BONDING PRIVATE PROJECTS OPENS DOORS

CONTRACTORS CAN ACQUIRE MORE WORK, GENERATE MORE REVENUE

BY MARC RAMSEY

More and more contractors realize the benefits of obtaining surety bonds on private projects. In addition to building contractors' credibility and confirming their ability to perform the job, bonding provides a competitive edge and enhances their ability to acquire work.

"The surety's prequalification of the contractor validates its experiential and financial soundness and enhances its ability to bid private and public work," says Dennis Perler, president, Liberty Mutual Surety.

Doug Hinkle, chief underwriting officer, CNA Surety, adds, "The ability to bond is independent validation of the contractor's capabilities and is viewed favorably by banks as lending partners and private owners as potential customers. Bonding involves a prequalification process that, upon bond issuance, tacitly declares the contractor has the ability to complete the work in accordance with the given plans and specifications."

So, what are the advantages to contractors?

- **Qualifications**—In today's bonding market, the value of prequalification is high. Not all contractors qualify for bonds. The fact that a contractor has a relationship and bonding capacity with a surety company is a strong indication of its qualifications.
- **Relationships**—The contractor should use the relationship with a surety bond producer and underwriter to the company's advantage. Contractors should view bonding capacity as a special type of credit. Just as contractors use bank lines of credit to finance an expansion of the business, a surety bond assists the contractor in generating new business by opening doors to new project opportunities. The contractor should hold out its bonding capacity as a "seal of approval" to encourage project owners to enter into relationships.
- **Credibility with owners**—Bonding builds a level of credibility with the project owner by giving the owner greater certainty and comfort in the contractor's ability.
- **Self-confidence**—A bond demonstrates the contractor is confident enough in its ability to secure its performance. The contractor also is making a sound risk-management recommendation to the owner, indicating that the contractor has a high interest in protecting the owner.
- **Financial strength**—During the prequalification process, the contractor's financial strength and ability to support a viable business are assessed. This includes an analysis of corporate financial statements, personal financial statements of construction company owners and work-in-process schedules.
- **Experience**—The contractor's resources, expertise and experience also are assessed

during the prequalification process. This involves a review of the contractor's largest jobs completed and its organizational chart with the résumés of key personnel.

- **Character**—A contractor's character also is analyzed by checking references and credit reports.

While most contractors equate bonding with public contracts, bonds are just as essential in private construction as a risk-management tool.

"Contractors should view surety as a marketing tool," says Henry Nozko Jr., president, ACSTAR Insurance Co. "Once you have a surety bond, it provides you with a clear, distinctive advantage over your competition that may not have a bond. Small contractors can bid to larger contractors that require all of their subcontractors to be bonded."

"Sureties," Nozko continues, "provide contractors the prequalification that will get them into doors they otherwise would not get into without a bond."

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Benefits of Surety Bonding

1] Provides contractors with a competitive advantage.

2] Validates a contractor's financial strength, capabilities and qualifications.

3] Provides contractors with value-added services.

4] Generates new business opportunities.

5] Builds credibility and trust with project owners.

CONTRACT SURETY BONDS OR BANK LETTERS OF CREDIT?

This chart highlights the differences between surety bonds and bank letters of credit.

By Marla McIntyre

CONTRACT SURETY BOND	BANK LETTER OF CREDIT
Definitions	
• A three-party agreement where the surety assures the obligee (the project owner) that the principal (the contractor) is capable of performing the contract in accordance with the contract documents.	• A cash guarantee to the owner. The owner can call on the letter of credit on demand. The letter of credit then converts to a payment to the owner and an interest-bearing loan for the contractor.
Prequalification	
• Capital • Capacity • Character	• Quality and liquidity of collateral
Borrowing Capacity	
• Often issued on an unsecured basis • No direct effect on bank line of credit • Credit enhancement	• Assets used as collateral • Diminish existing line of credit • Can affect cash flow
Duration	
• Duration of contract • Maintenance period	• Date specific—usually one year • Evergreen clauses for renewal
How to Obtain	
• Issued through surety bond producers	• Issued through banking or lending institution
Cost	
• –2 percent of contract price • Includes performance and payment bond and warranty period • Included in bid price	• Generally 1 percent of specified percentage of contract amount • Included in bid price
Coverage	
• Performance bond in 100 percent of contract amount • Payment bond in 100 percent of contract amount	• Typically 5 percent to 10 percent of contract amount • No protection for unpaid subcontractors
Claims	
• Surety investigates claim of default • Surety pays rightful claims of certain parties (payment bond)	• Payable upon demand • Owner determines validity of claims by subcontractors and suppliers

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