SECURING AN APPEAL BOND WITH A STOCK AND BOND PORTFOLIO

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When collateral is required to secure an appeal bond, marketable securities are another valuable alternative that can be used. Marketable securities for the purpose of this article are defined as money market funds, stock and bond investments, mutual funds and exchange traded funds (ETF's) held in a brokerage account. According to a 2016 Gallup poll, 52% of U.S. adults own marketable securities in some form making it a potentially important option for appellants.

How does it work?

The surety company will first request a copy of the most recent brokerage statement, so they can review the holdings in the account. They generally only accept highly rated investment grade securities held in non-retirement accounts. If the marketable securities are acceptable, the surety will generally discount the current value to account for possible market fluctuations.

The amount of the discount will depend on the type of investments. For example, US Treasuries are discounted very little, if anything, while an S&P 500 index fund will be discounted more. If this amount after the surety's discount exceeds the required appeal bond amount, the surety will consider proceeding forward. Otherwise, additional collateral may be required, which can be in another form, if necessary, such as cash, letters of credit or real estate.

The next step is for the surety to get in contact with the brokerage firm holding the securities to enter into an account control or pledge agreement. Among other things, this gives the surety the right to sell the assets and recoup a loss in the event they are forced to pay a claim out under the bond. The surety has their own account control agreement form that can be used, but the brokerage will sometimes have their own form.

Key to the process is the surety and brokerage must come to an agreement on the terms included in the account control agreement. In the instance that the surety and brokerage firm cannot agree, it is possible for the client to transfer their accounts to another brokerage that either has a track record of working with the surety or is willing to agree on the terms of the control agreement.

Benefits

One of the major benefits of using marketable securities to secure an appeal is the client does not have to liquidate their holdings, which could trigger

capital gains tax liability or cause them to lose out on potential future investment returns.

In some instances, the client may be given limited trading authority, which would allow them some control over continuing to manage their investments, but it is important to note that this is subject to the surety's approval.

What does it cost?

Due to the risk of market fluctuations that the surety undertakes, the surety sometimes charges a higher rate when using marketable securities than other forms of collateral like cash or a letter of credit. The specific rate will depend on the types of assets held in the brokerage account and the bond amount. One thing to keep in mind is the potential investment return the client can gain from not having to liquidate the assets can sometimes offset the higher cost, if applicable.

Other things to consider

If the client's brokerage firm is owned by a bank, the client may be able to get the bank to issue a letter of credit to the surety by securing it with the marketable securities. Letters of credit generally cost between 1-2%, which can potentially make it a less expensive option since the bond premium can be much lower when using a letter of credit as collateral.

It's important to note that brokerage firms that do not have bank affiliations do not have the ability to provide letters of credit.

Time frame

Timing is always an issue when securing an appeal bond since most jurisdictions have very short if any automatic stay provisions. The preliminary approval by the surety of the stock or bond holdings only takes a couple days, and the bulk of the time required lies in the negotiation of the account control agreement with the brokerage. We recommend allowing 2-3 weeks for the entire process, but if the surety already has a working relationship with a particular brokerage, we've seen it take as little as 1-2 weeks.

Conclusion

There is only one surety in the market that will consider accepting marketable securities as collateral and only a handful of agents with the experience in both appeal bonds and using this form of collateral. Therefore, it's important to talk to an expert well versed in putting together these arrangements to ensure the process is handled effectively and efficiently.

Dan Huckabay is president of Court Surety Bond Agency (CSBA), one of the leading providers of appeal bonds in the nation. He has underwritten appeal bonds in almost every state and federal district court for clients ranging from individuals to Fortune 500 companies. Mr. Huckabay is a frequent presenter, author, and expert witness on the topic. Dan can be reached at (877) 810-5525 or at Dan@courtsurety.com