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PERILS AND PROMISE OF COMMON LAW BONDS:
LIMITING THE SCOPE OF ELIGIBLE PAYMENT BOND
CLAIMS

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1. Introduction

This paper topic was born of a rather esoteric Florida payment bond issue the authors faced this past year. As we researched the claim, the final outcome yielded some valuable insights worthy of consideration by practitioners and claim handlers irrespective of the jurisdiction in which they practice.

Surety lawyers often encounter instances where what purports to be a statutory bond fails to include pertinent statutory requirements. More significantly, we have also encountered extra-statutory provisions, which often appear to provide greater coverage than that which is necessary under the pertinent bond statute. In some jurisdictions, including Florida, the inclusion of these extra-statutory provisions can have serious financial consequences for the surety.

The surety often has little input regarding the content of the offending instrument, and is simply asked to execute a bond form mandated by the terms of the general or subcontract bid documents. Where the surety does not participate in the drafting of a payment bond, the surety will often end up underwriting risk that would never be visited upon the owner or, as the case may be, the general contractor and the first tier surety. In other words, the expansive language of the bond creates an unnecessarily broad scope of coverage for the surety.\(^1\) This problem is not without a remedy.

Before undertaking a discussion of this issue, it is first important to understand the difference between a statutory and common law bond. It is also important to understand how various jurisdictions will treat a bond that on its face does not fall squarely within either category.

2. Difference Between a Statutory and Common Law Bond

Simply put, a statutory bond is one that is given pursuant to a statute, while a common law bond is not. A bond specifically referring to a statute and employing the statute’s terms is unquestionably a statutory bond. A common law bond is ordinarily a contract privately given without qualifying laws, which is strictly construed and not extended beyond the scope of the terms contained therein. A statutory bond on the other hand is given to the public in the

\(^1\) While there are occasions when a general contractor may have some reason for requiring more expansive bond coverage in a subcontractor’s payment bond, most often a general contractor is simply looking to reduce its payment bond exposure by providing lower tier bond claimants, who might otherwise be eligible to make a claim against the general contractor’s bond, an additional source of recovery.
observance of law and is to be read, construed and enforced according to the statute pursuant to which it is given. 2 With a statutory bond, the provisions of the statute are read into the bond and considered a part of the bond.

The general distinction between a statutory bond and a common law bond is that the former is required by and conforms to a statute, while the latter is not required by statute, or if required, is insufficient to fulfill the statutory requirements. 3 The primary test in determining whether a bond is a statutory or a common law bond requires an examination of the obligations imposed upon the principal and its surety. The test requires a comparison of the minimum requirements enunciated in the statute and the language contained in the bond.


Most jurisdictions appear to follow a few logical rules when construing statutory bonds. A bond issued in connection with a public project will be construed to contain the minimum requirement of the statute – among other things, the surety must provide coverage to all claimants protected by the statutory scheme. 4 Where statutory provisions are absent, they are simply read into the bond. 5 Statutory payment bonds are liberally construed to carry out their legislative purpose - that is to protect labor and material suppliers. 6

Problems arise when a bond contains extra-statutory provisions, or terms which appear to provide coverage broader than what is contemplated by the controlling statute. Courts in most jurisdictions will simply hold a surety to whatever extended protection is provided in its bond. Dow-Par, Inc. v. Lee Corp., 644 N.E.2d 150, 155-157 (Ct. App. Ind. 1994); C.S. Luck & Sons v. Boatwright (1932), 157 Va. 490, 499, 162 S.E. 53, 56; Travelers Indem. v. Housing Auth. Of Miami (1972), Fla.App., 256 So.2d 230, 234; Wal-Board Supply v. Daniels (1981), Tenn.App., 629 S.W.2d 686, 688; Aluma Systems, Inc. v. Frederick Quinn Corp. (1990), 206 Ill.App.3d 828, 151 Ill.Dec. 618, 635-36, 564 N.E.2d 1280, 1297-98; 17 Am.Jur.2d Contractor’s Bond Section 73 (1990); but cf. Construction Materials v. American Fidelity Fire Ins., 383 So.2d 1291, 1294 (La. App. 1980) (a public works bond can be neither broader nor narrower than the law which provides for it, and anything provided for by law and omitted from the bond must be read into the bond while anything provided by the bond which goes beyond the provisions of the law must be read out of it).

In Dow-Par, an Indiana appellate court determined that a lessor of earth moving equipment was not a claimant protected by the public works bond statute. This did not, however, end the court’s analysis. The court found that by adding extra-statutory provisions to its payment bond, the surety had expanded the scope of its coverage beyond that which was required by the public work bond statute. According to the bond, a claimant was “one

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3 Id.


having a direct contract with the [principal], or with a sub-contractor of the principal for…rental of equipment directly applicable to the contract.” *Id.* at 156. The Court found that the bond’s definition of a claimant exceeded the requirements of the public works bond statute and encompassed the lessor’s claim.7

It is not surprising that, like the *Dow-Par* court, most courts will enforce public works bonds in accordance with their written terms, given the public policy behind such bonds – protecting laborers and materialmen. What is surprising are the lengths to which courts in both Florida and Tennessee have gone to promote this policy.

4. Where the Bond Language Dictates the Nature of the Bond – The Florida Rule

Florida and Tennessee state courts have ruled that the inclusion of extra-statutory provisions will divest a bond of its status as a statutory bond. *Florida Keys Community College v. Ins. Co. of North America*, 456 So.2d 1250 (3d DCA 1984) is one of the most often cited cases for the proposition that a public works bond may be construed as a common law bond if its provisions are more expansive than those required by the applicable bond statute.

In *Florida Keys*, a community college brought an action against building contractors and their sureties for alleged construction defects at a fine arts center. The trial court dismissed the claims against the sureties on the grounds that they had not been filed within the one year period set forth in section 255.05(2), Florida Statutes, Florida’s public works bond statute.

The community college appealed. The Third District Court of Appeals reversed, holding that the bonds in question were common law bonds not subject to the one year limitations period, but rather subject to the four year limitations period applicable to common law bonds. The court simply held that where a bond provides more extensive coverage than the minimum statutory requirements, it will be construed as a common law bond for all purposes. The court wrote in support,

> [t]he primary test in determining whether a bond is a statutory bond or a common law bond depends upon an examination of the obligations imposed upon the principal and its surety. The test requires a comparison of the minimum requirements enunciated in the statute and the language contained within the bond…. We reject the argument proposed by the sureties that it was incumbent upon the college to find a bond which qualified under [the public works bond statute] and no other bond was allowable. They maintain that any bond obtained in satisfaction of the statute must be deemed a statutory bond regardless of its expanded provisions. Their argument ignores the many cases which recognize distinctions in bonds issued in connection with public projects. Even though a bond is furnished pursuant to a public works project, it will be construed as a common law bond if its provisions are more expansive than those required by [the public works bond statute].

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7 The court disregarded the surety’s argument that because the equipment lease was not made in contemplation of use on the bonded project, it was not “equipment directly applicable to the contract” and thus fell outside the scope of the bond.
Tennessee state courts apply the same analysis, finding that where a bond gives a claimant greater protection than that required by the statute, the bond is deemed a common law bond for all purposes. *White’s Electric, Heating, Air and Plumbing v. Lewis Construction Co.*, 199 WL 605654 (Tenn.Ct.App. 1999); *Wal-Board Supply Co. v. Daniels*, 629 S.W.2d 686, 687 (Tenn. App. 1981); see also *Koch v. Construction Technology, Inc.*, (924 S.W.2d 68 (Tenn. 1986)

(We cannot agree with the Court of Appeals’ conclusion that the bond is statutory. While §12-4-201 merely requires the general contractor to pay for all the labor and material used by the general contractor or an immediate or remote subcontractor, the bond in the instant case goes further. In the second paragraph quoted above, the principal and surety agree not only to pay for labor and materials, but also to pay ‘all just claims for damages and injuries to property.’ This is clearly an obligation above and beyond that contemplated by the statutes. Moreover, the bond makes no explicit reference to the [public works bond statute].)

Needless to say, these decisions make drafting a statutory bond in Tennessee and Florida a treacherous prospect. Fortunately, the Florida Statutes now provide forms sufficient to meet the requirements of both the public and private project bond requirements. Sureties are not, however, out of the water in Florida – sureties still face trouble when agreeing to underwrite subcontractor’s bond.

5. Potential Consequences of Failure to Comport with Statutory Requirements

As mentioned above, with few exceptions, most jurisdictions permit a surety providing a statutory bond to expand the scope of the bond coverage, particularly when the expanded coverage relates to the nature of eligible bond claimants. The negative financial consequences of doing so are evident: the surety will be forced to cover claims that would not have been compensable under the applicable bond statute. In addition, when a court determines that a bond is a common law instead of a statutory bond, the surety may be deemed to have waived the statutory notice requirements, and as we saw in *Florida Keys*, may also be subject to a lengthier statute of limitations period.

6. Lower Tier or Subcontractor’s Bonds

Lower tier bonds or subcontractor’s bonds are seldom mandated by statute, and by their nature are typically characterized as common law bonds. Where the bond is supplied on a public project, however, courts may allow the public bond statutes to influence the nature of

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8 § 255.05(3), Fla. Stat.

9§ 713.23(3), Fla. Stat.

10 For a complete discussion of this topic see Patrick J. O’Connor, Statutory Bonds or Common Law Bonds: The Public-Private Dilemma, Tort & Ins. L.J. 77 (Fall 1993)
a subcontractor’s bond. The Minnesota court of appeals has concluded that a subcontractor’s bond on a public project may be construed as a statutory bond.

In Iowa Concrete Breaking Corp. v. Jewat Trucking, Inc., 444 N.W.2d 865 (Ct. App. Minn. 1989), a supplier of concrete breaking equipment brought suit against a subcontractor and its surety when the subcontractor defaulted on its payment obligation. The subcontractor’s payment bond did not expressly cover attorneys’ fees, and therefore the subcontractor’s surety argued that the trial court erred by awarding fees. The appellate court disagreed. In upholding the fee award, the appellate court pointed out that the subcontractor’s bond incorporated all the terms of the subcontract, including the flow-down provisions, which required the subcontractor to undertake all the general contractor’s obligations to the state. One of the general contractor’s obligations, by virtue of the public works bond statute, was to cover reasonable attorneys’ fees. In this way, the appellate court for all practical purposes turned the parties’ common law bond into a statutory bond.

A few years later, on the same project, the court of appeals again had an opportunity to address this issue when another supplier was left unpaid by the same subcontractor. Saint Paul Fire and Marine Ins. Co. v. Central National Insurance Co. of Omaha, 480 N.W.2d 681 (Ct. App. Minn 1992). In this case, the issue was not attorneys’ fees, but whether the action was time-barred under the one year limitations period contained in the payment bond. The court held that the subcontractor’s surety was collaterally estopped from arguing that the Minnesota public works statute did not control the payment bond. The one year limitation in the subcontractor’s bond was superceded by the more liberal limitations rule under the statute. In support, the court restated its prior holding:

More specifically, the trial court and court of appeals were asked in that case [the Iowa Concrete case] to construe whether both the payment bond and the performance bond were governed by the provisions of the [Minnesota Public Works Statute]. Both courts concluded that the [bond], by incorporating [the] subcontract, where essentially converted from private to statutory bonds….Once this court concludes that the payment bond takes on the terms and conditions of the statutory bond by virtue of [the subcontractor’s surety’s] incorporation of the subcontract, [the surety’s] ‘separate’ defense based upon the bond’s status as a private bond in the instant action must fall.

Id. at 684.

As we see in these Minnesota cases, the incorporation of a public bond statute may have a negative impact on the surety. One would hope, however, that the logic underlying the Iowa Concrete and Saint Paul cases could be used in favor of a subcontractor’s surety. As discussed in some detail in section 7 below, a subcontractor’s surety may attempt to use a reference to the applicable public works statute to limit the scope of eligible claimants under a subcontractor’s bond.

7. Case Study: The Subcontractor’s Bond Surety vs. The Employee Leasing Company

A recent legal matter involving the company and the firm of the two authors provides a very good illustration of how appropriate limiting language in a lower tier bond can make a
11 Chapter 713 not only defines those parties eligible to file and foreclose a lien, but also those parties entitled to make a claim against a private project bond and a public project bond provided pursuant to section 255.05, Florida Statutes.
attempted to undercut *V.L. Orlando*. The employee leasing company provided Capitol with a copy of 2001 Florida Senate bill (attached as Exhibit B), asserting that the Florida Senate had responded to the “unjust” outcome in *V.L. Orlando* by including “temporary help firms” within the definition of the “sub-contractors” and “sub-subcontractors”, which, like laborers, are also covered by a Chapter 713 bond. In its renewed demand letter, the employee leasing company did not, however, cite to the full text of the amendment, leaving off the part that referenced section 443.101, Florida Statutes, which now supplies the definition of a “temporary help firm.”

Capitol responded to this last gasp by providing a copy of section 443.101, which reads, in pertinent part:

“Temporary help firm” means a firm that hires its own employees and assigns them to clients to support or supplement the client’s workforce in work situations such as employee absences, temporary skill shortages, seasonal workloads, and special assignments and projects. The term also includes a firm created by an entity licensed under s. 125.012(6), which hires employees assigned by a union for the purpose of supplementing or supporting the workforce of the temporary help firm’s clients. *The term does not include employee leasing companies regulated under part XI of chapter 468.* (emphasis added)

The employee leasing firm perceived itself to be out of options, and Capitol settled the claim for substantially less than the original $250,000 demand. However, all of this is not much more than background, the real teaching point here is in the subtext. The reason Capitol paid any money to settle the employee leasing company’s claim pre-suit was because a Florida court would likely have deemed Capitol’s bond a common law bond. The bond does not reference either section 255.05 (the public bond statute), nor does it reference section 713.23 (the private bond statute). Moreover, Florida’s statutory law, like most other state’s laws, does not directly contemplate a subcontractor’s bonds and with the *Florida Keys* case, it is hard to imagine a scenario in which a trial court could possible deem Capitol’s subcontractor’s bond a statutory bond.

After construing Capitol’s bond as a common law bond, a Florida court would likely have then found that Capitol’s bond covered the employee leasing company’s claim. Capitol’s bond defines a claimant as one “supplying labor and material in the prosecution of the work provided for in said Subcontract.” Any argument that the employee leasing company did not fall within this profoundly broad language would not have held much sway.  

9. The Proposal

Contract bond sureties often underwrite risk based upon the financial strength of the principal and its indemnitors. In addition to relying upon factors such as credit, collateral, personal net worth, type of contractor, years in business and work on hand, a surety should also pay close attention to the language of the bond, particularly when it comes to subcontractor’s bonds. Where a surety is permitted to do so, it should attempt to draft subcontractor’s bonds that adopt the same protective measures as the statutory scheme designed to protect the owner/surety – at least with respect to the class of bond claimants.

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12 See *Dow-Par*, 644 N.E.2d at 156.
This can often be accomplished by simply referencing the statutory section providing the definitions for eligible claimants.

Had Capitol been permitted to adopt the definitions of eligible claimants under section 713.01, or had it been permitted to restrict the scope of eligible bond claimants to those claimants otherwise entitled to recover against the general contractor’s payment bond, it would have been overwhelmingly difficult for the employee leasing company to recover against Capitol’s bond.

10. Drafting a Common Law Bond with Some Statutory Protections.

Attached as Exhibit C is a copy of Form Drafting Guide: Matters to Be Considered in Drafting Statutory Bonds, 3B Am. Jur. Legal Forms 2d Bonds §43:14. While this checklist applies to statutory bonds, many of the same considerations must be taken into account when drafting a common law bond, such as a subcontractor’s bond.

11. Conclusion

Commentators have suggested that an owner ought to be entitled to call for more protection than what might otherwise be mandated by mechanic’s lien statutes. It is hard to imagine, however, a need for an owner or general contractor to require bond coverage for individuals or entities which would never have a lien, or, in the alternative a recoverable claim against the general contractor’s payment bond. The fact is a general contractor has no incentive to craft bond language that limits the scope of eligible bond claimants to those that would otherwise make claims against its bond, and in most cases will provide a bond form with expanded coverage provisions. These provisions mean a surety will end up underwriting unnecessary risk. Sureties should take steps to insure that their bonds comport with the statutory requirements when underwriting statutory bonds and should be careful to limit their exposure when drafting subcontractor’s bonds and other common law bonds.