SLATER ALL LINES INSURANCE SCHOOL

Thank you for purchasing our online study program for the Washington State Surety Exam. Before you begin studying, please read this page thoroughly. As soon as you pass your state exam, we encourage you to email or call us with feedback about the state exam questions.

The study program you purchased from Slater All Lines Insurance School gives you a 90-day access pass to our Online Classroom, so ***please start studying right away and schedule your state exam within a month or so of the purchase date of this program*.** Memorize the material on these online PDFs and make sure to take the online practice exams several times to familiarize yourself with how to apply what you have learned to the sometimes difficult and ambiguous exam questions.

The Surety state exam consists of *50 multiple-choice questions*, administered by PSI testing company. Please keep in mind that the Bail Bonds section of the state exam consists of about 5-10 questions only! The majority of the exam questions are about the different types of bonds, their purposes, and State Regulations. You will need a 75% to pass.

The State Exams: Exams are conducted by PSI and test centers are located throughout the state. Please check the **PSI Washington Candidate Handbook** for times and fees by visiting www.psiexams.com.

SCHEDULING YOUR EXAM… Contact PSI testing company, at 1-800-733-9267 or www.psiexams.com, to schedule your state exams. To change or cancel an exam, you must call at least two business days prior to your exam date. There are no required study hours or completion certificates that need to be presented to PSI for you to be eligible to sit for the state exam.

- When you go to take your exam, remember to take two forms of valid identification (one must have your picture on it, i.e., a valid Washington Driver's License).

It is $49 to take the Surety Exam. If you pass your exam, the testing center will provide you with a test report that indicates you have passed the exam. If you do not pass the exam, the testing center will provide you a test report that tells you the exam must be taken again. There is a $49 charge to retake the Surety Exam.

Electronic fingerprints for license candidates are mandatory. You should schedule your fingerprint service for the same time as you take your exam at the testing center. Please call Identogo / Morpho Trust @ 888-771-5097 or go to www.identogo.com to arrange for your fingerprint service. You must pay for the service ahead of time with a credit card when you make your appointment.
• Your cost: about $55.00 for the fingerprinting.

Once you pass your state exams, *you will have 6 months to submit all of your paperwork and become licensed*. After 6 months, if you are not licensed you will need to take and pass the exam again.

After you have passed your state exam, the following will need to be sent into the Insurance Commissioner's office to get your license issued (*please note that your company/manager usually handles this paperwork for you*):

- Insurance License Application and Appointment/Affiliation Notice (if needed)
- Score Reports (originals or copies) from PSI testing center
- Surety License Fee = $20.00 and Filing Fee = $5.00

Test Center Addresses and directions: See www.PSIexams.com for other locations

Federal Way (Seattle)
500 South 336th St., Suite 220
Federal Way, WA 98003

- From I-5 to 320th street. Turn left on International (Pacific Way) (99).
  Turn right on 336th and pull in the 500 building parking lot.

Bellevue (Seattle)
Newport Place
4122 Factoria Blvd. S.E, Suite 303
Bellevue, WA 98006

- From I-405 - Exit 10 for Coal Creek Parkway towards Factoria.
  Turn left onto 128th Ave SE/Factoria Blvd SE. The test center will be on the right.
- From 1-90 E - Take Exit 10B.
  Turn Right onto 128th Ave SE/Factoria Blvd SE.
  Make a U-turn at SE 41st Pl. The test center will be on the right.

Arlington
18810 59th Dr. NE, Bldg. 44A
Arlington, WA 98223

- From Interstate 5 take the WA-531/172nd St NE exit, exit 206.
  Go East on 172nd St NE. Turn left on 59th Ave NE.
  Turn left on 188th St NE. The test site will be straight ahead.
  It is a 2-story grey building that says Arlington Flight Services on it.

Everett
1010 S.E. Everett Mall Way, Suite 208
Everett, WA 98208

- **North** on I-5, take Exit 189
  (WA-526 W/WA-527 N to Mukilteo/Whidbey Island Ferry/Broadway/Everett Mall Way).
  Bear right to WA-526 W / WA-527 N.
  You will see a sign reading "WA-527 N to Broadway/Everett Mall Way".
  At light, turn left on Bothell-Everett Hwy (SR-527) and go north for 0.5 mile to light at Broadway – get into left turn lane.
  Turn left onto Broadway which then becomes SE Everett Mall Way.
  Go approx. 0.8; just past light at West Mall Dr. get into middle left/right turn lane and turn left immediately before the Chevron gas station.
  Proceed down lane approx. one block to 1010 behind the gas station.
- **South** on I-5, take Exit 189
  (WA-526 W/WA-527 N to Mukilteo/Whidbey Island Ferry/Broadway/Everett Mall Way).
  You will see a sign reading "To Everett Mall Way".
  Take ramp to right to light at Everett Mall Way.
  Proceed through light onto SE Everett Mall Way (stay in left lane).
  Go approx. 0.8; just past light at West Mall Dr. get into middle left/right turn lane and turn left immediately before the Chevron gas station.

Proceed down lane approx. one block to 1010 behind the gas station.

TIPS FOR TAKING THE EXAMINATION

1. Remember that there are about 10-20 non-score-able questions within each state exam. Sometimes these questions appear as questions with no correct answer and sometimes the topics are not related to insurance as it pertains to what you will be scored on. DO NOT let these difficult and ambiguous questions throw you off. Just keep in mind that everything you can be graded on is in this textbook and the online computer program!

2. Always get a good night's sleep before the exam. In order for important information to remain fresh in your mind, study the class material every day until you do take the exam.

3. You will be taking your exam on a computer. Go through the exam and answer the easy questions first; skip the more difficult questions. Do not spend time and energy on difficult questions the first time around. With that being said, try to not second guess your answers to questions that you have already completed, because if you have studied the material thoroughly, your first answer usually will be the correct answer.

4. As you answer more and more questions on the test, your anxiety should ease and your ability to answer the questions will get better. **Read every question twice and eliminate all of the incorrect answers first before choosing the best answer**.

5. Please remember that there is material that has similar functions and similar sounding names. For example, "Guaranteed Insurable" and "Guaranteed Renewable" sound similar but have different meanings. There will be exam questions that will try to mix you up by using the similar material. Make sure you read each exam question and possible answers carefully, making sure the answer you choose matches the question being asked.

6. **<u>You have covered all of the material in this course that you will be tested on.</u>** We suggest you read the text book three to five times and do all of the quizzes online at least twice to pass the test. A number of studies have concluded that students retain material at a 90% rate if they learn by **doing**, rather than a 10% rate if they learn by just **reading**. It may also be helpful for you to read the textbook <u>out-loud</u> to insure you hear the material again. Slater All Lines Insurance School believes that using our Online Classroom practice exam simulations is critical in first-time test success, as it is great practice and will help build your confidence.

7. If you don't pass the test on the first try, don't worry. **Take it again as soon as possible** so that you will still have all of the material fresh in your mind. Immediately go back through all of the material and try to find any questions that you might have answered incorrectly. When you retake the exam, hopefully you won't make the same mistakes.

8. Just remember, even if it takes you more than once to pass the test, your future clients are not going to ask you how many times you had to take the exam before you passed it. **If you feel nervous or stressed, get up and stretch, take some deep breaths and remember that you will have plenty of time to finish.**

9. Passing the exam depends not only on how well you learn the subject matter, but also on how well you take exams.

A. Read the full question twice before marking an answer.
B. Avoid jumping to conclusions and watch for key words or phrases.
C. Interpret the unfamiliar questions.
D. Identify the intent of the question.
E. Memorize key points.
F. Beware of changing your initial answer to questions.

A. Read the full question twice before marking an answer. You cannot expect to answer a question correctly if you do not know what it is asking. If you see a question that seems familiar and easy, you might anticipate the answer, mark it, and move on before you finish reading it. This is a bad error on your part. Be sure to read the full question before answering it, as some questions are designed to trap exam takers. For example:

Mr. X incurs a medical bill of $1,100. His major medical plan has a $100 deductible and 80% - 20% coinsurance. How much of this bill will the insurer have to pay?

a. $100 b. $200 c. $300 d. $800

The correct answer is d. This is an easy question for someone to answer if they had read the question carefully because the question is asking about the insurer, NOT the insured (consumer). The insured would pay $300 of this bill and the insurer would pay $800. By reading this question too quickly you may answer it incorrectly.

B. Avoid jumping to conclusions and watch for key terms. The questions on the pre licensing exam are often misleading. To avoid being misled by seemingly obvious answers, make it a practice to read each question and each answer twice before making your choice.

While reading the questions, look for certain key terms such as, only, always, never, must, none or all, and except. Some terms frequently used are: all, except, and none except. Usually when a question starts with all or none and ends with except, you are looking for an answer that is opposite to what the question appears to be asking. For example:

All of the following injuries to an insured are exclusions in a medical policy, **EXCEPT:**

a. intentional injury caused by the insured
b. an employee's injury which is work related
c. insured's broken foot caused at home when he fell down the stairs
d. injury while the insured was in the commission of a crime

C is the correct answer. If you didn't read the question carefully and catch the term EXCEPT, you may have answered A, B, or D which are actually excluded (NOT COVERED) in medical plans.

C. Interpret the unfamiliar questions. Do not be surprised if some questions on the test seem unfamiliar at first. If you have studied the material, you will have the information to answer the questions correctly. The challenge may be a matter of understanding what the question is asking. Some questions will be presented indirectly and you may have to interpret the meaning of a question before you answer it. For example:

Mr. X's premium was due on March $1^{st.}$ He has a medical claim on March 5^{th}. The insurance company pays the claim. What provision in a policy allows this payment?

a. Incontestability period b. Entire contract provision
c. Grace period d. Assignment provision

The answer is C, the grace period. This question is asking you to apply knowledge of a provision in life and disability contracts to a "what if" scenario. Or a question could be asked like this…

A Grace Period is a period of time that ___.

a. allows insurance companies to pay claims
b. delays the payment of a claim
c. the insured is still covered by insurance even though the premium has not be paid
d. no claims would be paid because the premium was not paid

The correct answer is C. At first glance, the two questions appear to be different, but in fact they test your knowledge of the *grace period*. Be aware that the pre licensing exam may test your knowledge from two different angles.

D. Identify the intent of the question. Many questions on licensing exams supply so much information that you may lose track of what is being asked. This is often the case in a story question. For example:

Mr. X owns a life policy on himself and has named his brother, Mr. Z, as the revocable beneficiary. One year later Mr. X marries Mrs. X. Mr. X has no children of his own, but Mrs. X brings with her two children from her previous marriage. Mr. X now wants to change the beneficiary from Mr. Z to Mrs. X. How will this be done?

a. Mrs. X must request the change in writing to the insurance company.
b. Mrs. X's children must request the change in writing to the insurance company.
c. Mr. X must request the change in writing to the insurance company.
d. Mr. Z must request the change in writing to the insurance company.

C is the correct answer because Mr. X owns the policy. A clue to the correct answer is the end of the question. Who has the right to choose or change a beneficiary? Only the owner of the contract may request changes in the insurance policy. Take time to identify what the question is asking. However, your ability to do so assumes you have studied sufficiently. You will not answer questions correctly if you do not know the material.

E. Memorize key points. Reasoning and logic will help you answer many questions, but you will have to memorize a good deal of information. In our material, a lot of information is bolded or italicized, and online material adds the benefit of color. Obviously, items which are bolded, italicized and/or in color would be things to memorize. A lot of difficulty in passing the pre licensing exam is the volume of material you will need to know.

F. Avoid changing your answers. Never change any of your answers unless you know for sure that your original answer is incorrect. Your first impression is usually the correct one. However, some of the questions you answer later on will actually answer or clarify previously answered questions. If that is the case, do NOT go back to find that question. You have something to make notes on, make a note. Review when you are done and ONLY change the answers you know for certain are incorrect. Once you are done with the ISO or Industry section, review it and move to the State portion. Once you are in the State portion of the exam, you may NOT go back to the industry portion.

Surety Bonds Timeline

(The following timeline information is not needed for the prelicensing Surety exam, but is supplied to you as personal miscellaneous information only).

2,750 BC: Earliest known suretyship contract written on a Mesopotamian tablet. According to the contract, a farmer could not take care of his fields because he was drafted into the king's army, so another farmer offered to work the fields. The two agreed to split the profit evenly. A local merchant served as the world's first known surety by guaranteeing that the second farmer would keep his word.

1792-1750 BC: Suretyship first addressed in a written legal code–the Code of Hammurabi.

670 BC: Age of the oldest surviving written surety contract.

150 AD: Roman Empire developed first laws about surety.

1837: William L Haskins proposed the first surety company in America–the New York Guarantee Company. (Tasker, Murphy & Schwartzkopf)

1840: The first successful corporate surety, Guaranty Society of London, founded. (Tasker, Murphy & Schwartzkopf)

1853: New York enacted first law allowing establishment of corporate surety firms.

1865: Fidelity Insurance Company became first U.S. corporate surety company. (NYT)

1884: American Surety Company incorporated in New York and becomes first U.S. company committed to surety underwriting.

1894: Congress passed the Heard Act, requiring surety bonds on all federally funded projects.

1898: U.S. Supreme Court heard American Surety Co. v. Pauly, its first surety case.

1908: Fourteen corporate sureties formed the Surety Association of America. (surety.org)

1917: The victorious defendants of the Venner v. New York Central Railroad Company et al. Supreme Court case collected a $50,000 surety bond in legal fees from the plaintiff. (NYT)

1930: First known surety bond against suicide written.

1931: Handbook of the Law of Suretyship and Guaranty written to clarify fulfillment of sureties.

1935: Miller Act passed requiring public work contracts exceeding $100,000 to obtain performance bonds. It also mandated payment protection for contracts exceeding $25,000.

1938: American Surety Company and New York Casualty Company develop a new "Discovery Bond," which protects businesses against old acts of employee dishonesty yet to be discovered. (NYT)

1942: National Association of Surety Bond Producers founded to represent the needs and interests of surety agents and brokers. http://www.nasbp.org

1971: Federal Trade Commission entered the insurance field for the first time by challenging the 1969 merger between the American General Insurance Company and Fidelity and Deposit Company of Baltimore. The merger had made American General the leading surety bond underwriter and the largest fidelity writer in the United States.

1991: Municipal Bond Investors Assurance Corporation began offering new surety bonds that covered deposits local governments put into banks. The First National Bank of Chicago was the first bank to use the bond. (NYT)

1993: Westpac Derivative Products, Ltd., became the first specialist in its music to use a surety bond. The bond was issued for $100 million and allowed the company to earn the highest triple-A ratings. (NYT)

2003: Surety insurance companies, including AIG and Travelers, pay an unheard of $900 million settlement to Enron customers following the crash. (NYT)

Introduction to Suretyship

Suretyship is a term meaning one person or entity (the surety) guarantees another entity (the obligee) that the third entity (the principal) will or will not do something. In other words, contract surety bonds guarantee the performance or financial obligations of others.

Suretyship (bonds) is one of the oldest forms of financial service. In ancient times a person might leave a family member as "surety" to another until an obligation or debt was discharged. Suretyship today is usually conducted by insurance companies and is evidenced by a written contract called a surety bond. Surety bonds are used to provide a wide range of guarantees. One type of surety bond may guarantee that a contractor will comply with all of the obligations set forth in a construction contract and another may guarantee that an importer or exporter will pay duties as required by the United States statutes.

Most large property and casualty insurance companies have surety departments. In addition, there are some insurance companies for which surety bonds make up all or most of their business. In either case, in order for a company to write a surety bond in the United States, it must be licensed by the insurance department of one or more states in which the surety conducts business. ***A surety that wants to write bonds for federal government construction projects must have a certificate of authority issued by the U.S. Department of the Treasury.***

A Surety Bond is a type of bond that guarantees that a principal will carry out the obligation for which the principal is bonded. A surety bond is most often issued to a contractor, a person seeking a license or permit, or a person involved in a court case. **If the principal fails to fulfill its obligation, the surety will must fulfill the obligation or pay damages to the obligee**.

A Fidelity Bond is a type of bond that will reimburse an employer (the insured) for the **dishonest acts of employees**. Losses generally fall into one of the following categories of dishonest acts: Employee Dishonesty, Forgery, Burglary, Robbery and Theft.

License required to sell bonds:

- *Property and Casualty Producers license* allows the licensee to sell bonds.
- ***Limited-Line License*** means the **producer** can sell ***only one type of product***. **Limited Line Surety License** allows the licensee to sell bonds.
- No pre-license education or continuing education is required, however, **an initial state Surety insurance exam is still required. A Surety License is a limited lines license.**

CONTRACT PRINCIPLES (Elements/Parties/Power-of-Attorney)

A. Elements of a Contract… A **contract** is defined as an agreement enforceable by law.

It is entered into by two or more persons under which one agrees, for a consideration, to do or to refrain from doing an act in accordance with the wishes of the other party(s).

Insurance is a two party contract between a company and an insured, where an insurer agrees, for a consideration, to provide benefits, reimbursement or provide services for an insured. **Suretyship is a three party contract which will be discussed in detail**.

The **elements of a legal contract include:**

1. **Offer and Acceptance…** The applicant makes the "***offer***" to the insurance company. The insurance company "***accepts***" the ***offer*** by issuing the policy or bond.

2. **Consideration** means that ***something of value must be exchanged by all parties*** for the contract to be legal. It is the signed and completed application plus the premium from the insured or principal. The insurance company issues a policy or bond that represents a promise to pay.

3. **Legal Object…** In order for a contract to be legal, it must be for legal purposes only. This is why ***contracts do not cover intentional or criminal acts of the insured.*** **An insurance company may cancel a policy and deny a claim due to fraud committed by the insured or principal against the insurance company or bonding company.**

4. **Competent Parties…** The insured/principal must be of legal age, not be under the influence of intoxicants, and not be mentally handicapped. Any person 18 years of age or older will be considered of full legal age and may contract for insurance or bonds.

Special Note: Surety bonds are contracts and are subject to the statute of frauds and other common laws calling for certain types of agreements to be in writing. **Therefore, a surety bond is not enforceable unless it is in writing.**

B. Parties to a Surety Contract

The principal (obligor) – the party who has agreed to perform a contractual obligation.

The surety – the company providing the bond and agreeing to pay damages if the principal defaults. An individual could also act as a surety or indemnitor. If a bail bond has two or more indemnitors (guarantors) they would be listed as co-sureties or dual-sureties.

The obligee (the one protected) - is the recipient of the obligation. The party for whose benefit the bond is written, and to whom payment is made if the principal defaults.

C. Power of Attorney… A legal instrument (contract) in writing by which one person (a surety company for example) appoints another (bondsman or surety agent for example) as his agent and confers upon him the authority to perform certain **specific acts** (as in writing bonds for a surety company) ***on behalf of that person***. The purpose of a power of attorney is to evidence the authority of the agent to third parties with whom the agent deals.

- ***Because the bond agent has the "power of attorney" from a surety company the bonding agent can write bonds and sign on the surety's behalf.***

- ***Bond principals give their power of attorney to the bonding agent to act on the principals' behalf.***

- **Authority Agreement… An agreement (or contract) between the agent and the surety governing the use of the Power of Attorney.**

Differences between Suretyship (Bonds) and Insurance

Loss Payments: Differences between surety and insurance fields can be found with respect to indemnification and subrogation rights. Principals must indemnify the surety company for any losses and the ***surety has subrogation rights*** against the principal who purchased the bond. With insurance the insurer agrees to indemnify the insured or another party on behalf of the insured, and has ***no subrogation rights*** for paid losses against the insurer.

A surety bond is designed to protect the bonding company while an insurance policy is designed to protect the insured. ***Losses are NOT expected in the surety field*** so ***premiums are*** **not** ***collected to pay losses but*** **are actually paid for service fees*.***

Insurance companies are expected to have losses and charge premiums for paying those losses.

As an additional departure from Insurance contracts, Suretyship involves a continuous review process in order to determine that there is no negative change in the 3 Cs of a contractor and that the contractor's work program is progressing successfully.

Promise of Surety… If the principal fails to fulfill its obligation, the surety must either fulfill the obligation to the obligee or pay damages to the obligee. But then the surety has the right to recover its losses from the principal. This right of recovery is called subrogation and part of common law.

- In the event of a claim, the surety will investigate it. If it turns out to be a valid claim, the ***surety will pay it and then turn to the principal for reimbursement*** of the amount paid on the claim and any legal fees incurred. If the principal defaults and the surety turns out to be insolvent, the purpose of the bond is rendered void. Thus, the surety on a bond is usually an insurance company whose solvency is verified by private audit, governmental regulation, or both.

- ***A key term in nearly every surety bond is the penal sum***. This is a specified amount of money which is the maximum amount that the surety will be required to pay in the event of the principal's default. This allows the surety to assess the risk involved in giving the bond; the premium charged is determined accordingly.

Promise of Insurance is to assume, for a specified time, the losses suffered by the insured.
Insurance is a risk sharing device that expects losses based upon calculated probabilities. Though losses occur, bonds are structured and written with the expectation that few losses will occur and those that do occur are recoverable. A bond closely resembles a **bank letter of credit**. The **surety** is lending its credit to a person or organization to back their service or performance of an obligation.

Fidelity vs. Surety

Surety is a person (or entity), who is legally responsible for the contracts, debt, delinquency, or liability of another. If there is more than one surety, it could be called ***Co-sureties or Dual-sureties***. **Two or more individuals may act to guarantee that the principal will return for court**.

Fidelity means faithfulness to obligations, duties, or observances. It means adherence to right, careful and exact observance of duty, or discharge of obligations.

Fidelity Bonds are bonds that can protect business owners and employers from monetary or property loss at the hands of employees. Some businesses, including insurance companies, are required to utilize fidelity bonds. **Fidelity Bonds** are bonds issued to **protect an employer from financial or property losses due to the dishonesty of employees.**

Cancellation of a Bond: **Most bonds are continuous as long as premiums are paid**. ***However, with Fidelity Bonds, coverage for an employee is cancelled immediately upon discovery by the obligee of any dishonest act committed by that employee (the principal)***.

Indemnification and General Indemnity Agreement

If the principal defaults, the surety pays the obligee. **The surety has the common law right to recover its losses from the principal under the rights of subrogation**. Under subrogation only the bond penal amount (penalty amount) can be recovered by the surety and not any additional expenses or costs of the surety.

- ✓ **(General) Indemnity Agreement**— Is a contract provision which allows the surety to go after the principal for the recovery of expenses, costs and losses incurred by the surety over and above the bond amount. It in effect expands the subrogation rights.

The surety may not issue bonds unless it has received agreements from the principal and other indemnitors with sufficient assets to secure the surety from any claims that may be made against the bonds. This is done by an ***indemnity agreement to be signed by the principal and the individuals who will serve as indemnitors.***

The indemnity agreement sets forth and expands upon the separate common law obligations (subrogation rights) between the principal and the surety. A separate indemnity agreement may be issued for each bond or the parties enter into a **general indemnity agreement covering any bonds that the surety may issue to that contractor.**

The indemnitors (the contractor and individuals who have pledged their assets to support the bonds) agree that they will indemnify (completely reimburse) the surety for any liabilities, attorney's fees, expenses, or damages the surety may incur as a result of its issuance of a bond to the principal.

Surety, whether personal or corporate, is a guarantee that you will do something!

1. A **Personal Bond** (sometimes referred to as a **signature bond**) *is where you merely put up a promise to appear, or guarantee the bail with personal assets*. Fail to appear in court and you will owe the money for the bond. A Personal bond is just a signature for specific amount. The court wants a guarantee that you, as an individual, will properly administer the estate. A personal bond will need to be procured.

2. **Corporate Suretyship** was first formed in the 1800s. Prior to that time, individual arrangements were risky and there were no guarantees that the assets of a backer would satisfy the obligation. Once organizations began to specialize in issuing surety bonds, formal contracts backed up by corporate assets became available to meet individual and business needs. Bonds are usually issued by insurance companies.

A corporate surety is a company that charges for the guarantee; and

A personal surety is a person(s) who the court would accept as a guarantor (almost like a co-signor).

The Obligation of the Surety: by **Court Order**, by **Statute or** by **Contract.**

1. *Court Order*… Certain bonds are required by the courts. For example:

A ***court bond*** is a dollar amount set by a judge, which must be paid by the defendant charged with a crime, to ensure that the defendant returns for trial. A court bond can also be non-monetary -- or "on your own recognizance" -- meaning the judge believes the defendant will return to court on his/her own, without any disincentive from the courts. Bond can also be denied, and in the case of a homicide, usually is.

- The purpose of a court bond is to ensure a defendant returns to court. If the bond amount is paid, the accused may go home until the court date. If it is not paid, the defendant will be held at the local jail until the court case comes up.
- Bond, in many cases, ***is a set amount determined by the criminal statute*** that the defendant is accused of violating. Different classes of felonies and misdemeanors have different bond amounts. Sometimes, it is up to the judge's discretion; in others, it is not.
- Defendants usually don't have to pay the full amount of the bond. Most states have the ***10 percent rule which states*** the defendant only has to pay 10 percent of the total bond set. That is the bail amount.
- There are typically four different types of court bonds that can be issued after a person is arrested. There is the *signature bond*; the *cash bond*, in which the arrestee must pay the bail amount upfront before he is released; *the 10-percent bond*, in which the arrestee must pay 10 percent of the bail amount upfront before he is released; and *a* ***surety bond***, in which a bail bondsman, who is approved by the court, promises the court that the arrestee will appear on his court date, and that if he does not, the bail bondsmen will pay the bail amount in full.
  - ✓ **Bail bondsmen** are people registered and licensed by the state who will accept collateral in exchange for a cash payment to the court for bond.

Types of Court Bonds:

Signature Bond (a.k.a. Personal Bonds)

- A signature bond, or ***recognizance bond***, like other types of bonds, allows a suspect to be freed if he promises to show up in court. If he is not present for his court date, a bench warrant will be issued for his arrest and whatever amount of money was agreed upon between the court and the suspect will be paid to the court.
- Common crimes that may result in a signature bond include: theft, fraud, federal corruption, trespassing, disorderly conduct, drunken driving, drug possession, etc.
- ***A signature bond is different from a cash bond because the suspect does not pay the bond amount upfront***.

Personal Bond (a.k.a. Signature Bond)

- A personal bond, also known as a "***release on recognizance bond***," is a signed document that states your promise to appear in court on all future court dates related to your case if the court allows you to remain free. **A judge may issue a personal bond in lieu of bail or secured bonds.** If you fail to appear when required by the court's schedule, the judge will revoke the personal bond, take you into custody, and you must forfeit the amount of the personal bond to the court.

Probate Bond

- The property belonging to a deceased individual must be distributed through a probate court if the deceased did not leave a will. The ***court appoints an executor*** (usually a relative of the deceased) to maintain custody of the property until the proceedings have concluded. The executor must submit a probate bond to the court in an amount equal to the property's total value. A probate bond ***compensates the heirs of the deceased*** if any part of the property is stolen or unlawfully sold in the course of the proceedings.

Guardian Bond

- A guardian is a ***court-appointed agent*** charged with managing the finances or day-to-day care of a minor without living parents or of an individual with debilitating mental and/or physical handicaps. After accepting his/her duties, a guardian must submit a guardian bond to the presiding court. This bond protects the interests of the individual on whose behalf a guardian performs his/her duties. ***The bond compensates the individual if there is evidence of abuse of power or neglect by the guardian in court reports which the guardian must frequently submit.***

Appeal Bond

- Legal proceedings conclude with a **judgment** that favors either the plaintiff (the party who sues) or the defendant (party being sued). If the losing party chooses to appeal the judgment, the case passes to an appellate court, and the party who is appealing is not yet required to pay the penalties handed down by the initial judgment. Because judgments are often appealed for this very reason, ***appellate courts require an appeal bond from the appealing party.***

  If the appeal proceedings fail to overturn the original judgment, the appeal bond functions in two ways:

  - ***it ensures that penalties and applicable court costs are paid***
  - ***it discourages continued appeals solely to avoid these payments***

2. *Statutory Bonds* are bonds required by law or statutes, usually with the intention of protecting the public. Some of the same bonds are required by statute and by the courts, such as Appeal Bonds. Types of bonds that might be ***required by statute or law*** include:

Federal Officials Bond… coverage for the federal government in the event of loss due to dishonest acts of federal government employees.

Permit Bond… guarantees that a person licensed by a city or state agency will perform activities for which the bond was granted, according to the regulations governing the license.

Securities Bond… protects the issuer of securities (stocks and bonds) against forgery of the securities.

Appeal Bond… guarantees payment of the original judgment of a court. When a judgment is appealed, ***a bond is required by the court*** to guarantee that if the appeal is unsuccessful, funds would be available to pay the original judgment as well as costs of the appeal. This serves to discourage an individual from appealing merely to stall for time or for frivolous reasons.

Bid Bond… bond required of a contractor submitting the lowest bid on a project. ***If the contractor then refuses to undertake the project, the bid bond assures that the developer will be paid the difference between the lowest bid and next lowest bid.*** The bid bond encourages contractors to make serious bids and live up to their obligations.

Notary Bond… Notaries are licensed through the states. A claim against the notary in his/her professional capacity is filed ***against the state***. **The surety company collects a fee to write the notary bond. If a claim is made, the surety pays out to the state, as the obligee.**

Judicial Bond is a surety bond that includes either a *fiduciary* or a *court bond*.

- ***Fiduciary Bond***-guarantees those individuals in a position of trust will safeguard assets belonging to others placed under their control. For example, guardians appointed by a court who are authorized to pay expenses of the minor and administrators of estates who take care of a deceased's assets may require a fiduciary bond.

- ***Court Bond***-guarantees concerning ligation such as:
  - *Appeal Bond*, which guarantees that a judgment will be paid if an appeal is lost in a higher court
  - *Plaintiff's Replevin Bond*

- ***Replevin Surety*** *(Court)* ***Bond*** is secured by a plaintiff in a replevin ***court action*** to cover losses to the defendant or court officer when seizing the property in the defendant's possession and transferring it to the plaintiff. *If the plaintiff loses the case, the property must be returned. The bond pays if the plaintiff defaults.*

3. *Contract Bonds:*

Bid Bonds guarantee the owner that the principal will honor its bid and will sign all contract documents if awarded the contract. If the principal refuses to honor its bid, the principal and surety are liable on the bond for any ***additional costs*** the owner incurs in completing the contract. **This usually is the difference in the dollar amount between the low bid and the second low bid**. The penal sum of a bid bond often is ten to twenty percent of the bid amount.

Completion Bond… legal instrument used to guarantee the completion of a real-estate development according to specifications. **This is more encompassing than a performance bond, which ensures that one party will perform under a contract on condition that the other party performs.** The completion bond assures production of the development without reference to any contract and without the requirement of payment to the contractor.

Contract Bond… a guarantee of the performance of a contractor. In general, ***contract bonds are used to guarantee that the contractor will perform according to the specifications of the construction contract.*** If the contractor fails to perform according to contract, the insurance company is responsible to the insured for payment, up to the limit of the bond, which is usually for an amount equal to the cost of the construction project. The insurance company then has recourse against the contractor for reimbursement.

Payment Bonds guarantee the owner that subcontractors and suppliers will be paid the monies that they are due from the principal. The owner is the obligee; the "beneficiaries" of the bond are the subcontractors and suppliers. Both the obligee and the beneficiaries may sue on the bond. An owner benefits indirectly from a payment bond in that the subcontractors and suppliers are assured of payment and will continue performance. If the principal fails to pay the subcontractors or suppliers, they may collect from the principal or surety under the payment bond, up to the penal sum of the bond. Payments under the bond will deplete the penal sum.

Performance Bonds guarantee the owner (obligee) that the principal will complete the contract according to its terms including price and time. The owner (obligee) may sue the principal and the surety on the bond. If the principal defaults or is terminated for default by the owner, the owner may call upon the surety to complete the contract.

Many performance bonds give the surety three choices:

1) Completing the contract or project itself through a completion contractor

2) Selecting a new contractor to contract directly with the owner

3) Allowing the owner to complete the work with the surety paying the costs

Underwriting **(3 Cs)**

Unlike with insurance, there is little expectation of loss with surety bonds. Because of that, the bond premium is typically meant to cover ***prequalification services***.

The Prequalification (Underwriting) Process is often referred to as the 3 Cs of underwriting:

1. Capacity **2. Capital** **3. Character**

The surety company's prequalification process (underwriting) carefully analyzes the contractor's entire business operation, because the surety is backing the promise of that contractor to perform the contract. The surety company evaluates the contractor's capacity to perform this particular contract as well as other contracts already written, determines his/her financial strength, reviews his/her character, and may ask for personal or corporate indemnity.

1. Capacity to Perform - typically includes analysis of:

- Resumes of the contractor and key personnel
- Contractor's track record of successfully completed work
- **Adequacy of the contractor's equipment and tools required to perform the contract**
- Rationale for why the contractor is undertaking the project
- Continuity plan that illustrates how the company will continue performing its obligations in the event of the demise or departure of key personnel
- Contractor's future plans, goals, objectives, and growth strategies

2. Capital ***(Financial Strength)*** - typically includes analysis of:

- Detailed financial statements for the past 3-5 years. Accounting methods should comply with Generally Accepted Accounting Principles (GAAP). Financial statements should include: Balance Sheet, Statement of Earnings, Statement of Changes in Owner's Equity, Statement of Cash Flow and Contract Schedules.
- *The surety may ask for interim financial statements. Requirements for interim statements vary, but a six-month statement usually is the minimum.*
- Contract schedules that typically include a summary of completed contracts and contracts in progress. ***Sureties also will require a schedule of work in progress (usually quarterly).***
- Cost records that account for the financial status of the contractor's jobs.
- Credit reports demonstrating how the contractor handles payment of debts; and
- A bank line of credit showing unsecured credit that can be used as short-term working capital.

3. Character - Surety companies may review trade references from owners, architects, subcontractors, general contractors, material suppliers, etc., with whom the firm has worked to get a sense of the contractor's reputation for fair, businesslike dealings.

Indemnity Agreement - Surety companies may require the personal indemnity of the owners, their spouses, or major stockholder(s) of the construction firm to assure that they are going to put forth their best efforts to meet contract obligations. For a proper evaluation of what loss paying power the personal indemnity does provide, the surety may request the contractor to provide personal financial statements.

- The indemnity agreement sets forth and expands upon the separate common law obligations (subrogation rights) between the principal and the surety. A separate indemnity agreement may be issued for each bond or the parties enter into a **general indemnity agreement covering any bonds that the surety may issue to that contractor.**

As an additional departure from insurance contracts, Suretyship involves a continuous review process in order to determine that there is no negative change in the 3 Cs of a contractor and that the contractor's work program is progressing successfully.