

ARCHITECTURE, ENGINEERING & CONSTRUCTION

The Crucial Role of Supply Bonds in High-Stakes Projects



When you're in an industry at the epicenter of innovation and building, every detail counts, and time is of the essence. Unfortunately, supply chain turbulence has infused challenges into the process of construction and design. The pandemic brought on many of these challenges, but attacks on maritime vessels in the Red Sea and droughts in the Panama Canal region have been problematic as of late, causing shipping costs to skyrocket by over fourfold since late 2023.¹

Picture this scenario: A reputable design-build firm that specializes in crafting highly specialized buildings in the pharmaceutical and food and beverage space is tasked with creating a facility vital for vaccine operations. Because of this, the firm needs to procure very specific and costly equipment. But what if the designated distributor or manufacturer fails to deliver crucial materials and equipment on time? Faced with this looming uncertainty, the firm's leaders seek answers. Is there a safety net, an insurance or a risk transfer mechanism capable of mitigating the pitfalls of supply chain disruptions?

Luckily, there is an answer: supply bonds.

Supply Bonds Protect Against Supplier Default

In the intricate terrain of procurement, contractors and design firms concerned about supplier default should seek a carefully crafted contract backed by a supply bond. Unlike traditional insurance products, supply bonds are rooted in banking relationships, serving as a vital mechanism to ensure the smooth flow of materials and goods essential for project completion.

In essence, a supply bond provides assurance to the purchaser that they will either receive the contracted goods within the time and quality constraints specified or be financially compensated if the delivery falls short.

As one of several types of contract bonds designed to guarantee the fulfillment of supplier obligations, supply bonds come into play primarily in large-scale projects with extensive material requirements or high volumes of specialized components. Should a supplier falter in delivering the agreed-upon materials for any reason, the purchaser, typically represented by the project manager or owner, retains the right to file a claim. This breach of contract triggers the surety company's obligation to compensate the obligee, covering the losses or setbacks incurred as a result of the supplier's default.

However, the efficacy of supply bonds hinges not only on their existence but also on the meticulous crafting of contractual terms that address potential delay issues. A well-drafted contract should shield the business from accountability in the face of delays beyond their reasonable control, including acts of God or unforeseeable supply chain disruptions.

¹ SAFETY4SEA "[Swiss Re: Global shipping will continue to face turmoil.](#)" February 8, 2024.

Even if specific references to supply chain delays prove impracticable in the final contract, certain key points should be communicated and documented. These include:

- Acknowledgment by the owner of the inherent risk of delays in equipment delivery due to supply chain and other uncontrollable factors
- Understanding that estimated delivery times and material costs serve as projections rather than guarantees
- Recognition that such delays may disrupt sequencing and design coordination, potentially leading to additional costs
- Emphasis on the importance of including adequate contingencies in the budget to accommodate unforeseen costs and schedule extensions stemming from uncontrollable market conditions.

By integrating these provisions into your contracts, you can fortify your defense against the uncertainties of supply chain disruptions, ensuring smoother project execution and enhanced risk management.

Clarity and Support Are Available

In this tricky supply chain environment, it's important to recognize you're not alone. EPIC understands this business intimately, as well as the unique needs and challenges faced by clients. Whether you're pondering the intricacies of supply bonds or seeking guidance on mitigating unforeseen contingencies, EPIC can offer clarity and support. Let's chart a course toward greater resilience and success together.



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