

**SENATE JUDICIARY COMMITTEE**  
**Senator Thomas Umberg, Chair**  
**2025-2026 Regular Session**

SB 425 (Rubio)  
Version: March 26, 2025  
Hearing Date: April 29, 2025  
Fiscal: Yes  
Urgency: No  
ID

**SUBJECT**

Bonds: public entities as beneficiaries

**DIGEST**

This bill requires for a bond given to, or in favor of, a beneficiary that is a public agency, in connection with the purchase, construction, or rehabilitation of real property or tangible personal property, that the beneficiary agrees to fulfill certain obligations to the principal, in order for a bond to be effective and for liability to be assumed by the surety or principal.

**EXECUTIVE SUMMARY**

A bond is essentially a financial guarantee that the party that obtains the bond, called the principal, will do something, or complete their obligations under an agreement, for the beneficiary. If the principal fails to do so, the surety company that guarantees the bond will pay the beneficiary or utilize the bonded amount to find another party to complete the contract. In the construction context, performance bonds and payment bonds are often used to guarantee that the work agreed to under a contract is performed by a contractor and to guarantee that the workers of the contractor are paid for their work, respectively. SB 425 proposes to require, before a bond is effective and liability attaches to the surety and the principal on a bond given to, or in favor of, a beneficiary that is a public entity in connection with the purchase or construction or other improvement of real or tangible personal property, that the public entity agree to a number of obligations to the principal. Specifically, SB 425 requires the public agency beneficiary to agree to make all payments to the principal, or to the surety if the surety takes on the principal's work upon the principal's default, and to perform all necessary obligations owed to the principal under the contract. SB 425 is sponsored by the Associated General Contractors of California, and is opposed by the California Building Industries Association.

## **PROPOSED CHANGES TO THE LAW**

### Existing law:

- 1) Establishes the Bond and Undertaking Law to consolidate procedural rules and requirements for the execution, posting, and providing of a bond required by statute or an undertaking that is used as security. (Code Civ. Proc. §§ 995.010 et seq.)
- 2) Defines “beneficiary,” for the purposes of bonds, as the person for whose benefit the bond is obtained. (Code Civ. Proc. § 995.130.)
- 3) Defines “bond” to include both: a surety, indemnity, fiduciary, or like bond executed by both the principal and sureties; and a surety, indemnity, fiduciary, or like undertaking executed by the sureties alone. (Code Civ. Proc. § 995.140.)
- 4) Defines “principal” as the person who gives a bond, and specifies that “obligor,” “principal,” and comparable terms mean “principal.” (Code Civ. Proc. § 995.170.)
- 5) Defines “surety” as one who promises to answer for the debt, default, or miscarriage of another, or who pledges property as security for a loan, including a personal surety and an admitted surety insurer. (Code Civ. Proc. § 995.185; Civ. Code § 2787.)
- 6) Specifies that a bond remains in force and effect until the earliest of:
  - a) the sureties withdraw from or cancel the bond, or a new bond is given in place of the original bond;
  - b) the purposes for which the bond was given is satisfied or abandoned without any liability having been incurred;
  - c) a judgment of liability on the bond that exhausts the bond is satisfied; and
  - d) the term of the bond expires. (Civ. Code § 995.430.)
- 7) Requires bonds to be in writing, be signed by the sureties under oath, and to include a statement that the sureties are jointly and severally liable, along with other information. (Civ. Code § 995.320.)

### This bill:

- 1) Requires that, if a statute provides for a bond to be given to, or in favor of, a beneficiary that is a public entity in connection with the purchase, construction, expansion, improvement, or rehabilitation of any real or tangible personal property, the bond is not effective and liability is not assumed by the surety or principal unless the beneficiary agrees to:
  - a) make all payments to the principal, or to the surety if the surety agrees to complete the work upon the principal’s default, pursuant to the terms of the contract;

- b) perform all necessary obligations owed to the principal under the contract.
- 2) Defines, for the purposes of its provisions, “contract” to mean a written or oral contract, as defined in specified provisions of the Civil Code, that obligates a principal to purchase, construct, expand, improve, or rehabilitate real or other tangible personal property.

### COMMENTS

#### 1. Author’s statement

According to the author:

SB 425 will address a critical gap in the bond requirements for public entities in California. Existing law addresses payment and performance bond requirements for the direct contracting of public works improvements. However, gaps currently exist around bond requirements for public works improvements that are not directly contracted by public entities, but instead for which public agencies seek bond commitments, particularly payment and performance bonds. SB 425 will resolve this issue to ensure that public agency bond requirements are clearly defined and that bonding requirements are consistent, thereby providing greater clarity and consistency in the law governing bond obligations for public entities in California.

#### 2. The Bond and Undertaking Law

A surety bond is a legal instrument through which a principal obtains a bond from a surety company for the benefit of the obligee. An obligee is also considered the beneficiary to the bond. The bond is essentially a financial guarantee that the principal will do something, or complete their obligations under an agreement, for the obligee. If the principal fails to do so, the surety company guarantees the bond and will pay the obligee or utilize the bonded amount to find another party to complete the contract. In the construction context, a performance bond, for example, is a bond that guarantees that a contractor will actually perform their obligations to the obligee, such as by completing construction on the construction project. If the contractor fails to complete the construction as contracted for, the surety company may utilize the bonded amount to find another contractor to complete the project. A principal typically must pay an upfront fee that is a percentage of the bonded amount to the surety company to obtain the bond.

The Bond and Undertaking Law (Code Civ. Proc. §§ 995.010 et seq.) sets out the uniform legal framework and procedures for the execution, posting, and providing of a bond or undertaking that is used as security. Its provisions are meant to regulate the hundreds of different bonds that various statutes in California law provide. It includes

definitions of the different parties involved in a surety bond, such as a definition of “beneficiary” that specifies that the beneficiary is the person for whose benefit the bond is obtained. (Civ. Code § 995.130.) The Bond and Undertaking Law requires bonds to be in writing, to be signed by the sureties under oath, and to include a statement that the sureties are jointly and severally liable, along with other information. (Civ. Code § 995.320.) Typically, a bond becomes effective at the time it is given, and remains in effect until it is withdrawn or cancelled, a new bond is given, the purpose of the bond is satisfied or abandoned without any liability, the term of the bond expires, or a judgment of liability on the bond amount is satisfied. (Civ. Code § 995.430.) The beneficiary of a bond may enforce the liability on a bond against either the principal or the surety, or both, and may enforce this liability through a civil action against both. (Civ. Code §§ 996.410, 996.430.) For a public works project, the surety must be an admitted surety insurer, which are corporate entities licensed by the state to provide bonds. (Civ. Code § 995.311).

Bonds are required by a variety of state laws and in a variety of contexts. In construction projects done for a public agency, which are typically called public works projects, performance and payment bonds are required. (Pub. Contract Code § 10221; Civ. Code § 9550.) A performance bond, as described previously, ensures to the beneficiary (which in this case is a public agency) that the contracted-for work is completed. A payment bond ensures that a contractor pays all of their labor obligations for the project. However, while payment and performance bonds ensure the principal’s performance of certain obligations, they do not require or address any obligations of the beneficiary under the construction contract.

3. SB 425 requires public agencies to agree to certain commitments to the principal before a bond in favor of the agency is effective

SB 425 proposes to add obligations on the part of the public agency before a bond can go into effect. It would require, as a condition for a bond for a public agency to be effective and liability to attach to the surety and principal, that the beneficiary agree to both: pay all payments to the principal, or to the surety if it agrees to complete the work upon the principal’s default, pursuant to the contract; and perform all necessary obligations owed the principal under the contract. This requirement would apply to all bonds provided for by statute for the purchase, construction, expansion, improvement, or rehabilitation of any real or other tangible personal property.

Typically, if a public agency is engaging a contractor for a construction project or something similar, the public agency has a contract for the work to be performed and the funds to be paid for that work. Thus, in the relationship between the public agency and the direct contractor, the public agency has already agreed to pay the contractor for the work to be performed, and thus has privity with the contractor. The author asserts, however, that a gap currently exists when public works projects are not directly contracted for by the public agency, but for which the public agency still requires a

bond from the subcontractor. In this arrangement, the public agency does not have a direct contractual relationship with the contractor; it only has a contractual relationship with the developer, who then has a contractual relationship with the contractor they hire. The author asserts that a contractor may be required to obtain a payment or performance bond to the benefit of the public agency, but not have any contractual right to be paid by the public agency for their work under the contract. Instead, the public agency would pay the developer, who, in theory, would pay the contractor. If the developer fails to pay the contractor, the contractor must go after the developer for payment, even while they are required to complete the contracted-for work under the bond obligation.

However, developers can and do require bonds of their contractors, for which the developer is the beneficiary. It is unclear how often a contractor is required to obtain a bond to the benefit of the public agency, a party with whom they have no contractual relationship, instead of the developer. For example, in the statutory provisions requiring a payment bond on a public works project, the obligation of providing a payment bond is placed on the direct contractor, though the provisions permit a direct contractor to require a bond from the subcontractor. (Civ. Code § 9554.) Regardless of this, SB 425 aims at ensuring that a contractor who is required to obtain a bond for the benefit of a public agency receives some contractual promises from the agency regarding payment and obligations due the contractor.

#### 4. Arguments in support

According to the Associated General Contractors of California, which supports this bill:

As sponsors of this measure, we are seeking to address the existing ambiguity in payment and performance surety bond regulations, particularly for works of improvement that are not directly contracted by public entities but are ultimately financed and acquired by public agencies. This bill will amend the overarching statute governing surety bond obligations, thereby providing certainty for the surety bond market and ensuring that public agencies and associated public entities have in place surety bonds that protect contractors and local governments alike.

Under current law, Section 9000 et seq. of the Civil Code primarily addresses payment and performance surety bond requirements for the direct contracting of public works of improvement. Additionally, Section 995.010 et seq. of the Code of Civil Procedure, known as the Bond and Undertaking Law, prescribes procedures for bonds or undertakings executed as security pursuant to any statute. However, these laws do not adequately cover surety bond requirements for projects indirectly contracted by public entities.

The ambiguity in existing surety bond regulations has led some public agencies to request non-standard dual-obligee surety bonds from general contractors, naming both the agency and the developer as obligees. This creates a one-sided guarantee obligation, where the public agency can mandate payment and performance under the surety bond without any associated obligation to pay the contractor or surety for the mandated work if the project developer fails to perform. This situation is untenable for the surety bond market, which requires certainty that they will be compensated for services rendered.

SB 425 will add Section 995.450 to the Code of Civil Procedure, requiring that surety bonds given to public entities for projects involving buying, building, expanding, improving, or fixing any property must include provisions ensuring that the public entity agrees to pay the General Contractor or the surety if the surety must finish the work due to the project developer's inability to do so. Additionally, the public entity must fulfill all necessary duties owed to the general contractor under the bonded overarching development construction agreement.

#### 5. Arguments in opposition

According to the California Building Industry Association, which is opposed to SB 425:

Regretfully, CBIA is opposed to SB 425. We have met with the sponsors of the bill on more than one occasion but still do not understand why the bill is necessary. Contractors have contractual rights to be paid by developers, and developers typically obtain payment and performance bonds to ensure that the improvements are completed and that contractors are paid. We don't see how it is possible that contractors are being required to perform work for which they are not paid. Moreover, the Mello-Roos districts where this is used are acquisition districts. This means that District does not first fund the construction of improvements and then take ownership of them. Instead, the district takes ownership of the improvements after the improvements are complete and paid for by the developer where the developer is involved in the improvements. Putting aside that lack of clarity as to the cause of the problem, we are very concerned that this would jeopardize the use of Mello-Roos Community Facilities District funding and similar funding mechanisms. Since these special tax districts are a necessary infrastructure funding mechanism for the production of desperately needed housing in California, we do not want to jeopardize its use.

### **SUPPORT**

Associated General Contractors of California (sponsor)

### **OPPOSITION**

California Building Industry Association

### **RELATED LEGISLATION**

Pending Legislation: SB 61 (Cortese, 2025) prohibits an owner, direct contractor, or a subcontractor of a private work of improvement from withholding a retention payment from a direct contractor or subcontractor of more than five percent, except as specified. SB 61 is currently pending on the Senate Floor.

Prior Legislation:

SB 189 (Lowenthal, Ch. 697, Stats. 2010) established the provisions related to retention payments in private works of improvement that specify the timelines for when retention payments must be paid, and the penalties for an owner or direct contractor's violation of its provisions.

AB 263 (Correa, Ch. 181, Stats. 2001) required all bonds required on public works projects to be executed by an admitted surety insurer, and required the public agency to confirm that the surety was an admitted surety insurer.

AB 2751 (McAlister, Ch. 998, Stats. 1982) established the Bond and Undertaking Law to establish consolidated, procedural rules for statutory bonds and undertakings.

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