

SB

152

SFIN

FILE

SENATE FINANCE COMMITTEE REPORT

REPORTED OUT
APR 24 2001
SENATE FINANCE
COMMITTEE

DATE: 4/11/01

FURTHER:

DATE TURNED IN TO OFFICE: 25 April 01

Finance Committee considered

SENATE BILL NO. 152

DOTPF-RELATED CONTRACT CLAIMS

"An Act relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public Facilities delegates the responsibility for handling the controversies."
and recommends:

be replaced with _____ CS _____ (_____)

adopt previous _____ CS _____ (_____)

attached amendment(s)

adopt Letter of Intent by _____ Committee

further referral to _____ Committee

Senate Bill:

same title

new title

House Bill:

same title

technical title

new: SCR # _____

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#
D.CED/AIDFA	4/19/01	*		

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#
DOT & PF	9/10/01		✓	1

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	Do PASS	Do NOT PASS	No REC	AMEND
<i>[Signature]</i>				
<i>[Signature]</i>		X	X	
<i>[Signature]</i>	✓			
<i>[Signature]</i>	✓			
<i>[Signature]</i>				
COCHAIR: <i>[Signature]</i>	✓			
COCHAIR: <i>[Signature]</i>	✓			

APR 24 2001

SENATE FINANCE
COMMITTEE

FISCAL NOTE

STATE OF ALASKA
2001 LEGISLATIVE SESSION

Fiscal Note Number: 1
 Bill Version: SB 152
 (S) Publish Date: 4/11/01
 Dept. Affected: DOT&PF
 BRU: _____
 Component: _____
 Component Number: _____

Revision Date/Time (Note if correction): _____
 Title: An act related to the handling of interest on
contract controversies involving the Department of Transp...
 Sponsor: Senator Cowdery
 Requester: Senate Transportation

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	0.0	0.0	0.0	0.0	0.0	0.0

CAPITAL EXPENDITURES	0.0**	0.0**	0.0**	0.0**	0.0**	0.0**
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CHANGE IN REVENUES ()						
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FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
Other (Specify Type)						
TOTAL	0.0	0.0	0.0	0.0	0.0	0.0

Estimate of any current year (FY2001) cost: 0.0

Check this box (X) if funding for this bill is included in the Governor's FY 2002 budget proposal:

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

**This bill will result in additional interest payments on contract related claims. The additional interest could range from \$500.0 to several million dollars per year. Although this won't affect our capital budget request, these payments will reduce the amount available for other capital projects. Most of the additional interest payments will be eligible for 90% federal funding with a 10% GF match.

Prepared by: Dennis R. Poshard, Special Assistant Phone 465-3904
 Division: Commissioner's Office Date/Time 4/10/01 12:00 AM
 Approved by: Commissioner Joseph L. Perkins, P.E. Date 4/10/01
 Agency: Department of Transportation and Public Facilities

For distribution information, call the Governor's Legislative Office

FISCAL NOTE

STATE OF ALASKA
2001 LEGISLATIVE SESSION

Fiscal Note Number: _____
 Bill Version: SB 152
 () Publish Date: _____

Revision Date/Time (Note if correction): 04/19/2001 10:55a.m. Dept. Affected: DCED
 Title: DOTPF - Contract Related Claims BRU: AIDEA
 Component: AIDEA
 Sponsor: Senator Cowdery
 Requester: Senate Finance Component Number: 1234

Expenditures/Revenues (Thousands of Dollars)

Note: Amounts do not include inflation unless otherwise noted below.

OPERATING EXPENDITURES	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
Personal Services						
Travel						
Contractual						
Supplies						
Equipment						
Land & Structures						
Grants & Claims						
Miscellaneous						
TOTAL OPERATING	*	*	*	*	*	*
CAPITAL EXPENDITURES	*	*	*	*	*	*
CHANGE IN REVENUES ()	*	*	*	*	*	*

FUND SOURCE (Thousands of Dollars)

1002 Federal Receipts						
1003 GF Match						
1004 GF						
1005 GF/Program Receipts						
1037 GF/Mental Health						
1156 RSS						
TOTAL	*	*	*	*	*	*

Estimate of any current year (FY2001) cost: _____

POSITIONS

Full-time						
Part-time						
Temporary						

ANALYSIS: (Attach a separate page if necessary)

*AIDEA has a delegation of authority from DOTPF for construction of AIDEA Development Finance projects (AIDEA owned and operated). This bill will result in additional interest payments on contract related claims. There is no way to predict the costs in the future. AIDEA Development Finance projects generally do not use General Funds (Healy Clean Coal Plant and the DeLong Mountain Transportation System funding included slate grants). Additional costs, such as claims, are charged to the project proponent or are funded by AIDEA funds. In the past AIDEA has had small and multi-million dollar claims on construction projects. The claims have resulted in negotiated settlements. For example, a \$1.17 million claim was paid on the Healy Clean Coal Plant in 1999. If this legislation were in effect, AIDEA would have had to pay an additional \$188,018 (10% compounded interest for 18 months). Originally the claim was upwards of \$10 million. If AIDEA funds are required, AIDEA's net income declines, decreasing the annual dividend AIDEA pays to the General Fund.

Prepared by: Robert G. Poe, Jr., Executive Director Phone 907-269-3000
 Division: AIDEA Date/Time 04/19/2001 10:55a.m.
 Approved by: Commissioner Deborah B. Sedwick Date 4/19/2001
 Agency: Department of Community & Economic Development

For distribution information, call the Governor's Legislative Office

SENATE FINANCE COMMITTEE
2000 COMMITTEE ACTION

4/24

Bill Number SB 152			
Amendment			
Motion Pass			
<u>Motion by</u> Donley			
<u>Objection by</u> Hoffman			
<u>Removed</u>			
<u>Second Objection by</u>			
<u>Committee Member</u>	<u>Y</u>	<u>Vote</u>	<u>N</u>
Senator Leman	✓		
Senator Olson			✓
Senator Ward	✓		
Senator Wilken	✓		
Senator Austerman			
Senator Green			
Senator Hoffman			✓
Co-Chair Donley	✓		
Co-Chair Kelly	✓		
<u>Tally</u>			
Yea	5		
Nay	2		
Absent			
<u>MOTION</u> PASSED			

From the office of . . . Senator John J. Cowdery
State Capitol Building, Rm #101
Juneau, AK 99801
907-465-3879 phone
907-465-2069 fax

MEMORANDUM

Sponsor Statement for SB 152

Relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public Facilities delegates the responsibility for handling the controversies.

This proposed legislation would simply require that when a contract settlement with DOTPF is in dispute and finally settled in favor of the contractor that interest must be paid to the contractor on the settlement amount for the time the contract was in dispute.

Interest accrues at the rate applicable to judgements and the interest accrues from the date the claim was filed through the date of the decision.



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

April 6, 2001

Re: SB 152 – Interest on Contract Controversies

Dear Senator:

On public works projects in the State of Alaska, a contractor encountering a condition that requires a change in the contract, is required to perform the work even if there is a dispute as to the appropriate adjustment. Resolution of such a claim frequently takes as long as four years and the State currently disallows interest on the amount of the ultimate settlement.

Most, if not all, public works contracts include contract adjustment clauses that provide a method for adjusting the contract amount when the contractor encounters changed conditions or the owner desires to change the contract in some manner. The purpose of this clause is to assure that the contractor is fairly compensated for the extra work occasioned by the change.

Alaska courts generally recognize that awarding prejudgment interest to a plaintiff is necessary to make him "whole" by compensating him for the use of money rightfully his between the time of injury and trial. The courts have held that prejudgment interest should be denied only in the most unusual cases and place the burden of proving the unusual situation on the party opposing the award of prejudgment interest. The State of Alaska apparently believes that contractor claims in general represent an "unusual case" and therefore prejudgment interest should not be applied to these claims.

We urge you to support SB 152. This bill allows construction contract claims to be treated the same as all other claims in the State of Alaska. There is no public interest in discriminating against the entire construction industry in these matters.

Sincerely,

Richard Cattanach
Executive Director

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK
99669
TELEPHONE (907) 262-8535

INTEREST ON CONTRACT CONTROVERSIES
SB 152 & HB235

Position Paper of
The Associated General Contractors of Alaska

ISSUE: Given the complexity of construction projects, it is not unusual that differences sometimes develop between the owner and contractor regarding the scope of work covered in the contract. In those instances when the differences cannot be successfully resolved, the parties can avail themselves of the claims process set forth in the Alaska procurement code. One problem with this process is the inherent delay in the ultimate payment of the claim. The position of the State of Alaska is that they do not owe interest on the ultimate awards. Contractors believe that the delayed payment costs them not only foregone interest but also the costs of preparing and defending their claim, and that the avoidance of interest is not only contrary to common practice, it is bad public policy.

ADVANTAGES: For the State of Alaska, delaying claims allows them to earn interest on money they ultimately owe the contractor. Through such delays the State derives an economic interest in postponing the claims process. Another advantage enjoyed by the State accrues from its superior financial strength and legal resources, which sometimes can be used to force financially, strapped companies to settle their claims at a fraction of the claims value.

The current system offers no advantages to the contractor.

DISADVANTAGES: The primary disadvantage to the State will be derived from the addition of interest to the cost of a claim for the period the claim is being contended. The proposed law will put a premium on the expeditious settlement of construction claims. The State will have to change its procedures to handle such claims in a more timely manner.

There are no disadvantages to the contractor.

AGC POSITION

The current process regarding the settlement of a claim places the contractor at an economic disadvantage. Since the expenses underlying a claim have to be paid, the contractor incurs these costs plus the costs of preparing and defending its position. During this entire process the State is allowed to invest those funds for its own economic gain as well as using its superior resources to threaten the economic viability of the claimant. Payment of interest on claims is not only good public policy, but it is consistent with prior practices of the Department of Transportation regarding such claims. Currently the State of Alaska must pay prejudgment interest for virtually all other contract claimants. Contractors, however, have been singled out for disparate treatment.

TONY KNOWLES, GOVERNOR

DEPARTMENT OF LAW
OFFICE OF THE ATTORNEY GENERAL

P.O. BOX 110300
JUNEAU, ALASKA 99811-0300
PHONE: (907)465-3600
FAX: (907)465-2075

April 16, 2001

The Hon. Vic Kohring, Chair,
and Members, House Transportation Committee
State Capitol, Room 24
Juneau, AK 99801

Re: HB 235 – An Act relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public Facilities delegates the responsibility for handling the controversies.

Dear Representative Kohring,

I am the attorney assigned by the Alaska Department of Law to provide testimony on HB 235, which provides for prejudgment interest on administrative claims. Due to litigation demands in another case, I am in Ketchikan today and unable to testify. As a consequence, I respectfully submit this letter in place of in-person testimony. If any committee member has questions regarding the contents of this letter, I would be happy to meet with that member in person, or respond in writing to the entire committee. I can be reached by phone at 465-6712, and by fax at 465-6735.

• **Prejudgment Interest on Administrative Claims Not Allowed in Majority of Other States**

We have not undertaken a survey of every state in the country. However it appears that a fair number of states do not pay prejudgment interest on administrative contract claims either outright or because the law in those states limits payment of interest to "liquidated" claims, i.e., claims that are capable of calculation under some contractual formula that does not require the exercise of discretion by agency personnel.

The Honorable Vic Kohring, Chair,
and Members, House Transportation Committee
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Alaska law, AS 36.90.200(a), already requires payment of interest on "payment requests" for work satisfactorily performed on state construction projects. If the state gives notice to the contractor that the work covered under the payment request is unsatisfactory, no interest is paid on that payment request until 21 days after the unsatisfactory work is corrected. AS 36.90.200(c). While this statute does not cover payment of interest on contract claims filed under the State Procurement Code, it is an example of the type of "liquidated" amount on which interest would ordinarily be paid if timely payment were not made by the state.

Where contract claims are concerned, there may be good policy reasons to withhold the payment of prejudgment interest. There may be policy reasons why the agency should have the opportunity to examine such claims before prejudgment interest begins accruing.

- **Cost of Application of HB 235 to Construction Contracts**

Under the Alaska Procurement Code, the Alaska Department of Transportation has the procurement authority for all construction projects conducted in the state. AS 36.30.005(b). The Department of Transportation may delegate that authority to other agencies under AS 36.30.632. Therefore, since all construction is either being performed by DOT&PF or by other agencies under delegation of authority by DOT&PF, prejudgment interest will affect all agencies conducting construction that are either subject to AS 36.30 or that are required to have similar procurement procedures.

The costs to the state for prejudgment interest if HB 235 became law could be substantial. For example, DOT&PF estimates that annual interest indebtedness could be between \$500,000 and several million dollars if the companion bill to HB 235 (SB 152) were to become law, although federal matching money would be available to cover some of that cost. Fiscal Note 1, SB 152. On just three recent claims of which we are aware, prejudgment interest totaling approximately \$1,200,000 would have been paid by the state if prejudgment interest were due on those claims.

- **If HB 235 Becomes Law, How Will the State Pay Prejudgment Interest?**

FHWA Projects: DOT&PF does most of its construction in the State of Alaska by using funding from the Federal Highway Administration (FHWA). While the budget process for federal funding is beyond the scope of this letter, it appears that FHWA will participate in payment of interest on construction claims according to

The Honorable Vic Kohring, Chair,
and Members. House Transportation Committee

April 16, 2001

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a federal participation rate that typically is 90 percent. Of course, payment of interest on a project means that fewer dollars will be available for projects in the state. In other words, prejudgment interest paid on one project may mean that the state is unable to fund another project somewhere else in the state.

FAA Projects: DOT&PF also conducts construction activities at airports throughout the state to build new, or expand existing, facilities utilizing Federal Aviation Administration ("FAA") funding). FAA grants operate differently than those for FHWA-funded projects. In FAA projects, the amount of a grant is based on the state's total estimate of all costs to design and construct the project. Increases in the grant amount are limited to 15 percent of the original grant. Any additional costs incurred above the grant plus 15 percent must be covered entirely by the state. If interest exceeds the amount of the FAA grant, the state will have to fund all additional expenses without FAA participation.

HB 235 affects all agencies in the state that conduct construction activities under a delegation of authority from DOT&PF. Many of these projects are supported by programs that include funding and grants from federal agencies other than FHWA and FAA. As a consequence, it may be that federal participation in administrative claims is limited in certain situations, depending on the funding source, and that state funds will have to be used to pay interest claims. Because we have not undertaken a study of the way other agencies performing construction with a delegation from DOT&PF fund projects, it is unclear that federal participation will be available to fund interest payments owed as HB 235 is currently drafted.

- **Equal Protection Issues for Other AS 36.30 Claims**

There may be an equal protection problem with this legislation as presently drafted. HB 235 authorizes the payment of interest on claims under AS 36.30.620 - .630 and 36.30.670 - 36.30.685 against DOT&PF and other agencies acting under a delegation from DOT&PF. HB 235 therefore applies to DOT&PF construction claims. Contractors asserting claims against other agencies under AS 36.30.620 - .630 and 36.30.670 - .685 may allege that they are denied equal protection of the law because they are denied prejudgment interest on their claims, while DOT&PF contractors who file claims under the same statute are entitled to interest.

The state would have to demonstrate at least a legitimate state interest in allowing prejudgment interest on some claims while denying it on others. A court might conclude that the legislature's interest in limiting prejudgment interest only to

The Honorable Vic Kohring, Chair,
and Members, House Transportation Committee
April 16, 2001
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construction claims simply to save the costs of having to pay interest on all AS 36.30 claims does not bear a substantial relationship to a legitimate state objective.¹

- **Equal Protection Issues for Non-AS 36.30 Construction Projects**

The Alaska Railroad Corporation, the Alaska Aerospace Development Corporation, and the Alaska Seafood Marketing Institute must adopt procedures "substantially equivalent" or "substantially similar" to AS 36.30. AS 36.30.015(e), AS 36.30.015(h). Claimants against these agencies may argue that, by virtue of the changes proposed to the procurement code by HB 235, these agencies also have to provide for the payment of prejudgment interest on claims.

Other agencies exempt from AS 36.30 include the University of Alaska, the Alaska Housing Finance Corporation, the Alaska State Pension Investment Board, the Alaska Court System. AS 36.30.005(c), AS 36.30.015(i), and AS 36.30.030. These agencies do not have to adopt procedures equivalent to the State Procurement Code. However, the same or a similar equal protection argument may be advanced with respect to those agencies. In the recent past, at least AHFC and the Court System have faced construction claims.

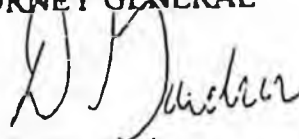
¹ The Alaska Supreme Court has held that Equal Protection Clause of the Alaska Constitution affords greater protection to individual rights than that afforded under the U.S. Constitution. *State v. Enserch Alaska Construction, Inc.*, 787 P.2d 624, 631 (Alaska 1989); *Laborers Local No. 942 v. Lampkin*, 956 P.2d 422, 429 (Alaska 1998). The court uses a sliding scale analysis that determines the relative importance of the individual right and the State interest and, depending on the importance of the individual interest, requires the State interest to "fall somewhere on a continuum from mere legitimacy to a compelling interest." *Enserch*, 787 P.2d at 631. The nexus between the State's interest and the means used by the State to achieve that interest must fall on a continuum from a "substantial relationship to [the] least restrictive means," again, depending on the importance of the individual right at issue. *Id.* at 631-32. *Williams v. State*, 895 P.2d 99, 104 (Alaska 1995); *Herricks Aero-Auto Aqua Repair v. State, DOT&PF*, 754 P.2d 1111, 1114 (Alaska 1988)(economic interests entitled to only minimal protection under Alaska Equal Protection Clause; cost savings alone may not be a legitimate state interest).

The Honorable Vic Kohring, Chair,
and Members, House Transportation Committee
April 16, 2001
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If you or any committee member has questions regarding the testimony summarized above, please advise.

Sincerely,

BRUCE M. BOTELHO
ATTORNEY GENERAL



By: Doug Gardner
Assistant Attorney General

cc: Michael K. Abbot, Legislative Director, Governor's Office
Vern Jones, Chief Procurement Officer, State of Alaska
Legislative Liaisons
Deborah Behr, Legislation Attorney, Department of Law
Chrystal Smith, Legislative Liaison, Department of Law.



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

April 23, 2001

The Hon. Dave Donley and Pete Kelly, Co-Chairs
and Members, Senate Finance Committee
State Capital, Room 520
Juneau, Alaska 99801

**Re: The Associated General Contractors, Alaska Chapter's Response to
the Department of Law's Position Paper Regarding SB 152 and HB
235**

Dear Senators and Representatives:

As many of you may know, the AGC is in favor of the passage of SB 152. I believe that the merits of the bill should compel passage but I believe that it is appropriate to address the "smoke screen" raised by the Alaska Department of Law concerning this bill.

I was just provided a copy of the State of Alaska Department of Law's position paper on HB 235, dated April 16, 2001 and authored by Assistant Attorney General Doug Gardner. I feel obligated to respond to a number of statements in the Department of Law's position paper because it glosses over the legal history and the recent Department of Law policy that led the AGC to advocate for the passage of this legislation.

In 1965, the Alaska Supreme Court first addressed the issue of whether a contractor claimant was entitled to prejudgment interest. *Wright Truck & Tractor v. State*, 398 P.2d 216 (Alaska 1965). In that case, the Alaska Supreme Court interpreted the precursor to Alaska Stat. § 09.50.280, [Alaska's waiver of sovereign immunity state], which provided as follows:

Sec. 20.04. Judgment for Plaintiff. If judgment is rendered for the plaintiff, it shall be for the legal amount found due from

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 D STREET, SUITE 100 • ANCHORAGE, ALASKA 99503

TELEPHONE (907) 561-5354 • FAX (907) 562-6118

the state with legal interest only from the date of judgment and without punitive damages.

Wright, 398 P.2d at 218.

While upholding the trial court's denial of the contract claimant's request for prejudgment interest pursuant to § 26.04, the Alaska Supreme Court was extremely critical of the inequity and unfairness of the State not having to pay prejudgment interest to contractor claimants:

We are in agreement with appellant's argument that the statutory prohibition can easily work an injustice on a party who has contracted with the state. There are business situations where agents of the state, in good conscience and even with business justification, may withhold for a time or even refuse payment. Where the contracting party is required by contract regulations to continue to perform, subject to later determination, as in the case before us, the problem often facing the contractor is where to get the capital to continue to finance his work. And even if the capital can be obtained the rate of interest required to be paid cannot be ignored. The matter would appear to be one, which the Legislative Council might refer to the legislature for reconsideration in the light of the greatly increased contract authority and activity of the State Department of Public Works.

Wright, 398 P.2d at 220. The Alaska Supreme Court issued the *Wright* decision on January 21, 1965.

In *State v. Phillips*, 470 P.2d 266 (Alaska 1970), the Alaska Supreme Court commented on its decision in *Wright* as follows:

Prior to 1965 the prevailing party in an action against the State of Alaska was entitled to interest 'only from the date of judgment.' In the *Wright Truck* case, decided in 1965, we said that the prohibition against prejudgment interest 'can easily work an injustice on a party who has contracted with the state,' and suggested to the legislature that it consider amending the statute. Two months later, the legislature acted on this suggestion, replacing 'only from the date of judgment' with 'from the date it (the amount found due from the state) became due.' The statute, AS 09.50.280, now reads:

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

If judgment is rendered for the plaintiff, it shall be for the legal amount found due from the state with legal interest from the date it became due and without punitive damages.

State v. Phillips, 470 P.2d at 272.

The March 19, 1965, modifications to Alaska Stat. § 09.50.250 and Alaska Stat. § 09.50.280 discussed in *Phillips* provided as follows:

Sec. 09.50.250. **Actionable Claims Against the State.** A person or corporation having a contract, quasi-contract, or tort claim against the state may bring an action against the state in superior Court. A person who may present his claim under AS 44.77.010 - 44.77.070 may not bring an action under this section except as set out in AS 44.77.040(c). . . .

Sec. 09.50.280. **Judgment for Plaintiff.** If judgment is rendered for the plaintiff, it shall be for the legal amount found due from the state with legal interest from the date it became due and without punitive damages.

Thus, in response to the Alaska Supreme Court's suggestion that prejudgment interest be made a component of actionable claims against the State, the 1965 State Legislature acted accordingly and intended, pursuant to Alaska Stat. § 09.50.280, that prejudgment interest begin accruing from the date it became due. Concurrently with this statutory modification expressly permitting the award of prejudgment interest, the legislature mandated that that certain types of claimants pursue and exhaust administrative remedies pursuant to Alaska Stat. § 44.77.010-.070.

In *State v. ZIA, Inc.*, 556 P.2d 1257 (Alaska 1976), the Alaska Supreme Court construed Alaska Stat. § 44.77.010-.070 with Alaska Stat. § 09.50.250 as requiring a contract claimant bringing an action against the State to first exhaust administrative remedies prior to initiating court action.

In *ZIA*, the contractor contracted with the State to install safety canopies on State equipment. *ZIA* then sued the State for breach of

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

contract without first pursuing the required administrative review of the claim. The Alaska Supreme Court explained that:

By virtue of AS 09.50.250 we recognize the legislative policy, which dictates that actions against the State first should be considered by the affected administrative agency. While we do not find AS 09.50.250 to be of the jurisdictional nature, . . . we find, with respect to cases which fall within AS 09.50.250, that that statute establishes an administrative procedure which can be characterized as a condition precedent, [to a suit in state court].

ZIA, at 1263.

In 1986, the State Legislature enacted Alaska Stat. § 36.30, et seq. -- the State Procurement Code -- thereby adopting internal administrative procedures for contract claimants. In conjunction with the adoption of the State Procurement Code, the legislature modified Alaska Stat. § 09.50.250 as follows:

09.50.250. **Actionable claims against the state.** A person or corporation having a contract, quasi-contract, or tort claim against the state may bring an action against the state in a state court that has jurisdiction over the claim. A person who may present the claim under AS 44.77 may not bring an action under this section except as set out in AS 44.77.040(c). A person who may bring an action under AS 36.30.560-- 36.30.695 may not bring an action under this section except as set out in AS 36.30.685.

Since adopting Alaska Stat. § 09.50.280 in 1965, there has been no statute enacted which limits any contractor claimant's entitlement to prejudgment interest from the date of the claim pursuant to Alaska Stat. § 09.50.280.

Further, the controlling case law does not afford the State any basis to argue that contractor claimants are not entitled to prejudgment interest. State agencies, in particular the Department of Law, have instead taken an arbitrary and unsupported position on this issue based upon an erroneous interpretation of dicta in a 1996 Alaska Supreme Court Case, *Danco Exploration, Inc. v. State*, 924 P.2d 432 (Alaska 1996).

Succinctly, Danco involved a claim that the State of Alaska Department of Natural Resources declined to return a bid deposit to the

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

claimant. The Alaska Supreme Court concluded that Danco was not entitled to prejudgment interest on the bid deposit because it was not an action against the state sounding in contract or tort.

This very argument defies common sense in a state where "prejudgment interest is a form of consequential damages [that] . . . becomes a part of the judgment proper" and where "it is only in the most unusual cases that prejudgment interest is not proper." *Power Constructors, Inc. v. Taylor & Hintze*, 960 P.2d 20, 35 (Alaska 1998).

The Department of Law's position paper must also be placed in historical context. In late 1976, the Department of Law adopted a strategy for handling contractor claims on public works projects. Assistant Attorney General Ray Preston authored the strategy memorandum. It states:

Thus looms the strategy of protracted conflict: the happenstance of one party (the State) with limitless resources and one without. Compounding things is the fact that attorneys fees go to the winner, which will be significantly more flowing from a de novo situation than one where it is review of the Board's decision, and whether that decision is supported by "substantial evidence based upon the record as a whole" (or something close to that). Thus, the State would have the opportunity of winning by attrition, including the factor of hiring a new expert who is even more proficient (and more expensive) than [the contractor] can muster and all the while building up the potential that the contractor will ultimately be liable for those costs. Thus, I believe that the strategy and advantages of protracted conflict in this case is available to the State alone, and that it should seriously be considered in this case.

This strategy of winning through attrition and forcing the contractor to spend literally hundreds of thousands of dollars through a lengthy and protracted claims process is precisely the strategy adopted by the Department of Law for the past several decades.

In 1993, seven years after the enactment of the State Procurement Code, the Alaska Supreme Court explicitly acknowledged that prejudgment interest was an appropriate component of a contractor's claim. *State v. Eastwind, Inc.*, 851 P.2d 1348, 1352 n.5 (Alaska 1993).

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

Up until 1998, State agencies recognized that contractors who prosecuted claims were entitled to an award of prejudgment interest on the ultimately claim amount awarded. For example, in a letter authored by Commissioner Perkins to the attorney for a successful contractor claimant, Commissioner Perkins directed Tony Johansen to "initiate payment in the amount of \$1,945,857.39, . . . plus statutory interest compounded at 10.5 % from October 10, 1996, . . ."

Even as late as March of last year, Commissioner Perkins personally advised me that:

On the issue of paying prejudgment interest on a claim appeal, we are not avoiding making such payments by choice. Rather, we are following the advice of the Attorney General's Office that such payments are contrary to law.

Thus, it is not the Department of Transportation and Public Facilities that opposes awards of prejudgment interest to contractor claimants. Rather, it is the Department of Law that opposes this legislation because it undermines their strategy of "protracted wars of attrition."

With that historical perspective in mind, I wish to address a number of statements submitted by the Department of Law in opposition to the passage of SB 152 and HB 235.

1. Prejudgment Interest on Administrative Claims Not allowed in Majority of Other States.

In the State of Alaska, every contract claim filed against a municipality, city, or federal agency requires an award of prejudgment interest. The state simply cannot argue that every individual who brings a contract action against the state of Alaska that does not fall within an administrative review process is entitled to an award of prejudgment interest. The department of law's assertion that "a fair number of states do not pay prejudgment interest on administrative contract claims . . . because the law in those states limits payments of interest to "liquidated" claims. . ." is sophistry. Contractors who file claims and certify that they are accurate are requesting a specific sum of money that is "liquidated."

Alaska's Prompt Payment Act, AS 36.90.200, was enacted to ensure that the State did not delay paying undisputed amounts to contractors.

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

4041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503
TELEPHONE (907) 561-5354 • FAX (907) 562-6118

Thus, where the State delays in making prompt payment for work accepted, the State must pay interest as a penalty for its dilatory processing of contractor pay requests.

The Department of Law's position paper suggests that "there may be good policy reasons to withhold the payment of prejudgment interest" and that "there may be policy reasons why the agency should have the opportunity to examine such claims before prejudgment interest begins accruing." No policy reasons are articulated for either proposition. A concrete reason to mandate the award of prejudgment interest on contractor claims lies in the same underlying rationale that resulted in the enactment of the Prompt Payment Act. It would encourage the State to make payment quickly when payment is due and it would encourage prompt and timely resolution of contractor claims.

2. Cost of Application of HB 235 to Construction Contracts.

The Department of Law's position paper states, "[t]he costs to the state for prejudgment interest if HB 235 became law could be substantial." My members and I dispute this for a number of reasons.

First, the availability of prejudgment interest on contractor claims would serve as an incentive for State agencies to quickly evaluate and resolve construction disputes. Contractors who suffer losses on state public works projects are only interested in resolving the claim and moving on to the next project. The State Agency and the Department of Law are the only entities that have no interest in timely resolving construction disputes. Rather, they perceive it is in their best interests to delay, make the contractor incur the costs of prosecuting his or her claim, and essentially "break" the contractor by adversely impacting the contractor's bonding capacity and ability to continue to exist.

Second, when state agencies refuse to negotiate or settle a contractor claim, they force the contractor to spend \$200,000 to \$300,000 to retain lawyers and expert consultants to prosecute the claim. As a general observation, most contractors would be content to recover a percentage of their liquidated claim rather than pay attorneys and consultants. When one adds in \$200,000 - \$300,000 in fees on top of that liquidated claim amount, the contractor is forced to pursue the administrative process vigorously to the end just to break even.

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



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TELEPHONE (907) 561-5354 • FAX (907) 562-6118

Third, for all FHWA projects, 23 CFR 635.124, describes those situations wherein the Federal Highway Authority will contribute its 90.97 percent of funds awarded to successful contractor claimants. Specifically:

(f) Payment of interest associated with a claim will be eligible for participation provided that the payment to the contractor for interest is allowable by State statute or specification and the costs are not a result of delays caused by dilatory action of the State or the contractor. The interest rates must not exceed the rate provided for by the State statute or specification.

Lastly, cost considerations are clearly appropriate in these budget-conscious times. I submit that creating a clearly identifiable incentive and downside risk for State agencies [and the Department of Law] to promptly settle these claims would result in cost savings in the long run. You should be aware that incurring costs is a two-way street. State agencies at issue and the Department of Law also incur tremendous expenses from retained attorneys, retained consultants, and retained experts for the purpose of defending against contractor claims. In some cases, state agencies have prospectively applied for hundreds of thousands of dollars in FHWA funds for the purpose of defending against a contractor's affirmative prosecution of a construction claim. It is our position that that those funds would be better spent by settling the claim in a timely fashion.

3. If HB 235 Becomes Law, How will the State Pay Prejudgment Interest?

This question ignores the fact that the State must pay prejudgment interest to virtually all other claimants. The better question is: Why have state agencies and the Department of Law made the arbitrary decision to treat construction contractors differently than any other contract or tort claimant? I assure you that neither the Department of Transportation & Public Facilities nor the Department of Law will provide you with a satisfactory answer to this question.

4. Equal Protection Issues for Other AS 36.30 Claims.

The AGC agrees that this statute should define Department as all state administrative agencies authorized to procure construction or contracts under the State Procurement Code, AS 36.30 et seq.

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535



ASSOCIATED GENERAL CONTRACTORS of ALASKA

1041 B STREET, SUITE 100 • ANCHORAGE, ALASKA 99503

TELEPHONE (907) 561-5354 • FAX (907) 562-6118

5. Equal Protection for Non-AS 36.30 Construction Projects.

The Department of Law's Equal Protection arguments appear to be designed to scare these honorable committees into inactivity with respect to this needed legislation. Notwithstanding these arguments, these committees should recognize that, based upon the institutional knowledge of the agency I represent, the Alaska Railroad Corporation, The University of Alaska, and the Alaska Court System have all had construction claims which were timely settled rather than drawn out through a 3 - 5 year claims process. These agencies, unlike the Department of Transportation and Facilities, recognize that timely resolution of claims avoids attorney's fees, consultant's costs, and expert witness fees, and the associated costs of defending a claim for several years.

Lastly, my apologies for the length of this letter. It was necessary to give the committee members a historical context and perspective into the Department of Law's opposition to this essential legislation. The Associated General Contractors of Alaska support this legislation, as it would give its members equal treatment to that accorded other tort and contract claimants who have claims against the state of Alaska.

If any of you has any questions regarding this letter, please advise me at your earliest convenience.

Very truly yours,

Richard Cattanach

Executive Director

FAIRBANKS
P.O. BOX 6005 • FAIRBANKS, AK 99706
TELEPHONE (907) 452-1809

SOLDOTNA
43335 KALIFONSKI BEACH ROAD, STE. 32 • SOLDOTNA, AK 99669
TELEPHONE (907) 262-8535

AURORA ELECTRIC DATATEL

April 23, 2001

Senator Pete Kelly
Alaska State Senate

Dear Senator Kelly:

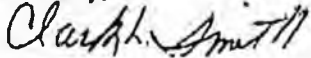
I am writing to urge your support in passage of Senate Bill 152 and House Bill 235 "An Act relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public Facilities delegates the responsibility for handling the controversies."

As a subcontractor who has been involved in construction in the State of Alaska for 19 years, this bill is especially important to me and other members of the construction industry. I am aware that the State of Alaska Department of Transportation & Public Facilities always paid prejudgment interest on claims until just very recently. I disagree with the State's position because prejudgment interest is, has been, and will continue to be an appropriate component of a contractor's damages. Why the State has decided to discontinue paying prejudgment interest is apparent. Prejudgment interest served as a valuable incentive for the Department to expeditiously handle contractor claims and subcontractor pass-through claims. Since the Department recently made the decision it would no longer pay prejudgment interest, I have heard several accounts of the Department literally dragging out its claims handling process for as long as three to four years. In some cases State maladministration of these contracts has resulted in good, reputable firms suffering tremendous financial burdens and even going under.

As a large subcontractor, my company cannot afford to finance State projects for these periods of time. As a result of this, we have even considered avoiding submitting bids on DOTPF projects or we factor DOTPF's retributive project maladministration into our bid to cover for these eventualities. While this may be wasteful of public funds for construction projects, it is essential for our survival in the competitive construction industry. I believe that the threat of prejudgment interest will result in State agencies treating general contractors and subcontractors more favorably. In addition to urging that you pass this legislation immediately, I urge you to make it apply to every claim that is pending as of the effective date of the legislation. This would provide relief for those contractors who successfully prosecuted claims through DOTPF's administrative process during the 3 1/2 year period that DOTPF arbitrarily and wrongly declined to pay prejudgment interest.

Please give this matter your immediate attention.

Sincerely,



Clark L. Smith
Business Development
Aurora Electric/DataTel
1118 E. 70th Avenue
Anchorage, Alaska 99688
(907) 868-2239

Tamsher Construction Inc.
PO Box 878990
Wasilla, AK 99687
(907) 373-3828
(907) 373-3822 FAX

April 18, 2001

President Rick Halford
State Capital, room 107
Juneau, AK 99801-1182

RE: Passage of Senate Bill 152 and House Bill 235

Dear Senator Halford:

I am writing to urge that you support passage of Senate Bill 152 and House Bill 235, "An Act relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public facilities delegated the responsibility for handling the controversies."

As a general contractor who has been involved in construction in the State of Alaska for 10 years, this bill is especially important to me and other members of the construction industry. I am aware that the State of Alaska Department of Transportation and Public Facilities always paid prejudgment interest on claims until just very recently. I disagree with the State's position because prejudgment interest is, has been, and will continue to be an appropriate component of a contractor's damages. Why the State has decided to discontinue paying prejudgment interest is apparent. Prejudgment interest served as a valuable incentive for the Department to expeditiously handle contractor claims and subcontractor pass-through claims. Since the Department recently made the decision it would no longer pay prejudgment interest, I have heard several accounts of the Department literally dragging out its claims handling process for as long as three to four years. In some cases State maladministration of these contracts has resulted in good, reputable firms suffering tremendous financial burdens and even going under.

As a small contractor, my company cannot afford to finance State projects for these periods of time. As a result of this, we have even considered avoiding submitting bids DOTPF projects or we factor DOTPF's retributive project maladministration into our bid to cover for these eventualities. While this may be wasteful of public funds for construction projects, it is essential for our survival in the competitive construction industry. I believe that the threat of prejudgment interest will result in State agencies treating general contractors and subcontractors more favorably.

In addition to urging that you pass this legislation immediately, I urge you to make apply to every claim that is pending as of the effective date of the legislation. This would provide relief for those contractors who successfully prosecuted claims through DOTPF'S administrative process during the 3 ½ year period that DOTPF arbitrarily and wrongly declined to pay prejudgment interest.

Please give this matter you immediate attention.

Sincerely,

Sharon Wessels
Office Manager



GENERAL & ENVIRONMENTAL CONTRACTORS

April 19, 2001

Honorable Senators and Representatives.
State of Alaska

RE: Senate Bill 152, and House Bill 235

Dear Legislators,

Currently, there are 2 bills before the state legislature that require vigorous support of our state representatives and senators. Those are Senate Bill 152, and House Bill 235. My husband and I have been involved in construction in the State of Alaska for over 20 years. The State DOT always used to pay prejudgment interest on successful claims until recently. This policy provides a disincentive for the State to handle claims expeditiously. In the long run, it only costs the State more time and money.

In April of 1997, we were the low bidder on a State of Alaska project, Ft. Richardson Fish Hatchery, for approximately \$2.5M. As the project started we became instantly aware of differing site conditions and design defects. The owner (State of AK ADF&G) acknowledged the problems and the delay and asked us to continue with the project and they would issue a change order at the end of the project after all the differing site conditions, design defects and delay was a completely known factor. We complied with the directive but put our objection in writing, that we wanted to be paid for the changes as they became known. The state refused and continued to direct us to perform 6 months of additional work to correct the design defects, then they backcharged us for not being complete with the additional work within the confines of the original schedule. The additional work and delay cost us \$1,020,000. The liquidated damages cost us \$168,000. It cost us an additional \$250,000 for an attorney and \$50,000 for expert witnesses and testimony.

In December of 1997, we filed a claim with the State of Alaska. The claim process mandated by the State of Alaska is very lengthy. We spent 2 years going through the process. In the summer of 1999 we were preparing for the Administrative Hearing level of the claim. In July of 1999 we spent 3-1/2 weeks in a Administrative Hearing trial. I knew I would need to provide inducement to the Department of Law to get them to settle the lawsuit because by now we did not have the additional funds to pay the attorney to continue to pursue the lawsuit.

We sued the state and "won" at the Administrative Hearing level. However the state of Alaska by statute, does not have to pay attorney fees or interest. The Hearing Officer's decision was rendered in December 1999. The Administrative Hearing Officer did not consider distinct costs for distinct work and simply awarded a lump sum of \$225,000 and a remission of \$80,000 in liquidated damages. We appealed to the Superior Court. In April of 2000, The State agreed to settle the suit with Linder Construction for \$460,000, no interest, no attorney fees.

To add insult to injury, Linder had to get a legislative appropriation to give the state a 'vehicle' and funding approval to pay us. If the State Department of Law did not have so much legislative pressure, they would have strung Linder out even longer. The \$460,000 was written into the supplemental funding bill. We got paid in June of 2000. But the damage had already been done to our business. Linder Construction is a small business. The normal reserves that we use as our operating capital were depleted by this devastating \$1.5M loss on the Fish Hatchery job. In the aftermath of the Fish Hatchery Claim, this small company could not withstand other negative impacts. Therefore, sadly we have made the strategic decision to avoid bidding on all state jobs. This lack of competition also costs the state additional money. I am on the board of directors of Associated General Contractors and I know many other contractors who have had the same negative experience with a State claim causing tremendous financial impact. They too have made the decision not to do business with the state.

It is for all the above stated reasons that I strongly urge you to pass Senate Bill 152, and House Bill 235. I believe this will afford the state a competitive slate of contractors and will result in State Agencies treating contractors more fairly. It will also promote the Governors policy that the state is '*Open for Business*'

In addition to passing this legislation, please make it apply retroactively to every pending claim and claims settled during the 3-1.2 year period that DOTPF arbitrarily and wrongly declined to pay prejudgment interest.

Sincerely,

LINDER CONSTRUCTION, INC.

S/b

Linda J. E. Henrikson
President & CEO

**SENATE COMMITTEE REPORT
First Committee of Referral**

DATE: 3/20/01

FURTHER:

Date of 5-Day Notice: 4/05/01
(in accordance with Uniform Rule 23)

DATE TURNED
IN TO OFFICE: 4/00/01

Transportation Committee considered SENATE BILL NO. 152

DOTPF-RELATED CONTRACT CLAIMS

"An Act relating to the handling of and interest on contract controversies involving the Department of Transportation and Public Facilities or state agencies to whom the Department of Transportation and Public Facilities delegates the responsibility for handling the controversies."

and recommends:

- be replaced with _____ CS _____ (_____)
- adopt previous _____ CS _____ (_____)
- attached amendment(s)
- adopt Letter of Intent by _____ Committee
- further referral to _____ Committee

Senate Bill:

- same title
- new title

House Bill:

- same title
- technical title
- new: SCR # _____

NEW FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#
DOT	4/10/01	**		1

PREVIOUS FISCAL NOTE(S):

Department	Date	Fiscal	Zero	FN#

APPROPRIATION - no fiscal note

SIGNATURES AND RECOMMENDATIONS:	DO PASS	DO NOT PASS	NO REC	AMEND
<i>Adrian L. Taylor</i>	✓			
<i>Greg Wilbur</i>	✓			
<i>John W. ...</i>	✓			
CHAIR: <i>John J. ...</i>	✓			

SENATE FINANCE COMMITTEE

SIGN-IN

SB 152 - DOTPF-RELATED CONTRACT CLAIMS

NAME: Douglas Gardner Subject/Bill No: 152
Co./Dept./Title: Ass't Atty Gen. Phone: 465-3600
Address: Junon Ct. Bldg. Zip: _____
Do you wish to testify? Yes No Respond To Questions

NAME: Pam LaBalle Subject/Bill No: 152
Co./Dept./Title: At. Staff Liaison Phone: 526-2323
Address: 217 2nd St. S.W. 201 Zip: _____
Do you wish to testify? Yes No Respond To Questions

NAME: _____ Subject/Bill No: _____
Co./Dept./Title: _____ Phone: _____
Address: _____ Zip: _____
Do you wish to testify? Yes No Respond To Questions

NAME: _____ Subject/Bill No: _____
Co./Dept./Title: _____ Phone: _____
Address: _____ Zip: _____
Do you wish to testify? Yes No Respond To Questions

SENATE FINANCE COMMITTEE

S I G N - I N

SB 152 - DOTPF-RELATED CONTRACT CLAIMS

NAME: Doucy Gardner Subject/Bill No: SB 152
Co./Dept./Title: Asst. AG Phone: 465-3600
Address: Dimond Courthouse Zip: 94801

Do you wish to testify? Yes No Respond To Questions

NAME: _____ Subject/Bill No: _____
Co./Dept./Title: _____ Phone: _____
Address: _____ Zip: _____

Do you wish to testify? Yes No Respond To Questions

NAME: _____ Subject/Bill No: _____
Co./Dept./Title: _____ Phone: _____
Address: _____ Zip: _____

Do you wish to testify? Yes No Respond To Questions

NAME: _____ Subject/Bill No: _____
Co./Dept./Title: _____ Phone: _____
Address: _____ Zip: _____

Do you wish to testify? Yes No Respond To Questions