Approved: 2-25-09
Date

MINUTES OF THE SENATE FINANCIAL INSTITUTIONS AND INSURANCE COMMITTEE

The meeting was called to order by Chairman Ruth Teichman at 9:30 a.m. on February 5, 2009, in Room 136-N of the Capitol.

All members were present.

Committee staff present:
Bruce Kinzie, Office of the Revisor of Statutes
Melissa Calderwood, Kansas Legislative Research Department
Terri Weber, Kansas Legislative Research Department
Beverly Beam, Committee Assistant

Conferees appearing before the committee:

Melissa Calderwood, Principal Analyst, Research Department
Bill Miller, American Subcontractors Association and Midwest Crane and Rigging, LLC (Attachment 1)
Richard Usher, Hill & Usher Insurance & Surety (Attachment 2)
Kenneth R. Keller, Western Extralite Company (retired) (Attachment 3)
Kurt Brack, Attorney, Holbrook & Osborn, P.A. (Written only) (Attachment 4)
Mark E. Gardner, George J. Siebers & Co., Inc. (Written only) (Attachment 5)
Erin Hoestje, Associate General Counsel, Securities Commissioner's Office (Attachment 6)

Others attending:
See attached list.

The Chair welcomed everyone to the meeting.

Hearing on

**SB 126 - Controlled insurance program act.**

Melissa Calderwood, Principal Analyst, Research Department, gave an overview of the bill. Ms. Calderwood stated that **SB 126** would enact the Controlled Insurance Programs Act. She said this bill defines controlled insurance program as a program of liability insurance coverage that is established by the owner or contractor who contractually requires participation by contractors or subcontractors who are engaged in work required by a construction contract. She said controlled insurance programs would include coverage programs on a single construction site. She said controlled insurance programs would be required to establish a method for quarterly reporting of claim details and loss information to all participants. She noted that programs must allow cancellation of any or all of the coverage provided to permit the participant to terminate the construction contract and receive payment for all work completed through date of cancellation. She said participants could not be charged a deductible for coverage; programs must keep self-insured retention fully funded by the owner or contractor; disclose specific requirements for safety or equipment prior to accepting bids; and allow fines for alleged safety violations to be assessed only by government agencies. She said participant deductions for general liability coverage or workers compensation premiums would not include insurance agent's fees or commissions. Finally, she noted that the bill also outlines requirements for a controlled insurance program that includes general liability coverage or workers compensation liabilities of the participants. The Kansas Insurance Department indicates there would be no fiscal effect associated with the enactment of this bill, she said..

Bill Miller, representing American Subcontractors Association and Midwest Crane and Rigging, LLC, testified in support of **SB 126.** He stated that owner or contractor controlled insurance programs, commonly referred to as wrap-up policies, have become the number one problem for subcontractors according to a survey completed last summer. He said wrap-ups are a relatively new insurance program for the general building construction industry that forces all subcontractors on a project to give up their own insurance program for that project and, in exchange for the premium that they would have paid, they are covered under one policy furnished by the owner or the general contractor. He said participation in these programs is not voluntary. Mr. Miller said these programs have serious deficiencies for the participants and, in many cases, for the owner

as well. He said **SB 126** addresses the most serious problems. (Attachment 1)

Richard Usher, Hill & Usher Insurance & Surety, testified in support of **SB 126.** Mr. Usher stated that debate over the perceived benefits of consolidated insurance programs (CIPs) also known as controlled insurance programs and more popularly referred to as "wrap-ups," has evolved over the past several decades into one of the most contentious issues within today's construction industry. He said a wrap-up is a centralized insurance and loss control program intended to protect the project owner, prime contractor and subcontractors under a single set of insurance policies. (Attachment 2)

Ken Keller, retired controller with Western Extralite Company, testified in support of **SB 126.** Mr. Keller said he does not oppose the concept of owner or contractor controlled insurance programs, also known as OCIPs and CCIPs and sometimes as wrap-up insurance programs, but he wants this legislation to make sure the subcontractor has the same protection under this program that he would have under his own insurance coverage. He said currently, that is not the case in some contracts. He said there are contracts that state coverage will end in three years. He said the statute of repose in Kansas is 10 years. That means you have to find coverage for the remaining seven years, or be willing to stand the risk of being self-insured. He said that coverage is not generally available. He said there are examples where coverage was cancelled before the job was complete, leaving the subcontractors with an enormous exposure self insuring the remainder of the work and subsequent risk. Mr. Keller noted that the list of potential problems in the wrap-up programs is lengthy, but they are addressed and will be corrected with the passage of **SB 126**. (Attachment 3)

Kurt Brack, Holbrook & Osborn, PA, submitted written testimony. (Attachment 4)

Mark E. Gardner, George J. Siebers & Co., Inc., submitted written testimony. (Attachment 5)

Senator Barnett suggested this bill go to the Insurance Commissioner for further clarification. The Chair closed the hearing.

Hearing on

**SB 137 - Viatical act; exemption for acts and orders of securities commissioner.**

The Chair called Erin Hoestje, Associate General Counsel, Office of the Securities Commissioner, who testified in support of **SB 137**. Ms. Hoestje stated that **SB 137** amends K.S.A. 2008 Supp 40-5012a(f), to include National Conference of Insurance Legislatures (NCOIL) Life Settlements Model Act language on page 3, line 36 of the bill which states, "this act shall not preempt, supersede, or limit any provision of any state securities law or any rule, order or notice issued thereunder." She said the statute already provides for preservation of our authority to investigate, examine and prosecute violations of law. She said there is no clear preservation of the administrative authority of the Securities Commissioner. She noted that failure to include this language will leave the Securities Commissioner in the awkward position of having to either ignore minor violations of the Kansas Uniform Securities Act or engage in criminal prosecution. (Attachment 6)

The Chair closed the hearing on **SB 137.** Senator Kelsey moved to pass **SB 137** out favorably. Senator Brownlee seconded. Motion passed. The Chair said **SB 137** will be placed on the Consent Calendar.

The next meeting is scheduled for February 9, 2009.

The meeting was adjourned at 10:20 a.m.

**FINANCIAL INSTITUTIONS & INSURANCE COMMITTEE GUEST LIST**
**DATE:** 2-5-09

| NAME | REPRESENTING |
|---|---|
| Anne Spiess | American Cancer Society |
| Erin Hoeflich | KSC |
| Bill Sneed | State Farm |
| LARRY MAGILL | KAIA |
| KERRI SPIELMAN | KAIA |
| John Meetz | KID |
| Lori Church | KAPCIC |
| Shanelle Dupree | KHPA |
| Leigh Kleck | Hein Law firm |
| Casey Halsey | JE Dunn Const. Co. |
| DAN MORGAN | Builders' Assn. & KC Chapter, AGC |
| Sandy Braden | NAIFA KS |
| John Peterson | Capitol Strategies |
| Natalie Haag | Security Benefit |
| Eric Stafford | AGC of KS |
| Haley DaVee | KCMA |
| Kari Presley | Kearney & Associates |
| Alex Kotogiantz | P.I.A. |
| Dan Murray | NFIB / Federico |
| Richard B. Usher | Hill & Usher |
| Tom Burgess | American Subcontractors Assn. |
| Ken Keller | Western Surety Co / ASA |
| | |
| | |

# MIDWEST CRANE AND RIGGING

15585 S. KEELER • P.O. BOX 970 • OLATHE, KANSAS 66051-0970
(913) 747-5100 • FAX (913) 764-0102

Feb. 5th, 2009

To: The Senate Financial Institutions and Insurance Committee

Re: SB 126 The controlled insurance programs act

Chairman Ruth Teichman, Vice Chair Karin Brownlee, and Committee

My name is Bill Miller. I am here to testify in support of SB-126.

I represent the American Subcontractors Association and my business, Midwest Crane and Rigging, LLC.

Midwest Crane is headquartered in Olathe, Kansas with offices in Topeka, Kansas and St Joseph, Missouri

ASA represents subcontractors and suppliers in Kansas and Western Missouri...

Owner or contractor controlled insurance programs, commonly referred to as wrap-up policies, have become the number one problem for subcontractors according to a survey completed last summer. Wrap-ups are a relatively new insurance program for the general building construction industry that forces all subcontractors on a project to give up their own insurance program for that project and, in exchange for the premium that they would have paid; they are covered under one policy furnished by the owner or the general contractor. Participation in these programs is not voluntary.

This on the surface seems innocent enough. This is not at all the truth. These programs have serious deficiencies for the participants and in many cases, for the owner as well.

SB-126 addresses the most serious problems.

1. The program sponsor can cancel the wrap-up policy at any stage of the project. When the wrap-up policy is terminated, each subcontractor is required to purchase like coverage at the same rate that was in effect. This cannot be done. Most general liability policies have a wrap-up exclusion that excludes any coverage if their insured is a participant in a wrap-up. The sub's underwriters will not provide coverage for a part of a project. They would have all of the exposure

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Attachment 1

and a very small premium. This bill prohibits cancellation of the policy unless the subcontractor also has the option of terminating the contract.

2. Completed operations coverage is coverage for resultant damage caused by latent defective work discovered after completion of the project. State law requires 10 years of protection for the owner for this possibility. Many wrap-ups cancel within 2 or 3 years. Since most general liability policies have wrap-up exclusion, and if the subcontractor is no longer is business, the owner is unprotected. This bill requires completed operations coverage to extend for the full term of the statute of repose.

3. Wrap-up policies do not provide coverage for owned or leased equipment on the site. Many wrap-ups do not provide coverage for the liability that a lessee is required to assume in a rental contract. They unknowingly are self insuring the leasing company. This bill requires severability of interests that treats each participant as if they were individually insured and picks up all liability that is required by a contract.

4. Most wrap-up program managers require that the participants insure them for any potential liability for off site activities related to the project. Most general liability policies have wrap-up exclusion and therefore there is no coverage to provide. This is a contractual requirement that cannot be met. This bill prohibits this contractual requirement that is beyond the coverage that is included in the wrap-up policy itself.

5. Some wrap-up policies have denied coverage for damage to a subcontractors work caused by another subcontractor who is also covered under the same policy. The severability of interest provision in this bill requires coverage for this type of claim.

6. Some wrap-up policies that include builders risk coverage could make a claim against a subcontractor for liability for damage to the building or materials for it. The subcontractor has no coverage of their own to cover this. This bill grants a waiver of subrogation to each participant to prevent this type of claim for which there is no coverage.

7. Workers compensation claims are chargeable to each participants experience as an employer which is used to establish the rate of premium based upon experience. This bill requires that the general liability portion reimburse the work comp side for the cost of claims that result from one subcontractor injuring another subcontractor's employee. This then is not charged to the experience rating of the injured workers employer.

8. When a subcontractor is forced to enroll in a wrap-up program, they lose their agent representation. With out their agent, they have no one to represent them to

ensure that they have the coverage necessary to protect them and others for whom they are liable. This is like being in a legal proceeding with out an attorney. This bill does not allow the deduction for the insurance premium to include the agency fee that would have covered the subcontractor's agent for professional services.

9. Most wrap-ups have an unusually high deductible that is passed on to the subcontractor. This results in cheaper premiums for the sponsor at the expense of the subcontractor. This bill does not allow this deductible to be passed on to the subcontractor.

10. Some wrap-up sponsors have disciplinary monetary fines that are assessed against the subcontractors that range up into the thousands of dollars. These fines are at the sole discretion of the contractor or construction manager and can be for perceived unsafe actions that would not be a violation under ordinary government safety standards. This bill would not allow monetary fines to be assessed unless by a government agency.

11. Wrap-up policies require that if a worker is injured, the subcontractor provide alternate duty and keep the injured worker on the payroll even if there is no alternate duty for the injured worker. The subcontractor is assessed a fine of approximately $1500.00 per week it this is not done. This is to keep the program sponsor from paying the temporary disability payments to the injured worker. This bill stops this practice.

12. All wrap-up program managers institute extreme safety programs that are far more stringent that Department of Labor standards. Some are so extreme as to make it nearly impossible to accomplish the work. This can be devastating to a subcontractor who is required to maintain a schedule that has severe daily liquated damages for project delay. This bill requires that the bid documents have detailed safety requirements that will be imposed for work on that site. This will allow the subcontractor to price the job accordingly and to determine if the schedule can realistically be met.

13. Most participants in wrap-up programs can not get claims details and loss history. Subcontractors are responsible for claims monitoring and most want to be involved in case management. This bill requires timely reporting of claims details and loss history to all participants.

14. Self insured retentions are similar to insurance deductibles with one major difference. This SIR must be paid before the insurance company becomes involved in a claim. Some SIRs are $1,000,000 or more. SB-126 requires that the SIR be fully funded for the duration of the state statute to ensure the funds are in fact available to cover the claim.

Please keep in mind that we are not trying to eliminate controlled insurance programs. There are regulations in place for most if not all types of insurance that is sold in Kansas. There are no current regulations that I am aware of to provide the protections that are necessary for the general public and public owners.

Wrap-up programs are necessary in many cases where the required limits are such that it would be cost prohibitive for every contractor and subcontractor to purchase. Unfortunately, these programs have become very lucrative for the very large owners and contractors at the expense of the subcontractors and in some cases at the expense of public owners. It is unusually apparent that on competitive bid projects, wrap-ups are not in use.

I urge your support for SB-126. We are not trying to eliminate wrap-up insurance programs. We want them to be regulated to comply with and provide the coverage that the policies we buy for ourselves provide.

Bill Miller

President
Midwest Crane & Rigging, Inc

# Wrap-Up Coverage Tips for Subcontractors

Richard B. Usher

Richard B. Usher

**Poorly designed** Wrap-Ups increase risk, cost time and money and might even sink contractors and projects. Avoiding uncontrolled, unlimited risks is especially important for subs.

Controlled Insurance Programs (CIPs) consolidate coverage of owners, general contractors and subs for General Liability and often include Workers' Compensation, Builders Risk and other lines.

Owner Controlled (OCIP) and Contractor Controlled (CCIP) Insurance Programs "Wrap-Ups" ostensibly improve efficiency and safety; reduce premiums; heighten transparency; increase coverage certainty (should eliminate some risk transfer); reduce litigation; cover difficult risks; increase participation; and, include Completed Operations coverage.

### CIPs are Not All Created Equal

When designed primarily to protect and enrich Sponsors, CIPs may leave subs seriously exposed.

### Fairer is Smarter

The American Subcontractor's Association (ASA) has a number of documents available that 1) educate subs 2) provide recommendations to level the playing field and 3) help subs remain financially sound.

### A Few Steps in the Right Direction

- **Cross Suits** between/among insureds under the same Wrap-Up are often expressly excluded by blanket cross-liability exclusions, which eliminate coverage for a sub when injured employees of another sub sue for negligence. Remove the exclusion for bodily injury.
- **Damage to the Work** can occur. Subs should be sure the Builders Risk will provide full coverage for damage to their work and/or the Wrap-Up treats them as third parties when they claim other Wrap-Up participants damage their work.
- **Blanket-Mutual Waivers of Subrogation** are problematic when not properly coordinated with coverage under Builders Risk, GL and Workers Compensation.
- **Warranty/Repair Endorsements** allow subs to do post-completion warranty work and other repairs. Without this endorsement on the Wrap-Up, as a sub, insure your GL coverage allows such work on Wrap-Up projects.
- **Sponsor's Termination for Convenience** without a corresponding right for the sub to terminate contract obligations may leave a sub in an untenable position.
- **Sponsor's Failure to fund SIR (Self-Insured Retentions)** leaves subs with significant financial burdens to trigger coverage for completed operations hazard when single-asset-project entities are insolvent.

CIP terms can be onerous. Wise subs evaluate project-insurance requirements before estimating and bidding. Look before you leap.

Exhausting Wrap-Ups is beyond the scope of this introduction. Additional, suggested articles by Richard B. Usher:

"Respond to Wrap-Up Risks With New and Updated ASA Resources." ASA Today. Special Report. January 2008. http://www.hillusher.com/files/Jan_2008_ASA_Today.pdf

"Risk Shifting - A Moral Hazard: Contract Additional Insured and Indemnity Obligations: A Deterrent to Construction Safety and Quality." http://www.corrdefense.org/Academia Government and Industry/B-07.pdf

*Richard B. Usher is principal of Hill & Usher Insurance & Surety, LLC, which specializes in construction insurance and is a full-service, multiple-line, nation-wide, independent agency for business, personal, and professional customers. To reach Richard call 1-800-956-4220. In Arizona: 602-956-4220. rbu@hillusher.com. www.hillusher.com.* <<





Attachment 2

WESTERN EXTRALITE COMPANY
DISTRIBUTORS OF QUALITY ELECTRICAL AND VOICE/DATA PRODUCTS
1470 Liberty St. • Kansas City, MO • 64102

Feb 5, 2009

To: The Senate Financial Institutions and Insurance Committee
Chairman Ruth Teichman and Vice Chairman Karin Brownlee

Madam Chairman

Thank you for allowing me to address you today in support of SB126 the Controlled Insurance Program Act. I'm Ken Keller, retired Controller of Western Extralite Company. I served in that capacity for 21 years. Western Extralite Company is an electrical supply house with a large portion of its business derived from the construction industry. We have 19 locations, 8 of which are in Kansas. In addition I represent the American Subcontractors Association, National Association of Credit Managers, the Electric League of Greater Kansas City and other interested parties.

First let me say I do not oppose the concept of owner or contractor controlled insurance programs, also known as OCIPs and CCIPs and sometimes as wrap-up insurance programs. What I want from this legislation is to make sure the subcontractor has the same protection under this program that he would have under his own insurance coverage.

Currently, that is not the case in some contracts. There are contracts that state coverage will end in 3 years. The statute of repose in Kansas is 10 years. That means you have to find coverage for the remaining 7 years, or be willing to stand the risk of being self-insured. That coverage is not generally available. We can show you examples where coverage was cancelled before the job was complete, leaving the subcontractors with an enormous exposure self insuring the remainder of the work and subsequent risk.

Some contracts call for coverage to cover "on-site" claims only. What happens when the electrical subcontractor sends an employee to Western Extralite for parts and he has an accident? He is not "on-site" therefore he is not covered and the job has been excluded from the regular coverage so where is the coverage? Who's responsible?

Currently if I'm on a job and another subcontractor damages my equipment or work there is a possibility there isn't any coverage. You can't have a claim against another person who is a named insured on the same policy. This position has been tested and upheld in the New York Supreme Court.

Currently, the premium the subcontractor pays into the wrap-up program includes the fee normally paid to his insurance agent to protect his interest. Now getting a copy of the policy for your agent to review is difficult at best. If you can then you have to ask your agent to review the policy to see that you are adequately protected. This results in another fee which is double dipping. This has to be done. Would you enter into a complicated contract without your attorney looking at it? The same should be true of your insurance and your agent.

The current contracts sometime call for monetary fines assessed by the owner or general contractor for safety violations. These are arbitrary and undefendable. These types of fines should only be assessed by the appropriate governmental agency.

The list of potential problems in the wrap-up programs goes on and on. They are addressed and will be corrected by the passage of SB126. I urge your support for this important legislation.

Thank You

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Attachment 3

Kenneth R. Keller
Retired Controller
Western Extralite Company

# HOLBROOK & OSBORN, P.A.

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ESTABLISHED 1980

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February 3, 2009

The Senate Financial Institutions
And Insurance Committee
Chairman Ruth Teichman
State Capitol
Room 241-E B
Topeka, KS 66612

Karin Brownlee
Vice Chairman
State Capitol
Room 136-N
Topeka, KS 66612

Re: Senate Bill 126
The Controlled Insurance Programs Act

Dear Chairman Teichman and Vice-Chair Brownlee and Committee:

My name is Kurt Brack, I am in here to offer testimony in support of Senate Bill 126, The Controlled Insurance Programs Act. I represent a number of subcontractors throughout the Kansas City Metropolitan Area, many of which have recently become involved with OCIPs (Owner Controlled Insurance Programs) and CCIPs (Contractor Controlled Insurance Programs). These programs are typically known as wrap-up programs. Simply stated, wrap-ups are an insurance program on a construction project whereby the owner buys insurance for other participants on the project and the owner ultimately requires participants to reduce their prices by the insurance costs. Under previous practice, each contractor or subcontractor purchased their own insurance in the open market. Typically, for a project that is covered by an OCIP or CCIP, participation in these programs is not voluntary but required. In theory, the owner expects to save money by being able to purchase insurance at a discount and avoiding contractor markup for insurance cost. In addition, the argument goes that if a claim occurs a single insurance carrier can more efficiently handle and process the claim.

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In reality, OCIPs and CCIPs raise a number of disturbing questions, particularly for subcontractors. Senate Bill 126 would address the most serious problems facing contractors in Kansas when confronted with a project covered by an OCIP or CCIP.

1. **Cancellation of Policy During Project.** In the typical OCIP or CCIP policy, the program sponsor can cancel the policy at any time. When this occurs, each subcontractor is required to purchase identical coverage. This is an impossibility. Most commercial CGL policies have a wrap-up exclusion that excluded any coverage if the insured is a participant in a wrap-up plan. Senate Bill 126 addresses this issue by prohibiting cancellation of the policy, once issued, unless the subcontractor also has the option of terminating the contract.

2. **Cancellation of the Policy after the Project is complete.** This is a particularly nasty problem for subcontractors when coverage is terminated prior to the running of the Statute of Limitations or Statute of Repose for claims. Many wrap-ups tend to be terminated within 2 or 3 years, which leaves the subcontractor exposed for an uninsured risk for the remaining period of the Statute of Repose, which could be 7 or 8 additional years. If the subcontractor was out of business, this would also cause an uninsured risk to the owner who would also be unprotected, and thus responsible for the loss. Senate Bill 126 addresses this concern by requiring completed operations coverage for the full term of the Statute of Repose. Therefore, there are no uninsured periods facing either the contractor or owner.

3. **Not all Wrap-ups are equal.** Many wrap-ups do not provide coverage for liability for owned or leased equipment on the job site. In fact, many wrap-up policies specifically exclude liability for owned or leased equipment used on the job site. However, the subcontractor is required to assume such liability in a rental contract if it leases the equipment from a rental company. In the event of loss or damage to the leased equipment, the subcontractor would be stuck with exposure with no coverage. Senate Bill 126 fixes this problem by requiring insurance coverage to match the specific work being performed on the project, including leased equipment.

I recently prepared a presentation of OCIPs and CCIPs to the American Subcontractors Association, Kansas City Chapter. I enclose a copy of this presentation for your review and reference.

I urge you to pass Senate Bill 126 into law to address and correct these and other issues involving Wrap-ups.

Thank you for your attention and courtesy.

Very truly yours,

HOLBROOK & OSBORN, P.A.

Kurt S. Brack

KSB:ld

# GEORGE J. SIEBERS & CO., INC.

BONDS AND INSURANCE

January 30, 2009

Mr. Bill Miller
P.O. Box 970
Olathe, KS 66051

RE: Contractor Controlled/Owner Controlled Insurance Wrap-up Info

DearBill:

As promised, I enclose the comments put together regarding the above referenced subject. We have very serious concerns as to this proposed programs impact on subcontractors.

The name of the game in today's world is volume. These type of programs proposed by general contractors or owners certainly tries to take advantage of this concept in a self serving way by having all of the proposed benefits accrue to themselves for being the buyer of the insurance. In my opinion, this program has serious ramifications to all subcontractors involved as it concerns coverage of the program, cost of the program in terms of administration and service issues that will undoubtedly come up. If the subcontractor does much work at all for the generals or the owners he will have his premium size severely reduced to his normal insurance carrier. I predict that the sub will see increased insurance rates for his or her non-CCIP/OCIP work. With less premium volume, the subcontractor could experience unfavorable loss ratios. I believe that there is a high probability of subcontractors receiving cancellation of their insurance program if things don't fall the right way in terms of premium volume and loss history.

I want to be very clear with an issue that we discussed with you in depth and on e which I have serious concerns. I predict that with a drop in volume of a particular subcontractor's premium size, the insurance company is going to want "something to sweeten the pot" if they are going to accept the risk in some cases. As you know, general liability and umbrella liability are certainly profitable lines for the insurance industry most years for most accounts. Auto and equipment coverage are more volatile and easily show unfavorable results over a period of


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Attachment 5

time. I predict that insurance carriers will insist, especially on good comp risk, that they write the workers comp instead of BASIF or any other plan in order to sweeten the pot. I don't believe that insurance underwriters are going to sit back and give up a big chunk of the profitable lines of the subcontractors account and keep the lines that historically have not been good without adverse consequences.

I also am enclosing a synopsis on OCIPS and CCIPS and all the issue that they present. I see the use of OCIPS & CCIPS having a negative impact on subcontractors in the industry.

Thanking you for your time and interest, I remain.

Very truly yours,

Mark E. Gardner

MEG:bl

After reviewing several proposed CIP (Controlled Insurance Program) that is being put forward by various entities, I offer the following critique. I will try to highlight the major issued with these types of programs, and I am sure there are more serious concerns than what is illustrated here.

First of all, there is nothing good that comes from these programs from the point of view of the subcontractor and his own insurance program. The fact that the program includes General Liability, Umbrella, Worker's Comp coverage severally reduces the size of the subcontractor's own insurance program. This will lead to higher rates simply because there is less insurance premium to work with for the risk. With reduces premiums, a subcontractor will likely have higher loss ratios due to the fact that he maintains coverage 100% of the time for his trucks, equipment, and worker's compensation on those projects. The end result is that the subcontractor faces an increased potential threat of cancellation due too the higher loss ratios and adverse loss experience that might not happen otherwise if the respective general liability and umbrella premium were included in his current insurance program.

The administrative issues that face the subcontractor are significant and raise the subcontractor's cost of handling his own insurance program. In respect to other administrative issues, I offer the following:

1. The insurance program is mandatory, with the potential to reduce payroll volume and increase insurance base rates that are charged by the insurance carriers.

2. Subcontractors will continue to receive audits from their own insurance carriers. Additionally they will be subject to potential audits from the OCIP/CCIP carrier. The administrative burden will be excessive and ultimately, add extra cost to the project.

3. Subcontractors will deal with claim adjuster from their own insurance carriers. Additionally with adjusters from agents/broker and the insurance carrier writing the CIP. Since there is no uniformity between carriers when it comes to reporting and claim handling procedure, subcontractors will have to learn and comply with multiple systems. Report forms will also vary, and this leads to less accurate reporting information

4. Multiple reporting of work comp information to the NCCI will introduce the opportunity for errors. If these errors cause a subcontractor's experience modification rate (EMR) to go up, the subcontractors will pay additional premium

5. When a subcontractor's employees spend time on CIP projects **and** Non-CIP projects during the same week, it will inevitably lead to battles over the location of the injury and which insurance program will respond. Based on the current CIP program language, work **off** of the site will not be included in the CIP plan. How will nearby storage yards, staging areas, and trucking operations be viewed? Will subcontractors tying up rebar cages in a nearby lot be covered?

6. The proposed plan will create a battleground between the CIP's insurance carrier and all others., There will be pressure on subcontractors to report claim situations as listed in the above paragraph under their own insurance program. In return, the insurance carriers for subcontractors will be looking for opportunities to exclude coverage when it is questionable whether the claim is outside of their definition of covered losses.

7. Payroll auditing will involve another layer of people, and usually the CIP programs language does not indicate any motivation general contractors or owners to be timely in it corrections.

8. The subcontractor's field management team will be burdened with extra time needed to meet with loss control representatives not only from the general contractors and their own insurance carrier, but also from the CIP Representative and the providing carrier of the CIP.

9. Subcontractors will be required to know and follow two safety programs, one for the CIP's and one for everything else.

10. Subcontractors will have to maintain their own drug testing program for those employees currently not working on a CIP program. Employees who work on both types of programs will be subjected to twice the potential number of drug tests. While this is not a bad thing, it is definitely a duplication of efforts and a substantial cost in manpower time.

11. Subcontractor will have to provide a separate orientation process to CIP employees. This will cost the subcontractor one to four hours of manpower time, per employee, depending on the depth of training provided.

12. The monthly payroll reporting forms must e separate for each job and due on certain dates of the month. Additional administrative costs will be incurred, and failure to report on time will subject the subcontractor to withholding of payments until required documentation is received. Matter of fact, it acts as a profit center.

13. Subcontractors will be held responsible for lower tier subcontractors. It is difficult enough to get a certificate of insurance from your sub's subcontractors which comply with the limits required on a job. It will be exponentially more difficult to see that the sub's subcontractors comply with all aspects of the program, including the respective cost of the insurance, rates, takeouts, takeout credits, enrollment in the plan with proper documentation provided to each lower tier subcontractors, etc.

14. Failure to complete the sub's subcontractor compliance process will mean that the subcontractor is exposed to no admittance on the job site, pay requests being held up, and no insurance coverage provided by CIP. What kind of notice would the subcontract have that he is no longer covered by the CIP? This is a significant issue.

Often the CIP's reserves the right to include or exclude any subcontractor or sub-subcontractor from the CCIP.

15. Often all the return premiums and dividends that are accrued to the generals or owners, the sub takes part in no cost savings, but has all of the additional incurred administrative costs of the program, there is no advantage to the subcontractor, it is all of the generals or owners.

16. Referring to "Late reporting of claims; the employer/employee does not report an incident in a timely manner, coverage may be denied under the CIP program. This will result in Subcontractor being responsible for payment of any medical or indemnity benefits accrued. Despite the subcontractor's best efforts to encourage/demand prompt claims reporting, it will be the subcontractor who will eat the interim cost of a claim. There will be no opportunity to recoup this cost from the subcontractor's non-CIP carrier, since this carrier will likely exclude any CIP covered employees from coverage.

17. In reference to filing the work comp experience with the NCCI or CIPS, CIPS have a poor reputation for delayed reporting. Any miscalculated modifications or disputes will be a problem, for the subcontractor. In fact, the proposed CIP plan has set criteria which have not been divulged in the document that was received.

18. Often times each subcontractor is required to establish a written safety program and to provide a designated safety representative who will be on site when any work is in progress. Minimum standards for subcontractor's safety programs is that often of the general contractor's safety and health manual, thus maintaining two separate safety programs as well as two separate safety directors.

19. Often time there is question as to how the limits of underlying coverage is provide, is it for each sub due to the separation of insureds or how do they work.

20. The program will often state that the subcontractor will send information to the agent or broker . This provision will not sit well with the subcontractor's existing insurance agency. The existing agencies do not see the general contractor sharing its payroll or vital insurance records with subcontractors, or with other competing agencies. The provisions make it convenient for the agent or broker to use the information for sales calls.

In summary, I believe that it is very questionable whether there is any cost savings achieved in forming CIP programs. The idea that subcontractors would exclude 100% of their insurance cost from their bids on the projects, in turn, will negatively impact the subcontractor's insurance cost is difficult to believe. The increased costs to subcontractors will include higher rates, higher loss ratios and adverse loss experience. These results will increase their chances of being cancelled by their own insurance carriers. Subcontractors have spent significant time and money, over the multiple years, working to perfect and protect their insurance program and safety record, Their

collective goal has been to ensure bids with the lowest possible insurance cost. If this idea is transferred to the CIP so that the general contractor can clip the savings that are otherwise earned by the subcontractor, then the economic incentive is certainly in jeopardy. Will subcontractor's actions be for the benefit of the general contractor, or for themselves? It is difficult to believe that any subcontractor will subsidize the general contractor's work by charging higher insurance cost to other generals and/or owners outside the work they do for the general contractors of CIP programs. To think so is pure folly.

As mentioned before, it is difficult to see the beauty in a program where work comp is covered by the CIP on certain size jobs and not covered on other size jobs. A subcontractor's insurance program needs to be seamless in terms of looking to one insurance carrier for a particular line of insurance, whether it is a private carrier, BASIS, o other. Having multiple carrier for the same line of coverage will ultimately lead to confusion for **all** parties. Construction employees move from job to job, and to movie in and out of a coverage area in the course of a day's work will cause many disputes. We fear that the subcontractor will lose most of these disputes.

We believe it will be difficult to get the subcontractor's insurance carrier to be excess over a program such as a CIP , and this will lead to holes in the subcontractor's insurance program. Coverage "holes" will lead to more "out of pocket" or "uninsured" expenses for the subcontractor.

To carry that idea one step further, an uninsured loss will certainly impact the financial stability of the subcontractor, which, in turn will impact his bonding and bank credits. This becomes a direct threat to the financial stability of the subcontractor.

In this country, we have an economic incentive to do things, and we distance ourselves from those things that aren't economically sound. Success can be measured and usually has a positive result year end and year out. It has been my experience that our contractors take immense pride in their safety program and their reduced insurance cost. They fully understand that the larger they are, the more volume credits they earn. The safer their program is, the more competitive their rates are. They vigorously defend their program from people who try to claim questionable losses. They have already passed on the savings to the respective entity who they bid to, whether it is the general contractor or owner directly. They continue to assume that they can earn those low rates and keep their safety program favorably intact so as to complete future work under hard money bid and not be over budget on their insurance and safety costs. It is painful to think that genera contractors or anyone else would take advantage of their subcontractors by clipping a coupon for "buying the insurance" and not recognize the tremendous negative impact it has on the subcontractor. Furthermore, to expect **all** subcontractors to just lay down and turn over their policies, rates, and payrolls to an outside third part whom they chose **not** to give it to in the first place is again very misguided. As far as I am concerned, everyone works hard to maintain confidentially in our modern world to comply with all of the privacy act requirements.

KANSAS

OFFICE OF THE SECURITIES COMMISSIONER

KATHLEEN SEBELIUS, GOVERNOR
CHRIS BIGGS, COMMISSIONER

**TESTIMONY IN SUPPORT OF SENATE BILL No. 137**
**Senate Financial Institutions and Insurance Committee**

**Erin Hoestje, Associate General Counsel**
**Office of the Securities Commissioner**
**February 5, 2009**

Madaam Chair and Members of the Committee,

The Office of the Securities Commissioner investigates and takes administrative, civil and criminal action related to securities law violations throughout the State of Kansas. Many of our cases involve alternative investment products, including viatical investments.

We have brought over a dozen cases related to viatical investments and returned in excess of $1,000,000 to Kansas investors. We have also worked in cooperation with the Kansas Department of Insurance to limit further damage to Kansans. The North American Securities Administrators Association (NASAA), of which we are a member, has cooperated with state insurance regulators to provide, seamless, non-duplicative, regulation of viatical products. Senate Bill 137 continues these efforts by clarifying the preservation of the Securities Commissioner's authority to investigate violations of the Kansas Uniform Securities Act involving viatical investments and utilize a full range of legal consequences appropriate to the violation.

Senate Bill 137 amends K.S.A. 2008 Supp 40-5012a (f), to include the following National Conference of Insurance Legislatures (NCOIL) Life Settlements Model Act language found at page 3, line 36, of the bill which states that this act shall not:

> …(2) preempt, supersede, or limit any provision of any state securities law or any rule, order, or notice issued thereunder;

The statute already provides for preservation of our authority to investigate, examine and **prosecute** violations of law. There is no clear preservation of the **administrative** authority of the Securities Commissioner. Failure to include this language will leave the Securities Commissioner in the awkward position of having to either ignore minor violations of the Kansas Uniform Securities Act or engage in criminal prosecution.

With this addition, we can continue to effectively protect Kansas investors. Thank you for your consideration and we would specifically request that the committee favorably pass Senate Bill 137.

FI&I Committee
2-5-09
Attachment 6

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