

Beyond Maintenance Bonds

Enhanced Protection for Cities

John Cunningham, ICPA

2012 Municipal Streets Seminar

Beyond Bonds

- What is a maintenance bond?
- Assignment of risk
- Maintenance Trust Account

What is a maintenance bond?

- Protection against defects
 - Workmanship
 - Materials
- Typical term in Iowa
 - 4 years
- The city is the beneficiary
 - Most other agencies do not use maintenance bonds
 - DOT
 - Counties
 - Airports



What is a maintenance bond?

- Underground and paving work are typically separate bonds
 - May have different terms
 - Task group members would favor matching terms
- Survey from SUDAS
 - 2 to 4 yrs. for utilities
 - 4 yrs. For streets
 - One city 2 yrs.
 - No warranties



What is NOT a maintenance bond?

- Warranty
 - Protection regardless of whether or not the contractor is able to perform
- Performance bond
 - Assures that the contractor will complete the work as established in the bid documents



How does a city benefit from a maintenance bond?

- If there is a defect that can be traced to workmanship or materials AND the contractor is no longer in business, then collection on a maintenance bond may be viable
- What about issues that are difficult to call defects in workmanship or materials?
 - Contractor still in business



Why would we want more?

- Construction issues
 - Settlement over utilities
 - Movement of soil
 - Damage by other construction
 - Design flaws
 - **Construction flaws**
 - Unpredictability of weather
 - Unforeseen circumstances
 - We just can't design out all the possible problems

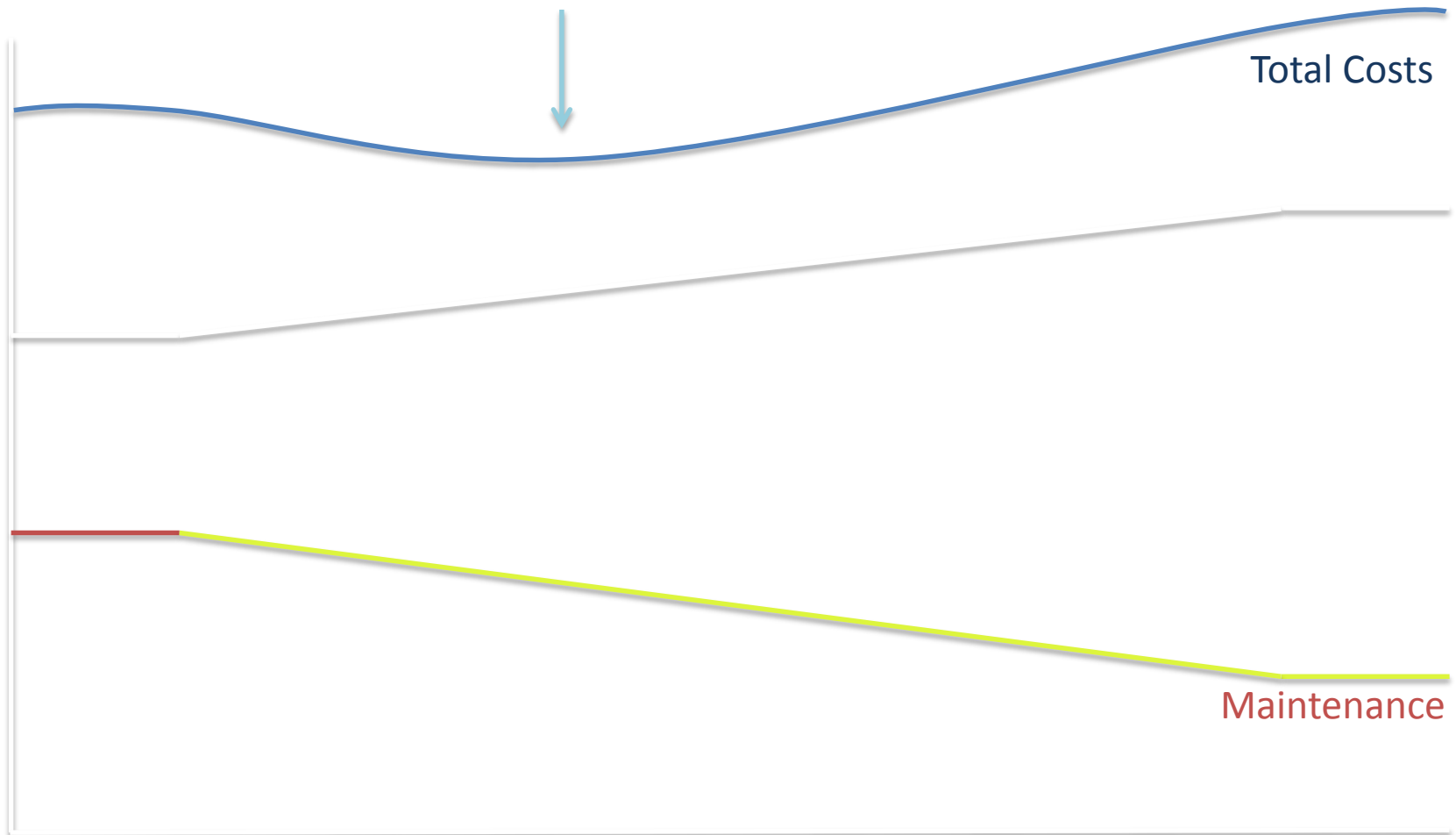


Reducing Risk for Cities

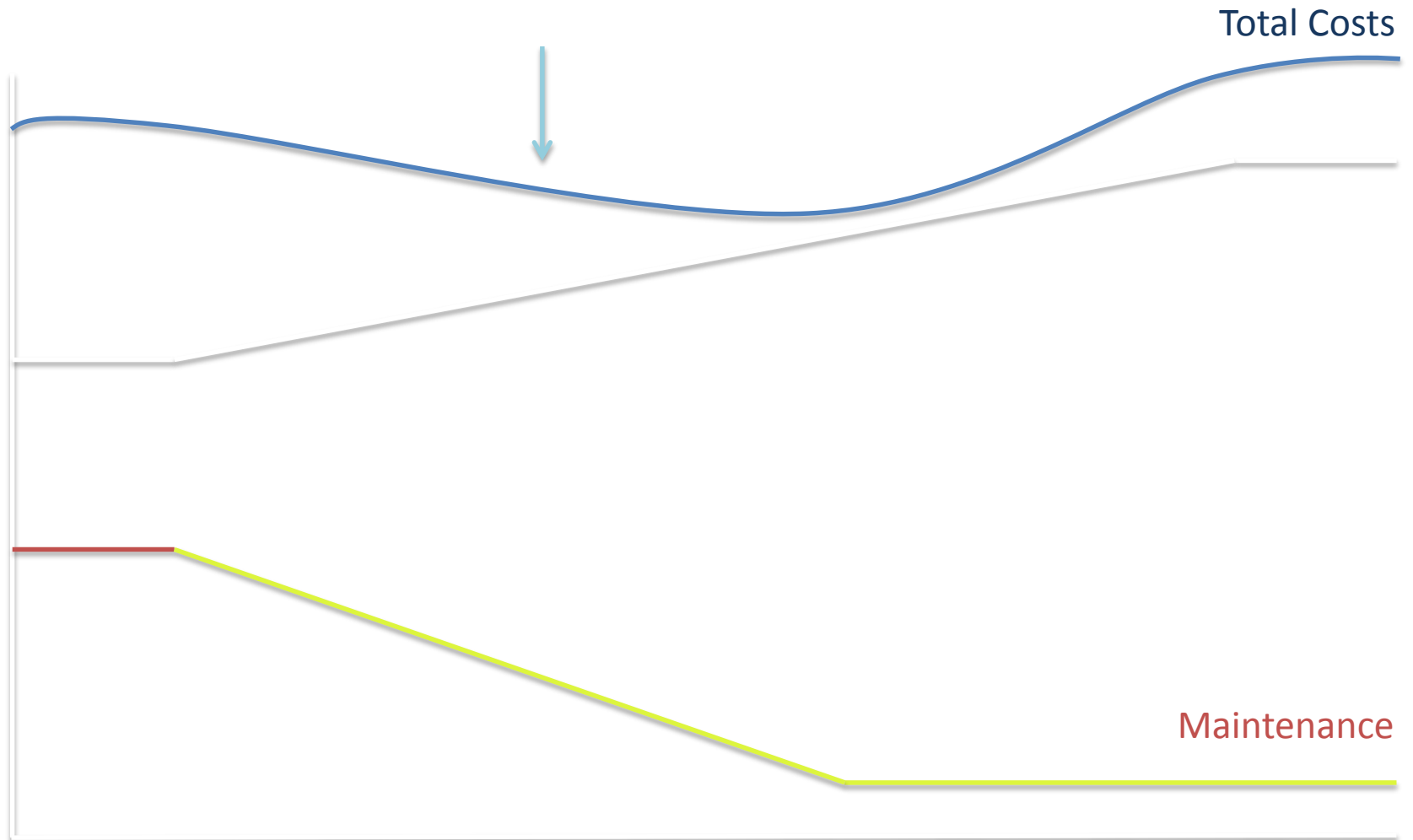
- More specifications
- More design work
- More inspection
- More quality control
- More responsibility on the contractor



Risk Assignment



Risk Assignment



City of Marion Example

- Maintenance self insurance
 - \$12/\$1000 of contract price
 - Estimated cost of typical maintenance bond is <\$3/\$1000
 - No maintenance bond
 - Only on subdivision work
 - One contractor has been taking this option
 - Most prolific contractor
 - Very, very low rate of consumption of the fund
 - Significant balance
 - Nothing returned to contractor



Task Group Recommendations

- Maintenance trust account
 - City of Marion example
 - With some flexibility
 - Adjust the percentage returned to the contractor
 - Quality assurance component
 - Adjust the payment
 - \$ per thousand of contract price



Maintenance Trust Account

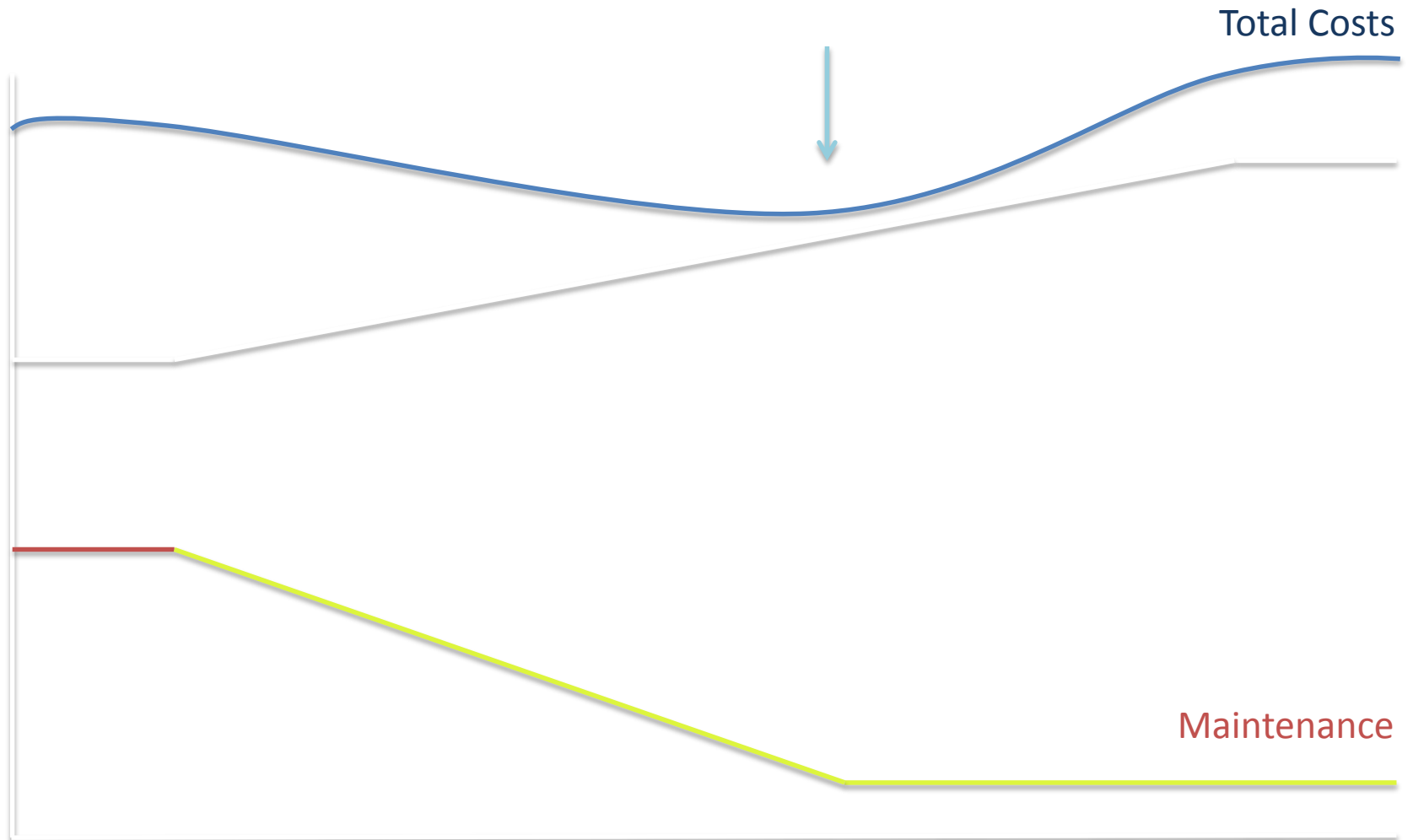
- Goals
 - Provide the city with funds to cover unforeseen, early-age issues that are determined, by nature of the bidding process, to represent an acceptable level of risk (cost) for the city
 - Minimize disputes over responsibility – just fix it
 - Allow the city a mechanism to encourage quality practices
 - Return unused funds to contractors

Maintenance Trust Account

- Single account for a city
- Deposits made per project
 - Amount set by city
 - <\$12 per \$1,000 contract price
 - Deposits and withdrawals tracked by project
- Maintenance bond still required
 - <\$3 per \$1000
- Portion of initial deposit might be returned
 - Percentage set by city
 - Greater percentage to encourage greater quality
 - Contractors could work expected returns into bids
- Term of the trust recommended at 4 years



Risk Assignment



City of Marion Example

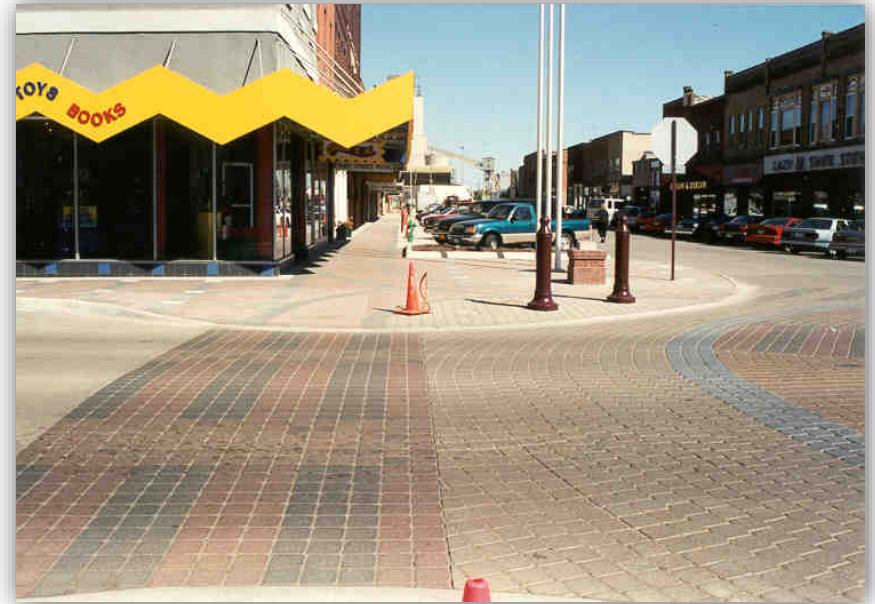
- “Payment into this fund will relieve the owner, developer and/or contractor of **any further responsibility or liability to remedy** any and all defects that may develop in said work by reason of bad workmanship or poor material used in the construction of said work or to keep the same in good repair after acceptance of the improvement except that payment into this fund shall not relieve any surety or principal of these obligations covered under the terms of a performance bond filed with the City for the same improvement.”

Maintenance Trust Account

- Payment into this fund will relieve the owner, developer and/or contractor of any further responsibility or liability to remedy any and all defects that may develop in said work by reason of bad workmanship or poor material used in the construction of said work or to keep the same in good repair after acceptance of the improvement **except that payment into this fund shall not relieve any surety or principal of these obligations covered under the terms of a performance and/or maintenance bond** filed with the City for the same improvement.

Remaining Process

- Forwarded to SUDAS
- Recommendations are the beginning
- Further exploration is needed to answer questions in depth
 - Legal aspects
 - Additions
 - Revisions
 - Refinement of language



Questions

Thank You