

PP013 – Commitments in Advance

Introduction

Whenever there is a request for an Agreement to Bond/Consent of Surety at the Request For Qualifications (RFQ) and/or Request For Proposal (RFP) stage, the Obligee is asking the Surety to bond a contract even before the actual contractual terms and conditions have been duly negotiated and subsequently agreed to between the Obligee and the Principal.

Background

It is quite common with Public-Private-Partnership (PPP or P3s) contracts or large infrastructure projects to see a requirement for the Surety to commit unconditionally – by way of the formal Consent of Surety/Agreement to Bond at the RFQ and/or RFP stage. At this stage, Sureties are extremely reluctant to issue an Agreement to Bond/Consent of Surety confirming the unconditional issuance of final bonds because it amounts to a blind guarantee – no one knows what will ultimately be required because the contract terms and conditions haven't been negotiated.

In the context of P3 projects, there can be confusion if the RFP requires the Proponent (or Project Co) to include in its proposal an Agreement to Bond/Consent of Surety. Often the assumption of the Obligee is that the Surety is committing to issue final bonds for Project Co guaranteeing the Project Agreement, whereas the Surety is normally prepared only to commit to issuing bonds for a Principal guaranteeing a “drop down” construction or design-build contract. In these situations, it is important for the Obligee to be clear that a proposal submitted by a Project Co Proponent can include an Agreement to Bond/Consent of Surety to issue bonds for the contractor and not for the Project Co.

SAC Position

The Surety Association of Canada (SAC) recommends that at the early project planning stages (RFQ and RFP), the Obligee request a Prequalification Letter. In this letter, the Surety confirms its relationship with the Principal and acknowledges the subject proposal. It then proceeds to state the following:

Based on the limited information available at this time and subject to our assessment of the project and our client's work program at the time of tender, we do not anticipate a problem in supporting the captioned project and supplying the requisite bonds, if expressly requested by our client to do so. However, the execution of any bonds will be subject to an assessment of the final contract terms, conditions, financing and bond forms by our client and ourselves.

A Prequalification Letter worded in this manner provides clear evidence to the Obligee that the Surety has been duly advised of the proposal, and indicates probable bond support for the project (subject to a favourable review by the Surety of the final form of contract, confirmation of financing and acceptable final bond forms).

Summary

Obligees that wish to confirm a Principal's "bondability" at the RFQ and/or RFP stage of a project should request a Prequalification Letter from the Surety. It is important to remember that a Surety's decision to issue any particular bond is based on an evaluation of the specific terms and requirements of a contract and the capacity of the Principal to successfully perform that contract in the context of the Principal's resources and overall program of work. When there is uncertainty about the specific contract terms, it is not appropriate for a Surety to commit in advance to guarantee performance of that contract with a bond.

Glossary of Terms

Obligee

An individual or organization in whose favour an obligation is created and to whom a bond is given.

Principal

The individual or organization that bears the primary responsibility for fulfilling the obligation under the written contract referenced in the bond and that has the duty to perform for the Obligee's benefit.

Surety

The party to a surety bond who answers to the Obligee for the Principal's default or failure to perform as required by the underlying contract, permit or law.

This paper is intended to serve as a general guideline to assist members and other readers in responding to the issues discussed. Nothing contained herein should be construed as legal advice and readers are cautioned to consult with legal counsel for such advice.

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