

From: Mark Wilson [<mailto:mwilson@frontierbonding.com>]
Sent: Monday, March 17, 2014 3:04 PM
To: Sen. Mike Dunleavy; Sen. Peter Micciche
Subject: SB 193

To the Members of the Alaska Senate Labor and commerce Committee

I am writing to offer testimony to be considered for passage of this bill.

I am President of Frontier Bonding Service, LLC. We are a Managing General Agent located in Seattle Washington. Our company specializes in providing access to surety markets for Alaska Insurance Agents. While I am not an Alaska resident, I do transact a great deal of business in your State. I have been active in the Alaska Insurance Industry for more than 25 years. One of the bonds we write frequently is the Alaska Contractors License Bond. Our company currently has over 1100 active contractor's license bond written in Alaska.

I have been following the bill closely since late February. My position is that the bill itself is beneficial but I believe that, as currently written, it could be improved. The Alaska contractor's license bond is classified by the surety industry as a blanket performance and payment bond. If multiple lawsuits are filed against a bond resulting in judgments then the bond amount is tendered to the court and the bond is apportioned to the claimants based on AS [08.18.081](#). Homeowners are fourth on the list. This priority only applies to situations where claims exceed the bond penalty. If a supplier files a claim for the full bond amount and it settles before a homeowner realizes there is a problem the bond has already been exhausted. In my experience, the majority of the claims that we see against the bond are payment claims from suppliers and performance and payment claims by other contractors. The last to file claims are consumers for breach of contract.

I spoke with an aide in senator Micciche's office about the bill who indicated that one of the main purposes of the bond and the increase is to afford protection to Alaska consumers who enter into contracts with licensed businesses and are harmed because the bond penalty was exhausted by other claims. By simply increasing the bond amount the consumer receives no more protection than they currently have. In my experience, the suppliers and other contractors who are more sophisticated in the process of filing and perfecting claims against the bond have a distinct advantage over the consumer. By statute their claims take priority over the consumer. In many cases the bond penalty is exhausted before the consumer is even aware that they have an issue for which the bond would provide relief or from which they could collect. I also believe that the suppliers and other contractors have other means at their disposal to mitigate their

risk. A supplier can choose to grant credit to a customer or not and can ask that customer to sign a personal guarantee. A contractor working with a subcontractor can require that subcontractor to provide a performance and payment bond for the specific contract, can joint check that subcontractor, can require certified payrolls and can get partial lien releases as work progresses. The owner who is entering into a contract for commercial construction can use most of the same tools with their general contractor that the general can use with their subcontractors. Most of these procedures are not known to a family that wants to remodel their home.

Increasing the bond penalty creates a barrier to entry to smaller contractors or those who wish to start a business. Bond premiums are based on the bond penalty. This bill will increase the bond penalty by 100 to 150% for most contractors resulting in a similar increase in premiums. Over time, as sureties file new rates to react to the increase those figures would probably go down somewhat but, in my professional opinion, you would be looking at a 50% to 70% increase in premiums for the bonds. For larger well established contractors these bonds are relatively inexpensive but premiums for new contractors and those contractors that present a higher risk profile to the surety are currently paying as much as 18% for their bond. One of our sureties has both a 10% and an 18% filed rate for these bonds and we regularly write them at these premium levels. Doubling the bond penalty has a substantial financial impact to these small and emerging businesses. It raises the barrier to entry for new businesses and it may cause some currently licensed businesses to fail to qualify for the new bond amounts. If the barrier to entry is raised it increases the number of people who will contract without a license and cause harm to the consumers who will now have no bond protection.

A bond increase per se is not a bad thing but I think that it would be better structured if it included a provision to bifurcate the bond penalty by reserving the increase in the penalty for the benefit of consumers for work performed on their primary residence. If this were done it would allow the more sophisticated construction consumers (commercial owners, suppliers and other contractors) the same protections they now have and it would preserve a portion of the bond for those who may find out later that they have an issue and need the protection of the bond. Both Washington and Oregon statutes have provisions to this effect.

In Washington RCW 18.27.040(4) states:

“The surety upon the bond shall not be liable in an aggregate amount in excess of the amount named in the bond nor for any monetary penalty assessed pursuant to this chapter for an infraction. The liability of the surety shall not cumulate where the bond has been renewed, continued, reinstated, reissued or otherwise extended. The surety upon the bond may, upon notice to the department and the parties, tender to the clerk of the court having jurisdiction of the

action an amount equal to the claims thereunder or the amount of the bond less the amount of judgments, if any, previously satisfied therefrom and to the extent of such tender the surety upon the bond shall be exonerated but if the actions commenced and pending and provided to the department as required in subsection (3) of this section, at any one time exceed the amount of the bond then unimpaired, claims shall be satisfied from the bond in the following order:

- (a) Employee labor and claims of laborers, including employee benefits;
- (b) Claims for breach of contract by a party to the construction contract;
- (c) Registered or licensed subcontractors, material, and equipment;
- (d) Taxes and contributions due the state of Washington;
- (e) Any court costs, interest, and attorneys' fees plaintiff may be entitled to recover. The surety is not liable for any amount in excess of the penal limit of its bond.

A payment made by the surety in good faith exonerates the bond to the extent of any payment made by the surety.

(5) The total amount paid from a bond or deposit required of a general contractor by this section to claimants other than residential homeowners must not exceed one-half of the bond amount. The total amount paid from a bond or deposit required of a specialty contractor by this section to claimants other than residential homeowners must not exceed one-half of the bond amount or four thousand dollars, whichever is greater.” (emphasis added)

Oregon Statute ORS 701.153 states:

“701.153 Recording of order as lien; satisfaction of order against residential contractor. (1) If an order of the Construction Contractors Board determines a complaint against a residential contractor that was filed with the board prior to July 1, 2011, and the order becomes final by operation of law or on appeal and remains unpaid 10 days after the date the order becomes final, the complainant may file the order with the county clerk in any county of this state.

(2) Upon receipt of an order described in subsection (1) of this section, the clerk shall record the order in the County Clerk Lien Record. In addition to any other remedy provided by law, recording an order described in subsection (1) of this section in the County Clerk Lien Record pursuant to the provisions of this section has the effect provided for in ORS 205.125 and 205.126, and the order may be enforced as provided in ORS 205.125 and 205.126.

(3)(a) Payments from the surety bond of a residential contractor pursuant to a board determination under ORS 701.145 are satisfied in the following priority in any 90-day period:

(A) Board determinations as a result of complaints against a residential contractor by the owner of a residential or small commercial structure have payment priority to the full extent of the bond over all other types of complaints.

(B) If the determinations described in subparagraph (A) of this paragraph do not exhaust the bond, then amounts due under board determinations for all other types of residential or small commercial structure complaints filed with the board within that 90-day period may be paid from the bond, except that the total amount paid from any one bond to nonowner complainants may not exceed \$3,000. (emphasis added)

(b) A 90-day period begins on the date the first complaint is filed with the board. Subsequent 90-day periods begin on the date the first complaint is filed with the board after the close of the preceding 90-day period.

(4) If the total amount payable under determinations issued by the board for complaints against a residential contractor filed with the board within 90 days after the board receives notice of the first complaint against the contractor exceed the amount of the bond available for payment, subject to the priorities under this section, the board shall decide how payment of the determined amounts from the bond is to be apportioned.

(5) If the total amount payable under determinations issued by the board as a result of complaints that were filed with the board within 90 days after the board receives notice of the first complaint do not exceed the amount of the bond available for payment, those determinations have payment priority over amounts due under determinations resulting from subsequently filed complaints.

(6) The total amount paid from a residential contractor bond for costs and interest under all determinations issued by the board under ORS 701.145 may not exceed \$3,000. [2007 c.836 §10; 2007 c.836 §52; 2011 c.630 §50]”

Reserving the increase in the bond amount to consumers would also reduce the financial impact to contractors because the sureties would recognize that the increase in exposure will not increase their losses by an equal amount. In both Washington and Oregon the rate increases were much less on a percentage basis when the bonds were increased because of the reservation provisions contained in their statutes. As I stated before there are far more payment claims paid by sureties than performance claims.

I thank you for your time and consideration.

Mark M Wilson

President

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