

SUNSET EVALUATION REPORT
CONTRACTORS
Chapter 444, Hawaii Revised Statutes

A Report to the Governor and the Legislature of the State of Hawaii

Submitted by the
Legislative Auditor of the State of Hawaii

Report No. 83-3
January 1983

FOREWORD

Under the "sunset law," licensing boards and commissions and regulated programs are terminated at specified times unless they are reestablished by the Legislature. Nationally, the first sunset law was passed in 1976. Within three years, 30 more states had enacted similar legislation. The rapid spread of sunset legislation reflects increasing public concern with what it sees as unwarranted government interference in everyday activities.

Hawaii's Sunset Law, or the Hawaii Regulatory Licensing Reform Act of 1977, scheduled for termination 38 occupational licensing programs over a six-year period. These programs are repealed unless they are specifically reestablished by the Legislature. In 1979, the Legislature assigned the Office of the Legislative Auditor responsibility for evaluating each program prior to its repeal.

This report evaluates the regulation of contractors under Chapter 444, Hawaii Revised Statutes. It presents our findings as to whether the program complies with the Sunset Law and whether there is a reasonable need to regulate contractors to protect public health, safety, or welfare. It includes our recommendation on whether the program should be continued, modified, or repealed.

Our approach to the evaluation of the regulation of contractors is described in Chapter 1 of this report under "Framework for Evaluation." That framework is also used for all our other sunset evaluation reports. It is based on the policies enunciated by the Legislature in the Sunset Law. The first and basic test we applied was whether an identifiable danger to public health, safety, or welfare could result from the conduct of the occupation or profession being regulated. Then the other criteria for the evaluation were applied.

We acknowledge the cooperation and assistance extended to our staff by the Contractors License Board, the Department of Commerce and Consumer Affairs, and other officials contacted during the course of our examination.

Clinton T. Tanimura
Legislative Auditor
State of Hawaii

January 1983

TABLE OF CONTENTS

<i>Chapter</i>		<i>Page</i>
1	INTRODUCTION	1
	Objective of the Evaluation	1
	Scope of the Evaluation	1
	Organization of the Report	1
	Framework for Evaluation	2
2	BACKGROUND	7
	Occupational Characteristics	7
	Origins and Development of Regulation	9
	History of Regulation in Hawaii	11
	Nature of Regulation	13
3	EVALUATION OF THE REGULATION OF CONSTRUCTION CONTRACTORS	17
	Summary of Findings	17
	The Need for Regulation	18
	Regulatory Operations	20
	Licensing Classifications	27
	Complaints Management	37
	Recovery Fund	41
	Conclusion	42
	Recommendations	43
	Appendix: Responses of Affected Agencies	45

LIST OF TABLES

<i>Table</i>		<i>Page</i>
3.1	Classifications of Specialty Licenses	30
3.2	C-68 Subspecialty Classifications	34

Chapter 1

INTRODUCTION

The Hawaii Regulatory Licensing Reform Act of 1977, or Sunset Law, repeals statutes concerning 38 state licensing boards and commissions over a six-year period. Each year, six to eight licensing statutes are scheduled to be repealed unless specifically reenacted by the Legislature.

In 1979, the Legislature amended the law to make the Legislative Auditor responsible for evaluating each licensing program prior to its repeal and to recommend to the Legislature whether the statute should be reenacted, modified, or permitted to expire as scheduled. In 1980, the Legislature further amended the law to require the Legislative Auditor to evaluate the effectiveness and efficiency of the licensing program, even if he determines that the program should not be reenacted.

Objective of the Evaluation

The objective of the evaluation is: To determine whether, in light of the policies set forth in the Sunset Law, the public interest is best served by reenactment, modification, or repeal of Chapter 444, Hawaii Revised Statutes.

Scope of the Evaluation

This report examines the history of the statute on licensing of contractors and the public health, safety, or welfare that the statute was designed to protect. It then assesses the effectiveness of the statute in preventing public injury and the continuing need for the statute.

Organization of the Report

This report consists of three chapters: Chapter 1, this introduction and the framework developed for evaluating the licensing program; Chapter 2, background information on the regulated industry and the enabling legislation; and Chapter 3, our evaluation and recommendation.

*NOTE: Originals for pages 2-5 are filed with Report No. 83-7,
Sunset Evaluation Report, Real Estate Brokers and Salesmen,
Chapter 467, Hawaii Revised Statutes.*

Chapter 2

BACKGROUND

Contractors in Hawaii are governed by Chapter 444, Hawaii Revised Statutes. They have been regulated since 1957 when the Legislature restricted the business of contracting to those licensed by the Contractors License Board. Numerous amendments have been made to the law since then, and Hawaii now stands among those states which have relatively extensive provisions governing contracting activity.

Occupational Characteristics

Unlike other professional fields, contractors do not have common educational or experience backgrounds that prepare them for contracting. Educational backgrounds may range from grade school to graduate college degrees. Experience backgrounds reflect a similar diversity.

General knowledge of construction methods is a first requirement. Contractors must also have some basic comprehension of the law and legal obligations as they deal, of necessity, with contracts. In addition, to be successful as a business, contracting demands such capabilities as those needed for salesmanship and contract negotiations, for financing and accounting, for managing personnel and for coordinating numerous field operations.

In addition, construction activities and the resulting products come under numerous regulations by local, state, and federal levels of government. These range from zoning to building codes, from environmental impact statements to occupational safety and health stipulations. Failure to comprehend and comply with these regulations can easily ruin a contractor. These demands may account for the high rate of bankruptcies in the occupation. In the mid-1970s, 20 percent of Hawaii's bankruptcy cases came from the construction industry.¹

A recent study on construction contracting describes contractors this way:

“The contractor is that party who brings together all of the diverse elements and inputs of the construction process into a single, coordinated effort. He may be responsible for constructing the entire project, in which case he is

1. Connell, John, “Proliferation or Planning?” Presentation to the Hawaii Coastal Zone Management Citizens Forum, January, 1976.

referred to as the 'prime' or 'general' contractor. On the other hand, he may function as a subcontractor or specialty contractor, in which case he has responsibility for only a limited aspect of the project. . . .

“The essential function of the contractor is close management control of field operations. Ordinarily, the contractor is in complete and sole charge of his field operations, including the procurement and providing of necessary construction materials and equipment. His chief contribution to the construction process is his ability to marshal and allocate the resources of manpower, equipment, and materials to the project to achieve completion at maximum efficiency of time and cost.”²

The actual activities of those regulated in Hawaii under Chapter 444, HRS, range from businesses involving a single person, such as a rug installer with projects amounting to a few hundred dollars to major corporations engaged in such vast projects as the Honolulu International Airport involving dozens of contractors interlinked in work running into many millions of dollars.

Some contractors specialize in residential work. Others specialize in large scale buildings for commercial, office, and apartment uses. Still others concentrate on producing facilities for industries and utilities. Another form of construction contracting involves public works projects, such as dams, harbors, tunnels, canals, highways, railroads, and airports. While there is some overlap, the differences among these various kinds of construction work are great enough for some states—Oregon and Arizona, for example—to license only certain kinds of contractors, such as residential home builders, and not others.

The industry has a significant impact on both the national and state economy. In the early 1970s, construction accounted for 14 percent of the gross national product.³ In Hawaii, data from the Bank of Hawaii show that projects completed exceeded \$1 billion every year from 1974 to 1980, with the exception of 1977. In 1981, projects completed exceeded \$1.5 billion.⁴

Nationwide, there were about 500,000 construction firms in the late 1970s.⁵ In 1980, there were about 4 million persons working in the construction trades. One out

2. Clough, Richard H., *Construction Contracting*, 3d ed., John Wiley & Sons, 1975, p. 2.

3. *Ibid.*, p. 3.

4. Bank of Hawaii, *Construction in Hawaii, 1982*, Honolulu, p. 2.

5. *The Encyclopedia of Careers and Vocational Guidance*, 5th ed., J. G. Ferguson Publishing Co., 1981, p. 205.

of five was self-employed and contracted with businesses and homeowners for small jobs.⁶ Information from the Department of Commerce and Consumer Affairs (DCCA) shows that Hawaii now has 1,439 licensed general contractors, 1,923 licensed specialty contractors, and 1,973 responsible managing employees who are in charge of contracting corporations.⁷ They employed an average of 22,300 persons in 1981.⁸

The major professional organization for contractors is the Associated General Contractors of America with members from a wide range of construction firms. The National Association of Home Builders actively represent the housing industry. In addition, there are the National Constructors Association, Associated Builders and Contractors and various specialty organizations.⁹

Origins and Development of Regulation

The need to hold builders accountable for their product has long been recognized. Faulty construction can kill and injure large numbers of people. The code of Hammurabi nearly four thousand years ago demanded the death of a builder if the owner were killed by the collapse of the structure. At Rome's peak of grandeur, buildings rose higher, increasing numbers collapsed, and control of construction through law was deemed a necessity.¹⁰

London's Lord Mayor promulgated a building code in 1186. Early colonial legislatures enacted measures to protect the public from fire and hazards in construction. The first building law on record in America was adopted in New Amsterdam as early as 1625.¹¹

By the end of the 19th century, the insurance industry and several professional organizations of engineers and construction contractors started to conduct research, testing and publication of standards for the construction industry. The American Society

6. U. S. Bureau of Labor Statistics, *Occupational Outlook Handbook, 1982-1983*, April 1982, p. 361.

7. Department of Commerce and Consumer Affairs, *Geographic Report*, September, 1982.

8. Bank of Hawaii, *Construction in Hawaii, 1982*, p. 3.

9. Clough, *Construction Contracting*, p. 17.

10. Colling, R. C. and H. Colling, *Modern Building Inspection*, Building Standards Monthly Publishing Co., 1950, p. 14.

11. *Ibid.*, p. 48.

for Testing and Materials, begun in 1898 and now comprising 28,000 members with 3,000 subcommittees nationwide, has published 5,700 standards. The American National Standards Institute began in 1918 to standardize manufactured parts used in industry and construction.¹²

The first model building code was formulated in 1905 by the National Board of Fire Underwriters (now the American Insurance Association.) The Association continues to issue the National Building Code which is a model general building code. Other model codes commonly used by local jurisdictions include the National Electrical Code published by the National Fire Protection Association, the Uniform Mechanical Code from the International Conference of Building Officials, the Uniform Plumbing Code by the International Association of Plumbing and Mechanical Officials, and the most generally used code, the Uniform Building Code issued by the International Conference of Building Officials.¹³

Governmental regulation of construction now takes various forms. Zoning dictates where different kinds of structures may be located. Building codes, now used almost universally in America, incorporate various national standards in governing construction in terms of protecting the public from fire, structural failure, and health hazards. Building permits and field inspections attempt to ensure compliance with building codes.

The safety of construction products is one reason for governmental concern. The other reason is protection for users of contracting services. These consumers are as varied as the contractors themselves, ranging from homeowners or renters to international conglomerates. They may suffer just as much from such things as failure by the contractor to do the agreed upon work, shoddy but safe workmanship, aesthetically inferior materials, and delays or failure to complete a project. These areas are not protected by building codes and similar regulations—unless such behavior by a builder might threaten public safety and inflict property damage on others.

Many states, including Hawaii, have found it necessary to establish additional ways to protect the public from those kinds of malpractice not covered by building codes and by fire, health and safety regulations. Twenty-one states require some form

12. Garrett, Michael D., *Complete Handbook of Successful Subcontracting*, Prentice-Hall, 1979, pp. 85–86, 89.

13. *Ibid.*, p. 96.

of licensure for contractors, usually through a state board or commission.¹⁴ Nine of the 13 western states require surety bonds of some kind.¹⁵

Three states, Hawaii, Virginia, and Arizona, pioneered in the collection of stipulated fees from contractors for use as a recovery fund to compensate the victims of licensed contractors who fail to fulfill their obligations.¹⁶

History of Regulation in Hawaii

Act 305 of 1957, now codified as Chapter 444, HRS, established Hawaii's system of licensing contractors. The intent of the legislation was to protect the public from dishonest, fraudulent, unskilled, or otherwise unqualified contractors.¹⁷ While there have been some modifications, the basic statute has remained essentially the same.

The current statute, its cited definitions little changed since the original legislation, defines a contractor as "any person who by himself or through others offers to undertake, or holds himself out as being able to undertake, or does undertake to alter, add to, subtract from, improve, enhance, or beautify any realty or construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish any building, highway, road, railroad, excavation, or other structure, project, development, or improvement, or do any part thereof, including the erection of scaffolding or other structures or works in connection therewith."¹⁸

The 1957 law established a licensing board with seven members. This was later increased to 13 members. The 1957 law also established the three basic classifications of contractors that still exist today:

- A. General engineering—specializing in such projects as irrigation, water supply, flood control, harbors, dams, highways, bridges, airports, parks, chemical plants, refineries, mines, and the like;

14. *Book of the States, 1982–1983*, Council of State Governments, p. 551.

15. State of Oregon, Legislative Research, *Staff Sunset Review, Builders Board*, August, 1980.

16. Costa, Al, et. al., *NASCLA Report: A Comprehensive Examination of the Arizona and Hawaii Contractors Recovery Funds*, May 6, 1982.

17. House Standing Committee Report 618 on House Bill 423, 1957 Regular Session of 1957.

18. Section 444–1(2), Hawaii Revised Statutes.

- B. General building—constructing shelters for residences, businesses and for animals; and
- C. Specialty contractors—using specialized trades and crafts such as plumbing, electrical, air conditioning, glazier, roofing, and painting, among many others.

Among the more important amendments made since 1957, are the following. In 1969, the law was amended to make it possible for an unlicensed person to own a legitimate contracting business (such as someone who inherited the company) provided that the company has a licensed “RME” or responsible managing employee. The law also specified that an unlicensed contractor has no recourse in the courts to recover payment for work performed. Also in 1969, the Legislature closed a loophole which previously allowed unlicensed contractors to operate by forming joint ventures with licensed contractors.

Two other measures were enacted in 1969. One measure strengthened the powers of the licensing board by authorizing suspension or revocation of licenses for any unfair or deceptive act or practice. The other measure gave the board the power to require a bond to be posted by contractors—of not less than \$2500 for specialty contractors and not less than \$5000 for general contractors—to be used to satisfy claims for unpaid wages and damages caused by the wrongful act of a licensee.

Act 191 of 1971 imposed a one-year residency requirement on all contractors. In 1973, Act 117 authorized the licensing board to prepare and administer examinations for applicants thereby establishing by statute what the board was already doing.

Also in 1973, Act 170 directed the contractors licensing board to establish, as trustee, a recovery fund to compensate those homeowners who are the victims of fraud, misrepresentation and malpractice by licensed contractors. To further strengthen protection of homeowners, the law was amended in 1975 to require a contractor to explain to a homeowner verbally and in detail the lien rights and responsibilities of all parties to a contract before it is signed. Also to be explained is the homeowner’s option to demand bonding on the project.

Nature of Regulation

Contracting activity is regulated currently by a 13-member Contractors License Board whose members are appointed by the Governor. Of the 13 members, 9 must be contractors, and 4, noncontractor public members. Eight members must be from Oahu, two each from Maui and Hawaii, and one from Kauai. Their terms run five years on a staggered basis.

Chapter 444, HRS, assigns the board the following general powers and responsibilities: to grant or refuse to grant licenses, to suspend or revoke licenses for established cause, to disseminate information about licensing, and to promulgate rules governing contractor acts and practices and the licensing process. To fulfill these duties, the board can investigate alleged malpractice complaints, conduct hearings, and evaluate applications. It is also authorized to prepare, administer and grade examinations of applicants.

The board is authorized to classify contractors into: A, general engineering contractors; B, general building contractors and C, specialty contractors. The board's rules now list 82 different specialties, each requiring its own distinct license. In addition to the standard specialties such as electrical, painting, and plumbing, there are delineations between such specialties as "solar energy systems" and "solar heating and cooling," between "ornamental metal" and "aluminum railings" contractors, between "electronic systems" and "fire burglar alarm" contractors, and between "landscaping" "hydromulching" and "tree trimming" contractors.

The board has the power to limit the scope of operations of a licensed contractor to those classifications for which the contractor holds a license. Thus, specialty contractors may contract only for the areas for which they hold specialty licenses although they may take on a contract involving the use of two or more unrelated trades if the work is supplemental to the work for which they are licensed. General contractors are not entitled to undertake contracts unless two or more unrelated trades are required on the project.¹⁹

19. Title 16, Department of Regulatory Agencies, Chapter 77, Rules Relating to Contractors, Chapter 444, Hawaii Revised Statutes, Section 16-77-33.

All contracting entities must be licensed. This includes individuals, corporations, copartnerships or joint ventures. In the case of corporations, there must be a licensed RME who is responsible for the direct management of the contracting business.

Eight categories of persons are exempt from Chapter 444. These include officers or employees of the federal, state or political subdivision; receivers; bankruptcy trustees; personal representatives and others acting under court orders or authorizations; those who sell or install finished products that are not a permanent part of the structure; projects with a contract price of less than \$100; registered architects or engineers acting in their professional capacity; those working as an employee solely for wages; owners who build structures for their own use or for their families and do not offer them for sale or lease; and any copartnership or joint venture in which all members hold licenses.

In order to be licensed, applicants must submit the following:

- . two character references;
- . three certificates in support of experience requirements of not less than four years of experience as a foreman, supervising employee or contractor in the particular field of contracting for which the applicant requests a license; and
- . current credit report covering at least the previous five years.

In addition, every applicant, except a responsible managing employee, must supply the Board with the following:

- . a current financial statement prepared by a certified public accountant or a public accountant;
- . a state tax clearance from the Department of Taxation;
- . a copy of workers compensation policy or a statement from the insurer that the policy is in effect;
- . a certificate of insurance showing coverage for comprehensive personal injury and property damage liability with minimum limits of \$100,000 for each person and \$300,000 for each occurrence for bodily injury and \$50,000 for each occurrence for property damage; and

affidavits of their officers, in the case of corporations or a copy of the registration of the partnership with DCCA, in the case of partnerships.

The board has the discretion to reject an application for a number of reasons, including such things as failure to satisfy the board that the applicant possesses a good reputation for honesty or has the financial capacity and responsibility to act as a contractor.

All applicants must also pass a written or oral examination to test the applicant's general knowledge of building, safety, health, labor and lien laws of the State and some basic administrative principles of the contracting business. They must also pass a test for their particular classification if one is offered. A grade of 75 is required to pass each of these two parts of the examination.

Under its rules, the board may issue conditional licenses for: (1) those applicants who are unable to meet all requirements for licensing; (2) as an alternative for those who have committed acts subject to revocation or suspension of their license; or (3) whenever the board considers it in the public interest to issue an applicant a conditional license. In these cases, applicants agree to comply with any condition established by the board including the provision that the license can be withdrawn at any time without hearing should the board determine that the licensee has violated the conditions or has not acted in the interests of the general public.

The board may revoke, suspend or refuse to renew a license for 17 cited reasons. Among these are: dishonest, fraudulent, or deceitful acts which cause damage to others; abandonment of a project without reasonable or legal excuse; willful diversion of funds; willful departure from plans and specifications; willful violation of law; failure to maintain required records; failure to have workmen's compensation insurance; and knowingly entering into a contract with an unlicensed contractor.

In lieu of suspending or revoking or refusing to renew a license, the board has discretion to impose a bond, fine, or other condition acceptable to all interested parties. The board can also require a bond as added proof of financial responsibility.

Several provisions in the law or the rules are aimed at protecting the homeowner or lessee. In addition to the Contractors Recovery Fund, there is the roofing contractors guarantee bond, disclosure requirements, and requirements for a written contract. Section 444–25.7, HRS, requires that every contract for building, repairing or improving a roof covering, which provides a guarantee of more than seven years, be accompanied by a bond for the replacement value of the roof. The bond is to be made out to the exclusive benefit of the owner or lessee of a private residence. The contractor is required to provide to the owner information on the bond and its conditions in writing.

The law requires all contractors to explain to owners the lien rights of all parties prior to signing a contract for home improvements. The board's rules also require contractors engaged in home improvement and renovation to provide the homeowner with a copy of the contract to be used, to disclose the approximate percentage of work to be subcontracted and the extent of bonding or financial security available to assure performance of the contract. All contractors are to provide homeowners with the written contract which shall cover, among other aspects, a statement of the amount of the contract, the date work is to begin, the number of days for completion, the work to be performed, and materials to be used.

To administer this licensing program on a day-to-day basis, the Department of Commerce and Consumer Affairs (formerly, Department of Regulatory Agencies) provides the board with an executive secretary, staff, and meeting place. Reorganization currently under way within the department will establish a Regulated Industries Complaints Office that will centralize and expedite all complaints handling, including complaints against contractors. Act 60, SLH 1982, imposed an annual fee of \$10 on all licensees regulated by the department to be deposited into a special fund, the "compliance resolution fund," which is to be used to hire hearings officers, investigators, attorneys, accountants, and other necessary personnel.

Chapter 3

EVALUATION OF THE REGULATION OF CONSTRUCTION CONTRACTORS

This chapter contains our evaluation of the need to regulate construction contractors, our assessment of the adequacy of the current licensing system and regulatory operations, and our recommendations for improvement.

Summary of Findings

We find that:

1. There is a continued need to regulate construction contractors to protect the public from financial loss and to ensure that contractors are qualified and have the financial responsibility to carry out their contracts.
2. There is room for substantial improvement in licensing operations. The financial capacity required of applicants serves little purpose, experience requirements are vague and restrictive and the examination system, which tests some for specialized knowledge but not others, is particularly questionable.
3. In the absence of any statutory authority, the Contractors License Board has issued conditional licenses to applicants who fail to meet the standards for licensure. In issuing these licenses, the board has imposed conditions that are both inappropriate and unenforceable.
4. The manner in which contractors are classified restricts competition and is subject to abuse. The board is currently issuing specialty contractors licenses in 82 specialty classifications and another 212 subspecialty classifications. This has resulted in jurisdictional problems between and among the trades without any clear benefit to the public.
5. Enforcement of the law has been severely deficient. Complaints are backlogged for several years and few disciplinary actions are taken.

6. The \$10,000 maximum amount that a homeowner who suffers losses can recover from the contractors recovery fund appears to be unduly low and restrictive, as is the \$20,000 limit in total claims that can be made against any one contractor.

The Need for Regulation

The construction industry pervades and directly affects the public's daily environment. Yet, its products are largely taken for granted. Despite the considerable potential for danger to public health and safety from fire, structural failure, and other health hazards, the general public assumes that standards are met, that structures are safe, and that the supporting infrastructure of utilities, sewers, water lines, and drainage facilities meet building standards and safety and health codes.

For the most part, the public is justified in this assumption. Control over health and safety standards is exercised by numerous federal, state, and county agencies through standards such as uniform building codes, water quality standards, and other regulations. These are enforced through processes such as building permits and field inspections of construction work.

The purpose of state regulation through the Contractors License Board is to provide a different kind of protection, that of protecting the public against dishonest, unskilled, or otherwise unqualified contractors. This other kind of control is needed to protect investments made by consumers who, for the most part, lack the technical knowledge, the legal expertise, and the financial resources to protect themselves against failure or malpractice by a contractor.

According to a study done for the New Mexico Construction Industries Commission, the consumers of construction services fall into two groups, the sophisticated and the unsophisticated. The sophisticated buyer, such as a large enterprise, is knowledgeable about the industry and either has the experience to be able to prejudge the qualifications of a contractor or is able to purchase such expertise. Unsophisticated consumers purchase construction services only occasionally. They generally do not have the knowledge to prejudge the services they wish to purchase. Neither can they afford to have expert advice in selecting contractors. The study says, "It is therefore the unsophisticated consumer of small construction projects that is most vulnerable to the inexperienced, incompetent and unscrupulous contractor. This group is made up mainly

of homeowners and small businesses. For these consumers, their investment in construction may be a once-in-a-lifetime event and may represent the largest financial investment that they will ever make.”¹

So much must be taken on faith in contracting. There is no product to inspect in advance. Buying contracting services is different from buying a toaster or a car. A consumer can check these in advance and return them if they are faulty. The basis for selecting any particular contractor is far more limited and irretrievable, short of incurring additional delays, costs, and strain. There is no way to inspect a painting job before it is done and no way to return it after it is finished. One does not know what one has purchased until it is all over.

There are also numerous potential sources of consumer dissatisfaction and financial hardship. One indication of this variety is seen in the kinds of complaints received by the Department of Commerce and Consumer Affairs (DCCA). Consumers complain to DCCA about costs, materials used, differing interpretations of design specifications, unfulfilled warranties, poor workmanship, and lost deposits. The number of complaints more than doubled between 1971 and 1980, from 175 in fiscal year 1971–72 to 405 in 1980.

To some extent, a significant portion of reported dissatisfactions arise from miscommunications about expectations. Consumers might not have expressed adequately their preferences and the contractor might not have grasped what was wanted. While written contracts and full drawings can reduce this problem, not everyone understands them.

This wide range of problems suggests that there is a continued need to protect the public from unqualified or irresponsible contractors. The intent of Chapter 444, HRS, is to provide this protection. In the next sections, our evaluation assesses the extent to which state licensing requirements are actually effective and appropriate in screening out incompetent and irresponsible contractors and the extent to which current regulatory operations are adequate in protecting the public.

1. Sears, Glenn A., *Final Report. A Comparison of Regional Licensing Procedures for General Contractors*, State of New Mexico Construction Industries Commission, February 1981, p. 25.

Regulatory Operations

Licensing requirements. The Contractors License Board meets 11 times a year. Board members volunteer a great deal of time to this effort. Committee work takes up most of the mornings and regular sessions take up most of the afternoons. Much of this time is spent in reviewing and approving applications for licensure, in hearing appeals on previous board denials of applications, and on various requests for waivers from licensing requirements.

The main purpose of licensing contractors is to ensure that those licensed have two key attributes: (1) that they are knowledgeable about the work to be done and capable in the craft or construction area for which they are to be licensed, and (2) that they are financially able to complete the work contracted for. Therefore, licensing requirements are appropriate only to the extent that they discriminate between those who have these attributes and those who do not. Our evaluation of the current licensing requirements shows that there are some requirements that have no relationship to either competency or financial responsibility whereas others that are of vital importance are not administered properly.

Among other requirements, applicants are supposed to submit a current financial statement prepared by a certified public accountant and three certificates in support of experience requirements. Upon board approval of their applications, applicants must then take and pass an examination before they are licensed. As discussed below, each of these is questionable in various respects.

Financial capacity and statements. At its June 1981 meeting, the board set the following requirements for evaluating the financial capacity of applicants:

- . A and B general contractors must have a financial capacity of \$17,500;
- . C specialty contractors must have a financial capacity of \$8,000 when they supply both labor and materials;
- . C specialty contractors must have a financial capacity of \$6,000 when they supply only labor for projects.

According to board minutes, financial capacity is defined as the position of an entity after subtracting current liabilities from current assets.²

The board has been using a financial capacity criterion for some time. At the June 1981 meeting, members of the board's applications committee voted in favor of increasing the amount to keep up with inflation. Other members of the board were concerned that the amounts set were prohibitive to newcomers in the business. The final amounts set as the criteria for financial capacity were based on a consensus of the board. As such, they are arbitrarily set amounts that bear no realistic relationship to financial responsibility.

The basis for this approach is found neither in the statutes nor in the rules. Nor is this standard of much value in predicting whether the applicant will be financially sound and responsible. Depending on the value of projects contracted for in the future, the amounts used by the board as an indication of financial capacity may have no meaning at all. Therefore, the financial statements, which are required to be submitted to reveal financial capacity, are of questionable usefulness in determining whether the applicants have the capability of responsible financial performance.

Contractors are also supposed to submit financial statements at the time they renew their licenses. These statements also serve little purpose as they are not systematically reviewed as they are received. They are merely filed. The DCCA staff say that they have neither the time nor the expertise to evaluate adequately the financial statements.

Inasmuch as there is no valid basis for the amounts set as criteria for financial capacity and no proper scrutiny is made of the documents purporting to show financial capacity, this requirement should be removed. If the board wishes to obtain some reasonable assurance that a person is financially responsible, emphasis should be given to the credit reports. The board requires applicants to submit credit reports covering the past five years. Rather than requiring financial statements of questionable value, the board should require the staff to review the credit reports carefully and flag out for the board's review and decision those reports which indicate dubious financial responsibility.

2. Minutes of the Contractors License Board, June 1981.

Experience requirements. According to Dr. Benjamin Shimberg, who has written extensively about occupational licensing, “The experience requirement is undoubtedly the most important prerequisite” [in the construction trades].³ Experience is the key to assessing whether applicants are knowledgeable or have had training in the field in which they wish to contract. The board requires four years experience of a supervisory nature, that is, the applicant must have been a foreman, a supervising employee, or contractor.

Most appeals to the board result from the board’s initial denial of applicants because of their lack of appropriate experience. Much time is spent on hearing these appeals, and the board frequently reverses itself when applicants appear to describe their experience in person.

Board minutes indicate that many applicants simply do not understand what kinds of documents the board will accept as satisfying the experience requirements. The board has no guidelines on what it means by supervising employee or contractor. Nor is it clear whether this must be all full-time employment or whether it can be part-time. The form and the instructions given to applicants provide few details to help them in determining what kinds of experience are acceptable. The application form merely asks them to list their employers, to supply some details on work done, and the periods of employment.

The board needs to establish clearer guidelines, and the licensing instructions should be revised so that applicants will have a better understanding of what is required. The experience form should request specific information on the nature of business conducted by former employers, the applicant’s exact position in the firm, whether the work was part-time or full-time, the exact number of people supervised, etc. This would reduce the unnecessary delay for those who might be qualified but are initially denied because they fail to submit the appropriate information. It would also help to reduce the unfair denial of those who do not appeal but who might have been qualified.

3. Shimberg, Benjamin, et. al., *Occupational Licensing, Practices and Policies*, Public Affairs Press, 1973, p. 80.

The requirement for four years of supervisory experience creates a hardship and an inequitable situation for many specialty contractors. For some, this means that they must have almost 10 years of experience before they can apply for a license. To illustrate, a plumbing apprentice must have five years of training before becoming a journeyman plumber. After becoming a journeyman, the plumber must have an additional four years of supervisory experience. In most cases, this means that they must have at least 10 years of experience before they are eligible to apply for a contractor's license. At the same time, applicants for A and B licenses in general contracting can engage in many of the specialty contracting areas automatically after four years of supervisory experience without qualifying further in those fields.

Several western states that license contractors allow experience as an apprentice to count towards fulfilling the experience requirement. Utah counts one year of work as an apprentice as one-half year of experience. Nevada and California do not require supervisory experience and will accept experience as a journeyman.⁴ California will also accept substitutions for experience. Technical training in an accredited school or completion of an approved apprenticeship program or its equivalent can count for up to three years of experience.⁵

The board should provide greater flexibility in its requirements for experience by allowing education, training, and experience as an apprentice or journeyman to count towards fulfilling the four year experience requirement. Although in its rules, the board has given itself the discretionary authority to accept training and other equivalent knowledge in lieu of the specific experience requirement, it has yet to develop more specific guidelines as to how it intends to use this discretionary power.⁶ As it is now, decisions on what is acceptable is made on a case by case basis with favorable decisions going only to those who question or appeal the board's initial decisions.

4. Sears, *Final Report*, p. 16.

5. State of California, Department of Consumer Affairs, *Contractors State License Board Rules and Regulations*, 1980.

6. Title 16, Department of Regulatory Agencies, Chapter 77, Rules Relating to Contractors, Chapter 444, Hawaii Revised Statutes, Section 17-77-19.

Examination requirements. The law allows the board to “prepare, administer, and grade such examinations and tests for applicants as may be required for the purposes of this chapter.”⁷ The board’s rules require all applicants to take and pass a test on the applicant’s general knowledge of the building, safety, health, labor, and lien laws of the State and some basic administrative principles of the contracting business.⁸ This is Part I of the examination.

Part II of the examination tests knowledge of the specific contracting fields for which applicants are applying. There are Part II examinations for the two A and B general contractor license classifications. In addition, 47 of the C specialty contracting categories have a Part II examination. This leaves 35 specialty contracting categories with no Part II examinations even though board rules require separate written examinations to be given in each contracting category to test the applicant’s specialized knowledge. Neither are examinations for specialized knowledge in effect for some 212 subspecialty categories.

The examination requirement appears to be both unfair and of little use in establishing competence as there is no evidence that contractors in those specialty categories who took and passed Part II examinations are any more or less competent than those who did not have to take a test at all.

The usefulness of the examinations is particularly suspect as 30 of the specialty examinations are over 10 years old. Twenty-one tests actually date from the mid- and late sixties. Many of the tests are obviously obsolete; they have never been revised; and, since there is only a single test for many of these fields, the identical questions are used over and over again. Applicants can keep on taking the same test until they pass.

The board also requires all applicants to pass their respective tests with a grade of 75. This assumes that all the Part II examinations are of equal difficulty. Whether that passing score is actually too high, too low, or just right is anyone’s guess. Yet, scores below 75 are used to deny licenses to applicants. Between January 1981 and August 1982, 1,061 Part II examinations were given for various contracting categories. Sixty-six percent passed the Part II examinations. However, in the absence of any evidence that these tests are actually job or competency related, this means that 34 percent of the applicants were denied licenses without a clearly valid basis. This is particularly inequitable in view of the fact that applicants for 35 specialty contracting classifications do not have to take any Part II examinations at all.

7. Section 444–4(6), Hawaii Revised Statutes.

8. Title 16, Chapter 77, Section 16–77–39.

In our 1982 report on the professional and licensing program of the DCCA, we identified a number of deficiencies in the department's administration of examinations generally. These problems are still present in the examinations for contractors' licenses. Tests are obsolete, and there is no evidence that they are competency related. The department's continuing difficulties in correcting deficiencies in examinations indicates that there is little likelihood of developing valid and reliable examinations to test competency in the numerous contracting categories. To avoid further administration of an unfair and invalid requirement, the board should take action to delete the Part II examination requirement.

At the same time, emphasis should be placed on improving the Part I portion of the examination. The experience requirement provides some assurance the applicants will have the necessary trade knowledge. However, the licensing process must include some criteria to ensure that applicants have the necessary knowledge of state laws, regulations, codes, and basic managerial, legal, and business practices. Contractors face an increasingly complex world of taxes, union contracts, government regulation, insurance needs, and finances. Many beginning contractors are unaware of the essentials of this side of contracting. The Part I examination requirement, developed properly, should be of assistance in ensuring preparation in this area.

Irrelevant requirements. In addition to the above, there are two relatively minor requirements which serve no purpose and should be deleted from the licensing requirements. These are the requirements for residency and good moral character. The statute requires an applicant to have been a resident of the State for at least one year. Residency requirements have been held by the courts to be unconstitutional.

The statute also requires each application to be accompanied by sworn certificates by not less than two persons that the applicant has a good reputation for honesty, truthfulness, and fair dealing. These letters provide little assurance of good character. In practice, the department either ignores this requirement or merely files away the character references. The statute should be amended to delete the requirements for residency and certification of character.

Conditional licenses. In its rules, the board has given itself the authority to issue conditional licenses. These licenses can be conditioned on any grounds that the board finds acceptable and it imposes any conditions it chooses.

Conditional licenses usually have two standard provisions: (1) that the applicant will apply for a conditional license, and (2) that the license may be revoked at any time without a hearing. In addition, the board imposes other special conditions depending on the particular circumstances under consideration. Some of these special conditions are unenforceable and inappropriate. A review of board minutes over the past two years shows some of the following kinds of conditions:

- . The board gave an applicant who lacked the necessary experience in general contracting a B license for general contracting on the condition that he engage only in erecting prefabricated buildings. There is no way to ensure that the contractor actually complies with this condition, and this limitation is not noted anywhere on his license.
- . The board gave a conditional license to a responsible managing employee (RME), who had a number of civil and tax judgments against him, on the condition that his activities be limited to construction operations and that he not engage in any financial affairs. This condition is not only unenforceable, it is entirely contrary to the concept of requiring contracting entities to be under the supervision of a responsible managing employee who would have overall control of all technical and administrative operations of a company.
- . The board gave a conditional license to an applicant, who had many judgments against him, on the condition that he supply documents showing satisfaction of judgments and that he keep the board advised as to the progress of lawsuits.
- . A contractor was awarded a conditional license on the condition that he limit his projects to his own developments and keep the board advised on his projects.

Many conditional licensees are also supposed to submit semi-annual financial reports and job reports. Efforts to follow-up on these conditions have been spotty. DCCA staff do not always check on whether conditional licensees have submitted the required reports, and they generally take no action against those who fail to comply with the specified conditions. Our review of a number of conditional licenses given over the past two years showed that none of them submitted the required information upon which their licenses were conditioned.

Conditional licenses are generally granted to those who were denied licenses for failure to meet licensing standards and who appealed these denials. The board will usually grant licenses to those who appeal. For example, between July 1981 and June 1982, the board heard 45 appeals on applications that it had previously denied. It reversed itself and approved 37 of these appeals, deferred action on seven, and denied one. It is evident that the board is willing to make exceptions to the rule. It will give conditional licenses even to those with outstanding judgments, tax liens, and lawsuits at the time of application. Once licensed, even on a conditional basis, the general public has no way of knowing that these contractors are any less qualified or reputable than other licensed contractors.

Our assessment is that the granting of conditional licenses detracts from rather than serves the public interest. Moreover, we do not believe that the statute provides the board with the authority to grant licenses which are, in effect, probationary licenses. The entire thrust of the current licensing statute is to license those who are qualified and to deny licenses to those who are not. The Legislature could decide that there is a need for a conditional license category, but unless the Legislature empowers the board to issue conditional licenses, it should cease doing so.

Licensing Classifications

The board has the authority to classify contractors in a manner consistent with established usage and procedure in the construction industry and to limit the field and scope of operations of contractors to those in which they are classified and qualified. The three major classifications are: A—general engineering contractors, B—general building contracting, and C—specialty contracting.

Our evaluation shows that there are two aspects to the licensing classification system that have the effect of restricting competition and are open to abuse: (1) the limiting of general contractors to those projects that require two or more trades, and (2) the licensing of 82 specialty contracting categories and another 212 unofficial subspecialty licensing classifications.

Limitations on general contractors. The law says that a general building contractor is one whose principal business is building structures that require “in its construction the use of more than two unrelated building trades or crafts, or to do or superintend the whole of any part thereof.”⁹ The board’s rules say further that the general building contractor is not entitled to take any contract unless it requires two or more unrelated trades.¹⁰

This provision exists more to prevent the general contractor from competing with specialty contractors than with public protection. For example, under this rule, a general building contractor is not permitted to bid on or to do fencing work if that is the sole work to be done. However, if the fence is to be built as part of a larger project, then the general building contractor would be eligible to do the work. Certainly, the general building contractor is no less competent to do the smaller job by itself than the smaller job when it is part of a larger project.

Similar contractors’ licensing provisions were reviewed in Arizona by Dr. Jonathan Rose, who has researched and analyzed anti-trust as it relates to occupational licensing. In reviewing the provision restricting general contractors to work involving two or more trades, he concluded: “. . .there appears to be no health or welfare justification for this statutory limitation of more than two trades. If the general contractor is permitted to do the work when it is part of a larger project, it is unclear what health or safety considerations justify restricting him from doing smaller projects. As mentioned, the only purpose of the statute seems to be to protect specialty contractors on certain kinds of jobs.”¹¹

Questionable need for nearly 300 specialty and subspecialty licenses. A more serious problem is the numerous specialty license categories that have been created. The board has established 82 different specialty license classifications in its rules. However, the delineation does not stop there. The last specialty category, C-68, is a catch-all to provide for further subspecialties that ostensibly do not fit into any of the other 81

9. Section 444-7(c), Hawaii Revised Statutes.

10. Title 16, Chapter 77, Section 16-77-33(2).

11. “Occupational Licensing and Related Entry Controls in Miscellaneous Public Welfare Areas” by Dr. Jonathan Rose in *A Performance Audit of the Arizona Registrar of Contractors*, State of Arizona, Office of the Auditor General, October 1979, p. IX-9.

specialty license classifications. These add up to another 212 subspecialty license classifications that appear in neither the rules nor any other officially adopted listing. Many of the classifications in the official list and all of the unofficial subspecialty licenses appear to be unwarranted and should be reviewed. These numerous license classifications create jurisdictional and enforcement problems which detract from rather than add to public protection.

Specialty classifications. The statutes authorize the board to grant specialty licenses to contractors “whose operations as such are the performance of *construction work* requiring special skill and whose principal contracting business involves the use of specialized *building trades* or crafts.”¹² (Emphasis added.)

The board has no guidelines for determining what falls within the scope of construction work or building trade. Without such guidelines, it is impossible to distinguish between what should fall within its purview and what should not. [Table 3.1](#) provides a listing of the 82 specialty licenses that are now being granted by the board. A review of the list shows that while some fall definitely within the scope of construction work, such as C-13, electrical contractor, or C-37, plumbing contractor, there are others that are only remotely connected with the building trades, such as C-27a, hydro-mulching contractor, or C-27b, tree trimming contractor, or C-15a, fire and burglar alarm contractor. The scope of work for each of these is described in the rules as follows:¹³

- C-27a Hydro-mulching – to place hydro-mulch material as a bed for ground cover and for containment of soil.
- C-27b Tree trimming – to prune, trim, and remove trees, including stumps, and to restore ground to a condition similar to adjacent area.
- C-15a Fire and burglar alarm – to install, maintain and repair central fire and burglar alarm systems.

In addition to the lack of guidelines as to what should fall within the scope of licensing by the Contractors License Board, there are also no guidelines as to when a particular activity should be licensed. Even though an activity may be clearly

12. Section 444-7(d), Hawaii Revised Statutes.

13. Title 16, Chapter 77, Section 16-77-28(3).

Table 3.1

Classifications of Specialty Licenses

C-1	Acoustical tile contractor;	C-35	Pile driving and foundation contractor;
C-3	Asphalt paving and surfacing contractor;	C-36	Plastering contractor;
C-3a	Asphalt concrete patching, sealing and striping contractor;	C-36a	Lathing contractor;
C-3b	Play court surfacing contractor;	C-37	Plumbing contractor;
C-4	Boiler, hot-water heating and steam fitting contractor;	C-37a	Sewer and drain line contractor;
C-5	Cabinet millwork and carpentry remodeling and repairs contractor;	C-37b	Irrigation and lawn sprinkler systems contractor;
C-5a	Garage door contractor;	C-37c	Vacuum and air systems contractor;
C-5b	Siding application contractor;	C-37d	Water chlorination contractor;
C-6	Carpentry framing contractor;	C-38	Post tensioning contractor;
C-7	Carpet laying contractor;	C-40	Refrigeration contractor;
C-9	Cesspool contractor;	C-40a	Prefabricated refrigerator panels contractor;
C-12	Drywall contractor;	C-41	Reinforcing steel contractor;
C-13	Electrical contractor;	C-42	Roofing contractor;
C-14	Sign contractor;	C-42a	Aluminum shingle contractor;
C-15	Electronic system contractor;	C-42b	Wood shingles and shakes contractor;
C-15a	Fire and burglar alarm contractor;	C-42c	Cement and clay tile contractor;
C-16	Elevator contractor;	C-42d	Composition shingle contractor;
C-16a	Conveyor systems contractor;	C-42e	Urethane foam contractor;
C-17	Excavating, grading and trenching contractor;	C-42f	Liquid asphalt roofing contractor;
C-18	Fencing contractor;	C-42g	Roof coatings contractor;
C-20	Fire protection contractor;	C-43	Sewer, sewage disposal, drain, and pipe laying contractor;
C-20a	Dry chemical fire repressant system contractor;	C-43a	Reconditioning and repairing pipeline contractor;
C-21	Floor covering contractor;	C-44	Sheet metal contractor;
C-22	Glazing contractor;	C-44a	Seamless aluminum gutter contractor;
C-23	Gunite contractor;	C-48	Structural steel contractor;
C-24	Building moving and wrecking contractor;	C-48a	Steel door contractor;
C-25	Institutional and commercial equipment contractor;	C-49	Swimming pool contractor;
C-27	Landscaping contractor;	C-49a	Swimming pool service contractor;
C-27a	Hydro mulching contractor;	C-51	Tile contractor (ceramic and mosaic);
C-27b	Tree trimming and removal contractor;	C-51a	Cultured marble contractors;
C-31	Masonry contractor;	C-51b	Terrazo contractor;
C-31a	Cement concrete contractor;	C-52	Ventilating and air conditioning contractor;
C-31b	Stone masonry contractor;	C-55	Waterproofing contractor;
C-31c	Refractory contractor;	C-56	Welding contractor;
C-31d	Tuckpointing and caulking contractor;	C-57	Well drilling contractor;
C-32	Ornamental metal contractor;	C-57a	Pumps installation contractor;
C-32a	Aluminum railings contractor;	C-57b	Injection well contractor;
C-33	Painting and decorating contractor;	C-61	Solar energy systems contractor;
C-33a	Wall coverings contractor;	C-61a	Solar hot water systems contractor;
C-33b	Taping contractor;	C-61b	Solar heating and cooling systems contractor;
		C-62	Pole and line contractor; and
		C-68	Classified specialists.

Source: Title 16, Department of Regulatory Agencies, Chapter 77, Rules Relating to Contractors, Chapter 444, HRS, Section 16-77-28.

construction work, it may pose no danger to the public and therefore, it may not need licensing. The basic premise underlying state regulation of professions and vocations is that regulation is warranted only for the purpose of protecting public health, safety and welfare. As the State's designated authority for licensing activities in the construction industry, the board needs to exercise care in determining whether licensing of certain construction activities is indeed needed for public protection.

A third area in which there are no guidelines is the question of what should be considered a "specialty." Many of the specialty classifications are merely fragments of a larger specialty. For example, all the specialties with alphabetical suffixes are segments of a more inclusive specialty. For example, C-42 is a roofing contractor. But there are also specialty classifications for C-42a, aluminum shingle contractor, C-42b, wood shingles and shakes contractor, C-42c, cement and clay tile contractor, C-42d, composition shingle contractor, etc. It is not clear what additional public protection is being provided by fragmenting the specialty into additional specialties when a single specialty would provide the same protection.

At this point, thought should be given to eliminating or combining some of the specialty classifications. Staff and board attention is spent in settling jurisdictional disputes over whether bidders on construction contracts hold the appropriate license classification. The focus appears to be more on determining who has exclusive jurisdiction over a particular scope of work rather than on the broader aspects of protection.

For example, specialty licenses are required for roofing and sheetmetal work. If a sheetmetal roof is to be built, questions arise as to which contractor has the exclusive right to the job. Then, there is the dispute involving painters and water proofers and whether painters have the right to apply water proofing materials. These kinds of disputes provide a mere sampling of what has occupied board and staff time. Yet, there is no evidence that such hair-splitting in any way serves consumers. So long as the board delineates classifications of contractors ever more narrowly, jurisdictional disputes will continue and even increase.

Dr. Rose, in analyzing the numerous specialty contracting areas, states: ". . .this classification system serves to fragment the market into a series of separate domains insulated from competition that might otherwise occur. . .There is no doubt that this

legally administered and enforced market allocation scheme is highly anticompetitive and undesirable. Just as the provisions discussed earlier insure that specialty contractors are not subject to undue competition from general contractors, this aspect of the classification system insures that various specialty contractors are not subject to competition from each other.”¹⁴

The board must develop guidelines on (1) what falls within the scope of construction work or building trade, (2) what activities warrant licensing, and (3) what criteria must an activity meet to be considered a specialty.

On the first item, the board should work with representatives of the construction industry, such as the General Contractors Association of Hawaii, other trade associations and the unions to develop a workable definition of what should be included for licensing. In doing so, the board should recognize that not all related activities need to be regulated.

An appropriate set of criteria which the board could use for determining the activities which warrant licensing would be the sunset policies in the Hawaii Regulatory Reform Act. These policies are set forth in Chapter 1 of this report and they form the basis for our evaluation of construction contractors. The board could assess each of the specialties against such criteria as evidence of abuse, consumer disadvantage in using the service, etc. In determining when certain activities should be classified as specialties, the board could use criteria such as whether the activity consists of an independent scope of practice that is not a fragment of another specialty.

Improper use of the C-68 specialty classification. According to the board’s rules, the C-68 classification is to be used for “construction work requiring special skill which work is *not related* to any of the listed classifications but which does meet the standards set by law for licensing.”¹⁵ (Emphasis added.) The rules go on to say that temporary classifications may be established in this area until the work is defined and a hearing held to establish the proper classification based on established usage in the construction industry.

14. *A Performance Audit of the Arizona Registrar of Contractors*, p. IX-12.

15. Title 16, Chapter 77, Section 16-77-28(3).

It is apparent that the intent is to allow individuals with unique construction specialties to be granted a license to work until the board has an opportunity to properly define and classify the scope of work and to hold a public hearing on the matter. However, the board's activities in this area violate its own rules in these respects:

- . the licenses have not been issued on a temporary basis,
- . the scope of work for these subspecialties has not been defined,
- . the classification is being used for work that is related to those in the listed classifications, and
- . public hearings have not been held on most of these subspecialties and the board has neither guidelines nor procedures for dealing with these.

As of July 1982, there were 212 subspecialty categories in the C-68 classification with 496 current licensees. Table 3.2 presents a listing of these C-68 subspecialty classifications. A review of some of the licensees in DCCA records shows that many of them are of long standing, dating back some 20 years. Thus, the licensees can hardly be considered as having been assigned to temporary classifications.

The scope of work that is permissible under each of the 212 subcategories has not been defined. All that is available is an alphabetical listing. The 212 subcategories are really groupings of like activities under such headings as "aluminum awnings," "caulking," "protective coating," "automatic temperature control," etc. Actually, there are far more than 212 subcategories. There may be as many subcategories as there are licensees as we were informed that each applicant is asked to describe and justify the scope of work that he or she intends to do.

Although the purpose of specialty licensing is to limit contractors to work in only those areas for which they have qualified, the lack of definition makes it impossible to determine exactly what these subspecialty contractors are entitled to do. In short, the board over the years has created a licensing and enforcement nightmare. It is impossible to determine whether an activity is supposed to be licensed or unlicensed;

Table 3.2

C-68 Subspecialty Classifications

Aluminum awnings	Installation of electronic clocks and control systems
Aluminum awnings, railings, patio covers	Installation of energy absorbing devices
Installation of aluminum awnings	Epoxy injection
Installation of aluminum gutters	Installation of epoxy bonded stones
Aluminum guard railings	Erecting stages, rigging stage curtains and tracks
Aluminum railings	Erection of radio, television, and FM transmitting antennas related systems and work for erection of these systems
Aluminum and vinyl siding	Estimate and bid to metal doors and frames, linen and rubbish chutes, etc.
Artificial turf installation	Floating floor systems
Removal of asbestos insulation	Installation of garage doors
Asphalt composition shingles	Installation of gas tanks, pumps, and hoists for service stations
Installation of automatic doors	Highway guard rails, fencing, signs
Automatic temperature control	Highway guard rails, signs
Installation of bifold doors and shutters	Installation of hot tubs
Limited building moving and wrecking	Hydro-mulching
Installation of carousels and conveyors	Installation of incinerators
Carpet laying (limited to bidding and signing contracts)	Installation of industrial instrumentation
Installation of cathodic protection systems	Pneumatic and electronic instrumentation and computer terminex installation and servicing
Caulking	Interior design
Caulking, deck coatings, exterior sealings of windows, expansion joints, etc.	Interior design (limited to bidding and entering into contracts; all work sublet to licensed contractors)
Caulking, liquid membrane waterproofing	Irrigation installation
Caulking, liquid membrane waterproofing, epoxy injection	Irrigation sprinkler systems
Caulking, saw cutting, joint sealing, liquid membrane waterproofing, concrete curing, installation of prefabricated concrete forms, sandblasting	Irrigation systems
Caulking and sealants; application of epoxy toppings	Installation of irrigation systems
Caulking and sealing in metal, cement, and precast stone; application of non-skid decorative coatings for lanais, deck, and walkways	Installation of jail and prison equipment; locking devices and control systems
Caulking, saw cutting, joint sealing, liquid membrane waterproofing, sandblasting	Lawn sprinkler system
Caulking and coating; liquid membrane waterproofing	Liquid membrane waterproofing
Caulking, sealing, sandblasting, spray-on insulation (urethane)	Liquid membrane waterproofing; epoxy injection
Chemical cement grouting, concrete drilling, cutting, sawing and coring	Maintenance dredging
Check out of electronic and pneumatic industrial instrumentation	Marble and granite
Cold applied felt	Marine construction
Composition roof	Material handling equipment (pneumatic tube system bridge, cranes, monorails, and hoists) conveyors
Composition roof and Harvey roof	Installation of material handling equipment
Composition shingle	Installation of mechanical doors
Composition shingles and roll roofing	Installation of mechanical equipment related material handling, collection, and compaction (including air and water pollution control)
Installation of composition and other types shingle	Construction of messenger and coaxial cable and amplifiers for a cable television network
Concrete curing, sawing, and sealing	Miscellaneous metals
Concrete cutting, drilling, sawing, coring	Install metal chutes, folding partitions, bleachers
Concrete drilling, sawing, etc.	Monier roof tile
Installation of conveyor machinery	Monier tile installation
Installation of conveyor systems and related equipment	Spray oil on shake and shingle roofs
Conveyor and materials handling installations	Installation of overhead doors
Corrosion coat control	Installing overhead, sliding, and roll-up steel doors
Corrosion control	Parking control equipment
Cultured marble	Installation of passenger loading bridges
Installation of cultured marble	Pavement marking
Decorating, treatment of roof and ground through use of rock or coral chips	Pavement markings, seal coating of asphalt driveways, parking areas, and incidental patching
Installation of deep well pumps	Pavement sawing, sealing, and grooving
Field erection of geodesic domes	Piling and caisson drilling
Dredging and filling reef runway	Piling, caisson drilling, and installation
Drilling and blasting	Pipe laying
Installation of drop line from CATV cable to television set	
Installation of dry chemical and Haylon fire repressant systems	

Table 3.2—continued

Fabricate and place corrugated metal and similar types of pipe	Solar hot water, heating, and cooling systems
Plastic coatings	Solar heating systems
Plastic coatings applicator	Installation of solar heating systems
Installation of plastic linings in lakes, ponds, reservoirs, etc.	Solar heating devices
Limited to fabrication and erection of plate steel structures	Solar energy systems
Pneumatic temperature systems	Solar water heating systems
Pneumatic tubes	Special tank coating
Pneumatic conveyance systems	Spray acoustic on concrete
Communication pole and line	Spray insulation for soundproofing
Communication pole and line (low voltage)	Spray acoustic ceiling texture
Erect new poles in new pole lines only	Prepare and finish ceilings and walls with drywall compound and apply simulated spray acoustic
Installation of poles in new pole lines only	Spray on carpeting
Installation of poles in new pole lines and replacement of poles where circuits of 600 volts or less are involved	Spraying of acoustical material between units in connection with drywall installation only
Pole and line—low voltage	Installation of sprinklers
Pole planting	Installation of sprinkler systems
Install and replace poles where circuits of 600 volts or less are involved	Striping and traffic marking of highways and parking lots
Install new poles in new pole line and replace poles where circuits of 600 volts or less are involved	Structured steel (limited to fabrication and erection of plate steel structures)
Application of polyurethane foam	Synthetic flooring
Application of polyurethane spray	Installation of synthetic marble
Pressure grouting	Installation of synthetic marble products
Protective coating	Tank lining
Pump installation	Tennis court construction
Installation of pumps and various piping including controls	Tennis court resurfacing
Pump installation with appurtenances	Terrazzo
Installation of water well pump and related equipment	Imbedding of terrazzo chips in epoxy coated concrete roofing decks; terrazzo; seamless flooring with terrazzo chips
Installing booster pumps and industrial equipment	Terrazzo; seamless flooring with terrazzo chips
Install radiation shielding	Test drilling and well injection
Raised flooring (computer)	Tinting of glass using 3M material
Raised floors	Traffic control devices
Reconditioning water supply lines	Traffic line marking
Refractory	Traffic markings and striping
Construct refractory lining and high temperature industrial furnaces	Installation of traffic safety devices, barriers, rails, signs, striping, etc.
Installation of specialized high temperature refractory equipment and maintenance	Traffic safety installation
Installation of prefabricated refrigeration panels	Trenching
Roof coating	Limited trenching only
Roof coating, simulated spray acoustic	Underwater work for all types but specializing in dock, bridge, and pier rehabilitation
Roof treatment	Urethane foam
Sandblasting	Application of urethane spray
Sandblasting, sealing, elastomeric coating and waterproofing, epoxy and epoxy injection	Vacuum and air systems installation
Install prefabricated sauna baths and wine cellars	Velvetex
Seal coating and color coating of tennis courts and parking lots	Installation of veneer stone
Seamless aluminum gutters	Installation of vertical sand drains and vibroflotation compaction
Seamless gutter	Vinyl lined swimming pool
Installation of seamless rain gutters and downspouts	Installation of prefabricated inground vinyl pools
Seamless spray flooring	Vinyl siding
Installation of service station equipment	Installation of wastewater treatment equipment
Sewage disposal systems (50,000 gallons)	Water catchment, storage, and transmission
Installation of sliding acoustical panels for containment of sound; installation of floating floors	Construction of water cooling devices
Installation of sludge treatment equipment	Application of water repellents and preservatives on wood, metal, and concrete
Sewage sludge incinerators and related equipment	Application of monopole waterproofing system
Installation and connection of prepackaged sewage treatment plants including necessary sanitation lines, not to exceed 10,000 gallons	Membrane waterproofing
Installation of simulated stone	Waterproofing
Soil stabilization, epoxy injection, erosion control	Waterproofing (limited to application of texture coatings, silicone sprays, and rubber deck coatings)
Installation of solar swimming pool heaters (limited to swimming pool heating)	Wood treatment
	Wrecking of small dwellings and road rights-of-way
	Wrecking of wood structures

Source: Listing dated July 22, 1981, provided by the Department of Commerce and Consumer Affairs.

the public has no way of knowing whether it should be dealing with a licensed or unlicensed contractor in certain kinds of work; and finally, practitioners have no way of determining whether they are free to practice or whether they are engaging illegally in an activity which should be licensed.

Most of the licenses that are being granted are not for work that is unique or unrelated to work in the official listed C classifications. Many of the C-68 subspecialties overlap with the official specialty classifications and some of the C-68 subspecialty classes have more licensees than the official classifications. For example, there are official specialties for solar heating: C-61, solar energy systems contracting; C-61a, solar hot water systems contractor; and C-61b, solar heating and cooling systems contractor. Yet, there are similar subspecialties under C-68 for solar heating system, solar heating devices, solar energy systems, and installation of solar heating systems. What the differences are is nowhere defined. There are no licensees in the official C-61b specialty but there are 17 licensees in the C-68 subspecialty for solar heating.

Carpet laying contractor is specialty C-7; yet, 18 licensees hold a C-68 license for the subspecialty carpet laying. There are specialty license categories for painting and decorating and for wall covering; yet, 21 licensees currently hold a C-68 license under a subspecialty of interior design.

We were informed that these C-68 licenses are being given to those individuals who either do not qualify for or do not wish to perform the entire scope of work for a listed C specialty classification. By accommodating these individuals, the board is allowing further unnecessary fragmentation of the existing classifications, again without any evidence that this in any way benefits the public. In addition, by licensing as C-68s those individuals who do not qualify for an official C specialty license, the board is, in effect, arbitrarily waiving licensing requirements for these specialties. The board has no guidelines on when it will require applicants to qualify for the entire specialty and deny a license to those who do not qualify and when it will allow those who do not qualify to be given a C-68 license.

The board has no policies or procedures on how to deal with these C-68 applications. Routine approval appears to be the prevalent practice. Between January 1981 and August 1982 the board approved 26 applications for C-68 licenses. With one

exception, the minutes do not show any substantive board discussion on why these applicants should be given C-68 licenses or whether these are unique occupations or any of the other questions that should be raised. To a large extent, the board has left these issues to its executive secretary and relies on his recommendations.

In the absence of any guidelines or criteria on the use of the C-68 license and the present loose practices, the result is arbitrary actions. There is also the possibility of abuse. It must be remembered that these licenses are being sought by applicants and that they are not being imposed by the board. The license confers an economic benefit on the licensee by allowing him or her the right to practice in a certain activity. And the narrower the subspecialty, the more exclusive it becomes.

In addition to the above, we found 18 contractors holding licenses for two categories that appear in neither the rules nor any other listing. They are C-45 and C-58, which are not now specialty licensing categories, although they apparently were at one time. Four of five C-45 licensees hold no other license. Six of the 13 C-58 licensees also hold no other license. This means that there are 10 contractors licensed to perform work (whatever it is) in non-existent classifications.

The board should cease immediately its licensing of additional C-68 subspecialties pending an overall review of specialty licensing. Immediate steps should be taken to identify work performed by each C-68 licensee. Those who appropriately belong in officially established specialties should have their licenses reassigned to that classification, provided they qualify. Those specialties that are not directly related to construction work or pose no danger to the public should not be licensed. Finally, the board should proceed to public hearing on those unique subspecialty classifications that warrant licensing.

Complaints Management

The handling of complaints against contractors is seriously deficient. At the time of our evaluation, cases were backlogged for some three years, an occasional case even longer. In 1982, we reported that 40 percent of the complaints against contractors that were referred for investigation took between 91 and 360 days to complete the investigation phase. Should it be decided by the board that the complaint should be referred

for a hearing, it took the attorney general's office an average of nine months to prepare the case for hearing.¹⁶ To this must be added the time interval between the Attorney General's request for hearing and the actual hearing and between the hearing and the issuance of a recommended order from the hearings officer. At the time of this evaluation, the situation had deteriorated further as few cases were brought to hearing in 1982. A period of three years from initiation of complaint to resolution is not uncommon.

Consumers with problems are ill-served by a process that is so unresponsive. Often, after waiting a considerable period of time, the consumer finally learns that no help is forthcoming from the department. Delays in investigating and resolving complaints also mean that unscrupulous or fraudulent contractors can continue to operate for months and years without having their licenses suspended or revoked.

In one instance, DCCA received 28 complaints about a responsible managing employee (RME) who was in charge of two companies. These complaints began in 1979. In each case, the RME took an advance deposit and did no work. The RME settled some of the earlier cases, apparently by taking deposits from new customers to pay off the earlier complaints. Eventually, he got into so much financial trouble, his corporations filed for bankruptcy before a hearing on the complaints could be held. In the meantime, the contractor's recovery fund was tapped to pay five civil suits thereby terminating the contractor's licenses.

Twenty-three months went by from the time the first complaint to reach hearing was filed with DCCA until the board accepted the hearings officer's report. That report, however, simply accepted a settlement agreement by the contractor to the effect that the contractor would no longer conduct contracting work. But that result was academic since the contractor's license had already been terminated and his company had filed for bankruptcy.

During the interim, many consumers were bilked out of their deposits, some amounting to thousands of dollars. The unfortunate complainants received little satisfaction when two and a half years after their complaints they received a letter from DCCA informing them that the contractor's license had been canceled and that they should seek civil recourse if they had sustained financial damages.

16. Legislative Auditor of the State of Hawaii, *Evaluation of the Professional and Vocational Licensing Program of the Department of Regulatory Agencies*, Report No. 82-1, January 1982, p. 48.

Even though there may be a dozen major complaints against a particular contractor, DCCA staff cannot reveal anything about investigations under way. Not until a formal hearing and board action have established a case of malpractice can such information be divulged. Consequently, DCCA staff are put in the uncomfortable position of having to give to an inquiring consumer a clean status on a contractor's license that should have been revoked long ago. The longer it takes to bring an errant contractor to final account, the more time there is for that contractor to compile a record of serious malpractice.

As a result of the problems in the overall complaints process, the Legislature in 1982 created a compliance resolution fund supported by a surcharge on all licensees in all categories. This fund is supposed to provide DCCA with the means to hire more investigators, its own attorneys, and hearings officers. The DCCA is now in the process of reorganizing and is in transition to the new program.

Under the new system, complaints will no longer be received by the executive secretaries of the various boards. All complaints will be channeled to a central point at the regulated industries complaints office (RICO). The RICO will have its own team of investigators and its own attorneys to prepare cases for hearings. The DCCA staff expect that the reorganization and the augmented staff will eventually overcome the present backlog and reduce the hearings process to between three and seven months. Certainly a three or even a seven month process is better than two or three years, but that many months can still be too long in terms of protecting the public, and RICO estimates that it will take three years to clear up the backlog.

The RICO must make a greater effort to develop and institute an efficient case management system. This was never done in the past. During our review of complaints relating to contractors it became evident that there is no systematic case management. It was difficult to determine the status of cases under investigation as investigation reports were not logged systematically, files were not where they were supposed to be, folders were removed without any record of who had them, and there was little overall supervision or monitoring of the progress of investigations.

An efficient case management system will require training to increase the skills of the investigators. As a substantial number of all complaints are about contractors, RICO should have some personnel who will concentrate and specialize in this area. The RICO should also have policies which can be used to establish priorities for the investigation of

complaints and for decisions on how far each complaint should be pursued. At the present time, no priorities are set and those cases that are likely to have a greater impact on consumers are handled just like any other complaint. For example, priorities could be set so that licensees with a number of complaints against them would be handled more expeditiously.

More effort should also be placed on investigating licensees who violate Chapter 444 with a view to revoking and suspending their licenses. At the present time, the department emphasizes the settling of complaints. If the individual complainant is satisfied, the case is not pursued even in the case of fraudulent behavior or other acts that are in violation of Chapter 444. For example, the licensee can settle with the first few complainants by paying back their deposits and the department will close the cases. However, the licensee can continue to take deposits from subsequent customers, as happened in the example given earlier.

The board should take more vigorous action against unscrupulous and unqualified licensees. Between July 1980 and July 1982, 55 complaint cases went through hearing. Contractors' licenses were revoked in only three cases. Licenses were suspended in 11 cases. In 15 cases, the licensees were fined amounts between \$200–\$500. Given the time and effort to take all these cases through hearing, it hardly seem worthwhile to assess that small a fine.

In view of the number of complaints and the delays, the department might consider adopting alternative or additional procedures to handle complaints more effectively. Following are some procedures that appear to be working well elsewhere.

The department might consider instituting a calendar call system which is currently being used in the family courts. This system has been suggested to RICO by a former hearings officer familiar with the complaints process. In the family courts, each juvenile meets with an intake officer and a public defender within three weeks of apprehension or referral before meeting with the judge. The youth can decide whether to ask for a full trial or to enter a plea that day. A major portion of cases are settled immediately. Time is not wasted on long preparation, and more staff time is available for the more complicated cases. The calendar call system would have to be modified for use in an administrative setting and perhaps could be instituted on a trial basis. All cases could go to a hearings officer within a short period after the complaint is filed. If the contractor

does not contest the complaint, the case can go immediately to the board for final disposition. Should the contractor request a full investigation and hearing, more time would be required but nothing would be lost.

Another possibility is the citation system which has been implemented by the California State Contractors Licensing Board. Based on investigation reports, regional office deputies determine whether there have been violations in the law or deficiencies in workmanship. The regional deputy is authorized to issue citations including civil penalties of \$50–\$1,500. The citation describes the violation, it may order corrective work to be done, and it sets deadlines for such work. The licensee has the option to appeal the citation but this must be done within 15 days. Resolution of citations include corrective work, restitution, reimbursement or payment of fines.

Yet another technique is the development of a *Manual of Workmanship Standards* such as that developed by the Arizona Registrar of Contractors. The manual establishes standards for measuring workmanship complaints in frequently encountered problem areas. It serves as a guide to investigators and hearings officers as well as providing information to consumers on how to file complaints and on what kinds of complaints are within an acceptable level of tolerance or are truly deficiencies in workmanship. The manual has standards for a variety of work, including concrete, cracking of slabs, roofing, etc.¹⁷

These kinds of strategies may be effective in assisting the department to move more swiftly in investigating and resolving complaints. They should be reviewed by the department to determine if they might be adapted for use in Hawaii.

Recovery Fund

The Legislature established the contractors recovery fund as a means of providing restitution to homeowners who suffer losses in their dealings with contractors. Recovery from the fund is limited to owners or lessees of private residences, condominiums or cooperative units, and the amount of recovery is limited to the actual damage suffered by the claimant, including court costs and fees and reasonable attorney fees.

17. Arizona Registrar of Contractors, *Manual of Workmanship Standards*, October 1980.

All licensed contractors were initially assessed \$50 to be deposited into the fund at the time they renewed their license in 1974. Since then, all new applicants for a contractors license have been assessed \$150 to be deposited into the fund. In 1978, all contractors were reassessed \$150 to replenish the fund. During the four year period between July 1978 and June 1982, expenditures amounted to \$280,166 of which \$198,526 was paid out for claims and \$81,640 for legal fees. As of June 30, 1982, there was a fund balance of \$459,000 in the contractors recovery fund.

The Legislature imposed two limits on claims:

- . \$10,000 maximum per injured party, and
- . \$20,000 in total claims against any one contractor unless the contractor pays back to the fund all or some of what was paid out on that contractor's behalf.

It would be appropriate for the Legislature to consider raising the maximum amount that an individual homeowner can recover. The \$10,000 limit has not been changed since 1973 even though the construction cost index has increased significantly. In fiscal year 1981-82, 11 claims were paid from the fund. Of these, five were for the maximum of \$10,000, and it is possible that homeowners would have received fuller restitution if the maximum had been higher. The Legislature should also consider removing the limit of \$20,000 for claims against any one licensee. Since it is possible for any number of homeowners to be injured by a single licensee, this provision discriminates unfairly against later claimants.

Conclusion

Our evaluation shows that there is a continued need to regulate construction contractors. However, a number of improvements are needed in licensing operations. Of particular concern are the board's operations in those areas in which there is no specific statutory authority: the granting of conditional licenses and the issuing of undefined subspecialty licenses. In each case, the board is granting licenses to those who do not meet official standards established by law or by its own rules. Finally, even as DCCA overhauls the existing complaints handling process, there are alternative strategies and procedures that should be considered to provide more effective response and protection to the public.

Recommendations

We recommend the following:

1. *Chapter 444, HRS, be reenacted to continue the licensing of construction contractors but amended to remove the requirements for residency and good moral character.*

2. *The board remove the requirement for applicants to meet financial capacity, as revealed by their financial statements, and instead, emphasize proper review of the credit reports of applicants to determine whether applicants are financially responsible.*

3. *The board improve the Part I examinations on the law, rules, codes, and basic managerial and business practices needed in construction contracting while eliminating the Part II examinations for each of the classifications.*

4. *The board establish guidelines and provide clearer instructions to applicants on the kinds of experience it will accept. The board should also provide greater flexibility in fulfilling the experience requirement by allowing education, training, and work as an apprentice or journeyman to count towards satisfying the experience requirement.*

5. *The board cease its practice of giving conditional licenses and amend its rules accordingly.*

6. *Chapter 444, HRS, be amended to remove restrictions on general contracting activity and the board adopt criteria and guidelines for evaluating all specialty and subspecialty classifications to determine if they meet the standards set forth in the law. The board should review all C-68 licenses to make sure that they are unrelated to existing specialty classifications and prepare to go to public hearing on those subspecialties that it intends to retain.*

7. *The department take immediate steps to develop and implement a complaints management system with emphasis on more efficient and effective case management. In doing so, the department must develop policies on priorities and the courses of action it intends to pursue in complaint cases. Consideration should be given to adapting strategies such as a calendar call system, citation system, or a manual to expedite the complaints process.*

8. *Chapter 444, HRS, be amended to raise the maximum amount of \$10,000 that a homeowner can recover from the contractors recovery fund and to remove the limitation of \$20,000 for recovery of funds from any one licensee.*

APPENDIX
RESPONSES OF AFFECTED AGENCIES

COMMENTS ON AGENCY RESPONSES

A preliminary draft of this Sunset Evaluation Report was transmitted on December 3, 1982 to the Contractors License Board and the Department of Commerce and Consumer Affairs for their review and comments. A copy of the transmittal letter to the board is included as Attachment 1 of this appendix. A similar letter was sent to the department. The responses from the board and the department are included as Attachments 2 and 3.

The board has responded to each of the recommendations made in the report. On the need for regulation, the board suggests that consideration be given to regulating only those contractors engaged in residential housing, home improvements and repairs, because commercial, industrial, and institutional contractors are seldom the subject of complaints. While this alternative was not discussed in our report and while there may be some problems in differentiating among the different types of contractors, the board's suggestion to concentrate the regulatory system on protecting the "unsophisticated consumer" is an approach which the Legislature might wish to consider.

The board disagrees with our recommendation on eliminating the requirement for applicants to demonstrate financial capacity, although it acknowledges that "requiring financial statements of licensed contractors at renewal is probably not cost-effective." The board also takes exception to our recommendation that it provide greater flexibility for applicants to fulfill the experience requirement, but it does say that it is reviewing its rules in this area to make them clearer.

The board takes exception as well to our recommendation that it cease awarding conditional licenses, which are, in effect, probationary licenses, and which are not specifically authorized by statute. The board says that this method prevents applicants from acting as unlicensed contractors and it knows of few conditional licensees who have been disciplinary problems. Because conditional licenses have been given to some applicants with outstanding judgments, tax liens and lawsuits, our assessment is that this licensing category detracts from, rather than enhances public protection as the board contends.

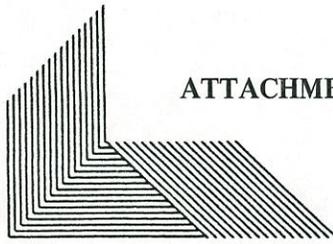
The board agrees with our recommendation that more emphasis be placed on the Part I examination which tests general knowledge of contracting and relevant laws. It also acknowledges the complexity of developing Part II examinations to test knowledge on each trade. Our evaluation recommends that the Part II examinations be eliminated.

The board, in turn, notes that some \$20,000 has already been committed to upgrade craft examinations, and that the process of keeping up with examinations is a “never-ending process,” which, if it is pursued, would require far greater resources. The board also agrees that the vast number of specialty classifications has led to problems and it is now studying improvements that can be made in this area, including creating a small number of specialty classifications under which subcontractors would be licensed. The board agrees as well with our assessment of problems in the complaints management procedures.

Finally, the board cautions that removing the limit of \$10,000 per incident and \$20,000 per contractor that homeowners may recover from the contractors recovery fund might result in fee increases. Our evaluation recommends raising (not eliminating) the \$10,000 limit per incident because the limit has not been adjusted since 1973 even though the construction cost index has increased significantly, and eliminating the \$20,000 limit per contractor since the provision discriminates unfairly against later claimants.

The Department of Commerce and Consumer Affairs responds that new procedures in its Regulated Industries Complaints Office should improve dramatically its ability to respond effectively to consumer complaints. The department also responded to our recommendation on examinations by agreeing that Part I of the examination should be improved but it says that the Part II examinations should be retained as the department has taken steps to revise and develop examinations for 56 categories of contracting. However, this still leaves a large number of specialty classifications without examinations. As the board has pointed out in its response, to keep current and to upgrade all examinations would be a never ending process requiring large expenditures and a larger full-time staff.

THE OFFICE OF THE AUDITOR
STATE OF HAWAII
465 S. KING STREET, RM. 500
HONOLULU, HAWAII 96813
(808) 548-2450



ATTACHMENT 1

CLINTON T. TANIMURA
AUDITOR
RALPH W. KONDO
DEPUTY AUDITOR

December 3, 1982

Mr. William W. Wilmore, Chairman
Contractors License Board
Department of Commerce and Consumer Affairs
State of Hawaii
Honolulu, Hawaii 96813

Dear Mr. Wilmore:

Enclosed are 14 preliminary copies, numbered 4 through 17, of our *Sunset Evaluation Report, Contractors*. These copies are for review by you, other members of the board, and your executive secretary. This preliminary report has also been transmitted to Dr. Mary G. F. Bitterman, Director, Department of Commerce and Consumer Affairs.

The report contains our recommendations relating to the regulation of contractors. If you have any comments on our recommendations, we would appreciate receiving them by January 3, 1983. Any comments we receive will be included as part of the final report which will be submitted to the Legislature.

Since the report is not in final form and changes may possibly be made to it, access to this report should be restricted solely to board members and those officials whom you might wish to call upon to assist you in your response. We request that you exercise controls over access to the report and ensure that the report will not be reproduced. Should you require additional copies, please contact our office. Public release of the report will be made solely by our office and only after the report is published in its final form.

We appreciate the assistance and cooperation extended to us.

Sincerely,

Clinton T. Tanimura
Legislative Auditor

Enclosures

ATTACHMENT 2



GEORGE R. ARIYOSHI
GOVERNOR

MARY G. F. BITTERMAN
DIRECTOR

DICK H. OKAJI
LICENSING ADMINISTRATOR

CONTRACTORS LICENSE BOARD

STATE OF HAWAII

PROFESSIONAL & VOCATIONAL LICENSING DIVISION

DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS

P. O. BOX 3469

HONOLULU, HAWAII 96801

December 30, 1982

RECEIVED

JAN 3 11 29 AM '83

OFC. OF THE AUDITOR
STATE OF HAWAII

Office of the Auditor
Attention: Mr. Clinton T. Tanimura
State of Hawaii
465 S. King Street, Room 500
Honolulu, HI 96813

Gentlemen:

RE: COMMENTS ON THE SUNSET EVALUATION REPORT, CONTRACTORS,
CHAPTER 444, HAWAII REVISED STATUTES

In response to your invitation, the Contractors License Board (CLB) is commenting on your preliminary report received December 3, 1982. Your office is to be complimented on a very detailed, thorough report; we take exception to many of your conclusions and therefore the recommendations flowing therefrom.

Item (1) The Need for Regulation

You make the case that the unsophisticated consumer is neither qualified nor can afford to have expert advice in selecting contractors. On the other hand, the sophisticated consumer (industrial and commercial firms and developers) do. We agree with this analysis and therefore recommend consideration to deregulate the portion of the construction industry that deals with industrial firms, commercial businesses, real estate developers, government, and other sophisticated knowledgeable industries. Only residential housing, home improvements, and repairs should be regulated. It should be noted that the great majority of commercial, industrial, and institutional contractors seldom are the subject of complaints and disciplinary action. This line of reasoning has been implemented in Arizona with much success.

The results of such a system would, in our opinion, save countless dollars, and free needed regulatory personnel and facilities to concentrate on protecting the "unsophisticated consumer." This system would place the cost of regulation on the segment of the industry that really requires regulation.

Item (2) Financial Capacity

Your report speaks to the CLB's system of determining an applicant's financial capabilities and specifically recommends the elimination of the requirement to submit financial statements. While we have to agree that a sound financial statement is no guarantee of a successful or honest contractor, it does provide for the thoughtful, careful consideration by the applicant to acquire sufficient working capital to begin his business. No business can be started today without some working capital. Our guidelines (Page 3-4, your report) are quite modest and in most instances do not limit entry into the business arena.

Reliance on a routine credit report tells us nothing about the contractor's ability to finance his projects prior to receipt of monthly progress payments.

Lack of working capital urges the contractor to request up-front money for work not done and tempts him to build up his cash at the expense of his customer. We disagree most strongly with this practice.

We do agree with your conclusion that requiring current financial statements of licensed contractors at renewal is probably not cost-effective. Although we do catch some applicants who have serious financial problems, the ratio may be only a small percent. A point should be made, though, that while we lack adequate staff to systematically review all statements, we do have the expertise to flag serious problem contractors. The question then becomes, is it important to prevent one troubled contractor from re-entering the marketplace? We think so.

A comment on credit reports: these only tell you what has taken place in the past. They do not predict the immediate future. We cannot do our job without access to all of the available tools at our disposal.

Item (3) Examinations

We are inclined to agree with you in this area of concern. While the Department of Commerce and Consumer Affairs has

committed some \$20,000 to upgrade craft examinations, this procedure is a never-ending process. Some states such as Florida place significant emphasis on examinations, spending many hundreds of thousands of dollars each year. The construction industry covers such a wide area of processes, procedures, materials, systems, and practices that to write and keep current all examinations we would have to have a larger full-time staff.

However, we do agree with you that more emphasis should be placed on the business functions (Part I). We would like to suggest that the CLB adapt a system much like the realtors who have developed a comprehensive exam and require successful completion of a formal curriculum to teach the subject material.

Item (4) Experience Requirements

You have quoted Dr. Schimburg as saying, "The experience requirement is undoubtedly the most important prerequisite" (in the construction trades). This is true of any successful business. The important question is, what kind of experience are we seeking? We know that most of the contractor applicants come from the tradesmen. But a competent, successful plumber will not necessarily make a successful plumbing contractor. Even our present rules that require four years in a supervisory capacity often fail to predict a successful business operator. Knowledge of contract law, accounting, finance, lien law, insurance, architecture, engineering, labor law, county and state laws pertaining to building permits, etc., must be employed to mold his business into a profitable, durable operation. Reliable, ethical contractors are generally profitable and knowledgeable in these areas.

We strongly disagree with those who would downgrade the present experience requirements. Considerable flexibility and discretion must be employed to consider the applicant as a whole person; that is, review his total performance history relative to craft, supervisory, and business experience.

The Board in reviewing the experience requirements of an applicant takes a liberal view of the Foreman, Supervising Employee, and Contracting background. For example, credit is given to the applicant who is self-supervised, or a journeyman who has directed an apprentice.

At present, the rules committee is reviewing this experience section of its rules with the intention of making the rules clearer in its interpretation.

You criticize the possibility that a person may spend 10 years before being allowed to apply for and be granted a license. What about doctors, lawyers, accountants, and even barbers? "Experience" takes time to acquire and we shudder to think that we would turn loose on the consuming public a person whose only experience was a few years as an apprentice or beginning journeyman.

Your observation that most of the applicants that appeal are granted a license and that those who don't appeal probably would also be approved. This stems from the fact that most applicants do not know how to fill our application properly. Those individuals who believe they are qualified appeal and after they explain fully their total experience we often agree. Those that do not appeal usually do not have the experience.

Item (5) Conditional Licenses

Conditional licenses do indeed pose a most difficult dilemma. Many applicants are borderline situations, either with regard to experience or financial capability. To arbitrarily deny these people may encourage them to act as unlicensed contractors or withhold the opportunity to earn a living. Placing them into a conditional (or as you indicate, "probationary") status serves notice that they must act with extreme care or they face immediate revocation.

We have knowledge of extremely few conditional licensees who had disciplinary problems. Therefore, we must conclude that it is a workable situation.

We disagree that this practice is not specifically allowed by statute. Withdrawing this procedure would remove another tool to assure that the consuming public is protected.

Item (6) Specialty Classifications

We must agree that the multiplicity of specialty classifications lead to the many problems you discuss. Most states that have license laws report similar problems, particularly in the C-68 classified specialist category.

Previously the Board would grant C-68 specialty classifications when requested. This practice was stopped four years ago. Currently a C-68 classified specialist license is not granted if the request is within the scope of an existing sub-classification.

The Board is currently studying the feasibility of creating a small number of broadly described specialty scopes under which sub-contractors would be licensed. These scopes of operation would allow the sub-contractor the latitude to operate without concerning himself with other specialty licenses or out-of-scope problems.

This concept is revolutionary, as most states now employ the same method of sub-classification as is currently employed by the Hawaii Board.

Item (7) Complaint Management

The Board wholeheartedly agrees with your criticism of the complaint management procedures. We have consistently been critical of the long delays in adjudicating complaints; unfortunately, this has been out of our control. We look forward to the success of "RICO" to make significant progress to provide speedy, decisive disposition of these complaints.

Item (8) Contractors Recovery Fund

We believe the recovery fund is a well thought-out and effective system to protect the public from dishonest, incompetent, and troubled contractors. Many states envy our success.

We do acknowledge your concern that inflation has taken its toll of the value of the statutory limits of \$10,000 per incident and \$20,000 per contractor. However, we urge caution in raising these limits without a simultaneous increase in the fee. We have been successful in maintaining the fund's integrity, but to raise the payout without providing for a compensating fee increase would be irresponsible. We oppose the wholesale elimination of the upper limits. Please bear in mind that these costs will eventually be paid by the consumer.

Item (9) Owner-Builder for New Residences

We further recommend that "owner-builders," exempted under the statute, be required to register as an owner-builder for residential homes without fulfilling the experience or financial requirements. This change would remove the discretion by the City Building Department and prevent the owner-builder that becomes an unlicensed contractor from practicing his trade.

Office of the Auditor
Page Six
December 30, 1982

We thank you for the opportunity to comment on your report. The Board, if re-enacted, will take serious consideration of many of your recommendations.

Very truly yours,

A handwritten signature in cursive script that reads "William W. Wilmore".

William W. Wilmore, Chairman

atlc.

ATTACHMENT 3

GEORGE R. ARIYOSHI
GOVERNOR



MARY G. F. BITTERMAN
DIRECTOR
Commissioner of Securities

STATE OF HAWAII
OFFICE OF THE DIRECTOR
DEPARTMENT OF COMMERCE AND CONSUMER AFFAIRS
1010 RICHARDS STREET
P. O. BOX 541
HONOLULU, HAWAII 96809

DONALD D.H. CHING
DEPUTY DIRECTOR

December 29, 1982

RECEIVED
DEC 30 12 57 PM '82
OFC. OF THE AUDITOR
STATE OF HAWAII

The Honorable Clinton T. Tanimura
Legislative Auditor
State of Hawaii
465 South King Street, Room 500
Honolulu, Hawaii 96813

Dear Mr. Tanimura:

Thank you for the opportunity to comment on your sunset evaluation report on Contractors.

Although the majority of the report deals directly with the Contractors License Board, there is one area which concerns the Department proper. Specifically, the section on complaints management mentions the pivotal role that will be played by the Regulated Industries Complaints Office (RICO) and the Hearings Office (HO) in processing consumer complaints. As mentioned in the report, the Department currently is reorganizing itself to initiate more constructive procedures. On December 1, 1982, all responsibility for the handling of complaints against licensed and unlicensed entities was assigned to RICO. Also, on that date RICO became fully operational.

Pages 3, 23, 24, and 25 contain a number of recommendations concerning a more efficient management of the voluminous number of complaints received by the Department. Recommendations such as having RICO's personnel specialize in certain licensee areas, establishing priorities for investigation and legal action, establishing a uniform complaint status log, and developing training manuals are now being pursued. Other recommendations such as instituting a calendar call system and establishing a citation structure demand more detailed study and contact with other states for guidance based on their experience with such processes.

The Department believes that the complaints management recommendations contained in the report highlight legitimate areas for immediate administrative action and, in some cases, for future legislation. We believe also that our new procedures practiced in RICO will improve dramatically the Department's ability to respond effectively to consumer complaints.

Legislative Auditor's Comments

The Legislative Auditor identified a number of deficiencies in the examinations of the Contractors License Board, particularly with respect to Part II of the examinations.

Generally, the Legislative Auditor criticized the Part II examination requirement as "both unfair and of little use in establishing competence." Specifically, the Auditor noted that:

- (1) A significant number of the C specialty contracting categories (35 of a total of 92 categories) do not require a separate written Part II examination to be administered;
- (2) All 212 sub-specialty C-68 categories do not require a separate written Part II examination to be administered;
- (3) Many of the existing examinations are obsolete;
- (4) The examinations have not been shown to be job or competency related.

Legislative Auditor's Recommendations

The Auditor recommended that the Board improve Part I and delete Part II of all examinations.

Division Comments

We agree that Part I of the examinations should be improved.

We disagree, however, with the Auditor's recommendation that Part II of the examinations should be eliminated. The reasons which support our position are two-fold.

The Honorable Clinton T. Tanimura
Page Three
December 29, 1982

First, we note that while Part I of the examinations tests general knowledge of certain statutes and administrative regulations, Part II of the examinations complements Part I by testing a candidate's knowledge of the particular contracting field to which he is applying. It is our position that Part II of the examinations is a necessary requirement to ensure that a candidate has achieved sufficient mastery of a specific contracting field to warrant public confidence.

Second, we contest the Auditor's finding that the examinations are unreliable and obsolete. Significantly, the Auditor has failed to take into consideration this Department's efforts to revise and develop examinations.

In June 1982, this Department contracted with Professor Harold Ayabe of the University of Hawaii to have the university revise and develop examinations for 56 categories of contracting. Eleven examinations have already been revised and implemented, namely: Contractor "B", Laws and Rules, Electrical C-13, Landscaping C-27, Painting C-33, Welding C-56, Cabinet, Millwork C-5, Drywall C-12, Plumbing C-37, Sheetmetal C-44, Ventilation and Air Conditioning C-52. In addition, the following 39 examinations have been revised and are soon to be implemented: C-40, C-41, C-42, C-42E, C-43, C-42D, C-68 Caulking, Excavating, Cold Applied Felt, Trenching and Concrete Curing, C-1, C-2, C-3, C-4, C-6, C-7, C-9, C-15, C-15A, C-16, C-17, C-18, C-20, C-21, C-22, C-23, C-26, C-30, C-31A, C-31B, C-36, and C-37B.

Recommendation

The Department of Commerce and Consumer Affairs recommends that the Contractors License Board, in conjunction with the Department, should continue to administer Part II of the examinations.

Sincerely yours,



Donald Ching
Acting Director