



**National Association of  
Surety Bond Producers (NASBP)**  
1828 L Street, NW, Suite 720  
Washington, DC 20036



**The Surety & Fidelity  
Association of America (SFAA)**  
1101 Connecticut Ave., NW, Suite 800  
Washington, DC 20036

## **Revitalizing the SBA Bond Guarantee Program**

The SBA Bond Guarantee Program (Program) was created to ensure that small and emerging contractors have the opportunity to bid on public construction work, grow their businesses and remain a viable part of the US economy. Surety bonds are a vital mechanism to protect taxpayers and workers on public construction projects from the danger of contractor default. Small businesses must have access to these bonds to obtain federal construction contracts, and the SBA program assists them in obtaining these bonds. However, over the years, the Program has become increasingly less effective. Significant reform is necessary to enhance the opportunities for small businesses.

Critical changes must be made to maximize use of the Program.

### ***Streamline the SBA Bond Program into a Unified Government Program With Enhanced Characteristics***

As the SBA Bond Guarantee Program has evolved, there are two plans under which sureties can participate in the Program. The Prior Approval Program ("Plan A") was the original SBA bond guaranty program. In this program, the surety must obtain SBA approval for each bond prior to writing the SBA guaranteed bond. The SBA indemnification of the surety's loss as a result of a bond claim in Plan A is 80%, and 90% for bonds written for socially and economically disadvantaged contractors and bonds written for contracts under \$100,000. The second program is the Preferred Surety Bond Program ("Plan B"). Under this plan, sureties apply to participate, submitting information up front on their underwriting practices and financial strength. Once a surety becomes a participant in Plan B, it is given an aggregate limit of bonds that it can write within the Program. As long as the surety complies with all of the requirements of Plan B, all bonds written within the program qualify for reimbursement of losses. The SBA does not review or approve each individual bond before it is written and the guarantee attaches and in Plan B, the surety receives a 70% indemnification.

*In order to guarantee more bonds and to provide better assistance to small and emerging contractors, the structure of the SBA Surety Bond Guarantee Program must be changed. There are several reforms necessary to achieve this:*

- Combine the SBA Prior Approval Program and the Preferred Program into one bond guarantee program, creating a unified model consistent with the Preferred Program. The SBA has done its own study of the structure and administration of its Bond Guarantee Program. The results of this study have yet to be released to public. It is our understanding that the recommendation to streamline the program will be supported by the SBA study and that the study could include vital information on how best to implement such a program.
- Require the SBA to track the contractors that participate in the program. The surety industry believes that the SBA Reauthorization Act should revitalize the SBA program so that it is attractive to sureties and agents and assists small and emerging contractors in obtaining their first bonds and graduating from the program into the traditional surety market. Although these contractors may continue to obtain some bonds through the program, there should be a common understanding between the surety industry, the SBA and Congress about what constitutes success for the program.
- Ensure that the SBA Bond Guarantee Program regulations keep pace with changes in law and practice in the construction and surety industries. Current SBA regulations, for example, require notice to the SBA of change orders exceeding a certain amount, but most construction contracts and bonds now require the surety to waive notice of such changes. Construction projects are delivered by new methods, such as design build. As another example, the SBA Bond Guarantee Program currently does not provide guarantees for design-build contracts, even where the design liability is carved out from the coverage of the bond.
- Create a system of due process in connection with the SBA Bond Guarantee Program so that sureties receive notice, a hearing and right to appeal if: 1) the SBA denies a surety's request to participate in the Program or eliminates a surety from the Program, or 2) denies a claim under a bond that the SBA has guaranteed. Such a process currently exists for the SBA loan programs but is absent for the SBA Bond Guarantee Program.
- Review the current fee structure of the Bond Program and establish reporting mechanisms concerning why fees continue to increase. The focus of the Bond Guarantee Program should be to provide increased contracting opportunities for emerging contractors and not to recoup administrative costs to fund the Program. Not ARRA
- Recognize that the SBA Bond Guarantee Program serves a useful public policy function and that it may not be self-sufficient each year. There always are competing interests in any federal budget. Congress, however, has never required the SBA Bond Guarantee Program to be self-sufficient. The Congressional declaration of policy for all the SBA programs in the Small Business Investment Act of 1958 was to stimulate and improve the economy by establishing assistance programs for small businesses, which are to be

“carried out in such a manner as to insure maximum participation of private financing sources.” (15 USC Section 661). If the purpose of the program is to help small and emerging contractors that may not otherwise qualify for bonds in the marketplace, it stands to reason that there will be losses. The most recent direction from the Office of Management and Budget (OMB) was two years ago when the OMB directed the SBA to increase its fees to cover SBA losses represent a major shift in philosophy and direction for the SBA program and are in conflict with the spirit of the law. The public policy of helping small and emerging contractors is a sound one, and it needs to be supported in the funding structure and reauthorization of the SBA. Not ARRA

***Apply the Enhancements for Loan Guarantees under ARRA to SBA Bond Guarantees and Continue other ARRA Reforms***

President Obama recently signed the SBA’s appropriations bill, which included \$125 million to continue the enhancements of increased guarantees and reduced fees for the SBA’s two largest loan programs through February 28. The enhancements were enacted in the American Recovery and Reinvestment Act (ARRA). The SBA estimates that the additional funding will support \$4.5 billion in small business lending and ensure that small business owners have the tools that they need to drive economic growth and create local jobs. Prior to the passage of ARRA, banks were reluctant to provide loans to small businesses that needed access to capital for business continuation and growth. According to an article that appeared in the *Washington Business Journal*, bankers cited reforms adopted in ARRA, such as the SBA eliminating fees on 7(a) and 504 loans and increasing the maximum government guarantee that banks loan to small business from 85% to 90%, led to an immediate nationwide increase in lending. Such reforms were not included in ARRA for the SBA Surety Bond Guarantee Program, despite the surety industry’s requests to do so. These reforms should now be implemented in a similar manner in the SBA Bond Guarantee Program to provide a similar boost to the bonding program.

*In order to increase access to bond guarantees by small and emerging contractors, the following changes should be considered:*

- Increase the SBA guarantees to sureties so that they are up to 95% of the bond amount for a period of 18 months and 90% thereafter. This should help increase greater surety company participation, similar to the response experienced in the SBA Loan Program.
- Require the Administrator to reduce or waive fees paid by contractors and sureties in the Bond Guarantee Program for 18 months, with authority to extend the time period for such actions. The construction industry currently has a higher percentage of unemployment than the country as a whole. While there may be indicators of economic improvement, there is an 18 month lag before any changes in the economy will be felt in the construction industry. The current fees to contractors may put them at a competitive disadvantage in the bidding process, which hurts them rather than helps them obtain public projects. The existing fee structure makes the program economically unattractive for many sureties and could affect the continued viability of the program.

- Make permanent the temporary changes enacted in ARRA in regard to higher contract amounts for bond guarantees.
- Make permanent the discretion given to the Administrator under ARRA to determine the Program's liabilities. A deterrent to participation in the SBA Program has been the denial of reimbursement to the surety after a claim has been made on the bond issued and guaranteed through the Program.

***A Coordinated Approach and Vision is Needed to Put all Available Federal Resources to Work for the Benefit of Small and Emerging Contractors***

“Small businesses are the backbone of the American economy,” Administrator Mills and Treasury Secretary Timothy F. Geithner wrote in their Small Business Financing Forum Report to the President. The construction industry serves as the catalyst for the emergence of many new such small businesses. Construction is a challenging and competitive business environment that demands specialized knowledge and skill sets of business owners, especially small and emerging businesses. Subsequently, it is essential that the SBA provides the necessary skills needed for these small and emerging businesses to compete and survive in the marketplace. Moreover, it is important that these businesses receive the necessary educational training on business and risk management topics so they graduate out of the SBA Bond Guarantee Program with the goal of qualifying for standard surety credit.

*In order to establish a holistic business approach model, the SBA Bond Guarantee Program should consider the following reforms:*

- Establish better internal coordination and communications between the SBA Bond Guarantee Program and other SBA small business programs, such as those relating to loan guarantees and business assistance. When a small business applies to any of the SBA programs in any of the SBA offices, a case file should be opened and communications should be opened between all SBA programs that can provide assistance to the contractor. The needs of small business should be reviewed so that it can be connected to the proper SBA program, i.e. loan, bond or other programs administered by the SBA. This should not delay any SBA program from providing the small business the specific assistance sought. If the business is a small and emerging contractor, for example, the SBA Bond Guarantee Program should proceed to provide a bond guarantee while other SBA programs review the contractor for collateral or other assistance.
- Implement the required interagency coordination. With loan and bonding programs in the SBA and DOT, and similar programs in the Department of Veterans Affairs proposed in this bill, coordination is needed among the various federal programs. H.R. 4253, enacted on February 14, 2008, provides a model for coordination. The Military Reservist and Veteran Small Business Reauthorization and Opportunity Act of 2007 requires the President to establish an interagency task force to coordinate the efforts of all federal agencies that are involved in increasing capital and business development opportunities for small business owners and service disabled veterans. The law directs the interagency

task force to coordinate administrative and regulatory activities and develop proposals relating to increasing capital access and capacity of these small business concerns through loans, surety bonding and franchising. To the best of our knowledge, this law has never been implemented.

***Education and Access to Needed Professional Services are Essential***

Congress should consider funding grants and establishing free standing educational programs to assist veteran, minority- and women-owned small businesses to improve their ability to compete in the construction industry.

*Legislation (H.R. 3771) has been introduced that amends the SBA Act to create grant and mentorship programs, which should be considered as part of the SBA Reauthorization Act. Specifically, H.R. 3771 would:*

- Provide grants up to \$15,000 to women-, minority- and veteran-owned construction firms in order to obtain funds to hire professional services such as legal, accounting and other advisers.
- Create a second grant component, which establishes a free standing educational program to provide grant funds to colleges, universities, vocational/technical schools, community colleges and business leagues or not-for-profit entities to develop and administer a small business construction executive business and risk management curriculum in conjunction with local professionals, such as accountants, attorneys, risk management experts, financial experts/bankers, surety bond producers and local professional and trade associations.