

# Protect Your Construction Lending Capital With a Surety Bond

## CONTRACT SURETY BONDS—

### INVESTMENT PROTECTION FOR TODAY'S LENDER

Construction surety bonding generally is a three party agreement which holds a contractor to the terms and conditions of the owner's contract. There are three types of contract surety bonds:

- The **bid bond** provides financial assurance that the bid has been submitted in good faith and that the contractor intends to enter into the contract at the price bid and provide the required performance and payment bonds.
- The **performance bond** protects the owner from financial loss should the contractor fail to perform the contract in accordance with its terms and conditions.
- The **payment bond** guarantees that the contractor will pay certain subcontractors, laborers, and material suppliers associated with the project.

For years, surety bonds have been mandated by law for federal public construction projects (\$100,000 or greater) under the Miller Act of 1935. Many state and local governments also require surety bonds on their public construction projects with "Little Miller Acts." Surety bonds also have been used voluntarily for many private projects as well. Moreover, an increasing number of construction financiers are now recognizing the wisdom of requiring contract surety bonds to protect loans secured by private sector projects.

### SURETY BONDS PROVIDE BENEFITS FOR ALL CONCERNED

Basically, surety bonds protect a project owner by guaranteeing the contractor's performance and payment for labor and materials. When a contractor provides a surety bond, you can be assured that he/she has met the surety company's rigorous prequalification standards. Indirectly, construction lenders are also assured that the project will proceed according to the terms of the contract. Thus, the parties are required to fulfill their financial and performance responsibilities—with protection from events which might inhibit project completion or cause financial loss.



***Construction is a risky business and the need to protect private owner investment capital remains. More than 80,000 contractors failed during 1990-1997, leaving a trail of unfinished private and public construction projects with liabilities of \$21.8 billion.***

*SOURCE: 1997 Business Failure Record-Dun & Bradstreet*

## THE SURETY'S ROLE IN PROJECT COMPLETION

When claims occur, the borrower's rights are protected, in turn, protecting the lender. The surety is prepared to provide assistance when necessary. Knowledgeable claims representatives are trained to facilitate completion of a project. And to this end, the surety may, among other things:

- provide personnel trained to consult and solve problems;
- arrange to bring in a completion contractor;
- provide for payment of subcontractors and suppliers to keep the job moving forward; and
- arrange financial assistance for the contractor.

When advised of problems in time, the surety can take steps to set a project back on course. However, should contractor default occur, settlement is made as fairly and quickly as possible. The goal is, of course, to see any project through to completion with the minimum amount of time and money lost. For you, the construction lender, contract surety bonds assure that your financial investment is protected by guaranteeing that the construction project will be done in accordance with the contract terms.

*For more information about contract surety bonds contact:*



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*The information source on contract surety bonds. SIO is supported by SAA and NASBP.*



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*SAA is a voluntary, non-profit, unincorporated association of companies engaged in the business of suretyship. It presently has approximately 600 member surety companies, which collectively underwrite the overwhelming majority of surety and fidelity bonds in the US, and 7 foreign affiliates. SAA is licensed as a rating or advisory organization in all states, DC, and Puerto Rico, and has been designated by all state insurance departments except Texas as a statistical agent for the reporting of fidelity and surety experience.*



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