

SB2463

SD1

LATE

TESTIMONY



**STATE OF HAWAII
STATE PROCUREMENT OFFICE**

P.O. Box 119
Honolulu, Hawaii 96810-0119
Telephone: (808) 587-4700
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TESTIMONY
OF
SARAH ALLEN, ADMINISTRATOR
STATE PROCUREMENT OFFICE

TO THE SENATE COMMITTEE
ON
JUDICIARY AND LABOR

February 25, 2014, 10:30 a.m.

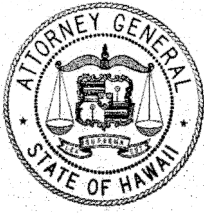
SB 2463, SD1

RELATING TO PROCUREMENT

Chair Hee, Vice-Chair Shimabukuro, and members of the committee, thank you for the opportunity to submit testimony on SB2463, SD1.

The State Procurement Office supports this bill with reservations.

Thank you.



**TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
TWENTY-SEVENTH LEGISLATURE, 2014**

ON THE FOLLOWING MEASURE:

S.B. NO. 2463, S.D. 1, RELATING TO PROCUREMENT.

BEFORE THE:

SENATE COMMITTEE ON JUDICIARY AND LABOR

DATE: Tuesday, February 25, 2014 **TIME:** 10:30 a.m.

LOCATION: State Capitol, Room 016

TESTIFIER(S): David M. Louie, Attorney General, or
Stella M.L. Kam, Deputy Attorney General

Chair Hee and Members of the Committee:

The Department of the Attorney General supports this bill.

This bill provides that the requirement for contractors licensed under chapter 444, Hawaii Revised Statutes (HRS), to defend a governmental body, or its officers, employees, or agents from claims arising out of the contractor's performance under the contract shall not extend beyond the expiration of the time limitation in section 657-8, HRS.

This bill contains the revisions that were provided by the Department of the Attorney General to the Senate Committees on Economic Development, Government Operations and Housing and Commerce and Consumer Protection.

We respectfully ask the Committee to pass this bill.

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Website: www.gcawhawaii.org



GCA of Hawaii

GENERAL CONTRACTORS ASSOCIATION OF HAWAII

Quality People. Quality Projects.

Uploaded via Capitol Website

February 25, 2014

TO: HONORABLE CLAYTON HEE, CHAIR, HONORABLE MAILE SHIMABUKURO, VICE CHAIR AND SENATE COMMITTEE ON JUDICIARY AND LABOR

SUBJECT: **SUPPORT & PROPOSED S.D.2 AMENDMENTS TO S.B. 2463, S.D.1, RELATING TO PROCUREMENT.** Provides that the requirement for persons licensed under chapter 444, Hawaii Revised Statutes, to defend a governmental body, or its officers, employees, or agents from claims arising out of the contractor's performance under the contract shall not extend beyond the expiration of the time limitation in section 657-8, Hawaii Revised Statutes. Takes effect 7/1/2050. (SD1)

HEARING

DATE: Tuesday, February 25, 2014
TIME: 10:30 a.m.
PLACE: Conference Room 016

Dear Chair Hee, Vice Chairs Shimabukuro and Members of the Committee,

The General Contractors Association of Hawaii (GCA) is an organization comprised of approximately six hundred general contractors, subcontractors, and construction related firms. The GCA was established in 1932 and is the largest construction association in the State of Hawaii. The GCA's mission is to represent its members in all matters related to the construction industry, while improving the quality of construction and protecting the public interest.

The GCA is in support of the intent of the current version of S.B. 2463, SD1, but would request the Committee's consideration of the attached Proposed Amendments being requested by interested stakeholders. The original version of the bill, S.B. 2463 would have no longer required government contractors, both design professionals and construction contractors to defend the state prior to negligence being established. However, after the previous Senate Committees amendments and upon review of the current SD1 version, interested stakeholders are proposing the attached Exhibit A for the Committee's consideration.

Stakeholders Proposed Amendments

The proposed amendments do not preclude the contractor's obligation to indemnify the state in the event that there is a judgment finding fault on part of the contractor. The purpose of the Proposed Amendments is to address the ongoing uneven application of the duty to defend clause in government contracts among both design professionals and construction contractors. The attached draft includes two separate provisions to apply to design professionals and construction contractors with regard to the duty to defend. First, the provision applicable to design professionals would prohibit governmental procurement contracts of any amount that are

exclusively for the services of engineers, architects, surveyors, or landscape architects, from requiring the person to defend the governmental body against liability not arising from the contractor's own negligence or fault. Second, the provision applicable to construction contractors, which is meant to include both prime contractors and subcontractors, would limit a construction contractor's requirement to defend the governmental body for the warranty period up to a maximum of one year after final acceptance. The limit of the duty to defend clause for those licensed under Chapter 444, HRS recognizes that to require defense of the state beyond the owner's acceptance of the project and a reasonable contractor's warranty period would be overly burdensome.

The GCA believes that a construction contractor for a state project should be limited in its defense requirements of the state prior to negligence being established. The duty to defend is executed by contract between the contractor and the government agency. A contractor's duty to defend the state has been unevenly applied absent a clear statute indicating whether it was required or not. Some agencies may require the duty to defend as part of their General Conditions in a contract, and others may not. Due to the absence of the duty to defend obligations in current law, state and county agencies may apply it inconsistently, which provides uncertainty for contractors doing public works projects.

In an effort to ensure fairness, GCA believes the attached proposed draft provides a consistent clarification for all state and county agencies to follow.

GCA **supports the attached Proposed Amendments** to S.B. 2463, SD1 and we respectfully request that this Committee pass the measure as requested.

A BILL FOR AN ACT

RELATING TO PROCUREMENT.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

SECTION 1. The legislature finds that contracts for public works often include a duty to defend clause, requiring the contractor to defend governmental entities before the contractor's negligence or fault is determined.

Designing and constructing public works projects are unique among services procured by the government. Public agencies have a strong involvement in budgeting and scoping services and working in collaboration with the contractor. Public works often involve large risks due to site circumstances, public environmental concerns and high public usage. Highways and public buildings have necessarily long service lives relative to other services procured, thereby increasing contractor risk beyond that of other government contracts.

Design professionals licensed under HRS chapter 464 are able to obtain professional liability insurance that covers the contractor for indemnifying the government; however, the insurance industry does not provide reasonable coverage for another party's defense costs if the design professional is not negligent. Thus, the legislature finds that design professional contractors should not be burdened with the duty to defend a governmental body before the contractor's negligence or fault is determined.

Further, the legislature finds that requiring a construction contractor licensed under HRS chapter 444 to defend the public agency beyond the owner's acceptance of the project and a reasonable contractor's warranty period is overly burdensome. Thus, the legislature finds that any contractual requirement to defend the governmental body by a construction

contractor should be limited to the construction and warranty period up to a maximum of one year after final acceptance.

Upon determination of negligence or fault the contractor may still be required to indemnify and hold harmless the governmental body from claims arising out of or resulting from the negligent, reckless, or wrongful acts, errors, or omissions of the contractor. Further, this legislation is not intended to restrict the ability of a government agency to require a construction contractor to provide general liability insurance coverage for a particular project, either independently or as an additional insured under the contractor's policy, for the protection of governmental body, its officers and employees.

The legislature further finds that, while some state and county agencies recognize the negative implications and have removed the duty to defend clause, inconsistency between agencies and departments still exists. The legislature further finds that the clause is detrimental in the long term by negatively affecting competition for contracts and innovation. The purpose of this Act is to standardize differing contract conditions regarding the duty to defend clause by prohibiting defense clauses in contracts entered into by persons licensed under HRS chapter 464, and to provide certain limits on the duty to defend for persons licensed under HRS chapter 444.

SECTION 2. Chapter 103D-713, Hawaii Revised Statutes, is amended to read as follows:

"~~[+]§103D-713[+]~~ **Defense of a governmental body.** (a) ~~Beginning July 1, 2014, [N]no contract [of less than \$1,000,000] that is entered into [on or after July 1, 2007,] by any governmental body, and is exclusively for services that may only lawfully be provided by~~ with a person licensed under chapter 464, HRS ~~may~~ shall require the contractor to defend the governmental body, or its officers, employees, or agents, from any liability, damage, loss, or claim, action, or proceeding arising out of the contractor's performance under the contract.

(b) Beginning July 1, 2014, the requirement for a person licensed under chapter 444, HRS to defend the governmental body, or its officers, employees, or agents, from any liability,

damage, loss, or claim, action, or proceeding arising out of the person's performance under the contract shall not extend beyond the owner's final acceptance of the project and the contractor's warranty period up to a maximum of one year after final acceptance.

(~~[b]~~[c]) Subsections (a) and (b) notwithstanding, the contract may require the contractor providing the services to indemnify and hold harmless the governmental body and its officers, employees, and agents from and against any liability, damage, loss, cost, and expense, including reasonable attorneys' fees, and all claims, suits, and demands therefore arising out of or resulting from the negligent, reckless, intentional, or wrongful acts, errors, or omissions of the contractor, the contractor's employees, officers, agents, or subcontractors in the performance of the contract or the contractor's professional services, and the provisions may remain in full force and effect notwithstanding the expiration or early termination of the contract.

(~~[e]~~[d]) No person licensed under chapter 464 that has agreed in any contract to defend a governmental body, including those contracts entered into before or after July 1, 2007, shall be required to defend the governmental body in a lawsuit filed more than ten years beyond the [~~substantial completion~~] owner's final acceptance of the project, except that this subsection shall not apply to any lawsuit that has been filed prior to July 1, 2007.

(~~[d]~~[e]) As used in this section, "person" means any person, partnership, corporation, or other entity conducting business in the State.

SECTION 3. Statutory material to be repealed is bracketed and stricken. New statutory material is underscored.

SECTION 4. This Act shall take effect on July 1, 2014.

BIA-HAWAII

BUILDING INDUSTRY ASSOCIATION

THE VOICE OF THE CONSTRUCTION INDUSTRY

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Stephen Hanson

simplicityHR by ALTRES

TESTIMONY TO THE SENATE COMMITTEE ON JUDICIARY AND LABOR

TUESDAY, FEBRUARY 25, 2014

10:30 A.M.

HAWAII STATE CAPITOL - ROOM 016

SUBJECT: S.B. 2463 - RELATING TO PROCUREMENT

Dear Chair Hee, Vice-Chair Shimabukuro, and members of the Committee:

My name is Gladys Marrone, Government Relations Director for the Building Industry Association of Hawaii (BIA-Hawaii), the Voice of the Construction Industry. We promote our members through advocacy and education, and provide community outreach programs to enhance the quality of life for the people of Hawaii. BIA-Hawaii is a not-for-profit professional trade organization chartered in 1955, and affiliated with the National Association of Home Builders.

BIA-Hawaii **supports the intent** of S.B. 2463 S.D. 1, which provides that the requirement for persons licensed under chapter 444, Hawaii Revised Statutes, to defend a governmental body, or its officers, employees, or agents from claims arising out of the contractor's performance under the contract shall not extend beyond the expiration of the time limitation in section 657-8, Hawaii Revised Statutes. **We recommend this Committee accept the proposed changes as outlined in the draft language being offered by stakeholders.**

The costs involved in defending the state prior to a contractor's fault being determined can be costly. The proposed language, agreed to by industry stakeholders, would no longer require government contractors, licensed under Chapter 464, Hawaii Revised Statutes, to *defend* the state prior to negligence being established.

For contractors licensed under Chapter 444, HRS, however, proposed is a one-year limit, after the owner's final acceptance of the project, on their duty to defend.

The proposed language would not preclude the contractor's obligation to *indemnify* the state in the event that there is a judgment finding fault against the contractor. S.B. 2463, S.D. 1, as well as the proposed draft, would make it the responsibility of each party named in a suit, which would include the state as a party, to cover the initial defense costs prior to negligence being established.

Some state and county agencies recognize the duty to defend clause as detrimental and have removed it from their contracts. The draft proposal would bring government contracts into uniformity by prohibiting defense clauses in contracts that are entered into by persons licensed under Chapters 444 and 464, Hawaii Revised Statutes.

Based on the foregoing reasons, BIA-Hawaii **supports the intent** of S.B. 2463, S.D. 1, **with the recommended amendments in the proposed draft.**

We appreciate the opportunity to share with you our views.

SAH - Subcontractors Association of Hawaii

*1188 Bishop St., Ste. 1003**Honolulu, Hawaii 96813-2938*

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February 25, 2014

Testimony To: Senate Committee on Judiciary and Labor
Senator Clayton Hee, Chair

Presented By: Tim Lyons
President

Subject: S.B. 2463, SD 1 - RELATING TO PROCUREMENT

Chair Hee and Members of the Committee:

I am Tim Lyons, President of the Subcontractors Association of Hawaii. The SAH represents the following nine separate and distinct subcontracting organizations which include:

HAWAII FLOORING ASSOCIATION
ROOFING CONTRACTORS ASSOCIATION OF HAWAII
HAWAII WALL AND CEILING INDUSTRIES ASSOCIATION
TILE CONTRACTORS PROMOTIONAL PROGRAM
PLUMBING AND MECHANICAL CONTRACTORS ASSOCIATION OF HAWAII
SHEETMETAL CONTRACTORS ASSOCIATION OF HAWAII
PAINTING AND DECORATING CONTRACTORS ASSOCIATION
PACIFIC INSULATION CONTRACTORS ASSOCIATION
ELECTRICAL CONTRACTORS ASSOCIATION OF HAWAII

We generally support this bill but we are vitally in need of an amendment that will extend coverage to subcontractors on government jobs. As we read the language in this bill, we find that it is only the "contractor's performance under the contract" which has a limitation beyond the time limitation with the governmental body that is covered. It is typical that only the prime contractor enters into the contract with the government and there may be as many as 15 or 16 other subcontractors who each enter into a separate contract directly with the prime contractor. It is our feeling that these individuals must be accommodated as well, but the reference to "the contract" might easily be interpreted as only the "contract" between government and the prime. Therefore, we support the amendment provided by the Hawaii Insurer's Council which clarifies that to "any subcontractor's performance pursuant to the contract".

In the absence of doing that, we find that it is entirely possible that the prohibition will protect the prime contractor, the engineer, the architect, the surveyor or the landscape architect but not any of the subs thereby leaving them to "stand alone" in any lawsuit.

Based on the above, we respectfully request your amendment to this bill.

Thank you.



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February 24, 2014

Senate Committee on Judiciary and Labor: Honorable Senator Clayton Hee, Chair; Maile S.L. Shimabukuro, Vice Chair; and Members of the Committee

Subject: TESTIMONY IN SUPPORT (with proposed revisions) of SB 2463,
Relating to Procurement
Hearing: Tuesday, February 25, 10:30 a.m., Conference Room 16

Dear Chair Hee, Vice Chair Shimabukuro and Members of the Committee:

We are in support of this bill, with the revisions proposed by the American Council of Engineering Companies. Our firm provides engineering consultation services for a number of State and County projects. The situation of government contracts for design professionals is out of control. Attorneys General and County Corporation Counsels have put into place unfair contract language without understanding the impact on our firms. They want to be able to tap into our insurance policies so the government doesn't have to pay for lawsuits. The problem is that these terms create liability that is not covered by our professional liability insurance.

A design professional's PLI only covers harm caused by the design professional's negligence; it will not advance the cost of defending other parties before the negligence of the design professional is established, and will not cover damages caused by other parties. The current contract language provides an unacceptable risk, especially considering that we design professionals are personally liable, and that this liability follows us into retirement.

Since the State and its citizens derive much more benefit from public works projects than design professionals, requiring design firms to defend the State in absence of negligence is unreasonable. It is simply not fair to require design professionals to pay for damages or defense costs if they have done nothing wrong. Most states do not have such contract requirements, and other states have recently revised their contract language to bring fairness to public contracts. We note that the contract would continue to require us to indemnify and pay attorney's fees if we are found to be negligent.

Our company provides excellent service to government entities, but we struggle with making the decision to conduct government work under these terms, and we won't accept these contract terms for high-risk projects. This bill benefits the State and its citizens by encouraging greater participation by qualified firms such as ours. We respectfully urge you restore fairness to government contracts and to pass this bill. Thank you for an opportunity to express our views in SUPPORT of this bill, with revisions.

Respectfully submitted,

A handwritten signature in black ink that reads 'COREY MATSUOKA' in all caps, written in a cursive style.

Corey Matsuoka, P.E., PMP, LEED AP
Principal

From: mailinglist@capitol.hawaii.gov
To: [JDLTestimony](#)
Cc: sawonglaw@hawaii.rr.com
Subject: Submitted testimony for SB2463 on Feb 25, 2014 10:30AM
Date: Monday, February 24, 2014 7:49:04 PM
Attachments: [InsuranceFactors"CommentsToSB2463.SD1.02252014.pdf](#)

SB2463

Submitted on: 2/24/2014

Testimony for JDL on Feb 25, 2014 10:30AM in Conference Room 016

Submitted By	Organization	Testifier Position	Present at Hearing
Sandie Wong	Insurance Factors	Comments Only	No

Comments: Please find attached a letter from Insurance Factors' re: background on design professionals' lack of insurance coverage for defend clauses in contracts.

Please note that testimony submitted less than 24 hours prior to the hearing, improperly identified, or directed to the incorrect office, may not be posted online or distributed to the committee prior to the convening of the public hearing.

Do not reply to this email. This inbox is not monitored. For assistance please email webmaster@capitol.hawaii.gov

February 24, 2014

Ms. Janice Marsters
Kennedy/Jenks Consultants
3375 Koapaka St., Suite F227
Honolulu, HI 96819

Dear Janice:

A Professional Liability policy purchased by a design professional is a legally binding contract between the insured and the insurance company. The nature of the policy is to cover a negligent act, error or omission committed by the design professional in performing the professional's services. Insurers have a duty to defend their insured, the design professional for wrongful acts committed by the designer. Professional liability insurance policies do not extend coverage or defense to additional insureds.

Many contracts will include an Indemnification clause requiring that the design professional defend the Client. This can pose a problem to the design professional as it is in opposition of what the policy provisions will provide. If the design professional accepts the Indemnification clause and agrees to defend the Client, the design professional is opening themselves up to personal loss because they are agreeing to something that the insurance policy will not provide.

Please feel free to contact me should you have any questions.

Very truly yours,



Valerie Moss, CIC
Vice President



February 24, 2014

Dear Sir or Madam:

I am writing in connection with two bills being considered by the Hawaii State Legislature: SB2463 and HB2047. These bills are being advocated by several design professional organizations in Hawaii, including the American Council of Engineering Companies of Hawaii, the American Institute of Architects Hawaii State Council, the Hawaii Chapter of the American Society of Civil Engineers, and the Coalition of Hawaii Engineering and Architectural Professionals.

Specifically, I understand that there is confusion regarding whether design professionals' professional liability insurance provides coverage for (i) non-negligent acts, and (ii) defense of the design professional's client. I would like to help clarify these issues, and I can speak to them with some authority, as I have over twenty years' experience working with design professionals as an attorney in private practice, a claim supervisor for a major insurer of design professionals, and as a broker specializing in insurance coverage and risk management for design professionals.

A design professional who indemnifies the client for damages caused by its negligent acts, errors, and omissions can be reasonably sure that its promise will have coverage under its professional liability insurance policy. But an indemnity for non-negligent performance likely will fall outside of the coverage grant of the professional liability insurance policy. The reason for this is that professional liability policies exclude coverage for "liability assumed by contract" unless the design professional would have been liable in the absence of contract. The law makes the design professional responsible for its negligence, whether or not the contract says so – and so a design firm's indemnity for damages caused by its own negligence is covered. But indemnifying the client for non-negligent acts, or for damages caused by other parties, is an obligation assumed by contract for which the design firm would not otherwise be liable, and thus triggers this exclusion.

Regarding defense expenses, professional liability policies will pay to defend the policyholder, but not the client or other parties not insured on the policy. This is a stark difference from commercial general liability policies and other coverages with which clients are familiar; those policies will allow the client to be named as an additional insured and thus entitled to a defense under certain conditions. This is not done on professional liability policies. If the policyholder is adjudged negligent, and the client's defense costs are part of the legal damages owed by the policyholder, the policy will in all likelihood cover those costs. But the policy will not pay to defend the client until and unless (i) the policyholder is found to be negligent and (ii) the client's defense costs constitute legal damages owed by the policyholder on account of that negligence.

In the world of insurance, it is dangerous to say "never," and there almost certainly are some carriers who might offer broader coverage, perhaps to a very large firm with a very good claims history. But the



overwhelming majority of design professionals cannot procure such coverage. For these design professionals, an indemnity clause that requires them to “defend” their client or to indemnify for non-negligent performance lacks insurance coverage and may well be a “bet the firm” proposition for that design professional. This uninsured – and, for all but a few, uninsurable – promise puts client and design professional both at risk.

I would be pleased to discuss this further, at your request.

Yours truly,

A handwritten signature in black ink, appearing to read "Karen Erger".

Karen Erger

Vice President and Director of Practice Risk Management

kerger@lockton.com

319-389-0312