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## legal

## Building a Custom Home? Protect Yourself

BY DAVID B. APPLEFELD

HAVE YOU BEEN hired to build a custom home or are you thinking about entering into a contract to do so? If your answer is “yes,” then it is critical that you understand the Maryland Custom Home Protection Act (the “Act”) and the requirements which that Act may impose upon you.

The Act was enacted by the Maryland Legislature to protect homeowners from unscrupulous builders. In doing so, the Legislature placed a number of technical requirements on custom home builders. As a result, even builders with the best intentions can find themselves in violation of the Act and subject to civil and criminal penalties.

The first question you need to ask is, “does the Act apply to me?” If you are contracting to build a single-family home on land that is owned by the homeowner (not on land you own), and the value of your contract is \$20,000.00 or more, then Act applies to you.

Initially, the Act requires that your contract be in writing and contain the following minimum information: (1) the contract must state in bold type whether or not you are covered by a home warranty program; (2) the contract must identify the names of the primary subcontractors who will be working on the custom home; (3) the contract must include a separate draw schedule which is signed by both you and the homeowner; (4) a requirement that all changes be documented as “change orders,” which specify the nature of the change and the change, if any, in the contract price; (5) a requirement that you give the homeowner, within 30 days after each progress payment, a list of any subcontractors or suppliers who have provided more

than \$500 of goods or services to date, indicating which have been paid; and (6) lien releases from all subcontractors, suppliers or materialmen within a reasonable time after the final payment for the goods or services they have provided.

In addition, the Act requires that you make certain written disclosures to the homeowner. For example, you must certify that within the past three years, you have not been judged to have failed to comply with any provision of either the Act or the Maryland Consumer Protection Act. You must also certify that there are no unpaid, outstanding judgments against you. Finally, you are required to provide the homeowner with a specific, separate, written notice, advising about the risks under the mechanics’ lien laws.

Keeping in mind that Act is intended to protect the homeowner, it also places restrictions on your use of deposits and funds obtained from the homeowner. If you receive a deposit in excess of five percent of the contract price, you must either place that deposit into a segregated escrow account, obtain a bond, or establish a separate account for each deposit received from each customer. This requirement does not apply if the amount of the deposit is five percent of the contract price or less. The Act also controls when you are permitted to draw down a deposit in excess of five percent of the contract price. The use of these funds is limited to: (1) returning money to the homeowner; (2) paying documented claims for labor or materials in accordance with the written draw schedule; (3) paying the builder in the event the homeowner forfeits a sum under the contract; and (4) making final

payment to the builder upon the issuance of a use and occupancy permit. In order to avoid these requirements, many builders limit the deposit they collect to five percent of the contract price.

Regardless of the amount of the deposit you collect, the Act establishes a fiduciary or “trust” relationship between you and the homeowner with respect to all funds you receive, whether in the form of the deposit or draw payments. The Act requires that these funds be used for the benefit of the homeowner.

Finally, the Act imposes both civil and criminal penalties for violations. A builder who fails to comply with the Act, or commits any breach of the trust relationship created under the Act (such as the misuse of a deposit or a draw), is deemed to have committed an unfair or deceptive trade practice and is liable for civil damages. Depending upon the nature of the violation, personal liability may also be imposed.

This discussion does not cover all of the potential pitfalls a custom homebuilder may encounter. Rather, it is intended to be a general summary of common traps into which the unwary may wander. In light of the serious ramifications, it is important for any custom homebuilder to understand the Act and the requirements it imposes before beginning any project. ■

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Mr. Applefeld is a member of the Law Firm Adelberg, Rudow, Dorf & Hendler, LLC whose practice concentrates in the area of construction law. If you have questions about the topic of this article or other legal matters, Mr. Applefeld can be reached at 410-539-5195 or [dapplefeld@adelbergurdow.com](mailto:dapplefeld@adelbergurdow.com).