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Alaska State Legislature
Senate Committee on Labor and Commerce

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Submitted electronically to: Senate.Labor.And.Commerce@akleg.gov

RE: SB 208, Contractors; Relating to Insurance - NAMIC's Written Testimony in Opposition

Dear Senator Costello, Chair; Senator Revak, Vice-Chair; and honorable committee members:

Thank you for affording the National Association of Mutual Insurance Companies (NAMIC) an opportunity to submit written testimony to the Senate Committee on Labor and Commerce for the public hearing on SB 208. NAMIC is the largest property/casualty insurance trade association in the country, with more than 1,400 member companies representing 40 percent of the total market. NAMIC supports regional and local mutual insurance companies on main streets across America and many of the country's largest national insurers. NAMIC member companies serve more than 170 million policyholders and write nearly $225 billion in annual premiums. NAMIC has 96 members who write property/casualty and workers' compensation insurance in the State of Alaska, which represents 41% of the insurance marketplace.

NAMIC appreciates what it understands to be the desired goal of SB 208 – namely, to protect consumers from improper, unprofessional, and unscrupulous contractor services. However, NAMIC is concerned that the proposed legislation will not meet the desired objectives. SB 208 does not appear to provide any meaningful legal protections to Alaska's consumers. Instead, the bill would create a host of costly legal and public policy problems that will only harm consumers, responsible contractors, and liability insurers.

On behalf of NAMIC's members, we respectfully submit the following comments *in opposition to* the proposed legislation:

A contractor's surety bond provides protections for Alaska consumers.

At the outset it is important to understand the critical difference between a surety bond and liability insurance. A surety bond is a three-party agreement involving the surety, the contractor, and the obligee (the party who receives the benefit of the bond, such as a homeowner). It is not put in place to protect the contractor; rather it assures the obligee (consumer) that the contractor's work will be adequate and complete. The terms of the bond are often dictated by the obligee. For example, the Alaska Department

of Commerce provides a surety bond form to satisfy the requirements of AS 08.18.071. Thus, the surety bond provides assurances to the obligee that the project will be performed and, when the contractor does not adequately perform, Alaska law allows the obligee to sue the contractor and/or the surety directly. (AS 08.18.081).

In contrast, liability insurance is a two-party contract between the contractor and the insurer. The typical commercial general liability policy (liability policy) ***only*** provides the contractor-policyholder with coverage for tort-based negligence claims, i.e. the insurance coverage is only for accidental damages caused by the contractor when it is providing professional services to the consumer. A liability policy does ***not*** provide coverage for "completed projects" and/or for shoddy/deficient professional services. For example, if a contractor improperly installed cabinets it contracted to install, the liability policy may not provide coverage because the claim arises from improper professional services provided by the contractor. On the other hand, if the contractor accidently damages a consumer's hardwood floors while installing kitchen cabinets, the liability policy may provide coverage because the damage was negligently caused by the contractor-policyholder but is unrelated to the completed project (installation of the cabinets). If a liability claim is made or a lawsuit is filed against the contractor-policyholder for damage to the hardwood floors, the liability insurer's duties to the contractor under the terms of the liability policy would be triggered. In contrast, the liability insurer would have no duties under the liability policy for claims arising from the contractors' improper professional services.

A direct action against the contractor's liability insurer may inadvertently allow the contractor to avoid responsibility for its conduct.

SB 208 would be counterproductive in that it would further incentivize an unresponsive contractor to not cooperate with the consumer. By failing to "acknowledge or act promptly" on a person's claim the contractor can trigger a lawsuit against the liability insurer, avoid a lawsuit, and ultimately evade personal responsibility for its conduct. Indeed, SB 208 seems to encourage contractors not to respond or work with their customers. The end result would be the consumer filing and litigating a lawsuit against the contractor's liability insurer. The consumer would be forced to fit the bill for what can be costly litigation that would not only address the contractor's alleged negligence or breach of contract but also the more complex insurance coverage issues. All the while, the unprofessional contractor who refused to engage would forgo any responsibility and simply continue with its operations as if nothing has happened. This scenario is not good for anyone but is especially bad for the innocent consumer – the individual this bill is designed to protect.

SB 208 seeks to address a problem that doesn't exist.

A direct action against the liability insurer serves no purpose because consumers can already easily sue and serve an unresponsive contractor. Alaska law allows a consumer to assert a civil claim seeking damages negligently caused by a contractor's poor workmanship and/or for a breach of the service contract. A civil complaint can be served through (1) a process server or certified mail, (2) a registered agent for service of process if the contractor is an entity, (3) publication in a newspaper, (5) posting on the court system website, or (6) email or other methods approved by the court. (Alaska Civil Rule 4). The contractor, after being served with the summons and complaint, would assuredly tender the lawsuit

to his insurer to cover the costs of defending the case and pay any indemnity owed for covered claims. NAMIC is not aware of any case where a consumer was not able to sue and serve the contractor or the contractor then did not tender the lawsuit to his insurer. Before deviating from longstanding policy against direct actions, the Legislature should ask why a consumer's lawsuit against the contractor is not sufficient.

SB 208 is inconsistent with well-established legal doctrine.

Allowing a cause of action directly against a liability insurer for the insured's conduct nullifies the longstanding policy prohibiting such actions. As noted above, contractor-policyholder purchases liability insurance to provide the contractor with indemnification for potential negligence and to provide a legal defense against liability claims. The contractual relationship does not include the consumer. SB 208 would appear to change that dynamic by creating a contractual duty between the contractor's liability insurer and the consumer. This proposed change to well established legal principals would create a potential conflict of interest between the contracting parties (contractor-policyholder and insurer) resulting in a legally flawed cause of action that insurers and the judicial system would have to resolve in order to protect long-standing and well-reasoned legal doctrine relating to liability.

SB 208's trigger for a direct action against a liability insurer is hopelessly vague.

The scope of and trigger for a direct action further demonstrates the flawed reasoning associated with SB 208. First, SB 208 does not limit the direct action to claims that are covered under the liability insurance policy. Nor does it limit the "civil action directly against a contractor's insurance" to the contractor's liability under the law. Second, the trigger for a direct action – failure to "acknowledge or act promptly" – leaves a lot of room for interpretation and grants a new right to sue the insurer if the contractor misses phone calls or emails "or other attempts by the person to contact the contractor." Likewise, requirement that the contractor failed to "attempt in good faith to resolve the person's claim" is open to interpretation based on the perspective of the party. What if the claimant takes an unreasonable position? Under SB 208 the unreasonable claimant would be able to sue the liability insurer directly simply because the contractor did not accept the claimant's unreasonable position.

SB 208 would be an unnecessary insurance rate cost-driver that could adversely impact small businesses.

Finally, SB 208 would create a number of insurance coverage underwriting issues, claims adjusting problems, and legal defense cost considerations that would have to be factored into insurance coverage rates for contractors. Consequently, the proposed legislation would be an insurance rate-cost driver that would provide consumers with little to no legal benefits. In fact, SB 208 would likely harm, not help, consumers because increased insurance policy costs for contractors will ultimately be passed on to the consumer via higher professional services prices and/or result in contractors going uninsured.

In sum, allowing a direct action against a liability insurer simply because contractor fails to respond to a claim made by a consumer – regardless of the substance or the validity of the claim – is dangerous. We respectfully suggest that before the Alaska Legislature embarks on that unique path, it first determines

that there truly is a need and consider the negative impact on consumers, contractors, and insurers. For these reasons, NAMIC respectfully requests that the members of the Senate Committee on Labor and Commerce VOTE NO on SB 208.

Thank you for your time and consideration. Please feel free to contact me at 303.907.0587 or at crataj@namic.org, if you would like to discuss NAMIC's written testimony.

Respectfully,

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