

Department of Legislative Services
Maryland General Assembly
2011 Session

FISCAL AND POLICY NOTE

Revised

House Bill 362

(Chair, Economic Matters Committee)

Economic Matters

Education, Health, and Environmental Affairs

**Maryland Home Improvement Commission - Sunset Extension and Program
Evaluation**

This bill extends the termination date of the Maryland Home Improvement Commission by nearly 10 years – from October 1, 2012, to July 1, 2022 – and requires evaluation of the commission by July 1, 2021. The bill changes various statutory provisions related to the regulation of the home improvement industry in the State. The bill includes a related reporting requirement.

The bill takes effect July 1, 2011.

Fiscal Summary

State Effect: General fund revenues and expenditures for the commission are maintained beyond FY 2013. The FY 2012 budget includes \$1,888,883 for commission operations. General fund revenues increase by an estimated \$282,500 annually beginning in FY 2012 due to an increase in the commission's licensing fees. General fund and nonbudgeted fund revenues may also increase beginning in FY 2013 due to fine revenue collected through the commission's civil citation program authorized by the bill. General fund expenditures increase beginning in FY 2012 to develop and then implement the civil citation program and, on a one-time basis, in FY 2012 for computer modifications; thus, general fund expenditures increase by a total of \$15,000 in FY 2012. Nonbudgeted expenditures increase by an amount commensurate with nonbudgeted revenues to obtain expert witnesses in Guaranty Fund cases.

(in dollars)	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016
GF Revenue	\$282,500	\$282,500	\$282,500	\$282,500	\$282,500
NonBud Rev.	-	-	-	-	-
GF Expenditure	\$15,000	\$7,000	\$7,000	\$7,000	\$7,000
NonBud Exp.	-	-	-	-	-
Net Effect	\$267,500	\$275,500	\$275,500	\$275,500	\$275,500

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Bill Summary/Current Law:

Civil Citation Authority

The bill gives the commission the authority to issue civil citations to individuals who fail to comply with State home improvement laws or regulations. The commission may establish, by regulation, a schedule of violations and associated fines to identify the circumstances under which a civil citation may be issued. One-half of the fine revenue collected through the commission's civil citation program is deposited into the general fund of the State, and one-half of such revenue must be deposited into a separate account within the Home Improvement Guaranty Fund and earmarked for expenses related to the use of an expert witness to resolve a disputed Home Improvement Guaranty Fund claim between a homeowner and a contractor licensed by the commission.

Licensing Fee Increase

The bill increases initial and renewal licensing fees by \$25 each for contractors, subcontractors, and salespersons – the three types of licenses issued by the commission; currently, fees for each type of license are \$225, \$125, and \$75, respectively. The bill also creates a \$20 processing fee for all initial applications. The commission's licensing fees have not been raised since 1991.

Home Improvement Contract Requirements

In addition to the current statutory requirements for home improvement contracts, the bill requires contractors to include a notice on all home improvement contracts that (1) specifies that consumer protections are available through the commission; and (2) advises the consumer of the right to purchase a performance bond for additional protection against actual loss caused by a home improvement contractor. The commission must establish, by regulation, specific language for the notice that is required by the bill. In addition, the bill requires all home improvement contracts to display the commission's website address and the contractor's phone number.

Website Requirements

The bill requires the commission to publish, on its website, consumer education materials that describe the protections available through the commission, including the availability of compensation from the Guaranty Fund. The bill also requires the commission to develop a searchable website that includes a listing of licensed contractors and information relating to any final disciplinary action taken by the commission against a licensee.

Home Improvement Guaranty Fund – Reporting of Low Balances

The bill requires the commission to submit a report to specified committees of the General Assembly in the event that the balance of the Home Improvement Guaranty Fund is projected to fall below \$250,000. The commission must report to the General Assembly within 30 days of any such projection and detail actions it is taking to restore the balance of the fund to a sustainable level.

Criminal Penalties for Unlicensed Practice

For a first offense, criminal penalties for unlicensed practice are less severe for practicing as an unlicensed home improvement contractor, subcontractor, or salesperson than the penalties for other violations of the Maryland Home Improvement Law. Either violation may result in a fine of up to \$1,000. However, unlicensed practitioners are subject to 30 days imprisonment for a first offense; licensees who violate the Maryland Home Improvement Law are subject to imprisonment for up to six months. The bill increases the maximum time an individual may be imprisoned for acting without a license to make the penalties consistent.

Mold Remediation Services – Delayed Implementation of Licensing Requirements

Chapter 537 of 2008 required firms or companies that offer mold remediation services to hold a license issued by the commission by June 1, 2010. The bill extends the implementation of that requirement to July 1, 2013. Accordingly, the mold remediation licensing program's evaluation and termination dates are delayed until July 1, 2018, and July 1, 2019, respectively.

Required Reports

The bill requires, by October 1, 2012, that the commission report to specified committees of the General Assembly. The report must include:

- a strategy for the implementation of multiple licensing levels for contractors;

- a summary of efforts taken to reduce the investigation and processing times for claims referred to the Office of Administrative Hearings (OAH);
- an analysis of the advisability of the institution of a performance bond requirement for all licensees and, if advisable, in what amounts and triggered by what contract price;
- a plan for facilitating better communication between licensees and consumers relating to contract performance completion dates;
- data regarding the number of Guaranty Fund claims settled through mediation; and
- any changes in the number of Guaranty Fund claims filed and any changes in the average time to resolve a claim.

Background:

Maryland Program Evaluation Act

The Maryland Home Improvement Commission is 1 of approximately 70 regulatory entities and activities currently subject to periodic evaluation under the Maryland Program Evaluation Act. The Act establishes a process better known as “sunset review” as most entities evaluated are also subject to termination, including the commission, which is scheduled to terminate October 1, 2012. During the 2010 interim, the Department of Legislative Services (DLS) conducted a full evaluation of the commission under the Act. The bill primarily embodies the statutory recommendations developed by DLS during the evaluation.

Commission Is Supported by General Funds

The commission is funded by general fund appropriations. The commission’s primary revenue source is fees paid by individuals obtaining a license or renewing an existing license. Over the last five fiscal years, the commission has operated with a funding gap averaging about \$1 million annually. In fiscal 2010, the commission’s funding gap increased to nearly \$1.8 million. The primary factor contributing to the gap between revenues and expenditures is the assessment the commission pays to OAH to adjudicate contested Guaranty Fund cases. The commission’s OAH assessment in fiscal 2010 was about \$1.7 million. Due to a change in how OAH calculates its costs, the commission’s fiscal 2011 OAH assessment is projected to be about \$324,000 – a nearly \$1.4 million decrease. DLS advises that OAH will continue to assess the commission at the lower rate in future years. **Exhibit 1** displays the commission’s projected revenues and expenditures for fiscal 2011 and 2012. As depicted in Exhibit 1, the commission’s projected two-year funding gap is about \$565,000.

Exhibit 1
Projected Commission Revenues and Expenditures
Fiscal 2011 and 2012
(\$ in Thousands)

	<u>FY 2011</u>	<u>FY 2012</u>
Funding Gap	(\$194)	(\$371)
Total Revenues	2,100	1,950
Total Costs	2,294	2,321

Source: Department of Labor, Licensing, and Regulation; Department of Legislative Services

Commission Regulates Nearly 20,000 Licensees

The commission issues licenses on a staggered, biennial basis. The total number of licensees increased gradually between fiscal 2006 and 2010 from about 17,300 to about 19,700. Roughly 80% of the licenses issued by the commission are for a contractor's license. The growth in the number of licensees slowed between fiscal 2009 and 2010, likely due to the economic recession. The overall increase in the number of licensees in recent years may be attributed, in part, to the commission's public awareness efforts that encourage unlicensed practitioners to become licensed and inform consumers of home improvement scams and the benefits of hiring a licensed contractor.

The Guaranty Fund: Restitution for a Homeowner's Loss

The Home Improvement Guaranty Fund was established to compensate a homeowner for the "actual loss" created by a licensed home improvement contractor. Losses due to actions of unlicensed individuals are not eligible for restitution from the Guaranty Fund. A homeowner may receive up to \$20,000 in compensation from the Guaranty Fund per claim. If the total amount of awards on behalf of one contractor exceeds \$100,000, then the fund limits the total awards to \$100,000.

The Guaranty Fund is maintained through assessments charged to licensed home improvement contractors at the time of their original licensure and when they renew their licenses. (Subcontractors and salespersons do not pay the assessment.) Currently, new licensees pay \$100; renewal licensees pay \$150 every two years. In addition, the commission may assess each contractor up to \$150 in a calendar year if the fund balance is likely to drop below the statutory minimum of \$250,000.

Home Improvement Guaranty Fund Balance Declining

The total amount of awards paid from the Home Improvement Guaranty Fund in fiscal 2010 was approximately \$1.74 million, which is about \$560,000 higher than the \$1.18 million paid out in fiscal 2009. The commission advises that the increase in the amount of awards paid out of the fund can be attributed to several factors, including (1) the fact that the economic recession has resulted in many contractors going out of business and abandoning projects; and (2) the increase, in 2008, in the maximum amount of a Guaranty Fund award from \$15,000 to \$20,000.

As of June 2010, the balance of the Guaranty Fund was \$620,356, which is the lowest fund balance in recent years. The decline in the fund's balance cannot be attributed solely to an increase in awards from the fund. The commission tries to keep the fund stable and solvent, while avoiding an unnecessarily high assessment on licensed contractors. In fiscal 2006, with the balance above \$2 million, the commission lowered the assessment on renewal licensees from \$100 to \$75 every two years. In May 2010, with the balance of the fund declining, the commission doubled the assessment to \$150 for renewal licensees.

Complaint Volume Has Decreased – Resolution of Complaints and Claims Is Slow

The number of complaints received by the commission decreased from about 2,900 in fiscal 2007 to about 1,600 in fiscal 2010. Nevertheless, the resolution of complaints, and – in particular – Guaranty Fund claims is slow. Many Guaranty Fund claims filed by a homeowner are disputed by the contractor accused of wrongdoing. The process of resolving a disputed Guaranty Fund case that must be adjudicated at OAH takes about two years from when the claim is filed with the commission. It typically takes about 18 months from when a claim is received by the commission until it is referred to OAH for an administrative hearing. In total, a commission case can take 7 to 10 months to move through the OAH process. Once a recommended decision is issued by the administrative law judge, either party can appeal the decision, which further delays resolution of the claim.

Cost containment measures have reduced funding for legal services allocated to the Division of Occupational and Professional Licensing, which has in turn limited the number of Guaranty Fund cases that can be forwarded to OAH for adjudication. Due to limited legal resources, the commission can only refer about five cases per week to OAH; as of June 2010, 187 cases were waiting to be forwarded to OAH. At this rate, a commission case that is ready for OAH review is delayed 30 to 40 weeks before being referred to OAH for a hearing. This bottleneck has significantly increased the time it takes for homeowners to receive restitution from the Guaranty Fund.

Commission Aims to Resolve Disputed Guaranty Fund Claims through Mediation

The commission has partnered with the Mediation and Conflict Resolution Office of Maryland to assist in handling Guaranty Fund claims. The commission believes that a significant number of Guaranty Fund claims could be resolved through alternative dispute resolution. The commission received a \$50,000 grant that it may use to mediate 100 to 150 claims within the next year in an effort to reduce the backlog of cases awaiting adjudication at OAH.

Lack of Funding for Expert Witnesses Also Slows Claim Resolution

The commission no longer has funds to obtain expert witness reports and testimony. Expert witnesses provide credible and impartial analysis that can be critical in helping an administrative law judge decide a contested case. Further, because expert testimony is often valued by both parties in a dispute, more claims are settled before they are referred to OAH. Without expert witness testimony, a case is less likely to settle out of court. Thus, more cases end up at OAH when an expert report is not available. A defendant may also fight a case more fervently if he or she knows no expert witness is involved.

The Department of Labor, Licensing, and Regulation (DLLR) advises that about \$75,000 per year was available for expert witnesses during the 1990s; the allocation for this purpose has been eliminated in recent years. DLLR advises that the average expert witness charges about \$150 to \$200 per hour and that an average case would require between 5 and 15 billable hours, resulting in an average cost ranging from \$750 to \$3,000 per case.

Tiered Licensing

Home improvement projects range in size and complexity. However, nothing in law limits the size of a project that a contractor may undertake. Thus, a contractor with limited experience may undertake a major project regardless of whether or not the contractor is properly experienced, equipped, and capitalized to complete such a project. A tiered licensing system, similar to a system used in Virginia, is one approach for reducing the likelihood that contractors engage in projects they may not be able to complete by imposing limits on the size of contracts that new or inexperienced contractors are allowed to accept. A tiered structure allows a contractor to perform work that is within the contractor's financial means. The tiered structures used in other states typically involve three tiers.

State Revenues: The bill increases fees for each license type by \$25; the increase applies to both new and renewal licenses. The bill also creates a \$20 processing fee for all new licenses. **Exhibit 2** displays an estimate of the additional annual revenue

generated by the proposed changes to the commission's fee schedule, based on the average number of licenses issued and renewed between fiscal 2005 and 2010.

Exhibit 2
Estimated Annual Revenue Resulting from Proposed Fee Increase

<u>Licenses</u>		<u>Net Increase in Fees</u>	<u>Estimated Revenue</u>
New	2,000	\$45	\$90,000
Renewal	7,700	\$25	\$192,500
Total Licenses Issued	9,700		\$282,500

Source: Department of Legislative Services; Department of Labor, Licensing, and Regulation

As depicted in Exhibit 2, general fund revenues increase by an estimated \$282,500 annually due to the bill, which assumes no increase in the number of licensees over time. DLS advises that this increase approximates the commission's projected \$565,000 two-year funding gap.

Under the bill, the commission has authority to issue civil citations to individuals who fail to comply with State home improvement laws or regulations. DLLR advises that the civil citation program will not be in place until fiscal 2013 because regulations must be drafted to establish a citation infrastructure for the issuance of citations and collection of payments. Once the program is operational, DLLR estimates that the commission may issue about 500 civil citations annually. DLS advises that the amount of fine revenue received cannot be reliably estimated; however, *for illustrative purposes only*, assuming an average fine of \$100, revenues could increase by \$50,000 annually beginning in fiscal 2013. The bill specifies that this revenue must be deposited evenly between the State's general fund and a newly created account, managed by the commission, to be used for expenditures related to expert witness testimony in cases where such testimony is deemed necessary by the commission. Therefore, beginning in fiscal 2013 general fund revenues and nonbudgeted revenues to the commission increase due to the disposition of fine revenues from the civil citation program.

State Expenditures: General fund expenditures increase minimally beginning in fiscal 2012 due to the bill. DLLR advises that computer modification and programming costs increase by \$5,000 in fiscal 2012 to implement the commission's civil citation program. Annually thereafter, general fund expenditures increase by roughly \$7,000 for printing and postage and communication expenses related to the ongoing operation of the civil citation program.

Computer modifications are also needed to develop and implement a searchable website whereby information is displayed regarding disciplinary action taken by the commission against a licensee. Thus, general fund expenditures further increase, on a one-time basis, by as much as \$10,000 in fiscal 2012 to modify the commission's website.

Nonbudgeted expenditures also increase due to the bill. The bill specifies that one-half of the fine revenue generated due to the issuance of civil fines must be deposited into a newly created account to be used by the commission to acquire expert witness testimony in a contested Guaranty Fund case. DLS cannot estimate the amount of money that will be available for this purpose beginning in fiscal 2013; thus, the extent of the expenditures from this account also cannot be estimated. However, expenditures from this account cannot exceed the amount of funds dedicated for this purpose.

Additional Information

Prior Introductions: None.

Cross File: SB 236 (Chair, Education, Health, and Environmental Affairs Committee) - Education, Health, and Environmental Affairs.

Information Source(s): Department of Legislative Services

Fiscal Note History: First Reader - February 16, 2011
ncs/mcr Revised - House Third Reader - March 31, 2011
Revised - Enrolled Bill/Clarification - April 22, 2011

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