the Home Builder Registration Unit on a quarterly basis, but would retain a small percentage as compensation for collecting and transferring this fee.

The net effect of this method would result in substantially reduced fees for builders who build few houses. For example, if the fee for the Home Builder Registration Act were set at \$25 per permit, the builder who builds five houses per year, or ten houses in a two year registration period, would pay \$250 in fees rather than the current \$600 flat fee.

If the General Assembly is interested in pursuing this idea, the Division is willing to explore the concept with the local permit offices.