

**SUBJECT:** Surety bond requirements for state projects

**COMMITTEE:** State Affairs — favorable, with amendment

**VOTE:** 10 ayes — Wolens, Brimer, Counts, Craddick, Danburg, Hunter, Longoria, McCall, McClendon, Merritt

0 nays

5 absent — S. Turner, Bailey, Hilbert, D. Jones, Marchant

**SENATE VOTE:** On final passage, April 26 — voice vote

**WITNESSES:** (*On House companion bill, HB 3530:*)  
For — John Avila; Robert Bass, Texas Coalition of Sureties; Derrell C. Dodson; Angela Dominguez; *Registered but did not testify:* Steven W. Dobson; Bo Gilbert, Independent Insurance Agents of Texas; Bill J. King; Tom Ragsdale; Steven Searcey; Tracy Tucker; John Ward; Audrey Williams; Francis T. Zebedeo

Against — None

On — Raymond Risk, Texas Construction Association

**BACKGROUND:** Under Government Code, sec. 2166.258, the General Services Commission (GSC) may require a contractor or subcontractor to meet part or all of the bonding or insurance requirements under a negotiated arrangement. Under sec. 2253.021, a governmental entity that makes a public work contract with a prime contractor must require the contractor, before beginning the work, to execute a performance and/or payment bond through a corporate surety.

**DIGEST:** SB 1268 would prohibit the GSC or another state agency from requiring a contractor or subcontractor for any public building or other construction contract to obtain a surety bond from any specific insurance or surety company, agent, or broker. To the extent consistent with the law, the commission or other agency could require a contractor or subcontractor to meet part or all of any other insurance requirements for the project.

For the purposes of Government Code, sec. 2253.021, the GSC would have to negotiate with a specific insurance or surety company, agent, or broker to establish a surety program for the benefit of small businesses and historically underutilized businesses (HUBs).

The bill would take effect September 1, 2001, and would apply only to a contract for a construction project made on or after that date.

**SUPPORTERS  
SAY:**

SB 1268 would prohibit the GSC or any other state agency from requiring a contractor or subcontractor to obtain a surety bond from a specific insurance or surety company, agent, or broker. A surety backs a construction contractor and acts as a silent partner in representing to an owner that the contractor is qualified to submit a responsible bid. Being qualified by the surety through the pre-qualification process means that a contractor has the experience, organization, financial resources, and fixed assets to complete the work according to the plans and specifications at the bid price and within the allotted time. The surety protects the owner from contractors who may become unable to complete a project for reasons related to their finances or performance. Sureties are especially important for public building projects since a lien cannot be placed on a public building.

A directed surety, also known as an owner-directed surety, occurs when a public agency mandates that all bidders for construction projects use a specific surety for bonding. Problems can arise when a directed surety refuses to bond a potential contractor, and the problem can be compounded when the contractor is a small business or HUB. SB 1268 would require the GSC to negotiate with a specific insurance or surety company, agent, or broker to establish a surety program for the benefit of small businesses and HUBs.

Current law allows directed sureties in Texas, although they are not known to be a practice with state projects. The federal government and 25 other states prohibit directed sureties on governmental construction projects. Directed sureties reduce competition in the surety market and thus in the construction market. SB 1268 would help ensure competition on public building and construction projects and keep costs lower.

OPPONENTS  
SAY:

The requirement in SB 1268 that GSC negotiate with a specific insurance or surety company, agent, or broker to establish a surety program for the benefit of small businesses and HUBS could be interpreted as allowing directed sureties for those entities. The bill would be more effective if it were consistent with language in the companion bill, HB 3530, which already has passed the House. That bill merely would require the GSC to structure a surety program to identify surety companies or brokers available to small businesses and HUBs for providing surety assistance.

NOTES:

The committee amendment would add to the Senate engrossed version of SB 1268 the requirement that the commission negotiate with a specific insurance or surety company, agent, or broker to establish a surety program for the benefit of small businesses and HUBs.

The House companion bill, HB 3530 by Wise, passed the House on May 10 and was referred to the Senate Business and Commerce Committee, which took no action on the bill by the May 11 Senate committee reporting deadline.