

The General Assembly has recently passed Public Act 11-79, An Act Concerning Bonds and Other Surety for Approved Site Plans and Subdivisions, which became law effective October 1, 2011.

### What Does the Act Require?

The Act contains five main elements:

1. It mandates that municipalities accept "surety bonds" for site plans and subdivisions, in addition to letters of credit, passbooks, or cash. At the behest of CCM, CCAPA, and other municipal advocacy groups, the Act was revised late in the session to allow commissions to review the "form" of the bond (i.e., its text, not the type of bond) and to approve the issuer of the bond.
2. It mandates that bonds not exceed more than 110% of the estimated costs (in other words, the contingency is limited to 10%).
3. It mandates that bonds be released within sixty-five (65) days of request or else provide the developer with a written explanation as to what additional work must be done.
4. It prohibits maintenance bonds following acceptance of public improvements.
5. For phased site plans or subdivisions, it requires that bonding be broken out so that each phase is treated as if it were a separate site plan or subdivision.

### What is the Effect of the Act?

The fiscal impact analysis of this Act by the non-partisan Office of Legislative Research concludes:

Enactment of this bill may increase the likelihood that a municipality will not have access to sufficient funds to complete or remediate public improvements in cases of default or inadequate work by developers engaged in site plan modifications or subdivision development. To the extent that a municipality elects to complete or

remediate any unfinished or inadequate work, corresponding costs, which may be of significant magnitude, would be incurred.

This is an accurate assessment of the Act's impact, and it succinctly states why municipal attorneys all over Connecticut do not accept surety bonds for subdivision improvements while they will accept passbook assignments, cash, and letters of credit. The reason for the distinction between surety bonds and letters of credit is the way in which these two instruments are structured:

Letter of Credit: When you go to a bank to borrow money, the bank requires security for that loan. The collateral may be land (a mortgage), a security interest in personal property (usually called a "UCC-1"), assignment of rents or other income flow, cash on deposit with the bank, or any combination thereof. The bank is then willing to give you the money that you borrowed to spend as you wish. In a letter of credit, however, the bank doesn't give you the money. Instead, it says to a third party, "we have the proceeds of this loan available upon demand." If the demand is made, the bank pays over the money without question because they have the security.

Surety Bonds: A surety bond is an insurance policy, just like your health insurance. Because surety bonds don't involve the same law of averages as health insurance, the premiums are set on a more case-by-case basis, but the fact remains that the insurance premium is a lot less than the amount owed in the event of a default. Therefore, when there is a default, the insurance company has a strong incentive to delay (keeping the interest on that money while they stall) or to raise all kinds of defenses to payment in the hope of coercing you into a compromise that involves a lesser payout. Unlike the bank in the letter of credit, when the insurance company pays out more in bonding than it collected in premiums, it won't get more premiums from the same party over time and it usually won't have the collateral. So the insurance company just loses money on that particular transaction and hopes to make it up on others.

For these reasons, surety bonds end up being very difficult to collect, especially for small sums. In a typical site plan or nearly-complete subdivision, the cost of suing the bonding company can exceed the amount of possible recovery and the insurance companies know it.

## What Should the Town Do?

The following courses of action are available:

Amend your subdivision regulations to eliminate any provision for bonding of subdivision improvements and use conditional approval, or completion of improvements prior to subdivision endorsement, exclusively. While the amended Statute would mandate the forms of bonds that you must accept, it continues to make bonding itself merely an option. Conditional approval still allows a subdivision to be approved and filed without bonds, but prohibits the sale of lots until public improvements are completed. This way, no innocent lot owner will be exposed to incomplete public improvements and will have no need to sue the town to complete them; **or**

If you decide to retain the bonding option, amend your regulations to incorporate the language that the form of the bond and the issuer of the bond must be acceptable to the commission. As to the form, we would suggest that the bond form mandate a deadline by which funds must be paid following a calling of the bond, with a penalty for delay; and the payment of attorney's fees and costs to the town in the event that litigation is required to collect on the bond. You should also require that all bonds be governed by the law of the State of Connecticut (not the law of the surety's home offices). As to the issuer, a good start would be to require that any surety maintain offices in Connecticut, so you don't have to chase an out-of-state insurance company.

Amend your subdivision and zoning regulations to provide that any bonds must be based on the cost of the work if performed by the town, including the cost of advertising for bid, bid evaluation, and oversight by a town inspector.

Amend your subdivision and zoning regulations to provide that no extensions of approvals may be granted until updated cost estimates for improvements are provided and approved by your town staff, and until new bonds are submitted in the new amounts. This will help to protect you against the 10% cap on contingency bonding.

Increase your zoning application fees to allow a factor for legal fees to collect on surety

bonds that are unpaid for site plan approvals.

Increase your zoning and subdivision application fees to incorporate the cost of . expanded inspections. With a 10% cap on contingency bonding, no provision for post-acceptance maintenance bonds, the required 65-day period within which to respond to bond releases, and the elimination of maintenance bonding, you will need to be vigilant in monitoring all work for which bonds are posted; and your inspectors will have to be ready to produce "punch lists" on short notice.

Impress upon your improvements inspectors the importance of identifying any and all defects and keeping accurate and complete records of them. This will make it easier to respond at the time that the bond release is requested.

With maintenance bonds, you may have been able to take a "wait and see" approach to defective work and see if it held up during the maintenance period, secure in the knowledge that any failures would be bonded. Now, that won't be the case. Therefore, require that all work be performed in *strict* compliance with the applicable standards, and that any defective work be corrected at once. You will not be able to accept excuses or delays anymore.

When accepting new subdivision streets, take your time. Since there is no maintenance bonding, you will have no recourse for defective work that shows up later on. While the Act requires bond releases within sixty-five days of request, it does not require road acceptance on any timetable. Even without bonding, your liability is greater once you accept the road as a public road.

The Act *does* allow your town to reject bonds (including surety bonds) from particular companies. The language is that you must accept the bond "provided the financial institution or other entity issuing any letter of credit is acceptable to the commission." Perhaps in cooperation with the Connecticut Conference of Municipalities, you should compile, maintain, and share a list of financial institutions that have failed to promptly honor their bond obligations and refuse to accept bonds from such institutions in the future.

Warn and educate the engineers and other professionals who review the improvements covered by this act that when a developer requests the return of a bond you must have

their detailed analysis of whether the work covered by the bond has been done completely and to the engineer's satisfaction sufficiently in advance that the town is not at risk of violating the sixty-five day limit set forth in this legislation. Failure to respond within the new statutory limit may result in towns being obligated to hand back bonds even where the work has not been done.