

CONSTRUCTION CLAIMS TASK FORCE
DRAFT
Regular Meeting Minutes
July 26, 2006

The Construction Claims Task Force met on Wednesday, July 26, 2006, in Room 260, Labor and Industry Building, 350 Winter Street NE, Salem, Oregon.

Members Present:

David DeHarrport	Jim Vavrek
Eric Grasberger	Jon Fahr
Elsie Jones	Bill Nesmith
Steve Malany	Laura Schauer
Tom Skaar	

Members Absent:

Staff Present:

Mark Long, Administrator of Building Codes Division
Richard Baumann, Building Codes Division
Chris Huntington, Building Codes Division
David Dahl, Insurance Division
Craig P. Smith, Construction Contractors Board
Gina Fox, Construction Contractors Board
Cece Newell, Insurance Division
Joel Ario, Insurance Division
Rick Blackwell, Building Codes Division
Michael Morter, Building Codes Division
Cathy Dixon, Construction Contractors Board
Ravi Mahajan, Building Codes Division

Guests Present:

Connie Rodriguez, CBIC	Christian Rataj, NAMIC
Ron Kozlowski, Towers Perrin	Jutta Beevny, Oregon Mutual Insurance
Jim Brown, Red Shield	Amanda Rich, CBIC
Tom Dymant, CBIC	Ron Manza, Stewart & Tunno & OPIA
Janet Adkins, Legislative Committees	James Bela, Oregon Earthquake Awareness
Steve Murren, State Farm	Joe Riter, Leonard Adams Co.
Scott Barrie, OHBA	Ron Bennett, Marsh
Gail Clark, Residential Warranty	Kelly Ross, CBIC
Lana Butterfield, BCS	Kirk Eland, CBIC
Toni Chodrick, Oregon Mutual	Bill Gorei, Red Shield
Ken Cochran, AFSCME	Steve Pinnell, Pinnell/Busch
Dave Johnson, 2-10 Home Buyers Warranty	Stephen Kafoury, ORA
Dick Hays, American Hallmark	Jim Nicks, City of Portland
Pat Dorney, CBIC	Steve Krieg, City of Woodburn
John McKee, CBIC	Greg Miller, AGC
Rob Walling, Pinnacle	John Powell, Insurers
Brian Doherty, CBIC	Brian Miller, Farmers
Pamela Love, JKS	Jack Munro

Action Items

- Submit public notice for August 23, 2006 meeting.
- Compile Phase II recommendations to date.
- Extend length of meeting to review Phase I proposals.

I. TASKFORCE BUSINESS**A. Call to Order:**

Chair Eric Grasberger called the meeting to order at 1:35 p.m. and reported that task force member Laura Schauer will arrive shortly.

B. Approval of Agenda for July 26, 2006 Meeting and Order of Business:

MOTION: Eric Grasberger moved to approve the agenda for the July 26, 2006 meeting.

VOTE: 8-0, Ayes—Grasberger, DeHarrport, Fahr, Jones, Malany, Nesmith, Skaar, and Vavrek.

MOTION APPROVED

C. Approval of June 28, 2006 Meeting Minutes:

MOTION: Eric Grasberger moved to approve the June 28, 2006 minutes.

VOTE: 8-0, Ayes—Grasberger, DeHarrport, Fahr, Jones, Malany, Nesmith, Skaar, and Vavrek.

MOTION APPROVED

D. Next Meeting Date:

MOTION: Eric Grasberger moved to approve the next meeting date of August 23 2006, 9:00 a.m. to 12:30 p.m.

VOTE: 8-0, Ayes—Grasberger, DeHarrport, Fahr, Jones, Malany, Nesmith, Skaar, and Vavrek.

MOTION APPROVED

E. Project Update:

Mark Long, Administrator, Building Codes Division, reported that this is the second meeting of Phase II. **(Exhibit 2)** This meeting will include a report on the insurance study, presentations from insurance industry experts and an opportunity for task force discussion. The third meeting in Phase II will be held on August 23rd and will include public comment as well as discussion and identification of Phase II recommendations for drafting. **(Exhibit 3)** The division has now completed a total of four proposals from Phase I for the task force to consider. The four proposals include clarifications to building codes requirements, enhancement to CCB enforcement powers, adoption of a recovery fund and increased consumer information. Time permitting, the task force will have an opportunity to discuss these proposals. The division plans to complete a total of six concept papers from Phase I. **(Exhibit 1)**

Joel Ario, Insurance Division, answered task force member questions from the June 28, 2006 meeting as follows:

1. *How do the number of contractors compare to other states?* Oregon has 36,000. Unfortunately we cannot get data from the other states. Only seven other states require contractors to have insurance and none of them compile the requested data.
2. *What about admitted carriers versus surplus lines?* In Oregon about 85 percent are admitted market carriers and 15 percent are surplus lines. We may be able to get data from other states. We are working with Surplus Lines Association, but it is difficult to get data.
3. *Premium and loss data by class.* We are looking for data and have asked ISO, which is the provider of this type of data to provide the information. They have not responded yet.
4. *What kind of exclusions are common in these policies?* There is material on this and it is incorporated into the insurance report.
5. *Could we get more data from Oregon specific companies on their losses?* The division has made some progress on this question. A couple more companies have responded.

II. NEW BUSINESS

Presentations were made by the following speakers:

- A. **Insurance Study Report:** William T. Flynn, Insurance Consultant and Joseph W. Pitts, Consulting Actuary from American Actuarial Consulting Group. (**Exhibit 9, Exhibit A and Exhibit B**).

William Flynn discussed the insurance report with task force members. Availability and affordability of liability insurance are directly related to the total cost of losses. General options are to reduce claim costs and reduce loss adjustment costs. There are two types of property damage insurance: direct protection (property insurance) and indirect protection (liability insurance). No property policies currently cover construction defects. In 1976 manufacturers and contractors (M & C) insurance was expanded to include completed operations. In 1986 commercial general liability insurance (CGL) was developed and it covers work-in-progress and completed operations.

Joseph Pitts reported that roughly one half of reported losses and loss expenses have been from construction defects. Legal costs represent 14.2 percent. The average premium per policy reported is \$1,700. Between 1998 and 2005 the average premium per policy has increased roughly 113 percent. The average premiums written for residential contractor classes range from \$400-\$2,400 per policy. Water intrusion causes 78 percent of the losses. Most defects can be traced to the building envelope. Some insurers are no longer covering roofers, water proofers, and siding installers. Some assumptions are that new home starts average 37,000 per year. The average new home value is \$205,000.

Task force members discussed that the data is might be skewed by small contractors with low premiums and do not reflect what they are seeing and hearing from contractors. Task force members also felt that the average cost of a new home was much higher than \$205,000.

William Flynn discussed alternative coverage mechanisms: warranty and wrap policies. Mandated minimum warranty requirements or mandated third-party warranty insurance. Only one state requires third-party warranties. He discussed cost comparisons with task force members. Typically warranties only cover the construction defect and not the resulting damage.

- B. Insurance Producers (Agents) Perspective: Ron Bennett, March USA Inc. (**Exhibit C**), reported that GL wrap-up policies are viewed as catastrophe coverage. Premiums are paid upfront for ten years of coverage. He doesn't see wrap-up policies being a viable option for single-family residential or small commercial contractors because it is not cost effective. He estimates that there are 25 to 50 wrap-up policies written in Oregon. There are only 250 to 300 wrap-up policies written nationwide and the policies are too new to know if claims will be covered by premiums charged. There is no single solution to fit all. Some alternative products are captives and risk retention groups. The State of Texas formed legislation aimed at addressing, mitigating and providing warranty coverage for certain types of claims. The State of Florida reduced its statute of repose from 15 years to 10 years.
- C. Insurance Companies Perspective: Dick Hays, Hallmark General Agency and Ken Buggy, Residential Warranty Corporation.

Dick Hays reported that the insurance crisis is not new. (**Exhibit D**) Good contractors need to be rewarded with lower rates. Three companies in Oregon insure most of the 42,000 licensed contractors. Homebuyers need to be given a list of maintenance items and a packet of information when they purchase a home that is signed by both the contractor and the homebuyer. The maintenance packet should layout when to notify the contractor. Warranty policies need to be part of the fix to the insurance problem. Another suggested fix is perhaps having contractors write a maintenance policy to be given to homeowners. He sees new companies moving back into Oregon to offer liability insurance. He likes two task force proposals, enhancing CCB's enforcement power and providing more funding for investigations. He would like to see more training prior to licensure with CCB and continuing education. Education is very important. He would like to see someone set up a maintenance group.

Ken Buggy reported that he would like to see a warranty program designed to use best practices. (**Exhibit E and Exhibit F**) Currently no one covers construction defects, a warranty program could help. Contractors become a member of RWC's risk retention group warranty group when they sign with them. His company screens contractors prior to them entering the program to ensure the contractor's financial soundness. All the parties have a duty to each other in the program. Homeowners have a duty to maintain their home, contractors have a duty to take care of problems, and the risk retention group agrees to act as a backup for problems. Membership has

it privileges with 1-2-10 policy coverage. Homeowners do not have to worry about the contractor going out of business because the warranty company will take care of problems for up to ten years. Warranty companies enforce duties of contractors. Sales volume plays a big factor in the cost of the warranty for a home; large companies get the best prices. If you take out the highs and the lows, the average cost per home for a warranty is \$170. The contractor buys the warranty to cover the home. Warranty policies are mandated and regulated in the State of New Jersey and require consequential damages coverage. The State of New Jersey will revoke a contractor's license if they do not perform the repair work required by the warranty. The State of New Jersey has 25 percent of the contractors in their pool. If a contractor is not able to get a warranty through the warranty companies, then the State of New Jersey sells them a warranty policy. We have a five-year remodeler's warranty program as well. Warranty programs prevent claims for insurers. The first two years the contractor is directly responsible for repairs, and for years three through ten the warranty program is also responsible.

III. TASK FORCE DISCUSSION:

A. Discussion of the Four Proposals:

MOTION: Tom Skaar moved to table the four proposals until the next meeting on August 23, 2006. The task force approved an extended meeting in August in order to discuss all of the proposals from Phase I.

VOTE: 9-0, Ayes—Grasberger, DeHarrport, Fahr, Jones, Malany, Nesmith, Schauer, Skaar, and Vavrek.

MOTION APPROVED

IV. ADJOURNMENT

Chair Grasberger adjourned the meeting 5:45 p.m.

Exhibits:

- 1 – Phase I Motions and Proposal Schedule (3 page) – *Agenda item I-E*
- 2 – CCTF Agenda/Timeline (1 page) – *Agenda item I-E*
- 3 – Phase II Insurance Issues (1 page) – *Agenda item I-E*
- 4 – DRAFT – Insurance study report (85 pages) – *Agenda item I-E*
- 5 – Building Code Amendments proposal (5 pages) – *Agenda item III*
- 6 – CCB Enforcement powers proposal (7 pages) – *Agenda item III*
- 7 – Recovery fund proposal (19 pages) – *Agenda item III*
- 8 – Consumer information proposal (3 pages) – *Agenda item III*
- 9 – Insurance study report – draft (149 pages) – *Agenda item II*
- A – American Actuarial Consulting Group presentation – (22 pages) – *Agenda item II*
- B – American Actuarial Consulting Group state statute summary – (1 page) – *Agenda item II*
- C – Ron Bennett, Marsh USA – presentation (9 pages) *Agenda item II*
- D – Dick Hays, Halmark General Agency – presentation (2 pages) *Agenda item II*
- E – Ken Buggy, Residential Warranty Corporation – presentation (2 pages) *Agenda item II*
- F – Ken Buggy, Residential Warranty Corporation – sample warranty (24 pages) *Agenda item II*
- G – Kelly Atwood, Contractors Insurance Services – testimony (9 pages) *Agenda item IV*
- D – Joe Riter, HBW – testimony (2 pages) – *Agenda item IV*