

COMMUNICATION & SURETY CLAIMS

A Surety Can Help a Contractor Get Back on Track

BY TIMOTHY MIKOLAJEWSKI

One of the critical elements needed to establish and maintain a solid surety relationship is open communication. This is not only essential when times are going well, but also when times are not going as planned.

How a contractor handles the impact of a bad project or a bad year often determines whether a business will survive or fail. Because getting new work is usually critical to working through problems, maintaining a strong surety relationship is essential.

No one relishes delivering bad news. When contractors get into trouble, sometimes they tend to wait too long to let their surety know of the situation. As a result, when the surety becomes aware of the problems, many of the options available to handle those problems no longer exist. On the other hand, if the surety learns of a problem early on, it likely will have resources available to assist in solving the issue.

Most surety companies in the industry today have been around a long time. Because surety is a very specialized industry, most tenured professionals in the business have developed a significant amount of experience entailing both positive and negative situations with contractors.

As a result of having dealt with negative experiences over the years, a surety typically does not overreact to bad news. Rather, the surety works closely with the contractor to develop strategies to overcome any problems and get back on track. The earlier problems are communicated, the more likely they will be solved and the faster the contractor will be back on track.

Contractors do not want to communicate bad news for two reasons. One is a sense of optimism that other work will offset the bad job. Thus, when discussing the bad project with the surety, the overall impact could already be in the past.

Another is the perception that the surety will overreact and suspend surety support, or that a surety's claims operation will have to get involved. Obviously, these two outcomes are not ones a contractor looks forward to. However, being in a surety claims department does not necessarily mean a contractor has or will cause a surety a loss. In fact, a vast majority of activity in a surety's claims operation is related to issues involving solvent contractors that are getting continued support from the surety's underwriting team.

Surety claims fall into three basic categories. The first category involves a situation where a solid contractor has a legitimate dispute with an owner, a subcontractor or a supplier. Typically the dollar amounts are small and the ultimate outcome will be a settlement handled between the parties involved, with the claim resolved relatively quickly. Generally, this will involve very little activity on the part of a surety claims operation.

The second category of claims is much more serious, but the surety still does not expect an ultimate loss. These types of claims can be time-consuming and typically involve a great deal of interaction among the contractor, the surety claims operation and the underwriting team. Contractors that end up with claims in this category generally are experiencing problems with one job rather than having systematic problems. One project might have significant changed conditions, a difficult owner or poor design. While the contractor has the technical ability to complete the project, the cash drain is such that the contractor cannot complete the job without financial assistance.

A common thread in these situations is a strong claims case against the owner where the contractor can recover considerable money in a reasonably short period of time.

The combination of this recovery and new work supported by the surety results in the contractor working its way out of the problem and getting back to normal business.

The above situation features one of the hidden values a project owner gets from a surety bond. The contractor's work with a particular owner or owners may be going along quite well. The owner would be surprised if the contractor said it could not finish the project. With the surety's assistance, the contractor can keep all work on track toward completion, honoring all obligations to owners, suppliers and subcontractors. Obviously, the contractor benefits by being able to continue in business rebuilding financial strength and making the surety whole. Communication is vitally important if a contractor and surety end up in this type of claims situation.

The third category of claims situations involves the contractor being unable to complete the work, thus needing the surety. When the situation gets this dire, it is difficult for the surety not to lose money. With considerable cooperation from the contractor, the loss to the surety has a good chance of being substantially mitigated. Hopefully, when a problem arises, early communication and cooperation between the contractor and surety can help avoid this scenario completely.

Open communication and cooperation provide tremendous benefits for all involved in the project—not just in claims situations. The owner receives qualified contractors to bid the work competitively, thus getting the best value for the project. The subcontractors and suppliers on the project receive payment bond coverage guaranteeing that if they are legitimately owed money they will be paid. The surety generates profitable premiums by writing the bond—giving financially sound surety companies the motivation to stay in the business and maintain a competitive surety climate.

And finally, the contractor maximizes its surety credit, allowing it to take advantage of opportunities to grow its business.

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