EY Report: Surety Bonding Provides Strong Economic Value and Strengthens Performance for Public and Private Construction Projects

SFAA
THE SURETY & FIDELITY ASSOCIATION OF AMERICA

Bonded project portfolios outperform non-bonded portfolios

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A comprehensive study, **The Economic Value of Surety Bonds**, finds public and private construction projects protected by surety have lower rates of contractor default, lower cost of completion in the case of default, and are finished faster than non-bonded projects. For a bonded portfolio of construction projects, the overall value of surety bonds more than covers their cost. The study, by Ernst & Young's (EY) Quantitative Economics and Statistics Group (QUEST), was recently conducted in collaboration with the Surety & Fidelity Association of America (SFAA) and is the first to fully assess the economic value surety bonding delivers.

EY's analysis quantified the benefits surety bonding generates throughout the lifecycle of a portfolio of public and private construction projects – including benefits extending beyond the financial protection surety companies provide when contractors default. As a result, EY's research found that bonded project portfolios modeled perform better than unbonded portfolios, even when considering conservative default rates.

"The report exposes the risks of unbonded construction projects, including project delays and higher costs, especially in the case of default, and shows that state and federal laws requiring surety bonds are sound. It's just good public policy," said SFAA president and CEO Lee Covington. "EY is a trusted, data-driven firm, and their analysis makes clear surety bonds deliver exceptional economic value for vital American infrastructure projects. EY's report highlights the economic value and protections surety bonds deliver for both public and private construction projects," continued Covington.

Based on a survey of public and private developers, interviews with experts on construction project defaults, and an assessment of project portfolios, the analysis identified three areas where surety bonds have a significant impact on public and private construction projects.

Lower cost of completion upon default and necessary completion expertise – Unbonded construction projects on which the contractor defaults were found to have a cost of completion 85% higher than projects protected by surety bonds. Experts on construction project defaults also unanimously indicated the surety is generally more able to provide the expertise and resources needed to promote a successful transition or re-procurement process than an owner. Over 90% of these experts reported public and private owners/developers generally do not have the expertise and resources to complete the project.

Lower rate or likelihood of default – Unbonded projects are more likely to default than bonded projects, perhaps by as much as ten times. This analysis assessed portfolio performance using a default rate of 2.5 times, 5 times, and 10 times a bonded portfolio's default rate, and generally found unbonded projects are more likely to default than bonded projects. This is in large part because unbonded projects lack the various types of support bonding provides to projects (e.g., prequalification of a contractor's expertise and financial strength, greater project oversight).

Improved or lower contractor pricing – 75% of owners/developers surveyed reported that surety bonding reduces contractor pricing. Respondents cited increased confidence in the general contractor to complete the project and pay subcontractors and payment protections for subcontractors as some of the factors that impact contractor pricing. The analysis demonstrates that any level of improved contractor pricing will only increase the cost benefits of a portfolio of bonded projects.

"This report represents the industry's most comprehensive examination of the economic benefits and protections of surety," said Principal & Co-leader, Ernst & Young (EY) Quantitative Economic and Statistics (QUEST) Group, Robert Carroll. "Based on our analysis, the multiple benefits surety delivers help manage risk and provide strong economic and performance value to construction projects," continued Carroll.

The EY report found additional benefits surety bonds bring to both public and private construction projects, including:

More appropriate prequalification and review – Prior to construction, prequalification was more likely to occur for bonded projects (96% of respondents reported that pre-qualification was performed for bonded projects as compared to 61% for non-bonded), and during construction, contractors provided more information for bonded projects – general contractors were nearly twice as likely to share more than one financial update for bonded projects as for non-bonded projects.

Higher priority placed on bonded projects and greater project oversight – Respondents reported that contractors prioritize bonded projects when experiencing financial challenges. Nearly 5 times as many respondents indicated that contractors place a higher priority on bonded projects as compared to unbonded projects when facing financial difficulty. Greater project oversight with more involvement by construction managers is likely to help prevent losses.

Greater timeliness of completion – 5 times as many public and private owners reported, bonded projects are more likely to be completed on time or ahead of schedule than non-bonded projects. And when a project does default, an unbonded project will take nearly 2 times longer to complete than a bonded project.

Necessary experience and resources when defaults occur – 100% of construction default experts surveyed/interviewed for this analysis said sureties have the expertise, tools and resources necessary to complete a project in the most cost and time-effective manner as compared to an owner who does not have the same expertise and experience as a surety.

To read the EY report and get additional information visit **www.surety.org/suretyprotects**.

The Surety & Fidelity Association of America (SFAA) is a nonprofit, nonpartisan trade association representing all segments of the surety and fidelity industry. Based in Washington, D.C., SFAA works to promote the value of surety and fidelity bonding by proactively advocating on behalf of its members and stakeholders. The association's more than 425 member companies write 98 percent of surety and fidelity bonds in the U.S. For more information visit **www.surety.org**.

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