

# THE BOTTOM LINE



Atlantic

Coverage

Corp.



EXCELLENCE IN SURETY BONDS

4th Quarter

2001

Volume 3, Issue 4

## Why Should I Bond Back Subs??

The bonding of subcontractors has been a common practice in the surety industry for many years. However, in the recent past, bonding companies had become lax in requesting this. As all of you know these requests are resurfacing on a daily basis. Every time we speak to a contractor about bonding back his subcontractors, we are faced with the same question, "Why Should I Bond Back My Subs?" This article will hopefully provide you with answers to this simple question.

Many prime contractors refer to bonding back subcontractors as "double bonding", however this is truly not the case. The bonds that the prime contractor provides to the owner are for the owner's protection. These bonds protect the owner when the prime contractor defaults. Prime contractors can get defaulted for various reasons, many times it is because of problems caused by their subcontractors. Without a subcontractor bond, the prime contractor is basically rolling the dice that its subcontractors will complete their work without a problem and pay all of their bills, thus making the prime contractor act as the surety.

There are four points that need to be discussed when talking about subcontractor bonds:

1. Prequalification
2. Risk transfer
3. More Surety Credit
4. Costs

Prime contractors know how much they can handle at any one time and have proved this on a daily basis to various owners and/or sureties. However, what prequalification do you perform before letting your subcontractor begin working for you? Many prime contractors do not have the trained staff, nor the money to devote to pre-qualifying subcontractors. By requesting a bond back from your subcontractors, you can be sure that a surety company is reviewing their payment history, financial statements and overall workload which will help determine whether these subcontractors have the capacity to complete your project.

When you receive a subcontractor bond, you are reducing your company's overall risk. Most contractors utilize various techniques to monitor

and control their subcontractors' performance, including withholding retainage and the use of payment affidavits. However, what happens if your subcontractors sub work out to other contractors? You as the prime contractor are ultimately responsible. Disputes between subs and suppliers or second tier subcontractors can result in liens being filed on your project. Once a lien is filed, it is the prime contractor's responsibility to bond back the lien which will ultimately increase your overall costs. By having the subcontractors bonded, any disputes between your subs and their subs or suppliers will have minimal affect on your business.

Bonding companies have taken bonds back on subcontractors into consideration when looking at the prime contractors' overall workload. When a contractor is pushing its limit in terms of total workload, many sureties will consider additional surety credit, in excess of normal limits if there are subcontractors bonded back. The reason for this is that the contractor's liability has been reduced. It is not however dollar for dollar. For example, if you received \$5,000,000 in bond backs, your bonding aggregate would not increase \$5,000,000 because the prime contractor is still ultimately responsible to the owner on the project.

One of the more common questions that we are faced with everyday is "Why doesn't bonding back a subcontractor reduce my bond premium?" Ultimately, your bonding company still has the exposure, hence the reason for the premium remaining the same. Many prime contractors complain that bonding subcontractors / suppliers will increase their costs. This unfortunately is true, however compared to other risk transfer mechanisms, subcontractor bonds are inexpensive. Responsible prime contractors would not permit their subcontractors on a project without their insurance. By requesting subcontractor bonds, you are basically rounding out the protection offered by these insurance coverages with the performance and payment guarantees.

After reading this article, we hope you will see that bonding back subcontractors should be implemented into your organization immediately.

### "Famous Quotes"

*"To be a champ you  
have to believe in  
yourself when no-  
body else will"*

*Sugar Ray Robinson*

*"Life is like riding a  
bicycle. You don't  
fall off unless you  
stop pedaling."*

*Claude Pepper*

*"Just when you  
think you've gradu-  
ated from the  
school of experi-  
ence, someone  
thinks up a new  
course."*

*May H. Waldrip*

*"The moment may  
be temporary, but  
the memory is for-  
ever."*

*Bud Meyer*

*"A man who does-  
n't stand for some-  
thing will fall for  
anything."*

*Peter Marshall*

## What Does It Take To Make Your Management Team Effective?

*"Probably nothing in the world arouses more false hopes than the first four hours of a diet."*

**Dan Bennett**

*"My interest is in the future...because I'm going to spend the rest of my life there."*

**Charles Kettering**

*"Sometimes the road less traveled is less traveled for a reason."*

**Jerry Seinfeld**

*"I'm opposed to millionaires, but it would be dangerous to offer me the position."*

**Mark Twain**

*"It's easy to get good players. Getting em to play together, that's the hard part."*

**Casey Stengel**

*"Enjoy the little things, for one day you may look back and realize they were the big things."*

**Robert Brault**

*"When we seek to discover the best in others, we somehow bring out the best in ourselves."*

**William Arthur Ward**

*"Changes starts when someone sees the next step."*

**William Drayton**

What makes some Managers effective leaders? This is a question that every officer, supervisor, project manager and department head should ask themselves. Individuals in these key positions bring many broad skills to their companies. An effective manager, however, must also bring leadership skills.

Key skills that can help a leader to be more effective include:

1. Set and Communicate a Vision
2. Know Your Team
3. Help the Team to "Buy-In" to the Vision
4. Understand What Motivates the Team
5. Maintain Accountability

When setting a vision it should not be just a string of words on a plaque or on the front of a company brochure. An effective leader must add meaning and purpose to the day's routine tasks. People need a sense of importance in their work. Knowing how to do each task is usually not enough to keep a worker satisfied. An understanding of the company's vision and how each person plays a part in realizing the company's goals can create a sense of personal worth. Too many people spend too much time just getting through their day. Excellent leaders help workers see the meaning of it all.

It is important for a company to set goals and establish a vision. Paint a picture of some desired future goals - both short and long term. Determine how to close the gaps between the way things are and the way they could be.

Does your company have core values? Are they explicitly communicated to the staff? Clear visions come out of an understanding of the company's core values.

Communication of the company's vision is crucial for an effective leader. Establishing a vision and not sharing it with those that can make it a reality, is as bad as not having a vision at all. Many leaders undermine their effectiveness because they are unaware of some basic communication skills. Words only make up a small percentage of the communication package. Attitude will override most spoken words. Focus on being positive. The tendency to see the negative or to be 'realistic' can effect the drive and energy of an effective team.

Listen, listen and then listen some more. Effective leaders really listen in order to

develop trust and a feeling of caring. A leader will never tap the creativity and energy of it workers without their trust.

Know your team. One of the keys to this skill is to know each person's strengths and weaknesses. Use their strengths to the advantage of the group and help them to improve on their weaknesses. There are many types of programs available to help the effective leader better understand what motivates each team member.

Take time with your team. Good leaders do not assume that all members will be motivated by the same things that motivate them.

Leaders must create an environment that boosts team building. Schedule a few social events - company picnics, holiday parties, etc. Real team building, however, comes from participation of each team member in problem solving, creating and celebrating successes.

Keep the team informed. Team members like being kept up to date on significant company events, both good and bad. When the teams are not informed, they feel left out and unimportant to the company. Workers do not work in a vacuum. Rumors abound throughout all companies. Even when having to impart bad news, remember a person's speculations and imagination is sometimes worse than the actual news.

'Buy-In' is critical in developing and implementing an effective vision. Executives must resist the temptation to define the company's vision on their own. Involvement of the entire team in the drafting of the vision or mission statement helps drive ownership and acceptance. Good leaders take the time to get feedback. Have meetings that allow open discussions. Involve all members that are responsible for making the vision a reality. The members that are doing the work on a daily basis are sometimes the most important members of the team. Their input is invaluable. Since they are the ones doing the job, their suggestions on how to implement the vision usually will be the most important. This technique is a quality practice that is effective. Leaders that create a structure where all decisions must go through them leave an impression with the team that they really don't have a say in major decisions.

If the team members' input is incorporated in the vision, it is more likely that

continues on page 3

## “The Three C’s of Suretyship”

Surety underwriting involves the analysis of a risk and making a decision as to its surety creditworthiness. Surety Bond Analysts will generally look for three qualities when analyzing a prospective contractor client. These three qualities have traditionally been referred to as the “three C’s”, and are also very basic to commercial credit transactions.

The three C’s of suretyship are:

- *Character*
- *Capacity*
- *Capital*

The first, *Character*, is indispensable. In underwriting, the character of the contractor client is defined as the moral and ethical attributes distinguishing the attitude and conduct of that particular client. An underwriter’s primary responsibility is to assess and understand the character of the contractor client through personal interviews and investigation. Character is measured by honesty, truthfulness, integrity, and cooperation and is critical to the relationship between the agent, contractor and bonding company.

The second, *Capacity*, requires that the contractor have the necessary skill or ability to perform the contract or obligation undertaken. The capacity of the contractor is not limited to the capabilities and talent of the owner of the construction entity but extends to everyone within the company. The bond underwriter will determine if the company is sufficiently staffed and capable of managing

the volume of work being performed. Are there enough experienced project managers and job superintendents available to run the projects? Review of resumes of key employees and conducting reference checks on the company’s completed contracts are important in measuring the capacity of the contractor client. Determining the level of capacity is especially important when underwriting contractors seeking to secure bond credit for jobs that are larger than normally assumed.

The third, *Capital*, determines whether the financial condition of the contractor justifies the approval of the risk. In times of economic stress, when the construction industry may be directly or indirectly affected, it becomes increasingly more important to consider the underwriting factors surrounding capital. This is especially evident during the hard surety market that agents and contractors are currently experiencing. A contractor’s capital is underwritten using CPA prepared financial statements, copies of corporate and personal bank statements, and credit surveys conducted with the company’s bank and vendors. Capital represents the level of financial resources available to the contractor required for covering overhead expenses and financing the start-up of new contracts.

The three C’s of suretyship is the foundation of the surety bond underwriting process.

## What Does It Take To Make Your Management Team Effective?

everyone will feel their worth.

Understand what motivates. Highly motivated people produce more over the long run. External motivational methods such as compensation, prizes and recognition do work, but have a relatively brief impact on changing behavior.

Internal motivational methods seem to endure longer. The trust, confidence and sincere appreciation leaders communicate to the staff are a driving force in itself. Self motivation occurs when a worker develops a sense of ownership. Workers should feel empowered, not powerless. By giving workers decision making responsibility and making them accountable for measurable results, they will realize the importance of their job and build an understanding of the way the

leader runs his/her business.

Accountability must be maintained. When workers do not perform as expected, communicate this immediately. Failure to act is self-destructive. Coaching is a one-on-one process. Unless the non-performer understands that a problem exists and what the problem is, no amount of talking will correct the problem.

One of a leaders most powerful tools is excellent coaching and mentoring. A good leader will work on honing these skills by practicing them regularly. A successful leader understands that his job is to help other people to be successful.

Remember, you are only as strong as your weakest link.

*“The best wood in most amateurs’ bags is the pencil.”*

*Chi Chi Rodriguez*

*“Yesterday is but today’s memory, and tomorrow is today’s dream.”*

*Kahlil Gibran*

*“I am not in this world to live up to other people’s expectations, nor do I feel that the world must live up to mine.”*

*Fritz Perls*

*“Sometimes I think the surest sign that intelligent life exists elsewhere in the universal is that none of it has tried to contact us.”*

*Calvin & Hobbes*

*“Vision without action is a day-dream. Action without vision is a nightmare.”*

*Japanese Proverb*

*“Win and they carry you to the clubhouse on their shoulders. Lose and you pay the caddy in the dark.”*

*Gene Sarazen*

*“Today’s greatest labor-saving device is tomorrow.”*

*Tom Wilson*

## Can We Help Someone You Know With Their Bonding?

If you think we can help someone you know with their bonding needs, please call us at (516) 682-5000. These referrals fuel Atlantic Coverage Corp.'s growth and success.

### Amwest Declared Insolvent

On June 7, 2001, a Lancaster (NE) District Court Judge issued an order for the liquidation of Amwest Surety Insurance Company. Based in Calabasa, CA, Amwest is domiciled in Nebraska. The liquidation order was a result of a finding of insolvency by the director of Nebraska's Department of Insurance. For further information, contact:

1. Claimant Services toll free number: (866) 789-8119
2. Amwest website address: [www.amwest.com](http://www.amwest.com)
3. Nebraska Department of Insurance website address: [www.nol.org/home/ndoi](http://www.nol.org/home/ndoi)

It has happened before, however it is highly unusual for a major nationwide surety company, ranked by A.M. Best as the 10th largest company in 2000 among top surety writers, to be declared insolvent and have insufficient funds to meet its obligations. A question that has been asked is regarding if a claim can be filed against an Amwest bond?

For the most part, the bond claimant will probably not be able to recover against Amwest. Amwest has advised all policyholders, principals, obligees, and surety bond producers associated with its company that because of the Order of Liquidation, Amwest "will no longer defend or pay for the defense of its insureds and principals and, therefore, any insured or principal residing in such a situation should make arrangements to employ independent counsel to defend against any legal action which would otherwise be covered under an Amwest policy or bond."

### ACC Reaches Another Milestone

Thanks for 5 years!!! October 2001 marks a milestone for Atlantic Coverage Corp. It marks our 5th year in business. And while we're celebrating, we'd like to share the accolades with you, our Customers. For it has been your business and referrals that have helped us grow. We look forward to many more years of servicing you and your company's bonding needs.

### Letter from the Editorial Staff

This newsletter is designed with our readers in mind. All inquires and ideas regarding this or future newsletters are appreciated. Please send all inquires to me at [anthony@esuretybond.com](mailto:anthony@esuretybond.com). If you know anyone who you feel would like a copy of our newsletter, please let us know so that we can include them in our mailing list. Please let us know if you would like to receive this newsletter via e-mail.

### Disclosure

The Bottom Line is published quarterly by Atlantic Coverage Corp., 6800 Jericho Tpke., Suite 212E, Syosset, NY 11791. Telephone (516) 682-5000. A service for our clients, contacts and friends, it is meant to provide useful business information and practical advice and encourage its readers to keep up with all the latest developments. These articles are not intended to provide a complete discussion of the subjects presented. Because each situation is unique, we advise you to contact us before acting upon any of the following information or planning ideas contained in this newsletter. Any questions you might have about any topics mentioned in this newsletter, please contact our office.

**Atlantic Coverage Corp.**  
**6800 Jericho Turnpike**  
**Suite 212E**  
**Syosset, NY 11791**

[To Return To esuretybond.com, Click Here](http://esuretybond.com)

[To View Last Quarter's Newsletter, Click Here](#)

[To View The Bottom Line Archives, Click Here](#)