Contents

PURPOSE AND TYPES OF SURETY BONDS

What is the Surety's Job? To protect public and private interests against financial loss resulting from a company or individual's bankruptcy or failure to perform a contracted service. **If the principal fails to fulfill its obligation, the surety must either fulfill the obligation to the obligee or pay damages to the obligee**.

There are many bonds available from a milkman's bond to a tax collector's bond to removal bonds… you get the picture. This chapter will focus on Commercial bonds and Contract bonds.

Insurance is designed to protect the insured against financial losses from covered perils. Insurance protects things, houses, cars, or people.

Surety protects actions or the promise of action.

- ***For example***: *A contractor is awarded a building contract for a school. The principal (the contractor) will usually be required to provide a performance bond (or contract bond). The performance bond guarantees the obligee (the school) that the work will be completed in accordance with the contract. If the contractor (the principal) defaults, the surety will be responsible for completing the work or paying damages to the obligee (the school).*

Period of Coverage**:** Surety bonds ordinarily do not terminate until the principal has fulfilled its obligation, which may take only a few days or as long as many years. Consequently, **surety bonds are not issued as year-to-year contracts and they normally do not allow either the surety or the principal to cancel them.**

A. Commercial Bonds

1. **License and Permit Bonds** are bonds that are required prior to obtaining a license or permit from a city, county, state, or occasionally the federal government. These bonds are a financial guarantee that whatever the underlying statute, state law, municipal ordinance, or regulation requires it will be followed. Statutory bonds are governed by law and guarantee compliance with the underlying laws. The purpose is usually to safeguard the public. A consumer who has been harmed by the individual who obtained the bond can file suit and be paid by the surety company.
   - *Examples of a license or permit bond include brokers, public adjusters, and contractors.*

2. **Public Official Bonds** are bonds that protect against the dishonesty or lack of performance of duties by a public official. A Public Official is someone who holds a public office; e.g., mayor or school board official.

- **Blanket Position Public Official Bonds** are bonds that protect from loss due to dishonest acts of public employees. The bond is issued for a fixed amount and **each position** is covered for this amount.
- **Blanket Public Official Bonds** are bonds that protect from loss due to the **dishonest acts of all public employees.**
   - ***For example***; *should a public official's office have a $20,000 blanket bond, and three employees cause a total loss of $50,000, the bond will only pay $20,000. The blanket amount is a fixed total amount for a loss, NOT per employee.*

3. **A Court Bond** is a bond that guarantees proper performance or completion of fiduciary duties (e.g., the execution of a will) in compliance with court orders.

Some basic court terms will help you understand:

i. **Defendant** — the party against which an action is brought.

ii. **Plaintiff** — the one who initially brings suit.

iii. **Appellant** — the one (defendant) who appeals a court's decision made against them.

For example: A plaintiff wins a suit against an individual or defendant. The defendant decides to appeal the court decision. That defendant is now referred to as an appellant and the court will require the ***appellant to get an appeal bond****.*

a) **Judicial Bonds** are a class of bonds needed if you enter into a lawsuit to guarantee payment of the costs related to the suit. Judicial bonds can be divided into 2 categories; Defendant and Plaintiff. There are many different types of these.

   i. **Defendant bonds** may block plaintiff actions or postpone payment of a judgment. Common types of defendant bonds are Bail bonds. Appeal bonds, Counter-Replevin bonds, and Release of lien bonds.

   ii. **Plaintiff Bonds** are required of plaintiffs to ensure protection of the defendant should the plaintiff lose the lawsuit. Common types of plaintiff bonds are attachment bonds, injunction bonds, and replevin bonds.

b) **Appeal Bond** See Supersedeas Bond below.

c) **Supersedeas Bond** (a.k.a. *Appeal Bond*) is a type of surety bond that a court requires from an appellant (***the party who appeals a court's decision***) who wants to delay payment of a judgment until the appeal is over.

- **Appeal Bond (supersedeas)** guarantees that the judgment will be paid if affirmed and that the costs of the appeal will also be paid should the defendant default.
- The appeal or supersedeas bond guarantees that the judgment will be paid to the plaintiff if affirmed by the court, including the costs of the appeal, should the appellant default. This protects the plaintiff against the bankruptcy of the appellant and assures that if the appeal is lost the initial judgment is still available. This can also stop frivolous appeals since the funds are already paid out, though to a third party for holding.

  Terms of the Appeal Bond… Appeal bonds must be collateralized 100 percent. This means a defendant/appellant cannot put down a mere fraction of the bond amount and let the surety finance the remainder, as is the case in most surety bonds. ***An appeal bond must be backed entirely by cash and/or other valuable assets.***

d) **Attachments Bond** or writ of attachment bind is used in civil cases where a creditor seizes property of the debtor. When a debtor owes money the creditor may ask the court to seize or attach property up to the value of the debt. Before this happens though, the courts may request a bond in that amount in the event the property was wrongfully seized. If that was the case, the bond allows the debtor to be paid for any property not returned as well as any legal costs and other damages.

e) **Injunction Bond**: An injunction bond (very similar to the appeal bond) guarantees that damages to a defendant will be paid by the plaintiff, if it is later decided that a preliminary injunction should not have been issued. The bond instructs the plaintiff to indemnify a defendant against financial damages they may incur if the court decides the injunction was not needed. Financial damages can include court costs, legal fees, and other damages.

A plaintiff may seek an injunction against another party, but the courts require that an injunction bond be furnished before granting the injunction.

- An injunction is a court order to stop or start doing something. There are 3 types of injunctions;
  - Temporary injunction, a.k.a a temporary restraining order (TRO)
  - Preliminary injunctions are issued at the start of a lawsuit to prevent certain conduct, and these remain in effect until a verdict. They may become…
  - Permanent injunctions, issued as a final judgment
- E.g., Wrongful firing, taken to court, may result in an injunction for the company to rehire you. A party that fails to comply with an injunction faces criminal or civil penalties, including fines or imprisonment.
- E.g., an insurer selling a product that has not been approved by the commissioner would have a cease and desist order against it.

f) **Probate Bond**, sometimes called a fiduciary bond, is written for the executors of an estate to protect the estate from mishandling. It is ordered before the court will appoint an executor. The purpose is to hold them accountable and liable so they perform the duties necessary. *E.g., pay the bills of the deceased and distribute the remainder of the estate according to the will have the deceased (rather than taking a world cruise with the money).*

g) **Fiduciary Bond** - guarantees that 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 the expenses of the minor and administrators of estates who take care of a deceased's assets may require a fiduciary bond.

Fiduciary Bonds (usually required by Court Order or by Statute) guarantee that a fiduciary will faithfully perform duties and act in the best interests of the person being represented. ***A fiduciary is someone who has a legal right to handle the affairs of others. Fiduciary bonds are available for administrators and executors of estates.*** Fiduciary bonds are also issued to receivers in bankruptcy cases and to various trustees.

Fiduciary: person or company holding assets in trust for a beneficiary. The fiduciary is charged with the responsibility of managing the money wisely for the beneficiary's benefit. Some examples of fiduciaries are executors of wills and estates, receivers in bankruptcy, trustees, and those who administer the assets of underage or incompetent beneficiaries.

- A broker is a *fiduciary* for the seller.
- A banker is a *fiduciary* for the bank's depositors.
- An attorney may be a *fiduciary* for the client.
- A guardian or trustee is a *fiduciary* for the beneficiaries. ***Guardians or trustees*** may need to be bonded because they are often ***appointed by courts*** to handle the affairs of people who are incapable of doing so for themselves.
- The bond needed may be called a **Guardian Bond** or a **Trustee bond**, depending on the case.
- A qualified producer (or Surety) who receives collateral or security for a bond is a ***fiduciary*** of the property.

Most U.S. States have laws about what a fiduciary may or may not do with a beneficiary's assets. *For instance, it is illegal for fiduciaries to invest or misappropriate the money for their personal gain.*

Prudent Person Rule: a standard adopted by some U.S. states to guide those with responsibility for the money of others. Such fiduciaries (executors of wills, trustees, bank trust departments, and administrators of estates) must act as a prudent man or woman would be expected to act, with discretion and intelligence, to seek reasonable income, preserve capital, and, in general, ***avoid speculative investments***.

h) **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 and additional losses and expenses to the defendant must be paid. The bond pays if the plaintiff defaults.*

- Replevin means an action for the **recovery of property taken** rather than for the value of that property. A legal form of action ordinarily employed to recover possession of specific personal property withheld plus damage for its detention. This can also be known as Claim and Delivery or Revendication.
- A **Replevin bond** allows the plaintiff to possess the property before the trial begins.
- A **Counter-Replevin bond** allows the defendant the right to have the property back.

B. Surety Laws RCW 48.28

1. **RCW 48.28.010 Requirements deemed met by surety insurer.** Whenever by law or by rule of any court, public official, or public body, any surety bond, recognizance, obligation, stipulation or undertaking is required or is permitted to be given, any such bond, recognizance, obligation, stipulation, or undertaking which is otherwise proper and the conditions of which are guaranteed by an authorized surety insurer, or by an unauthorized surety insurer as a surplus line pursuant to chapter 48.15 RCW of this code, shall be approved and accepted and shall be deemed to fulfill all requirements as to number of sureties, residence or status of sureties, and other similar requirements, and no justification by such surety shall be necessary.

2. **RCW 48.28.020 Fiduciary bonds—Premium as lawful expense.** Any fiduciary required by law to give bonds, may include as part of his or her lawful expense to be allowed by the court or official by whom he or she was appointed, the reasonable amount paid as premium for such bonds to the authorized surety insurer or to the surplus line surety insurer which issued or guaranteed such bonds.

3. **RCW 48.28.030 Judicial bonds—Premium as part of recoverable costs.** In any proceeding the party entitled to recover costs may include therein such reasonable sum as was paid to such surety insurer as premium for any bond or undertaking required therein, and as may be allowed by the court having jurisdiction of such proceeding.

4. **RCW 48.28.040 Official bonds—Payment of premiums.** The premium for bonds given by such surety insurers for appointive or elective public officers and for such of their deputies or employees as are required to give bond shall be paid by the state, political subdivision, or public body so served.

5. **RCW 48.28.050 Release from liability.** A surety insurer may be released from its liability on the same terms and conditions as are provided by law for the release of individuals as sureties.

6. **RCW 48.18.230 Binders—Duration—Premium.**

   (1) A "binder" is used to bind insurance temporarily pending the issuance of the policy. No binder shall be valid beyond the issuance of the policy as to which it was given, or beyond ninety days from its effective date, whichever period is the shorter.

   (2) If the policy has not been issued a binder may be extended or renewed beyond such ninety days upon the commissioner's written approval, or in accordance with such rules and regulations relative thereto as the commissioner may promulgate.

   (3) Where the premium used in the binder differs from the actual policy premium by less than ten dollars, the insurer shall not be required to notify the insured and may use the actual policy premium.

C. Contract Bonds

C. Contract Bonds are bonds that provide financial security and construction assurance on construction jobs. By law, most public construction projects in the U.S.A. require a surety bond to guarantee the project.

It assures the project owner (the obligee) that the contractor (the principal) ***will perform*** the contracted work and/or pay subcontractors, laborers, and suppliers. **If the principal (the contractor) fails to fulfill its obligation, the surety must either fulfill the obligation to the obligee or pay damages to the obligee**. Types of contract bonds include:

a) **A Bid Bond** guarantees that if the bidder is awarded the contract, two things will occur: one, the bidder will actually sign and accept the contract, and two, a performance bond will be issued. The bid bond guarantees that the contractor, if low and selected and fails to complete the job, the surety is obligated to pay the additional costs incurred to use the next highest bidder to complete the job. The surety will then subrogate to the first bidder.

For example, if the successful bidder defaults on either account, the obligee may use as much of the bid bond penalty as necessary to cover resulting losses and expenses. **Extra expenses are incurred if a project must be rebid or if the job must be awarded to the next highest bidder.**

b) **A Payment Bond** (a.k.a. labor and material bonds) is a bond given to ***guarantee payment,*** usually of a contractor to sub-contractors and suppliers. It operates in conjunction with a performance bond. This is frequently the only protection offered to those supplying work or materials to a public job. Sometimes a single bond will contain both the performance and the labor and payment clauses.

c) **A Performance Bond** is a bond guaranteeing the performance of the terms of a contract. It guarantees the project will be completed on time, at the agreed-upon price, and per the contract terms and conditions. These protect the owner of the contract from financial loss should the contractor refuse or be unable to fulfill the contract obligations.

d) **A Completion Bond…** When a contractor borrows money to fund a construction project, the lender may require a guarantee that the project will be carried out and that the contractor will be paid for the work. A completion bond guarantees the lender (obligee) that the contractor (borrower and principal to the bond) will apply the funds to the project and complete the project free of any liens or encumbrances.

e) **Retention Bond** is a type of guarantee used in the construction industry after construction is complete. Where a performance bond guarantees the completion of a project according to the terms of the contract, this acts like a warranty. The contractor is responsible for repairs from defects or problems that may show up in a specified period of time.

Retainage is an agreed-on portion of the contract price that is withheld until the completion of the project. This bond bypasses that need without withholding funds from being paid, putting the funds back in the hands of the contractor.