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470

p.m. with Senators Mulcahy and Pettyjohn present. Senator Rodey joined the Committee a few minutes later. Senator Sackett was absent.

The first bill up for consideration was SB 470--"An Act relating to insurance". Senator Mulcahy, prime sponsor for SB 470, stated this legislation was an in-depth rewrite of the statutes pertaining to surplus line insurance. The Division of Insurance has taken an active part in drafting SB 470, and therefore, Ken Moore, Director, is very qualified to comment on the merits of this legislation.

Number 014

Ken Moore, Director of the Division of Insurance, testified the basic intent of SB 470 is to provide a mechanism which protects the individual who purchases insurance in the non-admitted market. This legislation upgrades the Unauthorized (non-admitted) Insurers Act and the Surplus Lines Insurance Act to be in accord with the recently adopted models of the National Association of Insurance Commissioners.

SB 470 will give the Division of Insurance the ability to deal with the competence of the licensee and provide more meaningful protection for the public.

Number 098

Don Koch, Division of Insurance, informed the Committee that Ken Moore chaired the National Association of Insurance Commissioner during the adoption of the surplus line model bill. SB 470 is an "Alaskanized" version of the model bill.

Koch pointed out a definition change in Section 20, 9 (A) that indicated a vessel of 50 displacement tons or less was not included in the definition of "marine" and therefore not included in the requirements of SB 470.

Number 128

Chairman Eliason wondered what the displacement value of an average crab boat would be?

Number 151

Koch proposed two amendments for the Committee's consideration.

1) Page 18, line 23 - delete "within 30

days after" and add "upon".

2) Page 18, line 24 - delete "file with director" and add "maintain".

Number 170

Senator Mulcahy moved that the Committee unanimously accept the preceding amendment. The motion carried.

Number 180

Additional amendments were proposed by the Division of Insurance.

3) Page 23, lines 9-10 - remove the language beginning at "except" to the end of the sentence.

4) Page 31, line 23 - remove the words, "under regulations which he shall adopt".

5) Page 31, line 27 - following the word "used", add the phrase "or the filing and approval of which are in the director's opinion, not desirable or necessary for the protection of the public".

6) Page 31, line 27 - remove the words "and regulations".

7) Page 32, line 16 - add a new section to read: "Sec. 26. AS 21.33.015, AS 21.33.041, AS 21.33.045(b), AS 21.33.051, and, AS 21.33.068-21.33.300 are repealed".

Number 285

Henry George, President of the Surplus Line Brokers, urged support for SB 470 stressing this legislation is important to assure that the companies insuring Alaskans are solvent. The licensing regulation will make it possible for the Division of Insurance to monitor the non-admitted market. As the majority of the surplus line insurance is placed with out-of-state companies, it is extremely important that the Division of Insurance can track these companies.

SB 470 will allow (1) greater control of the non-admitted market; (2) licensing; (3) stronger participation of the Surplus Line Broker's Corporation. Mr. George testified that this close partnership will help deter present abuses in the system.

Number 332

In response to Chairman Eliason's question, George listed several abuses that currently

are found:

- (1) Surplus line brokers who are not properly licensed.
- (2) Brokers who place insurance without adequate capital back-up.
- (3) Brokers who slowly pay back claims due to cash flow problems.

SB 470 will allow surplus line brokers to work with the Division of Insurance to "clean up" the industry.

Number 347

Don Coates, Director of the Surplus Line Broker's Association, remarked he has been a surplus line broker for 15 years and as a broker is very supportive of SB 470. The current reporting system needs to be refined. Recently, four companies have declared bankruptcy and under the current statutes the companies were untouchable. If SB 470 had been in effect, the Division of Insurance would have had more control.

Number 366

Chairman Eliason initiated discussion among the Committee regarding the proposed amendments.

Number 374

Senator Mulcahy moved the Committee adopt the proposed amendments and asked for unanimous consent.

Number 381

Chairman Eliason directed the staff to have a Committee Substitute for SB 470 drafted.

Number 387

The next bill for consideration was SB 525-- "An Act relating to Unemployment Insurance." Jack Shay, Director, Division of Employment Security, began his testimony by outlining the various sections of this legislation.

Section 1 states that the training and building fund will not lapse until 30 days following the last day of each fiscal year.

Sections 2 and 3 adds a 21st class to the ranking of employers. This new class is to conform to suggested federal guidelines. In 1983, 163 employers would have been effected. This new class would create an \$18.00 increase for each employer in the new 21st class. In 1984 no employer would be

3AAC26.070. Standards for Prompt, Fair and Equitable Settlements Applicable to All Insurers. (a) An insurer or a person designated by the insurer to act on its behalf involved in the settlement of a claim must, within 15 days or the time frame specified in the insurance contract, after receiving a properly executed proof of loss or other evidence of loss acceptable to the

insurer from a first party claimant, advise the claimant of the acceptance or denial of the claim.

(b) A claim denial must be in writing and a copy or the capability of reproducing its text must be included in the claim file.---

(c) A claim denial based on a specific policy provision, condition or exclusion must include, in the written denial, reference to that specific provision, condition, or exclusion.

(d) If an insurer or a person designated by the insurer to act on its behalf needs more time to determine whether the claim of a first party claimant should be accepted or denied, notification must be given to the first party claimant within 15 working days after the receipt of the proof of loss giving the reason more time is needed. 45 days from the date of the initial notification and every 45 days thereafter while the investigation remains incomplete, written notification must be provided to the claimant stating the reason additional time is necessary to complete the investigation.

(e) An insurer or a person designated by the insurer to act on its behalf may not fail to settle a claim for first party claimant on the grounds that responsibility for payment should be assumed by others, except as may be expressly provided otherwise by the provisions of the insurance policy issued by the insurer.

(f) If negotiations for settlement of a claim continues directly with a claimant who is neither an attorney nor represented by an attorney to a point in time when the claimant's rights may be affected by a statute of limitations or a policy time limit, written notification must be provided to the claimant stating that the time limit may be expiring and may affect the claimant's rights. Notice must be given to first party claimants not less than 30 days before, and to third party claimants not less than 60 days before, the date on which the insurer believes the time limit may expire.

(g) A statement may not be made that indicates the rights of a third party claimant may be impaired if a form or release is not completed within a given period of time, unless the statement is given for the purpose of notifying the third party claimant of the provision of a relevant statute of limitation.

(h) If an insurer has a reasonable basis, supported by specific information available for inspection by the division of insurance, for suspecting that a first party claimant has fraudulently caused or contributed to the loss, the insurer is relieved from the requirements of this section. However, the insurer must, within a reasonable time for full investigation and after receipt of a properly executed proof of loss, advise the claimant of the acceptance or denial of the claim. (Off. / / , Reg. )

Authority: AS21.06.090  
AS21.36.125  
AS21.36.350

SB 470 TITLE & SPONSOR SUMMARY 16:41 6/04/84 PAGE 1 OF 3  
RENDED TITLE: CSSB 470(RLS)  
AN ACT RELATING TO INSURANCE

GENERAL DOLLARS: \$0 (F. NOTE)  
PRIME SPONSOR: MULCAHY.  
OTHER DOLLARS: \$0

CO-SPONSORS:

CURRENT STATUS: 5/30/84 TRANSM TO GOVERNOR

SB 470 SENATE ACTION 16:41 6/04/84 PAGE 2 OF 3  
LEGISLATIVE ACTION

DATE	SEQ	PAGE	LEGISLATIVE ACTION
02/13/84	01	2043	FIRST READING -- COMMITTEE REPORTS
03/23/84	02	2446	L&C -- CS04, NR01
03/23/84	03	2446	L&C F/NOTE EQUALS ZERO
05/03/84	04	2705	FIN -- L&C CS05
05/14/84	05	3078	RLS -- DP(AM)04, OTHER04 TAKEN UP IMMEDIATELY
05/14/84	06	3079	SECOND READING
05/14/84	07	3079	RLS CS ADOPTED BY UNAN CONSENT
05/14/84	08	3079	ADVANCED TO 3RD READING BY UNAN CONSENT
05/14/84	09	3079	THIRD READING
05/14/84	10	3080	PASSED BY DIV 20-00-00
05/30/84	19	3416	TRANSMITTED TO GOVERNOR

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SB 470 HOUSE ACTION 16:41 6/04/84 PAGE 3 OF 3  
LEGISLATIVE ACTION

DATE	SEQ	PAGE	LEGISLATIVE ACTION
05/15/84	11	3050	FIRST READING -- COMMITTEE REPORTS
05/23/84	12	3961	L&C -- DP03, NR02
05/28/84	13	4102	SECOND READING
05/28/84	14	4102	ADVANCED TO 3RD READING BY UNAN CONSENT
05/28/84	15	4102	THIRD READING
05/28/84	16	4103	PASSED BY DIV 32-00-08
05/28/84	17	4103	NOTICE OF RECONSIDERATION GIVEN
05/29/84	18	4139	PASSED ON RECONSIDERATION BY DIV 32-00-01

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# COMMITTEE REPORT

## SENATE

FURTHER:

FINANCE

2/13/64

Date 3/22/64

Mr. President

The Committee on LABOR & COMMERCE considered SB 470

relating to insurance.

and (a majority of the committee) (the committee) reports it back with the following recommendations:

- do pass
- do pass with attached amendment(s)
- replace with/or adopt CS for SB 470 (L+C)
- new title
- same title and recommends do pass
- and attached a "LETTER OF INTENT"  NEW FISCAL NOTE
- reports it back without recommendation
- recommends referral to \_\_\_\_\_ Committee

MEMBERS SIGNING DO PASS

[Signature]

[Signature]

[Signature]

[Signature]

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MEMBERS HAVING OTHER RECOMMENDATIONS

[Signature]

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\_\_\_\_\_

Chairman

Chairman recommendation

3/20/84

I have read CS 58470 (L+C) and it does resolve the questions we posed at the last hearing on the bill. The amendments we did request at that time have been incorporated in the substitute.

  
Don Bush  
Division of Insurance



STATE OF ALASKA 1984 LEGISLATIVE SESSION  
FISCAL NOTE

Revision Date: \_\_\_\_\_

REQUEST

Bill/Resolution No.: SB 470  
Title: Relating to Insurance

Sponsor: Mulcahy  
Requestor: Senate L&C  
Date of Request: 2/15/84

FISCAL DETAIL

Agency Affected: Dept. of Comm. & Econ. Dev.  
Program Category Affected: Public Protection  
BRU, Program or Subprogram(s) Affected: Insurance

EXPENDITURES/REVENUES: (Thousands of Dollars)

	FY 84	FY 85	FY 86	FY 87	FY 88	FY 89
OPERATING						
100 PERSONAL SERVICES						
200 TRAVEL						
300 CONTRACTUAL						
400 SUPPLIES						
500 EQUIPMENT						
600 LAND & STRUCTURES						
700 GRANTS, CLAIMS						
800 MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0
CAPITAL	0	0	0	0	0	0
REVENUE	0	0	0	0	0	0

FUNDING: (Thousands of Dollars)

GENERAL FUND						
FEDERAL FUNDS						
OTHER						
TOTAL						

POSITIONS:

FULL-TIME						
PART-TIME						
TEMPORARY						

SOURCE OF FUNDS TO OFFSET FISCAL IMPACT OF BILL:

ANALYSIS: Attach a separate page for analysis

Prepared By: Kenneth C. Moore, Director Phone: 465-2515  
Division: Insurance Date: 2/15/84

Approved by Commissioner: Richard A. Lyon Date: 2/15/84  
Agency: Department of Commerce and Economic Development

Distribution (by Agency preparing fiscal note):

Legislative Finance  
Legislative Sponsor  
Requestor  
Office of Management and Budget  
Impacted Agency(ies)

12/1/83

AMMENDMENTS PROPOSED

Page 23, lines 9-10.

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Dept's Proposed Amendments

## INSIDE INSURANCE

# Big losses raise question of 'moral hazards'

*'Most people are not in a position to make money off of sinking their vessel'*

by Robert Mann

Millions of dollars worth of fishing vessel losses in 1982 have broken over Seattle's marine insurance community like a rogue wave at sea. The result, according to brokers and underwriters, could be that fishermen will be paying higher deductibles and premiums in the very near future.

Although the Coast Guard does not keep track of the total number of fishing vessels and processors lost in a given year, some worried underwriters are drawing up lists of their own. The 1982 numbers look pretty grim to companies that are insuring Alaskan fishing vessels.

According to one list, there have been over \$48 million worth of total losses of crabbers, seiners, draggers, processors and gillnetters through November of 1982. Five processors, three of which burned and sank within a six week period,

accounted for \$29 million worth of the total; the *Al-Ind-Esk-A-Sea*, which burned and sank off Everett on October 22, was perhaps the most spectacular of the losses. Another underwriter said over \$22 million worth of crabbers sunk, burned, or ran aground this year.

Bad times seem to bring an increase in the number of reports of vessel owners burning or deliberately sinking their boats to collect the insurance money so they can get out of the business. The fact is, though, that not much is usually gained from that kind of act, according to several underwriters.

"When people are going broke, it seems that the friction of the mortgage against one's wallet seems to heat up the back of the boat, and away she goes," quipped John Adams. Adams manages Pacific General Agency, Inc., a company that insures millions of dollars worth of fishing vessels throughout the U.S.

Adds Adams: "It really does a fisherman no good to file a claim or

have a convenient loss, if he is going to lose his ability to make a living. Most people are not in a position to make money off of sinking their vessel. At best, they usually get the mortgage paid off."

Maurice Oaksmith, an insurance broker, agrees with Adams for different reasons. "I really don't think that 'moral hazards' (intentional sinkings and burnings) are a factor right now, even with the depressed state of some of the fisheries. I've got great faith in human nature, particularly in the fishing industry."

Others in the insurance business, however, do not share Oaksmith's "faith" in human nature in the fishing fleets. One president of an insurance company here instructed his underwriters not to carry any more lines on converted processors, which he labeled, "floating fire hazards." Another marine insurance underwriting firm, Mathews & Livingston, Inc., bailed out of the fish vessel business in 1981 because "it is a volatile market and we were

looking at doubling our rates from our London connection," says a company spokesperson.

"My friends at Lloyd's say the Northwest and Alaska losses have just about destroyed their marine underwriting syndicate," says a former British underwriter who has worked in the U.S. marine insurance industry for two years.

Lloyd's and other western European companies that assume part of the risk on American fishing vessels are quoting prices that many U.S. brokers and underwriters are finding hard to sell to customers. An understanding of why the European insurers are shying away from the fishing vessel business requires a brief explanation of how marine insurance works.

Imagine a pyramid with the broker or underwriter sitting at the top. The fisherman comes into the office, and tells the broker or underwriter what kind of policies he wants and what he is willing to pay. (Most fishermen are covered for losses or damage to the hull and

machinery. A fisherman, no matter what his past record, can usually find someone to insure him.) The broker then goes to his underwriters—the first set of risk-takers, who usually carry only a small percentage of risk themselves. The risk on expensive fishing vessels is always spread out among re-insurers.

The most reliable re-insurers are in London at Lloyd's or the Institute of London Underwriters and other western European countries. Those companies, though, may spread the risk even further down the pyramid. At the bottom of the pyramid, you might find that a company you never heard of in Latin America might be assuming a fraction of a percentage of the total risk on an Alaskan fishing vessel. When claims are made, payment starts at the pyramid's bottom and works its way up.

According to Adams and others, North Pacific fishing vessels have a bad reputation in the European re-insurance market, hence the doubling and tripling of rates in the last two or three months. As a result of the increases, some smaller companies have been forced to seek reinsurance with unproven foreign security firms.

"The London and Western European reinsurance markets have just dried up," says Adams. "It's imprudent for a company like ours to hold all the risk on a crabber with a high degree of hazard. We have to have re-insurers and as these re-insurers drop out, there goes the market."

In the competitive marine insurance business, some companies are so hungry for premium dollars they are re-insuring through companies in South Africa, the Bahamas, and Hong Kong. "You have to realize that there are over 600 companies based in Hong Kong alone, and most of them are only a name in the phone book," said Adams, who adds that many claims go unpaid. "Many of the foreign securities firms will disappear before the claims can get in."

Says Maurice Oaksmith, "Insurance companies and syndicates make money from underwriting and investment income. Now that interest rates are lower on short-term money, the competition for insurance premium dollars is getting even heavier. Some people want to make a quick killing by buying their reinsurance as cheaply as possible so that they can keep most of the premium. They tend to stray into left field re-insurers."

Oaksmith says that "If underwriters are selective, and properly re-insured, they can make money writing fish boats at or near the level of where premiums are today."

John Adams knocks on his desk and says his firm has made money. "We have tried to be cautious with those people that we suspect." But Adams feels that most marine insurance underwriters and brokers today do not know their market. "In the past few years we've seen the inundation of the marine insurance market with inexperienced people with all kinds of capacity. There have been more and more companies coming in and diving right out again after a few hard licks."

rie says there are quite a few "damn good salesmen who are very gullible because they don't want to know the truth about the security they're representing. If it's an undesirable risk, it will usually end up with what we consider to be the less inquisitive underwriters who fail to ask the questions they should ask."

Adams maintains that there are very few underwriters who truly understand the fishing business well enough to know when to ask if a person is a "known troublemaker with a poor record in the past. Some people, though, are not crooked, they're just doggone unlucky," says Adams.

Adams feels most underwriters insuring fish boats should know how machinery operates so that they can know if a claim is legitimate or not. "Most underwriters don't know anything about claims. Unfortunately, the claims people think the underwriters know everything," says Adams.

Although Adams has worked around fishing boats a long time, he says he is often too busy to get the chance to visit the docks to inspect fishing vessels he insures, although he says he tries to as often as possible. Like others, he relies on marine surveyors, the eyes and ears of every underwriter or broker. (See accompanying story.)

Marine surveyors perform condition and valuation (C&V) surveys for vessel owners, insurance companies, and banks. They check a vessel's wiring, construction, deck equipment, rigging, navigation equipment, electronics, cabin arrangements, safety and life saving equipment, hydraulics, engine room, and even the vessel's housekeeping and appearance. They also note any recommendations for improving the vessel before reaching what they feel is a fair market value for the boat.

"Surveyors have a pretty good feeling for what a boat's value is, and they understand replacement costs," says Oaksmith. "But there can be honest differences of opinion between a surveyor and a boat owner."

Some surveyors say they are pressured to keep boat values high even though their market values might be depressed in a weak market. According to one surveyor who ran a C & V survey on a large

floating processor in 1979, the vessel's owners pressured him to keep the value high because the bank had loaned them a lot of money on processing equipment. The surveyor says he told the owners that the boat had no track record and needed more work, so he valued it substantially less than what the owners had wanted.

"I gave them two legal-sized sheets of repair and safety recommendations, and two months later they had somebody else doing the survey. They obviously wanted someone who would agree with their value," the surveyor says. He asked to remain anonymous. "I have quit one job before because the guy hasn't done what I've asked him to do. But within a week he's got insurance from somebody else."

"What's happening in the present market is that a lot of people are not insuring market values. They're insuring investment value," says another veteran surveyor. "A lot of money had to be put into that processor to get her operable, and



Maurice Oaksmith

## BOAT INSURANCE

*continued from page 31*

the company wanted to insure that investment."

However, other surveyors say they are rarely pressured into inflating vessel values. John Adams, for instance, says "Sometimes the vessel owner wants surveyors to deflate the value because he doesn't want to pay the money on high insurance premiums on boats that are fully paid for."

"Most surveyors know what they're doing," says one claims investigator, "but some have great gaps in their experience and training. Some surveyors specialize in cargo only, others in tug boats, others in yachts, and some in crab boats. Frequently their expertise is limited to their specialty class of vessels, and they're not able to adapt well to new classes."

Adams adds, "The jam is that many people will accept a surveyor's

report on a matter for which he is not truly qualified."

Surveyors have already formed their own national association fifteen years ago in an effort to police their own trade. In order to join the National Association of Marine Surveyors an applicant must have at least five years full-time surveying experience and he must pass an exam on his specialty class of vessel. "It's still in its infancy," says one member.

Whether an underwriter or vessel owner decides to hire, fire or believe a surveyor does not diminish the importance of their C & V surveys. When claims are paid, they are the most important records available, because foul play is almost impossible to prove. Underwriters rarely go to the bother and expense of trying to prove arson or intentional sinking; they simply pay the claims based on a vessel's surveyed value. Raising the vessel and re-surveying it is the only way to change the surveyed value.

Adams jogs his memory back to 1958 when a wooden seiner sank in the Puget Sound and the underwriters raised the vessel. "There were funny ax holes in the bottom of the boat that were made from the inside. These rapid termite jobs are good for some people, but when an owner gets caught with evidence like that, it is a federal crime and the punishment can be severe. From an underwriter's standpoint, you have to look at how much a mortgage is on a vessel before thinking about deliberate sinkings.

"It's easy to say that when the mortgage is high and the value are dropping beneath the mortgage, it

becomes advantageous to have an accident. But that's only part of the story," says Adams.

"The other part is that people are working harder and pushing their crews harder and harder trying to make a profit. Everybody gets tired."

Maurice Oaksmith, who grew up on Alaskan fishing boats, says, "I think fishing vessels in many ways are a better risk today than they were four years ago. There are many more alarms, detection devices, and better navigational equipment. But one thing you've got to guard against, as technology advances, is complacency."

Adams blames accidents involving some crabbers on "electronic creature comforts" along with drug use by younger crew members who doze during their wheel watch.

In some cases, though, he says accidents are not due to overwork, drugs, or high-tech instruments. "In Bristol Bay we never have a total loss prior to the season unless it's truly accidental. It always seems to happen just before the end of the season, and "Oh, my god, the fire started," or "I hit a rock." There aren't very many rocks in Bristol Bay, so they either swamp or burn.

"It always happens where it's hard to recover the boat, in the dark of night; a friend just happened to be coming along and he saw the fire, and 'I got off without getting my tennie runners wet.'"

Adams admits that he is speaking somewhat facetiously; he knows that Bristol Bay permits can cost up to \$100,000. Yet he sincerely feels that 'moral hazards'—"sinking the damn boat"—are higher these days,



John Adams

and the way to prevent them is to make sure the owner starts accepting some of the risk.

He looks back to the 1930's during the Great Depression when there were a lot of similar vessel losses occurring. According to Adams, an underwriter would co-insure the vessel, assuming only part of the risk in case of partial losses; the owner would pick up the rest. The other alternative he sees is charging very high deductibles.

Adams thinks strict Coast Guard enforcement of safety regulations helps reduce risk, too. Under Section 46, Parts 24 through 26 of the Code of Federal Regulations, the Coast Guard can board uninspected fishing vessels and check for safety and fire fighting equipment violations. But Coast Guard spokespeople say they do not have the manpower to check fishing vessels unless they receive a specific See **BOAT INSURANCE** page 45

## BOAT INSURANCE

continued from page 34  
complaint.

Maurice Oaksmith, one of the founders of the National Council of Fishing Vessel Safety and Insurance, says the "industry ought to consider self-regulation. The principal reason for forming this national group was that insurance costs were high, and the only way to bring them down was to decrease the severity and frequency of accidents. I would say that about 90% of all accidents and fatalities are avoidable. Usually they result from somebody doing something they shouldn't do."

There is a general consensus among marine surveyors, underwriters, and claims investigators

that human error, due to lack of adequate training, is responsible for many legitimate accidents. In the case of converted floating processors, however, there are other dangers.

During the conversion process, bulkheads and cofferdams are usually removed to make more room for processing equipment, forklifts, and elevators. "They cut out watertight bulkheads so it's easier to move cargo down to the freezing holds and along the processing deck," explains surveyor Jim Goldade.

"In the case of one processor," says another surveyor, "all three holds had been cut through all the way back to the engine room. You can pump such a vessel full of water,

but you've got no way to pump it out again. There are no subdivisions to control flooding or fire in these vessels."

Highly flammable polyurethane foam is also an acknowledged fire hazard aboard such processors.

"We've glossed over these problems in the last few years because of a very competitive insurance market, due to excess capacity and underwriters seeking premiums at any cost," says one concerned claims investigator. "Now that interest rates are declining and losses are continuing to accelerate, the conditions are set for a scarcity of insurance and possibly a recognition that standards will be necessary if losses are to be controlled." □