

Unravelling the Mystery of COURT BONDS



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FOR PARTIES ENGAGED in litigation, court bonds are often a useful tool. Because there is such a variety of these bonds, it is often difficult to know the proper name and purpose of each of them. This article will provide a brief explanation of the primary types of court bonds that are available, along with a few useful tips for producers and underwriters.

Appeal and supersedeas bonds

The most common types of court bonds are appeal bonds and supersedeas bonds. There is often confusion between these two types of bonds, the terms of which are improperly used interchangeably.

Appeal bonds

An appeal bond covers the opposing party's court costs if the appeal is unsuccessful. Any party can bring an appeal after a final judgment in civil litigation. The specific

rules regarding the appeal and the costs covered vary from jurisdiction to jurisdiction and from state court to federal court.

The court will determine the penal sum of the appeal bond. Because damages are usually limited to court costs, such as filing fees, transcripts, etc., attorneys' fees are generally not covered unless the appeal involves a specific statute providing for fees. The producer should gain a working understanding of the law in his or her jurisdiction and advise the surety to ascertain the relevant law and to seek proper guidance when underwriting the account.

Supersedeas Bonds

The supersedeas bond guarantees the successful trial court litigant that it will have a source of collection after the appeal. When a party prevails in the trial court

and obtains a judgment against its opponent, the opponent may want to appeal that decision. In addition, the judgment debtor does not want the plaintiff to collect on the judgment while the appeal is pending.

In order to put the collection efforts on hold, the judgment debtor appealing the decision (appellant) must obtain a stay of enforcement. To obtain the stay, the appellant will have to file a motion with the court and then post the bond. If the court grants the stay, the court will determine the amount of the bond. The amount of the bond is usually around 125 percent of the judgment amount to account for costs, interest, and other damages that might arise during the course of the appeal.

Because the appellant has already lost in the trial court, the surety is taking on a substantial

risk by issuing a supersedeas bond. Sureties generally require that these bonds be fully collateralized before issuing them.

The typical supersedeas bond guarantees that, if the defendant loses the appeal, then the surety and principal are jointly and severally liable to the obligee (appellee) to satisfy the judgment. The specific liability will vary depending on the language of the bond.

Injunction bonds

An injunction is a court order generally either requiring a party to take a certain action or preventing a party from doing something. Sometimes injunctions are issued before a full trial, as in the case of a temporary restraining order or preliminary injunction. In those cases, the court sometimes requires an injunction bond.

However, it is not the enjoined party (who is generally the person accused of doing something wrong) who is required to obtain an injunction bond, but rather the person requesting the injunction who must do so. The purpose of the injunction bond is to protect the enjoined party from damages resulting from an improper injunction. See, for example, *Longshore Lakes Joint Venture v. Mundy*, 616 So. 2d 1047 (Fla. Dist. Ct. App. 1993). In other words, the party benefitting from the injunction bears the risk that the court (following a full hearing on the merits) will decide that the injunctive relief was not warranted.

An example of the damages an enjoined party could suffer from an improper injunction would be a company's lost profits if prevented from manufacturing and selling a product while a patent infringement lawsuit is pending. See, for example, *Apple, Inc. v. Samsung Electronics Co., Ltd.*, 678 F.3d 1314 (Fed. Cir. 2012).

As the amount of potential damages that could result from an injunction is often speculative, a court can generally set the amount of the bond at its discretion, as provided for in Federal Rule of Civil

BECAUSE THE APPELLANT HAS ALREADY LOST IN THE TRIAL COURT, THE SURETY IS TAKING ON A SUBSTANTIAL RISK BY ISSUING A SUPERSEDEAS BOND. SURETIES GENERALLY REQUIRE THAT THESE BONDS BE FULLY COLLATERALIZED BEFORE ISSUING THEM.

Procedure 65(c). The surety's liability is limited to the amount of the bond. Note, however, that the wrongfully enjoined party does not have to prove that the injunction proceeding was brought in bad faith to collect under the bond, only that the injunction was improper. Accordingly, most states allow a presumption in favor of recovery by the wrongfully enjoined party under the bond. See, for example, *U.S. D.I.D. Corp. v. Windstream Communications, Inc.*, 775 F.3d 128 (2d Cir. 2014). Thus, bond producers and sureties should keep in mind that injunction bonds can be a risky endeavor, and securing collateral (as discussed below) is recommended.

Attachment/dissolution bonds

Just as with a preliminary injunction, an attachment is a remedy provided to a plaintiff before a full trial or other hearing on the merits. In certain situations, a court may order the seizure or "attachment" of a defendant's property to make sure that the property remains available to satisfy an eventual judgment for the plaintiff.

To obtain a pre-judgment attachment, the plaintiff must show there is a reason to believe the defendant will improperly take some action to deprive the plaintiff of an opportunity to collect on a judgment. For example, the Federal Rules of Civil Procedure provide that the United States, in attempting to collect a federal debt, should be granted a pre-judgment remedy (such as attachment) only if it can show there is reasonable cause to believe that the debtor is going to leave the jurisdiction, dispose of, convert or destroy property, or evade service of process. See 28 U.S.C. § 3101(b)(1).

Because attachment is considered an extraordinary remedy, the plaintiff must post a bond to cover any damages to the defendant resulting from the attachment if it is later determined the attachment was erroneous. Just as with injunction bonds, those damages could include lost profits resulting from the defendant's inability to use the property. The laws of each state should be consulted to understand how the amount of the bond is determined, but generally a court has discretion to set the amount based on the facts of the case and nature and value of the property attached.

A defendant whose property has been seized through attachment can regain possession of the property through a "dissolution" or "release" bond. A "dissolution" bond, the amount of which should be at least the value of the property, provides a source for recovery if the plaintiff eventually obtains a judgment. Dissolution bonds, as the name suggests, actually dissolve the attachment. If the plaintiff wins the lawsuit, it can simply collect on the bond. On the other hand, "release" bonds allow the defendant possession of the property, but the attachment remains. The release bond guarantees that the property will remain available for satisfaction of a judgment. Obviously, whether the bond is for dissolution or release is an important distinction for bond producers and sureties. Because the property will not necessarily be available to satisfy a judgment following a "dissolution" bond, surety professionals must take that into account when determining how much collateral will be needed.

Replevin bonds

Replevin, which is also known as "claim and delivery," is the legal process that enables a person to

recover his or her personal property after another unlawfully takes it. Technically, replevin is defined as a civil action to recover possession of goods or chattels that have been unlawfully taken or unlawfully detained and to recover damages sustained as a result of the unlawful taking or unlawful detention. A chattel is movable or transferable property, especially a movable object capable of manual delivery and not the subject matter of real property.

See *Black's Law Dictionary* at 251 (8th ed. 2004).

The procedure for pursuing a replevin action varies by statute, but, in general, it requires that the plaintiff do two things. First, the plaintiff must file an affidavit (a sworn written statement) or complaint describing the property, its value, and stating that the plaintiff is the owner of the property. Second, the plaintiff must post a replevin bond. The replevin bond protects the defendant from

losses that may result from the plaintiff's seizure of the personal property. Typical provisions in a replevin bond include that the property be returned if ordered by the court and that the plaintiff pay for any damages that were likely caused by the seizure.

Note that these bonds are similar to "attachment" bonds discussed above, except that the attached property in a replevin action is the subject matter of the lawsuit (rather than simply a means of satisfying an eventual judgment).

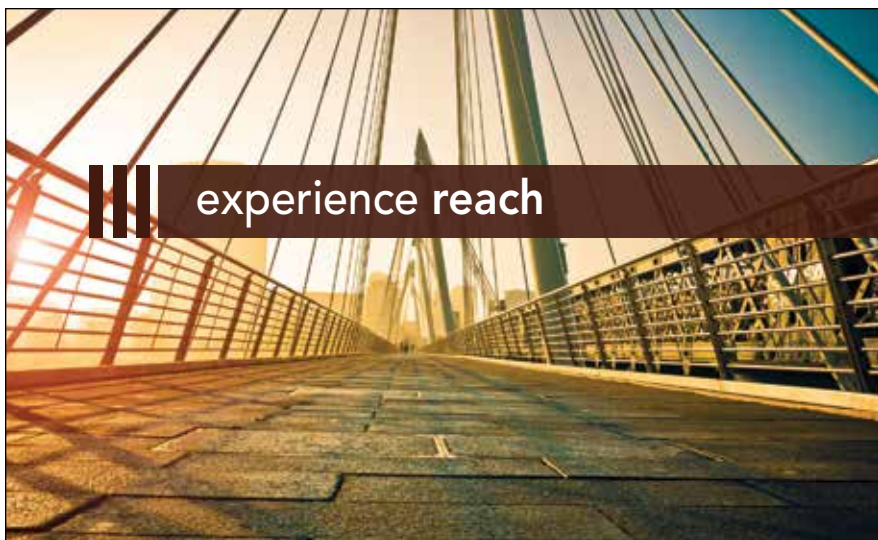
Receiver bonds

Receivership is the scenario where a corporation or other entity is being controlled by a receiver. A receiver is a disinterested person appointed by a court, or by a corporation or other person, to protect or to collect property that is the subject of various claims (for example, because the property belongs to someone who is going through a bankruptcy or is the subject of a lawsuit). See *Black's Law Dictionary* at 1296 (8th ed. 2004). A receiver's typical powers and duties are to collect, administer, and disburse the receivership property for the benefit of all persons interested in the estate.

In many jurisdictions, before the court will appoint a receiver, the receiver must post a bond that will protect interested parties from damages caused by the receiver's failure to properly discharge his or her duties. Generally, a receiver bond guarantees the following duties of the receiver: (1) the care and preservation of the property that the receiver is controlling; and (2) the disposition and distribution of the property pursuant to court orders. In many cases, a material, or substantial, breach of the receiver's duties creates liability under the receiver bond.

Bail bonds

After an arrest, bail is the process undertaken where a person obtains the release of the accused by providing security to ensure future court appearances. See *Black's Law Dictionary* at 150 (8th ed. 2004). If the



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accused does not appear before the court when ordered, for example, for an arraignment or a trial, the court may keep the bail and issue a warrant for the accused's arrest.

A surety bond can be used to secure bail. Bail bonds are useful when the accused cannot afford to pay the full amount of his or her bail. A surety that issues a bail bond pledges to pay the full value of the bail if the accused does not appear in court. In return, the surety often charges a 10 percent premium and secures its obligation with collateral (for example, title to real property, car, boat, jewelry).

Claims on court bonds

Some of the court bonds listed above are payable on demand after a condition precedent is satisfied. Examples include a supersedeas bond, which the surety must pay if the defendant loses its appeal, and a bail bond, where the surety pays when the accused fails to appear in court. Other types of court bonds, like an appeal bond and an attachment bond, require an analysis to determine the amount of costs or damages the surety will have to pay.

Indemnification and collateral

As with other bonds, sureties issuing court bonds should, and typically do, require the principal (and sometimes others) to execute an indemnity agreement, requiring reimbursement to the surety for any losses, costs, expenses and attorneys' fees. Whether indemnity is obtained from one or more individuals (when the principal is an entity) depends on the size and financial strength of the entity and its history with the surety, among other factors.

Depending on the nature of the bond, a surety may also require the principal to deliver collateral to the surety, providing an immediate source of recovery in the event the surety suffers losses. Collateral is typically required for appeal or supersedeas bonds, as the risk to the surety is extremely high in those circumstances (in which a court has already found the principal liable).

The amount of collateral will depend on the nature of the bond. For example, for an attachment bond, the value of the attached property and the potential damages to be suffered by the defendant should be taken into account when determining the appropriate amount of collateral. Collateral can take the form of a bank's letter of credit, a lien on real property, or some other assignment or transfer of property.

Note that each surety has differing policies with respect to what collateral

can be accepted. Accordingly, depending on the type of collateral a principal or indemnitor has to offer, a bond producer may have to check with different sureties to find the right fit. For example, some sureties may only accept letters of credit; and it may be necessary to find a surety willing to accept a less conventional type of collateral, such as an interest in real (or even personal) property.

Because many of these bonds are similar (and are often confused),

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producers and underwriters must confirm what bond is required by the court and what liability the surety may ultimately face. A careful review of what bond is necessary will not only ensure that the correct type of bond is issued, but also it will enable the producer to secure the correct amount of collateral.

Finally, producers and underwriters should check the requirements of the relevant jurisdiction, to make sure that any specific local rules or requirements are taken

into account when deciding on a bond form. ●

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Subcontract notification clauses require the prime contractor to provide notification to the government prior to the prime contractor entering into a subcontract. The most prevalent subcontract notification clause in federal government contracts, FAR 52.244-2, Consent to Subcontract, is typically included in cost-type contracts and requires the prime contractor to not only notify the government of a potential subcontract award, but also to obtain the government's consent prior to the prime entering into the subcontract. A related subcontract notification clause, FAR 52.244-5, Competition in Subcontracting, requires the prime contractor to notify the government reasonably in advance of placing a subcontract and also generally requires the prime contractor to select the subcontractor on a competitive basis.

Subcontract performance clauses limit the prime contractor's ability to subcontract out certain portions of the work called for under the prime contract. In this area, the most prevalent clause, FAR 52.219-4, Limitations on Subcontracting, is included in most small business set-aside contracts. The clause operates to prevent large business contractors from circumventing the

requirements of the set-aside programs. Under this clause, when a small business contractor receives a set-aside award, it is required to perform a certain percentage of the work itself; and the contractor is prohibited from subcontracting out work in excess of that percentage. The percentage of work that must be performed by the small business varies from contract to contract, with the small business being required to perform only 15 percent of the work under a general construction contract and generally 50 percent of the work under a services or supply contract.

In sum, the subcontracting limitations placed on subcontractors are numerous, but compliance with these clauses is relatively straightforward. Notwithstanding the relatively straightforward requirements, recent enforcement actions in this area, also in the form of False Claims Act suits, demonstrate that certain contractors have repeatedly failed to understand and follow the subcontracting limitations in their contracts. Again, to the extent questions arise as to how to comply with subcontracting limitations, contractors are well-advised to seek guidance in this increasingly targeted compliance area.

As addressed above, the consequences for compliance failures can be severe. Government claims, termination for default, suspension and debarment, and False Claims Act suits are all mechanisms that can be brought to bear against a contractor, with any one of these mechanisms capable of serving a crippling blow to a contractor's business. However, while compliance can be burdensome, the burden associated with compliance is far outweighed by the potentially devastating result that can flow from a contractor's compliance failure. And the key to compliance is an understanding of each contract's requirements. While the compliance burden on federal construction contractors may seem daunting, a thorough understanding of the government's compliance requirements and maintaining an effective system to stay informed of those requirements makes federal contracting a manageable and lucrative endeavor. ●

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Be sure to read Avery's next article on Evolving Compliance Requirements: the New Anti-Human Trafficking Requirements.