



U.S. Small Business
Administration



**DESANCTIS
INSURANCE**

Introduction to Contract Bonding Surety Bond Guarantee Program for Small Businesses

Presented by:

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Just a quick background on who I am and the Agency I represent:

- DeSanctis Insurance Agency has been in business since 1973, specializing in providing insurance and bonding programs for commercial clients all over New England. www.desanctisins.com
- Long tenured partner with the SBA Surety bond program
- Appointed with over 15 different surety (bond) companies in an effort to ensure proper placement for each client.

Paul Patalano – Senior Vice President:

- B.S. in Safety and Environmental Science- Mass Maritime Academy (2001)
- Certificate in Construction Project Management - Northeastern Univ. (2005)
- Jacobs Engineering - Project Coordinator (1999 – 2001)
- Keville Enterprises Inc., - Lead Construction / Engineering Inspector (2001-2006)
- Joined DeSanctis Insurance Agency, Inc. in 2006.



The Basics – What to Look For

- **Contract Surety Bonds:**
 - ✓ Contract bonds & why they are required
 - ✓ Getting pre-qualified
 - ✓ What bond underwriters look for
 - ✓ Working capital & bank support
- **SBA Surety Bond Guarantee Program:**
 - ✓ Eligibility
 - ✓ Required information
 - ✓ Application process & fees
 - ✓ Locating SBA certified agents

Common Definitions

Principal: small business/contractor or its owner(s).

Surety: A company that provides surety on behalf of someone else. In most cases, a surety company is a division of a large insurance company. Surety companies typically are authorized and qualified to do business by the state insurance commissioner where they are domiciled and in the jurisdiction where the bond is issued.

Agent: representative of the Surety authorized to issue bonds. They market and prepare applications to the Surety and SBA.

Obligee: project owner who contracts with the Principal for the performance of a contract. If the Principal defaults on a project the Obligee is made whole by the Surety.

Contract Bonds Defined

Bid Bond: guarantees that if the Principal is awarded a contract, the required performance and payment bonds will be provided

Performance Bond: guarantees the contract will be successfully completed in accordance with contract terms and conditions

Payment Bond: guarantees that subcontractors and labor and material suppliers will be paid for their work

Maintenance Bond: guarantees that any defects in workmanship or materials will be remedied within a specified time period, usually one to two years

Bonds are signed by the Principal and Surety and delivered to the Obligee to guarantee the terms of the contract or bid proposal.

Why Surety Bonds are Required

Surety bonds are required on many projects to ensure that the contracts are properly completed, protecting the Obligee, subcontractors, labor and material suppliers.

Federal Government: all Federal construction contracts greater than \$150,000 require Performance and Payment bond under provisions of the Miller Act

- For construction contracts greater than \$35,000, but not greater than \$150,000, the contracting officer shall request a payment bond only.

State, County & Local Government: most other governmental entities have adopted similar provisions referred to as “Little Miller Acts”

Private Sector: many private sector Obligees also require surety bonds

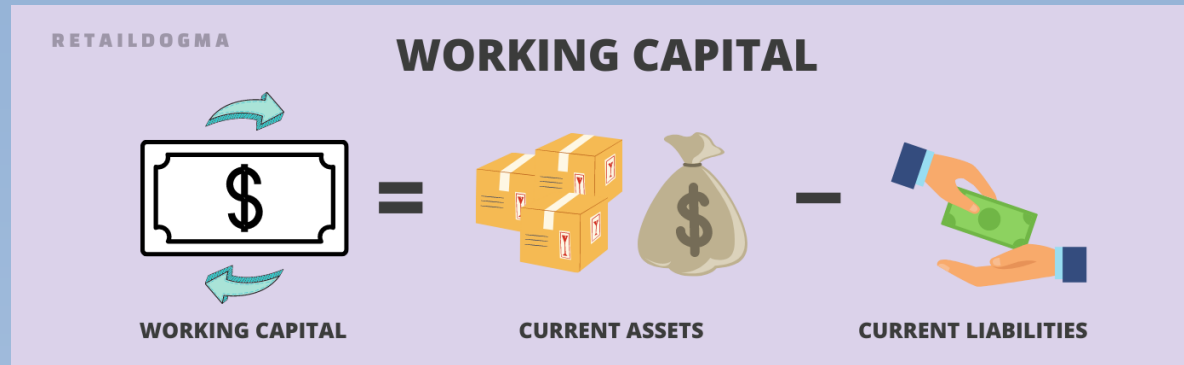
Pre-Qualification

- Pre-qualifying means knowing what your allowable bond credit levels will be **in advance** of bidding to assure bonds will be available
- **What you are trying to obtain:**
 - ✓ Single Contract Limit (\$500,000)
 - ✓ Total Aggregate Work Program (\$1,000,000)
 - ✓ Allowed Type of Work (General Construction, Electrical, etc.)
- **Becoming bondable is similar to the process of obtaining bank credit**
- **Allow plenty of lead time**

Surety's Underwriting Focus

The 3 C's of Bonding

- **Character** - refers to the moral qualities unique to an individual or entity. Character can sometimes be the most important. If the principal falls a little short in one of the other Cs, character can often move the needle from declined to approved.
- **Capital** – being able to show your financial position such as working capital, equity and profitability (financial statements)
- **Capacity** – contractor's capability, job history, available responsible workload. Character can sometimes be the most important. If the principal falls a little short in one of the other Cs, character can often move the needle from declined to approved.



What is Working Capital?

- Measures business's ability to meet current and future financial obligations
- **Adequate working capital is essential to obtaining bonding**
- Working Capital is calculated from the balance sheet:
Cash + Accounts Receivable + ½ of Inventory
(+ Available BLOC Balance for OSG)
- Current Liabilities
= Allowed Working Capital

Bank Support

A good banking relationship is important to obtaining bonding.

Agent will request information on:

- Accounts
- Cash Balances
- Bank Line of Credit (BLOC)



- ✓ **BLOC - SBA counts the available balance on a BLOC as available cash flow**
- ✓ Get to know a banker before you need credit



Maximize Your Surety Credit

- Find an agent & be thorough in the information provided
- Get pre-qualified
- Retain profits and build up these important balance sheet items:
 - ✓ **Working Capital**
 - ✓ Net Worth
 - ✓ Debt/Net worth
- **Prepare quality financial statements (CPA prepared is best)**
- Obtain credit with bank & suppliers
- **Document past contract performance**

Benefits of Obtaining Surety Credit

- ✓ Establish a history of successfully completing bonded jobs
- ✓ **Bonded businesses are favorably viewed by agents and obligees**
- ✓ Access new revenue streams through bonded jobs - many GCs and other Obligees work only with bonded businesses
- ✓ **Opportunity to grow as a prime contractor**



SBA Surety Bond Guarantee Program

Mission - Provide surety bond guarantee assistance for new and existing small businesses by partnering with Surety companies and their Agents.

- **SBA guarantee allows small businesses to obtain contract specific bid, performance and payment bonds not available elsewhere**
- SBA's guarantee strengthens a small business's ability to compete in the construction market and secure bonded work
- **Commonly requested bonds that are not eligible for an SBA guarantee: License Bonds, Subdivision Bonds, Financial Guarantee Bonds (except Timber Sales)**



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SBA has been assisting small and emerging businesses obtain surety bonds since 1972. SBA can help many small businesses including:

- **Start-ups and firms in business less than 3 years**
- Firms with limited financial resources (cash, working capital, net worth)
- **Firms with recent losses**
- Firms with limited track record in prior completed job size
- **Firms with no prior public works/bonded work experience**
- Firms wishing to increase current bond limits
- **Firms with some credit issues**

SBA Surety Bond Guarantees

SBA provides the Surety a guarantee of 80% or 90%, reducing the Surety's liability for each bond, allowing the Surety to issue bonds to businesses that would not otherwise qualify.

Prior Approval Program

- **90% Guarantee:**
 - ✓ All veteran owned & service disabled firms
 - ✓ Minority owned businesses
 - ✓ 8(a) and certified HubZone businesses
- **80% Guarantee:**
 - ✓ All other small businesses

Business Size Eligibility

NAICS (North American Industry Classification) Codes:

- **Business (including affiliates and subsidiaries) must be small for the primary industry it and the affiliates are engaged in based on average annual revenues for the last three fiscal years**
- Construction Firms –
 - **\$ 19 million** for specialty trades such as:
 - ✓ electrical (238210) or roofing (238160)
 - **\$ 45 million** for heavy construction such as:
 - ✓ commercial construction (236220) or highway, street and bridge (237310)
- Service, supply and manufacturing firms may also be eligible
- www.sba.gov Search NAICS to locate Size Standard

Contract and Bond Eligibility

- Maximum Contract Size: \$6.5 million
 - ✓ Up to \$10 million on Federal contracts with contracting officer certification
- The small business and its owners must:
 - ✓ Certify they need a bond and are unable to obtain it elsewhere with reasonable terms
 - ✓ Not be barred from doing business with the Federal Government
 - ✓ Not be on probation or parole or in bankruptcy
- Bid, performance and payment bonds must be required by the contract¹⁷



Bond Application Package

Agent may request:

- Contractor Questionnaire
- Owner's personal financial statements
- Company financial statements (3 years + current)
 - CPA prepared not required for jobs \$500,000 or less
- Bank relationship information
- Work on hand schedule
- Job references
- Principal's resumes
- General Indemnity Agreement

SBA Forms:

- **SBA Form 994** - Application for Surety Bond Guarantee Assistance
- **SBA Form 912** - Statement of Personal History



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Fees for SBA Bond Guarantees

- **Bid Bonds:** No SBA fee
- **Performance and Payment Bonds:**
 - ✓ SBA Guarantee Fee: .6 % of the Contract Amount
 - ✓ Surety's Bond Premium: 1 to 3% of the Contract Amount

Include these costs in bid estimates and first pay requests to ensure reimbursement by the Obligee

Fastrack for Jobs Up to \$500,000

- **FAST Approval – personal credit based program**
- All Types of Work Except Environmental Risks & Timber Sales
- **Maintenance Terms Up to One Year but will allow renewable contracts**
- **Relaxed SBA Underwriting – No Credit Scoring**
- Apply Prior to Start of Work
- No Previous Defaults, Claims or Complaints
- **Eliminates WIP, Financial Statements & Other SBA Forms**

Costs of Bonding Example

An 8(a) contractor received an SBA guaranteed bid bond and was subsequently awarded a \$500,000 Federal contract to install new energy efficient windows in three buildings at an airbase.

Example of Contractor's Bond Costs:

\$ 9,000	1.8 % Surety's Bond Premium ($\$500,000 \times 1.8\%$)
<u>3,000</u>	.6% SBA's Guarantee Fee ($\$500,000 \times .729\%$)
<u>\$12,000</u>	Total Cost for Bonds

Application Process

1. Small business contacts SBA approved bond Agent requesting assistance
2. **Agent evaluates credit, character and capacity and obtains Surety approval**
3. Agent applies for a bond guarantee to SBA electronically
4. **SBG Area Office reviews & approves qualified applications within 4 days – currently less than 2 days on average**
5. Agent provides bond to the small business

Note: A Surety may bond a business with or without an SBA guarantee or decline to bond the business if they do not qualify.

Common Reasons SBA is Unable to Provide a Bond Guarantee

- **Inadequate working capital**
- Principal not a small business under SBA regulations
- **Project size exceeds OSG limit**
- Ineligible bond type

Locating an SBA Approved Bond Agent

- Use SBA's list of Bonding Agencies by State available at: www.sba.gov/osg
- Contact an SBG Area Office for a referral
- Ask your current agent if they participate in SBA's Surety Bond Guarantee Program

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