

SURPLUS LINE ASSOCIATION OF OREGON COMMENTS (SHOWN IN RED) TO:

**CONSTRUCTION CLAIMS TASK FORCE
INSURANCE ITEMS FOR CONSIDERATION
8-23-06**

At the request of the task force chairman, the Oregon Department of Consumer and Business Services has provided these proposals for consideration by the Task Force. These proposals are based on input received from presentations and discussions by industry professionals, Task Force members, and American Actuarial Consulting Group. The Department is presenting these for discussion purposes only, and most of them would require further analysis before either the Department or the Task Force could make a final decision on their feasibility and potential impact on the availability and affordability of insurance and potential impact on consumer protections.

1. WARRANTY PROGRAM

Proposal: A warranty program could be established that would allow for warranty coverage for targeted sections of the contractor market.

Discussion: The warranty program could provide a mechanism to address issues impacting targeted contractors such as new residential construction.

Most programs would have the builder maintain responsibility for the warranty for the first full year or two after occupancy of the dwelling. The program could be modeled after elements of the British Columbia model known as the 2/5/10 Program or the New Jersey model, both of which require a third party insurer to stand behind the warranty.

The warranty provider could cover a specific schedule of items and conditions. The liability of a builder or warranty provider is normally limited to the purchase price of the home or the fair market value of the home on its completion date. The scope of the warranty program might be aligned with the definition of residential structure in the state building code – that is, detached single family homes, duplexes, townhouses, rowhouses and residential structures three stories or less in height.

SLAOR supports this and also suggests that provision needs to be made for contractors to have equal access to all sources for their insurance. As long as their needed coverages are in short supply, contractors should be permitted equal access to the admitted and non-admitted markets which would require adoption of “export list” provisions as currently practiced in 16 other US jurisdictions. The export list would allow the insurance division to specify certain distressed coverages that could be written in the non-admitted market even though there might be an admitted market willing to write the coverage at a higher price. The division would add coverages to the export list when such coverages were in short supply and the division felt that the admitted market did not have sufficient interested insurers to assure a competitive admitted marketplace.

2. GENERAL LIABILITY COVERAGE TO INCLUDE COMPLETED OPERATIONS

Proposal: Depending on whether the Task Force proposes the warranty option, the insurance requirement for contractors under ORS 701.105 could be expanded to include coverage for completed operations.

Discussion: The Department of Justice was asked to interpret the statutory language under ORS 701.105 and determine whether the intent of the law would allow the required insurance to exclude completed operations coverage. Legal analysis concluded that “the law does not appear to impose” the requirement that completed operations be provided.

On several occasions during the course of the work by the Construction Claims Task Force this has been an issue of discussion. Submitted written testimony suggests that coverage should include completed operations that would extend for the entire period of the statute of repose.

The rationale for this proposal would be less compelling if the warranty is adopted since warranty and general liability coverage do overlap in some areas of property damage liability. However, completed operations general liability would also extend to certain areas such as bodily injury issues, which may not be covered under a warranty option.

The Task Force may want to limit the scope of the proposals for warranty and completed operations to the affected areas of the market.

SLAOR endorses adoption of this proposal – amending the licensing requirements but not trying to address the issue by amending the insurance statutes. Using the statutes to prohibit issuance of certain policies under certain circumstances would be cumbersome.

3. LOWER LIMITS ON WRAP PROJECTS

Proposal: Regulatory restrictions on wrap projects could be streamlined by lowering the project eligibility limit under ORS 737.602 to \$10 million to reflect the current liability claim environment.

Discussion: Currently, ORS 737.602 allows “wrap” coverage for construction projects when the aggregate value exceeds \$90 million. This statute also requires the project sponsor to show that the grouping will substantially improve accident prevention and claims handling. This statute further describes rating, auditing and deposit requirements. The qualifying project limit was determined in 1990 when construction defect claims, which often involve multiple claimants and multiple insurer expense costs, were a small portion of the general liability claim costs.

The proposed limit was selected to allow medium sized projects to benefit from the loss prevention and claim handling incentives provided under wrap projects. Testimony to the Task Force has indicated that “safety groups” are being used for projects in the \$10 million range. Allowing those projects to qualify as “wrap” projects would offer additional flexibility to include workers’ compensation.

The rating plan filed under ORS 737.602 could also be streamlined by removing the requirement for prior approval and allowing a file and use format to reduce regulatory barriers. Deposits could be eliminated or reduced. The requirement that the grouping demonstrate accident prevention and claims handling improvement could also be eliminated, since this has been demonstrated by prior filings.

Construction defect claims currently are at least 40-60% of the contractors total liability claim costs. Since legal expenses can comprise as much as half of the total construction defect loss and adjusting expense, any project or insurance mechanism that coordinates legal defense costs for construction defect claims is likely to streamline claim processing for the construction project and project contractors.

SLAOR endorses this broadening the market for wrap ups but, again, suggests adding a provision that contractors be allowed unlimited access to both the admitted and non-admitted markets through the use of an “export list” of coverages eligible for placement in the non-admitted market even when obtainable through the admitted market.

4. LOSS CONTROL DISCOUNTS

Proposal: Loss control discounts for contractors who adopt mandatory or voluntary best practices could be encouraged by streamlining the filing process and reducing any documentation requirements.

Discussion: Discussions and proposals stemming from Phase I of the Task Force's work may potentially reduce construction defect claims – and consequentially, contractor losses. Since construction defect claims can have up to a ten-year reporting period, the effect of these proposals may not be reflected in contractor loss experience for several years.

There is currently a model to mandate discounts in Auto Insurance. ORS 742.490 mandated discounts for drivers 55 years of age or older that participated in accident prevention courses approved by the Department of Transportation.

SLAOR is neutral on this issue but we would point out that loss control discounts are tricky – especially in a market composed of smaller accounts. To mandate precise loss control discounts would assume that the law makers somehow know the value of loss control procedures and how they might change over time. If such a “crystal ball” existed we wouldn't have a problem now.

5. AGENT DISCLOSURE OF MARKET SEARCH EFFORTS

Proposal: Agent duties could be clarified to ensure that contractors are provided reasonable opportunity to have their insurance placed in the admitted market before being offered surplus lines coverage or being told that no options are available.

Discussion: Agents working with any licensed contractor or contractor seeking new licensing could be required to present full disclosure of their marketing efforts when asked to write coverage or quote for insurance required by ORS 701.105. Information presented to the contractor might include: names of insurance carriers, names of brokers and the contact person at the brokers office, specific reasons for denial to quote coverage, specific rating and underwriting information presented in the quotation request and final outcome. Disclosure issues would necessarily be sensitive to privacy requirements.

Under current law ORS 735.410 requires a “diligent search” of the market before a risk can be placed with a surplus lines. The definition of “diligent search” could be amended to include the duty of an agent to advise the potential contractor client that there may be other alternatives to the coverage offered by his/her agency through outside sources and to identify those whenever possible.

The SLAOR believes an increase in the “diligent search” requirements is not needed. Surplus lines placements already require the retail insurance producer, the one who deals directly with the insured, to make a “diligent search” of the admitted market before placing the insurance and the producer must be ready at any time to disclose the confidential details of such search to the Insurance Division. This “diligent search” is only required if the producer is proposing placement in the non-admitted market. For the vast majority of placements, those in the admitted market, there is no requirement for any “diligent search” and related report of admitted market placement attempts. Creating a new report to be completed on admitted market placements and increasing the information needed on non-admitted placements would be time consuming and serve little useful purpose.

The state already operates a “Market Assistance Program” where interested contractors may find the names of insurers and insurance producers who offer contractor insurance. SLAOR and other associations offer this information and stand willing to assist in broadening the reach of such programs through volunteer staffing etc. if asked.

6. SPECIFIC DATA REPORTING

Proposal: Insurers could be required to report premium and loss information for contractors general liability insurance in a standardized format to the Oregon Insurance Division.

Discussion: There is no consistent publicly available information on construction contractors general liability premium and claim levels. As a result, some insurers were unable to report the requested information for use by the task force. In order to obtain data in a standard format and be able to compile a solid picture of the condition of the marketplace, including the extent to which Oregon premiums are dependent on regional or national specific data reporting could be required.

This would allow the Division to monitor progress in response to the work of the Construction Claim Task Force and to have an earlier indication of market difficulty if it should occur. Requested information could include written premiums, number of policies written, number of reported claims, paid losses and case reserves as of year end starting with 2007. The data could also be divided into premises operations and construction defect completed operations and non-construction defect completed operations claims. Timely reporting of this basic information may help insure that there is relevant information on contractor business.

Any reporting requirement should consider increased cost as well as the expected benefit the data may provide.

SLAOR takes no position on this issue other than to point out that this is a can of worms and unless the insurers are behind it and willing to comply it could backfire with insurers withdrawing from the market rather than incorporating IT changes to their entire claim systems to address the specific requirements of Oregon.