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A nighttime photograph of a city skyline reflected in water. A bridge with blue lights is in the foreground. The skyline features several tall buildings, some with illuminated tops. The sky is dark with some clouds.

BONDING DEMYSTIFIED

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From Basic to Beyond

BASIC BOND 101

- **What is a Surety Bond?** “Cosigner for Hire”
- ***Parties to a Bond include:***
 - The “Principal”, the party required to provide the bond
 - The “Obligee”, who the bond is in favor of (usually an Owner, GC or Govt Agency)
 - The “Surety”, the company guaranteeing the obligation under the bond per the contract
- ***Types of Bonds:***
 - Contract:** Includes Bid, Performance and Payment, Maintenance and Supply
 - Commercial Bonds:** Non-Construction contract, license and permit, court, janitorial, healthcare and so many more!
- ***Benefits of having a bond include transfer of risk, guarantee of contract performance, 3rd party verification of Contractor capability, protects tax payer dollars on government projects.***

NAVIGATING THE UNDERWRITING PROCESS

The 3 C's of Surety

“Capital, Capability, Character”

Financial Strength

Experience in the scope of contracted obligation

Credit Rating of Indemnitors

History of Paying Suppliers and Subs

Established Bank Relationship and Line of Credit

Experience of Key People

Financial Statement Quality

Bond Limits

Based on underwriting criteria such as:

- ▶ Largest job completed
- ▶ Available working capital
- ▶ Surety Treasury Limits
- ▶ Financial Statement Quality
*based on current market trends
 1. Internal statements (\$2MM)
 2. CPA Compiled Statement (\$4MM)
 3. CPA Reviewed Statement for bonds over \$2MM (Most bonding programs are provided at this level)
 4. CPA Audited Statements for bonds and programs that exceed \$25 Million

Bond Costs

Costs range depending on type of bond and underwriting criteria

- ▶ Bid Bonds – No Charge (in standard bonding program)
- ▶ Performance and Payment Bonds – 1-5% of contract price*
- ▶ Commercial and Misc. Bonds – generally 1-3% of bond penalty amount

Other factors that could influence overall cost is use of additional tools such as collateral, funds dispersal (fka Funds Control) and SBA Bonding Program. These apply to non-standard bonding programs

WHERE DO I START?

Gather your “A” Team

- Banker
- Obtain CPA specializing in your industry that understands surety
- Retain Attorney specializing in your industry
- Insurance Agent
- **Professional Bond Agent**

Plan to Fail

- Consult CPA BEFORE fiscal year end and obtain “Percentage of Completion” basis statement either on “Review” or “Audited” (depending on your needs, keep in mind a “3-year tail”)
- Have your attorney review contracts PRIOR to signing
- Obtain your bank lines of credit when you DON'T need them for as high as you can qualify.

Get Sophisticated

- Obtain an integrated accounting and job costing system
- Knowledgeable bookkeeper/CFO
- Maintain high quality, quarterly interims and job schedules
- Maintain a system for collecting receivables on a timely basis

THINK OF THE 3 “C”S OF SURETY!

Capital
Character
Capability

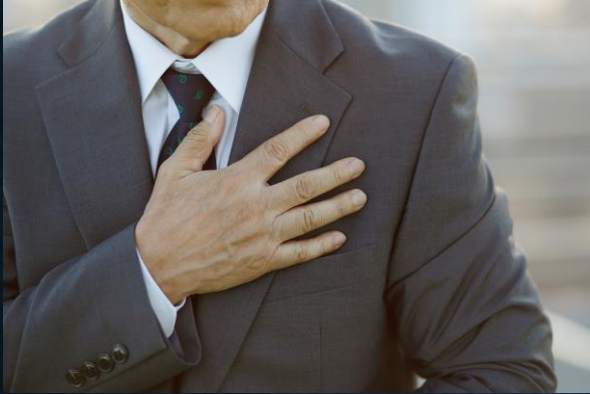
The background of the entire slide is a dense, overlapping collage of US dollar bills. The bills are shown in various orientations, some as individual notes and others as thick stacks, creating a sense of abundance and wealth. The colors of the bills (green, blue, and yellow) are visible throughout the background.

CAPITAL

“CASH IS KING”

WORKING CAPITAL = CURRENT ASSETS – CURRENT LIABILITIES

- **Maximize cash**
- **Bill and Collect Accounts Receivables**
- **Analyze Inventory**
- **Avoid inter-company transactions**
- **Avoid loans to shareholders/employees**
- **Reduce bank debt**
- **Build Corporate Net Worth**
- **Maintain available bank credit**
- **Finance necessary equipment purchases***
- **Reduce bonuses and overhead if profits decline**
- **Try to limit annual distributions if possible**
- **Don't buy the boat or plane unless it is pertinent to the function of your business**



CHARACTER

“Nobody likes surprises”

- Maintain your good credit and reputation (not just corporate)
- Get letters of recommendation
- Meet the surety underwriter
- Share your reasonable business plan
- Provide regular updates and communicate problems quickly
- Communicate with your CPA prior to making large purchases that could affect your balance sheet
- Communicate with your “A” team about any changes in ownership or continuity BEFORE it happens (Succession planning)
- Communicate in advance if there are any upcoming projects that are beyond normal scope and size BEFORE you sign the contract
- Be upfront with your surety agent about any credit issues, remember they are on your team!

CAPABILITY

Build your “Winning” track record

- Obtain References and CPARS
- Maintain equipment schedules/appraisals
- Pictures! Proposals! Resumes!
- Job schedules (current and past)
- Job site visits with your “A” Team
- Have a succession plan (No one is immortal except Elvis)
- Job cost breakdown/favorable contract terms



Roadblocks to Success

You are what you do, not what you say you'll do

DON'T

- Ineffective financial management system
- Maxed Bank lines of credit
- Poor estimating/job costing
- No business plan
- Lack of communication
- Litigation/Notice of Non-Payments/Tax Liens
- Uncontrolled growth
- Venturing into unknown territory or scopes of work
- Signing contracts without reading or negotiating terms in advance – Be Sure to watch for onerous language!

DO

- Communicate openly with your agent
- Remember there are two parties to the contract, negotiate fair terms for both parties
- Watch out for extended warranty provisions – the surety will only bond between 1- 3 years, must be written in contract.
- Watch out for high liquidated damages! Sureties generally prefer no more than \$2500 per day or a percentage cap of the contract price. (max of 25%)
- Look for “Consequential Damages” they are a surety killer!
- Look for reasonable response times in your contracts
- Check your bonds for accuracy prior to sending to client, especially a contracting officer

Questions?

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