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Mr. Andy Marr
Director
Mr. Mike Kelly
Attorney
Utah Division of Facilities Construction and Management
4315 South 2700 West, Third Floor
Taylorsville, Utah 84129

Delivered via email to: **amarr@utah.gov, mkelley@agutah.gov**

Re: Proposed Amendment to Utah Administrative Rule R23-1 – R23-1-1103, Payment and Performance Bond Requirements for Projects

Dear Director Marr and Mr. Kelly:

On behalf of the National Association of Surety Bond Producers (NASBP), a national trade association representing firms employing surety bond producers, including licensed resident and non-resident agents placing construction surety bonds in Utah, we appreciate the opportunity to provide comments regarding the proposed amendments to Rule R23-1, and specifically proposed Section R23-1-1103 governing payment and performance bonds on construction projects administered by the Utah Division of Facilities Construction and Management (DFCM). NASBP recognizes that the proposed rule implements H.B. 508, now codified at Utah Code § 63G-6a-1103, which provides DFCM discretion to require a performance bond, payment bond, when DFCM determines such protection is necessary to address financial loss or performance risk. For your consideration, NASBP's offers questions and concerns for DFCM's consideration when it decides not to require bonds.

The important protection of surety bonds; prequalification

Statutory bond requirements in the form of mandatory performance and payment bonds are defining features of public procurement at all levels for critical policy reasons—bonds provide public authorities with time-tested, professional third-party prequalification of construction companies seeking public contract awards to assure that those companies are qualified to perform contracts successfully and, in turn, the performance and payment bonds provide guarantees of contract performance and payment in the event that the awarded contractor defaults, transferring the risk of loss away from Utah taxpayers to the surety company writing the bonds.

Performance and payment bonds typically are written for 100% of the contract amount, giving the public authority up to 200% coverage in the event of contractor default. This is invaluable protection of taxpayer funds, so contractor defaults or insolvencies do not result in taxpayers having to pay substantial additional funds for completion of construction contracts. Subcontractors and suppliers providing labor and materials on public construction contracts also receive critical protection through the existence of the payment bond. Notably, on public construction projects, subcontractors and suppliers do not have mechanics' lien rights against public property. Consequently, the payment bond provides them with an important, alternative means to recover payment should the construction contractor fail to pay. Failure to have a practical recourse for payment jeopardizes the viability of these often small, local businesses.

Evaluate performance and payment bonds separately

Proposed R23-1-1103 allows DFCM to require either a performance bond or a payment bond or both, but its listed factors largely concern the difficulty of completing construction. NASBP requests that the rule directs DFCM to assess the need for each bond separately and add payment-specific factors, including the extent of subcontracted work, reliance on specialty trades and suppliers, and the contractor's payment history. NASBP respectfully recommends that DFCM revise R23-1-1103 to expressly recognize contractor capacity and qualifications in the bond-risk determination and provide a mechanism for considering contractor-specific risk before DFCM finally determines that performance and/or payment bond protection is unnecessary.

Role of Bid Bonds

The current regulatory scheme, R-23-1-1102, requires the provision of bid security, including bid bonds, for construction contracts of $100,000 or more. Bid bonds function to ensure a qualified pool of bidders, as sureties undertake careful and substantial evaluation of potential bidders to determine their wherewithal to perform the particular contract. Furnishing the bid bond gives the project owner assurance that the bidder is qualified and that the bidder, if successful, will honor the bid price, enter the contract, and supply performance and payment bonds.

The regulation does not address circumstances in which bid bonds are required but final performance and payment bonds are not. In such circumstances, bid security other than bid bonds should be employed, as among the essential purposes of the bid bond is to backstop the delivery of the final bonds, which are not being required.

R-23-1-1103(1)(3)—Determination

DFCM may require performance and payment bonds based on several factors, including complexity of scope, DFCM's familiarity with the project type, regional conditions, site characteristics, procurement and construction-management methods, funding sources, and project budget. However, if bonds are not required by DFCM, what analysis will it use to determine if a contractor has the financial wherewithal and capacity to perform to ensure taxpayers and subcontractors are protected in the event of contractor default? Surety underwriting provides an independent assessment of these considerations. Consequently, bonding provides DFCM with more than a source of financial recovery following contractor default; it also provides an independent prequalification mechanism designed to evaluate whether a contractor has the capacity to perform the bonded obligation. That prequalification is comprehensive in nature, focusing on the contractor's character, capacity, and capital, and goes well beyond DFCM's stated project factors, examining carefully even the contractor's overall program.

R-23-1-1103(3)(a)—Complexity of scope

NASBP is concerned that "complexity of scope" is not defined sufficiently or accompanied by specific, objective criteria in the proposed rule. Almost all construction projects, especially new and renovation projects, are inherently complex, as they involve unique owner requirements, different mixes of constructing parties, multipart contractual requirements, intricate schedules, changing site conditions, changing supply chains, among many other variables. No two projects are alike, and few construction projects should be considered "simple." A relatively small project can involve difficult phasing, specialized systems, occupied facilities, multiple trades, accelerated schedules, or significant subcontractor coordination, and higher-dollar, straight forward projects may involve both complexity and scale that poses substantial performance risk to the public owner and taxpayers in the event of default. Therefore, employing "complexity" as a determinant without specific defined criteria likely will produce inconsistent bonding decisions. Such inconsistent decisions ultimately do not provide uniform protection to the State and do not provide decisional uniformity for the construction community seeking to understand the risk environment of DFCM administered projects. Without published objective standards for determining complexity, contractors, subcontractors, and suppliers cannot readily anticipate which future DFCM projects will be bonded.

R23-1-1103(4)—Written decision prior to bid solicitation

Proposed R23-1-1103(4) appropriately requires a written decision prior to bid solicitation if the director will require performance and payment bonds. Given the inherent complexity of most construction projects and the need to protect the financial interests of the State of Utah and its taxpayers, NASBP requests that the director make written bonding determinations for construction procurements as the rule, with few exceptions. NASBP requests that the proposed rule incorporate greater transparency by requiring the director to identify the means by which the State will be protected from financial loss, explain the factors influencing the decision on each bond, and retain the written determination in the project file for public purview.

Each construction solicitation also should state plainly whether bid security, a performance bond, and a payment bond are required, and specify their respective amounts. That information allows bidders to obtain accurate terms and alerts subcontractors and suppliers the status of payment bond protection before they commit to the project.

Section 14-1-19—subcontractors' risk of exposure

Section 14-1-19 makes a public agency liable to unpaid subcontractors when that agency fails to obtain a required payment bond. The enactment of HB 508, (subsection 5), however, removes DFCM from having any liability for not requiring a payment bond. As the only construction procuring state agency to be exempt from such liability, DFCM's advance notice to prospective subcontractors and suppliers on the status of payment bond protection on their construction projects is even more critical.

U.S. Treasury listed sureties

Finally, when DFCM determines that bonds are warranted, proposed subsection (5) provides meaningful safeguards by requiring the surety to be authorized to do business in Utah and listed in U.S. Department of the Treasury Circular 570, subject to the specified bonding amount requirement. The provision also appropriately prohibits DFCM from directing a contractor to obtain its bonds from a particular surety company, producer, agent, or broker. NASBP supports maintaining these protections.

NASBP would welcome the opportunity to discuss these recommendations with DFCM. Thank you for considering our comments.

Sincerely,



Larry LeClair
Director, Government Relations