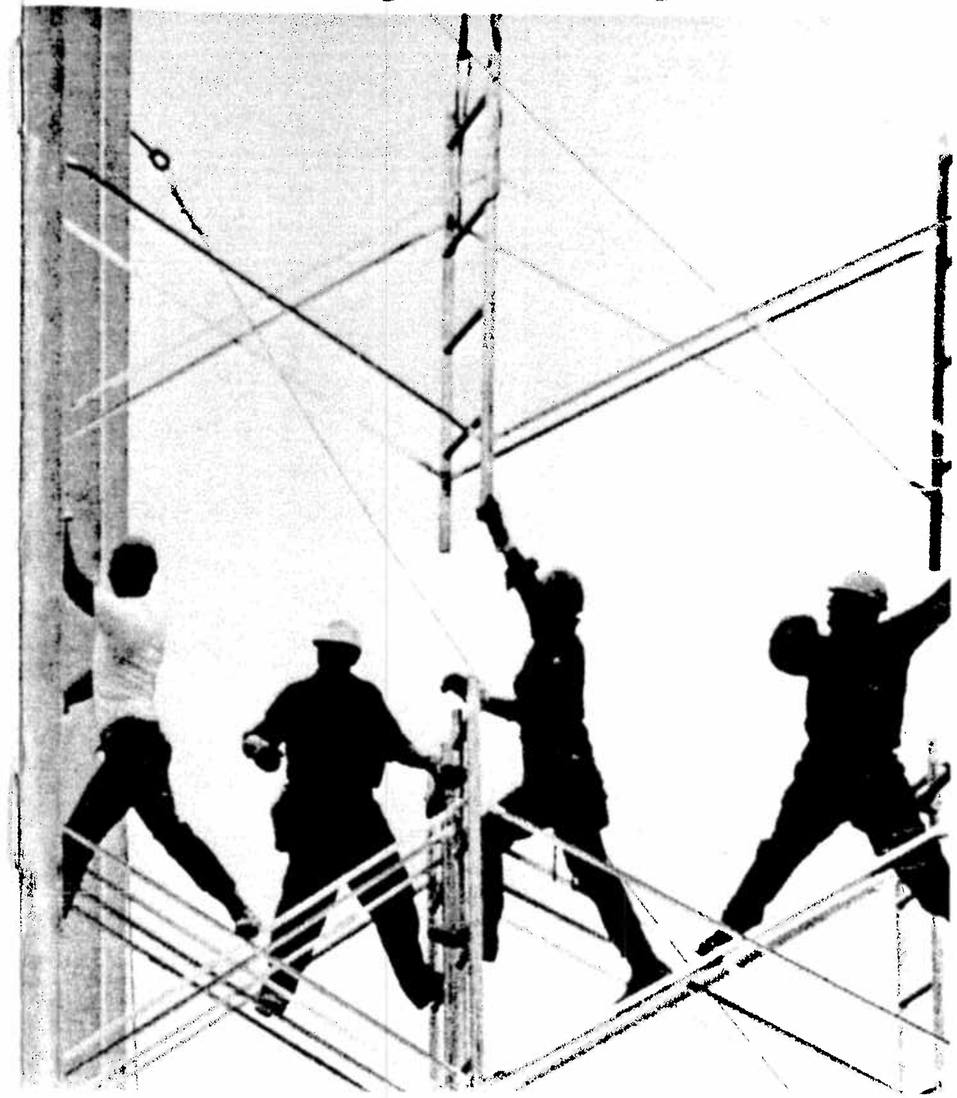
THE SURETY ASSOCIATION OF AMERICA
100 Wood Avenue South

CONTRACT BONDS
The Unseen Services of a Surety



CONTRACT BONDS
The Unseen Services of a Surety

THE SURETY ASSOCIATION OF AMERICA
100 Wood Avenue South
Iselin, N. J. 08830

CONTRACT BONDS
The Unseen Services of a Surety

Suretyship has been in existence since the beginning of time. In fact, the Bible is filled with references to it. Genesis recounts that Judah became surety to his father for his brother, Benjamin[1] and Solomon warned that "he that is surety for a stranger shall smart for it."[2] The Code of Hammurabi, Herodotus and the *Magna Carta* all refer to forms of suretyship and in Shakespeare's play "The Merchant of Venice" the leading issue was the contract of suretyship entered into by Antonio and Shylock. Shylock was to take a pound of Antonio's flesh if Bassanio, a friend of Antonio's, was unable to pay his obligation to Shylock on the due date.[3]

1. Genesis 43:9
2. Proverbs 11:15
3. Backman, *Surety Rate-Making*, New York: The Surety Association of America, 1948, p 2.

CORPORATE SURETYSHIP

These forms of suretyship are different from suretyship as we know it today. These old references pertained to personal suretyship and involved the principals trying to find someone, usually a friend or relative, to provide a guarantee of performance for him. However, personal suretyship had obvious defects because the surety could die or go broke, thereby making his bond worthless.

As business and commerce in the United States became more sophisticated, the need for a better form of suretyship arose. In the latter part of the 19th century, corporate suretyship came into being and is the suretyship which is generally used in the U. S. today.

What Does the Surety Do?

Today all the 50 states, as well as the federal government, require contractors of certain public works to furnish contract bonds.[4] However, few understand exactly what a surety does in providing these bonds. This pamphlet will document some of the services performed by the surety through a selection of actual cases from surety company files. Several hundred case histories were submitted for this purpose by competing surety companies through the Surety Association of America and the American Insurance Association. From this number these brief examples were extracted to illustrate the various ways both large and small surety companies handle construction bond problems.

Surety Tries to Avoid Contractor Default

The goal of the surety in most of these cases was to avoid default on a bonded job. To the extent that the surety was successful, the existence of the problem may not have become known to the bond obligee, i.e. the owner or governmental body which contracted for the work. The cost of the services contributed by the surety in such cases may not be reflected in the surety's loss figures since no claim or formal default was involved. Nevertheless, these costs are part of the expenses of the surety and these services are part of the value of the contract bond.

Because these contributions of the surety and their concomitant expenses may be outside the "loss ratio" picture they are often unseen. Study commissions, advisory groups and government committees, attempting to measure the value of surety bonds, invariably look to the number of defaults which have occurred on bonded jobs. If the number of defaults is small they infer that the bonds were unnecessary. This inference is unjustified. Success by the surety in avoiding or limiting defaults in no way demonstrates that bonds are unnecessary. Rather, such successes would appear to evidence the value of the bonding process.

4. Cushman, *Bonds on Public Works*, Credit Manual of Commercial Law p. 667 (1973 Edition).

Value of Bonds Not Fully Measured by Loss Dollars Paid

Mistaken conclusions are sometimes drawn from a short range comparison of total dollars paid to sureties for the purchase of bonds with the loss dollars paid by the surety to the owner or governmental body requiring the bond. Many of the cases extracted herein illustrate instances of financial assistance from sureties directly to bonded contractors without any question of formal default and without any notice to the owner. For any one of a number of reasons a surety may choose to provide *immediate* payment of a contractor's obligations to its materialmen, subcontractors or laborers. Such payments are not made to or through the owner nor are they made through the governmental body requiring the bond.

A minimal number of defaults and an absence of owner-contractor litigation indeed suggests that sureties have been successful in screening out incompetent contractors from the bidding process. To the extent inadequately financed or incompetent contractors are allowed to bid, particularly in our "lowest bidder" award system, the number and cost of defaults will increase. Good "loss results" bespeak the value of bonds to the purchasers of them; no inference can be drawn therefrom that their purchase was unnecessary.

Surety Companies Compete for Bond Business

Surety companies are made up of people. It is not surprising then that underwriting philosophies and approaches differ as between companies, or that underwriting results differ from one company to the next. It is these "people" differences that create varying company viewpoints on the desirability of a given type of bond business and which, in combination with the economics of competition and geographic location, make for an open market for contract bonds. No governmental agency could maintain the varietal viewpoints present in the marketplace created by the existence of hundreds of independent, competing surety companies. Despite these different company attitudes the job of the bond underwriter involves certain fundamental considerations.

Qualification of Contractors

The process of evaluating contractors to determine if they can perform a given contract is sometimes called "prequalification." This process is similar to a credit examination made by a bank which attempts to measure the financial ability of the contractor to undertake and complete the job. In screening applicants for bond, however, the surety must go beyond the financial picture and analyze the management and organization of the contractor, his expertise for the kind of work involved, and the equipment and present capacity he has to finish the contract in the required time.

The surety will attempt to verify and evaluate financial data, review other work being performed or to be performed by the contractor and will carefully examine the legal terms and payment provisions of the contract for which bond is sought. Finally, the surety will attempt to determine that the owner has funds available to him sufficient to meet the payment schedule provided in the contract. This process is called "underwriting."

Although prequalification of a potential bidder is but the first step in the surety underwriting process, it is an extremely important one and must be performed by a politically disinterested body. Politically appointed or politically oriented individuals could often find themselves under strong pressures in favor of certain contractors. For this reason the screening of potential bidders in the United States is almost always done by surety companies rather than by governmental bureaus or municipal agencies. The Honorable Herbert J. Stern testified to the dangers inherent in public official involvement in contractor qualification from his experience as United States Attorney for the District of New Jersey. He stated, in part:

> "We have found in our investigations that one of the ways in which competitive bidding is defeated is by the requirement of a prequalification statement. We have found that this has given certain public officials, who do not have the public interest at heart, the ability to disqualify certain businessmen before they even can get their bids in.

"....I'm just talking about a public official in a city or county government saying this or that firm doesn't have enough machinery, doesn't have enough men, doesn't have enough experience. These are all subjective factors. We have found them to be capable of misuse and we would suggest to you that it may be well to consider that, provided a firm can give an adequate surety bond, the legitimate interests of the municipality or the county or the State are guaranteed without the necessity for that kind of subjective judgment."[5]

A Surety is a Pool of Experienced People

The surety underwriter is trained to make disinterested judgments as to "whether or not a man's firm can do the job." Suretyship is a "judgment" business. "Judgment" is subject to error. Losses occur to the surety when it exercises poor underwriting judgment. Losses may also occur when there are drastic financial changes in the economy or unforeseen physical changes in the job site or job conditions which impose extraordinary demands upon the contractor. Usually, it takes an unfortunate combination of such events to bring a viable contracting organization to the point of job failure. For example, the illness or death of key employees or the mental or physical breakdown of a member of the management team may in combination with other factors force a contracting company into potential default. When such circumstances arise the professional expertise of the surety is available, a pool of technical knowledge and practical experience which an individual owner, whether public or private, would not be able to marshal. Given the resources of the surety and the cooperation of the contractor, it is likely that the ultimate loss can be minimized and the job completed on time.

A Good Faith Relationship

Generally, neither owners nor governmental contracting bodies are in a position to make fully objective decisions as to how best to attack a potential default in order to cut down the eventual loss. The "good-faith" confidential relationship which must exist between contractor and surety is difficult if not impossible to achieve between the contractor and an arm of government. To establish a comparable governmental mechanism able to mitigate such losses would require, at the very least, a substantial organization and resulting continuous expense to taxpayers. This "claim" organization would be in addition to the structure necessary to supply and maintain adequate "prequalification" information.

5. Testimony before the New Jersey Local Government Conflicts of Interest and Code of Ethics Study Commission, p. 28-30 (February 21, 1973).

Other Advantages for the Owner

There are indirect advantages which accrue to an owner on bonded work. In many instances lower prices for materials can be obtained, since the suppliers and subcontractors generally give more favorable credit where a job is to be bonded. The efforts of competing surety companies sometimes result in an increase in the number of bidders, thereby increasing potential competition and possibly lowering contract cost. One approach is to initiate a new "partnership" of contractors to perform a particularly large contract. These are called "Joint Ventures." The surety may also provide help to a potential bidder, for example, by arranging for additional capital or bank credit so as to make a local or minority bidder capable of performing larger jobs. The surety will, as a matter of course, keep an eye on the work-program of a bonded contractor, making sure that he does not overextend his total resources. Should the contractor get into difficulties despite this, the surety may be able to arrange for the loan of supervisory personnel, skilled technicians or special equipment from other contractor-clients of the surety.

But Keep the Job Moving

When the surety becomes aware that its contractor is having financial difficulties which may affect his ability to complete, there are several approaches which the surety can use to meet the problem. One of these is to guarantee a line of bank credit for the contractor to enable him to keep the job going. The surety, by giving the bank its guarantee, assures a steady flow of materials to the work site even though the contractor's bank may have previously refused additional unguaranteed credit to the contractor. As a result of such guarantees and of direct payments by sureties, hundreds of millions of dollars are paid out annually to progress bonded jobs, without the assistance of courts, without any formal default process and often without any direct notice to the owner or bond obligee

The confidential nature of the surety relationship is part of the reason why these services are so often "unseen." Another factor is the necessity for keeping the job moving without disquieting the subcontractors, materialmen and the experienced labor force already engaged. Any "break" in the job invites the loss of key workmen and supervisory personnel.

Two Parts to a Contract Bond

Usually a contract bond consists of two separate parts—a "performance" bond and a "payment" bond. The surety, within the terms of its performance bond, guarantees the owner or governmental body reimbursement for any reasonable cost in completing the project when such cost is in excess of the agreed contract price. Thus the owner or governmental body contracting for the work can be more certain of actually having a fixed cost contract.

The second part of the bonding package is the payment bond. This bond is intended to secure payment for those who work on the job or supply materials to it. Laborers and materialmen often have the protection of state Mechanics Lien Laws if the work being done is of a private nature. Where the work being done is for a public building or other public construction, however, the Mechanics Lien Laws usually do not apply. As a result, the payment bond evolved to give financial protection to laborers, subcontractors and suppliers who do work or supply materials on public construction. Today such bonds are used on private as well as public works. Making a claim under a payment bond is less cumbersome and technical than the filing and foreclosing of a statutory Mechanics Lien. Claims under the payment bond are handled and paid directly by surety companies. Seldom are such claimants forced to comply with technical legal requirements.

Financial Protection for Workmen and Suppliers

If for any reason payment bonds were eliminated on public work, some other practical method would have to be found to give laborers, subcontractors and suppliers rights against public bodies adequate to guarantee them payment for their contribution to the work. In such circumstances an extensive federal, state and local administrative bureaucracy would no doubt be required to deal with the substantial problem of unpaid laborers, materialmen and subcontractors. No one bureaucratic department could efficiently deal with the situation where there are defaults by one contractor on several jobs, some public, some private, in different jurisdictions.

Contract bond sureties find that settlements of claims on payment bonds are their largest source of loss. Such claims usually involve unpaid labor and material bills on otherwise completed jobs. Substantial sums, however, are also paid by sureties to laborers and suppliers on jobs still in progress. These may include jobs where the surety has elected to hire a second contractor to complete (the first contractor having defaulted) or where the surety undertakes to finance the original contractor to completion. Sureties vary in their approaches to these problems and solutions must, of course, be responsive to the facts of each situation. Some of the possible fact situations are documented in these cases as is the resourcefulness of sureties in responding to them.

Bonds Help America Build

The surety bond industry is proud of its role in helping both government and private builders meet the demand for new and improved housing, highways, bridges, dams, offices, factories and the numerous other facilities made necessary by America's economic and population expansion. The following cases themselves best illustrate the role of the corporate surety and the value of contract bonds.

The Surety Association of America

Index to Cases

		PAGE NO.
GROUP I Cases 1 to 15	Cases Illustrating Surety Financial Assistance to Avoid Default	15
GROUP II Cases 16 to 30	Cases Showing Engineering, Accounting, Consulting and Other Technical Services Contributed by Surety	21
GROUP III Cases 31 to 45	Cases of Surety Guaranteed Bank Loans to Original Contractor	31
GROUP IV Cases 46 to 60	Cases of Surety Completion Using Original Contractor	41
GROUP V Cases 61 to 75	Cases of Surety Completion Using a Replacement Contractor	49

Group I. Cases Illustrating Surety Financial Assistance to Avoid Default

CASE 1

Financial Assistance and Accounting Expertise— Supervised Performance.

The principal, a boat building corporation, advised the surety of its inability to complete the remaining 30% of its $1,710,000 contract with the Navy to build and deliver 55 56′ landing craft. Further, the surety was informed the contractor had just been awarded a $1,500,000 unbonded, high priority Navy contract to build and deliver, within thirteen weeks, 22 24′ light craft. The contractor was originally designated a "sole source" for such boats.

To avoid cessation of bonded work, the surety advanced $150,000 and supervised performance of both jobs. Although the surety eventually was reimbursed 100%, except for loss expense of $16,000, its financial assistance and accounting expertise were directly responsible for (1) completion on schedule of the bonded job, (2) the performance and completion on schedule of an unbonded high priority defense contract, (3) the prevention of additional loss and time to the Navy, which necessarily would have flowed from the principal's collapse, and (4) rehabilitation of a major boat building organization. At no time was the Navy aware of the extent of the surety's involvement or of the direct and indirect benefits to the Navy resulting from this involvement.

CASE 2

Surety Finances Completion of Road Building Contract Where Contractor Takes a "Flyer".

Contract price $2,500,000 for the construction of seven miles of state road. During the course of construction principal experienced unusual problems in rock excavation which increased its cost and depleted working capital. In addition the president of the corporation organized a subsidiary to teach flying. This venture was unsuccessful and was a further drain on corporate

assets and diverted the president's attention from his chief responsibility of road building. The job was 88% complete and it was necessary for the surety to take over and finance the job to completion requiring expenditures in excess of $800,000.

CASE 3

Surety Saves Contractor Building Bridge with Exploding Pilings.

This claim involves a $12,500,000 bridge contract in which inflation absorbed the contractor's anticipated profit, thus causing the job to cost more than the bid price.

At a time when the job was 95% complete, the pilings began to explode and the State Highway Department withheld further funds to the contractor that included a large earned estimate.

The surety became involved and made funds available to the contractor, under proper supervision, which enabled the job to be completed and payment made to all materialmen and subcontractors. The outlay of the surety was $1,300,000. The surety also made arrangements to have a proper analysis made to determine the cause of the exploding pilings, so corrective work could be performed.

This is a case in which the surety saw to it that a financially ailing contractor had proper financing rather than having the owner declare default. This aid, in the long run, saved the contractor from bankruptcy, caused completion of the bridge promptly for public use, saved the contract from being relet, and provided overdue payments to many subcontractors who were on the verge of bankruptcy themselves.

CASE 4

Surety Invests Large Sums to Prevent Default.

When contractor's bank refused to renew annual line of credit and demanded payment of equipment notes it became necessary for the surety to arrange financing to prevent default on four uncompleted jobs with original contract price of $26,500,000 and to absorb payment obligations in excess of $2,200,000 on the uncompleted projects and nine completed projects. This type financing has required an outlay in excess of $8,000,000 with a current pre-liquidation loss of approximately $6,000,000.

CASE 5

Seven Building Contracts Completed with Surety's Assistance.

Contractor became financially unable to complete seven building contracts including schools, hospital additions and small airport terminal building totaling $1,900,000. Surety arranged a revolving trust account funded by claim drafts, exercising administrative joint control over a total of $1,000,000 to pay for completion of work and payment of labor and material suppliers, subcontractors, etc. Surety's loss was $175,000. Jobs were completed on time without additional cost to the owner.

CASE 6

Co-Sureties Make $3,000,000 Loan to Contractor to Complete Project.

Contractor engaged in performance of $6,200,000 contract for construction of water tunnel became insolvent because of extra costs. Co-sureties on performance bond loaned contractor more than $3,000,000. Project completed, no default.

CASE 7

Surety Advanced $9,000,000 Over Time it Took Contractor to Work Out of Difficulties on 17 Jobs.

Contractor was short of funds and unable to continue performance of seventeen jobs which were underway at the time. Contract amounts totaled approximately $50,000,000. He appealed to surety for assistance. Surety advanced monies directly to the contractor, thus avoiding defaults on all seventeen jobs.

All jobs were completed by contractor and unpaid bills satisfied. Surety pumped in close to $9,000,000. Approximate surety loss $700,000.

CASE 8

Surety Works Out Orderly Completion.

Contractor became financially unable to complete his work and pay his obligations on 6 sewer and water line contracts totaling $1,000,000 including 2 contracts with municipality and 3 subcontracts. Surety established a revolving line of credit funded by claim drafts and made many direct payments to subs and suppliers to enable completion and payment of obligations on bonded contracts in an orderly and timely manner. All work was completed satisfactorily. Loss to the surety was $270,000.

CASE 9

Surety Provides Financial Assistance to Plumbing & Heating Contractor.

Contractor called upon surety for financial assistance when unable to make payments to laborers and materialmen totaling over $800,000. At the time surety agreed to arrange financial assistance the contractor had completed seven jobs totaling $1,800,000 and had 4 jobs to complete totaling $1,700,000. With the help of the surety all jobs were completed and all bills paid. Financial assistance to the extent of $125,000 was necessary to accomplish the foregoing.

CASE 10

Surety Advances More Than a Million Dollars to Effect Completion.

Contractor had 13 jobs for various city and county governments. Contracts totaled $7,000,000. Contractor required financial assistance from surety to pay labor and material bills and to complete work. Surety furnished the necessary financial assistance by special trust account. The surety had to advance $1,100,000 to effect completion of work and payment of labor and material bills.

CASE 11

Surety Financing of Some $3,000,000 Enables Completion of Public Housing.

Contractor unable to complete several public housing projects and pay bills on others. Surety promptly financed to avoid defaults, putting about $3,000,000 into seventeen different projects. Eventual loss to surety will probably exceed $2,000,000.

CASE 12

Co-Sureties Financed Contractor to Completion.

American contractor took $18,500,000 contract to build dock facilities, breakwater, deepen harbor project in the Bahamas. The contractor ran out of funds and was about to default. Co-sureties on bond financed contractor and project completed with final loss to sureties approximately $5,000,000.

CASE 13

Surety Makes Cash Advances to Further Completion.

Contractor specialized in the design and installation of technical equipment for military bases throughout the Western Hemisphere. Firm became involved in severe financial problems and was on the verge of total collapse when the surety stepped in, advancing money for payment of outstanding claims, and making further advances to meet heavy payroll and operating charges. Total advances aggregated over $375,000 but the surety was successful in keeping the work proceeding without interruption and with no defaults on any of the jobs in this far-flung operation. Here again, it is quite likely that government officials never knew of the difficulties besetting its contractor, all because of the surety's prompt attention in providing funds and arranging for the completion of the contracts.

CASE 14

Surety Assists in Completion of School Contracts.

Contractor became financially unable to complete two school contracts totaling $800.000. Surety established a revolving trust account funded by claim drafts and exercised administrative joint control over the receipt and expenditures of $410,000 to pay for completion costs, labor and material and subcontractors, etc. There was no loss of momentum and jobs were completed on a timely basis. Loss to surety was $195,000.

CASE 15

Surety Financed Contractor in Order to Complete Work.

Contractor was misled on the financial affairs of his company by Public Accountant whom he employed. There was no question about his ability to perform. The financial figures submitted by the Public Accountant were erroneous. The contractor ran out of money. Six jobs were underway at the time, all in medium to high six figure amounts. Surety financed contractor enabling him to complete work and pay all bills. Surety's loss covering labor and material bills totaled approximately $700.000.

Group II. Cases Showing Engineering, Accounting, Consulting and Other Technical Services Contributed by Surety Often in Conjunction with Financial Assistance

CASE 16

Engineering and Financial Review—Interim Financing—Completion W/O Default. Surety Took Control—Advanced Large Sums.

Just into the second construction season for this project, which involved a contract in the amount of $8,600,000, the contractor revealed a very dire financial plight. In fact, the corporation was close to financial collapse, with current payables in excess of $500,000 and total payables, including other projects, in excess of $1,000,000. Interim financing was provided to buy time necessary for extensive engineering and financial review and analysis. The conclusion was to finance the project to completion. The alternative would have involved a default and termination by the public body, with consequent shutdown and delay to permit re-bidding, etc.

The surety took control of the project, managed the corporation and advanced huge sums, approaching $3,000.000. Field engineering and consulting service was provided for almost three years. The project was completed with no delay or interruption of the work and without the intervention or additional cost to the public body. The only apparent change imposed was a different mailing address for the earned estimate checks.

The surety's final loss on this contract reached nearly $1,000,000.

CASE 17

Surety Arranged Loan of an Experienced Project Manager.

Contractor undertook to construct a multi-level parking structure. The contractor encountered technical difficulties with which he had not had previous experience, and the project was falling seriously behind schedule. When the surety became aware of the problems, it arranged with another of its contractor clients for a project manager experienced in that type of work to be loaned to the contractor for the duration of the project. As a result the project was satisfactorily completed without default of the original contractor.

CASE 18

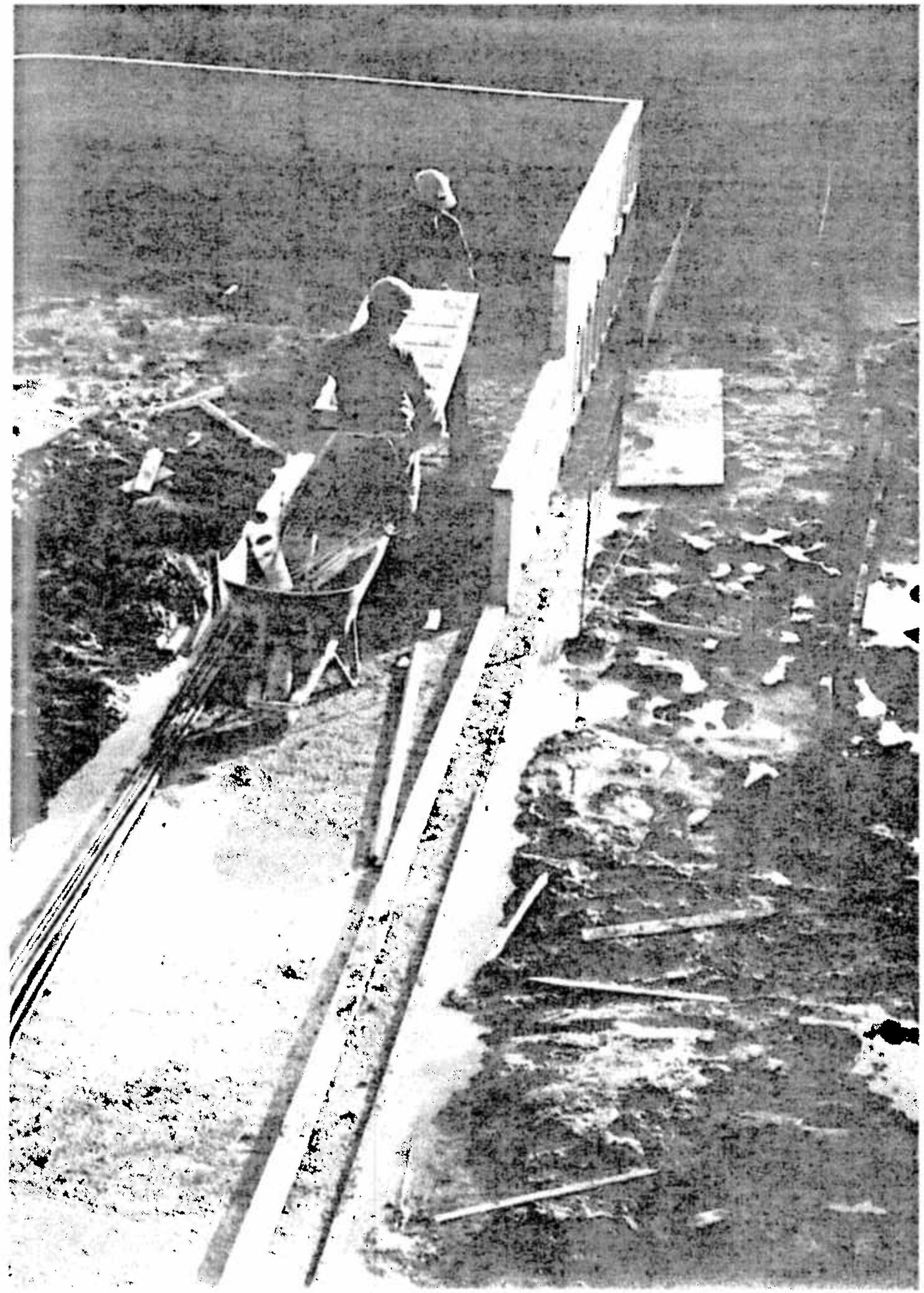
Construction Engineer and Project Superintendent Employed—Surety Advanced Money—Contracts Completed.

Following notice of default by the obligee involving the construction of a public school, the surety assumed control of the operations of the contractor. This was one of six contracts in various stages of completion.

The contracts involved federal and public work and are taken as a group. as a default on any project would have precipitated the collapse of the contractor. The most significant project involved the completion of a junior high school to accommodate 1,700 students at the Fall term.

An engineering and accounting survey developed that the contractor's cash flow was inadequate and that an infusion of approximately $500,000 would be needed to prosecute the contracts to an orderly and timely completion. The surety's remedial action included the employment of a construction engineer and project superintendent. They were successful in reenergizing the projects by their day-to-day supervision of the work under progress.

Absent financial assistance from the surety, bankruptcy would have resulted and a reletting of all projects would have been required. This would have caused a severe problem on the junior high school project and would have necessitated the school officials to enter into a program of double sessions, which was averted by the surety's timely intervention. With the exception of the town officials, the other obligees were unaware of the contractor's financial plight and an orderly completion of all contracts and a prompt disposition of subcontractor and supplier accounts were effected.



CASE 19

Substantial Cash, Outside Engineering—Assistance with Computer Operation.

A large, well established and well known contracting firm had a work program of approximately $90,000,000 in various stages of completion. Difficulties were encountered on one of its major projects resulting from unrecognized soil conditions which involved substantial additional work. The surety was called into the picture when advised that the contractor was in severe financial straits as the Federal Government refused to recognize the validity of the additional work involved nor was it willing to finance. The surety initially advanced $3,000,000 within a three month period to pay job creditors numbering in excess of 650. Outside engineering expertise provided by the surety together with the improvement of a computer system to facilitate creditor payments enabled the contractor to complete the contract and avoid threatening bankruptcy. The unrecovered loss to the surety at this point is approximately $8,000,000.

CASE 20

Surety Assists Contractor Toward Goal of Better Job Management.

Contractor became financially unable to complete 14 school and college buildings and sewage treatment plant contracts totaling $22,800,000. Surety arranged a revolving line of credit funded by a maximum guaranteed loan of $1,500,000 and exercised administrative joint control over several million dollars flowing through the account for payment of completion costs, labor and material suppliers and subcontractors. Surety was also instrumental in replacing the general superintendent for better job management. Momentum was maintained and improved and all work was completed in a timely manner. Surety's loss was $1,100,000 of which $300,000 has been recovered over a period of 4 years.

CASE 21

Surety Satisfied Creditor Indebtedness—Helps Revamp Accounting and Estimating Procedures.

An old line, highly regarded construction firm embarked on an equity building program and within a comparatively short period of time experienced a severe cash flow shortage. At that point a $53,000,000 work load was underway at various locations along the entire eastern seaboard. The contractor was unable to meet payroll and unpaid creditors threatened bankruptcy. Prompt action on the part of the surety in satisfying $4,800,000 of creditor indebtedness enabled the contractor to continue in business. The surety in cooperation with the principal completely revamped accounting and estimating procedures and established a claim section to process disputed contractual items and provided aid to the principal in prosecuting Federal tax claims. At the present time the surety has expended approximately $4,000,000 on this account.

CASE 22

Surety Hires Contract Consultant Where Active Owner of Contracting Firm Suffers Heart Attack.

Contract price $145,000. In the early stages of the job contractor became aware of the need for financial assistance due primarily to errors in his original bid resulting in a losing job. While advances were being made to him on labor and material obligations principal owner suffered a heart attack resulting in his assuming an inactive status. It was necessary for surety to engage a contract consultant to review the job records and proceed with completion of the work and payment of all labor and material bills. As a result of surety's efforts, contract was completed and accepted without defaulting the contractor.

CASE 23

Surety Provides Consultant and Financial Help to Corporate Contractor Threatened by Accidental Death of its President and Vice President.

The president and vice president of a highway contractor were killed in an air crash. Outside management was brought in by the heirs but within a short time the formerly highly successful operation was at a point where they had 21 contracts totaling $32,000,000 on which there remained over $8,000,000 of work to do, and they owed $2,280,000 to subs and suppliers and had no cash. Other area highway contractors estimated it would cost at least $11,000,000 to complete the $8,000,000 of work. The surety brought in two recently retired successful highway contractors, who after investigation believed the contractor had a good organization which needed proper direction and accounting. Under their direction their equipment repair plant which was costing the contractor $1,000,000 a year was discontinued and liquidated in an orderly manner and cost accounting methods set up. Additional unbonded work was taken on with resulting $500,000 bills paid. The surety ended up with a $2,000,000 loss.

CASE 24

Cash. Engineering and Accounting Assistance.

A very prominent bridge building contractor attempted to expand his operations into highway work. Technical problems developed with which he was not sufficiently experienced and the first notification of trouble to the surety was that on a total work program of $4,500.000 the unpaid bills amounted to $1,800,000. All available cash had been funneled into the difficult highway project to maintain completion schedule because of severe liquidated damage penalty. The surety promptly satisfied unpaid bills and rendered accounting, record keeping and engineering assistance preventing formal default as well as serious delays. The surety continued to render assistance to the contractor over a three year period with the result he was able to rehabilitate himself and the contractor is presently carrying a work program in excess of $15,000,000.

CASE 25

Large Sewer, Water and Tunneling Contractor Survives With Surety's Assistance.

Contractor has completed projects in excess of $10,000,000 and has had aggregate work loads in excess of $20,000.000. The contractor advised surety that he could no longer obtain bank credit and would have to cease operations if he could not obtain at least an additional $1.000,000 in working capital. The circumstances that led to his problem were:

1. Contractor had bid between 500 and 600 jobs in a two-year period. Two projects which aggregated $9.000,000 had been obtained about two months prior to the time his problem came to a head. Both new projects involved unusually high start-up costs.

2. Labor problems on work in one state had created two years of substantial loss.

3. Retainages aggregating in excess of $500.000 had been tied up in litigation for a period of two years and a recently completed job, where approximately $800.000 in retainage was expected. developed a strong possibility that another suit would arise. This resulted in over $1,300,000 in retainage being frozen for an indefinite period of time.

Surety proceeded as follows:

1. An analysis of the bids on the $9,000,000 of work which was just getting started.

2. A thorough investigation and an appraisal of the litigation involving retainages.

3. A complete appraisal of the contractor's equipment position. Certain equipment was designated to be sold for retirement of bank loans.

4. A thorough investigation and an appraisal of the contractor's organization from field supervision level through top management.

5. A cash flow projection for a period that anticipated completion of all work on hand.

6. An agreement with the banks as to past and future payments on the principal due on loans which they had made on equipment.

7. Arrangements to provide the contractor with bank credit for additional working capital up to $1,350,000. The amount of the bank line used by the contractor was $955,000.

Surety succeeded in keeping the assistance to this contractor completely quiet so that the contractor's reputation and standing in the industry was not damaged. Over 400 materialmen and subs were paid and pay checks for approximately 75 employees were continued without them knowing of the surety's involvement. The contracts progressed, without disruption for the owners and engineers, who were not aware that the surety was involved.

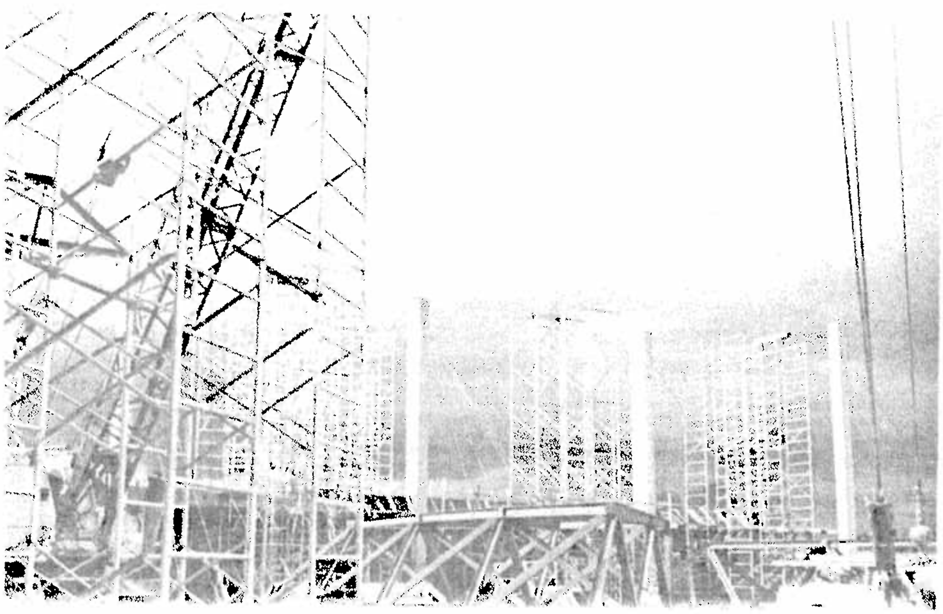
Surety's assistance was terminated three months ahead of the date that had been projected, even though the retainages which were frozen remained frozen.

CASE 26

Surety Contributed Technical Support and Bank Credit to Help Contractor Meet Government Deadline.

Just two years ago this big grading construction firm was trying to complete a large railroad relocation project. Because of commitments made by the federal government to deliver the project on a given date demands were made on the contractor to accelerate his performance. Such acceleration, while it may or may not have been properly ordered, nevertheless forced the contractor into extra high costs and soon ran him out of funds.

The surety elected to assist the contractor to meet the government's demands, and proceeded to engage experts to assist in locating additional equipment and additional technical labor and also provide bank credit, plus clearing up outstanding bills to avoid default and keep the job going. Fortunately, the combined efforts of surety and principal accomplished completion just short of the government's deadline. The job was delivered on time as per plans and specifications.



CASE 27

Help to Meet Payroll—Engineering Consulting Firm—Legal Aid Furnished.

A prominent contractor had a work program of approximately $12,500,000 underway covering projects as diverse as power plants, school buildings, shopping centers and housing projects when the surety was advised that the contractor was unable to meet the weekly payroll. Unpaid bills in excess of $1,000,000 were promptly satisfied and a consulting engineering firm hired to assist the contractor in completion of the work. While the ultimate loss is not determinable at this time, expenditures to date on the part of the surety exceed $1,700,000.

CASE 28

President of Contractor Firm's Death Results in Minimal Delay in Current Jobs.

Contractor awarded a $180,000 contract in May and three more in August, for $160,000, $160,000 and $180,000. All contracts were with the same owner. A supplier's claim for $73,000 was received by the surety which immediately scheduled a meeting with the contractor and supplier. However. before the meeting took place, the president of the contracting firm died. Another meeting was scheduled with the supplier claimant and for the surety to appraise the capability of new officers of the contractor. Within three weeks, settlement details for the claim were worked out and the claim taken care of by surety. The surety was convinced of the capability of new management and gave its support. All jobs were completed without the delay which would have been caused by the obtaining of a new contractor.

CASE 29

Surety Arranges a Joint Venture to Provide Bonds.

$4,000,000 HUD-backed apartment complex had fallen through because contractor could not furnish required bonds by closing date. Surety worked this out by having a joint venture formed with electrical contractor who had general construction experience, bonding all subs, and establishment of going-in $200,000 joint venture bank account.

CASE 30

Surety Keeps Small Painter in Business Through Silent Joint Venture.

Small painter in $20,000 job bracket had run out of work and would have to lay off force. Surety knew of $130,000 contract for painting several bridges and put together small painter in silent joint venture with larger contractor. Job was profitable and small painter kept force and went on to bigger jobs.

Group III. Cases of Surety Guaranteed Bank Loans To Original Contractor

CASE 31

$2,000,000 Revolving Loan by Surety—Co-Sureties Monitored Performance—No Default or Disruption of Contract.

This contract, in the amount of $24,000,000 is one of a series awarded by a city in a massive effort at pollution control. Principal was a joint venture of three contractors, two of which are large, experienced firms with tunnel background. As work progressed, numerous unforeseen difficulties and conditions were encountered, with a very significant increase in cost per lineal foot. The joint venture operating fund was exhausted, after which each joint venturer contributed corporate assets, all of which were inadequate to carry the project.

The co-sureties made a careful analysis of the project, using an internationally known tunnel expert to establish probable cost. Also, the financial position of each joint venturer was evaluated and the ability of each to contribute talent and manpower. The joint venture requested financial assistance, so as to be able to complete, a position which, after evaluation, was considered sound.

As a result, a $2,000,000 revolving loan was established, underwritten by a guarantee of payment by the co-sureties. Adequately financed, the project continued with no interruption or slowdown of work, no change in the method of payment of estimates, and today is 95% completed. The co-sureties have continued to monitor performance of the work, which will finish satisfactorily.

The public body was not required to issue a termination notice or even threaten this event. To all outward appearances, the contract was performed without difficulty and at no time was intervention by the city necessary.

CASE 32

Surety Drops a Bundle Working Out Complicated Completion.

Contractor was a corporation whose stock was publicly owned. At the time surety found out about the contractor's financial difficulties there was an agreement with another contractor, also publicly owned, for an exchange of stock so that one contractor would become a subsidiary of the other contractor. The other contractor was also in the hands of its surety with a substantial guaranteed loan outstanding. Our contractor had six jobs bonded by surety underway with the value of incomplete work totaling approximately $15,000,000. It had other jobs bonded by other companies underway. There were substantial unpaid bills outstanding on all jobs. All of the bonded jobs were multi-million dollar contracts —one was with a school district for the construction of a high school; two were with the state for the construction of a public park in the heart of a metropolitan area and the construction of an athletic practice field for a large metropolitan university; one was with another school district for the construction of several buildings to be used for a junior college; and, the other two were with the United States for the construction of a multi-storied data processing center for NASA and for the construction of a multi-storied office building for the Department of Interior, Bureau of Reclamation. These projects were located in various parts of the country.

After difficulties with the management of principal corporation and the management of the new owner of principal corporation, arrangements were made to joint control contract money and ultimately to finance the construction of the jobs by guaranteed loans. The dispute with the principal and principal's owner did not materially affect the jobs and did not involve the owners. Surety lost approximately $1,750,000 in assisting the contractor financially in the performance of the jobs with minimum inconvenience to owners and approximately on time.

CASE 33

Surety Guaranteed $3,000,000 Bank Loan—Assisted in Procuring Engineering Experts.

The surety wrote separate contract bonds for two independent contractors and for contracts they undertook on a joint venture basis. At the time the surety claim division became involved there were six contracts in various stages of completion. The aggregate of contract prices of those contracts totaled $39,000,000. The total cost to complete all contracts, meet overhead and pay sub-contractors and materialmen on these and completed contracts totaled $8,600,000. Of that amount $2,500,000 represented unpaid creditors. The surety arranged for a guaranteed bank loan of $3,000,000 to the contractors. The contracts took longer to complete than originally expected for reasons not necessarily the fault of the contractors. The surety elected to pay the bank loan and incurred total losses of approximately $5,000,000. However, the contracts were all completed by the contractors without default. The surety assisted in the selection of, and financed the cost of, engineering experts to resolve numerous technical problems encountered by the contractors.

CASE 34

Surety Contributes $1,500,000 Plus to Enable Municipal Work to Be Finished Without Delay.

Contractor became financially unable to complete his work and pay his obligations on four contracts totaling $4,300,000 including a Flood Control District storm drain, a sanitary sewer gravity flow trunk line system and treatment plant for a county, a by-pass sewer for a Water District and a Municipal Water District arterial system and feeder lines. Surety arranged a revolving line of credit funded by a guaranteed bank loan maximum of $750,000 and claim draft deposits. Surety exercised administrative joint control over receipt and disbursement of approximately $2,000,000 to pay costs to complete, sub-contractors and labor and material suppliers. In addition, surety furnished consulting services and extremely critical weather data which were instrumental in changing construction methods on the trunk line sewer job to complete on time and in a satisfactory manner. Loss to surety was $1,600,000. Some minor recovery is anticipated.

CASE 35

Surety Assisted in Rehabilitation Program— Bank Guarantees.

An old established contracting operation considered to be one of the outstanding construction firms in the country gradually deteriorated to a critical point where it was faced with $7,000,000 in past due bills and a minimal working capital position at a time when it had a total uncompleted work program of $270,000,000 of which $70,000,000 was bonded. The contractor's bank placed a moratorium on existing debt and granted additional credit secured by the surety's guarantee and other collateral. The total of such indebtedness amounted to $22,000,000. With the cooperation of the bank a rehabilitation program was undertaken involving payment of bills, preservation of assets, prosecution of claims and improved management. All work was completed and payment of bills placed on a current basis. Release of contract funds was expedited by the surety's assurances to contract owners. The surety's out-of-pocket loss totaled $12.500,000 although there are prospects for some further recovery.

CASE 36

Business of Road Builder Going on as Usual— With Several Million Dollars of Loss to Surety.

A large southern road building and earth moving contractor reported his inability to finance his winter shutdown, pay his bills and mobilize his costs in the spring. Surety found over $15,000,000 in contract funds to be potentially earned on projects in three southern states and in excess of $500,000 to be earned on a dam construction project. All were public work. Unpaid bills totaled nearly $2,000,000. All projects were equipped with machinery valued at approximately $8,000,000 and carrying encumbrances of $6,500,000.

Surety determined that, if the contractor were allowed to default, bankruptcy would be likely. Due to the difficulties in locating new contractors, completion dates would be delayed on several projects. Surety arranged for a multi-million dollar bank loan, guaranteed by it. The contractor has brought his bills and equipment payments current. All work is being prosecuted by the contractor. None of the owners have been notified of any difficulty,

except for notification that contract balances have been assigned to the financing bank. Subcontractors and material suppliers continue to deal directly with the contractor and to receive payments from him. To outside parties, it appears to be "business as usual", and yet the surety expects an ultimate loss of several million dollars.

CASE 37

Surety Advances Interest Free Monies to Keep Large General Contractor in Business.

A large General Contractor came into his surety's head office at a time when he had twelve uncompleted public jobs totaling over $66,000,000 about 70% completed. He was out of money and could borrow none from banks to whom he already owed over $3,000,000. He owed $1,000,000 on past due bills to suppliers and subcontractors. The surety arranged for a $1,000,000 bank credit, repayment guaranteed by the surety to enable the contractor to continue.

As the work continued it was necessary for the surety to advance additional monies in excess of a $1,000,000 all while the $1,000,000 guaranteed bank loan remained outstanding. The surety also continued to provide suretyship for new jobs. The contractor's difficulties arose from inadequate financing in outside building projects. The surety provided him counseling and help in these areas resulting in his recovering his investment. All jobs were completed and all creditors paid and last year the bank loans, including the one guaranteed by the surety were paid off. The contractor is in good financial condition and still in business and obtaining new bonds from the surety.

CASE 38

Sureties Bailed Out Contractor Who Ran into Difficulties Not of His Own Making.

Contractor entered into a $7,000,000 contract with the United States Corps of Engineers to construct a port facility for another nation under U. S. foreign aid. The work required the contractor to excavate rock from a specified area, construct a pier and protective area using this rock. In addition, contractor was required to dredge a channel and create a harbor.

Contractor discovered that the area specified by the contract failed to contain the specified rock in sufficient quantities to perform the contract. Contractor was directed to seek the specified rock in several other areas more distant from his base of operations. This proved to be a costly and fruitless search. The government then changed its specifications and agreed to accept rock of less density and weight. However, this increased contractor's cost so substantially that he exhausted all of his working capital and bank credit. On the verge of default, the contractor sought financial assistance from his co-sureties.

The co-sureties arranged a guaranteed line of credit for contractor. The contractor was able to borrow in excess of $5,000,000 with the co-sureties' guarantee and completed the contract to the satisfaction of the government. Co-sureties paid off loans. The total cost of performance exceeded $14,000,000. With continued bonding and new profitable work the contractor was able to survive and continue in business.

CASE 39

Surety Arranged and Guaranteed Bank Credit, Paid Job Bills—No Default.

A very substantial contract operation engaged in heavy construction work including dams, highways, etc. found itself in an impossibly tight cash position at a time when as a sole venturer it was engaged in 28 such projects amounting to $210,000,000 including domestic and foreign contracts. When confronted with this emergency, the surety promptly arranged for sufficient bank credit guaranteed by the surety. In stages the bank loan ultimately amounted to $11,000,000 and in addition the surety expended from its own funds something in excess of $11,000,000 in payment of job bills. There was *no default* in performance and the entire work program was completed substantially on schedule by the original bonded contractor.

CASE 40

Employee Embezzlement Threatens Federal Contracts of $12,000,000.

This Contractor had a workload of over $12,000,000 but because of a large embezzlement by an employee of the organization the firm found itself in a distressed working capital position. Bank credit not only stopped but the loans were called and the principal was faced with having to default on ten large federal contracts in various stages of completion.

Under its bonds the surety paid outstanding bills, assisted the contractor with guaranteed bank loans, and thus avoided default on all jobs. Surety actually paid $2,500,000 of its own money in this operation, with the result that work progress never stopped but went forward without delay to the federal government. Some of these contracts were Space Agency projects and others were military contracts, all of which were deemed to be urgently needed by the government agencies involved. It is quite possible that the federal contracting officers never knew of the problems of this contractor nor of the investment and support of the surety.

CASE 41

Surety Guaranteed Bank Loans.

Surety wrote several bonds for a contractor which found itself in a tight financial situation on two of its contracts totaling over $10,000,000. One problem grew out of complications which developed in the Federal missile program and the other grew out of encountering more rock than had been anticipated on a highway project in the California mountains. Surety guaranteed bank loans in excess of $1,200,000 which made available sufficient funds for work to continue with no interruption.

CASE 42

Surety Assists Financially Drained Contractor to Finish 20 of 21 Jobs Without Default.

A major prime contractor informed its surety it was financially unable to complete its contracts. At this time, it had 21 open jobs totaling approximately $24,700,000 in bonded obligations, for U. S. Government, State, and private work.

Reason for financial problem was laid to the contractor's recent acquisition of a mechanical subcontractor. The financial demands of the sub and the inability of the contractor to exercise knowledgeable control of the sub's operation drained the contractor of needed performance dollars.

Analysis of jobs and companies was undertaken and a guaranteed bank loan of $800,000 was arranged. Due to heavy cash flow requirements an additional $950,000 in cash advances was necessary.

There remain presently six jobs open and nearing completion. Due to the surety's financial assistance no job interruption was experienced. All jobs will be completed on time except one.

CASE 43

Contractor with 13 Jobs Open Finds Luck is Bad.

Contractor was financially unable to complete his work and pay his obligations on 13 contracts totaling $4,000,000 including two contracts with General Services Administration for construction of an addition to U. S. Court House and the extension and modernization of a Post Office; four State Public Works Contracts for construction of two high schools, a college building and a reformatory; and six private works contracts for additions to a hospital, two Catholic Schools, an office building and two store buildings. Surety arranged for a revolving line of credit funded by a guaranteed loan maximum of $650,000 and claim drafts; and exercised administrative joint control of receipts and disbursements of $3.250.000 to pay completion costs, sub-contractors and labor and material suppliers. All work was completed in a satisfactory and timely manner. Loss to surety was $800,000 with approximately $60,000 salvage recovery received to date.

CASE 44

Surety Completes, Pays Subcontractors and Labor and Material Suppliers.

Contractor became financially unable to complete his contracts and pay his bills on seven interstate highway contracts totalling $27,000,000. Surety established a revolving line of credit funded by a guaranteed bank loan maximum of $2,500,000 and exercised administered joint control over receipt and disbursements of $8,000,000 for payment of completion costs, subcontractors and labor and material suppliers, etc. Momentum was maintained from date surety became involved. However, the job was already 253 days behind schedule at that time. Surety's loss is estimated to be $1,500,000.

CASE 45

Surety Arranged Guaranteed Loan for Contractor in Trouble Caused by Shopping Center Owner's Insolvency.

Contractor, a general builder, suffered serious losses on non-bonded contracts when the owners of the shopping centers under construction became insolvent. This impaired contractor's working capital and bank credit so drastically that he was on the verge of defaulting several bonded contracts with State agencies

The contractor brought his problems to his surety. The surety arranged a $600,000 guaranteed loan for contractor through his bank, which surety later paid. Contractor went on to complete all of his work without incident and the State agencies never became fully aware of contractor's financial dilemma.

Through good management, resourcefulness and new profitable work, the contractor was able to recover from his financial problems, pay off all his creditors, and remain in business.

Group IV. Cases of Surety Completion Using Original Contractor

CASE 46

Surety Advances $3 Million Plus to Complete Wide-Ranging Highway Projects.

The contractor, engaged in road construction in a three state area, incurred heavy operating losses and could not continue to operate without financial assistance.

Five road construction projects totaled nearly $8,000,000. A related company was engaged in seven road improvement contracts for a total contract price of about $1,400,000. The projects were in various stages of completion when the contractor called on his surety for financial assistance.

The contractor had borrowed heavily from his bank and they were not willing to grant any further credit. Surety company made an investigation of the contractor's financial situation and initially it did not appear to be a case where the contractor could be furnished with funds for the completion of the bonded contracts because of nearly $1,000,000 in due and past due, non-bonded obligations. Various programs were arranged so that this non-bonded debt could be reduced and a financing program was arranged by the surety. Funds were furnished and bonded job obligations were quickly brought up to date. Prior to the involvement of the surety, job progress had slowed; however, with the program outlined by the surety the jobs began to progress at a much more satisfactory rate. The financing program called for the immediate advancement of about $1,000,000.

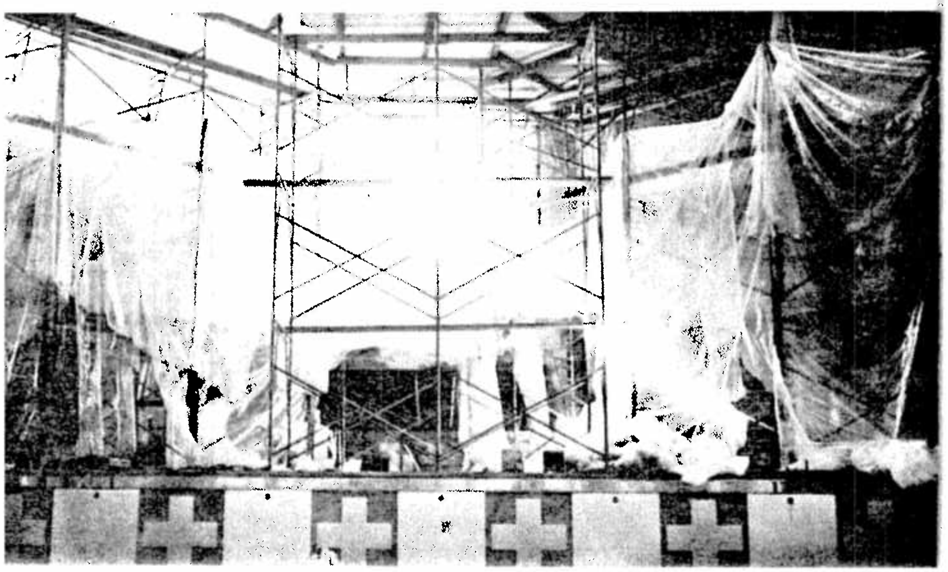
The program continued in a satisfactory manner for several months when, due to pressures from creditors not connected with bonded projects, the contractor was forced into bankruptcy under the provisions of Chapter 11. The surety and the contractor met with the referee in bankruptcy and orders were signed which allowed the program to continue with the surety advancing the funds necessary for completion of the projects.

All of the projects have now been completed and net surety advances to the contractor exceed $3,300,000. Retainage has not been collected on two jobs and the net loss figure to the surety may be further reduced by future salvage recoveries.

CASE 47

Surety Completed in Contractor's Name.

This involved nine contracts for water or sewer lines and treatment plants, contract prices totaling $4,385,000. Principal became insolvent with over $1,000,000 of uncompleted work. It was estimated that at least $1,500,000 would be needed over and above progress payments to complete work and pay all outstanding bills. Causes of the difficulty were underbidding, over-extension and unforeseen site conditions. Surety took over principal's work force and completed in his name. All work was completed on time and the matter entirely acceptable to the obligee. Net loss and expense will exceed $950,000.



CASE 48

Surety Completed so as Not to Delay Other Contracts.

Surety learned contractor was in trouble on job with a city involving approximately $2,500,000. This resulted from bad bid and inability to hold an organization together. In order to keep work covered by the bond moving and in order to avoid delay to five other contracts which were involved, surety took over completion, advanced funds of over $1,300,000 covering work yet to be done and paid bills of almost $500,000.

CASE 49

Surety Financing Necessary to Long Term Contract.

Bond covered the construction of a hurricane barrier to provide protection against hurricane and tidal flooding to the commercial and industrial center of one of the larger cities which had sustained losses in excess of $80,000,000 over the past several decades.

The surety was obliged to render financial assistance to the contractor, as a deficit under the contract was projected at $3,500,000. This acute financial condition was brought about by delays in completion as a result of modifications to the contract, as well as a delay in receiving equipment necessary to the performance of the contract. Further, an expanded work program, without adequate planning and sufficient long-term financing, and excessive overhead expense were several other factors which brought about the contractor's difficulties.

As it was determined that the contractor had the capacity to complete the project, both as to quality of work and competence of the entire operation, the acquisition of additional financing and continued support of the surety were essential; otherwise, a default requiring a relet would have created horrendous delays in completion and would have subjected the area to exposure from the elements in the event of a catastrophic storm. Therefore, the contractor continued, and the project became operational and was completed at an excess cost to the contractor of $3,200,000.

The contractor's expertise in construction, particularly in the area of highway and bridge construction, was a decided factor for the surety's decision to continue to render financial assistance continuing over a ten year period during which period the contractor performed federal, state and municipal contracts worth in excess of $120,000,000.

Rehabilitation of the contractor by the surety has been successfully concluded. Prompt intervention by the surety and the rendering of financial assistance not only prevented a serious default but saved the federal and state governments substantial sums, in that it maintained a competitive atmosphere in the state and contributed to its economic condition.

CASE 50

Surety Completed Job Using Principal's Labor Force.

A general contractor filed bankruptcy. Surety bonded five uncompleted state college jobs totaling $7,000,000 on which there remained $4,500,000 yet to be earned, and progress was far behind schedule. It owed $600,000 to its subs and suppliers on these jobs. No other general contractors would take over completion on a fixed price basis. To avoid delay and correct progress the surety engaged a construction consultant to complete with principal's labor forces and the original subcontractors. All jobs were completed within a time satisfactory to the public body. The loss to the surety was over $2,000,000.

CASE 51

Surety Helped Finance Bankrupt Contractor to Complete Jobs.

A contractor engaged in performing several projects, including two missile sites, two bridges and several other projects, became bankrupt, filed petition for corporate reorganization and was about to default on performance of contracts. Surety arranged for completion of the projects by bankrupt contractor and guaranteed $2,500,000 of additional financing. All projects completed.

CASE 52

Financial Information Supplied to Contractor by Public Accountant Caused Him to Go Bust.

Contractor had fifteen jobs underway involving Post Office, Air Force Dining Hall, Courthouse, Libraries, College Buildings, etc. when he became aware that the financial information being supplied by his Public Accountant was not reliable. Instead of his work being profitable as indicated by the Public Accountant, he was actually producing losses. Before anything could be done to remedy the situation the financial condition had deteriorated to a point where all agreed that the surety should step into the picture, complete the work and pay the outstanding bills, causing a total loss to the surety of approximately $75,000.

CASE 53

Surety Completed Utilities in Order to Meet Highway Use Date.

Contractor was given sub-contract for the completion of the sub-base and utilities in connection with a federally financed state project in the heart of a major city. The total amount of the contract was $700,000. Within six months from the beginning of the work, the contractor was declared in default and the surety elected to complete the project in order that the prime contractor, the state and the federal government would have the highway in use on the original completion date. The cost to the surety was $275,000.

CASE 54

Key Man Killed in Accident, Surety Expedites Completion.

Three contracts in the total amount of $3,300,000. The key man in the contracting organization was killed in an accident. Cash flow problems appeared within a short time. Investigation disclosed more serious financial deficiencies, but the surety expedited completion by utilizing the contractor's organization. The surety's loss totaled $650,000.

CASE 55

Surety Arranges Completion of Public School Contracts.

President and principal operator of contracting corporation disappeared. Twenty contracts, including twelve public schools and one hospital in various stages of completion. Surety arranged for continuation of operations and completion of all work at net loss to surety of more than $70,000.

CASE 56

Surety Financed Completion Without Default.

Thirteen contracts, all but two of which were federal, were involved in this group of cases and were in various stages of completion when construction came to an abrupt halt. The contractor's difficulties arose when contract funds approximating $250,000 were used to finance extracurricular investments.

Efforts by the contractor to raise capital were unsuccessful and, on inquiry, the surety determined that, without injection of additional capital and relief from the burden of accumulated and unpaid debts on completed contracts, a complete stoppage of work, as well as bankruptcy, was imminent.

The surety agreed to finance completion of all projects and was concerned primarily with the timely completion of the federal projects involving construction of the deep space structure, in the amount of $427,000, which was 25% completed, and the addition to the environmental control system building, in the amount of $170,000, which was 30% completed. These facilities were essential to the country's lunar space program. The Government was unaware of the contractor's difficulties and, by the use of a two-shift labor force and overtime, timely completion was achieved at a total cost to the surety in excess of $300,000.

CASE 57

Surety Finances Contractor to Completion.

The contract price to construct a maintenance dock was approximately $1,500,000. The contractor, having encountered difficulties in prefabricating the iron work for this large aircraft dock, had exhausted its finances in attempting to get the main truss properly in place. Because of the unique problems involved with this large structure, and the principal's ability to solve the problem if it had sufficient financial resources, surety decided to finance the contractor to completion. In this effort, surety expended over a two months period approximately $125,000 which sum went directly to finance the principal and cover over-drafts and other over-extensions of the principal. The job was completed without the assessment of damages for delay by the Government at the net cost to the surety of over $400,000.

CASE 58

Prompt Payments to Subs and Suppliers Ensured Delivery of Critical Equipment.

Principal had a contract for approximately $1,500,000 for general construction and electrical construction. Principal became financially distressed, and would have been unable to complete. Surety made periodic advances amounting to more than $400,000 to the principal. Total advances exceeded the remaining contract monies by approximately $100,000. Surety promptly satisfied unpaid subcontractors and suppliers, insuring that critically needed equipment would continue to be delivered. Surety's total loss, including advances to the principal and payments to creditors, was in excess of $500,000 but a default was prevented and possible delay in finishing the job was minimized.

CASE 59

Surety Helps Contractor Avert Default.

A statutory performance bond covering sewer and water works was executed in the amount of $250,000.

The contractor's difficulty was created when he encountered excessive ledge rock, bad weather and inability to get labor. These conditions created a delay beyond the 120 days called for in the contract. Under the circumstances, the contractor was temporarily put in a financial bind.

The surety was brought into the picture since it was a possibility that the contractor might be put in default by the owner. This did not come about, but the surety by counseling and assistance rendered to the contractor and its attorney was able to stabilize the situation and the job was completed and accepted by the owner. The surety suffered no loss under this situation but did, as above noted, render considerable aid in carrying out the contract.

CASE 60

Surety Applies Pressure to Contractor to Facilitate Completion Without Default.

Performance and Payment Bond was executed in the amount of $680,000 covering construction of college building.

Due to the tight money market, mismanagement and increased costs, the contractor, although able to complete the job, was in a financial bind and was unable to pay all suppliers and subcontractors. These factors caused considerable delay in the performance of this contract. The owner did not want to put the contractor in default and did not do so.

The surety entered into the matter and by counseling and paying the outstanding past due bills and subcontractors and in keeping the pressure on the contractor the job has been brought to completion. The gross amount of loss is approximately $125,000.

Group V. Cases of Surety Completion Using a Replacement Contractor

CASE 61

Surety Pays Premium to Finish Work on Time. Takes Three Million Dollars Loss.

Surety learned that the individual behind its principal corporation had disappeared. During the following month he apparently committed suicide.

At the time of his disappearance, there were 13 multi-million dollar contracts in various stages of completion. Three were for the construction of schools which were scheduled to open shortly after September 1. The others were for the construction of schools, a classroom building for a college and a high-rise apartment building for the elderly. Through cooperation with the owners the schools were opened shortly after September 1, although construction continued, some of it being performed at premium time wage rates. Eventually all incomplete work was completed by the surety with other contractors with minimum inconvenience to owners. The surety sustained a loss of about $3,000,000, about $1,000,000 of which was excess cost of completion, the remainder in bills incurred by the contractor prior to default. A number of subcontractors of this principal may have become bankrupt had not the surety promptly paid obligations owed under the payment bonds. While the owners were aware of the surety's involvement, their only obligation was to pay the original contract balance to the surety. They were not required to find other contractors to complete the work or otherwise become unnecessarily inconvenienced because of the default. All contracts were completed with minimum delay and any liquidated damages which were incurred as a result of the default were waived by the owners.

CASE 62

Surety Goes into Butterfly Valve Business.

Principal entered into a contract to design and furnish nearly 100 butterfly valves to a large water district. The contract price was nearly $700,000 and a bond in the amount of $349,000 secured performance.

After the design of the valves had been approved, the subcontractor manufacturing the valves went bankrupt. Principal was unable to physically or financially continue. The water district requested that surety takeover the contract, avoiding the necessity of total reprocurement. It was estimated that redesigning and manufacturing, if performed by a new contractor, would delay delivery of the valves at least one year.

Surety purchased the plans, specifications and work in progress. It rented the plant and equipment formerly owned by the bankrupt subcontractor. It arranged for the subcontractor furnishing the valve actuators to continue performance and entered into employment contracts with key employees. Total cash outlay by the surety reached a maximum of over $300,000. The owners advanced no funds, but agreed to pay the contract price for the valves as they were delivered. Contract was completed on time, the surety has recovered all of its funds, all suppliers received full payment and the employees have received a sizeable bonus.

CASE 63

Surety Gets Schools Open on Time.

Principal was a school constructor. When surety became involved, there were eight bonded projects under construction. Seven were nearly finished, and the remaining project, a $2,500,000 junior high school was 50% performed. In addition, another surety had bonded three school buildings which were also incomplete.

The sureties made payments for payroll, material and subcontracts to keep all projects operating without interruption. It became apparent that the largest project could not be completed by the principal's forces. Surety thereupon agreed with the school board that it would complete in its own name, using a local contractor known and acceptable to the board members. Surety continued to provide funds to keep the project operating until the new contractor was mobilized and ready to assume control without interruption in the work. The new contractor was successful in getting the school ready for occupancy at the beginning of the school term. The sureties completed all other projects as well, and have corrected all defective work found by the owners. The owners paid the contract balances to the sureties, as they were earned, but otherwise took no action and incurred no loss. Surety loss, while not final, appears to be $1,500,000. The other surety also sustained a loss in excess of $1,000,000.

CASE 64

Surety Replaces Key Subcontractor Without Holding Up Job.

Principal, a subcontractor, sustained losses on a number of bonded contracts. Surety was advised that principal was unable to handle his job costs on a subcontract for $7,000,000 for the installation of reinforcing steel and concrete at a large building complex. The prime contractor furnished the concrete and reinforcing steel at no cost to his subcontractor. Surety also bonded a number of projects for this principal in the mid-west, all of which were substantially performed, with large unpaid material bills.

Surety provided funds for payroll purposes and critical bills to keep progress moving. When it became apparent that principal could not continue, surety arranged for the prime contractor to employ principal's work force while a new subcontractor was sought. Surety and prime contractor jointly arranged contract terms with a new subcontractor, and surety purchased heavy equipment at the project to avoid the possibility of disruption which the loss of this equipment might cause. Work was then scheduled so that the new subcontractor commenced operations after only a one-week shut down and mobilization period.

Owner was aware that a key subcontractor had defaulted, and observed the subsequent events, but did not in any way participate in the arrangements. The architect for the owner has calculated that throughout the default and relet period, a total of less than three days normal production was lost. The new subcontractor has made up the one month the principal was behind as well as the lost three days. Owner's representatives have expressed appreciation to all parties for the smooth transition.

Increased cost of completion was about $1,250,000. Surety will also pay about $1,000,000 as claims for unpaid creditors of principal, and for correction of defective work installed by principal.

CASE 65

Surety Keeps Work Force Together. Two Million Dollar Loss.

This contractor corporation had received a franchise to manufacture and sell in the United States a concrete railroad cross tie. In order to promote this product in the United States, principal entered into two contracts to install the track work in mass transit systems being built in two cities.

Subsequent to entering into these contracts principal was acquired by a mini-conglomerate and before either contract was completed, the parent organization filed a Chapter XI proceeding in bankruptcy. These events impaired principal's finances and caused it to default in the performance of both contracts.

At the time of default, one project was in its final stages and dedication scheduled about six weeks later. Surety provided funds to keep the work force and equipment employed continuously, and dedication was held as scheduled. In order to do so, it was necessary for the surety to enlarge the labor force, pay for premium time work, obtain additional equipment and insure the flow of materials by prompt payment of past due obligations.

The other project was shut down for the winter at the time of default and by the time the winter had moderated, surety had arranged for another contractor to move onto the job and had arranged to purchase the necessary concrete cross ties from the only manufacturer available.

The surety's loss on these projects was approximately $2,000,000.

CASE 66

Surety Completes All Work of Insolvent Contractor. One Million Dollar Loss.

A State had five contracts for highway construction with this contractor. Total contract amounts exceeded $3,500,000. The contractor became insolvent after completing only one job. The State requested that the surety complete the work directly without involving the State in the arrangements.

Surety completed all work. In selecting new contractors, surety gave preference to contractors favored by the owner. Surety effected corrections of defective work, and made prompt payment of claims of materialmen and subcontractors. The State was obligated to pay the contract balances to the surety, but did not otherwise assume any duties or responsibilities.

The loss to the surety, when finalized, will be about $1,000,000.

CASE 67

Surety Arranged for Completion by a New Contractor. Surety's Loss: $3,800,000.

Contractor engaged in performing construction of college dormitory projects costing approximately $8,000,000 defaulted. Surety arranged for another contractor to take over and complete both projects, resulting in final loss to surety of approximately $3,800,000.

CASE 68

Surety Re-Lets Job Default.

A performance and payment bond in the amount of $2,400,000 was executed covering the construction of an addition and alteration to a memorial hospital.

The contractor's difficulty arose due to the tight money market, and further he was trying to complete an old contract with new labor and material prices. The contractor owed a considerable amount of money on payroll withholding taxes creating an additional financial crisis.

The contractor was in default and the surety was called in to make arrangements to relet the job. This job was relet with a minimal time delay. The surety made payments to the suppliers, subcontractors, bringing them up to date and on a current basis. The job was continued and it is essentially completed. The loss is estimated at $230,000.

The owners are now using the building

CASE 69

Deaths of Key People Force Contractor into Bankruptcy. Surety Takes Over.

A water proofing contractor subcontracted to do the necessary water proofing on two different sections of an interstate highway being constructed. The contractor's manager and general superintendent died and the corporation was forced into bankruptcy. At this time the work is still in process and the surety anticipates losses somewhere in the vicinity of $250,000.

CASE 70

Various Other Approaches Taken by Sureties to Get The Job Done.

The contractor had two separate contracts with a city for the installation of subsurface drainage. The contractor encountered financial difficulties and was in the process of liquidating its corporation after completing all of its other contracts but without having begun work on these two contracts. The first contract was assigned to another contractor to perform at the original contract price after the surety assured obligee that the assignment was without prejudice to any and all rights of the city as against surety under the terms of the contract. Thus the work was completed and accepted without additional cost to the obligee or surety.

On the second contract the surety allowed the obligee to enter into a new contract with the second lowest bidder without being compelled to secure new bids, and the surety agreed to pay obligee the difference between the price of the original contract and the price bid by the second lowest bidder, some $3,500.

CASE 71

Minority Contractor Defaults: Surety Completes.

Performance and payment bonds of $800,000 each executed March 1970 for a minority contractor covering four-story apartment for the elderly. Project, upon completion, was to be taken over by Public Housing Authority. Contractor defaulted leaving uncompleted work as well as numerous unpaid subcontractors and suppliers. Surety assisted obligee in arranging for completion and investigated and paid some 48 claims at a loss of $119,000.

CASE 72

Public Acknowledgment of The Surety's Efforts Are Few, But They Do Occur.

On a contract price of $200,000 for the electrical work only on a new police building, principal was unable to complete because of financial problems. Without causing interference with the other contracts, the surety relet the job at a net loss to the surety of over $92,000. The Mayor and City officials stated publicly that the surety acted above and beyond its obligation, thereby saving the City the time and cost of readvertising the work.

CASE 73

Surety Finances, Then Completes Job.

A general contractor went broke with three uncompleted contracts totaling $1,000,000 on which there was yet to be earned $700,000.

Initially the surety financed contractor, and when due to other non-job obligations it could not complete, surety arranged for another contractor to complete with principal's work forces and original subcontractors. Construction was not interrupted or delayed as it would have been by a reletting of the contracts. Loss to the surety was approximately $450,000.

CASE 74

Surety Arranges Completion Where Contractor Bows Out.

In accordance with the terms of a $130,000 contract, after part of the project had been completed work was shut down for the winter. Investigation by the surety disclosed that the contractor was experiencing personal and serious financial problems and that the site conditions made performance of the work unusually difficult. The contractor voluntarily defaulted and the surety made other arrangements for completion. Work resumed as soon as weather conditions permitted and the project was completed within the time allowed. The surety paid $130,000 for completion of the work.

CASE 75

Surety Arranged for Completion of Contract; Resulting Loss Was Almost Double Original Contract Amount.

Contract was in the amount of $180,000 covering site work at a High School. Contractor experienced many difficulties with the specifications. Management of firm was left to son after his father died and he was not able to arrest a deteriorating situation. Firm eventually went into bankruptcy. Surety stepped in when it was determined that the contractor had been overpaid for the work completed. The surety engaged another contractor to complete the work. Final loss to the surety was approximately $350,000.