

THE SURETY & FIDELITY ASSOCIATION OF AMERICA

MEMORANDUM

TO: Government Affairs Advisory Committee
Contract Bonds Advisory Committee

FROM: Lenore S. Marema, Vice President-Government Affairs

DATE: July 21, 2007

SUBJECT: 2007 Overview of the State Legislative Sessions—Contract Surety

Only six states still are meeting in regular session: Illinois, Massachusetts, Michigan, North Carolina, Ohio and Wisconsin. Illinois and North Carolina will adjourn for the year in the next two weeks. A few other states remain in regular session but are in recess for the summer: California, District of Columbia, New Jersey and Pennsylvania. New Hampshire and New York are in recess until called back into session. New York may come back for a while in the fall.

The following summarizes key state legislation affecting contract surety that SFAA has been working on most recently with AIA and the NASBP. This report updates the June 2007 overview report, which can be accessed on the SFAA website for reference.

Bad Faith

The trial lawyers resurrected their bad faith and anti-tort reform agenda in states that experienced a turnover in leadership as a result of the November 2006 elections.

New York SB 6306 is one such bill that passed. The bill would prohibit insurers from denying a claim based on the failure of the insured to give a timely notice unless the insurer can demonstrate that it suffered “material prejudice” because of the late notice. The bill also would permit third parties to bring a declaratory judgment action against an insurer regarding coverage issues prior to the resolution of the underlying tort action.

The insurance industry is involved in a widespread effort to convince Governor Spitzer to veto this bill. AIA met with the New York Insurance Department, and it appears that Superintendent Dinallo will recommend that the Governor veto the bill. The AIA letter to the Governor requesting a veto is attached. Many insurers wrote individual letters to Governor Spitzer as well. While the bill is poorly drafted, we believe that it was not intended, and likely would not be misconstrued, to apply to surety. SFAA decided not to write a letter to the Governor detailing the potential impact on surety, so that it could be argued that the bill applies to surety.

If the bill is vetoed, the issue will go back to the Legislature in 2008 for a bill that is more carefully crafted to resolve actual or perceived claims problems. SFAA and AIA have discussed

an approach in which any future legislation would either specify the lines of business covered and/or specifically exclude surety.

The Governor has 10 days to sign or veto a bill after it is delivered. When the legislature is not in session, the Governor also has the option of not taking any action on the bill, which has the same effect as a veto. SB 6306 was sent to the Governor on July 20.

The insurance industry and business communities will work together on a referendum to reverse Washington SB 5726, which enacted the lowest standard for insurance bad faith in the country. The coalition obtained the necessary signatures to qualify for a referendum that would put the issue on the ballot for the voters to overturn in the November elections. The industry also had tried to work with a task force of the Governor to see if corrective language can be worked out for the 2008 session. Any negotiations with the trial bar for a meaningful bill in 2008 proved to be impossible.

State Bond Thresholds

--Enactments. **Connecticut** SB 1182 raises the state bond threshold for payment bonds from \$50,000 to \$100,000. The State increased the performance bond threshold last year. **Florida** HB 1077 eliminates the surety requirements for electrical contracts in the City of Key West. **Florida** HB 1153 increases the bond threshold from \$15,000 to \$50,000 for projects on the Hillsborough County Aviation Authority facilities.

--Recent Developments. Because of some recent issues and problems with the New York Port Authority that have been made public, New Jersey Governor Corzine and New York Governor Spitzer both have called for changes in the operation of the Port Authority. SFAA is working with AIA to determine if this presents an opportunity to address the surety bonding issues in the Port Authority's operations. The Port Authority is an interstate compact between New York and New Jersey. The Authority historically has taken the position that it is not bound by either New York or New Jersey law, but rather by the rules of the compact, which it promulgates. The Port Authority generally requires bid bonds on construction projects but often waives the final bonds. Even when the Authority chooses to require final bonds, it often has refused to pay additional bond premiums as a result of change orders. SFAA is working with AIA to determine whether the current situation presents a real opportunity to change the Authority's bonding practices.

Retainage

--Bills on the Move. **New Jersey** AB 3649 would extend the 2005 retainage law for DOT projects to the construction and maintenance projects of the New Jersey Turnpike Authority. The bill would set retainage at 2% until substantial completion, after which 1% of a payment could be withheld. The Authority would be able to withhold 4% if the project is not progressing according to specifications. The bill is on the Governor's desk for signature.

North Carolina SB 1245, as introduced, would have prohibited retainage on public construction contracts where the total project cost is less than \$300,000. The bill has been amended and passed the Senate. As revised, SB 1245 would prohibit retainage in contracts less than \$100,000. The bill would limit the amount of retainage that could be withheld in contracts in excess of the threshold to 5% of each progress payment on contracts over the threshold until 50% completion.

After the project has reached 50% completion, no more retainage could be withheld so long as the contractor performed satisfactorily. If the contractor's work became unsatisfactory, the owner would be able to resume withholding retainage at the maximum rate described above. Release of the retainage would be contingent upon the approval of the architect, engineer, or the designer, and the consent of the contractor's surety. SB 1245 has passed the Senate and is in the House where SFAA and AIA are working to defeat it.

Anti-Directed Surety

--Enactments. Hawaii HB 1833 prohibits any person or entity from requiring that the bond for a public construction contract be acquired from a particular surety or group of sureties or a producer or agent of any surety or group of sureties.

Bond Guarantee and Technical Assistance Programs

--Bills on the Move. Illinois SB 1511 still has life as the deadline for enactment has been extended once again. It is now July 31, 2007. The original bill would have allowed the Board to waive bonds for small and minority-owned contractors. SFAA and AIA worked together to amend the bill in the House, so that the Board could accept cash, letters of credit, U.S. debt obligations or debt obligations backed by the full faith and credit of the State of Illinois from small and minority businesses in lieu of surety bonds.

Electronic Bidding

--Enactments. Louisiana SB 280 permits electronic bidding by eliminating the requirement that all bid documents must be submitted in writing. The new law also requires all bids on projects in excess of \$50,000 to be submitted with a bid bond. It eliminates the prior options of a cashier's check, certified check, money or company check. North Carolina SB 579 authorizes the City of Charlotte to receive bids electronically in addition to or instead of paper on public construction projects.

Contractor Qualifications

--Enactments. Connecticut SB 707 applies the requirements in existing law regarding contractor qualifications to contractors on public projects and sets a \$500,000 threshold at which the qualification requirements apply. The new law also requires the surety bond on a public project in excess of \$500,000 to contain the following provision: "In the event that the surety assumes the contract or obtains a bid or bids for the completion of the contract, the surety shall ensure that the contractor chosen to complete the contract is pre-qualified pursuant to section 4a-100 of the Connecticut general statutes in the requisite classification and has the aggregate work capacity rating and single project limit necessary to complete the contract."

Contracts with Veterans

Arkansas HB 1646 would have given a 10% preference and set a 3% goal for the Office of State Procurement in awarding contracts to qualified disabled veterans. **Connecticut** SB 1020 would have required a 3% set aside for such contractors measured by the total value of all construction contracts let by each agency in a fiscal year. **Indiana** HB would require the Department of Administration to collect information on price preferences for certain contracts, provide a price preference for disabled-veteran businesses in certain contracts and public works projects and set a goal for contracts with disabled-veteran businesses equal to 3% of total expenditures.

Maryland HB 742 would have established goals for certified, disabled-veteran business in state contracts. **New York** AB 7733 would have given a 3% bid preference to service-disabled-veteran-owned businesses.

--Carryover. **Washington** SB 5289 would increase state contracts with veteran-owned businesses, declare that the purpose of this act is to mitigate economic damage to veteran-owned businesses as a result of military service and provide opportunities to them in recognition of the outstanding service they have given to their country and require a report to the legislature outlining the progress made in implementing this agreement.

--Still Pending. **Pennsylvania** HB 62 would establish goals for certified, disabled-veteran business in state contracts.

Bidding Preferences

--Bills on the Move. **Illinois** HB 634 would permit a 5% bid preference to bidders using biobased products. The bill is on the Governor's desk for signature.

--Dead for 2007. **New York** AB 8442 would require that a bidding preference be given to any state contractor, including construction, that provides its employees with employer-sponsored health coverage. The bill died on the Assembly floor when the legislature adjourned.

Other Issues

--Enactments. **Tennessee** HB 1006 requires home improvement contractors to post a license bond, which may be in the form of cash, a surety bond, a "property bond" or an irrevocable letter of credit in the amount of \$10,000.

The new law also prohibits any deposit being paid to the contractor in excess of 1/3 of the contract price prior to the contract's execution. A deposit in excess of this amount may be made if the construction contract allows the contractor to furnish a performance and payment bond, lien and completion bond, or a bond equivalent covering full performance and completion of the contract. The amount of the bond or its equivalent cannot be less than 1% of the net sales of the contractor's business in terms of labor, which must be determined on an annual basis, beginning on January 1.

In lieu of the performance and payment bond, the owner may elect to make final payment to the contractor for the project before completion for his or her convenience, or the parties may agree on a schedule of payments to be made before, during and after completion of the project; provided however, the contractor must advise the owner in writing of his or her right to withhold up to 100% of payment until the project is completed.

--Bills on the Move. **Illinois** HB 773 would enact a new prompt payment act. The bill would require owners to pay contractors within 15 days from the owner's approval of the application for payment. A payment application will be deemed approved if the owner has not provided a written reason for withholding the payment within 25 days. Contractors must pay subcontractors within 15 days of receipt of payment from the owner. The interest on late payments is 10%. The bill is on the Governor's desk for signature.

2007 Overview of the State Legislative Session—Commercial Surety

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LICENSE BONDS

Home Improvement Contractors

--Enactments. **Tennessee** HB 1006/SB 1728 requires home improvement contractors to post a license bond, which may be in the form of cash, a surety bond, a "property bond" or an irrevocable letter of credit, in the amount of \$10,000. The aggregate liability of the surety under the new law may not exceed the aggregate amount of the bond.

--Still Pending. **Massachusetts** SB 220 would require all irrigation contractors to obtain a permit. As a condition of obtaining a permit to operate, the contractor would have to show proof of liability and workers compensation insurance, a surety bond and a letter of credit.

Mortgage Brokers and Lenders

--Enactments. **California** SB 998 requires finance lenders, residential mortgage lenders and residential mortgage services to file an original surety bond, including all riders and endorsements, with the Commissioner of Corporations rather than a copy of the bond as provided under prior law. **Rhode Island** SB 104 increases the license bond for mortgage loan brokers from \$10,000 to \$20,000 and from \$25,000 to \$50,000 for mortgage lenders.

Check Cashing and Money Transmitters

--Enactments. **Alaska** SB 116 enacts the Uniform Money Services Act of the National Conference of Commissioners on Uniform State Law. Money transmitters must be licensed and post a bond of \$25,000, plus \$5,000 per location up to an additional \$125,000. The total maximum bond would be \$150,000. The Department of Commerce, Community and Economic Development could increase the bond up to \$500,000, if the financial condition of the licensee required such an increase. **Delaware** SB 81 allows sellers of checks and money transmitters to post a letter of credit in lieu of a surety bond.

Credit Counseling and Debt Management Services

--Enactments. **Missouri** HB 329 requires debt adjusters to furnish a blanket bond in favor of the State of Missouri in the amount of \$100,000 for the benefit of any debtor who is damaged by the debt adjuster's breach of the debt management plan or the debt adjuster's failure to administer debtor funds collected and disbursed under the plan. **Rhode Island** SB 34 requires debt collectors to be licensed and bonded. The bond amount is \$15,000, and it would run to the State for its use and any person who would have a cause of action against the licensee under this new law.

--Still Pending. **New York** AB 8153 would require debt collection agencies to be licensed and to post a bond in an amount based on the number of persons the licensee employs. The bond amount is \$10,000 for one to four employees; \$25,000 for five to nine employees and \$50,000 for 10 or more employees. The bill passed the Assembly.

Motor Vehicles

--Enactments. **Florida** HB 7205 requires recreational vehicle distributors and importers to post a license bond in the amount of \$10,000. Existing law concerning license bonds for recreational vehicle manufacturers is applicable to this license bond requirement. **Missouri** SB 82 subjects power sports vehicles and trailer dealers to an existing \$25,000 license bond. As originally drafted, the bill would have increased the motor vehicle license bond from \$25,000 to \$30,000.

Health Related Entities

--Enactments. **Connecticut** SB 74 requires pharmacy benefit managers to post a surety bond in connection with registration. The bond must be in an amount of 10% of one month of claims in the State over a twelve-month period; provided, however, the bond may not be less than \$25,000 or more than \$1 million. **Connecticut** SB 1213 requires preferred provider networks for health insurers to maintain financial security in an amount sufficient to make payments to participating providers for two months, the actual amount outstanding to such providers or another amount that the insurance commissioner shall determine. A bond could be posted as security. **Kansas** SB 11 authorizes the State Board of Pharmacy to adopt regulations for the registration and bonding of wholesale drug distributors.

Other License Bonds

--Enactments. **Colorado** SB 249 requires independent settlement service providers in the real estate industry to post a \$25,000 bond in connection with registration. **Nebraska** LB 124 requires a \$50,000 surety bond for licensure as a business offering retail sales installment contracts. **New Hampshire** HB 895 requires court reporters to be licensed and to post a \$1,000 bond. The bond is conditioned that the court reporter does not violate any of the duties, terms, conditions, provisions or requirements of the new law. The new law also allows any aggrieved person to maintain an action on the bond directly.

--Recent Introductions. **District of Columbia** Bill No. 294 would require viatical settlement providers to be licensed and provide evidence of financial accountability in the amount of \$250,000 through a surety bond, deposits of cash, certificates of deposit, securities, an errors and omissions policy or any combination of these.

PUBLIC OFFICIAL BONDS

--Enactments. **Alabama** HB 834 makes the probate judge in Crenshaw County responsible for the assessment and collection of ad valorem and sales taxes on motor vehicles, motor vehicle titles and non-motorized vehicles. In addition to any other required bonds, the judge is required to post an additional bond from a surety company licensed in the State for the faithful performance of this new duty. **Delaware** SB 140 requires the treasurer and town clerk of Frederica to post a surety bond as the town council requires. **Massachusetts** HB 2029 creates a corporation for the city of Marlborough's development. The treasurer of the corporation is required to post a bond conditioned on the faithful performance of his or her duties in an amount that the corporation's board will determine. **Missouri** HB 426 creates the Propane Safety

Commission and requires a \$100,000 bond from the Executive director and a \$50,000 bond from each of the seven commissioners. **Rhode Island** HB 6282 enacts a charter for the Dunn's Corner Fire District that requires both the treasurer and tax collector to be bonded. **New Hampshire** HB 256 requires all town treasurers and any employees to whom the treasurer delegates treasury functions to be covered under the town's blanket bond policy.

A number of bills enacted in **Florida** establish a charter for a new public entity in which surety and/or fidelity bonds are required for public officials. HB 777/SB 1622 (Polk Transit Authority), HB 995 (Holt Fire District), HB 1029/SB 3004 (North Springs Improvement District) and HB 1099 (Blackman Fire District) all now have been signed into law.

--Bills on the Move. **Illinois** SB 684 clarifies that the amount of the bond for trustees of the North Shore Sanitary District is \$10,000. The bill is on the Governor's desk for signature. **New Jersey** AB 4336/SB 2796 would create the New Jersey School Development Authority and require each member of the Authority to post a surety bond. The bill is on the Governor's desk for signature.

--Still Pending. **Massachusetts** SB 1116 would establish the Public Guardianship Commission (Commission) and would require the Commission to post a bond for the joint benefit of all persons for whom the Commission was appointed to act in such a capacity.

COURT BONDS

--Enactments. **Nevada** SB 46 adopts the Uniform Custodial Trust Act, which would allow a beneficiary to petition the court to require the custodial trustee to furnish a bond or other security for the faithful performance of fiduciary duties.

New York had a number of bills this session that imposed new taxes and required a surety bond to be posted if the tax assessment was challenged. Several of these bills passed and are on the Governor's desk for signature: SB 4070/AB 7046 (new hotel and motel tax in Geneva), SB 4692 (Town of Chatham community preservation fund), SB 4829/AB 7939 (Town of Fishkill community preservation fund) and SB 23966/AB 4461 (County of Yates new hotel and motel tax).

--Bills on the Move. **California** AB 1727 would provide that attorneys' fees and costs in a successful action against the conservator or guardian for breach of duties are surcharges and, as such, would have to be paid by the surety if such fees and costs went unpaid. The bill has passed the Assembly and is moving in committee in the Senate.

SCHOOL BONDS

--Enactments. **Delaware** HB 168 increases the bond for a private business or trade school from \$5,000 to \$ 25,000. **New Hampshire** HB 536 requires martial arts schools to register and post a surety bond or other financial instrument in the amount of \$50,000 in order to operate.

--Bills on the Move. **California** SB 823 would authorize the Board for Private Secondary and Vocational Schools (Board) to require such institutions that committed a violation, which does not merit revocation of its approval to operate, to post a surety bond in an amount that the Board would determine to protect students from the potential consequences of the violation. The bill has passed the Senate and is moving in committee in the Assembly.

UPDATES ON SOME RECENT COMMERCIAL SURETY ISSUES

The following is an update on some relatively new commercial surety issues in the state legislatures that SFAA has been tracking.

Boxing/Martial Arts

There is some interest among the states in licensing and bonding promoters of these events.

--Enactments. **Hawaii** HB1866 originally would have required promoters of mixed martial arts contests to post a surety bond in connection with an event. As amended and enacted, the new law authorizes the Department of Commerce and Consumer Affairs to adopt rules to guarantee that a promoter meets its financial obligations in connection with such contests. **Louisiana** HB 348 requires promoters of mixed technique events to be bonded under the requirements of existing law, which requires a \$5,000 license bond. **Oregon** SB 492 subjects promoters of mixed martial events to the existing licensing and bonding requirements for promoters of boxing and wrestling matches. The license bond is in an amount that the Superintendent of State Police deems acceptable. The bond is conditioned upon the promoter making all required payments to the State and its political subdivisions, for the purses of competitors, for the costs of any cancelled events and for the compensation of all inspectors, referees, timekeepers, judges and medical personnel.

--Bills on the Move. **Illinois** HB 1947 would extend the license and bonding requirements for boxing to promoters of martial arts matches. The bill is on the Governor's desk for signature.

Amendments to the Uniform Commercial Code

In its Restatement of the Law on Surety, the American Law Institute (ALI) referred to sureties as "secondary obligors," even though ALI restatements generally summarize an existing body of law rather than break new ground. This new terminology has caused states to amend their versions of the Uniform Commercial Code to contain the reference to surety as "any other secondary obligor." These changes to the law have no substantive impact on surety. **Florida** SB 252 is the most recent bill to be signed into law. **Pennsylvania** HB 1152 has passed the Assembly and is in committee in the Senate.

Private Investigators

--Bills on the Move. **Pennsylvania** HB 825 would require private investigators, security professionals and fugitive recovery agents to post a license bond in an amount that the State Board of Private Investigators, Security Professionals and Fugitive Recovery Agents would determine. The bill has passed the House and is in committee in the Senate.

2007 Overview of the State Legislative Session—Fidelity

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UPDATE ON CURRENT FIDELITY ISSUES IN THE STATES

Condo Associations

--*Enactments.* **Hawaii** SB 1704 permits a community association unable to obtain the required fidelity bond to apply to the Real Estate Commission for an exemption, deductible or bond alternative. Existing law requires associations with five or more units to post a fidelity bond in the amount of \$500 multiplied by the number of units, but not less than \$20,000 and not more than \$200,000.

--*Bills on the Move.* **Illinois** HB 1071 would require managers of community associations to be licensed and bonded. A fidelity bond would be required in an amount not less than all the funds of the association and must cover the manager and all partners and employees of the firm in which the manager is employed. The bill is on the Governor's desk for signature.

--*Still Pending.* **North Carolina** SB 1315 would require community association managers to obtain a fidelity bond.

Pharmacy Benefit Managers

--*Carryover.* **Georgia** HB 798 would require pharmacy benefit managers to post a fidelity bond equal to at least 1% of the funds handled or managed annually.

--*Failed.* **Texas** HB 1974 would have required pharmacy benefit managers to be licensed and maintain a fidelity bond equal to at least 10% of the funds handled.

Public Officials

A number of bills enacted in **Florida** and **Georgia** establish a charter for a new public entity in which surety and/or fidelity bonds are required for public officials. In Florida, see HB 777/SB 1622 (Polk Transit Authority), HB 995 (Holt Fire District), HB 1029/SB 3004 (North Springs Improvement District) and HB 1099 (Blackman Fire District.). In Georgia, see HB 93 (City of Bainbridge), HB 477 (City of Richland), HB 496 (City of Arlington), HB 588 (City of Maysville), HB 696 (City of Alamo) and HB 805 (City of Buchanan).

OTHER RECENT ENACTMENTS

Missouri HB 426 creates the Propane Safety Commission (Commission) and permits the Chairman of the Commission to obtain a blanket bond covering all members of the Commission and the employees in lieu of individual bonds.

New Hampshire HB 256 requires officials and employees to whom the town treasurer delegates certain treasury functions to be covered under the town's blanket bond.

Oregon SB 350 authorizes the Director of the Economic and Community Development Department (Director) to require officers and employees to obtain a fidelity bond if they have charge of, handle or have access to, any state money or property. The Director is charged to set the amount of the bond.