

# Can Public Owners be Held Liable to Subcontractors and Suppliers for Failure to Require General Contractors to Obtain Required Payment Bonds?



BY TODD REGAN

**IT'S A TROUBLING** scenario. After months of promises from the general contractor that payment would be issued soon, that it is about to

negotiate a large change order with the owner, and that "they haven't been paid yet either," the subcontractor simply can't wait any longer. The subcontractor has been financing the project for months by paying its own employees and suppliers, without receiving the continually promised progress payments. Finally, the subcontractor asks the owner's representative for a copy of the payment bond, only to hear something it never even considered: the general contractor never posted the payment bond required by law. To make matters worse, because it's a municipal

project, it doesn't have the right to file a mechanic's lien; and the prime contractor is heading towards bankruptcy.

Unfortunately, subcontractors do find themselves in this predicament. Despite the requirements of the federal Miller Act, 40 U.S.C. § 3131, *et seq.*, and the similar state laws, the statutorily required payment bonds are not always in place. Perhaps the school board failed to appreciate that the project was subject to the statutory bonding requirements. Perhaps the city council neglected to check if the prime contractor actually submitted the required bonds. Perhaps the contracting officer failed to ensure that the bond was issued by a licensed surety authorized to do business in the state. Perhaps the surety became insolvent after the project started and the owner failed to require a new bond. Regardless of the reason, subcontractors might perform work on public projects with the assumption that their right to payment is secured, only to find out too late – after the prime contractor defaults on its payment obligations – that there

is no payment bond in place. What then is the unpaid subcontractor's remedy?

Bond producers and other surety professionals should take note that, under certain circumstances, subcontractors and suppliers may have a right of recovery directly against the public owner for failing to ensure that the required payment bond is posted. Whether the subcontractor has such a right of recovery, or whether it is left out in the cold, varies widely across jurisdictions.

The issue of whether to allow a subcontractor to hold a public owner directly liable for failing to require a payment bond invokes a conflict between two fundamental principles underlying the statutory bonding requirements: protecting the payment rights of subcontractors and suppliers performing public work versus protecting the public coffers from claims for payment. A rule imposing liability on public owners for failing to ensure that the required bonding is in place has the dual benefit of protecting subcontractors and giving public

owners an added incentive to ensure compliance with the bonding requirements. Without question, it is the public owners, and not the subcontractors, that are in the best position to ensure that contractors comply with the bonding requirements. Yet, as set forth in the 50-state survey chart accompanying this article, the majority of jurisdictions do not recognize such a cause of action.

### No remedy for the “hapless subcontractor” on federal projects

A subcontractor on a federal Miller Act project has no recourse against the federal government in the event that the required payment bond is not posted. In *Arvanis v. Noslo Engineering Consultants, Inc.*, 739 F.2d 1287 (7th Cir. 1984), *cert. denied*, 496 U.S. 191 (1985), two unpaid subcontractors brought suit against the federal government after the prime contractor, who failed to post a Miller Act payment bond, went into bankruptcy. In dismissing the subcontractors’ claims, the court ruled that the federal government has no affirmative obligation to ensure that a prime contractor obtains the payment and performance bonds required by the Miller Act. The court further held that the claims were barred by the government’s sovereign immunity. The court noted, with a tangible sense of disappointment, that it is the “hapless subcontractor” and not the federal government that is left “holding the bag” when a prime contractor fails to obtain the required bonding. Although the court recognized that the outcome was “unjust,” it noted that it was up to Congress to address the issue by amending the statute.

Significantly, although the court in *Arvanis* advises subcontractors to protect themselves by inquiring with the contracting officers to ensure that the required bonds have been posted, under the statutory language of the Miller Act, in order to obtain a certified copy of the payment bond, the subcontractor must first submit an affidavit to the government certifying that it has not been paid for its work, which may be far too late. See U.S.C.

§ 3133(a). However, subcontractors and suppliers should take note that the Federal Acquisition Regulations provide methods for subcontractors and prospective subcontractors to obtain information about the payment bond posted by the prime contractor as well as a copy of the bond itself prior to entering into the subcontract or performing work on the project. The regulations provide that the contracting officer must furnish this information to subcontractors or prospective subcontractors on request. FAR 28.106-6(b). The regulations similarly require a prime contractor to provide “a prospective subcontractor or supplier offering to furnish labor or material” with a copy of its payment bond upon request. FAR 52.228-12.

Accordingly, subcontractors and suppliers on federal projects are well advised to use these tools to obtain a copy of the prime contractor’s payment bond prior to executing a subcontract for the project, rather than waiting until payment disputes arise.

### Differing approaches by the states

A subcontractor’s ability to assert a claim for payment directly against a public owner for failing to require the prime contractor to post a statutorily required payment bond varies widely from state to state. In a small minority of jurisdictions, a public entity’s liability for failing to require bonds is set forth expressly by statute. For example, in Connecticut, a subcontractor is expressly authorized by statute to bring suit for payment directly against a municipality (but not against the state) for failing to ensure compliance with the bonding requirement. See Conn. Gen. Stat. § 49-41(d). Similarly, in Idaho, a public body that fails to ensure compliance with the bonding requirement must, on demand, promptly make payment directly to unpaid subcontractors. See Idaho Code Ann. § 54-1928. The potential consequences to a municipality for failing to ensure that payment bonds are posted are even more dire in Missouri. Not only does the statute, Mo. Rev. Stat. § 107.170,

create an express duty on public entities to ensure that the required bonds are in place, but also public officials may be held *personally liable* for the claims of unpaid subcontractors if they fail to ensure that bonds are posted. See *Union Pacific R.R. v. St. Louis Marketplace, Ltd. P’ship*, 212 F.3d 386 (8th Cir. 2000) (Mo.).

However, as noted by the Alaska Supreme Court, most courts in states that do not expressly impose liability by statute on the public owners have read the bonding statutes narrowly and have declined to impose liability by implication. See *Imperial Mfg. Ice Cold Coolers, Inc. v. Shannon*, 101 P.3d 627, 632 (Alaska 2004).

In rejecting an implied cause of action against the public entity, the court in *Imperial Mfg.* held that such a rule “would be contrary to the premise on which the Little Miller Act is based, which is that neither the government nor government property may be charged by those with whom the government has no contractual relationship. We believe that if the legislature had intended to impose government liability – in effect as the school district puts it, to require public entities ‘to pay twice for a public project’ – this intention would have been expressed because it is a significant variation from the existing norm.” *Imperial Mfg.*, 101 P.3d at 630. Other courts have refused to impose liability on public owners on the grounds that subcontractors have a means of verifying the existence of the payment bond prior to entering into a subcontract. See *Blanchard v. Burns*, 162 S.W. 63 (Ark. 1913).

In contrast, courts that have recognized an implied cause of action against public owners for failing to require bonds have focused on the importance of protecting the rights of subcontractors and suppliers that are deprived of the right to file mechanic’s liens against public property. For example, in *Walt Rankin & Associates v. City of Murieta*, 84 Cal. App. 4th 605 (2000), the California Court of Appeals held that a municipality has a mandatory duty to ensure that payment bonds

# 50-State Survey on Public Owner Liability to Subcontractors and Suppliers for

## ALABAMA

\*None

\*\*Medical Clinic Bd. v. Smelley, 408 So. 2d 1203, 1981 (Ala. 1981) (public agency liable for subcontractor's payment claim for failing to require payment bond).

## ALASKA

\*None

\*\*Imperial Mfg. Ice Cold Coolers, Inc. v. Shannon, 101 P.3d 627, 632 (Alaska 2004) (subcontractor could not sue school district for failing to ensure that bonding requirements of Little Miller Act were met).

## ARIZONA

\*None

\*\*Flori Corp. v. Yellow Rose Dev. & Constr., Inc., 911 P.2d 546 (Ariz. Ct. App. 1995) (city not liable to unpaid subcontractors for failing to ensure that payment bond from viable surety remained in place for life of the project).

## ARKANSAS

\*None

\*\*Blanchard v. Burns, 162 S.W. 63 (Ark. 1913) (directors of school district could not be held liable to subcontractor for failing to require payment bond).

## CALIFORNIA

\*None

\*\*Walt Rankin & Assocs. v. City of Murieta, 84 Cal. App. 4th 605 (2000) (municipality has a mandatory duty to ensure that the payment bond posted by a prime contractor is issued by a sufficient admitted surety licensed in California and, in failing to do so, becomes liable for claims of unpaid subcontractors).

## COLORADO

\*None

\*\*Newt Olson Lumber Co. v. School Dist., 83 Colo. 272 (1928) (school district not liable to subcontractor for failing to require payment bond).

## CONNECTICUT

\*Conn. Gen. Stat. § 49-41 (d) (political subdivision of the state liable for payment of subcontractor claims for failure to require contractor to post bond; only applies to

municipalities and does not apply to claims against the State).

\*\*York Hill Trap Rock Quarry Co. v. Conn-Strux, Inc., 2012 Conn. Super. LEXIS 375 (Feb. 10, 2012) (statute applies only to municipalities; does not waive the state's sovereign immunity).

## DELAWARE

\*None

\*\*None

## FLORIDA

\*None

\*\*Palm Beach County v. Trinity Indus., 661 So. 2d 942 (Fla. Dist. Ct. App. 1995) (bonding statute interpreted to impose implied obligation on public entity to ensure compliance with contractor's bond requirement; county directly liable for payment of subcontractor due to its failure to require a bond).

## GEORGIA

\*Ga. Code Ann. § 13-10-61 (public entity liable for payment of unpaid subcontractors in the event that it fails to ensure that general contractor posts required bond).

\*\*City of Atlanta v. United Elec. Co., 414 S.E.2d 251 (Ga. Ct. App. 1991) (City of Atlanta has been held liable to an unpaid subcontractor for failing to require a payment bond from a general contractor, as provided by statute).

## HAWAII

\*None

\*\*None

## IDAHO

\*Idaho Code Ann. § 54-1928 (any public body subject to the act that fails or neglects to obtain the required payment bond must, upon demand, itself promptly make payment to all persons who supplied materials or performed labor in the prosecution of the work under the contract).

\*\*H-K Contractors v. Firth, 101 Idaho 224 (1979) (court affirmed summary judgment in favor of subcontractor's claim against city for failure to require prime contractor to post payment bond).

## ILLINOIS

\*None

\*\*Western Waterproofing Co. v. Springfield Hous. Auth., 669 F. Supp. 901, 902 (C.D. Ill. 1987) (subcontractor successfully sued public entity for failure to require prime contractor to post required payment bond, on a third-party beneficiary theory).

## INDIANA

\*None

\*\*None

## IOWA

\*None

\*\*Star Equip., Ltd. v. State, 843 N.W.2d 446 (Iowa 2014) (when public entity waives bonding requirement for small businesses, unpaid subcontractors can, in the absence of a payment bond, recover directly against the public entity).

## KANSAS

\*None

\*\*Freeman v. Chanute, 63 Kan. 573, 578 (1901) (public entity cannot be sued by unpaid subcontractor for failure to require bond).

## KENTUCKY

\*None

\*\*None

## LOUISIANA

\*None

\*\*None

## MAINE

\*None

\*\*None

## MARYLAND

\*None

\*\*Bd. of Educ. v. Alcrymat Corp. of America, 258 Md. 508 (1970) (school board protected by doctrine of sovereign immunity from subcontractor's suit for failure to require payment bond).

## MASSACHUSETTS

\*None

\*\*None

## MICHIGAN

\*None

\*\*ABC Supply Co. v. City of River Rouge, 216 Mich. App. 396 (1996) (public entity cannot be sued by subcontractor for failing to require bond or failing to ensure bond remains in place, but if public entity

furnishes subcontractor with a certified copy, it is liable to the subcontractor if the bond later is determined to be invalid).

## MINNESOTA

\*Minn. Stat. § 574.29 (public body liable for payment of subcontractors if it fails to require contractor to post payment bond).

\*\*Green Elec. Sys., Inc. v. Metro. Airports Comm'n, 486 N.W.2d 819 (Minn. Ct. App. 1992) (Metropolitan Airport Commission liable to subcontractor for failure to require payment bond if subcontractor can establish that general contractor was insolvent and unable to pay subcontractor for its work).

## MISSISSIPPI

\*None

\*\*Mississippi State Bldg. Comm'n v. S & S Moving, Inc., 475 So. 2d 159 (Miss. 1985) (when state failed to require contractor to post bond as called for in contract, unpaid subcontractors could maintain action for payment directly against state when contractor became insolvent; by entering into contract the state waived sovereign immunity); but see Pidgeon Thomas Iron Co. v. Leflore County, 135 Miss. 155 (1924) (subcontractor's negligence claim against public entity for failure to require payment bond barred by the doctrine of sovereign immunity).

## MISSOURI

\*Mo. Rev. Stat. § 107.170 (all public entities have a duty to ensure that the required bonds are posted; permits public entities to indemnify any of its officers and employees from personal liability for failure to comply with the statute).

\*\*Union Pac. R.R. v. St. Louis Marketplace, 212 F.3d 386 (8th Cir. 2000) (Mo.) (unpaid contractor could maintain action against city as well as individual city officials personally for failing to require developer to post required bonds).

## MONTANA

\*Mont. Code Ann. § 18-2-202 (public entity liable for payment of subcontractors if it fails to ensure required payment bond

are issued by a sufficient surety that is licensed in California and, in failing to do so, becomes liable for the claims of unpaid subcontractors. In *Rankin*, a city awarded a contract for the construction of a playground to a general contractor that posted a payment bond issued by a Turks and Caicos company not licensed as a surety in California. When the

general contractor defaulted on its payment obligations to a subcontractor, the subcontractor asserted a payment bond claim. Unfortunately, shortly after issuing the bond for the project, the president of the surety was indicted, the surety vacated its offices, and its assets were unknown or nonexistent at the time of the lawsuit. The subcontractor then brought

suit against the city for negligently failing to require a bond posted by a sufficient surety. The court found an implied obligation on the part of the public owner to investigate and verify the sufficiency of the surety, despite the lack of an express statutory obligation to do so. In the aftermath of this decision, the legislature passed a statute, Cal. Code Civ. Proc.



# Failure to Require General Contractors to Obtain Required Payment Bonds

is posted).

**\*\*None**

## NEBRASKA

**\*None**

**\*\*Chicago Lumber Co. v. Sch.** Dist. No. 71, 227 Neb. 355 (1988) (subcontractor could maintain a negligence action against school district for failure to require payment bond).

## NEVADA

**\*None**

**\*\*Charlie Brown Constr. Co. v. Boulder City**, 106 Nev. 497 (1990) (subcontractor could sue municipality for failing to require payment bond required by municipal code).

## NEW HAMPSHIRE

**\*None**

**\*\*None**

## NEW JERSEY

**\*None**

**\*\*None**

## NEW MEXICO

**\*None**

**\*\*None**

## NEW YORK

**\*None**

**\*\*Davidson Pipe Supply Co. v. Wyoming County Indus. Dev. Agency**, 85 N.Y.2d 281 (1995) (overturning decision of the trial court holding an industrial development agency was liable to unpaid subcontractor for failure to ensure posting of bond required by State Finance Law § 137, on grounds that the project was not a "public improvement" within the meaning of the bonding statute; leaves open the possibility of a private cause of action against a public owner for failure to require a bond); **Murnane Assocs. v. Harrison Garage Parking Corp.**, 239 A.D.2d 882 (N.Y. App. Div. 1997) (similar holding based on finding that the project was not a public improvement; does not address lower court's finding that the statute provides an implied right of action against the public owner for failure to require a bond).

## NORTH CAROLINA

**\*N.C. Gen. Stat. § 44A-32** (each contracting body shall designate an official to require the bonds described by the Article; if the official designated

fails to require the bond, he will be guilty of a Class 1 misdemeanor).

**\*\*James River Equip., Inc. v. Tharpe's Excavating, Inc.**, 179 N.C. App. 336, 345 (2006) (unpaid supplier had no cause of action against county board of education for failing to require prime contractor to post replacement bond when original surety became insolvent, although the Little Miller Act does require the public entity to ensure that bonding remains in place throughout the life of the project; the statute only provides a misdemeanor criminal penalty and does not create a private civil cause of action in favor of unpaid subcontractors or suppliers).

## NORTH DAKOTA

**\*None**

**\*\*None**

## OHIO

**\*None**

**\*\*Ray v. Buel**, 50 Ohio App. 525 (1935) (town board of trustees could not be held liable for failure to require payment bond); **Art's Rental Equip., Inc. v. Bear Creek Constr. LLC**, 2010 Ohio Misc. LEXIS 531 (Mar. 16, 2010) (Port Authority not obligated by statute to require bonds; even if statute did require bonds, there would be no private right of action against a public entity for failure to comply with the statute).

## OKLAHOMA

**\*None**

**\*\*Boren v. Thompson & Assocs.**, 2000 OK 3 (2000) (absent an express statutory provision, a school board cannot be held liable to an unpaid subcontractor for failure to ensure that statutorily required bonds are posted; but project architect hired by town to design the project and oversee construction can be held liable to subcontractor for approving release of progress payments to prime contractor without ensuring that required bonds had been posted).

## OREGON

**\*Or. Rev. Stat. § 279C.625** (State of Oregon or the public body

and the officers authorizing the contract shall be jointly liable for the labor and materials used in the performance of the work for failure to require posting of payment bond).

**\*\*Platt Elec. Supply, Inc. v. JC Northwest, Inc.**, 159 Ore. App. 328 (1999) (public housing authority liable to unpaid subcontractor for failure to require payment bond).

## PENNSYLVANIA

**\*None**

**\*\*Cassady-Pierce Co. v. Spagnol**, 160 Pa. Commw. 666 (1993) (court will not read an implied private right of action against public entity for failure to require a bond if it is not expressly stated in the statute).

## RHODE ISLAND

**\*None**

**\*\*Accent Store Design v. Marathon House**, 674 A.2d 1223 (R.I. 1996) (public entity has no liability for failing to ensure that prime contractor posts bonds).

## SOUTH CAROLINA

**\*None**

**\*\*Shirley's Iron Works, Inc. v. City of Union**, 403 S.C. 560, 574 (2013) (unpaid subcontractor may sue city for failure to require payment bond under a third-party beneficiary breach of contract theory; city's liability is limited to unpaid contract balances at the time it received notice of subcontractor's claim; city's obligation is only to ensure that bond is posted; it is not obligated to ensure that a viable bond stays in place for the life of the project).

## SOUTH DAKOTA

**\*S.D. Codified Laws § 5-21-2** (public corporation liable to unpaid subcontractors if it fails to ensure that payment bond is posted).

**\*\*Pete Lien & Sons v. City of Pierre**, 577 N.W.2d 330 (S.D. 1998) (statute did not apply because the project was not public improvement within the scope of the bonding statute).

## TENNESSEE

**\*Tenn. Code Ann. § 12-4-202** (if any public officer, whose duty it is to award contracts, awards any contract without

requiring payment bond in compliance with § 12-4-201, such officer commits a Class C misdemeanor).

**\*\*None**

## TEXAS

**\*Tex. Gov't Code Ann. § 2253.027** (if a governmental entity fails to obtain from a prime contractor a payment bond, the entity is subject to the same liability that a surety would have if the surety had issued a payment bond and if the entity had obtained the bond).

**\*\*None**

## UTAH

**\*Utah Code Ann. § 14-1-19** (if the state or a political subdivision fails to obtain a payment bond, it shall, upon demand by a person who has furnished labor or supplied materials to the contractor or subcontractor for the work provided for in a contract subject to § 14-1-18, promptly make payment to that person).

**\*\*None**

## VERMONT

**\*None**

**\*\*None**

## VIRGINIA

**\*None**

**\*\*None**

## WASHINGTON

**\*Wash. Rev. Code § 39.08.015** (county, incorporated city or town, or other municipal corporation shall be liable to unpaid subcontractors or suppliers for failing to require prime contractor to post bond).

**\*\*None**

## WEST VIRGINIA

**\*None**

**\*\*None**

## WISCONSIN

**\*None**

**\*\*Holmen Concrete Prods. Co. v. Hardy Constr. Co.**, 2004 WI App 165 (Wis. Ct. App. 2004) (municipality liable to unpaid subcontractors for failure to require payment bond).

## WYOMING

**\*None**

**\*\*None**

**\*Express Statutory Liability for Failure to Require Bond**

**\*\*Potential Liability Addressed by Courts**

§ 995.311, which creates a streamlined process for public owners to verify the status of a surety on the website of the State Department of Insurance and provides owners a safe harbor against claims for failure to verify the sufficiency of the surety. Thus, public owners now have a simple way to verify the sufficiency of sureties, and subcontractors and

suppliers are protected against the posting of bonds by unlicensed fly-by-night sureties.

Although some jurisdictions have recognized an implied cause of action against public owners for failing to ensure that payment bonds are posted, most have declined to go so far as to conclude that the public owner has an obligation to ensure

that a valid payment bond remains in place for the life of the project. In *Flori Corp. v. Yellow Rose Development & Construction*, 911 P.2d 546 (Ariz. Ct. App. 1995), the contractor's surety entered into liquidation during the project and was unable to pay the claims of subcontractors. The court rejected the subcontractors' claims

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that the public owner was obligated to not only ensure that a bond was posted at the inception of the project, but also to require the prime contractor to post a substitute bond after its surety became insolvent.

Similarly, in *Sloan Construction Co. v. Southco Grassing, Inc.*, 395 S.C. 164 (2011), South Carolina's Supreme Court declined to hold a public owner liable for failing to ensure that a viable payment bond remained in place for the life of the project, after the surety became insolvent and entered into liquidation. The Michigan Appellate Court came to a similar conclusion, noting that, "it would be a herculean task for those governmental units which are engaged in a number of public works projects at any given time to continually check to ensure that a payment bond is still in force for each project and to determine the identity of the various subcontractors

and suppliers and to advise them of the status of the payment bond." *Barnes & Sweeney Enters v. City of Hazel Park*, 425 N.W.2d 572, 575 (Mich. 1988).

### Conclusion

Thus, although an unpaid subcontractor may, under certain circumstances, enforce its payment claims directly against a public owner for failing to ensure compliance with the bonding requirements, it is extremely unlikely that a court would find a public owner liable for failing to ensure that a viable bond remained in place through the life of the project. This, of course, poses a particular challenge to subcontractors and suppliers, who have little ability to monitor the viability of the bond during the course of the project.

Even with a potential right of recovery directly against the public owner,

a subcontractor's best course is still to obtain a copy of the payment bond prior to executing the subcontract. Depending on the jurisdiction, the subcontractor may even have an established right to receive a copy of the payment bond, either from the contracting officer or the prime contractor. If the contractor fails to make timely payments during the course of the project, the subcontractor will be in position to notify the surety on the payment bond about unpaid amounts due. Failing to be proactive about the payment bond can leave the subcontractor holding the bag. ●

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