



## Bonds and Bonding

By Dr. Robert Sullivan

From time to time a small business, especially those performing contracting services will be asked to bond his work in advance. In some states certain types of contractors are required to be bonded. What is a bond, how do you get one, and what does it do?

Simply put a bond (sometimes referred to as a surety bond) is a third party obligation promising to pay if a vendor does not fulfill its valid obligations under a contract. There are various types of bonds such as **LICENSE, PERFORMANCE, BID, INDEMNITY & PAYMENT**. A bond is a financial guarantee that you will honor a business contract. Frequently a customer will require that your company be bonded.

- A **PERFORMANCE bond** is a guarantee that you will perform work in accordance with the terms of a contract.
- A **BID bond** is a guarantee you will perform work if the bid is won by you.
- A **INDEMNITY bond** promises to reimburse loss incurred if you fail to perform or if you fail to pay other vendors in the performance of the contact.
- A **LICENSE bond** is required by some states for certain businesses. In some cases you pay the state directly rather than obtaining a bond.
- A **PAYMENT bond** promises you will pay all subcontractors and material providers utilized in the performance of a contract.

**A bond is NOT an insurance policy.** This is important to remember. A bond provides assurance that the contracted work will be satisfactorily completed only. For example your bond will not pay for property damage or personal injury resulting from your work.

For this you need conventional insurance coverage. Your local yellow pages will list companies that provide bonding services under "surety bonds." Also, check with Bond-By-Fax, Commercial Surety Department at **1 (800) 395 CBIC**. Generally speaking, bonding companies will only provide bond coverage in an amount that you can cover with existing liquid assets.

Before you purchase a bond from any bonding company, have the bond documentation reviewed by your attorney and ensure that you understand exactly what the bond can and cannot protect against - for you and your customer.

## Job Costs

Job costs are divided into two groups. Direct job costs such as labor, materials, and subcontractor expenses can be traced directly to the construction project. The wage paid to a site manger is an example of a direct labor cost. Similarly, direct materials would include lumber for framing a house or concrete for the foundation of a shopping center.

**Direct job costs** also include amounts paid to subcontractors. Subcontractors work for and are paid by the general contractor on a project. Subcontractors may also provide the raw materials for the job. Labor and materials provided by a subcontractor are generally treated as direct costs.

**Indirect job costs** are all the costs necessary for the performance of the contract other than direct materials, direct labor, and subcontractors. The expenses included in indirect job costs differ depending on whether you are a small or large contractor.

## Allocating Indirect Costs

You have learned that indirect job costs benefit the project but are not tied as clearly to it as direct costs are. Indirect

job costs often involve expenses that benefit more than one job and must be allocated among all the jobs that received benefit.

**Example** Norm started three different jobs in 2000. None of the jobs were completed by the end of 2000. He spent 6 months on the first job, 4 months on the second job, and 2 months on the third job.

He had \$12,000 of indirect costs to be allocated to the three jobs. Norm would allocate the indirect costs as:

**First Job**

6 mo. X \$12,000 = \$6,000 Allocated Indirect Costs 12 mo.

**Second Job**

4 mo. X \$12,000 = \$4,000 Allocated Indirect Costs 12 mo.

**Third Job**

2 mo. X \$12,000 = \$2,000 Allocated Indirect Costs 12 mo.

**Indirect Job Costs for Small Contractors**

- Repair & maintenance expenses for equipment & facilities
- Utilities
- Rent of equipment & facilities
- Quality control
- Taxes relating to labor, materials, supplies, equipment or facilities
- Administrative costs
- Indirect materials and supplies
- Tools & Equipment Depreciation
- Insurance on equipment & machinery
- Indirect labor and contract supervisory wages
- Production period interest expense

**CONTACTS**

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**PFA Notice:**

The Met. Council's PFA program only accepts W/MBE businesses listed with the State Department of Administration and the DBE Unified Certification Program.

For more information call Roderic Southall at **651-602-1184**.

<b>Contractor/Consultants</b>	<b>Total Contract Amount</b>	<b>Total Paid to Date</b>	<b>DBE Paid to Date</b>	<b>(1) DBE % Actual to Date</b>	<b>(2) DBE % Total Contract Value</b>	<b>Target DBE % Goal</b>
Minnesota Transit Constructions (MnTC)	327,385,281	316,757,550	41,142,152	12.99%	12.57%	15%
Other Contractors	6,252,001	6,032,918	775,774	12.86%	12.41%	
O'Brien Kreitzberg (OBK) (3)	19,000,000	19,597,657	3,239,858	16.96%	17.49%	15%
Marsh	545,000	485,000	149,318	30.79%	27.40%	5%
Other Consultants	27,440,257	24,615,396	1,698,690	6.90%	6.19%	
<b>SUB-TOTAL</b>	<b>380,622,539</b>	<b>367,488,521</b>	<b>47,089,792</b>	<b>12.81%</b>	<b>12.37%</b>	
Other Commitments *	92,469,347	88,901,756	N/A	N/A	N/A	N/A
<b>TOTAL</b>	<b>473,091,886</b>	<b>456,390,277</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>

\* ROW Cooperative Agreements, Other Direct Costs, etc. (1) Calculates DBE percentage based upon DBE dollars expended vs. contract dollars paid to-date (actuals). (2) Calculates DBE percentage based upon DBE dollars expended vs. total contract value. (3) Value as of July, 2004 - Preliminary \*\* Incorporates Amendment #2 to the URS/OBK Agreement