NATIONAL ASSOCIATION OF SURETY BOND PRODUCERS
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Mr. George A. Schutter
Chief Procurement Officer
441 4th Street, 700 South
Washington, D.C. 20001

Submitted via: OCPRulemaking@dc.gov.

RE: Comments to Proposed Changes to Chapter 27, Bonds, Other Security, and Insurance of Title 27 DCMR, Contracts and Procurement

Dear Mr. Schutter;

On behalf of the National Association of Surety Bond Producers (NASBP), a national trade association of firms employing professional surety bond producers licensed and conducting business in the District of Columbia, Maryland and Virginia, I am contacting you concerning the proposed changes to Chapter 27, DCMR, Contracts and Procurement. NASBP's comments will focus on Section 2703 (Performance and Payment Security) and specifically address Sections 2703.3, 2703.6 and Section 2703.12

The proposed changes in Sections 2703.3 and 2703.6 allows for the reduction of payment and performance security to 50% of the original contract amount. Requiring bonds in amounts less than 100% of the contract will not make surety credit more available nor will it reduce the amount of the bond premium. Before a surety extends surety credit, it conducts a careful and thorough underwriting analysis to assess the contractor's ability to perform the construction contract and to pay its subcontractors and suppliers. The surety reviews the character, capacity, and capital of the contractor, and provides surety credit only if the surety finds that the contactor possesses the wherewithal to fulfill its contractual obligations successfully.

Partial bonds—bonds for less than 100% of the contract amount—do not lessen the surety's underwriting scrutiny of the contactor. The surety views the contract risk as the total contract obligation, not simply the face amount of the bond. The surety also will base its bond premiums—fees charged for the bond—on rates filed with the state insurance department. These filed rates are predicated on contract amounts, not bonds amounts. In short, partial bonds neither make bonds easier to obtain nor reduce the cost of the bond premium. However, partial bonds do offer less protection coverage to the project owner, subcontractor and suppliers should the contractor default on the project. Surety bonds in 100% of the contract amount, provides invaluable protection to parties furnishing labor or materials on construction projects in assuring that they will be paid.

Section 2703.12 allows the contracting officer to accept a letter of credit (LOC) in amount equal to 10% of the portion of the contract price instead of a surety bond. In comparing and contrasting the two products, there is a significant difference between surety bonds compared to an LOC. A surety bond is a three-party agreement between the surety, the project owner, and the contractor. A LOC, on the other hand, is a cash guarantee to the owner, who can make a demand at any time.

A surety company assesses the contractor's business operations, financial wherewithal, and experience to assure the project owner that the contractor is capable of performing the contract. In comparison, banks do not prequalify contractors other than to ensure specific liquid assets to secure an LOC. Thus, a LOC can diminish the contractor's line of credit and appear on the contractor's financial statement as a liability. Subsequently the contractor's cash flow in funding initial stages of construction and retention amounts throughout a contract term can be adversely affected. The restriction of cash flow can have a significant impact on small construction businesses.

Protection is perhaps the most important distinction between a surety bond compared to a LOC. A surety bond provides 100% performance protection to the project owner in accordance with the contract amount and 100% payment protection for subcontractors and suppliers. Should the project owner declare the contractor in default, the surety investigates and addresses any improper default, through providing payment, and a replacement contractor or other means. Furthermore, the payment bond ensures that subcontractors and suppliers will be paid.

The LOC may be obtained for any percentage of the contract, but 5% to 10% is customary. Such a small amount may not be adequate to remedy the contractor's default. Moreover, there is no payment guarantee for subcontractors and suppliers.

Finally, a surety bond remains in force for the duration of the contract plus a maintenance period, and the surety is subject to the terms and conditions of the bond, the contract documents, and underlying statutes. A LOC is usually date specific, generally for one year only.

For these reasons, NASBP requests that performance and payment bonds should remain at 100% of the contract amount. We strongly posit that a surety bond, not a LOC, is the best form of security to protect DC taxpayers, subcontractors and suppliers.

Please feel free to contact at 202-686-3700 or lleclair@nasbp.org should you have any questions.

Sincerely,

Larry LeClair

Lawrence E. LeClair
Director, Government Relations