

**REPORT
 HIGHLIGHTS
 PERFORMANCE AUDIT**

Subject

The Registrar of Contractors (agency) began regulating contractors in 1931. As of January 2003, it had over 41,000 active commercial and residential, general and specialty contractor licenses. The agency also inspects workmanship and investigates violations of laws and rules.

Our Conclusion

The agency should improve consumer protection by identifying and disciplining problem contractors, and by providing the public more complaint information. The agency should also resolve a large deficit in the Residential Contractors' Recovery Fund. Finally, the agency should stop assigning take-home vehicles and eliminate 22 inefficiently used vehicles.



2003

**Consumer Protection
 Can Be Enhanced**

Arizona is one of 12 states that has a central state agency to regulate the construction industry. Investigating complaints about licensed contractors' workmanship to protect consumers is an important aspect of this regulation.

Complaints—Key Facts

- 29—number of certified inspectors
- 10,000—number of complaints filed in 2002
- 17 days—average time to conduct a job site inspection from time complaint received
- 79 percent—percent of complainants reporting they received “excellent service”

Agency should identify and discipline problem contractors—The agency's complaint process may result in some valid complaints being closed without proceeding to a disciplinary hearing. Only about 8 percent of the licenses had a valid complaint filed against them in the past 2 years. When a complaint is filed and an inspector determines it is valid, the agency gives the contractor an opportunity to correct the problem. If the contractor corrects this problems, the case is usually closed without any disciplinary action. While this practice can help resolve the consumer's complaint, in some cases it may allow a problem contractor to repeatedly commit violations, but escape discipline.



The Agency can decide to keep a complaint open to ensure that a disciplinary hearing takes place. In making such a decision, the agency should consider factors such as the severity of the complaint, the dollar value of the problem, and the number of complaints the contractor has received. Few contractors receive multiple complaints—only 1 percent of licenses received three or more complaints in the past 2 years—so a previous history of complaints is important when deciding whether to close a complaint without pursuing disciplinary action.

Need to provide the public more information—Like many state agencies, the Registrar of Contractors has a Web site and phone center to provide information to the public. However, the agency does not provide the public as much information about valid complaints as other regulatory agencies. For example, the Web site does not describe whether a valid complaint involves minor or serious issues. In addition, the agency did not report unconfirmed complaints to the public until February 2003. An unconfirmed complaint is a complaint that the agency cannot confirm because 1) no problem existed, or 2) the contractor has addressed the

consumer's concern before the agency's inspection occurs. Before the agency began reporting this information, the public did not know that a problem may have existed. Other Arizona regulatory agencies report such complaints to the public.

Voluntary "courtesy inspections"—In the 1980s the agency began an informal dispute resolution process between consumers and contractors. This process allowed contractors or consumers to request a "courtesy inspection" and have an inspector informally determine whether a contractor's workmanship met

standards. This process was faster for consumers than a formal complaint and allowed contractors to resolve issues without having a formal complaint filed against them. While there is no statutory authority for this, the agency conducted almost 1,100 of these courtesy inspections in fiscal year 2002. The agency has not reported the results of these inspections to the public.

The agency discontinued these courtesy inspections when auditors pointed out the lack of authority. However, the agency believes that these inspections provide a valuable service and would like to resume them.

Recommendations

The Registrar of Contractors should:

- Consider factors such as the severity of the complaint and the number of previous complaints before deciding to close a complaint and not pursue disciplinary action.
- Make the nature of valid complaints available on its Web site and through its phone center.
- Seek legislation if it wishes to provide courtesy inspections and make the inspection results public.

Recovery Fund Changes Needed

The Legislature established the Residential Contractors' Recovery Fund in 1981 to assist consumers who suffered financial loss due to a licensed residential contractor. Consumers may recover the amount of their actual damages up to \$30,000. Consumers have up to 2 years to file a claim.

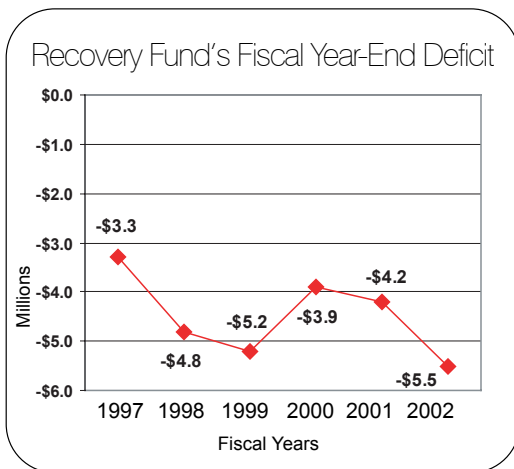
Residential contractors' fees constitute most of the Fund's revenues. Each residential contractor pays an initial \$300 fee to the Recovery Fund and a \$150 annual fee thereafter. In addition to these fees, the Fund earns interest income and receives money recovered from contractors or their bonding companies.

Recovery Fund—Key Facts

- \$30,000—claim limit per consumer
- \$200,000—total claim limit per license
- 515—number of claims paid in FY 2002
- \$3.9 million—total claim amount paid in FY 2002
- 114-153 days—low and high monthly average time to process claims in FY 2002

Recovery Fund deficit—The Fund’s statutes and insurance industry standards require that the Fund have resources to cover all claims. Because consumers have up to 2 years to file a claim, the Fund needs enough resources to pay for the claims that have been filed and those that may be filed in the next 2 years. Statute requires actuarial projections to estimate these anticipated claims.

However, the agency has operated the Fund on a pay-as-you-go basis. Although the Fund’s total liabilities—including anticipated claims—total \$11.6 million, the Fund has net assets of only \$6.1 million as of June 30, 2002. As a result,



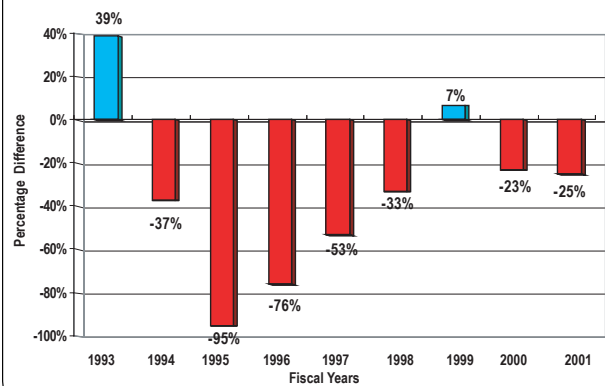
the Fund had approximately a \$5.5 million deficit. The Fund has had at least a \$1 million deficit since 1985 and in the past 6 fiscal years the deficit has been at least \$3 million.

Further, an actuary has never calculated the amounts necessary for the Fund to pay all claims, including anticipated claims. The agency has used a Certified Public Accountant (CPA) to make these estimates and has underestimated the Fund’s anticipated claims for 7 of the past 9 years. These underestimations have ranged from 23 to 95 percent.

Statute requires the agency to assess contractors an additional fee to resolve the Fund’s deficit. Assessing each of the participating contractors approximately \$220 would provide the Fund adequate reserves, based on current claims estimates.

The Fund’s deficit may also affect its administrative expenses. These expenses are limited to 10 percent of the Fund’s balance. Since the Fund is in a deficit situation, administrative expenses would technically not be permitted. Administrative expenses should be linked to Fund revenues, as is the case with other funds like the Arizona State Lottery.

Percentage Difference Between Actual Payments and Estimated Payments from the Recovery Fund¹



Recommendations

The Registrar of Contractors should:

- Contract with a qualified actuary to project anticipated future claims.
- Reassess contractors an amount necessary to resolve the Fund’s deficit.
- Seek statutory changes for a more appropriate method of establishing an administrative cost limit.

Vehicle Fleet Should Be Reduced

The agency leases 65 vehicles from the Department of Administration (DOA).

Take-home vehicles are inappropriate—The agency has assigned over three-fourths of its vehicles to employees as take-home vehicles. The agency should stop this practice because it violates statute and the State Constitutions' public gift clause.

Eliminate inefficiently used vehicles—According to DOA, a vehicle should be used at least 10,000 to 15,000 miles per year to justify its cost. The agency should return 22 vehicles driven fewer than 10,000 miles for the year ending September 30, 2002.

Last year the agency paid more than \$127,500 to lease, maintain, and provide fuel for the 22 inefficiently used vehicles.

It may also be possible to eliminate a number of other vehicles. Agency employees drove 27 vehicles between 10,000 and 15,000 miles, but this includes the commuting miles for the personally assigned take-home vehicles. One year after the agency eliminates the take-home status for its vehicles, it should reassess and eliminate vehicles used less than 10,000 miles per year.

Increase monitoring of vehicle usage—To ensure that employees use vehicles appropriately, the agency needs to better monitor their use. DOA recommends that the agency maintain detailed mileage logs for its vehicles. Such reports would help identify whether employees efficiently and appropriately use the vehicles.

TO OBTAIN MORE INFORMATION

A copy of the full report can be obtained by calling
(602) 553-0333



or by visiting our Web site at:
www.auditorgen.state.az.us

Contact person for this report:
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Recommendations

The Registrar of Contractors should:

- Stop its practice of assigning take-home vehicles to employees.
- Return to DOA the 22 vehicles that are driven fewer than 10,000 miles per year.
- Review whether it can eliminate other vehicles once it stops assigning take-home vehicles.
- Require detailed mileage reports on all vehicles.