

# Surety Bond Quarterly

AN OFFICIAL PUBLICATION OF  
THE NATIONAL ASSOCIATION OF  
SURETY BOND PRODUCERS

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## Be Guaranteed to Succeed Campaign: Surety Drives Project & Personal Success

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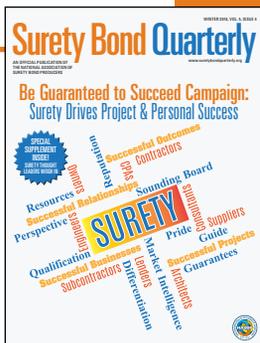


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### ON THE COVER

#### WINTER 2018

The driving force behind contract surety is project success. A new NASBP public relations campaign aims to drive that message home by raising the status and the visibility of the industry's product.



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Sugar Land, TX

## ANNUAL MEETING & EXPO

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Austin, TX

## NASBP ROAD SHOW: BONDING WITH BOB

February 2019  
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## LEGISLATIVE FLY-IN

June 5-6, 2019  
Washington, DC

## NASBP ROAD SHOW: BONDING WITH BOB

February 2019  
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## SUMMER SURETY SCHOOL—Levels I, II, III & COMMERCIAL SURETY

August 4-9, 2019  
Bellevue, WA

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From the CEO

# Guarantee the Success of Surety; It's Time to Tell Our Stories!



Few would argue that the surety industry is well-known outside of its immediate circle of participants and stakeholders. Among those with varying levels of exposure to surety bonding, many may harbor basic misperceptions of the role and function of surety bonds. Some might even contend that the industry has not sought to foster strong brand awareness and that the industry has relied far too long on the fact that its bonds are required by statute or by regulation, rather than elected by choice. Such reliance may have been acceptable when competitive bidding was the predominant public procurement method around the country. But times have changed, and procurement methodologies and project financing have changed as well. To continue a strategy of “they will come” seems nothing more than complacency, and complacency, it is said, kills opportunities for the future.

Such thoughts have fueled the actions of NASBP leaders, emboldening them to undertake an unprecedented campaign to bolster the public image of surety bonding to key constituencies and the public. NASBP identified and retained a prominent public

relations firm to script a campaign, titled “Be Guaranteed to Succeed.” The campaign is comprised of different components: informed, unified messaging, a campaign website ([www.nasbp.org/guaranteed](http://www.nasbp.org/guaranteed)), a downloadable communications toolkit to empower local action, social media posts and templates, print and digital ad placements in information markets to owners, contractors, design professionals and others, and testimonial videos, among other tools and deliverables. Attendees at NASBP regional meetings this year have received an overview of the public relations campaign to date, including the debut of several of the testimonial videos, which personalize tangible benefits of surety relationships in the words of bonded principals. More short videos are on their way, for as entrepreneur Richard Branson once said, “A good PR story is infinitely more effective than a front page ad.”

NASBP realizes that shaping or changing perceptions about an entire industry will not occur without a sustained effort, and the NASBP leadership is committed to a multi-year public relations campaign, which will continue to expand and change shape over time to extend its reach. In many regards, NASBP had embarked on this journey well before the present campaign; this magazine, *Surety Bond Quarterly*, and the NASBP e-newsletter, *NASBP Smartbrief*, both of which offer free digital subscriptions, are two vehicles by which NASBP has been offering information on and shaping the picture of surety to thousands. The “Be Guaranteed to Succeed” Campaign, [www.nasbp.org/guaranteed](http://www.nasbp.org/guaranteed), is the next logical step in moving surety out of relative obscurity and into its rightful position of being seen as a partner to

successful businesses and to successful project outcomes.

This issue of *Surety Bond Quarterly* provides information that can empower you to be a capable surety brand ambassador. Author Krista Neher, a leading authority on internet and social media marketing, provides an article that details the steps to take to build your own online personal brand that is memorable, authentic, different and educated, steps also transferable to being a positive surety brand ambassador. In another article, NASBP members Mark Munekawa and Tracy Tucker discuss their leadership roles in formulating the present “Be Guaranteed to Succeed” campaign and their insights into spreading the positive stories of surety to clients and to the public. You should also note among the pages of this issue a full-page print advertisement that is one of the ads developed for the campaign for placement in various trade press markets.

Each surety professional’s willingness and actions to be a surety brand ambassador can preserve a bright future for surety bonding as a venerated product with associated relationship benefits and a wonderful way to make a livelihood. I cannot think of anything more important to our cherished surety industry than devoting time and resources to the pursuit of an effective public relations campaign. The power to effect and to project a positive and purposeful image cannot be understated. In the words of Microsoft founder Bill Gates, “If I was down to my last dollar, I would spend it on public relations.”

Warm regards,

**Mark H. McCallum**  
NASBP CEO

## NOT IF, BUT HOW

# Embracing the future in the credit and surety business

Earlier this year, Munich Reinsurance America, Inc. (Munich Re America) appointed Sarina Puccio to the position of Head of the Credit and Surety Team. Sarina succeeded Frank Bonner who retired from the company after a 40 year career in the surety industry. We are very grateful for Frank's many contributions to both Munich Re and the industry. We wish him a wonderful retirement and congratulate him on an excellent career.

The insurance industry is experiencing many changes driven by a number of factors including the trend towards globalization, the consolidation of sureties, and digitization. As a result, this puts an increased strain on our primary surety clients to retain good business. With continued pressure on terms and a demand to provide more value-added service, the current marketplace is more competitive than in the recent past. As one of the global leaders in reinsurance, Munich Re is constantly driven by the question: How can we continue to be a valuable partner in a changing environment?

### Reaping the value of first-rate service and diverse expertise

Throughout this change, Munich Re America remains committed to the surety and credit insurance industry and to providing our clients with the highest quality service. We view our relationship with each of our surety clients as a partnership and will do our utmost to help them achieve their strategic objectives. Our very strong Credit and Surety Team enables us to provide the high-quality client service that both our clients and we expect. Our team of professionals possess deep industry expertise as well as backgrounds in a number of relevant fields including actuarial science, international business, and primary surety. This team, along with the global reach of the Munich Re Group, positions us exceptionally well to adapt to a rapidly changing environment. Below is a brief snapshot of Munich Re America's Credit and Surety Team.

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As one of the global leaders in reinsurance, Munich Re is constantly driven by the question: **How can we continue to be a valuable partner in a changing environment?**

“The one aspect of the business that I enjoy most is the people and their interest in building long-term relationships.”

– Sarina Puccio

**Sarina Puccio**

Head of the Credit and Surety Team, joined Munich Re America as a Vice President and Production Underwriter for the credit, surety, and political risk business in January 2017. She previously served for nearly five years as a portfolio underwriter, credit, surety, and political risk, for a European-based reinsurance company that underwrites business in the U.S. market from abroad. From 2003 to 2012, she was employed by one of the largest credit insurers in the world holding a variety of positions in client and project management and branch and field support working in the firm’s German and French offices.

**Karsten Herrmann**

Political Risk Trade Credit Manager, completed his law studies in Munich with additional legal clerkships in Athens, Sydney, London, and Moscow. In 1999, Karsten joined Munich Re in Germany as a Graduate Trainee and participated in a rotation through the organization including placements with a primary insurer and in the company’s Singapore office. In October 2003, Karsten was transferred to Munich Re’s

Credit and Surety Team and has since held various positions of increasing responsibility. Karsten is a member of the U.S. Trade Finance Advisory Council that advises the U.S. Secretary of Commerce on a variety of matters including how to improve access for financing especially for small to medium-size enterprises.

**Charles Costantini**

Senior Production Underwriter, Surety, has been with Munich Re America for 20 years and has more than 20 years of experience in the reinsurance industry. He brings a strong analytical skill set to the team, leveraging his expertise from his prior role within the company as an actuary.

**DJ Pennett**

Production Underwriter, Surety, joined the Credit and Surety Team in 2006 after spending seven years in primary surety. Prior to his surety career, DJ spent 13 years in the construction industry working for and ultimately managing a family-owned business in New Jersey. With over 30 years of related industry experience and expertise, DJ brings a unique perspective and knowledge base to the Credit and Surety Team

as well as to the company’s surety clients. He particularly enjoys the team environment at Munich Re as well as working closely with other surety experts.

**Rob Piaia**

Production Underwriter, Surety / Political Risk & Trade Credit, joined the team in July 2018 from the primary surety side, where he was responsible for field production underwriting in the Northeast Region. His nine years of experience also includes roles as a Business Analyst and Fidelity Underwriter. Prior to joining the Surety & Fidelity industry, Rob received his MBA degree from the University at Buffalo with a concentration in Finance. He was drawn to Munich Re America’s Credit and Surety Team by the company’s global presence and innovative culture.

**Tom Krech**

Surety Specialist, has been responsible for the Canadian market since November 2016. Prior to joining Munich Re, Tom gained an in-depth understanding of this market by working as a surety underwriter for seven years at a large primary insurance carrier.

# Be Guaranteed to Succeed

## NASBP's new industry public relations campaign highlights surety's role in project success

**WHAT IS YOUR** answer when an owner, contractor, or lender asks why surety is important? Instead of launching into a detailed technical explanation involving contracts, risks, and performance, try this response: *"Surety ensures project—and personal—success."*

That's the slogan at the heart of NASBP's new *Be Guaranteed to Succeed* campaign, launched at the association's Annual Meeting in April. The campaign is the result of more than two years of work by a volunteer task force (formed by 2016-2017 NASBP President Lynne Cook of Early, Cassidy & Schilling) and members of the NASBP's Executive Committee.

"Lynne Cook felt that we didn't do a very good job of communicating what we do to the general public—what our product is and how it can be used," said Tracy Tucker, the Tucker Agency. He originally chaired the marketing task force and then served as co-chair with Past President Susan Hecker, Arthur J. Gallagher & Co., as that group focused on a public relations campaign.

The 20 members of the task force spent most of the first year talking to NASBP members about what they thought was needed to improve the industry's status and the visibility of its product. In addition, the NASBP Executive Committee (Immediate Past President Howard Cowan, President

Robert Shaw, First Vice President John Bustard, Second Vice President Mark Munekawa, Third Vice President Tracy Tucker) asked the PR firm GMMB to interview surety company representatives, contractors, lenders, public owners, private owners, public officials, members of the Surety & Fidelity Association of America, and others to get their perception of surety bonds and the industry.



Go to [www.nasbp.org/guaranteed](http://www.nasbp.org/guaranteed) and learn more about the campaign.

"There are so many stakeholders coming from different directions who influence the use and the perspective of what surety bonds are and what the role of a bond producer is. Our challenge was how to capture all those various points of view," said Mark Munekawa, Woodruff-Sawyer & Co., NASBP Second Vice President. He's worked on the PR project and will continue to support it during his upcoming presidential year.

Despite interviewees' disparate viewpoints, a common theme emerged. "We found that the universal comment about surety, the projects we do, and the projects that the owners

were creating all had to do with success. That was the driving force. Once they started a project, its success was their biggest accomplishment," said Tucker.

From this, NASBP and GMMB developed a new communications strategy. "Framing surety in terms of successful outcomes for projects and personal reputations—and using language that is less technical and more connected to the pride and accomplishment clients feel about their projects—can help shift perceptions of surety from a line-item cost to a business advantage," according to NASBP's new Producer Communications Toolkit, developed for the *Be Guaranteed to Succeed* Campaign.

"Our message can't just be what we do and how we do it; it also has to be why we do what we do," explained Munekawa. "We want to take it to the next step, so that people understand why surety matters, why our role matters, and why what we do influences contractors, project owners, and lenders in a positive way. That's the message we really need to deliver."

### Tools for Success

One important advantage of NASBP's new campaign is that it provides surety bond professionals with a single, unified approach to explaining the



importance of surety. To help spread that word, NASBP has launched a special *Be Guaranteed to Succeed* website (<https://www.nasbp.org/guaranteed/home>) that's directed to surety customers.

When visitors click on "Surety is for Owners" and/or "Surety is for

Contractors," they get brief, targeted explanations of how surety benefits each group. In addition, the website provides an easy way for potential customers to locate NASBP members in their area.

The website's Surety Stories section links to compelling videos of

contractors talking about how surety has helped their businesses:

- David Mik & Hilary Tigue of Power Engineering Construction Company explain the value of a surety relationship in the success of their marine construction firm performing challenging construction projects.
- Ken Wenham of Roebbelen Contracting talks about how his surety partners have supported his business, including through an ownership transition.
- Rich Zito describes how the relationship with his surety producer has helped his business, DMZ Builders, get work and grow, even though he started his business later in his professional career.

More videos will be added to the site as the campaign continues.

The other campaign tool, the **Producers Communications Toolkit 2018**, is a how-to guide for NASBP members.



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(It's available for download on the *Be Guaranteed to Succeed* website <https://www.nasbp.org/guaranteed/home>.)

The Toolkit starts by explaining the research and reasoning behind the *Be Guaranteed to Succeed* campaign. From there, it offers suggestions for communicating the campaign's major ideas. The Toolkit includes:

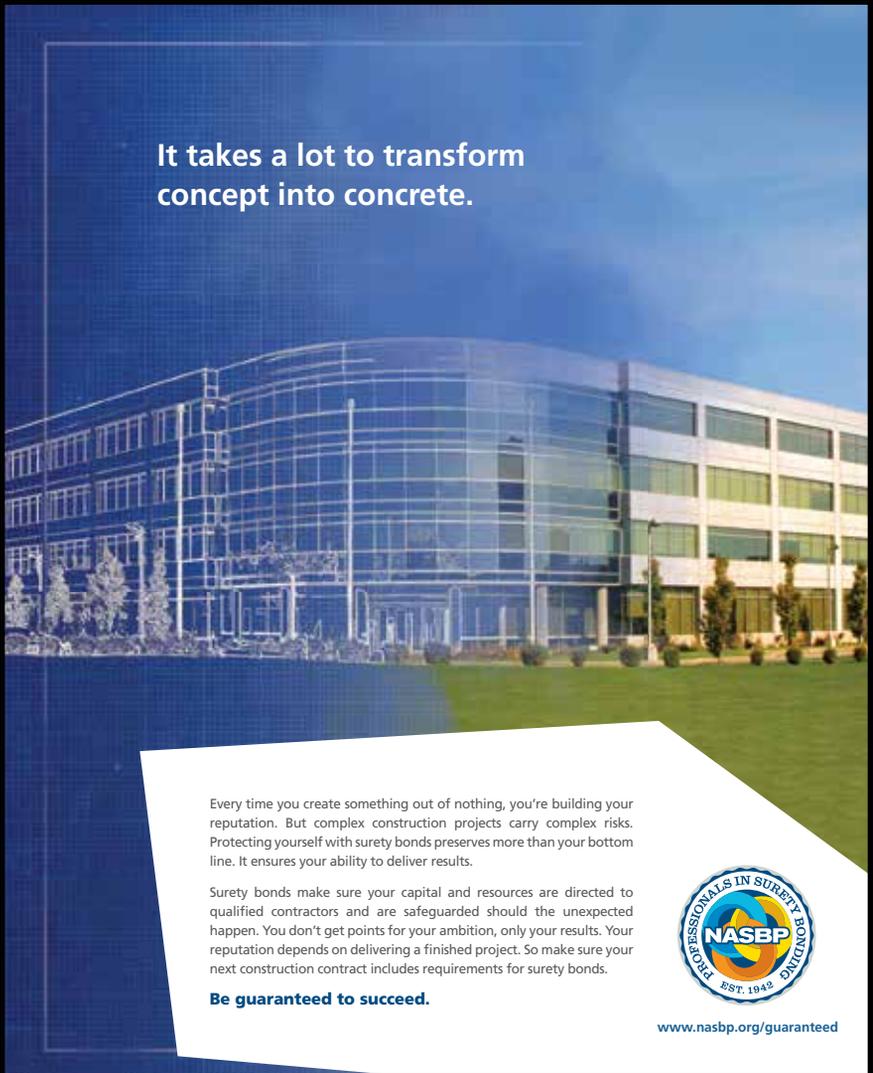
- An "elevator speech" that provides a succinct way to talk about the value of surety.
- Summaries of the different mindsets of owners, contractors, and lenders and suggested talking points for each group that address the issues most important to them.
- A downloadable surety "sell sheet" that can be printed and distributed to help reinforce the value of surety with potential clients. The sell sheet can be customized with an agency's logo and contact information.
- Downloadable *Be Guaranteed to Succeed* content—copy and images—for use on social media (Facebook, LinkedIn, and Twitter).
- Detailed information, up-to-date best practices, and tips on how to use social media to communicate the concept that "surety ensures success."

### Member Participation Critical

Both Tucker and Munekawa stress that it will take the efforts of all NASBP members to make the *Be Guaranteed to Succeed* campaign effective.

"As an executive committee, we have really made the decision to invest time and resources into a campaign that we think is very important to the industry. People need to understand that we've done this, but it can't succeed without every member taking it upon himself or herself to help carry the message to their local business community and to their circles of influence," said Munekawa.

"Members don't have to spend money; they don't have to create anything or make any decisions. We are giving them the tools they need to help them make some presentations or even just talk casually to friends or



**It takes a lot to transform concept into concrete.**

Every time you create something out of nothing, you're building your reputation. But complex construction projects carry complex risks. Protecting yourself with surety bonds preserves more than your bottom line. It ensures your ability to deliver results.

Surety bonds make sure your capital and resources are directed to qualified contractors and are safeguarded should the unexpected happen. You don't get points for your ambition, only your results. Your reputation depends on delivering a finished project. So make sure your next construction contract includes requirements for surety bonds.

**Be guaranteed to succeed.**



[www.nasbp.org/guaranteed](http://www.nasbp.org/guaranteed)

to their bankers about surety when they see them," Tucker added.

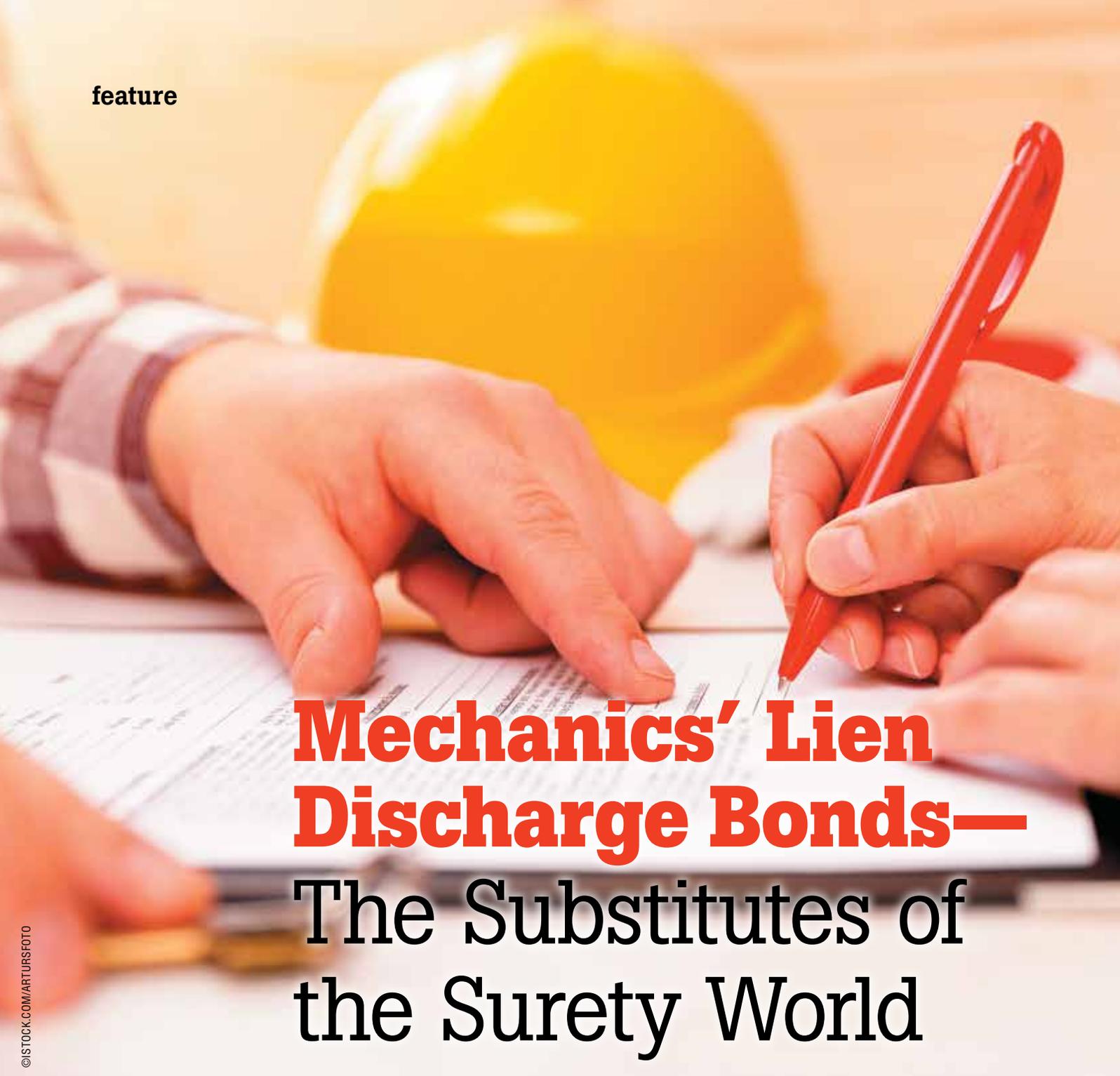
NASBP plans to develop training programs to assist members in this outreach. Online virtual seminars, run by social media-savvy members, will demonstrate how to use the various components of the *Be Guaranteed to Succeed* campaign on platforms like Twitter, LinkedIn, and Facebook. The campaign will be highlighted at NASBP's Annual Meeting next year as well.

"We also anticipate that the NASBP board members are going to be very involved in helping to convey the message down to the grass roots," Munekawa added. "Every geographic area of the country has different key players, and, thankfully, NASBP has active members in almost every one of those key areas. We are really

going to be looking to them to reach out to local surety associations so that they also understand what we are trying to do. We are trying to get other partners in the surety industry to help us convey the message."

NASBP will be sharing a limited number of the informational tools with surety bond producers who aren't members because this campaign is so important to the overall industry.

"What we are really trying to accomplish is changing the way that people look at surety," Tucker said. "Don't just think of the surety as the people who come in and solve the problem. Think of surety as the people who resolve the problem before it ever happens. You hire us and we keep you out of trouble, but if there is trouble, we have the product there to fix it." ●



# Mechanics' Lien Discharge Bonds— The Substitutes of the Surety World

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BY MIKE F. PIPKIN AND JACOB L. MCBRIDE

**AS KIDS IN** school, just about everyone loved substitute teacher days. They typically meant a departure from the daily routine and a reprieve from the normal class rules. Substitutes meant a little extra time in PE or watching videos. Sometimes, they meant relief in the form of extra time to study for an exam, or to complete an otherwise late assignment. This relaxed environment also brought out the worst in some classmates, which could create its own set of risks. For the most part, however, finding a different face at the head of the classroom was usually a good thing.

Mechanics' lien discharge bonds are the substitutes of the surety world. They substitute for a previously filed mechanics'



## MANY CONTRACTORS HAVE LEARNED THEIR LESSON THE HARD WAY BY FAILING TO FOLLOW PROCEDURES, FAILING TO GIVE TIMELY NOTICE TO ALL NECESSARY PARTIES, OR FAILING TO FILE SUIT TO FORECLOSE IN TIME.

from foreclosure, while contractors have a simpler alternative to recovery than foreclosure.

### **The Teacher—Mechanics' Liens**

All 50 states have mechanics' lien statutes aimed at protecting the interests of contractors and subcontractors that supply material and/or labor on construction projects. While these statutes vary greatly in form and substance, the general principle is the same: by timely following the locally prescribed procedures, an aggrieved contractor can place a lien on the project that is duly recorded in the local property records. When done properly, these liens give the contractor significant leverage, allowing it to foreclose its lien and take possession of the subject property, if the invoices remain unpaid.

However, you need not search long to discover why these statutes with their varying requirements make great teachers. Many contractors have learned their lesson the hard way by failing to follow procedures, failing to give timely notice to all necessary parties, or failing to file suit to foreclose in time. Contractors that operate across state lines have the added difficulty of navigating different lien perfection requirements in each state. In some states, contractors may need to start sending their notices of intent to file a lien before their outstanding invoices are due or risk losing the ability to secure payment with a lien for all the work they performed. The complexity of the process increases when it comes to competing and often prior liens, stringent judicial foreclosure requirements, and equally varied and convoluted statutes governing how foreclosure proceeds are to be disbursed. Failing to protect lien rights,

thereby losing leverage to obtain payment, is a tough teacher.

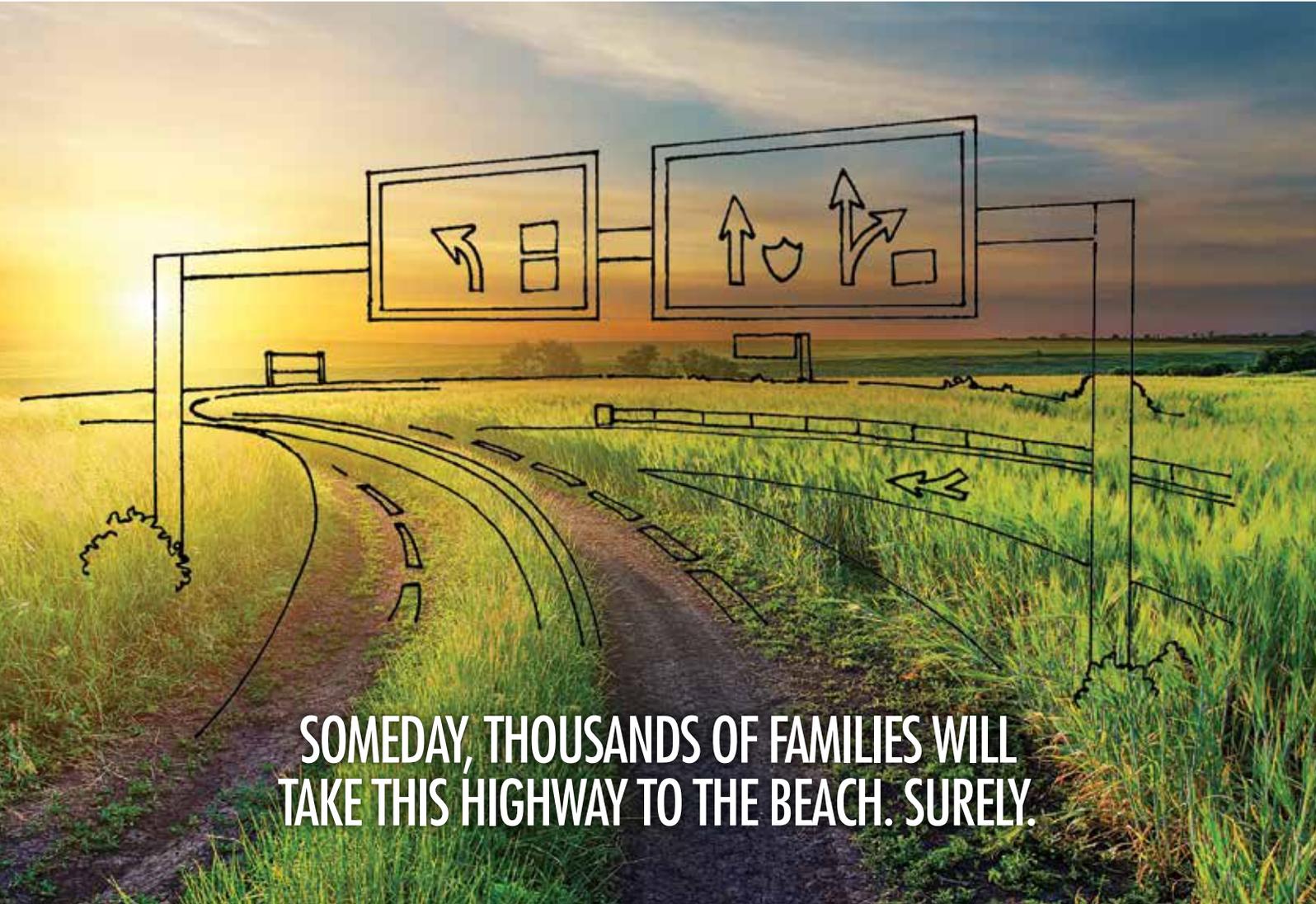
As for property owners, little needs to be said about the burden that a mechanics' lien places on the project. Aside from the risk of losing property in foreclosure, the filing of the lien itself places a cloud on title and may constitute a breach of a mortgage, deed of trust, or other security agreement, triggering action by a prior lienholder. As such, most states also provide property owners with ways to protect their property from foreclosure and limit liability under a mechanics' lien, including the option of bonding around the lien.

### **The Substitute—Mechanics' Lien Discharge Bonds**

Most states have statutes setting forth the rules, timing, and other procedures for lien discharge bonds. Like their mechanics' lien counterparts, these statutes are equally varied. But the general principle is the same: by following locally prescribed procedures and requirements, which may include provisions on timing, notice, filing, or recording, and which may set bond amount minimums, an owner or other stakeholder may purchase a bond to discharge the lien. The contractor's security interest in the subject property through its lien is replaced or substituted by the bond. Many states allow other lienholders or stakeholders to purchase lien discharge bonds, including mortgagors, trustees, co-owners, or any other party with an interest in discharging the bond.

The result of the lien discharge bond is a largely positive outcome for the contractor and the owner or other bond principal alike. The owner avoids foreclosure and restores clean,

or materialman's lien, providing relief to owners and contractors alike from the onerous procedures, rules, and remedies that such liens carry with them. They may provide added time to negotiate a settlement by substituting their own statutes of limitations. While mechanics' lien discharge bonds are not without their risks, they offer a satisfying alternative in that owners and other stakeholders can insulate their property interests



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marketable title to the property, allowing the owner to market and sell the property while preserving his or her defenses to the contractor's claims. The contractor's interests are likewise protected, with the bond substituting for the security interest in the property that the lien provided. The bond also presents a simpler alternative to recovery than foreclosure. Lien discharge bonds may also extend the time available for the parties to mediate or otherwise attempt to settle their dispute before engaging in costly litigation.

Like the substitute teacher, lien discharge bonds can provide a reprieve and reduce the pressure brought on by a mechanic's lien.

### **The Substitute's Risks—Into the Fray**

Unlike a typical payment bond, issued to protect against potential future circumstances, a lien discharge bond is born out of an existing dispute over nonpayment that resulted in a lien being filed on real property. In other words, a surety executing a lien discharge bond steps into a situation where the principal is already not paying the obligee(s). Furthermore, to provide additional protection to lien claimants that lose the persuasion of the foreclosure power, many states require lien discharge bonds to be executed in amounts exceeding the total value of the liens on the property. As an example, the Texas Property Code requires bonds to indemnify against a lien to have a total penal sum double the value of liens totaling \$40,000 or less. For lien amounts greater than \$40,000, the penal sum of the bond must be the greater of 1.5 times the value of liens or the amount of the liens plus \$40,000. These circumstances present additional risk to a surety bond provider executing lien discharge bonds. As such, keen underwriting and collateralization are key in protecting the surety's interests. These risks are tempered by the fact that, unlike a typical payment bond with its broad scope covering an unknown number of potential claimants with an unknown value of claims

at the time of execution, the scope of a lien discharge bond is limited to specific, identified lien claimants with specific, limited lien values, giving an underwriter a clear basis to assess the risk.

Despite these risks, the surety substitute is not without its defenses. Like the wise substitute teacher who learns and enforces the class rules, the surety can assert the defenses of its principal. Because a lien discharge bond provides substitute security for the lien, most states require a claimant to have complied with the requirements of the lien statute to make a claim on the bond. The lien discharge surety can defend against a claim by identifying any defects in the lien claim, such as failure to meet standing requirements, failure to provide proper notice, and failure to perfect the lien claim, among others. The surety may also use any substantive defenses it has available to the validity of a claim as well as applicable affirmative defenses, such as statute of limitations and waiver. When defending such a bond claim, it is important to consider that most lien discharge bonds are statutory bonds and the courts will look first to the language of controlling statutes.

### **Not the Only Substitute Competing for the Job**

As varied and diverse as the mechanics' lien and lien discharge bond statutes are throughout the country, there is an equal variety of title insurance regulations and policies occupying an overlapping role in circumstances where an owner seeks to market a property subject to a lien. While title insurance companies are typically prohibited from issuing a clean title policy in the face of outstanding mechanic's liens, many states are providing exceptions that allow the title insurer to "insure around" this cloud on title. These exceptions include circumstances where a title company obtains an indemnity agreement from a bank or other financial institution, or where sufficient funds are deposited with the title company. In other words, title companies can step in and fill the surety's role. Like

the substitute teacher who doesn't act quickly to accept a placement, the job may go to another player.

For banks and other financial institutions, these insure-arounds come with their own set of exposure and risk. Arguably, the lien discharge bond is a more marketable option than a title company insure-around, because of the certainty and stability it provides the parties involved. Nevertheless, surety bond producers may continue to lose business to title companies willing to comply with regulations to insure around a lien. Indeed, aside from the owner simply paying off the lienholder to discharge the lien, a lien discharge bond is likely the most simple and secure option, a feature which must be highlighted in the market.

### **Here's to Substitutes!**

Mechanics' liens often result in foreclosure litigation or other disputes that could be avoided with the lien discharge bond. These bonds are practical and marketable and provide a more stable option for all parties involved. ●

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feature

# Potential Pitfalls Under the Contract Disputes Act

## for Federal Government Contractors, Sureties, and Surety Professionals

Part 2 of 2



BY SARAH K. CARPENTER

The background of the page features a close-up, slightly blurred view of architectural blueprints. A wooden gavel with a silver metal head is positioned in the lower-left foreground, resting on the blueprints. The lighting is bright, creating a professional and legal atmosphere.

For an overview of basic information any party contracting with the government should know when faced with the necessity of making a claim against the federal government under the Contract Disputes Act, see Part One of this article, which is titled “The Contract Disputes Act: What Every Contractor, Surety, and Surety Professional Should Know” and published in the fall 2018 issue of *Surety Bond Quarterly*.

**THE CONTRACT DISPUTES ACT (CDA)** governs monetary and non-monetary disputes arising out of contracts or implied-in-fact contracts between the federal government and any party to a government contract (contractor). Because the CDA is an exclusive remedy, it is important that contractors and surety professionals be wary of the many pitfalls that may be encountered by a contractor seeking to assert a claim against the government under the CDA.

The pitfalls faced by a contractor under the CDA can arise before a contractor becomes aware of a potential claim. Pursuant to the Federal Acquisition Regulation (FAR) § 43.204(c), a contracting officer should include in any supplemental agreement, including any change order, a Contractor’s Statement of Release, which requires a contractor to execute a broad release of the government from any and all liability under the contract. As a result of this FAR provision, in executing a routine change order, a contractor may inadvertently release its right to pursue a potential claim under the CDA. A contractor should always review any release language prior to executing a supplemental agreement or change order with the government.

For sureties, the issue of standing to bring a claim under the CDA must be analyzed as preliminary matter. The CDA defines a “contractor” as “a party to a government contract” so that only a party in privity with the government may bring a claim under the CDA. Even where a surety has been assigned all rights and claims of a contractor or a surety is entitled to equitable subrogation of contractor’s rights, its status as an assignee or subrogee cannot confer the privity required to bring a claim under the CDA. As an initial matter, a surety must ensure it has executed a take-over agreement or is otherwise in privity with the government prior to asserting a claim under the CDA.

Once it becomes aware of a potential claim, a contractor may become ensnared by the specific criteria necessary to make a claim under the CDA. To qualify as a claim

under the CDA, the claim must be in writing. Verbal demands made by a contractor upon a contracting officer do not constitute a claim under the CDA. Furthermore, a contractor’s written claim must include a demand or assertion. A mere notification by a contractor notifying a contracting officer of an issue or an amount the contractor believes it is entitled to does constitute a claim under the CDA. All claims must be directed to the contracting officer. Field representatives and technical representatives do not have authority to respond to claims.

Under the CDA, a contractor’s written demand or assertion must seek the payment of money in a sum certain, the adjustment or interpretation of contract terms, or other relief arising under or relating to a contract between the government and the contractor. Whether a contractor’s claim is a “sum certain” will be dispositive of whether the claim may be asserted under the CDA. A contractor’s claim must be either a sum certain, that is, a fixed or specific amount of money, or capable of determination by a simple mathematical formula. A contractor’s assertion for payment “approximately” or “in excess of” an amount will not constitute a claim under the CDA.

Additionally, in order to constitute a claim under the CDA, the claim by the contractor must include a specific request for a final decision or otherwise set forth a clear indication that the contractor would like the contracting officer to issue a final decision. As a matter of good practice, a contractor should explicitly request a final decision from the contracting officer in its claim.

A contractor must also be cognizant of any time limitations in bringing a claim under the CDA. “Claims by federal contractors are subject to a six-year statute of limitations, which means that claims must be submitted within six years of the time when all events establishing alleged liability for the claim were known or should have been known.” However, a contractor’s claim may be subject to additional

time or notice requirements under the FAR, particularly if the claims relate to changes, differing site conditions, or suspension of work.

Another specific requirement that must be satisfied to assert a claim under the CDA is a contractor's certification of any claim in excess of \$100,000. For claims exceeding \$100,000, a contractor must certify that (i) the claim is being asserted in good faith, (ii) the supporting data are accurate and complete to the best of

the contractor's knowledge, (iii) the amount requested is accurate, and (iv) the person asserting the claim is duly authorized to certify the claim. Importantly, the omission of this certification cannot be cured by a retroactive submission of the certification. Furthermore, a contractor cannot avoid this certification requirement by separating a single claim into multiple claims in amounts less than \$100,000. It should also be noted that a contractor's certification is required

to be signed and that, according to the ASBCA, a typewritten name intended to be a signature does not meet this requirement.

A contractor's certification of a claim can be particularly troublesome for pass-through claims submitted against the government by the contractor on behalf of a subcontractor. Although a contractor may and should obtain a certification from a subcontractor for any pass-through claims, the contractor is required to provide a certification for the claim as well. However, a contractor does not have to agree with every aspect of a pass-through claim and must only certify that the pass-through claim is brought in good faith.

Once a contractor asserts a claim under the CDA, a contracting officer is required to issue a final decision on the claim. After receipt of a final decision by a contracting officer, a contractor may choose to engage in alternate dispute resolution (ADR) with the government regarding its claim. However, if a contractor decides to pursue ADR prior to, or instead of, appealing the contracting officer's final decision, the contractor should be aware of the expiration of the statute of limitations and any notice requirements because participating in ADR with the government does not toll or extend these deadlines. Additionally, when sureties engage in ADR with the government, they must be aware of limitations on their ability to settle a contractor's claim. Specifically, a surety—even a surety that has stepped into the shoes of a contractor as assignee or subrogee or entered into a takeover agreement with the government—cannot waive a contractor's right to bring claims under the CDA. A contractor has an unwaivable right to bring claims under the CDA and to appeal the contracting officer's final decision, even if it has entered into an indemnity or assignment agreement with its surety prior to the submissions of its claims.

If the contractor chooses to appeal the final decision to the United States Court of Federal Claims or one of the agency boards of contract appeals (BCA), additional pitfalls are presented

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under the CDA, beginning with the contractor's choice of forum for filing its appeal. A contractor must file a BCA appeal within 90 days of receipt of a final decision. Alternatively, a contractor has 12 months from receipt of a final decision to file with the Court of Federal Claims. Once a contractor elects the forum for its appeal, it can no longer bring its claim in the other forum.

In filing its appeal, a contractor could become ensnared by a seemingly simple decision regarding which carrier to use to deliver its appeal of the contracting officer's final decision to a BCA. For example, pursuant to the Armed Services Board of Contract Appeals rules, the date of the filing of an appeal is the date of transfer of a properly addressed, postage-paid package to the United States Postal Service. Conversely, an appeal delivered by a commercial carrier, such as FedEx or UPS, is deemed filed on the actual date it is received by the Board. Although appeals may now be submitted by email, it is best practices for a contractor to submit its appeal in sufficient time to permit the contractor to correct any issue with the transmission of the appeal.

One pitfall that often arises while a contractor is in the process of litigating its claim, either before the Court of Federal Claims or a BCA, is the issue of whether the contractor is attempting to appeal a claim that was not subject to a final decision by a contracting officer. It is a jurisdictional prerequisite that all claims asserted under the CDA must first be subject to a final decision by a contracting officer. If the contracting officer fails to issue a final decision within the time limits prescribed by the CDA, the contractor can file a "deemed denied" appeal. This typically results in an order requiring the contracting officer to issue a decision.

After an appeal is filed, the contractor may want to assert a claim that has not been subject to a contracting officer's final decision. If the claim asserted is an entirely new claim, it cannot be addressed on appeal. However, a claim derived from the same operative facts and seeking the

same relief but merely asserting a new legal theory for a claim that has been properly appealed is generally permitted and is not considered a new claim.

From the beginning of a contractor's work on a government project through a contractor's appeal of a contracting officer's final decision, the Contract Disputes Act presents pitfalls that every contractor and surety professional should know and seek to avoid.

*A version of this article is appeared in the February 26, 2018, Smith, Currie*

*& Hancock, LLP newsletter, Common Sense Contract Law.*

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# KNOW THE FUNDAMENTALS of Contractor Financial Statement Analysis

## Part 2 of 2

Part one of this article was published in the fall 2018 *Surety Bond Quarterly* and addressed the different service levels that contractor clients can receive from CPAs, what level of assurance the users of the financial statements should expect, and aspects of a contractor's balance sheet.



BY JULIAN M. XAVIER

**THIS ARTICLE HIGHLIGHTS** a contractor's income statement and key disclosures that should be included in a contractor's financial statements.

### Contractor Income Statements

When analyzing a contractor's income statement, there are a few items of significance that should be noted. Regarding contract revenues, cost, and gross profit, ideally there will be a breakdown of the types of construction costs (materials, subcontracts, equipment, etc.) either on the face of the income statement or as a supplemental schedule. Additionally, if there are different sources of revenue, such as construction, aggregate sales, etc., these should be broken out on the income statement as well. If a contractor has an equity-method joint

venture investment, the contractor can either show his or her share of the profits/losses from the joint venture as one line item as shown below, or the contractor can record the percentage interest of the revenue and costs and gross up the income statement to show his or her interests in the joint ventures. If the joint venture activity is significant, showing the proportionate share of revenue and costs will present a better picture of the contractor's efforts for the year from a volume perspective. Lastly, remember that a pass-through entity won't record income tax expense as the company's profit will be passed through and taxes paid by the company's shareholders. Users of financial statements need to factor this in when comparing profitability of C Corporations to pass-through entities.

Below is a sample contractor's income statement with key items highlighted.

### Key Disclosures

Some of the key disclosures that should be included in a contractor's financial statement include a summary of accounting policies related to revenue recognition and contract costs, accounts receivable, a reconciliation of over/under billings on contracts, revisions in contract estimates, and information on unapproved change orders and claims.

### Summary of Accounting Policies

A contractor should include information on how the contractor recognizes revenue on his or her construction contracts. If a contractor is using the percentage of completion method, the contractor should disclose the basis for determining percent complete (that is, cost to cost, milestones, units of production, etc.). Additionally, the overall accounting for construction costs should include a description of the types of direct

	20X1	20X0
<b>Contract revenues earned</b>	<b>\$ 22,758,800</b>	<b>\$ 16,251,600</b>
Cost of revenues earned	20,436,100	14,981,300
<b>Gross profit</b>	<b>2,322,700</b>	<b>1,300,300</b>
Selling, general, and administrative expense	895,600	755,600
<b>Income from operations</b>	<b>1,427,100</b>	<b>544,700</b>
Other income (expense)		
<b>Equity in earnings from unconsolidated joint venture</b>	<b>49,900</b>	<b>5,700</b>
Gain on sale of equipment	10,000	2,000
Interest expense (net of interest income of \$8,800 in 20X1 and \$6,300 in 20X0)	(69,500)	(70,800)
<b>Total other expense</b>	<b>(9,600)</b>	<b>(63,100)</b>
Income before provision of income taxes	1,417,500	481,600
Provision for income taxes	662,900	225,000
<b>Before net income attributable to non-controlling interest in affiliates and joint venture</b>	<b>754,600</b>	<b>256,600</b>
<b>Income attributable to non-controlling interest in affiliates and joint venture</b>	<b>(128,000)</b>	<b>(26,200)</b>
<b>Net income</b>	<b>\$ 626,600</b>	<b>\$ 230,400</b>

costs that are included in contract costs (that is, materials, subcontractors, equipment, etc.) and also the types of indirect costs included in contract costs. Disclosure should also indicate that losses on uncompleted contracts are recognized in full in the period the projected loss is determined. Additionally, there should be a general disclosure indicating that revisions in estimated contract amounts and profitability are recognized in the period in which such revisions are determined (discussed in more detail later in article). Lastly, the contractor's policy related to recognition of costs and revenues related to claims (claim revenue is recognized to extent of costs if certain conditions are met) should be disclosed.

### Accounts Receivable

As mentioned during the discussion on the balance sheet, accounts receivable are typically broken down by contracts in progress, completed contracts, and retainage. Additional disaggregation may be disclosed regarding the types of contract owners (federal, state, local, private, etc.). Concentrations of credit risks with customers and related valuation allowances associated with each type of contract owner may also be disclosed. Another disclosure item that is missed frequently is the disclosure of receivables that are expected to be collected after one year from the balance sheet date (typically, retention receivables). A nice disclosure, although not required, is a break out between open and closed jobs to let the users of the financials know how much of the outstanding receivables are from jobs that are closed. The closed jobs receivables should ideally be a less significant number as large amounts of receivables on completed projects could indicate collection issues. Lastly, retentions are also required to be disclosed if not reflected on the face of the balance sheet.

Above is a sample footnote that can be used to summarize this information.

	20X1	20X0
Completed contracts including retentions		
Contracts in progress:	\$ 65,000	\$ 46,000
Progress billings	2,535,000	2,375,000
Retentions withheld until completion	1,289,200	1,013,100
Total	3,889,200	3,434,100
Less allowance for doubtful accounts	100,000	100,000
	\$ 3,789,200	\$ 3,334,100

	20X1	20X0
Costs incurred to date on contracts in progress	\$ 50,000,000	\$ 45,000,000
Estimated gross profit to date	15,350,000	14,750,000
Contract revenue earned to date	65,350,000	59,750,000
Less billings to date	65,435,100	59,871,100
Excess of billings over revenue earned	\$ (85,100)	\$ (121,100)

The excess of billings over revenue earned is included in the accompanying balance sheets under the following captions:

	20X1	20X0
Costs and estimated gross profit in excess of billings on contracts in progress	\$ 156,900	\$ 100,600
Billings in excess of costs and estimated gross profit on contracts in progress	(242,000)	(221,700)
Excess of billings over revenue earned	\$ (85,100)	\$ (121,100)

### Billings, Costs, and Estimated Earnings on Uncompleted Contracts

The footnotes should include a recap of activity on contracts in progress from inception to the balance sheet date. This information should be derived from and reconcile to the supplemental open job schedule accompanying the basic financial statements.

Above is a sample footnote that would provide the required information.

### Revisions to Contract Estimates

One of the disclosures that is required and helps a user understand the current year results is the impact of gain/fade on the current year earnings. To calculate the change, contractors will use the updated gross profit numbers at the current year-end on all their contracts that were open at the end of the prior year, and recalculate how much gross profit would have been recognized in the prior year using the updated total estimated contract value and projected gross profit. The difference between what was originally recorded and what would have been recorded using the revised estimated amounts is disclosed. This information helps the users of the financial statements understand the impact to current year results from

significant changes in estimates on contracts.

### Unapproved Change Orders and Claims

Contractors are required to disclose certain information if they have recorded revenue for the period on both unapproved change orders and claims. This information will help alert the users of the financial statements of the magnitude of these amounts and their potential impact. The required disclosures include the following: amounts included in receivables related to unapproved change orders and claims, the total revenue and applicable costs recorded from unapproved change orders and claims, and a description of the nature and status of the principal items comprising the totals.

### Supplemental Schedules

Supplemental schedules are NOT a required part of the financial statements; however, they are typically included for banks and sureties to provide them additional insights into the contractor's results. The most common supplemental schedules include schedule of contracts in progress, schedule of completed contracts, schedule of cost of goods sold

*continued on page 38*

feature

# Building Your Personal Brand Can Give You Powerful Results



BY KRISTA NEHER

LIKE IT OR NOT, EVERYONE HAS A PERCEPTION OF YOU. DISCOVER THE SOCIAL MEDIA TECHNIQUES FOR SHAPING THAT PERCEPTION TO BENEFIT YOUR LIFE AND CAREER.



**PEOPLE DO BUSINESS** with people and brands that they know, like, and trust. This simple, age-old sales principle still drives our decisions—from the car we drive to the laundry detergent we use to the bank we use to the surety company we do business with.

Building know, like, and trust is both a big risk and a big opportunity in the digital age. The risk happens when people search for you online to assess your credibility and come up empty. The opportunity is that your digital footprint can be a powerful tool to grow your professional network and your position as an expert, which, ultimately, can impact your bottom line.

The reality is that people are Googling you before and after they meet you. They want to check you out, see your credentials, consider your trustworthiness, recommend you to a friend, or maybe they are just curious. Your online brand is like the suit you wear to look professional. It's the waiting room of your office; it's your business card; it's your first impression. Of the 75% of U.S. adults who Google themselves, nearly half say that the results are not positive (according to Google). Smart business professionals aren't just focusing on building a personal brand that isn't a liability—they are using it as a strategic tool to grow their reputation and business success.

### **What My Personal Brand Brought Me**

I started thinking about my personal brand a long time ago. In the days before Facebook I had a sweet Myspace page. I mostly used it to connect with friends, but as I started to get more visibility in my industry, I noticed that business contacts started to friend me there. While I wasn't posting anything terrible, it really wasn't how I wanted to present myself.

Over the next 10 years I've journeyed to build a strong personal brand. I started by taking LinkedIn more seriously. Then I created a blog. Then I got active on Twitter. Next I built a personal website. These were all small steps that I took one by one over many years.

When I reflect back now, most of my best professional opportunities came as a direct result of the online brand that I created for myself. International speaking opportunities. Writing a textbook. Being quoted as a media expert. Clients. Job opportunities. Writing a Dummies book. All of these things came directly because of the online brand that I crafted and strengthened over the years.

You may not want these things. Perhaps speaking doesn't appeal to you. Maybe you don't want the spotlight but want to grow your client base, industry contacts, or get a promotion. Regardless of your ambitions, your online personal brand can help you achieve your goals.

### **What is a Personal Brand?**

Your personal brand is the perception that people have about you. You already have a personal brand (whether you like it or not) as everyone with whom you come into contact has a perception about you.

We often think of branding as something that applies to consumer products like Coca-Cola or Starbucks, but people have brands, too. A brand is really just the perception that you have of a product or person—and it may be both logical (Apple makes great computers) and emotional (Apple products are cool). The idea of online personal branding is to extend your personal brand online in a smart way so you can reach more people more effectively as a business professional.

### **Building Know, Like, and Trust Online**

Building and extending relationships online is a powerful networking tool that more and more professionals are taking advantage of. Connecting with clients and prospects on social networks helps them to get to know you better and allows you to stay top of mind. Being in front of your audience continuously

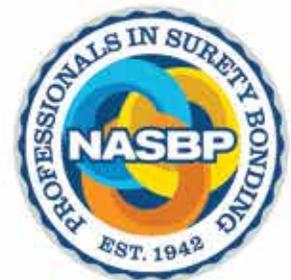


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on a network like LinkedIn helps people to think of you first when they need someone.

Your online presence can also lead to people liking you more. Studies actually show that just seeing someone more often (online or in real life) makes them like you more. So being in front of people on multiple channels can actually make people like you more.

Finally, you can build trust and credibility with your online presence by sharing relevant, interesting, and credible information. This helps to establish your expertise and really position you as an expert. With more and more publishing tools like video, live, blogs, and notes, there are more options than ever to share interesting and credible information.

### **Start with an Audit**

If you are ready to get started taking your online personal brand to the next level, start with an audit. What happens now when someone Googles you? What do they find? What public information shows up on social networks?

Some people breathe a sigh of relief when they Google themselves and don't find anything bad. But this isn't your goal. Your goal isn't to not have anything embarrassing. Your goal is to smartly position yourself as a knowledgeable business professional that people want to do business with.

### **How to Build Your Brand: Define, Design, and Deliver**

When it comes to establishing your personal brand, there are three distinct steps. Defining your brand focuses on self-discovery and deciding what you want your brand to be about, as well as your key proof-points and credibility boosters to set you apart. Designing your brand focuses on crafting smart assets that bring your brand to life in a meaningful way. Delivering your brand is about how you actually bring your brand to life. This includes everything from your elevator pitch to your LinkedIn profile, to your public Facebook information,

to how you are represented on your corporate website.

### **Define a Powerful Brand**

Before you even get started defining your personal brand, it can be helpful to explore your personal goals and objectives. What do you want for yourself and your career over the next two to five years? More clients? Better opportunities? A larger network? A promotion? Knowing why you want to build a strong online presence will help you to find the value in investing to create one and also will help you to create a strong personal brand.

The key to defining a brand that stands out is to think about your personal and professional attributes and determine how you want to present yourself. This is usually difficult for business professionals, as we don't typically think of ourselves this way; but brands and people can be positioned very differently.

Think about this. Apple Computers and Windows PCs are both making computers and software—but both are positioned very differently. Apple is usually associated as being hip and cool, while PCs are considered old and stuffy. This is true with many brands—think of the different perceptions you have about Starbucks vs. Dunkin' Donuts, or J.P. Morgan vs. E\*trade.

Evaluate yourself and start to think about:

- What makes you different vs. other similar people?
- What personality strengths do you have?
- What do people remember about you?
- What credibility boosters do you have?
- What professional accomplishments set you apart?

It is sometimes helpful to think of yourself and compare yourself to a colleague in a similar position or a competitor. What unique qualities and/or talents do you bring to the table?

Some people really struggle with this stage. If you struggle with it, you can also ask friends, a boss, or coworkers who can help you to define your strengths.

### **Designing Your Personal Brand**

Designing your personal brand isn't about creating a logo. It's about deciding how you want to present yourself online. The best and strongest personal brands are **Memorable, Authentic, Different, and Educated** (you can remember this with the acronym MADE).

#### **Be Memorable**

Be memorable to someone who meets you. Brands that are specific and clear are more likely to be remembered. When I first started thinking about my personal brand, I had just left corporate America and was at a networking event. I had started my social media marketing business but didn't want to be "pigeonholed" as a social media marketer because I could do so much more, such as branding, strategy, etc.

When someone asked me what I did, I listed a number of different things. The problem with this is they were just confused about what I really did. They would say, "Krista does something with marketing, I think." When I embraced social media and started to say, "I specialize in social media training," I found that I started getting referrals and introductions because people could easily remember what I was best at.

#### **Be Authentic**

Your brand should be true to who you are and highlight the best and most compelling parts of your personality. It is difficult for people to connect with someone who isn't real. Sharing (appropriate) parts of your personal life can deepen these connections further. People feel more connected with other people that they have things in common with—so sharing parts of you that create these connections are key.

#### **Be Different**

If you want to stand out, it is important to be unique. There are tons of people who are similar to you, of course; but what is it that makes you different? This sometimes sounds challenging to business professionals, as many others in their industry may have similar qualifications.

Think about how you approach things differently, your unique background, or your approach. Do you have unique soft skills?

Differentiating yourself is key to having a strong brand.

### **Educated**

What are the credentials and credibility factors that make people trust working with you? Many business professionals don't take the time to really dig into their credentials and

credibility, but this is really important in building trust. Have you won awards? Been published? Exceeded objectives? Achieved top-rating in your industry?

Consider the credentials that you can highlight in your online and in-person brand to instantly build your credibility.

### **Delivering Your Personal Brand**

Delivering your personal brand is about how you bring your personal

brand to life—and we especially focus on online personal brand delivery. The reality is that people search for you online before, during, and after they meet you. You want to put your best foot forward and that starts with taking charge of your online reputation.

### **Measure Your Online Wow Factor**

Start by auditing yourself. Google yourself. What do you find? Look at your social media presence objectively. What would you think of this person? Remember that the goal isn't to "not find anything bad." The goal is to have a WOW brand. The audit should give you some things to consider, and you can then start thinking about how to put them into action.

### **Content**

What type of content is most appropriate for you to be posting? Before diving in to social networks, consider the content that you will post that reveals your personality and builds a connection while also positioning you as an industry expert. As you evaluate the content that you can post, keep in mind how you can use visuals as a part of your content mix. Specifically, video and images are the two content types that perform the best online to build online personal brands.

### **LinkedIn**

LinkedIn is the natural starting point for building a strong online personal brand, as most people searches on Google show LinkedIn results towards the top. Also, many people go directly to LinkedIn to search for people online.

- Make sure you have a great LinkedIn profile that includes all of your relevant experience and credentials.
- Connect with people in a professional context who can help you grow your network and expand your visibility and brand.
- Stay active on LinkedIn and position yourself as an expert.

### **Facebook**

Check your Facebook privacy settings and make sure that you have a Facebook page that represents you

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well professionally, even if you use it as a personal social network. Consider how you want to use Facebook professionally and what type of content is appropriate based on how you plan to use it.

### Twitter

Twitter has been losing a little steam over the last few years, as other social networks such as Instagram and SnapChat, have grown in popularity. That being said, Twitter is still a powerful place to connect with industry thought-leaders, to expand your network, and to position you as an industry expert.

### Blogging

A blog is a great way to showcase your expertise and really connect with your target audience on a deeper level. Blogging allows you to share longer format thought-leadership content that positions you as an expert.

Some start their own blog, while others blog on LinkedIn, or on online publishers like Medium, while others contribute to a corporate blog.

Blogs also make a great reference point for FAQs or other questions that are often asked.

### Just START

One of the biggest mistakes that people make is waiting to get started. There are so many excuses (that are far too easy to find) that prevent us from taking action. Maybe your hair doesn't look great in the video, or you aren't as articulate as you can imagine. An imperfect but consistent starting point, however, is better than doing nothing at all.

If you are new to building your personal brand online, start with one network and really master it. As you get more confident, you'll be able to add other networks in to the mix and find efficiencies through cross-posting. Dedicate a half hour a day or a few hours to getting yourself set up and then make time a few times a week to continue to build and grow your online personal brand.

*Be sure to listen to the recording of the NASBP Virtual Seminar presented*

*by Krista Neher where she discusses the NASBP Be Guaranteed to Succeed Campaign and provides step-by-step instructions on how surety professionals can start "Growing A Credible, Powerful Personal Brand Online." Your brand is key in the relationship-driven world of surety. Purchase the recording at <https://www.nasbp.org/learn/learn-virtualseminars>.*

*Krista Neher is an industry expert, trainer, and CEO of Boot Camp Digital,*

*a leading provider of digital marketing training and consulting solutions. She is a social media pioneer, having created one of the first successful corporate Twitter strategies and corporate blogs. Neher is an international keynote speaker and author of three best-selling books, including Social Media Field Guide: Discover the Strategies, Tactics and Tools for Successful Social Media Marketing. She can be reached at [info@bootcampdigital.com](mailto:info@bootcampdigital.com) or 513.223.3878.*



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# Arbitrating Your Construction Dispute— Does it Have to Be Final and Binding?



BY MIA LEVI AND MICHAEL A. MARRA



AMERICAN ARBITRATION ASSOCIATION®

**LIMITED JUDICIAL REVIEW** of arbitration awards can be a determining factor for parties deciding between arbitration and litigation. The finality of an arbitration award can be an advantage when it minimizes post-award disputes and the losing party's ability to delay enforcement by initiating time- and cost-consuming appellate proceedings. But many parties may find it frustrating not to have an automatic process for review of an award.

In 2011, the Cornell-Pepperdine/Straus Institute Conflict Prevention & Resolution (CPR) Survey asked corporate counsel in Fortune 1,000 companies whether they used arbitration and, if not, why. The most common reason given by those who did not use arbitration was because of the difficulty of appeal.<sup>1</sup> Indeed, the Federal Arbitration Act provides courts with very narrow statutory grounds for vacating an award in judicial proceedings.<sup>2</sup> The court generally must look to the integrity of the process (award procured by fraud, evident partiality of the arbitrator, arbitrator acting in excess of authority, refusal to hear material evidence, and refusal to postpone a hearing for good cause), rather than the substantive propriety of the arbitrators' decision.<sup>3</sup>

In response to these concerns and in order to provide for an easier, more standardized process for non-judicial appeals of



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arbitration awards, ADR providers have begun to introduce optional appellate arbitration rules. Such an appeals process is available to participants in arbitration, in the American Arbitration Association (AAA) Optional Appellate Arbitration Rules, or with other institutional rules such as JAMS's Optional Arbitration Appeal Procedure or the CPR Arbitration Appeal Procedure.

Appellate procedures are particularly useful for parties who are or may soon be involved in a case deemed significant, due to its legal and factual complexity, its practical repercussions, or its amount in controversy. Accordingly, company disputes that have traditionally been litigated for lack of appellate rights and remedies can now be more

confidently arbitrated under arbitral appellate procedures.

#### **How to Include an Appellate Process in an AAA Arbitration**

The AAA Optional Appellate Arbitration Rules, effective November 1, 2013, allow parties to include, as part of their ADR clause, a further provision that the decision of arbitrators may be appealed to an AAA Appeal Tribunal, which may review those decisions based upon alleged errors of law that are material and prejudicial to a party and "clearly erroneous" determinations of fact.

The appeal provision should appear in the agreement between the parties, but can also be inserted in a post-dispute arbitration agreement. An appeal provision to be included

in a contract would ideally outline the process to which the parties wish to adhere. The following sample language is included in the AAA's Optional Appellate Arbitration Rules:

Notwithstanding any language to the contrary in the contract documents, the parties hereby agree: that the Underlying Award may be appealed pursuant to the AAA's Optional Appellate Arbitration Rules ("Appellate Rules"); that the Underlying Award rendered by the arbitrator(s) shall, at a minimum, be a reasoned award; the Underlying Award shall not be considered final until after the time for filing the notice of appeal pursuant to the Appellate Rules has expired. Appeals must be initiated within thirty (30) days of receipt of an Underlying Award, as defined by Rule A-3 of the Appellate Rules, by filing a Notice of Appeal with any AAA office. Following the appeal process the decision rendered by the appeal tribunal may be entered in any court having jurisdiction thereof.<sup>4</sup>

Under these rules, the appellate panels do not have the authority to remand to the original panel. Instead, they may adopt the first instance award themselves or substitute their own award (per Rule A-19(a)). The Appeal Tribunal's decision becomes the final award for purposes of judicial enforcement proceedings.

Upon the filing of a Notice of Appeal under the AAA Optional Appellate Arbitration Rules, the parties agree that the underlying award will not be considered final for purposes of any court actions to modify, enforce, correct, or vacate the underlying award; and the time period for commencement of judicial enforcement proceedings is tolled during the pendency of the appeal. The parties also agree to stay any already initiated judicial enforcement proceedings until the conclusion of the appeal process.

#### **Selecting the Appellate Tribunal**

The appellate tribunal will be selected from the AAA's Appellate Panel that consists of former federal and state

judges and other arbitrators with strong appellate backgrounds. A panel of three appellate arbitrators will be appointed unless the parties agree to use a single arbitrator. The process of selecting a panel is similar to that used in an underlying case: a list of names is sent to the parties, who can either agree to the arbitrators or strike and rank the candidates on the list. The AAA requires prospective arbitrators make the same disclosures of relationships as other AAA arbitrators.

### Benefits of the Appellate Process

Claims that the creation of an internal level of appellate review within the arbitration system would simply duplicate the features of litigation are unfounded, as the parties to any dispute still have the many benefits of arbitration at their disposal. The confidentiality of the arbitration process remains in place, which can minimize negative publicity as well as preserve working relationships. Construction disputes in particular can still benefit

from having an arbitrator with subject matter and industry expertise decide the case. In court, the parties would be left at the mercy of a judge or jury who might not understand the complexities of a construction project.

The benefits of an appellate process can begin during the arbitration itself. With an option to appeal the award, parties who might otherwise be apprehensive to select a single arbitrator might elect to do so. The option of selecting a sole arbitrator over a three-arbitrator tribunal can reduce the costs of arbitrator compensation by 79% as well as reducing the amount of delay caused by competing schedules.<sup>5</sup>

Finally, the process continues to be faster and more cost effective—the AAA rules anticipate the appeal process can be completed in about three months. Since the process can be tailored to the parties' schedules and needs, the full length of the appeal process remains up to the parties. However, in reviewing the five cases to date that used the AAA

Optional Appellate Rules, the average length of the appellate process added merely 4.7 months. This remains faster than court, where cases take more than 12 months longer to get to trial than those cases adjudicated by arbitration (21 months longer when a court appeal is involved).<sup>6</sup>

### Considerations When Allowing for an Appellate Process

Certain considerations are involved in anticipating the appellate process. Whether or not the parties actually file the appeal, they will need to take certain steps in preparation for its potential use. Because the appellate tribunal does not rehear the case, a "record" of the case itself must exist and be sufficient to permit a review of the proceedings. Parties should consider using a stenographer in arbitration; otherwise, the record on appeal consists of any expert reports, deposition transcripts, documentary evidence, briefs, or other materials presented at the arbitration. In addition, the parties should request



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a fully reasoned award (with findings of material fact and rulings on outcome-determinative questions of law) from the arbitrator.

Parties should also be aware of the costs of the appellate process. Under the AAA rules, any party that wishes to appeal an arbitral award must pay a non-refundable \$6,000 administrative fee upon the filing of a Notice of Appeal, and any party filing a cross-appeal must pay the same non-refundable fee. Where there is no cross-appeal, the appealing party is responsible for all fees and costs, including the fees of the appellate tribunal members; if there is a cross-appeal, the appealing parties share these equally. The rules do allow the tribunal to reallocate the parties' share of costs and fees in the award (per Rule A-12(d)) and also grant the tribunal discretion to award reasonable costs and fees to the non-appealing party if the appeal is unsuccessful (per Rule A-11).

### Conclusion

The tenets of arbitration stem from the control and flexibility the parties have to create a process that works for them. The Optional Appellate Rules enhance that control and flexibility. Indeed, for those parties who value the option of having an appeals process in place to ensure substantive review of an award, the Optional Appellate Rules provide such a process without requiring the parties to resort to litigation. ●

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*Michael A. Marra is Vice President for the AAA Construction Division and has served with AAA for more than 17 years. He was appointed District Vice President of the AAA Philadelphia Office in September 2001. He is responsible for expanding the use of*

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### End Notes

1. See Thomas J. Stipanowich & J. Ryan Lamare, *Living with ADR: Evolving Perceptions and Use of Mediation, Arbitration, and Conflict Management in Fortune 1000 Corporations*, 19 Harv. Negot. L. Rev. 1, 53 (2014) (Table P. Reasons Why Companies Have Not Used Arbitration).
2. The Federal Arbitration Act (FAA), 9 U.S.C. § 10(a), limits the bases on which a court can consider vacating an arbitration award. Moreover, parties may not expand the scope of review of a court to which either party appeals, even where they would be in agreement to do so. *Kyocera Corp. v. Prudential-Bache Trade Servs. Inc.*, 341 F.3d 987, 1000 (9th Cir. 2003).
3. The Supreme Court restricted the grounds for vacatur of an arbitration award to those set forth in § 10 of the FAA, 9 U.S.C. § 1 *et seq.* See *Hall Street Associates, L.L.C. v. Mattel, Inc.*, 128 S. Ct. 1396, 1403 (2008). Despite the ruling, there is a variance in the circuits as to whether expanded review, through the manifest disregard of the law doctrine, is still permissible.
4. AAA Optional Appellate Arbitration Rules, pp. 3-4.
5. Statistics are estimates based on AAA construction arbitrations awarded in 2016 with claims of \$1 million or more.
6. A 2017 study found that, on average, U.S. district court cases took more than 12 months longer to get to trial than cases adjudicated by arbitration (24.2 months v. 11.6 months); when the comparison involved time through appeal, U.S. district and circuit court cases required at least 21 months longer than arbitration to resolve (33.6 months v. 11.6 months). *Micronomics, Efficiency and Economic Benefits of Dispute Resolution through Arbitration Compared with U.S. District Court Proceedings*, March 2017, pp. 3-4. <http://www.micronomics.com/>.



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(including unallocated job costs), and a schedule of general and administrative costs. These supplemental schedules must reconcile back to the information presented in the income statement and balance sheet!

**Conclusion**

Having accurate financial statements presented in the proper format, with required disclosures, will help contractors portray their financial strength in the best possible light. This will go a long way in maximizing their prequalification efforts with their customers and maximize their banking and bonding capacity. ●

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A.M. Best: affirmed 10/2/2017

T-Listing: Affirmed July 2018, Nationwide Mutual Insurance Company, [https://www.fiscal.treasury.gov/fsreports/ref/suretyBnd/c570\\_a-z.htm#N](https://www.fiscal.treasury.gov/fsreports/ref/suretyBnd/c570_a-z.htm#N)

S&P: affirmed 5/24/2017

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