Surety FAQ

Surety Frequently Asked Questions

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What will 2010 mean to the surety industry and your ability to secure bonds?
According to a recent NASBP (National Association of Surety Bond Professionals) survey, 64% percent of bond producers think it will be harder to obtain bonds in 2010 compared to 2009.

Is green building still a niche sector?
According to FMI's 2008 U.S. Construction Overview, construction industry stakeholders are increasingly recognizing green building capabilities as a necessary part of a firm's best practices.
Three major trends are pushing green building to the forefront of the construction industry's consciousness:

- An unprecedented level of government initiatives.
- Heightened residential demand.
- Improvements in sustainable materials.

What is Suretyship?
Suretyship is a very specialized line of insurance that is created whenever one party guarantees performance of an obligation by another party. There are three parties to the agreement.

- The principal is the party that undertakes the obligation.
- The surety guarantees the obligation will be performed.
- The obligee is the party who receives the benefit of the bond.What is a surety bond?

A surety bond is a written agreement where one party, the surety, obligates itself to a second party, the obligee, to answer for the default of a third party, the principal. There are two categories of surety bonds:

Contract Surety Bonds provide financial security and construction assurance on building and construction projects by assuring the project owner (obligee) that the contractor (principal) will perform the work and pay certain subcontractors, laborers, and material suppliers.

Contract surety bonds include:

- bid bonds, which provide financial assurance that the bid has been submitted in good faith, and that the contractor intends to enter into the contract at the price bid and provide the required performance and payment bonds.
- performance bonds, which protect the owner from financial loss should the contractor fail to perform the contract in accordance with its terms and conditions.
- payment bonds, which guarantee that the contractor will pay certain subcontractors, laborers, and material suppliers associated with the project.
- maintenance bonds, which normally guarantee against defective workmanship or materials for a specified period.
- subdivision bonds, which guarantee to a city, county, or state that the principal will finance and construct certain improvements such as street, sidewalks, curbs, gutters, sewer, and drainage systems.
- Commercial Surety Bonds - guarantee performance by the principal of the obligation or undertaking described in the bond.Commercial surety includes:
- License and permit bonds, which are required by state law or local regulations in order to obtain a license or permit to engage in a particular business, e.g. contractors, motor vehicle dealers, securities dealers Blue Sky bonds, employment agencies, health spas, grain warehouses, liquor, and sales tax;
- Judicial and probate bonds, also referred to as fiduciary bonds, secure the performance on fiduciaries' duties and

compliance with court order, e.g. administrators, executors, guardians, trustees of a will, liquidators, receivers, and masters. Judicial proceedings court bonds include injunction, appeal, indemnity to sheriff, mechanic's lien, attachment, replevin, and admiralty;
 - Public official bonds, which guarantee the performance of duty by a public official, e.g. treasurers, tax collectors, sheriffs, judges, court clerks, and notaries;
 - Federal (non-contract) bonds are those required by the federal government, e.g. Medicare and Medicaid providers, customs, immigrants, excise, and alcoholic beverage; and
 - Miscellaneous bonds, e.g. lost securities, lease, guarantee payment of utility bills, to guarantee employer contributions for Union fringe benefits, and workers compensation for self-insurers; What characteristics of suretyship are like more common forms of insurance?

 - They are both risk transfer mechanisms.
 - State insurance commissioners regulate them both.
 - They both provide for financial loss.How is suretyship different from more common lines of insurance?

 - In traditional insurance, the risk is transferred to the insurance company. In suretyship, the risk remains with the principal. The protection of the bond is for the obligee.
 - In traditional insurance, the insurance company takes into consideration that a certain amount of the premium for the policy will be paid out in losses. In true suretyship, the premiums paid are "service fees" charged for the use of the surety company's financial backing and guarantee.
 - In underwriting traditional insurance products the goal is "spread of risk." In suretyship, surety professionals view their underwriting as a form of credit so the emphasis is on prequalification and selection.How does a surety underwrite?
Each surety company has its own guidelines and underwriting criteria. However, the following basic factors will be taken into consideration in some format.
 - Capacity. Does the applicant have the skill and ability to perform the obligation?
 - Capital. Does the financial condition of the applicant justify approval of the particular risk?
 - Character. Does the applicant's record show him to be of good character and likely to perform the obligation he or she assumes?

What is Personal Indemnity?
It is common for a surety to request the indemnity of the owners of a closely held corporation. Typically, the spouse's indemnity also is required because personal assets are jointly owned. The two main reasons for this requirement are that the surety requires all personal assets to be available to back the guarantee and that there is less chance a principal will avoid its responsibilities if its personal assets are at stake.

How does collateral security relate to a surety bond?
If an underwriter is unable to approve a bond request based on the qualifications given by the principal, the company may suggest depositing some form of collateral as an inducement to write the bond. In practice, many bonds are written on this basis, particularly ones that are considered financial guarantees.

What is a financial guarantee bond?
A financial guarantee bond obligates the surety to pay a certain amount of money if the principal does not perform its obligation. Examples include tax bonds and Medicare and Medicaid bonds. These bonds are extremely hazardous and very carefully underwritten.

What is the Treasury List, or T-list, and how can I get a copy?
Circular 570: Federal Treasury Listing of Qualified Sureties, also known as the T-list, provides a list of all surety companies qualified to write bonds on federal contracts. Access the T-list online at www.fms.treas.gov/c570/c570.html.

What is Embezzlement?
Wikipedia defines embezzlement as "the act of dishonestly appropriating goods, usually money, by one to whom they have been entrusted." The Association of Certified Fraud Examiners reports that the median loss suffered by organizations with fewer than 100 employees was $200,000. This is higher than the median loss in any other category, including the largest organizations. "Small businesses also suffered the largest losses in our 2006 study. Check tampering and fraudulent billing were the most common small business fraud schemes."

Who other than California is having budget issues?
Many states are facing a great fiscal crisis. At least 46 states faced or are facing shortfalls in their budgets for this and/or next year, and severe fiscal problems are highly likely to continue into the following year as well. Combined budget gaps for the remainder of this fiscal year and state fiscal years 2010 and 2011 are estimated to total more than $350 billion.

For more information please visit http://www.cbpp.org/

Loss of control by the shareholders?
The shareholders will never lose control unless they voluntarily give it up. A shareholder with as little as one single share

can control the company by voting the one share he/she owns outside the ESOP and as Trustee of the ESOP vote all the shares inside the ESOP.