

1989

# Financial Performance Guarantees: The State of Practice

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## Recommended Citation

Feiden, Wayne; Burby, Raymond; and Kaiser, Edward, "Financial Performance Guarantees: The State of Practice" (1989). *Journal of American Planning Association*. 72.  
[10.1080/01944368908975438](https://doi.org/10.1080/01944368908975438)

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# Financial Performance Guarantees

## The State of Practice

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Wayne M. Feiden, Raymond J. Burby, and Edward J. Kaiser

**Financial performance guarantees are tools for ensuring that funds needed to pay for improvements called for by development permits and approvals are available in the event a developer defaults on permit requirements. Once limited to surety bonds and cash escrows, new types of guarantees have been developed and are coming into common use. Standby letters of credit, in particular, are being used more widely and have a number of advantages. To use guarantees successfully, municipal governments must make careful decisions about a number of administrative matters. Evidence from 309 municipalities reported in this article can help local planners make the right choices.**

Financial performance guarantees are designed to ensure that funds needed to complete public and private improvements required by local ordinances or development approvals are available in the event of a developer's default or bankruptcy. Guarantees create legal and financial incentives for developers to perform work required as a condition for issuance of permits, and they make it easier for governments to finish such work if a default occurs. When properly designed, they also contribute to a number of other objectives. They can make administration of land use and environmental regulations easier and more efficient, reduce the frequency and expense of litigation, provide protection for consumers purchasing property in new projects, and, importantly, allow communities to be more flexible in responding to developers' needs for more time to complete infrastructure after occupancy permits are issued or to delay completion of landscaping until weather conditions are favorable.

Performance guarantees have long been used in local subdivision regulation, where they are "an esoteric but important part of the planning process" (Rogal 1974), but not much is known about local governments' experience with them here or in other regulatory areas. In this article, we describe the frequency with which financial performance guarantees and accompanying administrative forms and techniques are used in the United States, and we draw on local planners' experience and perceptions to indicate which approaches to guarantees and their administration seem to be working best in actual practice. Our information expands and updates the only previous survey of the use of guarantees (Seidel 1978), and it provides planners interested in adopting or revising their financial performance guarantees with feedback from practical experience that they can use to augment various commentators' words of wisdom (e.g., American Law Institute 1976; Freilich and Levi 1975; Kelley and Schultz 1988; Mandelker 1982; Rogal 1974; Schultz and Kelley 1985; Yearwood 1971).

The data for this article come from questionnaires returned by planners working in 309 municipalities across the United States. The survey, completed during the summer of 1988, was sent to a random sample of 500 municipalities with populations between 15,000 and 500,000.<sup>1</sup> Although planners working in communities that use financial guarantees may be slightly overrepresented in our data, since they are more likely to be interested in the topic and thus to have returned a questionnaire, we believe the sample size and response rate (62 percent) are high enough for readers to have confidence in our findings.<sup>2</sup> Also, comparison of the distribution of responding and nonresponding municipalities reveals no significant differences between respondents and nonrespondents by region or population.<sup>3</sup>

### How Guarantees Are Used

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The survey confirmed that subdivision regulations authorize the use of financial performance guarantees far more frequently than do any other municipal regulations

(Table 1). That practice is reflected in the literature as well, which discusses almost exclusively the use of guarantees as a tool for obtaining compliance with subdivision regulations (e.g., Kelley and Schultz 1988; Rogal 1974). The survey also revealed, however, that financial performance guarantees now are used for a wide variety of other land use and environmental regulations as well. A substantial minority of jurisdictions (between 17 percent and 30 percent) write performance guarantees into zoning, stormwater, erosion/sedimentation, and on-site sewage regulations. In those jurisdictions, guarantees were required for a substantial (but minority) proportion of the total number of the permits issued for each type of regulation during the last full year of record.

Traditionally, local governments have used financial performance guarantees to ensure the completion of improvements to be dedicated to the public. Many of the improvements required by subdivision, zoning, erosion control, stormwater, and on-site sewage regulations, however, are not dedicated to the public but instead remain in private ownership (these include such improvements as landscaping, storm drainage facilities in commercial and apartment projects, and septic tanks). A majority of the communities (56 percent) use financial guarantees in some cases to ensure that required improvements which will be privately owned are built to specified standards and are completed before a project is occupied.

## Types of Guarantees

Several types of financial performance guarantees are available to local governments. Performance (surety) bonds and cash escrows are described most frequently in the literature, but other options are also available and are commonly used. These include property escrows, standby letters of credit, improvement credit agreements, and liens and covenants. We will describe each of these briefly and then examine the frequency with which they are being used.

### Performance Bonds

Where a performance bond serves as the guarantee, a surety company agrees to pay the value of the bond to a local government (the obligee) if a developer (the prin-

cipal) defaults on the permit conditions. The greater assets of a surety company assure the local government that the financial resources will be there to complete required improvements. Performance bonds have some similarities to insurance, because the surety company is taking some risk and surety exists to reduce the risk to local government. But, unlike the conditions with insurance, the risk is not spread widely, and as a result, surety companies take only limited risks. Because of that, performance bonds can be difficult or impossible for small or new companies to obtain (Seidel 1978). For larger developers with collateral, however, obtaining a performance bond at a reasonable premium has not been difficult (Rogal 1974).

If a developer is in danger of default, a surety company may assist in completing required improvements, possibly by loaning the developer required funds, if that might avoid greater liability. Once a developer defaults, a surety company has several options: it can finance completion of the project by the original developer and, if the project is a success, recover its capital; it can hire a new contractor to finish the project; or it can pay off the bond principal. If the surety company takes an option other than paying off the face value of the bond directly to local government, its liability may exceed the amount of the bond.

Most commentators believe that surety companies would rather pay off a bond than follow the first two courses of action (Schroeder 1982; Webster 1982; Schultz and Kelley 1985). Our data indicate, however, that surety companies are somewhat more likely to arrange to have an improvement completed than to pay local governments the amount of the bond. Thirty-four percent of the municipalities we surveyed reported that, when developers defaulted, the surety company gave them the funds, 40 percent said the surety company arranged to have the improvement completed, 16 percent reported both experiences, and 10 percent reported a variety of other outcomes.

Schultz and Kelley (1985) argue that, while performance surety bonds are better than no guarantee, they are the least preferable of the financial guarantees available because local governments often have to go to court to collect (and, they argue, surety bonds add an unreasonable cost for the developer, most of which is passed on to consumers). Britt (1982) agrees that some claims may be settled for less than the full principal, but he argues that most surety companies pay claims in full and that few cases go to court. Our data indicate that municipalities using surety bonds are neither more likely nor less likely than municipalities using other types of financial performance guarantees to have to go to court to settle claims. Twenty-one percent using surety bonds went to court one or more times between 1983 and 1988, while 20 percent using other types of guarantees and not using surety bonds went to court during that time.<sup>4</sup>

### Cash Escrows

A cash escrow is a special bank or other third party account that can be converted readily to a specified sum

**TABLE 1: Use of financial performance guarantees with regulations**

Type of regulation	Municipalities using financial performance guarantees to ensure compliance with regulation (%)	Permits issued with a guarantee required (%)
Subdivision	76	70
Zoning	30	33
Stormwater	28	27
Erosion/sedimentation control	23	27
On-site sewage	17	21

of money. Usually, only local government can authorize release of the money to a permit holder, in accordance with terms of the escrow. The government also can collect the money if it declares that a developer has defaulted on specified permit obligations. Traditionally, escrows are the second-most-common form of financial performance guarantee after surety performance bonds. For many years bonds and cash escrows were the only performance guarantees authorized in many communities.

Cash escrows are unpopular with developers, since they are very costly if required for the full value of improvements plus a margin of safety and are not released until after the improvement has been completed. In order to avoid the need for double funding of improvements, escrow agreements often allow either partial release of funds to developers after completion of each required improvement and assurance that there are no unpaid bills, or release of funds to subcontractors to complete required improvements. When partial disbursements are made, governments may reduce the risk of having to declare a developer in default, but they expose themselves to the risk of financial shortfalls if escrow accounts are exhausted before all required improvements are installed (Seidel 1978; Schultz and Kelley 1985). That potential can be offset to some extent, however, if interest on escrow funds is accumulated in the account and added to the principal amount (McPherson 1974).

### **Property Escrows**

Property escrows are structured in the same way as cash escrows, but instead of cash, real property, such as land, buildings and improvements, or personal property in the form of stocks, bonds, or equipment is placed in escrow. Property escrows have a number of disadvantages. They involve valuation of property, assurance that property is free of liens, and, if a default occurs, the time and bother of marketing property to obtain funds required to complete improvements. Because of those disadvantages local governments have avoided property escrows (Seidel 1978).

### **Standby Letters of Credit**

A standby letter of credit is an agreement by a bank or other financial institution to pay specified sums of money to a third party, such as a local government, in the event a developer defaults on responsibilities to complete required improvements to standards and on schedule, as specified in the terms of the letter. The borrower (e.g., a developer) agrees to repay the bank in a separate agreement.

Developers tend to favor letters of credit because they are less expensive and more readily available than surety bonds, while they do not require the outlay of capital required by escrows. Standby letters of credit appeal to local governments as well because they ensure the availability of funds if a developer defaults, and they provide a simple mechanism for collecting the funds (a government presents the bank with documentation of default).

### **Improvement Credit Agreements**

An improvement credit agreement is a three-party agreement between a developer/borrower, a bank, and a local government in which the bank agrees to pay for improvements as they are completed if the local government accepts the improvement. Unlike the case of a standby letter of credit, which is used only if developers default on their obligations, the developer and the local government authorize the bank to make payments to the developer and subcontractors as required improvements are made. Improvement credit agreements ensure that money is available to make required improvements and that local governments will have an opportunity to approve those improvements before funds are dispersed. Because money is dispersed incrementally, there is more risk to local governments than with standby letters of credit, since the line of credit could be exhausted before all improvements are made.

### **Liens/Covenants**

Although not technically financial performance guarantees, liens or covenants can be placed by local governments on a property being developed to record an encumbrance on the property. The liens remain in effect until the necessary improvements have been made and approved. If a developer defaults on the improvements, local governments can initiate foreclosure proceedings. Liens remain with the property if it is transferred and help ensure that future owners are aware of the nature of the encumbrance.

If a developer goes bankrupt because there are usually other liens and mortgages on property being developed, the cash value of the local government claim may be very limited; thus, the main purpose of the lien is to clarify the encumbrance for future owners and to minimize the danger of a solvent developer refusing to build an improvement to required standards.

### **Frequency of Use**

In 1976, Seidel (1978) surveyed 80 local governments and found that 96 percent used performance or improvement bonds, 71 percent cash escrow accounts, 9 percent real property escrow accounts, and 6 percent letters of credit. He did not ask about the use of improvement credit agreements or liens. We found, 12 years later, that bonds continue to be the most frequently used financial guarantees (Table 2). We also found that there has been a dramatic increase in the use of letters of credit, which are authorized for use by a majority of local governments and now actually are used in practice more frequently than cash escrows (see the right-hand column of Table 2), even though they are still not authorized by enabling legislation as frequently as cash escrows. We believe that this increase stems from the ease and relatively low cost of obtaining letters of credit and, to a lesser extent, because local governments increasingly are encouraging developers to use letters of credit rather than performance improvement bonds. Governments continue to use real

**TABLE 2: Frequency of use of performance guarantees**

Type of guarantee	Municipalities authorized to use the guarantee (%)	Permits that included a guarantee <sup>a</sup> (average per municipality) (%)
Performance or improvement bond	78	43
Cash escrow	66	16
Letter of credit	59	36
Improvement credit agreement	18	2
Lien on development	13	3
Noncash and real property escrow	6	1

a. Over the past 5 years.

property escrows infrequently, but a larger, although still small, proportion of governments are using improvement credit agreements and liens.

### Structure and Time Limits

Municipalities may establish guidelines regarding the type of improvements (permanent or temporary) for which financial guarantees are required, time limits for the completion of improvements, and whether warranties of performance after an improvement is completed will be required. Our data indicate that local practices vary widely across municipalities (Table 3). Permanent improvements include most of those dedicated to the public, such as roads and sewers, as well as many improvements, such as landscaping and permanent erosion-control structures, that will remain in private hands after construction is completed. Temporary improvements, such as temporary erosion control devices, usually remain in private ownership and are no longer required at the end of the construction process. Financial guarantees are far more common for permanent improvements than for temporary ones because permanent improvements are more numerous, often have greater impact, and are more likely to be dedicated to the public. Nevertheless, guarantees are important in both cases, since the damage due to failure to provide a needed temporary improvement, such as erosion control, can be substantial and long lasting.

Municipalities using financial performance guarantees give developers a specified period of time within which to complete required improvements. At the expiration of the time limit, developers can be declared in default, and the municipality can use guarantee funds to complete the improvement. A sizable minority of the municipalities we surveyed (37 percent for permanent improvements and 47 percent for temporary improvements) use flexible time limits, varying the time allowed to complete improvements with the size of development projects. Such

flexible limits enable local governments to allow large, phased developments several years to finish a project while not being forced to allow the same amount of time for smaller projects that reasonably can be completed in a matter of months. Among jurisdictions with inflexible time limits, the vast majority allow developers from one to two years after permit issuance to complete required improvements (see Table 3.) In most cases, however, time limits can be renewed at the discretion of the municipality (89 percent of the municipalities surveyed) or by the developer as a matter of right (8 percent of the municipal-

**TABLE 3: Requirements imposed by performance guarantees**

Guarantee characteristics	Municipalities (among those using guarantees) (%)
<b>Type of improvement for which a guarantee is required</b>	
Permanent improvements	99
Temporary improvements	69
<b>Time limit for completing improvement</b>	
Permanent improvements	
Less than 6 months	2
6-11 months	12
12-24 months	41
More than 24 months	9
Varies with project size	37
Temporary improvements	
Less than 6 months	8
6-11 months	13
12-24 months	32
More than 24 months	1
Varies with project size	47
<b>Improvement completion after issuance of certificate of occupancy</b>	
Not allowed	31
Allowed	69
Improvements to be privately owned	
Private landscaping	47
Private paving projects	28
Private on-site sewage systems	4
Other private improvements	29
Improvements to be dedicated to the public	
	27
<b>Maintenance/performance warranty</b>	
Not required	19
Required	81
Length of warranty	
Less than 12 months	20
12-24 months	63
More than 24 months	5
Varies with project size	13

ities surveyed). Only 3 percent of the jurisdictions we surveyed prohibit extensions of time limits.

For some types of required improvements, many municipalities (69 percent of those surveyed) will issue certificates of occupancy before required improvements are completed. Almost half of the municipalities with performance guarantees, for example, will issue certificates of occupancy before privately owned landscaping has been completed; about a quarter (28 percent) do the same for privately owned paving projects. Similarly, about a quarter of the municipalities allow developers to occupy projects before they complete improvements to be dedicated to the public.

More than four out of every five municipalities (81 percent) using financial performance guarantees authorize or require maintenance warranties for at least some improvements. Those warranties most commonly are required for 12 to 24 months after completion of the improvement (see Table 3).

### Costing and Releasing of Guarantees

Two of the most difficult tasks of administering financial performance guarantees are costing and releasing guarantees. Costing is the process of establishing the minimum dollar amount that the permittee must guarantee. The amount should be large enough to cover the cost of the improvements the municipality would have to provide if the developer defaults, but at the same time it should not be so large that it creates an unreasonable or illegal burden on permittees. Most communities (67 percent) use their own expertise in estimating the cost of improvements. Some (29 percent) use data from permit applicants to estimate costs, and some (21 percent) use actual contractors' bids (Table 4).

Municipalities generally (65 percent of those we surveyed) require that financial guarantees cover the entire estimated cost of required improvements. A quarter of those we surveyed have a flexible policy, sometimes requiring a financial performance guarantee for the full cost of an improvement and sometimes not, and 10 percent require a guarantee for only part of the estimated cost of the improvement. In addition, a majority of municipalities (68 percent) add a margin of safety to their estimates to account for inflation and the possibility of underestimation of costs. Among municipalities adding a margin of safety, 51 percent add from 1 to 10 percent to cost estimates, 23 percent add from 11 to 20 percent, and 17 percent add 20 percent or more. For 9 percent of the municipalities the exact amount of the margin of safety was not determined.

In order to reduce project costs, developers may request that municipalities release them from financial guarantees in stages as the project progresses. Sixty-one percent of the municipalities responding to our survey allow staged release of guarantee funds, but most also keep back some funds until all improvements are completed. The percent of the entire guarantee retained until completion varies among municipalities with a few (5

**TABLE 4: Costing and releasing financial performance guarantees**

Municipal practice	Municipalities (%)
<b>Costing</b>	
Source of improvement-cost estimate	
Municipal engineer	35
Permit administrator	32
Permit applicant	29
Subcontractors' bids	21
Other	7
Margin of safety	
None added	32
1-10 percent	33
11-20 percent	16
21-30 percent	7
31 percent or more	12
<b>Releasing</b>	
Staged release of funds	
Not used	39
Used	61
Percent of funds held until completion	
1-10 percent	57
11-19 percent	16
20 percent or more	21
Varies	16
Check for liens on the improvement by subcontractors and others before accepting dedication	
Sometimes or never	35
Always	65

percent) holding back as much as 40 percent of the guarantee amount. The most common practice (among 57 percent of municipalities), however, is to hold back 10 percent or less of the guarantee until final completion of all required improvements.

Before accepting dedicated improvements, municipalities should check to ensure that all payments have been made to subcontractors and that there are no liens on the improvement. Actual practice, however, sometimes differs from recommended practice. Thirty-five percent of the municipalities we surveyed report that they do not always check for liens before accepting dedications and releasing guarantees.

### Enforcement and Collection

Financial performance guarantees decrease the chance that a municipality will find it necessary to use public funds to complete unfinished improvements or to reconstruct improvements that have design or construction defects. If guarantees are difficult to collect, however, they fail to achieve their purpose.

Municipalities use several techniques to check for compliance with their regulations and to determine if

enforcement actions are necessary. Almost every municipality (98 percent) relies heavily on staff inspections. A majority of municipalities (69 percent), however, also require external professional certification in at least some of their regulations or for some types of projects (e.g., larger projects). While an applicant's consultant's certification is more likely to be biased than a municipal inspection, an outside professional can inspect many aspects of a project in more detail than staff has time to undertake. In recognition of that consideration and to avoid the bias possible when developers pay for professional certification, a number of municipalities (29 percent) choose the consultant to perform needed inspections.

If a project is found to be out of compliance with municipal regulations or permit provisions, municipalities have a number of options for obtaining compliance before calling in financial guarantees. In order of the percentage of municipalities authorized to use them, these options include withholding the occupancy permit (93 percent of municipalities); seeking civil penalties (83 percent); withholding other permits for the same project (57 percent); seeking injunctive relief (49 percent); seeking criminal remedies (40 percent); withholding sequential permits for other lots in the same development (38 percent); and withholding permits for unrelated projects by the same developer (9 percent) (Table 5).

In spite of these options, 40 percent of the municipalities we surveyed declared one or more developers in default of a financial guarantee between 1983 and 1988. Of that number, 39 percent said that after calling the guarantee there always were enough funds to pay for required improvements, 51 percent said there sometimes were enough funds, and 10 percent reported there never were enough funds from the guarantees to cover costs.

One of the reasons that guarantees are not always adequate to pay for improvements is that, if a permittee is bankrupt, other creditors may attempt to collect the guaranteed funds and may have access to those funds before the municipality. While this rarely happens, 17 percent of the municipalities that have attempted to collect on financial guarantees report at least one experience where creditors collected some of the money before the municipality. Cash escrows have been accessed by creditors most frequently (this has happened in 59 percent of the cases where attempts were made by other creditors), because they represent direct assets of the permittee that can be attached. In the other cases where guarantees were accessed by creditors, 35 percent were using surety bonds, 18 percent were using improvement credits, and 6 percent were using property escrows. Letters of credit, if properly written, are impossible for creditors to draw on because they represent an obligation of a bank to a municipality, not an obligation of the permittee. Hence, none of the municipalities that lost funds to other creditors was using a letter of credit as a guarantee.

Although in theory each type of financial guarantee can be collected without going to court, obstacles do arise, particularly when there are other creditors or when

**TABLE 5: Enforcement and collection of guarantees**

Municipal practice	Municipalities (%)
<b>Sanctions to secure compliance with regulations</b>	
Occupancy permit withheld	93
Civil penalties	83
Other permits for the same property withheld	57
Injunctive relief	49
Criminal remedies	40
Sequential permits withheld for lots in the same development	38
Permits for the same developer on unrelated developments withheld	9
<b>Calling in of financial performance guarantees between 1983 and 1988</b>	
None called	60
Bonds	23
Letters of credit	20
Cash escrows	17
Improvement credit agreement	2
Property escrow	1
<b>Adequacy of performance guarantee funds to finish improvements when developers have defaulted</b>	
Always enough funds	39
Sometimes enough funds	51
Never enough funds	10
<b>Creditors' accessing of funds before municipality</b>	
Has not occurred	83
Has occurred	17
<b>Type of guarantee used</b>	
Cash escrows	59
Surety bonds	35
Improvement credit agreements	18
Property escrows	6
Letters of credit	0

guarantee language is unclear or ambiguous. Between 1983 and 1988, 20 percent of the municipalities we surveyed that declared developers in default and attempted to collect on improvement guarantees went to court to enforce the guarantee. That represents a total of 54 court cases (5 of the 29 municipalities that declared developers in default and went to court did not report the number of cases). Presumably other cases have been settled out of court. In addition, the costs of litigation probably discourage some municipalities from taking legal action. Nevertheless it appears that the administration of financial performance guarantees results in only limited litigation. The percentage of municipalities using financial guarantees that resorted to court action to collect a guarantee between 1983 and 1988 was as follows: property escrows, 11 percent; liens/covenants, 14 percent; surety bonds, 21 percent; cash escrows, 23 percent; letters of

credit, 25 percent; and improvement credit agreements, 32 percent.

## Planners' Evaluations

When asked to sum up their overall experience with financial performance guarantees, 90 percent of the planners responding to our survey evaluated them as either very effective tools (58 percent) or somewhat effective tools (32 percent) for ensuring compliance with regulations. Community size has little association with perceived effectiveness, but effectiveness ratings do vary by type of guarantee used and other guarantee characteristics.

Planners are more likely to be pleased with the overall effectiveness of performance guarantees when their municipality is using surety bonds, cash escrows, and/or letters of credit. Significantly lower overall effectiveness ratings accompany the use of real property escrows, liens, and improvement credit agreements (less than 80 percent of the municipalities rate their use of guarantees as very or somewhat effective). Planners rate financial performance guarantees as more effective in achieving compliance with regulations under the following conditions: when agreements are set to cover the entire cost of an improvement; when higher margins of safety are used in estimating costs; when the municipality always checks for liens before accepting dedication of improvements; and when creditors have not been able to access the funds.

Municipalities have found that permittees generally do not find financial performance guarantees unreasonably onerous. Less than 1 in 20 of the municipalities we surveyed said they had received "many" complaints from developers. In part, that may stem from the relatively low cost of the guarantees to the development community. Eighty-five percent of the municipalities surveyed estimate that guarantees cost developers 2.5 percent or less of total project costs, and 23 percent put the cost to developers at less than 1 percent of total project costs.

## Conclusions and Policy Implications

In actual practice, financial performance guarantees are an effective, although not infallible, means of ensuring that improvements required as a condition for issuing development permits and approvals will be built to specified standards if the permittee defaults. They are being used widely and successfully by both large and small municipalities throughout the United States, not only in subdivision regulations, but also in other regulatory programs that require developers to construct on- and off-site improvements, and they appear to be accepted by the development community.

Financial guarantees seem to be useful not only for improvements dedicated to the public but also for those that remain in private ownership after completion of development. Thus, they provide a degree of consumer

protection in the development process. When improper installation of privately owned facilities has the potential to threaten public health, as is the case with septic tank installations, they benefit the general public as well.

Although municipalities can choose among a variety of types of financial performance guarantees, experience in actual practice suggests that a relatively new form of guarantee for municipalities—standby letters of credit—has a number of advantages, not the least of which is reduced exposure to loss of guarantee funds to other creditors. Survey data reported here indicate that there has been a substantial increase in the use of letters of credit over the past decade. In contrast to that trend, surety bonds and cash escrows are becoming less dominant. Surety bonds may be difficult for small and undercapitalized developers to obtain, and cash escrows are readily accessible to other creditors in the event a developer declares bankruptcy.

We recommend that municipalities that are not using financial guarantees give careful consideration to the adoption of this tool for ensuring compliance with development regulations, and that municipalities using guarantees for some programs, such as subdivision regulations, consider their use in others, such as zoning, stormwater management, erosion and sedimentation control, and wetland regulations, areas where guarantees are not commonly used at this time.

We also recommend that letters of credit be authorized whenever any financial guarantee is allowed or required. Letters of credit generally provide the best protection for a municipality because they represent an obligation of a bank that is independent of a developer's financial situation, and they are relatively easy for developers to obtain. Letters of credit, however, may lack the flexibility of some other types of guarantees. Thus, we also recommend that municipalities authorize use of a variety of types of guarantees. Large developers, for example, might find that surety bonds are easily obtainable, while small developers, who cannot obtain a surety bond, nevertheless might have the capital to put up a cash escrow.

In conclusion, financial performance guarantees are a powerful tool, and are being used in an increasing number of local government regulatory programs. They are appropriate in all communities. They can improve compliance with local regulations and reduce court costs for local governments, and they can assure consumers and the community as a whole that development meets local standards for the quality of the built environment.

## NOTES

1. We obtained the sample frame for the local government survey from *Municipal/County Executive Directory/1987* (Carroll Publishing). We did not survey jurisdictions with populations below 15,000 because, although there is a very large number of them, they represent a small proportion of the U.S. population. Their inclusion in the random sample would have

skewed the sample toward very small places. That might have been handled by drawing a stratified sample, but we believed the advantage in an ability to generalize to a larger universe was more than offset by the more cumbersome data analysis and reporting that inclusion of smaller jurisdictions would have entailed. We excluded cities of 500,000 or more people (of which there are 23 in the United States) from the sample frame because they represent a small category of local governments and have regulatory approaches and planning problems that tend to be unique.

2. The 309 municipalities represented in the data reported here constitute 16 percent of the 1,881 municipalities in the United States with populations between 15,000 and 500,000. Confidence intervals around the proportions reported in this article vary depending upon whether data represent the entire sample of 309 cities or a subgroup of those cities. The broadest confidence intervals (at the 95-percent level of confidence) range from  $\pm 5.6$  percent for responses to dichotomous questions (e.g., use or nonuse of performance guarantees and various administrative measures), with a 50 percent/50 percent split in responses and all 309 cities represented, to  $\pm 10$  percent with 96 cities represented (the smallest subgroup for which data are reported). Those confidence intervals narrow the larger the subgroup and the more that proportions vary from a 50 percent/50 percent split toward a 0 percent/100 percent split in responses to dichotomous questions.
3. Of the municipalities that returned questionnaires and are represented in the data reported here, 54 percent have populations between 15,000 and 29,999; 30 percent have populations between 30,000 and 59,999; and 16 percent have populations of 60,000 or more. We note, however, that among the cities surveyed, we could find no systematic differences between larger and smaller cities in the use and administration of financial guarantees.
4. Those results have to be viewed with some caution, however, since municipalities often use a variety of types of guarantees, and we did not ask specifically if court action was related to a surety bond or to another type of guarantee. Thus, it is possible (although it seems improbable) that the municipalities using surety bonds that reported court action during the past five

years to collect on a performance guarantee could have gone to court to collect on other types of guarantees than surety bonds.

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