

## Bonds

A surety bond is a guarantee whereby one party (the surety) undertakes to pay the direct loss suffered by a second party (the employer) as a result of a breach of contractual or legal obligations by a third party (the contractor). A surety bond is a written agreement that transfers risk of a contractor's default to a surety providing protection for the employer. In practice, insolvency of a contractor is the most common reason that breaches occur.

A surety bond may also be referred to as a contract guarantee or performance bond. We arrange many types of surety bonds. These include:

- **Contract Performance Bonds** - Contractors will usually be asked to provide a performance bond for up to 25% of the contract price to protect the employer.
- **Advance Payment Bonds** - In circumstances where advances are being given before work is carried out or material delivered an advance payment bond protects the party making the advance recover the funds if the work is not completed or materials are not supplied.
- **Retention Bonds** - At practical completion stage half the retention money is usually released. If a retention bond is provided all the retention may be released securely.
- **Development/Roads and Services Bonds** - Required by the Planning Authorities as a condition of a planning permission to ensure the proper completion of roads, sewers, public open spaces and other services.
- **Customs Trade Bonds** - are required by Customs to guarantee compliance with conditions of concessions. We offer a wide range of these including deferred duty bonds, transit bonds and tax warehouse bonds.

This list is by not exhaustive and should you have a bond requirement we are prepared to review the documentation and confirm if we can arrange the bond you require.

A bonding facility represents a commitment to provide bonds up to an agreed limit subject to the stated terms and conditions being met. A facility limit is set at an amount agreed between the surety and the contractor bearing in mind the anticipated bonding requirements for the coming year. Facilities are then reviewed and renewed at an appropriate level on an annual basis following the provision of updated satisfactory information.

At each review the terms and conditions are confirmed and detailed in writing. This allows a contractor to tender knowing with certainty that bonds can be provided, the cost of a bond and that evidence can be provided by either a letter of intent or a form of undertaking that bond facilities are in place.

### **In obtaining a bond from an insurance company neither a contractor's working capital nor borrowing facilities are affected.**

Where a bond is obtained from a bank it is regarded by the bank as part of the contractor's banking facilities and the bank usually insist that it will have to be fully supported with tangible collateral.

In addition an insurance Company will issue bonds that are linked to contract performance, they give the contractor the protection of the contract conditions and non performance has to be clearly shown before payment is made under the bond.

An insurance policy is traditionally a two party relationship whereas bonds are a three party arrangement. The three parties involved are:

- The Employer (or beneficiary) who has awarded the contract and requires the comfort and protection of a bond.
- The Contractor (or principal) who has agreed to carry out the work and arranges to put a bond in place.
- The Surety (or guarantor) who has agreed to compensate the employer for any losses should the contractor fail to meet their contractual obligations.

In addition bonds are made available on a recourse basis, with counter indemnities being obtained from the contractor/principal, so that should the surety be required to make a payment to the beneficiary they are entitled to seek recourse from the contractor/principal.

Generally speaking once issued a bond CANNOT be cancelled without the agreement of the beneficiary.

Unless the bond is released or expires in accordance with its express terms, only the beneficiary can agree to release the bond.

### **What information is required in order to process a bond application?**

We adopt a holistic approach and rather than dealing with a contractor on a contract-to-contract basis, we prefer to consider the firms overall bonding needs. In this manner we feel we can best service a contractor's requirements.

For a first time applicant a completed facility proposal form provides insurers with a company profile, this provides background information and contact details of the applicant and its advisors.

In addition we require information that allows us to assess each applicant on the basis of professional experience, financial stability, technical ability and capacity for contracts.

This will ordinarily include the following:

- Audited accounts for the last 2 years
- A forecast of the current years trading and management accounts, if available
- Details of banking facilities
- A Workload schedule
- Details of contracts completed in the previous 5 years.
- Details of key personnel

These details help to provide a comprehensive profile of the contractor.

A Bonding facility represents an extension of credit and as such insurers must assess an applicant's financial strength.

We need to have a full and clear understanding of your business therefore a complete analysis of your financial position is necessary. The financial information allows us to assess that an applicant's financial performance is satisfactory and

provides assurance that the applicant is continuing to trade both profitably and within their capabilities.

Once a contractor has established a facility with an insurer(s), a bond application can be processed within days of receipt of all relevant information.

However for a first time application the process usually takes a little longer as insurers need to gather a lot of initial information from the company that is not necessarily required for future applications.

The rates charged vary and each contractor is assessed on their own merits. The rate applicable will be determined by a number of factors including:

- the financial strength of the contractor,
- the volume of bond business and
- Underwriting analysis.

For more information on Bonds contact Paul Farrar or your Account Director.

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