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SHOULD SUBCONTRACTOR DEFAULT INSURANCE REPLACE TRADE CONTRACTOR SURETY BONDS FOR MASSACHUSETTS PUBLIC WORK?

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I. EXISTING LAW.

The Construction Manager at Risk (CMR, referring in this article as to both the construction manager at risk program and to individual construction managers at risk) procurement system was originally enacted into law in 2004. This system can be used for the construction, reconstruction, installation, demolition, maintenance or repair of any building estimated to cost not less than $5,000,000. Approval for each such procurement has to be obtained from the Inspector General.

Under the CMR procurement method, as stated by MGL C. 149A, s. 2:

> " "Construction management at risk" or "Construction management at risk services" or "Construction management at risk delivery method", a construction method wherein a construction management at risk firm provides a range of preconstruction services and construction management services which may include cost estimation and consultation regarding the design of the building project, the preparation and coordination of bid packages, scheduling, cost control, and value engineering, acting as the general contractor during the construction, detailing the trade contractor scope of work, holding the trade contracts and other subcontracts, prequalifying and evaluating trade contractors and subcontractors, and providing management and construction services, all at a guaranteed maximum price, which shall represent the maximum amount to be paid by the public agency for the building project, including the cost of the work, the general conditions and the fee payable to the construction management at risk firm."

Under this system, 'Trade Contractors' are roughly analogous to filed subbidders in plans and specifications public procurements. Each Trade Contractor (TC or subcontractor) has to supply 100% surety bonds, the premium of which is included in the Trade Contractor's bid and contract. Since subcontractors are referred to as 'subcontractors' other than in the CMR program and referred to as 'trade contractors' under the CMR program, for this article, both shall be referred to as 'subcontractors', a more familiar term.

Per plans and specifications public works projects (MGL C. 30, s. 39M) and public building projects (MGL C. 149, s. 44A-H) and CMR projects (MGL c. 149A) are based on the model that the general contractor will have both a payment bond and a performance bond. And, a 'Construction Manager at Risk' also must have both a payment bond and a performance bond.

Second tier subcontractors and material suppliers may make claim against the general contractor's payment bond for all three construction models referenced above. In many cases, the bonds supplied by filed subbidders and Trade Contractors will also permit second tier subcontractors and material suppliers to make claim against them even though that exceeds the requirements of MGL C. 149, s.44F. This is because sureties tend not to 'manuscript' (create) custom bond forms for specific situations within specific states, using, rather, their existing form or generally-accepted payment bond forms such as the AIA 311 and the AIA 312, which may provide greater coverage than the law requires.

While a general contractor can declare a subcontractor in material breach of its subcontract, the subcontractor will be entitled to litigate that issue in court or arbitration. And, with regard to all of the surety bonds referenced above - both payment and performance - the surety is not under an obligation to perform until it is determined that its principal has defaulted on its contract.

II. THERE IS A BILL PENDING BEFORE THE MASSACHUSETTS LEGISLATURE WHICH, IF PASSED, WOULD ALLOW CONSTRUCTION MANAGERS AT RISK TO SUBSTITUTE SUBCONTRACTOR DEFAULT INSURANCE FOR SURETY BONDS.

There is a bill pending before the Legislature – House Bill 1702 – which would allow CMRS the right to choose between having surety bonds or having subcontractor default insurance (SDI) for Trade Contractors. (If you would like to see a copy of this bill, email me and we'll send it to you.) There was a similar bill introduced during the 2015-2016 session, which was not passed.

There was a committee meeting on this bill in June of 2017 in which various persons spoke in favor of this bill and against this bill. Speaking against this program included knowledgeable surety bond producers such as Michael Regan from Boston. The bill is solely involved with the CMR program, which involves a CMR as the general contractor and trade contractors as the subcontractors. For the ease of convenience in this Squib, CMRS may be referred to as general contractors because this is a more familiar term and other than for the CMR program in Massachusetts, this program is employed elsewhere with general contractors and subcontractors. But, this bill is solely limited to MGL. C. 149A, the CMR program, in which the party in the position of a general contractor is the CMR and the party in the position of the subcontractor is the trade contractor.

This bill provides that as an alternative to subcontractor payment and performance bonds, the constrruction manager at risk firm shall have the option to obtain a subcontractor default insurance policy in lieu of bonds for some or all of the trade contractors. The intention to use such a program shall be made known by the construction manager at risk and awarding authority after the receipt of trade contractor bids. If a trade contractor is not covered by the SDI policy, then that trade contractor must provide payment and performance bonds. For those trade

contractors bidders that are included in such a program, they shall pay to the CMR a credit equivalent to the anticipated bonding costs which they included in their bids.

The purpose of this Squib will be to help define what SDI is (and isn't) looking at the advantages and disadvantages of this form of project model, as well as its suitability with regard to Massachusetts public work.

I wish to point out that most bills in the Legislature become effective - enforceable laws - ninety days from the date they are passed. This bill has no accompanying regulations or any other guidelines as to how general contractors are to prequalify subcontractors to participate in the SDI program, which prequalification is a significant element of this program. Nor has any public agency been referenced as some kind of referee or governing body for the protection of subcontractor interests for those participating in this program.

III. CONTRACT SURETY BONDS: WHAT THEY ARE.

One definition of contract surety bonds (payment and performance bonds) is that they are "an extension of unsecured credit." For individuals and companies seeking to be bonded, there are a great many similiarities between what the bank requires from its borrowers before granting a loan and what sureties require from its principals prior to issuing bonds.

Surety bonds are not, actually, insurance products. This for is many reasons. We'll discuss two of the differences: (A) Indemnity; (B) Fault on the part of the principal. By comparison, payment under most insurance policies require no indemnity by the insured of the insurer (absent fraud) and are not necessarily exclusively based on the fault (or lack of fault) on the part of the insured.

The principal ('principal' is the equivalent of 'insured' in surety-speak) is generally liable to the surety (the insurance company) to reimburse the surety for any loss payments (monies paid to claimants) and expense payments (monies paid to lawyers, appraisers, accountants, etc. hired by the surety to assist it with claims). With insurance, the insured, generally speaking does not have to repay the insurance company for loss and expense payments. Whether or not the insured contributed to the event or solely caused the event is not exclusively relevant irrelevant because with regard to the insured, some insurances are "no fault", such as certain automobile coverages.

Surety companies will always be looking for repayment of any monies they expend as the result of having executed for a principal surety bonds, even when the principal was right and not at fault. These obligations are usually stated in a general indemnity agreement executed by the principal and by individual indemnitors before the surety line is established.. Insurance has no such requirement.

Generally speaking - and, greatly simplified - contract bonds (payment and performance bonds) are dependent on a determination of who is at fault. A performance bond provides

something in the nature of a guarantee that a project will actually get finished by the surety if a principal fails to meet its obligations under a construction contract. A payment bond provides something in the nature of a guarantee that if the principal doesn't pay subcontractors, material suppliers and equipment suppliers, the surety will.

But, for either of these obligations arise, the principal usually must be in a state of 'default' (except for second tier claims against the general contractor's payment bond.) Namely, it can be proved that the principal has clearly breached some obligation of the contract. For a performance bond, this could be not completing the contract work in compliance with the terms of the contract. For a payment bond, it would have to be clear that the principal is in breach of some payment provision in a subcontract or material purchase order.

The surety is not under an obligation to perform under either its performance bond or payment bond until it has made its own investigation and determination of its principal's default. This can take quite a period of time and, in reality, many sureties don't actually make much of an investigation. This requires the general contractor to fund completion of a defaulted subcontractor's performance out of whatever monies remain in the subcontractor's account and using its own monies. On a Massachusetts public project, subcontractors and sub-subcontractors and material suppliers and second tier material suppliers can seek payment for their claims from the general contractor's payment bond, which includes a reasonable attorneys' fee provision. Then, the general contractor will submit a claim to the subcontractor's surety, which the surety might pay as a claim or might only pay after litigation is initiated.

Soime protection is given to the general contractor due to the provisions of MGL C. l76D (3) (9) which defines what constitute unfair insurance claims settlement practices, which can include not having a reasonable claim investigation process and refusing to pay when liability is reasonably clear. Such violations can be MGL C. 93A, s. 11 violations under which the surety might have to pay double or triple damages and the general contractor's attorneys' fees. Statutes such as this should always be brought to the attention of the surety if your claims situation warrants it, as, otherwise, the surety may not be aware of their existence.

Does this mean that with bond claims there necessarily will be litigation (a lawsuit)?

The answer to that is 'maybe, maybe not'. As between payment bond claims and performance bond claims, sureties want to get on top of the performance bond claims as quickly as possible, as it is with performance bond claims that there is the possibility of much larger claims and ultimate payments than with payment bond claims. More than half of the contract bonds sold by sureties are on public projects. To the extent reasonably possible, sureties want to properly service obligees (the beneficiary of the bond, which with a general contractor will be the owner).

Sureties generally don't generally want obligees to complete the work under a performance bond claim without the surety's knowledge and participation because this will almost always cost more than what the surety could have completed the project for. Additionally, from a purely practical standpoint, sureties are much more concerned with claims

against them for bad faith as filed by owners against their performance bonds than they are for such claims as filed by individual payment bond claimants. Massachusetts is a very pro-consumer and anti-insurance company state. I represented a surety that was literally thrown out of Massachusetts with a fine of one million dollars, not because of how they handled surety bond claims but as to how they handled claims relating to taxi insurance.

Payment bonds may be more problematic in terms of grabbing the surety's attention, as most sureties have a greater concern for performance bond claims than they do for payment bond claims. Their first and greater efforts are with performance bond claims.

But, we are talking public work here and any claims by first and second tier subcontractors and material suppliers against the general contractor and its surety are subject to the provisions of C. 149, s. 29, which provides for the payment of attorneys' fees to successful claimants. And, given that it takes five years for a case to come to trial in the superior court and that there is an interest factor of 12% per year, sureties don't want to be dealing with the possibility of a 60% interest payment plus the attorneys' fees in addition to whatever the judgment is.

But, it is to be noted that a surety will not be making payments unless it believes its principal to have materially breached its contract. Fault is a key issue in surety claims, while often irrelevant or less relevant with many kinds of insurance claims.

Also, vis a vis claimants, there are no self-insured retention or deductibles or co-pays on surety claims. The claimant gets what the claimant is entitled to so that the claimant has 'first dollar' rights meaning, if appropriate, the claimant will recover the entire amount of its claim. And, since principals need to keep their sureties happy to get future payment and performance bonds, there is an incentive for principals to properly perform once claims have been made.[2] If the necessity for future bonds doesn't convince principals to honor their obligations, the fact that sureties have indemnity rights against the principal and its individual indemnitors to be reimbursed for every dollar the surety expends, whether as 'expense' payments to attorneys, consultants, accountants, construction managers or as'loss' payments by paying a claimant's claim should catch the principal's attention. Most indemnity agreements provide that the surety doesn't need the principal's acquiesence or permission to pay a claim. And, the obligation to indemnify is total, meaning that the surety has to be indemnified even if the principal was right on a claim and the claimant did not prevail.

Sureties prequalify bidders, usually well before that bidder is submitting bids, by studying their audited financial statements and reviewing the principal's performance under prior contracts. And, since filed subbidders have to be in a position to provide bonds if the general contractor requests them on MGL C. 149, s. 44A-H projects and where all trade contractors have to supply bonds as a contractual obligation pursuant to MGL C. 149A, s. 8, bidders have to have a surety line all set up before they submit bids. There won't be any lag time in providing the payment and performance bonds due to having the surety evaluate its principals' suitability for bonding because this has already been done.

If a principal gets terminated under a contract for fault, it has the immediate right of pursuing dispute resolution procedures challenging the termination for default. So, that if the subcontractor was unfairly terminated, it might be entitled to damages.

Advantages for using surety bonds to secure a general contractor's and a subcontractor's performance include:

(1) A general contractor will not default a subcontractor lightly. Wrongful termination can expose general contractors to subcontractor claims for lost proftits.
(2) There is first dollar coverage - no deductibles or co-pays. What this simply means is that a valid claim for ten thousand dollars will be paid ten thousand dollars. And, with some exceptions, generally speaking, the amount of payment and performance bonds for Massachusetts public work will be sufficient to entirely deal with the amount of the claims made against them.
(3) Also, compensated, commercial surety products have been around for one hundered and thirty years or so. There are literally thousands of legal cases interpreting the rights and obligations of bond principals, sureties, obligees and claimants. This causes people to understand before trouble arises what their rights and obligations will be and to understand after the trouble arises what their rights and obligations will be.
(4) Subcontractors are typically prequalified by public authorities as to what size jobs and trades the subcontractors can bid well before any bids are submitted.
(5) Surety bonds lines are also established outside of the time parameters of dealing with specific bids, meaning that the evaluation of future principals is not under some time pressure during the contract bidding and award phases.
(6) A surety's qualifying a company for various single project and aggregate bond limits is the traditional way of prequalifying contractors to particpate in the bidding process. And since the surety is a third party to the construction process - neither a subcontractor nor a general contractor - it has a certain amount of independence and neutrality.
(7) Subcontractors contesting default have the right to litigate whether or not any particular default is justified.
(8) And, of course, a subcontractor's performance and payment bonds provide some protection to their obligee (the general contractor) if the subcontractor refuses to or is unable to perform.
(9) In the public scheme of construction, second tier subcontractors and material suppliers will have the right to make claim against the general contractor's payment bond. And, while the staated purpose of a filed subbidders's payment and performance bonds is to protect the general contractor and its surety, typically, sureties do not 'manuscript' (write state specific) bonds. One of the results of this is that using industry standard forms, frequently, the second tier subcontractor and material suppppliers will also be able to make claim on the subcontractor's payment bond. Since claims by second tiers are easier against subcontractor bonds - fewer (or no) notice provisions and a longer statute of limitations (the time within suit has to be filed) than as to the general contractor's payment bond, the subcontractor's bond can often be the only bond against which a second tier can make claim.
(10) As things presently stand, all of the public construction models discussed herein are exclusively set up to being serviced by surety bonds only.
(11) On the lighter side, bonds have been around for a very long time. I once had an insurance agent who had enjoyed his lunch - olives and very small onions doubtlessly involved - a bit too

much call me up and tell me about the six specific prohibitions against suretyship which are in the book of Proverbs in the Bible! One example is Proverbs 11:15 KJV: “He that is surety for a stranger shall smart [for it]: and he that hateth suretiship is sure.” Several decades of living have taught me that it is not usually a good strategy to go against the wishes of the Big Guy! For some reason, he *always* knows best!

Disadvantages of surety bonds include:

(1) Frequently, there is some delay on the part of a subcontractor’s performance bond surety before it decides whether or not it will act on a general contractor’s performance bond claim.
(2) This can have general contractors incurring the costs of what should be secured by the performance bond until such time as the subcontractor’s surety accepts responsibility.
(3) Particularly with payment bond claims, many sureties, unfortunately, are not willing to settle claims as claims but only settle them as litigations (law suits).
(4) Subcontractors without bonding lines may be kept from bidding on public work, particularly with regard to filed subbidders and trade contractors, both of which must be bondable.
(5) There might be a method as to the completion of the defaulted subcontractor’s work spelled out in the bond which becomes less feasible or more costly as a particular job progresses. Under SDI, the general contractor itself unilaterally determines the method for the completion of the defaulted subcontractor’s work.

IV. SUBCONTRACTOR DEFAULT INSURANCE (SDI): WHAT IS IT.

This is a product originated by Zurich Insurance in 1996. There are no more than four or five insurers who currently offer or have offered similar products but the number of sureties providing payment and performance bonds in Massachusetts is at least in the dozens, possibly higher.

Now, my research into SDI found that it was hard to obtain copies of specimen SDI policies. Rather, the literature is from various parties involved in the construction process discussing it, such as those involved in the insurance industry and various lawyers. Therefore, the following is a generalization of SDI concepts, which may not have application to any specific SDI program but is only intended to provide a basic idea as to this kind of insurance product.

1. This is insurance, not a surety product. Whereas a surety bond typically has three parties - principal, obligee and claimant - this product essentially has two parties - the insurance company and the general contractor.

2. This generally will apply to only very large general contractors who have very large sales volumes with subcontractors. The literature says this volume might be between fifty and seventy-five million dollars of subcontractor volume or more in a year. One would think that with regard to the general contractors currently working in Massachusetts, there probably is only a fairly limited number of general contractors who could meet that criteria. This might

encourage more out of state general contractors of this size to bid on Massachusetts work, which is not necessarily a good thing.

3. There are no Massachusetts legal cases concerning this product, which suggests that there would be an entirely unpredicatable complete assessment of the rights of the insurance company and the general contractor and the subcontractors should this become part of the public construction arena until a body of law was built up by decisions of Massachusetts' appellate courts. Surety bonds have been around for approximately one hundred and thirty years and the SDI product has only been around for about twenty-one years with very little application, comparatively speaking. Nationwide, there are thousands of legal cases interpreting the rights of the various parties involved with the surety process. Not so as to the SDI product.

4. This type of insurance has typically high deductibles (five hundred thousand dollars is mentioned in the literature, sometimes lower and sometimes higher) and co-pays with regard to claims. This essentially makes SDI catastrophic insurance, as compared with surety bonds which have no deductibles and no co-pays and provide coverage from the first dollar of the claim. Put another way, if there is a subcontractor default under SDI, a lot of what the general contractor incurs for costs will have to be borne by the general contractor.

5. It is the general contractor, after receipt of trade contractor bids, which prequalifies the subcontractors who can particpate in this program. Other than potentially delaying construction, the general contractor will have to hire accountants and others familiar with surety bond underwriting to perform that process with regard to SDI. In fact, one might argue that their review should be even more strenuous than the surety's review due to the fact that the general contractor will be bearing some of the costs of a loss. Obviously, there is a cost factor involved with this, which will be included in the CMR's price, making construction with this model probably more expensive for owners.

6. The general contractor can terminate a subcontractor. The insurer, unlike a surety with a surety bond claim, can not contest this termination. The general contractor can then finish the subcontractor's work using whatever method makes sense to it (not by a method provided for in the bond which may be less workable and more likely to create a delay in obtaining completion contractors.) Because there is no specific oversight over a general contractor's termination of a subcontractor, one wonders if the general contractor would work less with a difficult subcontractor and just get rid of him. After all, under SDI, a general contractor would not need any other party's prior consent with regard to a termination.

7. The general contractor then presents the bill to the insurer which, after the general contractor has met its deductible and co-pays, the insurer has to pay within a fairly short period of time, such as thirty days. (For surety bonds, payment might take years of litigation, worst case.)

8. One of the ideas of SDI is that its cost is less than the cost of surety bonds. (Of course, so is its coverage because of deductibles and co-pays.)

9, With the current bill before the Legislature, it is limited solely to trade contractors participating in the CMR program. Outside of Massachusetts, owners can take out such policies on their general contractors.

10. Some of the literature suggests that SDI is most appropriate for large commercial building projects.

11. With SDI, the general contractor has the possibility of using its own insurer to obtain the SDI insurance, rather than dealing with various subcontractor surety companies, the idea being that he might already have some relationship and level of comfort with the insurer who will be paying the bill.

12. The literature suggests that SDI is used or has been used by the following contractors: EllisDon, Turner, Skanska, Barton Malow, Bechtel, PCL, J.A. Jones, Weitz, Haskell, Webcor, Hunt Construction and Perini Corp and others. According to the literature, as many as 80 contractors have purchased an SDI policy from Zurich. (Another piece of literature suggests that this number may be as high as 150 contractors participating in an SDI program.) SDI seems to work best for contractors that subcontract more than $100 million of work a year.

13. Another aspect of SDI is that general contractors with good (low) loss records will have lower insurance premiums over time.

14. And, with SDI, subcontractors who are too small or lack a sufficient track record to obtain surety bonding might particpate in jobs they otherwise would not be able to obtain.

15. SDI may also include elements of insurance as to items not paid for generally with surety bonds. Qualifying direct costs include the cost of attorneys and consultant fees incurred to remedy the default or in the defense of any dispute with the defaulted subcontractor. These typically would not be recoverable against a subcontractor's performance bond. Indirect costs covered by the policy include delay damages, acceleration cost, and extended overhead.

16. And, coverage limits for any subcontractor are not limited to the amount of the subcontract but to the amount of the general contractor's policy limits, which will, generally, be a great deal higher than the amount of any one subcontract. And, for a subcontractor who defaults on many projects, this can be treated as one loss, not several, which would be the case with surety bonds.

17. There seem to be fewer benefits for subcontractors participating in this program. But, there are some benefits. Enrollment in an SDI project may not tap their available bonding capacity or require personal indemnity.

V. IS THIS SOMETHING THAT WOULD WORK IN MASSACHUSETTS?

In a word, without accompanying regulations and changes to various of the existing

public bid laws, I think the answer is clearly 'No'.

Why not?

Well, let's look at how this would really work within the context of Massachusetts' other public work statutes. One can't change public construction by adding three sentences worth of a very serious new change without either modifying existing statutes/regulations or issuing new ones. This proposed act does neither.

Two dozen other reasons why SDI would probably not work in Massachusetts in the form presented by this bill are:

First of all, DCAMM and other public agencies regulate subcontractors in terms of what trades they are prequalified in and thus able to bid, what should be their largest single project and how much work they can have ongoing at any particular time. Sureties, before they establish a bonding line, do the same thing, with more emphasis on single bond limits and total bond limits and their underwriters are specifically trained to do this work. Why would Massachusetts need a *third* prequalification of subcontractors by construction managers at risk, such prequalification probably not up to the standards of a public agency or surety evaluation?

For a second reason, how would the issue of whether or not a subcontractor should be prequalified be resolved if DCAMM (or another public agency) were to say the subcontractor should be prequalified and the CMR says otherwise?

For a third reason, more subcontractors would be probably be terminated under SDI than would be the case with with surety bonds. Under SDI, it's just so easy to do it in the short term, before the terminated subcontractor sues. Under SDI, the insurer is not entitled to challenge the CMR as to the issue of a subcontractor's default. With surety bonds, before the subcontractor's performance bond is triggered, the subcontractor's surety would be entitled to investigate the situation to find out whether or not there is principal default. So, the CMR would have to have the subcontractor's surety agree with it as to the issue of subcontractor default before the subcontractor's performance bond obligations can be triggered, which would not be a precondition as to an insurer's obligations under SDI.

The very fact that it takes a surety longer to make its investigation and claim decision than would ostensibly be the case under SDI is a factor that works *against* subcontractor termination because there is less immediate relief. There is less immediate gratification. This may cause the CMR to provide supplementation to the subcontractor (rather than terminating him) or, in certain circumstances, negotiate jointly with the subcontractor terms of the conclusion of the subcontract or issue a termination for convenience notice, which is not involved with issues of fault.

SDI proponents might argue that under the surety system, the general contractor has to fund subcontractor performance longer as compared with their system. My experience has been that very few general contractors allow subcontractors to get ahead of them money-wise. And,

subcontractors seldom default without some gradual prior notice. It is something that someone can see coming on, like a hurricane in another state. This causes general contractors to hold more of the subcontractor's monies, putting itself in a better position to finish the subcontractor's work using those monies and the current retention that has not been paid.

For a fourth reason, SDI is not a 'first dollar' product, the way that surety bonds are. With a subcontractor performance bond surety, if it cost the general contractor one hundred thousand dollars to complete a defaulting subcontractor's work, the general contractor would be entitled to recover one hundred thousand dollars from the surety bond. SDI, by comparison, has hefty deductibles and co-pays (not present with the surety bond product) which means that for smaller defaults, it will be paying for the subcontractor default completely out of its own pocket. One must always keep in mind that a fundamental principle of SDI is that this is *catastrophbic* insurance, not insurance designed to pay for smaller losses.

For a fifth reason, there are only three or four insurance companies which currently offer SDI nation-wide. SDI hardly represents a tidal wave crashing through the construction process. In 1996, when Zurich originally offered SDI, it was the *only* insurer with this program. What possible good would the Massachusetts public procurement system achieve from SDI when it is a product offered only by a such a very small minority of insurers and yet has so many deficits with regard to public construction?

For a sixth reason, some of the trade contractors may not be covered through the subcontractor default insurance policy program and would, therefore, have to submit payment and performance bonds. Why have two different procedures/programs for the same job?

For a seventh reason, what will be the criteria for determining whether or not a subcontractor qualifies for this program? Will it differ from CMR to CMR or from job to job? Where would there be the uniformity that should exist throughout the public bid process among bidders/subcontractors? A statute like this should not be enacted without establishing at the same time very specific procedures for the evaluation of trade contractor bids.

For an eighth reason, what kind of documents will the subcontractor have to submit to the CMR for the prequalification process? Audited financial statements? For how many years? What happens to this very sensitive financial information after the qualification process has concluded? Or, after the job is completed? How would the subcontractor be really sure that no one retained his sensitive information? What protection is there that different (more strenuous) prequalification procedures might be required from less favored subcontractors than would be the case with favored subcontractors?

For a ninth reason, if DCAMM or any other public agency has already prequalified a subcontractor for the kind of work it can do, the largest single job it can do and the total program it can do, why would CMR prequalification be even necessary? Wouldn't this only duplicate the prequalification by people who know what they are doing?

For a tenth reason, trade contractor prequalification taking place after the CMR is

selected will likely extend the period of the construction process because this process will take time. Is this process worth it if would push a job into winter conditions that would otherwise not be going there?

For an eleventh reason, many contractors bid jobs as subcontractors on some jobs and as general contractors on other jobs. This could cause subcontractors to have to submit sensitive financial information to their competitors, which might be used against them on future jobs.

For a twelfth reason, at least as to the SDI program as described in the literature, this would be only for CMR's who have between fifty and seventy-five million dollars of annual subcontractor volume or more. How many CMRS would be able to meet this criteria?

For a thirteenth reason, with deductibles of five hundred thousand dollars or more (per the literature), how many CMRS would even want this? It must be remembered that SDI is designed *only* to be catastrophic insurance, assuming that the general contractor itself is going to absorb big chunks of monies with a large default. As no company is in business to lose money, one way or another, this exposure will be passed on to public owners. Too many defaults under SDI at the same time might put a CMR out of business.

For a fourteenth reason, there is a great deal of case law concerning and interpreting surety bonds and almost no case law interpreting SDI. This could be a pig in a poke. Until the Appeals Court or Supreme Judicial Court has commented on a statute, its meaning is not necessarily 100% clear. And, that process takes lots and lots and lots of years.

For a fifteenth reason, one of the chief selling points of SDI is, that over time, this is cheaper than bonds. The literature is clear that for any particular job, not all of the subcontractors will be allowed to participate in this program. What if the bids of two trade contractors in a specific trade are very close and the difference in their overall price is the fact that the SDI one is paying for is cheaper than the other trade contractor's surety bonds? In other words, their actual bids for the work are essentially the same apart from the SDI for one and surety bonds for the other. Who gets this job?

For a sixteenth reason, if a dispute arose between two subcontractors over one having SDI and the other having surety bonds and for any other bid law issue involved with SDI, the AG would have no authority to hear bid disputes until the statute granting them that power - MGL C. 149, s. 44H - is amended.

For a seventeenth reason, how does the possibility of having SDI insurance protect and further the public interest?

For an eighteenth reason, because many subcontractors would not want to submit to CMRS sensitive financial information which the CMRS say is necessary to prequalify the subcontractor, this could have the effect of having fewer subcontractors bidding CMR jobs, thus, ultimately, probably raising the price of public construction.

For a nineteenth reason, MGL C. 149A, s. 8 already provides for a trade contractor prequalification committee for the project at hand. Does this mean that with SDI this committee will no longer exist and/or will cease having the authority to prequalify trade contractors, particularly where there is a lot of statutory authority advising how this process is to be accomplished? Will both the prequalification committee and the CMR perform prequalifcation of trade contractors simultaneously? Isn't this a ridiculous duplication of effort? And, what happens if the trade contractor prequalification committee and the CMR don't agree on whether a particular trade contractor is prequalified? Whose prequalification will be used?[3]

For a twentieth reason, all contractors and subcontractors obtaining a surety bond program have to sign agreements of indemnity to indemnify the surety as to loss and expense payments incurred on their account. Will that mean that the trade contractors under the SDI will also have to sign an indemnity agreement either with the CMR and/or with the insurer who may incur losses under the SDI program?

For a twenty-first reason, since CMRS know they are going to have to meet the amount of the deductible and the co-pay before the SDI insurance company pays the first dollar, doesn't that necessarily mean that CMR prices will go up to provide for such losses the CMR iteself will have to incur?

For a twenty-second reason, there are numerous Massachusetts cases which say that prequalification is a cornerstone of public construction. But, the current Massachusetts scheme limits prequalification to public agencies, not to general contractors. Presumably, a public agency's review of a subcontractor's qualifications will be quite extensive and neutral, neither favoring a subcontractor nor disfavoring a subcontractor. And, on top of that, the public agency is more likely and in a better position to keep that sensitive financial information more confidential.

For a twenty-third reason, there are probably not that many Massachusetts general contractors who are large enough to made SDI insurance work. That would seem to be an invitation for out-of-state general contractors to come in and bid Massachusetts work. Other than taking the work away from Massachusetts companies and employees, years of experience have demonstrated to me that it can quite often be difficult litigating with out of state firms for a number of reasons. Subpoenas do not work over state lines. Those who know the most about the job are out of state companies and residents, not subject to subpoena. In many instances, once a Massachusetts court has issued a judgment against a foreign corporation, to enforce that judgment in the state in which the foreign corporation is domiciled, a second legal action may be required to 'domesticate' the Massachusetts judgment by a court in that state. More delay. More expense.

For a twenty-fourth reason, all that this bill does is to describe an *idea*. It does not set forth what the elements of the program would be and what the guidelines would be to evaluate subcontractors. For the purpose of uniformity and fairness, there would have to be very specific regulations describing the subcontractor prequalification process, which this bill does not address at all. And, for such a program to have any chance of success, there probably should be

some public agency overseeing it, which is not an element contained in the existing bill.

VI. CONCLUSION.

For the reasons stated above, this would not work in Massachusetts without a significant revision of various others public bid statutes, regulations and procedures, including, without limitation, MGL C. 30, s. 39M, MGL C. 149, s. 44A-H and MGL C. 149A, which this bill simply and completely totally ignores. This bill, if it became law, would necessarily have to be incorporated into other aspects of the public bid laws.

For those of my readers who agree SDI under these circumstances is just plain dumb, idiotic and stupid as well as unworkable, contact your representatives and senators and tell them so before the Legislature, in its ignorance, enacts this. If this Squib makes sense to you, you might provide your legislator with a copy of it. I strongly recommend that those in the insurance and surety industries get involved with this issue before it becomes a nightmare, which is would be if it passed and became law in its current form.

In my conversations with various members of the Legislature, they have often told me that they hear from their constituents only infrequently. As to this issue, let's create an exception!

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[1] A 'squib' is defined as 'a short humorous or satiric writing or speech'. Wiktionary defines a 'squib' as: "a short article, often published in journals, that introduces empirical data problematic to linguistic theory or discusses an overlooked theoretical problem. In contrast to a typical linguistic article, a squib need not answer the questions that it poses."

[2]On October 24, 2017 and October 26, 2017, we will be giving our last seminar, "DEALING WITH YOUR SURETY WHEN CLAIMS ARE MADE AGAINST YOUR BONDS". This is an issue that arises with viable contractors as well as with insolvent contractors.

[3]This is going to create lawsuits out the wazoo. To the best of my knowledge this is not, uh, exactly a legal term.