WINTER 2015, VOL. 2, ISSUE 4

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Contents

WHAT'S INSIDE

WINTER 2015

32

FEATURES

14 **Hot Topics in Federal Government Contract Compliance**
Here's what surety professionals and their contractors should know.

16 **Fraud Schemes and Related Controls in the Construction Industry**
Fraud in the construction industry takes on many forms, so awareness is vital.

20 **Unravelling the Mystery of Court Bonds**
A brief explanation of the primary types of court bonds that are available, along with a few useful tips for producers and underwriters.

25 **NASBP Attorney Advisory Council Participates in NASBP Regional Meetings**
The AAC was constituted for the purpose of serving as a resource team to NASBP and providing substantive content to NASBP.

26 **Public-Private Partnership Projects**
Consider the bonding process for P3s.

30 **Mining the Value of the NASBP Member Network**
Experienced producers and new agents alike can reap rewards from the Association's membership network.

32 **Applied Education**
The NASBP Surety School provides tools to use every day.

DEPARTMENTS

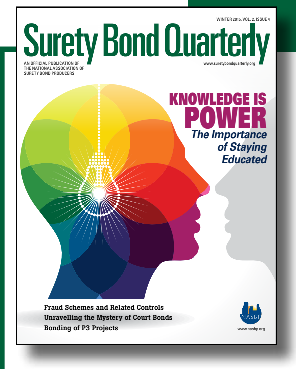
7 **NASBP Upcoming Meetings & Events**

7 **2015-2016 Executive Committee**

8 **From the CEO**

10 **Practical Insights: What You Need to Know**

34 **Index to Advertisers**



ON THE COVER

WINTER 2015

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From understanding ever-changing laws and compliance requirements to avoiding damage caused by fraud, this issue will help you retain your status as the best and brightest in the industry.

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Surety Bond Quarterly is brought to you by the National Association of Surety Bond Producers, 1140 19th St. NW, Suite 800, Washington, DC 20036-5104; Phone: 202.686.3700; Fax: 202.686.3656; **www.nasbp.org. NASBP Manager:** Kathy Jo Mapes Hoffman

Published by: Naylor Association Solutions, 5950 NW 1st Place, Gainesville, FL 32607; Phone: 800.369.6220; Fax: 352.331.3525; **www.naylor.com. Publisher:** Heidi Boe, **Editor:** Christine Cusatis, **Project Manager:** Douglas Swindler, **Marketing:** Catherine Rios, **Advertising Director:** Doug Smith, **Advertising Sales:** Shane Holt, Rick Jones, Daniel Narvaez, Jason Zawada, **Layout & Design:** Manish Dutt Sharma

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Colorado Springs, CO

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June 7–8, 2016
Washington, DC

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June 9, 2016
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August 1–5, 2016
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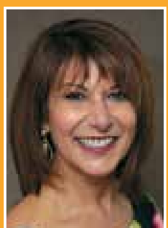

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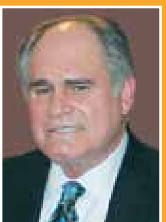

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Never Forget Your Latin:
Ignorantia Juris Non Excusat

For those who never had the opportunity to learn Latin or to attend law school (you may have been fortunate in both cases), the Latin maxim *ignorantia juris non excusat* can be translated to "ignorance of the law excuses not." Code-based legal systems may use the Latin phrase *ignorantia iuris nocet*, which translates to "not knowing the law is harmful." I am sure that you are familiar with this legal principle or maxim. Perhaps you have received a traffic citation or other legal violation that has brought the meaning of the maxim to your personal experience. This principle is very much alive today and seems to resound with increasing significance in the experiences of those pursuing public construction contracts and of those supporting them.

Public construction procurement and the legal compliance requirements surrounding such procurements have grown increasingly numerous and complex over the last several decades. Nonetheless, under our legal system, everyone is imputed with knowledge of the laws surrounding public procurements. If you fail fully to comprehend that the federal government has set specific compliance expectations of its contractors, you may head down an inadvertent path that could place your ability to work with the government in the future and, in turn, the viability of your company in jeopardy. And ignorance is no excuse, even if the laws are conflicting, confusing, or unclear.

What to do? The antithesis of ignorance is knowledge. Though a Herculean task, being aware of and educated on the myriad and changing laws and requirements is a must. Read, read, and read. Find knowledgeable attorneys who can acquaint you with changes in the procurement landscape and can answer your questions. Learn from your construction clients as to what they are facing and why, and help them connect with the proper professionals to analyze their challenges, so they undertake the right actions and maintain compliance. A team approach to spot potential issues definitely is required, and your clients will, no doubt, appreciate the extra set of watchful eyes.

Part of this issue of *Surety Bond Quarterly* is devoted to making you more aware of your clients' legal and compliance challenges in the public procurement arena. Barron Avery, an attorney in the Washington, DC, office of the law firm of BakerHostetler, provides an introduction to complying with the many federal construction requirements in today's federal procurement marketplace. This is the first in a series of articles on this critical topic. Ernest Brown with the law firm of Smith, Curries & Hancock in the San Francisco and Los Angeles, California offices informs us of the threats posed to sureties by contractors failing to maintain proper licensure or of pursuing work without a license. And, in the public-private partnership context, Todd Regan of the Hartford, Connecticut office of the law firm of Robinson & Cole, LLP acquaints us with some of the unique risks faced by P3 contractors and by the sureties providing them surety credit.

Increasing your knowledge can pay significant dividends in mitigating the possibility of future problems, but preparedness for the occurrence of problems also must play a role. It comes as no surprise to you that insurance is just for that purpose. The occurrence of business fraud has been a story of late in many news reports. Any business, including construction businesses, can be a victim, even from their own employees (actually, the most likely source). Internal fraud leads to other problems, including compliance problems on public contracts. This issue of *Surety Bond Quarterly* contains an article from accountant Jeremy Clopton of the accounting firm of BKD that explores why and how construction firms need to be vigilant against incidences of internal fraud and the products available, commercial crime policies and fidelity bonds, which exist to help address the damage done by such fraud. This is an insightful and informative article.

Now that I have laid out the critical information in this issue, do you have an excuse for not reading it cover-to-cover? Ignorance is not bliss, as they say.

Warm wishes,

Mark McCallum
NASBP CEO

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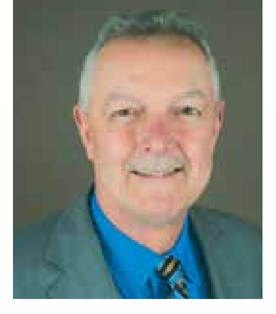

BY ERNEST C. BROWN

Unlicensed Contractors A Threat to Their Sureties

THE LAPSE OF a contractor's construction license can be a big problem for its surety.

A surety must heavily rely upon its principal to comply with applicable business requirements, including the qualification to do business in the jurisdiction of the project and a valid contractor's license. However, a contractor's license can be quickly suspended or revoked for failure to pay fees, update names of officers, maintain worker's compensation insurance, or renew the license bond. A failure to obtain a proper license may occur when contractors form joint ventures or enter a new state to obtain new work. These are generally matters of record that can be verified on the licensing board's website.

The principal's contractor's license can also be voided as a sanction for failing to appear at a disciplinary hearing or similar agency action. In addition, if the principal performs work outside of the scope of its license or if its work is not closely observed or managed by the licensed individual, the construction entity may be found to have performed unlicensed work. These are circumstances not likely to be reflected in public records at the time.

In most states, contractors face serious consequences for performing unlicensed work. Contractor licensing laws generally reflect a public policy of protecting the public from dishonest and incompetent contractors. The licensing requirements provide a minimal degree of assurance that persons offering contracting performance have the requisite skill and character. Once the lack of license is discovered, the contractor will generally be fired by its client and invoices will go unpaid.

Further negative ramifications of doing unlicensed work may include a judicial finding of negligence *per se* for work performed, an assessment of civil penalties, a permanent license suspension, debarment, and other severe penalties. Where there has been a tragic loss of life or serious bodily injury, there is a very real threat of criminal prosecution.

In California, a contractor is prohibited from enforcing a contract if it

was not properly licensed the entire time the contract was being solicited, created or performed. Under the California Business & Professions Code § 7031, a party cannot bring an action in law or equity to collect compensation for services unless he or she proves that he or she was licensed when the services were performed. This is true whether the contractor is a general contractor, a subcontractor or a supplier performing unlicensed installation work. He or she will not collect anything for labor, goods or other services. Where a general contractor is found to be unlicensed, its surety will be subject to numerous labor and materials claims by subcontractors, vendors, employees, and their union trust funds. And, of course, the owner will also want the project to be completed by the surety under the performance guarantee. These are the type of claims where the entire penal sum can be consumed.

Federal contracts, bonds and licenses

In the federal construction environment, the Miller Act and relevant regulations require contracts over $150,000 to have surety bonds equal to the contract price. By guaranteeing payment to covered subcontractors and suppliers engaged in public works construction, the Act protects certain subcontractors and material suppliers involved in the construction of federal public buildings. Such entities cannot place liens against federal property to recover unpaid amounts. A general contractor put out of business by a licensing issue will likely be unable to pay the amounts due subcontractors and material suppliers, and the surety would be on the hook for those expenses and costs.

Interestingly, the risk to the surety for bonding an unlicensed general contractor on a federal contract is lessened by federal preemption. There is considerable Miller Act and related case law stating that state contracting licensing laws are preempted by the federal procurement law. See, for example, *Gartrell Construction Co. v. Aubry*, 940 F.2d 437, 438 (9th Cir. 1991). The underlying argument is that the federal government is selecting the contractor, under laws passed by Congress, and that states and local jurisdictions cannot regulate the federal government's selection process through the imposition of a local licensing process. (For example, the U.S. Congress does not want its military construction efforts in time of war being blocked by the state of Hawaii's Contractor's License Board.)

There is a substantial body of law, however, that indicates the federal exemption **does not** apply to subcontractors. See, for example, *U.S. ex rel. Technica, LLC v. Carolina Casualty Insurance*, 2011 WL 1121276 (S.D. Cal. June 29, 2010). In that case Technica was a subcontractor on a federal construction project but was not licensed in the state. The California statute precluding a non-licensed contractor from suing in California was applicable to a "second-tier contractor" that contracted with a subcontractor to provide labor and other services on a Miller Act project. Although U.S. Supreme Court and Ninth Circuit precedent prohibits a state from requiring a general contractor to be licensed in the state when the contractor enters into a contract to perform work on a federal construction project, the prohibition does not apply to second-tier contractors. See also *Stellar J Corp. v. Smith & Loveless, Inc.*, 749 F. Supp. 2d 1137 (D. Or. 2010)(a subcontractor was not licensed at the time it performed the work on the bonded project and failed to obtain a license before filing its counterclaims, so it was precluded from challenging the contractor's unlicensed contractor defense). Thus, in federal contracting, the surety's risk is much higher when bonding a subcontractor or supplier (that does unlicensed work). As the federal government does not directly select subcontractors, so there is arguably no federal preemption regarding their selection. So, the argument goes, subcontractors are subject to local licensing laws. Of course, some federal subcontractors require approval by the federal government–especially in high security and military environments–so the licensing law might still be preempted in those situations.

If a federal subcontractor is not licensed, it may be prohibited from completing the project or exercising its Miller Act rights. And its surety may, therefore, be on the hook for its sub-subcontractor's, supplier's and employee's claims, as well as the subcontract completion costs.

State and local contracts

The risk to the surety for failure of its principal to obtain or maintain its contractor's license is far more severe in state and local contracts. All fifty states have enacted statutes that require surety bonds for state and local government construction contracts. These are often referred to as "Little Miller Acts."

A general contractor entering into such contracts must provide a labor and materials bond and a performance bond. These state and local bonding requirements often have broader categories of claimants. As stated above, any failure of the general contractor's license places the performance and payment surety in

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the bullseye of claims for completion and outstanding labor and material claims.

In certain instances, a lack of a subcontractor's license benefits a general contractor's surety. The California Supreme Court has held that an unlicensed second-tier subcontractor could not recover against a subcontractor **or its surety** where it started the work before it became licensed. See *MW Erectors, Inc. v. Niederhauser Ornamental and Metal Works Co., Inc.,* 36 Cal. 4th 412 (2005). See also *Steller J Corp. v. Smith & Loveless, Inc.,* 749 F. Supp. 2d 1137 (D. Or. 2010) (a subcontractor that was not licensed at the time it performed the work on a bonded project and failed to obtain a license before filing its counterclaims was precluded from challenging the contractor's unlicensed contractor defense; contractor and surety were entitled to summary judgment against the subcontractor).

Surety takeover agreements

There is also a longstanding controversy over whether a surety must obtain a contractor's license when it takes over a project under the performance guarantee. Generally, a surety is only liable for the penal sum of the bond, the definite amount on the face of the bond based on the underlying contract amount. See *Bill Curphy Co. v. Elliott,* 207 F.2d 103 (5th Cir. 1953) (Texas); *Mayor & City Council of Baltimore v. Fidelity & Deposit Co. of Md.,* 386 A.2d 749 (Md. 1978). However, in the event of nonperformance by the contractor, a surety can elect to step into the shoes of the principal and complete performance or cause the work to be completed. In most takeover situations, the surety will simply hire a licensed contractor.

However, the surety's liability is not limited to the penal sum; and it may be accused of acting as an unlicensed contractor and be at risk for the same range of financial losses set forth above. *International Fidelity Insurance Co. v. County of Rockland,* 98 F. Supp. 2d 400 (S.D.N.Y. 2000) (when a contractor defaults, and the surety then elects to take over its principal's contract under the provisions of the performance bond and to complete the contract on its own or hire an agent to do so, the surety ordinarily will be subject to liability beyond the penal limit of the bond). Under the 2010 AIA A312 bond form, a surety's liability is specifically **not** limited to the amount of the bond in the case of a takeover action. ●

Strategic Guidance

What can sureties do to prevent contractor license lapses and mitigate problems?

1. Check the license status of any principal requesting a bond with the relevant state licensing board and/or official website.
2. Become an expert (or hire someone who is) in local licensing laws to verify eligibility.
3. Keep a notebook of contractor "Qualifications to Do Business" and current licenses.
4. Calendar the filing and renewal dates for major contractors that carry substantial bonding.
5. Be sure the responsible managing employee (RME) and responsible managing officers (RMO) of your principal are active in the business. This is a statutory requirement in many states.
6. Request special notices for any cancellation or lapse of the contractor's license bond and workers' compensation insurance.
7. Regularly check the license status for pending disciplinary issues.
8. Hire a fully licensed contractor for situations where the surety must complete the work.
9. Verify local license laws to be sure the surety is properly licensed, if required.

How can sureties respond to allegations of lack of a license?

1. Hire a third party (licensed attorney) to do a contractor license investigation.
2. Encourage the contractor's legal team to immediately correct any deficiencies.
3. Attempt to get retroactive extensions of time to correct lapses.
4. Work with local license experts to restore the license and explain gaps.
5. Look for a "federal nexus" that might create federal license preemption.
6. Investigate the boundaries of "substantial compliance" in the jurisdiction.
7. Do not compound the problem by involving other "unlicensed" individuals.
8. Attempt to limit the damages by creating a "workout atmosphere."
9. Keep in mind the contractor's risk of exposure on other projects.
10. Call a construction lawyer who understands contractor licensing in the relevant jurisdiction.

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Hot Topics in Federal Government Contract COMPLIANCE

Here's what surety professionals and their contractors should know.

This is the first in a series of five articles on federal government contract compliance requirements that contractors often fail to satisfy.

BY W. BARRON A. AVERY

WHEN IT COMES to federal government contracting, compliance can be the last item that construction contractors want to address. It can be burdensome and time-consuming, and every dollar amount that a contractor devotes to compliance cuts into a contractor's bottom line. Despite the arduous nature of compliance, however, the risks and consequences of not complying with contractual requirements far outweigh the burdens encountered and the costs of compliance. These risks, consequences, and costs are particularly outweighed when compared to the relatively straightforward compliance requirements that contractors often fail to satisfy.

Set forth below is a discussion of the potential consequences of compliance failures, a summary of two selected compliance areas that have recently been the focus of the federal government's compliance enforcement efforts, and conclusions for surety professionals and their construction contractors.

A. Severe consequences for compliance failures

Federal government contractors' failures to comply with various contract requirements are not taken lightly by the government. Draconian penalties are commonplace, and even a single violation can be catastrophic for contractors with a government contracting portfolio. These draconian penalties are frequently levied through the government's assertion of claims against contractors, termination for default of contractors' contracts, suspension and debarment of contractors, and False Claims Act suits against contractors.

At the very least, and similar to concepts in the commercial sector, contractors' failure to comply with contractual requirements can result in litigation and the government's termination for default of contracts. With respect to litigation, non-compliance with a contract requirement may have a financial impact on the government; and, particularly in light of recent budget limitations, the government can seek to mitigate that financial impact by asserting claims against the contractor. In connection with terminations for default, even a seemingly minor failure to comply can result in a termination; and recent budget woes within the federal government have incentivized the government to terminate contracts and increased the number of

terminations against contractors. Even more significant, government claims and terminations for default can (and likely will) lead to more serious penalties, such as suspension and debarment and civil False Claims suits.

Moving up the scale in the list of penalties, compliance failures can also result in suspension and debarment, the effect of which is tantamount to the "blacklisting" of contractors from federal awards. Given federal government contracting agencies' unique position as guardians of the federal treasury, the government strives to only contract with business entities that are responsible contractors; and the government will suspend and debar any contractor it deems to be irresponsible. A contractor's lack of responsibility can be determined in a number of ways, but a contractor's intentional breach of a contractual compliance requirement or even a pattern of noncompliance can result in a finding of a lack of responsibility and then suspension and debarment.

Finally, and perhaps the most serious of all consequences, failures to comply with contractual requirements can result in False Claims Act suits, which can result in staggering monetary penalties against contractors. Although false claims can arise under many different circumstances, relevant to the compliance discussion, false claims can arise under the implied certification doctrine, which generally holds that a contractor's failure to comply with a contract requirement makes any invoice submitted by the contractor for work performed under the contract false. And under the False Claims Act, a contractor may be assessed a penalty in the form of treble damages—a penalty equal to three times the amount of the falsified invoice. Therefore, the False Claims Act, particularly in recent years with the adoption of the implied certification doctrine, is tailored to enforcing contractors' compliance; and recent False Claims Act litigation demonstrates that compliance remains a focus in federal enforcement efforts.

Accordingly, given the severe consequences that can result from a failure to comply with a contractual requirement, compliance must be at the forefront of any construction company's business.

B. The Davis-Bacon Act and the FAR's limitations on subcontracting

Surety professionals and their contractors should pay particular attention to two specific compliance areas. Compliance requirements imposed by the Davis-Bacon Act and contractual requirements imposed through the Federal Acquisition Regulation's (FAR's) limitations on subcontracting are particularly relevant, given the government's recent focus on these compliance areas. Fortunately, compliance in these areas is relatively straightforward as long as contractors invest at least a modicum of effort into understanding the requirements. Set forth below are short summaries of these two important compliance areas.

1. The Davis-Bacon Act's compliance requirements

The Davis-Bacon Act presents a unique compliance challenge for contractors participating in public works projects. The Davis-Bacon Act arises under a 1931 law requiring federal contractors to compensate certain "laborers" and "mechanics" specified rates for labor performed on public works. These rates are set by the U.S. Department of Labor and vary according to the employee's labor classification and the geographic area where work is performed. In addition to regulating wage rates, the Davis-Bacon Act imposes significant recordkeeping requirements and requires employers to submit detailed certified payrolls on a weekly basis.

Notably, the Davis-Bacon Act only applies to laborers and mechanics employed at the "site of the work" or travelling between "sites of the work." Even if the work in question is not being performed at the physical location called for in the contract, the "site of the work" may include headquarters, tool yards, batch plants, and other locations, if the work at these locations is dedicated exclusively to the project and the locations are adjacent to the site of the work. The "site of the work" does not include home offices, fabrication plants, tool yards, or other sites where the location and its continued operation are determined without regard to the project. While these distinctions can seem byzantine, the distinctions are important because employees who are employed at the "site of the work" are entitled to Davis-Bacon Act wages; and contractors can quickly run afoul of the Davis-Bacon Act if they improperly define the "site of the work" in connection with a Davis-Bacon Act covered project.

In short, the Davis-Bacon Act's requirements can be burdensome and intricate, but it is important that contractors familiarize themselves with the Act's requirements and seek guidance when questions arise in contract performance. Recent enforcement actions, in the form of False Claims Act suits, have focused on contractors' failure to compensate their employees the proper amounts due under the Davis-Bacon Act; and contractors are well-advised to devote particular attention to this increasingly targeted compliance area.

2. Subcontracting limitation compliance requirements

Most federal government contracts include FAR clauses that restrict how and to whom a prime contractor can subcontract work. Collectively, these clauses are referred to as "subcontracting limitations"; and these limitations come in numerous different forms with which contractors are required to comply, particularly in the areas of subcontract notification and subcontract performance limitations.

Continued on page 24

Feature

FRAUD SCHEMES
and Related Controls in the Construction Industry

BY JEREMY CLOPTON

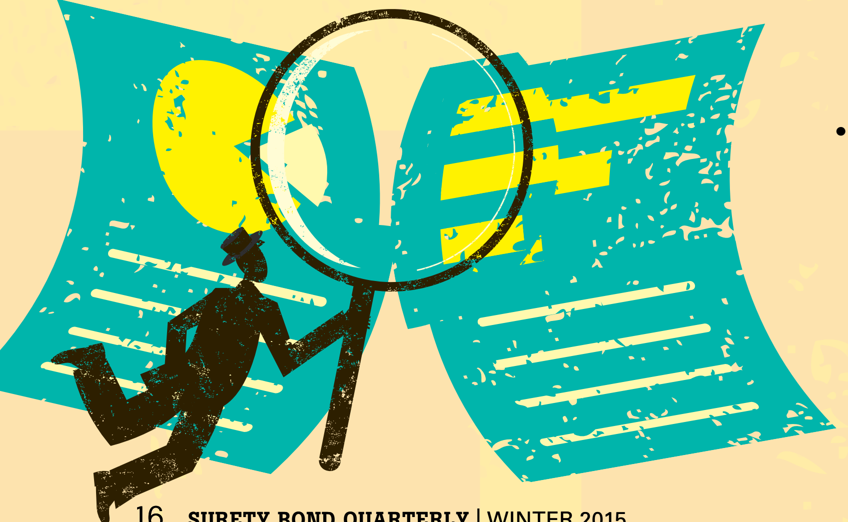
FRAUD IN THE construction industry takes on many forms, from asset misappropriation to financial statement fraud. According to the Association of Certified Fraud Examiners' *2014 Report to the Nations on Occupational Fraud and Abuse* (RTTN), the average organization loses five percent of its revenues to occupational fraud. Factor in waste, abuse, and non-occupational fraud (fraud committed by those outside the organization) and the risk of lost revenues increases even further. Bond producers who are aware of these related schemes and the related controls better position themselves to sensitize their contractors and their issues.

Common schemes in construction

Proper application of data analysis for fraud detection and deterrence requires first understanding the various types of schemes committed within the construction industry. Figure 1 contains the five most common schemes in the industry, based on RTTN statistics.

Data analytics as an anti-fraud control

Many construction firms wonder what they can do to prevent fraud from occurring in their organization. After all, a determined employee can be very difficult to stop. It is unrealistic to think all frauds are preventable, but there is almost always more that organizations can do to reduce fraud risk in key areas.



Based on the RTTN, the most effective anti-fraud control is "proactive data monitoring and analysis" (data analysis). In fact, data analysis resulted in a nearly 60 percent reduction in median fraud losses and a 50 percent reduction in median scheme duration in the cases studied. In addition to the data analysis category, the process is also inherent in two of the most common methods of detection: management review and internal audit. For these reasons, and the growing volume of data generated by organizations each day, it is important for contractors to know how to use data analysis to deter and detect fraud.

Application of data analysis

Using the definitions of the schemes described above, we can identify the largest fraud risks: vendor management, disbursements, non-cash areas (generally inventory and/or fixed assets) and payroll. Some of the most common analysis techniques in each of these areas include:

- **Vendor management**: Many times, corruption and billing schemes occur through the vendor file. Looking for potential related parties or conflicts of interest, by comparing the employee and vendor files based on key attributes (name, address, phone, TIN, etc.), may help identify high-risk vendors. Other beneficial analyses include a geospatial analysis of vendors to identify those located in residential areas, identification of vendors using a mailbox service and identifying vendors without an address, or some variation of "hold for pickup."
- **Disbursements**: Billing and check tampering are both fraudulent disbursement schemes. In addition, corruption schemes typically involve a disbursement. Perhaps the most effective analysis technique related to disbursements is trend analysis, focused on the identification of accelerating patterns of activity. Other common analytics include identifying checks issued on weekends, holidays or in round, thousand dollar increments.
- **Inventory and fixed assets:** Detection of non-cash schemes through data is sometimes more challenging than schemes involving cash. This is caused by the limitations on available data for many non-cash assets. Some of the most effective techniques involve monitoring of inventory levels relative to sales, analysis of inventory shrinkage, testing existence of fixed assets and analysis of expensed fixed assets. The key to incorporating data into an analysis of non-cash assets is being proactive in capturing and retaining related data elements.

Figure 1.

Scheme	Definition[1]
Corruption	A fraud scheme in which an employee misuses his or her influence in a business transaction in a way that violates his or her duty to the employer in order to gain a direct or indirect benefit.
Billing	A fraudulent disbursement scheme in which a person causes his or her employer to issue a payment by submitting invoices for fictitious goods or services, inflated invoices or invoices for personal purchases.
Check Tampering	A fraudulent disbursement scheme in which a person steals his or her employer's funds by intercepting, forging or altering a check drawn on one of the organization's bank accounts.
Expense Reimbursements	A fraudulent disbursement scheme in which an employee makes a claim for reimbursement of fictitious or inflated business expenses.
Non-Cash	Any scheme in which an employee steals or misuses non-cash assets of the victim organization.

[1]*Source: 2014 Report to the Nations (Glossary of Terminology)*

Additional controls

Beyond data analytics, there are a number of other effective anti-fraud controls. Hotlines are also an effective anti-fraud control. According to the RTTN, tips are the number one way frauds are detected. Providing employees, vendors, customers and others a means to communicate potential fraud to the organization is important to detecting frauds. For those organizations without a hotline, other methods of detection increase whereas tips decreased as a detection method. In addition to hotlines, other effective anti-fraud controls include:

- Surprise audits
- Management review
- Internal audits

While these are some of the most effective controls, the controls that work best for specific organizations may differ. The anti-fraud control structure for each construction firm will vary, depending on the firm's risk tolerance, personnel structure, and available resources.

Recovery of losses

While data analytics is the most effective anti-fraud control, analytics don't provide a means for recovery of losses. In fact, according to the RTTN, more than half of the organizations surveyed saw no recovery of losses. Only thirteen percent of respondents received full recovery. This is very consistent with my experience as a fraud examiner. Generally speaking, individuals committing occupational fraud are not looking to save the money for a rainy day. The funds are typically expended to help with a perceived financial pressure—gambling problems, credit card debt, an addiction, or others. In the instances where recovery has occurred, the organizations have had an appropriate insurance policy in place.

While data analysis is the most effective anti-fraud control, it alone is not enough to deter and detect fraud. The most effective fraud prevention program combines multiple elements that, as a whole, create an environment where fraud is less likely to take root. In addition to data analysis, it is important to explore the many other anti-fraud controls that could be implemented in a construction firm. For recovery, it is important to have an insurance policy, such as a commercial crime policy, in place that covers occupational fraud. The RTTN contains information regarding other anti-fraud controls to help deter and detect fraud.

Bond producers should advice contractors to evaluate all possible anti-fraud controls. Where possible, contractors should incorporate data analysis to increase the effectiveness of their anti-fraud efforts.

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WE KNOW CONSTRUCTION
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We unite over 7,500 construction companies across the nation and continue to grow. If your clients' accounting firm doesn't know the construction industry as well as they should, then we can help.

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Feature

Unravelling the Mystery of COURT BONDS

BY JEFFREY M. FRANK BY OMAR J. HARB BY JESSICA L. WYNN

FOR PARTIES ENGAGED in litigation, court bonds are often a useful tool. Because there is such a variety of these bonds, it is often difficult to know the proper name and purpose of each of them. This article will provide a brief explanation of the primary types of court bonds that are available, along with a few useful tips for producers and underwriters.

Appeal and supersedeas bonds

The most common types of court bonds are appeal bonds and supersedeas bonds. There is often confusion between these two types of bonds, the terms of which are improperly used interchangeably.

Appeal bonds

An appeal bond covers the opposing party's court costs if the appeal is unsuccessful. Any party can bring an appeal after a final judgment in civil litigation. The specific rules regarding the appeal and the costs covered vary from jurisdiction to jurisdiction and from state court to federal court.

The court will determine the penal sum of the appeal bond. Because damages are usually limited to court costs, such as filing fees, transcripts, etc., attorneys' fees are generally not covered unless the appeal involves a specific statute providing for fees. The producer should gain a working understanding of the law in his or her jurisdiction and advise the surety to ascertain the relevant law and to seek proper guidance when underwriting the account.

Supersedeas Bonds

The supersedeas bond guarantees the successful trial court litigant that it will have a source of collection after the appeal. When a party prevails in the trial court and obtains a judgment against its opponent, the opponent may want to appeal that decision. In addition, the judgment debtor does not want the plaintiff to collect on the judgment while the appeal is pending.

In order to put the collection efforts on hold, the judgment debtor appealing the decision (appellant) must obtain a stay of enforcement. To obtain the stay, the appellant will have to file a motion with the court and then post the bond. If the court grants the stay, the court will determine the amount of the bond. The amount of the bond is usually around 125 percent of the judgment amount to account for costs, interest, and other damages that might arise during the course of the appeal.

Because the appellant has already lost in the trial court, the surety is taking on a substantial

risk by issuing a supersedeas bond. Sureties generally require that these bonds be fully collateralized before issuing them.

The typical supersedeas bond guarantees that, if the defendant loses the appeal, then the surety and principal are jointly and severally liable to the obligee (appellee) to satisfy the judgment. The specific liability will vary depending on the language of the bond.

Injunction bonds

An injunction is a court order generally either requiring a party to take a certain action or preventing a party from doing something. Sometimes injunctions are issued before a full trial, as in the case of a temporary restraining order or preliminary injunction. In those cases, the court sometimes requires an injunction bond.

However, it is not the enjoined party (who is generally the person accused of doing something wrong) who is required to obtain an injunction bond, but rather the person requesting the injunction who must do so. The purpose of the injunction bond is to protect the enjoined party from damages resulting from an improper injunction. See, for example, *Longshore Lakes Joint Venture v. Mundy*, 616 So. 2d 1047 (Fla. Dist. Ct. App. 1993). In other words, the party benefitting from the injunction bears the risk that the court (following a full hearing on the merits) will decide that the injunctive relief was not warranted.

An example of the damages an enjoined party could suffer from an improper injunction would be a company's lost profits if prevented from manufacturing and selling a product while a patent infringement lawsuit is pending. See, for example, *Apple, Inc. v. Samsung Electronics Co., Ltd.*, 678 F.3d 1314 (Fed. Cir. 2012).

As the amount of potential damages that could result from an injunction is often speculative, a court can generally set the amount of the bond at its discretion, as provided for in Federal Rule of Civil Procedure 65(c). The surety's liability is limited to the amount of the bond. Note, however, that the wrongfully enjoined party does not have to prove that the injunction proceeding was brought in bad faith to collect under the bond, only that the injunction was improper. Accordingly, most states allow a presumption in favor of recovery by the wrongfully enjoined party under the bond. See, for example, *U.S. D.I.D. Corp. v. Windstream Communications, Inc.*, 775 F.3d 128 (2d Cir. 2014). Thus, bond producers and sureties should keep in mind that injunction bonds can be a risky endeavor, and securing collateral (as discussed below) is recommended.

BECAUSE THE APPELLANT HAS ALREADY LOST IN THE TRIAL COURT, THE SURETY IS TAKING ON A SUBSTANTIAL RISK BY ISSUING A SUPERSEDEAS BOND. SURETIES GENERALLY REQUIRE THAT THESE BONDS BE FULLY COLLATERALIZED BEFORE ISSUING THEM.

Attachment/dissolution bonds

Just as with a preliminary injunction, an attachment is a remedy provided to a plaintiff before a full trial or other hearing on the merits. In certain situations, a court may order the seizure or "attachment" of a defendant's property to make sure that the property remains available to satisfy an eventual judgment for the plaintiff.

To obtain a pre-judgment attachment, the plaintiff must show there is a reason to believe the defendant will improperly take some action to deprive the plaintiff of an opportunity to collect on a judgment. For example, the Federal Rules of Civil Procedure provide that the United States, in attempting to collect a federal debt, should be granted a pre-judgment remedy (such as attachment) only if it can show there is reasonable cause to believe that the debtor is going to leave the jurisdiction, dispose of, convert or destroy property, or evade service of process. See 28 U.S.C. § 3101(b)(1).

Because attachment is considered an extraordinary remedy, the plaintiff must post a bond to cover any damages to the defendant resulting from the attachment if it is later determined the attachment was erroneous. Just as with injunction bonds, those damages could include lost profits resulting from the defendant's inability to use the property. The laws of each state should be consulted to understand how the amount of the bond is determined, but generally a court has discretion to set the amount based on the facts of the case and nature and value of the property attached.

A defendant whose property has been seized through attachment can regain possession of the property through a "dissolution" or "release" bond. A "dissolution" bond, the amount of which should be at least the value of the property, provides a source for recovery if the plaintiff eventually obtains a judgment. Dissolution bonds, as the name suggests, actually dissolve the attachment. If the plaintiff wins the lawsuit, it can simply collect on the bond. On the other hand, "release" bonds allow the defendant possession of the property, but the attachment remains. The release bond guarantees that the property will remain available for satisfaction of a judgment. Obviously, whether the bond is for dissolution or release is an important distinction for bond producers and sureties. Because the property will not necessarily be available to satisfy a judgment following a "dissolution" bond, surety professionals must take that into account when determining how much collateral will be needed.

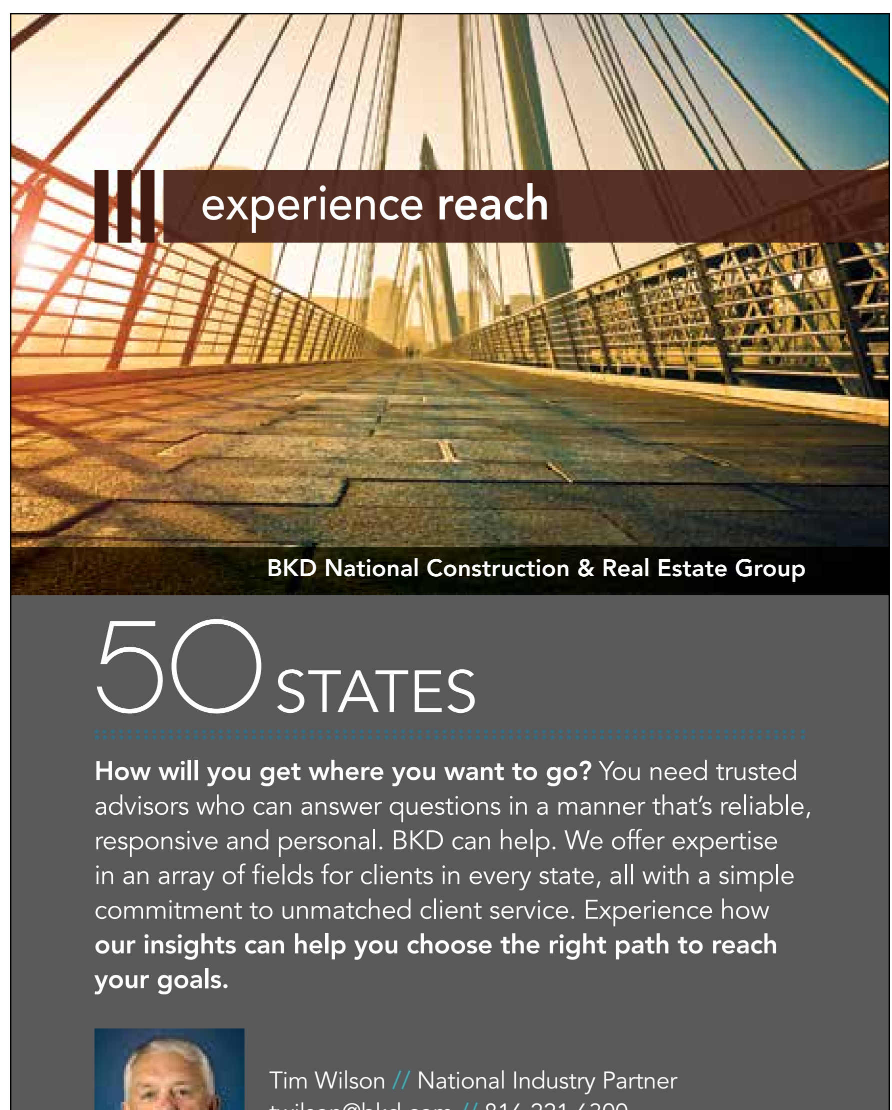
Replevin bonds

Replevin, which is also known as "claim and delivery," is the legal process that enables a person to

recover his or her personal property after another unlawfully takes it. Technically, replevin is defined as a civil action to recover possession of goods or chattels that have been unlawfully taken or unlawfully detained and to recover damages sustained as a result of the unlawful taking or unlawful detention. A chattel is movable or transferable property, especially a movable object capable of manual delivery and not the subject matter of real property. See *Black's Law Dictionary* at 251 (8th ed. 2004).

The procedure for pursuing a replevin action varies by statute, but, in general, it requires that the plaintiff do two things. First, the plaintiff must file an affidavit (a sworn written statement) or complaint describing the property, its value, and stating that the plaintiff is the owner of the property. Second, the plaintiff must post a replevin bond. The replevin bond protects the defendant from losses that may result from the plaintiff's seizure of the personal property. Typical provisions in a replevin bond include that the property be returned if ordered by the court and that the plaintiff pay for any damages that were likely caused by the seizure.

Note that these bonds are similar to "attachment" bonds discussed above, except that the attached property in a replevin action is the subject matter of the lawsuit (rather than simply a means of satisfying an eventual judgment).



Receiver bonds

Receivership is the scenario where a corporation or other entity is being controlled by a receiver. A receiver is a disinterested person appointed by a court, or by a corporation or other person, to protect or to collect property that is the subject of various claims (for example, because the property belongs to someone who is going through a bankruptcy or is the subject of a lawsuit). See *Black's Law Dictionary* at 1296 (8th ed. 2004). A receiver's typical powers and duties are to collect, administer, and disburse the receivership property for the benefit of all persons interested in the estate.

In many jurisdictions, before the court will appoint a receiver, the receiver must post a bond that will protect interested parties from damages caused by the receiver's failure to properly discharge his or her duties. Generally, a receiver bond guarantees the following duties of the receiver: (1) the care and preservation of the property that the receiver is controlling; and (2) the disposition and distribution of the property pursuant to court orders. In many cases, a material, or substantial, breach of the receiver's duties creates liability under the receiver bond.

Bail bonds

After an arrest, bail is the process undertaken where a person obtains the release of the accused by providing security to ensure future court appearances. See *Black's Law Dictionary* at 150 (8th ed. 2004). If the

accused does not appear before the court when ordered, for example, for an arraignment or a trial, the court may keep the bail and issue a warrant for the accused's arrest.

A surety bond can be used to secure bail. Bail bonds are useful when the accused cannot afford to pay the full amount of his or her bail. A surety that issues a bail bond pledges to pay the full value of the bail if the accused does not appear in court. In return, the surety often charges a 10 percent premium and secures its obligation with collateral (for example, title to real property, car, boat, jewelry).

Claims on court bonds

Some of the court bonds listed above are payable on demand after a condition precedent is satisfied. Examples include a supersedeas bond, which the surety must pay if the defendant loses its appeal, and a bail bond, where the surety pays when the accused fails to appear in court. Other types of court bonds, like an appeal bond and an attachment bond, require an analysis to determine the amount of costs or damages the surety will have to pay.

Indemnification and collateral

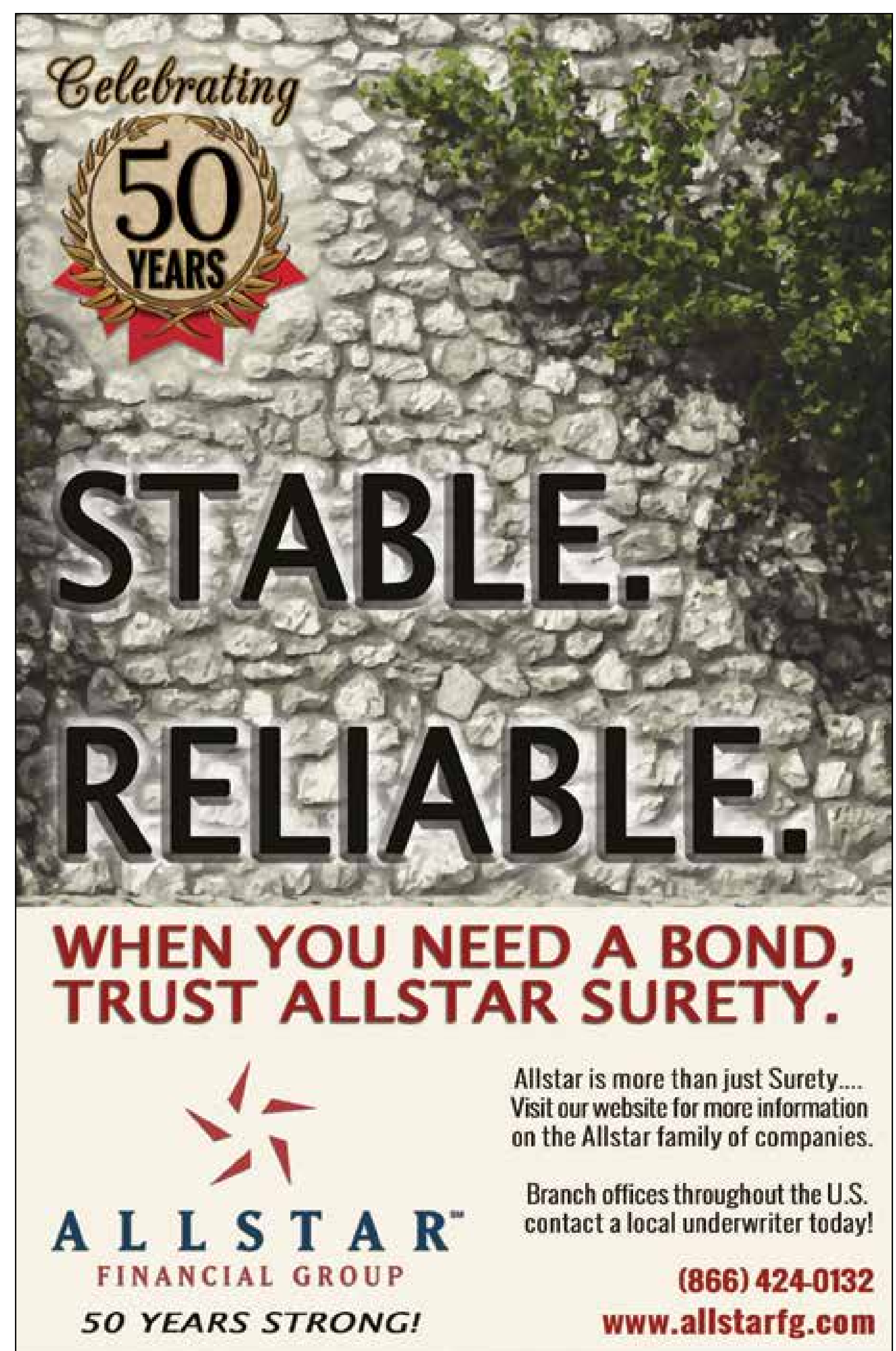
As with other bonds, sureties issuing court bonds should, and typically do, require the principal (and sometimes others) to execute an indemnity agreement, requiring reimbursement to the surety for any losses, costs, expenses and attorneys' fees. Whether indemnity is obtained from one or more individuals (when the principal is an entity) depends on the size and financial strength of the entity and its history with the surety, among other factors.

Depending on the nature of the bond, a surety may also require the principal to deliver collateral to the surety, providing an immediate source of recovery in the event the surety suffers losses. Collateral is typically required for appeal or supersedeas bonds, as the risk to the surety is extremely high in those circumstances (in which a court has already found the principal liable).

The amount of collateral will depend on the nature of the bond. For example, for an attachment bond, the value of the attached property and the potential damages to be suffered by the defendant should be taken into account when determining the appropriate amount of collateral. Collateral can take the form of a bank's letter of credit, a lien on real property, or some other assignment or transfer of property.

Note that each surety has differing policies with respect to what collateral can be accepted. Accordingly, depending on the type of collateral a principal or indemnitor has to offer, a bond producer may have to check with different sureties to find the right fit. For example, some sureties may only accept letters of credit; and it may be necessary to find a surety willing to accept a less conventional type of collateral, such as an interest in real (or even personal) property.

Because many of these bonds are similar (and are often confused),



producers and underwriters must confirm what bond is required by the court and what liability the surety may ultimately face. A careful review of what bond is necessary will not only ensure that the correct type of bond is issued, but also it will enable the producer to secure the correct amount of collateral.

Finally, producers and underwriters should check the requirements of the relevant jurisdiction, to make sure that any specific local rules or requirements are taken into account when deciding on a bond form.

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Continued from page 15

Subcontract notification clauses require the prime contractor to provide notification to the government prior to the prime contractor entering into a subcontract. The most prevalent subcontract notification clause in federal government contracts, FAR 52.244-2, Consent to Subcontract, is typically included in cost-type contracts and requires the prime contractor to not only notify the government of a potential subcontract award, but also to obtain the government's consent prior to the prime entering into the subcontract. A related subcontract notification clause, FAR 52.244-5, Competition in Subcontracting, requires the prime contractor to notify the government reasonably in advance of placing a subcontract and also generally requires the prime contractor to select the subcontractor on a competitive basis.

Subcontract performance clauses limit the prime contractor's ability to subcontract out certain portions of the work called for under the prime contract. In this area, the most prevalent clause, FAR 52.219-4, Limitations on Subcontracting, is included in most small business set-aside contracts. The clause operates to prevent large business contractors from circumventing the requirements of the set-aside programs. Under this clause, when a small business contractor receives a set-aside award, it is required to perform a certain percentage of the work itself; and the contractor is prohibited from subcontracting out work in excess of that percentage. The percentage of work that must be performed by the small business varies from contract to contract, with the small business being required to perform only 15 percent of the work under a general construction contract and generally 50 percent of the work under a services or supply contract.

In sum, the subcontracting limitations placed on subcontractors are numerous, but compliance with these clauses is relatively straightforward. Notwithstanding the relatively straightforward requirements, recent enforcement actions in this area, also in the form of False Claims Act suits, demonstrate that certain contractors have repeatedly failed to understand and follow the subcontracting limitations in their contracts. Again, to the extent questions arise as to how to comply with subcontracting limitations, contractors are well-advised to seek guidance in this increasingly targeted compliance area.

As addressed above, the consequences for compliance failures can be severe. Government claims, termination for default, suspension and debarment, and False Claims Act suits are all mechanisms that can be brought to bear against a contractor, with any one of these mechanisms capable of serving a crippling blow to a contractor's business. However, while compliance can be burdensome, the burden associated with compliance is far outweighed by the potentially devastating result that can flow from a contractor's compliance failure. And the key to compliance is an understanding of each contract's requirements. While the compliance burden on federal construction contractors may seem daunting, a thorough understanding of the government's compliance requirements and maintaining an effective system to stay informed of those requirements makes federal contracting a manageable and lucrative endeavor.

W. Barron A. Avery serves on NASBP's Attorney Advisory Council and is an attorney at Baker & Hostetler, LLP in Washington, DC, where he specializes in federal government contract law. Avery can be reached at 202.861.1705 or wavery@bakerlaw.com.

Be sure to read Avery's next article on Evolving Compliance Requirements: the New Anti-Human Trafficking Requirements.

Feature

NASBP Attorney Advisory Council Participates in NASBP Regional Meetings

W. Barron A. Avery, pictured, of Baker Hostetler presenting at the Regions 1, 2 & 3 Meeting.

Peter E. Strniste, Jr., standing at podium, and Todd R. Regan of Robinson & Cole LLP presented at the Regions 8, 9, 10 & 11 Meeting.

From left, Rick Levesque of the Hartford Bond, Jonathan Dunn of Salamirad Morrow Timpane & Dunn, LLP, Mike Pipkin of Weinstein, Radcliff, Pipkin, LLP, and Todd Bauer of Guardian Group, Inc. presented a CE session for producers titled "Bond Claims–Shaken and Stirred" at all three Regional Meetings. They are shown here at the Regions 1, 2 & 3 Meeting held in Vancouver, BC.

THREE ATTORNEYS WHO serve on the NASBP Attorney Advisory Council (AAC) delivered presentations at the NASBP Regional Meetings. The NASBP Attorney Advisory Council, formed this spring, is comprised of eight attorneys, with deep knowledge and experience in surety law, construction law, and/or government contracts. They serve as a resource team to NASBP and provide substantive content to articles, virtual seminars, presentations, white papers, and in-person seminars on a wide assortment of industry issues that surety professionals face on a daily basis.

This fall, W. Barron A. Avery of Baker Hostetler presented at the Regions 1, 2 & 3 and Regions 4, 5, 6 & 7 Meetings on U.S. government contracting compliance issues, including recent developments with the Davis-Bacon Act, subcontracting limitations, and mandatory disclosure requirements. Todd R. Regan of Robinson & Cole LLP along with Peter E. Strniste, Jr., also of Robinson & Cole, presented at the Regions 8, 9, 10 & 11 Meeting in Amelia Island, FL on "Deciphering and Navigating the Terms and Conditions of Industry and Modified Bond Forms." Mike Pipkin of Sedgwick, LLP was among four panelists who presented a continuing education session (CE) for producers sponsored by the Hartford, which was titled "Bond Claims–Shaken and Stirred" and delivered at all three Regional Meetings. The other panelists included Rick Levesque of the Hartford Bond, Todd Bauer of Guardian Group, Inc., and Jonathan Dunn of Salamirad Morrow Timpane & Dunn, LLP.

For more information about the AAC, visit http://www.nasbp.org/aac/home.

See Regan's article on page 26 that covers the section of his presentation he made that addressed public-private partnerships.

Feature

PUBLIC-PRIVATE PARTNERSHIP PROJECTS

BY TODD R. REGAN

Bonding process considerations for bond producers and sureties.

PUBLIC-PRIVATE PARTNERSHIPS (P3s) continue to be a hot topic of discussion, and their use for delivering large, multifaceted infrastructure projects continues to grow in the United States. According to Aon Risk Solutions' *2015 Surety Market Update and Forecast*, there were five closed P3 deals in the U.S. in 2014, with a combined value of $4 billion, and 15 P3 projects in the procurement process in 2015, totaling $15 billion in construction.

Accordingly, bond producers, surety underwriters, and contractors need to understand the particular challenges and risks posed to sureties by P3 projects, both to properly underwrite those risks and to combat the notion that bonds are somehow unnecessary or not properly suited for P3 projects. In order to effectively bond a P3 project, producers and underwriters must have a seat at the table when the P3 partnering agreement is structured to ensure that the bonds meet the needs of the project and the surety's and principal's rights are protected.

P3s: The background

The country's rapidly decaying infrastructure and shortfalls in public funding have made P3s, long popular internationally, an increasingly attractive means of procuring large infrastructure projects. The American Society of Civil Engineer's (ASCE) most recent "Report Card for America's Infrastructure" gives America's infrastructure a grade of D+ and estimates that a $3.6 trillion overall investment in the county's infrastructure will be necessary by the year 2020. The U.S. Federal Highway Administration estimates that 68,842 bridges nationwide (which is more than 11 percent of the nation's total highway bridges) are currently "structurally deficient." Thus, the need for large-scale investment in the nation's infrastructure is well documented.

In many ways, despite the participation of private players and private financing, P3 projects can be viewed as an alternate method of delivering public works projects. P3s allow government bodies to tap into private sector resources and ingenuity to fund, design, construct, operate, and maintain facilities that benefit the public—facilities that would otherwise have been procured under the typical design-bid-build project delivery system.

P3 projects come in many different shapes and sizes, and a detailed analysis of the potential iterations is beyond the scope of this article. On

THE COUNTRY'S RAPIDLY DECAYING INFRASTRUCTURE AND SHORTFALLS IN PUBLIC FUNDING HAVE MADE P3S, LONG POPULAR INTERNATIONALLY, AN INCREASINGLY ATTRACTIVE MEANS OF PROCURING LARGE INFRASTRUCTURE PROJECTS.

the highest level, a P3 project will typically involve a public owner or sponsor that enters into an agreement (the partnering agreement) with a private partner (the concessionaire), which is often a special purpose vehicle (SPV) made up of a consortium of private players. The concessionaire typically will also have agreements with lenders and equity investors to finance the project, as well as separate agreements with a design-builder and an entity that will be charged with the long-term operation and maintenance of the facility.

Depending on the structure of the P3, the concessionaire may be responsible for the design, construction, operation, and maintenance of the facility, or one or more of these functions. In return for constructing and operating the facility, the concessionaire may be entitled to collect revenue generated by the completed facility (for example, tolls) or may be entitled to "availability payments," which are rent-like payments received from the public partner based on having the facility in operation for the public use.

Legislative approaches

A particular challenge in the surety underwriting process is the lack of uniformity in P3 enabling statutes on the federal level and from state to state, and even within states for different types of projects (for example, road construction v. school construction). Bonding a P3 project requires producers and underwriters to navigate a labyrinth of differing legislation for any given project. Significantly, only about 34 states presently have P3 enabling legislation, and, of those, only 26 states expressly require payment and performance bonds. To complicate matters further, of those states that do mandate bonds, not all require that the bonds be subject to that state's Little Miller Act. The result is that the producer and underwriter may be faced with a custom, project-specific bond form that, unlike bonds issued pursuant to Little Miller Acts or standard industry bond forms (such as the AIA A312 Bonds), has not been interpreted by the courts and that may not preserve the surety's typical rights and defenses.

Letters of credit

Another concern in bonding P3 projects is that, due to the high liquidity requirements posed by private lenders and investors, sureties may be asked to issue a bond that is more akin to a letter of credit than a traditional surety bond. Delays and missed milestones and completion dates can have particularly significant financial consequences on P3 projects, where the flow of toll money or availability payments is needed to service debt obligations to lenders or to repay equity investors.

Consequentially, there has historically been a preference on P3 projects for letters of credit, which permit the beneficiary to draw down a lump sum of cash on demand in the event of a default. In contrast, performance bonds typically entitle the surety to receive a written declaration of the contractor's default, provide the surety with a period of time to investigate and contest the grounds for default, and give the surety various performance options in order to remedy the default. The desire for liquidity (and to avoid the surety's defenses to performance) has led to the use of letters of credit over surety bonds on P3 projects. Furthermore, because rating agencies have historically given higher

ratings to projects that are secured by letters of credit than by bonded projects, concessionaires may be able to obtain financing on more favorable terms when letters of credit are used.

Significantly, according to surety industry representatives, there appears to be some movement of late for rating agencies to accord more credit to surety products than in the past. When bonding P3 projects, producers and underwriters must be wary of efforts to strip the surety's traditional performance defenses from the bond form by turning the performance bond into a demand bond.

Despite the historical preference for letters of credit, there are numerous compelling reasons why P3 projects should be bonded; and NASBP has been on the forefront of this debate. Despite the presence of a private partner, at the end of the day, the project is essentially a public improvement that will ultimately be paid for by public money. Furthermore, when letters of credit are used as security for P3 projects, the penal sum is typically limited to 20 percent of the contract sum. In contrast, the payment bond and the performance bond are each typically in the full amount of the contract value. Consequentially, unlike surety bonds, letters of credit do not guarantee a lien-free completion of the project, nor do letters of credit guarantee the right of laborers and suppliers to be paid for their work. Moreover, sureties prequalify contractors during their extensive underwriting process by closely scrutinizing the contractor's character, capacity, and capital, thereby further ensuring that contractor is qualified to complete the project and lowering the risk of default. Finally, in the event of default, the surety industry possesses the unique knowledge and experience to step in and manage the completion of the project.

Beware of scope and duration

When bonding P3 projects, surety professionals must pay particular attention to the proposed duration and breadth of the bonded obligation. Due to the structure of P3 projects, sureties could potentially be asked to issue bonds covering more than just traditional construction activities. Indeed, underwriters should be wary of efforts to enlarge the scope of the bond to guarantee the concessionaire's financing obligations, as well as the long-term operation and maintenance (O&M) portions of the project.

Care must be taken to ensure that the bonded obligation is limited to traditional construction activities. Oftentimes, the partnering agreement will call for the concessionaire to operate and maintain the facility for 99 years or longer. Certainly, this is not a risk that a construction surety would knowingly take on. One possible solution to this issue is for the surety to issue separate bonds covering the O&M obligations for a limited period of time, subject to renewal on an annual basis at the surety's option. In this manner, the surety can limit the duration of the bonded obligation and avoid an open-ended risk that could run for over a century.

It is also important to ensure that the surety's right of equitable subrogation to use the remaining contract balances to complete the project in the event of default is protected. Under so-called lender direct agreements, in the event of a contractor default, the lender may have the right to step into the shoes of the contractor and take over the project. This, of course, may conflict with one of the surety's most fundamental of rights and must be addressed during the structuring of the P3.

Notably, P3 projects often will use the design-build project delivery method, under which the concessionaire assumes responsibility for both design and construction of the project. The use of a design-build project delivery method raises even more questions for the surety to consider when bonding P3 projects and may increase the surety's risk. Does the performance bond guarantee the completion of the principal's design obligations? Is the surety being asked to insure against design errors and omissions? Does the principal (or surety in the event of default) lose the right to pursue claims against the owner and designers based on incomplete or defective design? Do design subconsultants have the right to assert payment bond claims? These are all additional risk factors that the surety will need to take into account in the process of underwriting P3 projects.

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One potential solution is to make use of the Design-Build Institute of America's (DBIA) newly issued performance bond, DBIA No. 620, specifically crafted for design-build projects. As discussed in Bill Quatman's recent article in the Fall 2015 edition of *Surety Bond Quarterly,* the surety community, including NASBP, worked closely with DBIA in the development of new bond forms intended to address the particular issues that arise on design-build projects. Under the new DBIA form, design subconsultants will, as in the past, look first to their E&O insurance coverage for damages caused by design errors or omissions. Only in the event that there are shortfalls in coverage, if the claim is barred by exclusions, or if the policy is depleted, will the surety be liable for the damages caused by design defects.

Another approach, which differs significantly from the approach taken in the DBIA form, is that taken in the ConsensusDOCS 470 Design-Build Performance Bond, which, although it covers the costs of completing the design aspects of the principal's work, expressly disclaims coverage for any damages caused by design defects if the damages in question are of the type that are typically covered under professional liability insurance.

Bonds tailored for P3 projects

In response to the market's demand for liquidity in P3 projects, the surety industry has started to develop bonds that maintain the surety's typical performance bond defenses while adding a liquidity component. For example, Zurich has a developed its "Public-Private Partnership Performance Bond," and XL Group offers a P3 bond called "BuildSecure." These P3-specific bonds commonly have a lower penal sum than typical bonds, usually in the range of 20 to 30 percent of the contract sum. In order to provide liquidity, the bonds incorporate an on-demand feature that requires the surety to make an immediate payment of up to 10 to 20 percent of the penal sum upon the declaration of contract default (the loss mitigation payment). In order to preserve the surety's defenses, the bonds contain a fast-track dispute resolution procedure, whereby claims are submitted to a default review board for an expedited resolution, with all parties bound by its decision. Meanwhile, construction continues while the dispute is pending before the dispute resolution board.

While the use of this new product is in the development stage in the U.S. market, AON reports that the Canadian market has seen more activity with these new products. Their use in both markets is expected to grow in coming years. It should be noted that a surety product with a liquidity component may not be readily available in all surety market segments and requires contractors of a significant size, sophistication, and working capital level. These P3-specific bonds present an innovative approach by the surety industry to the challenges posed by P3 projects, and the surety industry should be applauded for developing surety solutions as procurement evolves.

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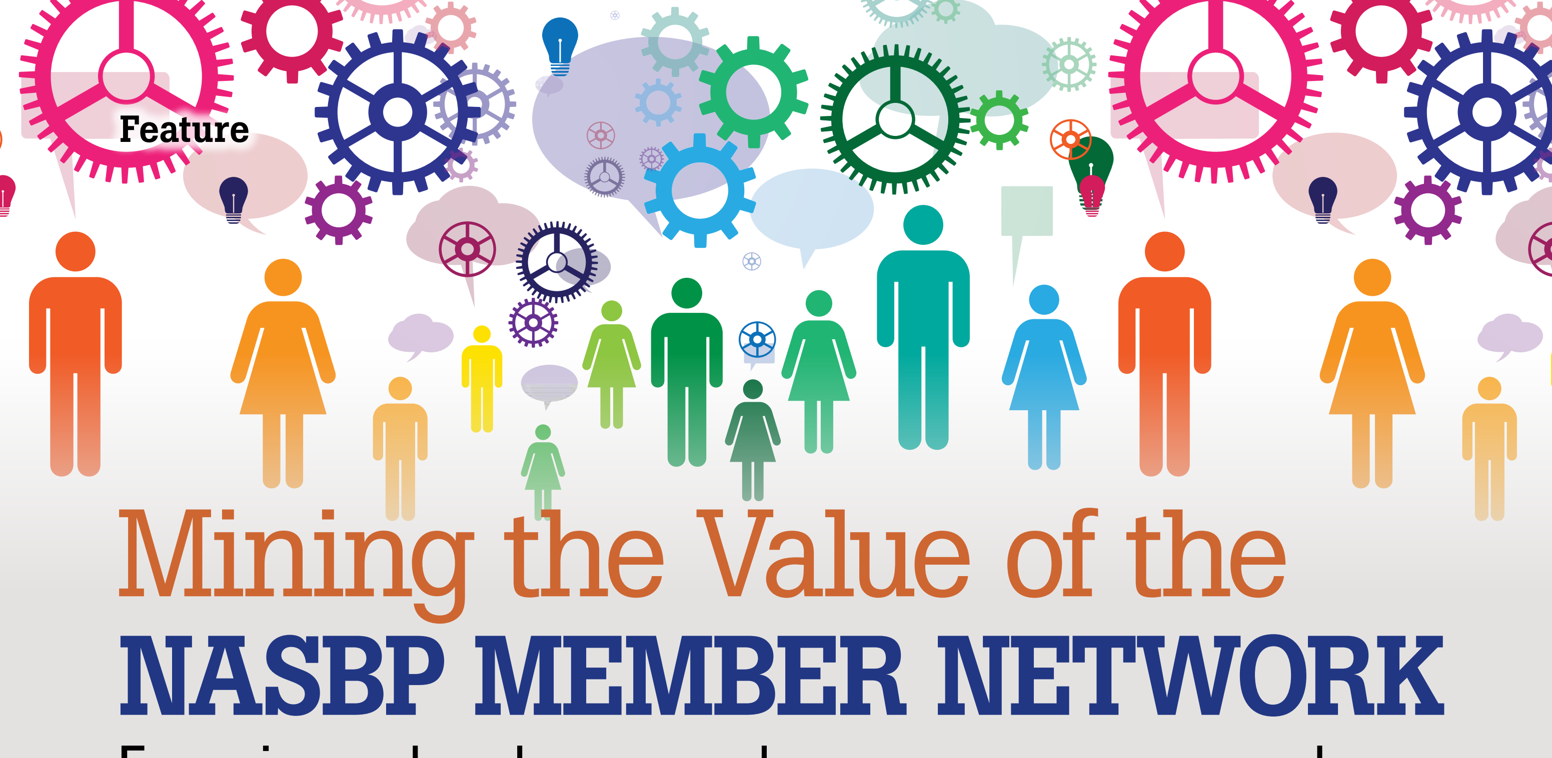

Mining the Value of the NASBP MEMBER NETWORK

Experienced and new producers can reap rewards from the Association's membership network.

A LAST-MINUTE BID bond misrouted by a courier can be a heart stopper for a client. When a producer doesn't have an office in the same town where that client is working, it's even more distressing. Fortunately, when the paperwork Susan Hecker's customer needed didn't arrive as planned, she knew just where to turn. "I went onto NASBP's database and searched Austin, Texas, where the client was located," recalled Hecker, Executive Vice President and National Director of Contract Surety at Arthur J. Gallagher and Company in San Francisco, and President of NASBP.

Not only did Hecker quickly find four potential partners in Austin who might be able to help, but also, as she said, "I was able to see the locations of those agencies compared to where our customer's office was." The NASBP database also showed her which of those shops were likely to represent the same sureties Gallagher used for its own customers.

One phone call to USI Southwest in Austin put everything in order. The agency agreed, as a favor to a fellow NASBP Member, to execute Hecker's bid bond and prepare it for the customer to pick up, all in less than 30 minutes.

Helping Clients Enter A New Geographic Market

Many surety agents support customers who don't focus solely on a small area. The NASBP network enables a bond producer to provide clients guidance in addition to supplying a bid or performance and payment bond. "We might typically have contractors that are local, but everyone has contractors who either perform or supply work in other states or territories," said Todd Loehnert, President of L A Surety Solutions in Louisville, KY, and Chair of NASBP's Membership Committee.

One of his customers, a stadium seating contractor specializing in educational facilities, has executed jobs from California to Florida. Each region has its own nuances, and the power of the NASBP Member network gives Loehnert all the information he needs when a wide-reaching customer enters a new market. "I can go online, obtain contact information of surety professionals in the area and talk with them," he said. Producers familiar with the region are available to answer questions that may range from what the bond forms look like to who is known to be slow-paying. Loehnert added that the NASBP network is a free, vast knowledge base that doesn't just benefit NASBP producer Members, but their clients and NASBP Affiliates and Associates, as well.

I CAN GO ONLINE, OBTAIN CONTACT INFORMATION OF SURETY PROFESSIONALS IN THE AREA AND TALK WITH THEM.

THE ABILITY TO REACH OUT THROUGH NASBP'S NETWORK OFFERS OUR AGENCY AN OPPORTUNITY TO EXTEND OUR RELATIONSHIPS BEYOND OUR LOCAL BOND COMMUNITY FOR THE BENEFIT OF OUR CONTRACTOR CUSTOMERS.

Familiarizing Clients With A New Employer

The NASBP Member network is a time-saving and effective resource for

becoming acquainted with, and communicating with, others in the surety industry. "This network is particularly helpful given our location in Hawaii, since we're isolated from the offices of most producers and surety underwriters," said John Bustard, Executive Vice President of Honolulu-based King & Neel, Inc., and NASBP Regional Director of Region 2. "The ability to reach out through NASBP's network offers our agency an opportunity to extend our relationships beyond our local bond community for the benefit of our contractor customers." For example, when a Hawaii-based customer of King & Neel's was asked to provide subcontractor quotes to a GC from the Midwest who was interested in breaking into that marketplace, Bustard worked through the Association's network to develop an understanding of the Midwest GC." We contacted a NASBP Member in the Midwest who is the producer for the GC, and with information gleaned from the Midwest Member, King & Neel provided enough input to our subcontractor customer to help them develop confidence in dealing with the new arrival in town," he explained. With the information gleaned from the Member in the Midwest, Bustard was able to provide input to his customer that would have been much more difficult to gather if he hadn't had access to his fellow producer.

Advancing Agency Operation Knowledge and Services

More than two decades ago, when Thomas Padilla, Senior Vice President of Surety at HUB International Insurance Services in Albuquerque, NM, and Immediate Past President of NASBP, unexpectedly found himself in charge of surety for his agency, he was essentially a one-man surety operation in a large insurance shop. If a question came up, he didn't have anyone in the office to look to for advice. "Without the resources of other NASBP Members across the country willing to help and share experience and give advice, I would never have survived," Padilla recalled. Padilla remembers questions about unusual bond forms, new markets entering his state, and large contractors appearing in New Mexico, whose reputation and history was unknown to him. The network was also particularly helpful when he "needed to issue a license bond in Nebraska and needed an agency to sign it or understand it, or just to find the form," he said.

WITHOUT THE RESOURCES OF OTHER NASBP MEMBERS ACROSS THE COUNTRY WILLING TO HELP AND SHARE EXPERIENCE AND GIVE ADVICE, I WOULD NEVER HAVE SURVIVED.

Now that Padilla is part of a large, international agency, he has access to offices in most states and two other countries. "But the reality is, in most cases, I still call on my NASBP friends, because they'll help me and oftentimes may have more direct experience."

NASBP producer Members benefit from connecting with others—producers, underwriters and construction CPAs, with whom they have developed relationships through the Association. The NASBP network is a resource for business operation education and advice for NASBP professionals at every level. "It's not only the ongoing NASBP Surety School that provides information—NASBP's Regional and Annual Meetings offer powerful learning experiences as well," Bustard said.

Furthering New Professionals' Careers

New surety professionals in the industry also can find the NASBP network of value. "When NASBP Members see a young surety professional, they reach out their hand," Loehnert said. On many occasions, he has described the benefits of participating on NASBP committees, provided details on the educational offerings available through the Association, and discussed the power behind the online Membership database to a new producer. "I would rather compete against a professional who is doing things right than someone who is not," Loehnert explained.

New surety professionals should also consider the 5-15 Leadership Circle Committee. This Committee is an aspect of the NASBP Member network that offers those newer to the surety producer role a chance to develop their skills and prepare for more senior-level responsibilities as their careers grow. "It's a group of young people who have been in the business at least five years but less than 15," Hecker explained. Those newer members enter the 5-15 Leadership Committee, where one of the requirements of participation is to be matched up with a mentor. "Part of their development is giving them someone to talk to on a regular basis that they don't have a business relationship with," Hecker said. Mentors are typically located in the same general region of the country, but not where they might compete directly with their mentee. Hecker said another benefit of these strategic networking relationships is that "they're able to sit down in person with their mentor once a year at NASBP Regional Meetings."

Padilla said those new to the industry may want to begin their participation in the Association at a NASBP Regional Meeting. "They're smaller and you won't be intimidated," he explained. Attending a seminar or the Surety School is also a surefire way to jump in. "I and a lot of other individuals have been teaching for years at the NASBP Surety School," Padilla said. "When you leave a NASBP School or seminar, you receive a roster with contact information for the instructors as well as every student or attendee." It isn't unusual for him to get calls from students who came through the NASBP Surety School years ago, proving that this contact list—which includes producers and underwriters from across the U.S. as well as other countries—is another valuable NASBP networking resource for participants.

Feature

APPLIED EDUCATION

NASBP Surety School provides tools to use every day.

VISIT THE OFFICE of Sean Cunningham, professional associate at ACE Surety in Philadelphia, and you'll see the binder that he received at NASBP's Level II Surety School sitting on his desk. "I refer to it at least five times a week, refreshing myself on what I learned there," he said. "We covered all the fundamentals about the work in process, starting from scratch."

NASBP's William J. Angell Surety School offers that kind of practical, immediately applicable knowledge to people in the surety industry twice a year. Graduates of the Level I and Level II classes shared their views.

I ESPECIALLY APPRECIATED THE INSTRUCTOR DYNAMIC, WITH ONE FROM A SURETY AND ONE A PRODUCER.

Level I - Gaining The Big Perspective

Level I classes cover the fundamentals—a valuable experience for people who are new to the industry. Lorne Brooks, account executive with Harding Brooks Associates LLC in Vestal, NY, said the class was a critical tool in establishing the base of his surety career. "I would be light years behind if I had not taken Level I," he said. "Before the class I did only a very small amount of surety processing, mostly on the contract side; I had no real exposure to the commercial side."

Brooks admitted he had wanted to go straight to Level II classes but was glad that instructors persuaded him to start with Level I. "This class really gets your feet underneath you," he said. "The most important piece that I got out of it was how to analyze the balance sheet, to really look at a prospective account, and how to underwrite it. We learned how to get our arms around what they do, what they are projecting, and whether they are growing or shrinking. It's helped with digging into the numbers and knowing enough of what you're doing to be able to give an opinion," he added.

I WOULD BE LIGHT YEARS BEHIND IF I HAD NOT TAKEN LEVEL I.

The length of the class—three full days—was perfect for newcomers to the industry, Brooks said.

For Nolen Bevill, underwriting operations analyst at Lexon Surety Group in Mt. Juliet, TN, the Level I Surety School provided an understanding of the surety industry beyond her own role as underwriter.

"Other professionals—the producers, the agents, the claims

Guest speaker David Moody, Jr., President and CEO of C.D. Moody Construction Company, Inc. of Atlanta, addressed the NASBP Level III students attending the school in August.

2015 Summer Level I students responded to a question posed by their instructors.

THE MOST IMPORTANT PIECE THAT I GOT OUT OF IT WAS HOW TO ANALYZE THE BALANCE SHEET, TO REALLY LOOK AT A PROSPECTIVE ACCOUNT, AND HOW TO UNDERWRITE IT.

people. Level I was a great overview," Bevill said

Sarah Drinnan, client services representative at Florida Surety Bonds Inc. of Maitland, FL, said the instructors were outstanding. "The instructors took the time to make sure we understood everything that was being said by using many helpful examples."

Level Ii - Digging Into The Details

During the Level II classes, participants added to their practical knowledge of surety.

"Level II is a more in-depth, hands-on experience than Level I," Molly Motyka, account management executive at Main Street America Group, Raritan, NJ, said. "I especially appreciated the instructor dynamic, with one from a surety and one a producer.

"I was familiar with the underwriting process, but this really solidified some of the things that I already knew but wasn't actively working on," added Joseph Halleran, AFSB, client services manager at Assurance Agency Ltd. of Schaumburg, IL.

Ilyass Elmsaouri, a commercial surety underwriter with Aegis Security Insurance Company in Harrisburg, PA, said he benefitted from the class even though it has a heavy emphasis on contract surety. "I was still able to use lessons taught in class in my day-to-day underwriting of commercial accounts," he said. "For example, dissecting financial statements, understanding cash flow management, and analyzing work-in process are all tools that I've been able to apply to the underwriting of large commercial accounts.

Learning From Other Classmates

Participants in both levels of NASBP's Surety School said discussions with classmates significantly enhanced their learning experiences.

"The variety of perspectives in class discussions has helped me most in developing my surety knowledge," said Motyka. "With multiple players

IT TAUGHT ME TO REALLY UNDERSTAND WHO YOU ARE DOING BUSINESS WITH AND ENSURE YOU TRUST THEIR JUDGMENT.

I WAS STILL ABLE TO USE LESSONS TAUGHT IN CLASS IN MY DAY-TO-DAY UNDERWRITING OF COMMERCIAL ACCOUNTS.

in our industry, it is extremely valuable to hear the perspective from various producers, new underwriters, and seasoned professionals such as the instructors. The ethics discussions were also very useful, as ethics vary, even in an industry like ours with a focus on character. It taught me to really understand who you are doing business with and ensure you trust their judgment."

Halleran found solving case studies with other group members a very valuable experience. "There's a situation presented to you and you have to work in real time with the other people in your group to make decisions in 10 to 15 minutes," he said. "You see how other people work, and it makes you reflect on how you do things too."

Drinnan said the entire experience at the School is one she will never forget. "I was met with open arms from people throughout the country, and, as a result of that, I was able to make new friends, learn new things and best of all, walk away with a better understanding of what my role is in my position," she said.

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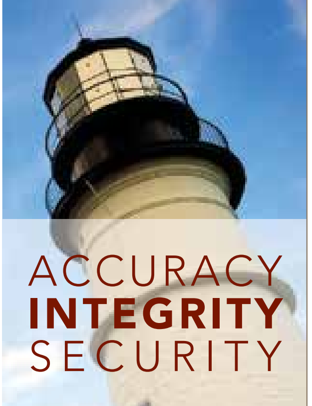

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