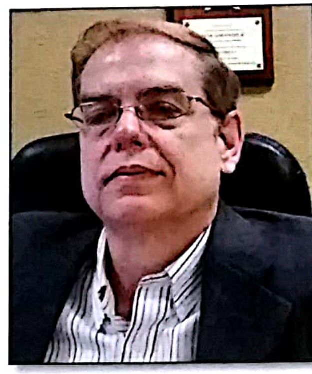
The SBA Bond Program
Help for Small & Emerging Contractors



The Soft Bond Market — Contractors who work for public owners are required to provide surety bonds. These bonds guarantee the work is performed as per the contract (Performance Bond) and all the subcontractors and suppliers are paid (Payment Bond). The current construction boom has resulted in an abundance of surety capacity. There are a lot of bond companies in the surety arena these days. As these companies compete more aggressively for business, underwriting requirements have become looser. The current surety market has become the "softest" we've seen in at least 15 years.

Jim Swindle is the owner and principal agent of Alamo Surety Bonds, a professional surety agency in San Antonio. Mr Swindle has been in the surety bond business for 29 years, both as a surety underwriter and agent. He gives presentations on contract surety bonds for construction trade associations, large general contractors, and governmental entities.

This new soft market has not yet, however, reached its way down to the small and emerging contractor segment of the industry. Bonding can still be a significant barrier for small contractors who often find bonding difficult or impossible. Fortunately, there are sureties and programs that cater to small and emerging contractors seeking their first bond or increasing their existing bond capacity. The Small Business Administration (SBA) has a program that guarantees up to 90% of a bond issued in the program. The SBA provides this backstop in exchange for a relatively small fee to the contractor - 0.729% of the contract amount. The SBA Fee is in addition to the bond company's premium charge, however, most sureties offer special SBA rates to adjust for the extra cost of the SBA Fee. The surety underwriter, in turn, is able to offer a more aggressive bonding line than would be possible without this SBA support.

Who Qualifies?

To be eligible for the SBA Bond Guarantee Program, contractors must meet the SBA's standards for qualification as a small business. A general contractor cannot have annual revenues larger than $36.5 million. Trade contractors cannot have more than $15 million in annual revenues. The SBA can guarantee single bonds up to $6.5 million, and up to $10 million on certain federal government projects.

How Does It Work?

To apply for bonding in the SBA Program, a contractor must go through an SBA-authorized surety agent who can place the bond with an SBA-authorized surety company. Even within the SBA Bond Program, a contractor must meet certain credit, experience, and financial capacity standards to qualify for bonding. The surety underwriter will require the same basic underwriting information. If the underwriter decides the contractor qualifies for bonds, but does not quite meet their standard underwriting guidelines, the surety may offer surety support in the SBA Bond Program. The SBA Bond Program can be a godsend to a bondable contractor because their underwriting requirements are considerably easier to satisfy than those found within the standard surety marketplace.

Response Time

It is true that in the past, the SBA's response time was not always very fast – at least in comparison to the turnaround times outside the program. This was largely due to the paper-intense process that had developed over the years. The same information was required on multiple forms that all required original signatures. Understandably, the SBA was often slow to respond under the weight of a cumbersome and outdated system.

Today's SBA has caught up with the times and has firmly embraced the digital age. The SBA-required forms have been consolidated down to a total of just two – the 994 (Application for Surety Guarantee) and the 912 (Personal History Sheet) - for the initial setup, and only one form (the 994) for each new bond request. The SBA Quick-Bond Program provides bonds for contractors with decent credit up to $250,000 – with no financial statements required. All the SBA forms are now available electronically through the SBA's website and can be submitted to the SBA-authorized surety agent via email.

The SBA also created the "e-App System," which is an internet-based bond submission and approval program. Agents and sureties in the SBA Bond Program use the system to upload underwriting information and the SBA forms instantly. The e-App System has increased efficiency, resulting in a very nimble and responsive process. The typical SBA response time for approval on a new account is 3 to 5 business days. For bid bond requests, the SBA usually responds within 24 hours and is even able to respond the same day if necessary. This is as good as, if not better than, the turnaround times available in the open bond market.

Benefits of the SBA Bond Program

In the SBA Program, a contractor without CPA-prepared financial statements can be approved for single bonds up to as high as $1 million. Many small and emerging contractors struggle with the issue of quality financial statement preparation. Obtaining a CPA Review for the first time from a construction-oriented CPA takes considerable time and can be somewhat expensive. It may even be cost-prohibitive unless the contractor will need several bonds per year to spread out the expense over the course of several jobs. With the SBA Program, the contractor can do significant bonded work while they seek out and form a relationship with a qualified CPA at the same time.

But perhaps the most important benefit of the SBA Bond Program is that it allows available limits on bank lines of credit as additional working capital. If a contractor has established a line of credit from an FDIC-insured bank, the amount available for use is added directly to the existing working capital shown on the contractor's balance sheet. In addition, the SBA's minimum working capital-to-backlog requirement is significantly lower than it is outside of the SBA Bond Program.

By taking advantage of the SBA Bond Program, a small contractor who may have once had only a modest ability to bond, can exponentially increase their surety capacity. This enables the small and emerging contractor to take their business to the next level of growth – and in a relatively short period of time. The resulting increase in local contractor participation on public works projects creates a boon to the local economy as more of those construction dollars stay within the community.

Most small and emerging contractors have tremendous growth potential, but can be held back by the inability to maintain adequate bond capacity. The SBA Bond Program encourages surety companies to provide significant bond capacity for these small contractors who otherwise would not qualify. The ultimate goal of the SBA Program is to give worthy and capable small contractors the chance to develop into large, successful prime contractors.