National Association of Surety Bond Producers
1140 19th Street, NW. Suite 800. Washington, DC 20036-5104
Phone: (202)686-3700
Fax: (202)686-3656
Web Site: http://www.nasbp.org
E-mail: info@nasbp.org

Sent via email at tjohnson@agctx.org.

October 27, 2011

Thomas L. Johnson
Executive Vice President
AGC of Texas
P.O. Box 2185
Austin, Texas 78768

Re: TXDOT Warranty Bond Requirement Relating to Polymer Overlay

Dear Mr. Johnson:

I am writing on behalf of the National Association of Surety Bond Producers (NASBP), a national trade association of member companies employing professional surety bond producers who place bid, payment, performance, and maintenance bonds for construction and infrastructure projects, including projects in the State of Texas. Recently, it has come to our attention that the Texas Department of Transportation (TXDOT) has specified certain contractual requirements, specifically a fifteen year warranty on “thin polymer overlay” coupled with a warranty bond covering that obligation, which, in the opinion of NASBP, are not realistic and may have the inadvertent impact of increasing the pricing of and lessening the competition for TXDOT projects significantly. I am writing you to provide our thoughts and concerns, as your members will be impacted by this matter, particularly if such requirements are routinely specified in the future.

Of particular note are two specification sections, which raise significant concerns from a surety perspective. They are “Special Specification 3238, Thin Polymer Overlay with Performance Warranty,” and “Special Specification 5983, Warranted Construction.” These specification sections make clear that the contractor winning award of the contract is expected to furnish a bond or bonds of a duration extending fifteen years from the date of final acceptance of the construction phase of the project and guaranteeing the performance of the polymer overlay. The penal value of the bond is significant, being specified at $2,000,000.00. Special Specification 3238 does indicate that the warranty bond may be furnished by the contractor or by the manufacturer, and that the warrantor will assume responsibility for compliance with all warranty requirements. However, obtaining a bond of such lengthy duration likely will prove problematic for any bond principal, whether such principal is a construction firm or a manufacturer. Manufacturers also likely have not established prior surety bonding relationships, which take time and effort to do so, since they do not furnish bonds in the regular course of their business.

A lengthy warranty bond duration, such as for fifteen years, poses considerable problems from a surety underwriting perspective. Sureties usually are comfortable in covering a warranty obligation of several years duration. Durations longer than two or three years increase substantially the uncertainty regarding projections about the contractor’s future viability. Simply put, sureties cannot gauge the soundness and financial wherewithal of a company at a single point in time for periods that extend too far into the future.

The present economic environment further underscores the difficulty of a guarantee obligation of such long duration. Even in the best economic times, a bond for fifteen years, even for five years, if available commercially, would be unavailable to most contractors or solely available to the largest and most well-capitalized companies. In this economy, many quality contractors simply do not possess the financial wherewithal they once possessed. Long guarantee and warranty obligations effectively eliminate most competition for such contracts, thereby reducing competition and elevating pricing. Small and medium-sized contractors will be precluded. As transportation projects use public funds, contracting considerations to maximize, not to reduce, competition should be foremost policy considerations.

I hope you find these thoughts and concerns informative. Please feel free to contact me should you have questions or wish further information or assistance with this matter.

Yours sincerely,

Mark H. McCallum

Mark H. McCallum
Chief Executive Officer