

CONSTRUCTION CLAIMS TASK FORCE

DRAFT

Regular Meeting Minutes

June 28, 2006

The Construction Claims Task Force met on Wednesday, June 28, 2006, in Room 260, Labor and Industry Building, 350 Winter Street NE, Salem, Oregon.

Members Present: David DeHarrport
Eric Grasberger
Elsie Jones
Steve Malany
Tom Skaar
Jim Vavrek

Members Absent: Jon Fahr
Bill Nesmith
Laura Schauer

Staff Present: Cory Streisinger, Director of Department of Consumer and Business Services
Mark Long, Administrator of Building Codes Division
Richard Baumann, Building Codes Division
Chris Huntington, Building Codes Division
David Dahl, Insurance Division
Kristie Patton, Construction Contractors Board
Gina Fox, Construction Contractors Board
Cece Newell, Insurance Division
Joel Ario, Administrator of Insurance Division
Cathy Dixon, Construction Contractors Board
Rick Blackwell, Building Codes Division
Ravi Mahajan, Building Codes Division
Michael Morter, Insurance Division

Guests Present:

Rep. Gordon Anderson
William T. Flynn
Joseph W Pitts
Jim Varco, HADD
Larry Boyd, Surplus Lines
Toni Chodrich, Oregon Mutual
Kenton Brine, PCI
David Golden, PCI
Kelly Ross, CBIC
Jutta Bonng, Oregon Mutual
Alan Seymour, ODOE
Steve Krieg, City of Woodburn
Tim Spencer Degussa Wall Systems
Jim Nicks, City of Portland
John Powell, Salem

Stuart Ramsing, OBOA
Rich Kingsley, Cammack/Kingsley
Christan Rataj, NAMIC
Mark Sektnan, AIG
Jeff Dean, ABC
Marc Johnson, Parsons, Farnell & Grein
Lana Butterfield, BCS
Kristen Leonard, OTLA
Brian Miller, Farmers Insurance
Jack Munro
Caroline O'Leary, Ankrom Moisan
Pat Dorney, CBIC
Amanda Rich, CBIC
Kirk Eland, CBIC
Tom Dymont, CBIC

Duncan Townsend, Detec Systems
Kelvin Dettwyler, Salem Insurance
Kay Erickson, DAS/BAM
Larry Peabody, ORA
Mary Bertram, Red Shield Insurance Co.

Janet Adkins, Legislative Committees
Ed Davis, Acordia
James Bela, Oregon EQ Awareness

Action Items

- Submit public notice for July 26, 2006 meeting.
- Compile status update on recommendations to date.
- Answer Task Force Questions

I. TASKFORCE BUSINESS

A. Call to Order:

Chair Eric Grasberger called the meeting to order at 1:35 p.m.

B. Approval of Agenda for June 28, 2006 Meeting and Order of Business:

MOTION: Eric Grasberger moved to approve the agenda for the June 28, 2006 meeting.

VOTE: 6-0, Ayes—Grasberger, DeHarrport, Jones, Malany, Skaar, and Vavrek.

MOTION APPROVED

C. Approval of May 24, 2006 Meeting Minutes:

Eric Grasberger asked that in the future with every set of minutes include a copy of the running list of proposals. Keep the synopsis with the minutes.

MOTION: Eric Grasberger moved to approve the May 24, 2006 minutes.

VOTE: 6-0, Ayes—Grasberger, DeHarrport, Jones, Malany, Skaar, and Vavrek.

MOTION APPROVED

D. Next Meeting Date:

MOTION: Eric Grasberger moved to approve the next meeting date of July 26, 2006, 1:30 p.m. to 5:00 p.m.

VOTE: 6-0, Ayes—Grasberger, DeHarrport, Jones, Malany, Skaar, and Vavrek.

MOTION APPROVED

Chair Grasberger discussed possible October meeting dates.

MOTION: Eric Grasberger moved to set the October meeting date for October 25, 2006 from 9:00 a.m. to 12:30 p.m.

VOTE: 6-0, Ayes—Grasberger, DeHarrport, Jones, Malany, Skaar, and Vavrek.

MOTION APPROVED

E. Project Update:

Mark Long, Building Codes Division, reported that this meeting begins Phase II insurance issues. **(Exhibit 1 and Exhibit 2)** Today's meeting will cover insurance regulation, an insurance overview, and an introduction to the insurance study report **(Exhibit 3)**. The July 26 meeting will be an insurance discussion, insurance industry panel presentation, the insurance study report, and time for task force work on Phase I proposals. The third meeting on August 23 will wrap up Phase II, include public comment, discussion and identification of Phase II recommendations for drafting, and task force work on Phase I proposals.

Included in your packet are two proposed concepts, including staff recommendations and the changes from previous meetings on Phase I construction defect issues. Proposal 1 "Clarifying Building Codes Requirements" **(Exhibit 4)** and Proposal 2 "Construction Contractors Board Enforcement Powers" **(Exhibit 5)**. Time permitting, we will address these today; if not, please submit your feedback to staff and we will incorporate your comments for the next meeting for discussion.

Eric Grasberger asked that since the recommendations and papers will be issued on a rolling basis, that staff create a schedule of when those papers will be reviewed and discussed by the task force.

II. NEW BUSINESS

Presentations were made by the following speakers:

- A. **Regulatory Environment:** Joel Ario, Administrator Insurance Division and Cece Newell, Property Casualty Technician, Insurance Division. **(Exhibit A, Exhibit B, and Exhibit C)**

Mr. Ario stated that the mission of the Insurance Division is "To administer the Insurance Code for the protection of the insurance-buying public while supporting a positive business climate." The Insurance Division ensures the financial soundness of insurers, the fair treatment of consumers, and the affordability and availability of insurance products. The Insurance Division licenses insurance companies, producers (agents), and consultants, enforces insurance laws, reviews insurance products and premium rates, and monitors insurer solvency.

In the spring of 2001, Insurance Division was receiving approximately 100 calls per month from construction contractors having problems obtaining liability insurance. Management looked at the issue and saw a pattern of residential contractors and those who worked on building envelopes having problems obtaining insurance. Insurance Division staff was able to guide them to agents and companies that could assist them in most cases. The division met with CCB to discuss the issues and work on resolutions to the crisis. The focus group that was created found that the problems were construction defects and escalating losses. In 2004, a market assistance plan (MAP) was created to help contractors find companies providing liability insurance and placed it on our Website. As a result of the MAP, the Insurance Division is currently receiving less than 20 calls per month from contractors reporting insurance problems.

Another issue is the increasing number of exclusions written into contractor insurance policies. The Insurance Division does have authority to ensure that exclusions are clearly stated and not misleading to the purchaser, but generally does not have the authority to prohibit exclusions unless there is a statute or rule that applies to the situation. Work-in-progress insurance is available to contractors, but not many are purchasing this type of coverage. Work-in-progress policies only cover the project during the construction work phase. The statistics from insurance companies' must show that the rates are justified and actuarially sound based on their costs. ISO (Insurance Services Office) data is most often used to set rates.

Chair Grasberger asked if premiums for liability insurance for contractors in Oregon are average based on what contractors pay in other states? Given Oregon's population, are the number of surplus lines average for the US and the amount of claims paid average? Staff will report back to the task force at the next meeting with information regarding these questions.

Mr. Ario reported that bonds cover poor workmanship, but do not cover resulting damage. The Insurance Division does not regulate warranties. Thirteen states have express warranty requirements where the contractors are required to cover the structure for a specified number of years. Only two states have third-party warranty requirements, New Jersey and Texas.

Task force members discussed changing statute to not allow exclusions in policies and perhaps require that liability insurance must cover completed operations coverage on residential work.

B. Overview of Insurance: David Golden, Property Casualty Insurers Association of America. **(Exhibit D)**

Mr. Golden described the different types of liability insurance. Basic general liability also called "manufacturers and contractors form" or M&C form" is a type of liability insurance that requires negligence to pay out on policy and is a premises and operations policy. Commercial general liability insurance also requires negligence to pay out on a policy and is a premises and operations policy, and typically includes completed operations coverage. These types of liability insurance do not cover warranties, breach of contract or failure to complete work. Most defects are warranty/breach in nature. Bonds cover completed work and workmanship issues.

First party warranties are contracts between a builder and an owner and commonly cover design, material, workmanship, and latent defects. Third party warranties are similar in coverage to first party warranties but are separate contracts. Mr. Golden urged task force members to be careful when talking about exclusions because there could be unintended consequences that could hurt the market. Insurance agents need to know who to sell a policy to and the type of work to be covered. Class rates are based on the type of business. Rates are driven by claim dollars paid out. Contractors need to improve quality to reduce exposure and reduce rates. Underwriting involves predicting the future and understanding the actual operations

and associated exposures and the claims experience. Use the right tool for the job at hand.

- C. Introduction to Insurance Study: William T. Flynn, Insurance Consultant and Joseph W. Pitts, Consulting Actuary from American Actuarial Consulting Group. William Flynn reported that he addressed the issues from the risk management perspective. He has spent time looking at construction defects and builder warranties. Warranty terms need to be clear. There are different types of warranties: implied, explicit, and third party. There are also two compensation type warranties where the state would: 1) act as a surety and require contractors to make repairs or 2) act as an insurance component with long tail coverage. The British Columbia model is a 2-5-10 warranty. Construction defect litigation claims are filed on the commercial general liability insurance policies. The litigation can affect the availability and affordability of insurance. Completed coverage payouts are 30 percent of losses are for non-construction defect losses, such as legal expenses, 50 percent are construction defects, and 20 percent are work in progress. The State of Texas mandates a warranty for new homes. Texas requires dispute resolution through the State Contractors Board, who act as mediator; and there is no enforcement authority on the decisions made. We conducted a data call of 23 insurance carriers in Oregon. Thirteen of those carriers responded to the call. We were able to use ten responses; although claim detail data was limited only four companies did some analysis by classification codes. We did see restrictions or no coverage in the admitted market for building envelope contractors (roofers, stucco installers, etc.). Eleven other states require warranties and one of the benefits is clarity of terms.

III. TASK FORCE DISCUSSION:

Task force members asked for research and answers on the following questions:

- What is the relationship between Oregon's statute of repose and warranties?
- What if Oregon disallowed exclusions on policies, what affect would that have on the availability and affordability of commercial general liability insurance?
- If warranties are filling the gap of things not covered by liability insurance, are we saving money?
- Is there any evidence to show if Oregon forced completed operations coverage what that would do to costs?
- Would we get the same consumer protection?
- Find a state close to Oregon that requires warranties and show the impact on general commercial liability insurance rates.
- What the cost of warranties are?

Task force members also requested that Insurance Division staff come and discuss their thoughts and input on the final report. Mark Long suggested inviting insurers, agents and contractors to come and comment as well.

Tom Skaar reported that Craig Smith, Administrator of CCB would like to see stronger language in proposal number two (**Exhibit 5**) giving a select number of CCB enforcement staff authority to issue criminal citations.

Chair Grasberger asked task force members to send their comments on proposals one and two (**Exhibit 4 and Exhibit 5**) via email before the next meeting to both Mark Long and Richard Baumann so there can be a discussion at the next meeting on the proposals.

IV. Public Comment

State Representative Gordon Anderson, District 3: Rep. Anderson was invited by the task force chair to testify before the task force and submitted written testimony (**Exhibit E**). Rep. Anderson shared his involvement with construction defect issues and his concerns regarding general liability insurance issues in Oregon.

Rep. Anderson made the following recommendations:

1. Separate commercial from residential complaints;
2. Require better training and continuing education for contractors;
3. Increase oversight on the job by architects, engineers, designers, and building inspectors;
4. Increase CCB enforcement; forbid contractors who continually violate code from licensure and they must register any relationship with another contractor;
5. Require contractors, not homeowners, to obtain all permits and bear responsibility;
- 6) Provide for severe penalties for building inspectors and/or building officials who pass work that does not meet code;
7. Establish a recovery fund from dues of \$100 per year from each active contractor:
 - a. Fund administration by non-government third-party overseen by the Portland Arbitration Association;
 - b. Funds can be used to fund enforcement by BCD;
 - c. Funds to be mainly used to help ameliorate homeowner losses;
 - d. Administration can adjust fees to meet needs;
 - e. Fund sunsets in ten years unless reauthorized.

V. ADJOURNMENT

Chair Grasberger adjourned the meeting 5:35 p.m.

Exhibits:

- 1 – CCTF Agenda/Timeline (1 page) – *Agenda item I-E*
- 2 – Phase II Insurance Issues (1 page) – *Agenda item I-E*
- 3 – DRAFT – Insurance study report (85 pages) – *Agenda item I-E*
- 4 – Building Code Amendments proposal (5 pages) – *Agenda item III*
- 5 – CCB Enforcement powers proposal (3 pages) – *Agenda item III*
- A – Insurance Division mission and purpose (1 page) – *Agenda item II-A*
- B – Insurance Division Overview of Insurance, Bonds and Warranties (1 page) – *Agenda item II-A*
- C – Insurance Division Insurance Terms Glossary (2 pages) – *Agenda item II-A*
- D – David Golden, PCI, Construction Liability: A National Perspective (11 pages) – *Agenda item II-B*
- E – Rep. Gordon Anderson's testimony – (3 pages) – *Agenda item IV*
- F – CBIC testimony (3 pages) – *Agenda item IV*