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AIA Revises Bond Forms

By: Todd R. Regan

In June 2010, the American Institute of Architects released updates to its long-standing and widely used forms for bid bonds (AIA A310) and performance bonds and payment bonds (AIA A312). Some of the changes to these bonds are significant, and readers should be aware of how these revisions impact the construction and surety industries.

The revisions, according to the AIA, result from the input of various industry groups, including those representing sureties, contractors, and owners. Some of the changes are designed to address, and in certain instances to correct, judicial interpretations of the previous bond forms. Many of the form changes, as discussed below, significantly impact the way that owners, contractors, and sureties manage risk in today's construction industry.

BID BONDS

In the first update in 40 years to the bid bond forms, most of the modifications are mainly stylistic and non-substantive in nature. The most significant change clarifies the duration of time in which the surety's obligations remain in effect prior to the contract award. Typically, bid documents set forth a time period for the owner's acceptance of bids. A prolonged delay in a contract award can have the effect of increasing the surety's risk. The revised bond form provides that the owner and contractor may agree to extend by 60 days the time set forth in the bid documents for accepting bids without obtaining the consent of the surety; however, an extension of the time for accepting bids greater than sixty days requires the surety's consent.

PERFORMANCE BONDS

The performance bond form, which was last revised in 1984, significantly changes the owner's notice obligations, the time afforded to the surety to take action in response to the owner's declaration of default, the surety's defense based on the owner's failure to provide notice of intent to declare the contractor in default, and the surety's liability limits. In general, these changes reduce sharply the amount of time for the surety to take action in response to the owner's declaration of default, remove a potential defense of the surety, and increase the surety's potential liability beyond the penal sum of the bond. Here are the specifics:

- Section 3.1 of the revised form deletes the requirement that the owner, in its notice of intent to declare the contractor in default, request a meeting with the surety and contractor prior to declaring the contractor in default; however, the owner retains the right to request such a meeting at its option. Furthermore, the revised bond form permits the surety to

request such a meeting within five business days of receipt of the owner's notice. If the surety requests such a meeting, the owner is required to attend.

- Section 3.2 of the revised form deletes the requirement that the owner wait 20 days after providing its notice of intent to declare a contractor default before actually declaring a default.
- Section 4 of the revised form expressly provides that the owner's failure to provide a notice of intent to declare a contractor default, as required by Section 3.1, shall not release the surety of its obligations; however, the surety's obligations may be reduced to the extent that it can establish that it suffered actual prejudice as a result of the owner's failure to give the prescribed notice.
- Under both the prior bond form and the revised form, the surety is obligated to take action "promptly" in response to the receipt of the required notices from the owner. Furthermore, when the surety fails to take action with "reasonable promptness," under both forms the owner must serve an additional written notice demanding the surety's performance as a prerequisite to declaring it in default. Significantly, under Section 6 of the revised form, the surety is afforded only 7 days to respond to the owner's additional demand for performance, which is a sharp reduction from the 15 days provided in the prior form.
- Section 7 and 8 of the revised form expressly state that the surety's liability may, in certain circumstances, exceed the bond's penal sum. More particularly, when the surety elects, pursuant to Section 5.2, to perform and complete the contractor's work itself, the revised form provides that the surety's liability is not limited by the penal sum of the bond. This language is consistent with case law holding that a surety that completes its principal's work without a takeover agreement may be liable for amounts in excess of the Bond's penal sum; however, the newly added language does not preclude the surety and owner from entering into a separate takeover agreement pursuant to which the parties may agree that the surety's liability shall be limited to the bond's penal sum.

PAYMENT BONDS

The revised payment bond form contains several key changes. Significantly, the revised form deletes the claimant's mandatory waiting period prior to asserting a bond claim, lengthens the surety's time to pay or deny a claim, clarifies the consequences of an untimely response by the surety, expands the required contents of a notice of claim and expands the class of potential bond claimants. Here are the specifics:

- Section 5.1, which governs claims by subcontractors not having a direct contract with the contractor (i.e. second- and third-tier subcontractors), has been modified to delete the 30-day waiting period before the subcontractor may submit a claim to the surety. Under the prior version of the bond form, the subcontractor was required to give the general contractor 30 days to respond to its notice of nonpayment prior to serving a claim on the surety. Under the revised form, the subcontractor may serve a claim on the surety at the same time it serves the contractor with notice of nonpayment. In addition, the subcontractor is no longer required to serve the owner with a copy of its notice of nonpayment.
- Section 6 of the revised form provides that the claimant's notice of nonpayment set forth in Section 5.1.1 may be satisfied by notice provided by the owner to the contractor. This change was made in recognition of the fact that owners often become aware of subcontractor claims and provide notice to the contractor. Notably, however, a subcontractor is still required to provide a claim to the surety when the owner has provided the required notice of nonpayment.
- Section 7.1 of the revised form expands from 45 days to 60 days the time in which the surety must respond to a claim.
- Over the past several years, court decisions, most notably in Maryland, Virginia, and Florida, [1](#) have held that the surety's failure to strictly comply with its obligation to respond to claims within the time period set forth in the bond acts as a waiver of the surety's and the contractor's defenses to payment. In response to these holdings, Section 7.3 of the revised form expressly states that the surety's failure to pay or deny a claim within the

prescribed time period does not constitute a waiver of the surety's or contractor's defenses to payment, except as to amounts for which the surety and claimant have reached an agreement. If, however, the surety fails to respond to the claim and to pay undisputed amounts within the prescribed time period, and the claimant ultimately prevails on its claim, the surety is liable for the attorney's fees of the claimant incurred in establishing its right to payment.

- Section 8 has been amended, in light of the revisions to Section 7.3 discussed above, to provide that the surety's liability may exceed the penal sum of the bond to the extent that it becomes liable for the attorney's fees of the claimant as a result of its failure to pay or deny the claim within the prescribed time period.
- Section 16.1 of the revised form expands the information that must be set forth in a claim. Significantly, the required claim information is the same for subcontractors having a direct contract with the general contractor as it is for lower-tier subcontractors. A claim must include the following:
 - The name of the claimant
 - The name of the person or entity for whom the claimant performed the work
 - A copy of the contract or purchase order pursuant to which the claimant performed the work
 - A brief description of the work performed
 - The claimant's last date of work
 - The total amount earned by the claimant as of the date of the claim
 - The total amount of payments received by the claimant through the date of the claim
 - The total amount due and unpaid to the claimant as of the date of the claim
- Section 16.2 of the revised form has been changed to expand significantly the definition of claimant to include any individual or entity who has rightfully asserted a claim under a mechanic's lien or under a similar applicable statute against the project. The prior bond form excluded subcontractors of the third tier and below from the definition of claimant. Under the revised bond, any tier of subcontractor or supplier may now assert a claim; however, it is important to note that a subcontractor who has filed a mechanic's lien is still required to comply with the notice of nonpayment and claim provisions of the bond.

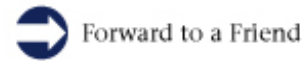
CONCLUSION

In summary, the revised bond forms represent significant changes in the rights and responsibilities of both claimants and sureties. These modifications highlight the importance of making a close examination of the terms and conditions of the applicable bond language. Of course, these modifications have no effect on preexisting bonds or on bonds that continue to be written on the prior forms. Furthermore, in the event of a conflict between the bond forms and applicable law, it is the stated intent of the forms that applicable law shall govern. Moreover, depending on the jurisdiction and the nature of the project, the language of the bond may be superseded by applicable statutory requirements. As such, it is important to obtain professional legal advice concerning your rights and responsibilities under any bond.

¹ See, e.g. *National Union Fire Insurance Co. of Pittsburg v. Wadsworth Golf Construction Co. of the Midwest*, 863 A.2d 347 (Md. Ct. of Spec. App. 2004), *aff'd sub nom. National Union Fire Insurance Co. of Pittsburgh v. David A. Bramble, Inc.*, 879 A.2d 101 (Md. 2005)(Surety's failure to deny claim within 45 days as required by ¶16.1 of the former bond form constituted a waiver of all defenses); *Casey Industrial, Inc. v. Seaboard Surety Co.*, 2006 WL 2850652 (E.D. Va. Oct. 2, 2006) (Surety waived factual defenses by failing to identify the defenses within the 45-day period); *J.C. Gibson Plastering Co., Inc. v. XL Specialty Insurance Co.*, 2007 WL 2916399 (M.D.Fla. Oct. 8, 2007), order vacated by *J.C. Gibson Plastering Co., Inc. v. XL Specialty Ins. Co.*, 2009 WL 2710316 (M.D.Fla. Aug 26, 2009) (NO. 3:07CV268J34TEM) (45-day period for surety's response to claim was triggered by initial bond claim containing the minimum information required by the bond form and not on later date when claimant provided backup documentation; surety's failure to pay or deny within 45 days held to be a waiver of defenses).

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