

## Performance Bonds and Payment Bonds

Performance Bonds and Payment Bonds are key elements of a successful contracting bid. They are among the most common contract surety bonds in existence today. These bonds give project owners and developers financial protection against a contractor that defaults or fails in some way to perform work as specified in the contract.

Performance Bonds are submitted by the winning bidder once a contract is officially awarded. They are typically issued with a Payment Bond, as the two are similar in nature. In fact, in many cases, these will be issued as a single “Performance and Payment Bond.” Together, these bonds ensure that work is performed as specified by a contract and that the winning contractor pays all subcontractors, suppliers and laborers as detailed by the contract.

These bonds can be especially important for public works projects. Mechanics liens cannot be held against public property, meaning that payment bonds serve as the only protection for workers who have not received payment for contracted services. For most public projects, Bid Bonds, Performance Bonds and Payment Bonds are all mandated by law. Since surety bonds are required by federal law for all projects in excess of \$100,000, many jobs on private property also involve a Payment Bond.

If there is a claim on the bond due to nonpayment or other contractual breach, the subcontractor (or other wronged party) files a claim on the bond. If the claim is found to be valid, the surety company that issued the bond will make sure the aggrieved party is compensated by the contractor who purchased the bond. Since this procedure effectively brings a neutral third party in to execute the agreement, it can provide a certain measure of reassurance to those involved with any project, particularly large and expensive developments.

The bond is purchased by the contractor during the contract negotiation phase of a construction job and is generally bought from a surety bond company or, in rare cases, an insurance company (though surety bonds are not insurance and should not be mistaken for such). The rate and amount is subject to both the size of the job and the contractor’s own credit rating and financial history. Should the contractor fail to qualify for a normal bond, special bonds for those with lackluster credit can be purchased for a considerably larger premium.

The market for performance bonds and payment bonds remains more straightforward given the current economic conditions nationwide. A more stable market means traditional underwriting practices will likely be employed. Qualified contractors can expect to find competitive rates.



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