# Glossary

## GUIDE TO KEY TERMS, FINANCIAL RATIOS, AND SBA FORMS

**SMALL CONTRACTORS INITIATIVE:**
BONDING & ACCESS TO CAPITAL

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# Key Terms

**8(a) Firm:** A firm participating in the SBA business development program created to help eligible small disadvantaged businesses become independently competitive in the Federal procurement market. A firm must be 51-percent owned and controlled by a socially and economically disadvantaged individual or individuals.

**Agent:** Representative of a surety with power of attorney to issue bonds. They market and prepare applications to SBA and the surety.

**Allowed Working Capital:** Calculated from the balance sheet as follows: Cash + Accounts Receivable + 0.5 of Inventory less Current Liabilities

**Ancillary Bond:** Ensures that requirements integral to the contract, but not directly performance-related, are performed.

**Backlog:** Total Estimated Costs less Costs to Date – A schedule that identifies the total amount of uncompleted work that a contractor has on hand at any given time. Often used by bond agents and lenders.

**Bid Bond:** Bonds that provide financial assurance that the bid has been submitted in good faith, and that a contractor will enter into a contract at the amount bid and post the appropriate performance bonds. These bonds are used by owners to prequalify contractors submitting proposals on contracts.

**BLOC:** Bank line of credit – Loans not used to purchase assets or for long-term financing. BLOC is a short-term business financing option.

Bonding Capacity: Refers to the single job and aggregate total that a company has qualified for with a surety company.

**CAPLines:** A special type of 7(a) loan that provides up to $5 million to help small businesses meet their short-term and cyclical working capital needs. The loan can be used to finance seasonal working capital needs; the direct costs of certain construction, service and supply contracts, subcontracts, or purchase orders; or the direct costs associated with commercial and residential construction; or to provide general working capital via lines of credit that have specific requirements for repayment.

**Cashflow Management:** The analysis and management of the flow of funds into and out of a business. Involves tracking current cashflows and analyzing them to identify challenges to meeting expectations, and taking steps to address issues that may result in negative cashflow.

**Cashflow Projections:** A 1- to 5-year objective estimate of the cash required for smooth business operations, including income and expenses; use of loans; and sales of equipment, property, and other assets.

**CDBG:** Community Development Block Grant – A flexible program that provides resources to address a wide range of community development needs. The CDBG program provides annual grants on a formula basis to 1,209 general units of local and State governments.

**CFR:** Code of Federal Regulations.

**Clearing Float:** Delay between that deposit of a check and the availability of funds to pay expenses.

**Collateral:** A security or asset pledged for the repayment of a loss, should one occur. The most common forms of collateral in the surety industry are cash, irrevocable letters of credit, and real estate equity.

**Collateral Value:** The discounted value of a pledged asset for loan or bond purposes if it had to be liquidated. For example, Real Estate = Market Value x 0.80 less Mortgage Balance; Trucks = Depreciated Value x 0.50; CDs are valued at 100 percent.

## Construction Accounting Methods:

**Accrual Basis:** Recognizes income/revenues and expenditures as they are physically received or paid, as well as those that represent accounts receivable and payable.

**Cash Basis:** Recognizes income/revenues and expenditures only as they have been physically received or paid. Cash basis accounting is not useful in the surety underwriting process.

**Completed Contracts:** An accrual-based accounting system that only recognizes income/profit on projects that have been completed during the reporting period.

**GAAP:** Generally Accepted Accounting Principles – Include the standards, conventions, and rules that accountants follow in recording, summarizing, and preparing financial statements.

**Percentage of Completion:** An accrual-based accounting method that recognizes income/profit as it progresses during the financial reporting period (yearly).

**Contract Work Hours and Safety Standards Act (CWH&SS/CWHSS Act):** Federal law requiring Federally assisted construction contracts worth over $100,000 to pay laborers and mechanics employed in the performance of the contracts one and one-half times their basic rate of pay for all hours worked over 40 in a workweek. This act also prohibits unsanitary, hazardous, or dangerous working conditions on Federal and Federally financed and assisted construction projects.

**Copeland Anti-Kickback Act:** Prohibits a Federal building contractor or subcontractor from inducing an employee to give up any part of the compensation that he or she is entitled to under the terms of his or her employment contract.

## CPA Financial Presentations:

**Audit:** The CPA must gain and document a broad understanding of the client's business, internal controls, and accounting procedures. In addition, the CPA will make inquiries, perform analytical procedures, and test the company's accounting procedures.

**Compilation:** The most basic financial statement that a CPA prepares. The CPA arranges client-supplied information into a financial statement format and interprets the data only to determine that it is free from obvious material misstatement. A compilation does not provide the CPA's assurance of the information contained in the financial statement.

**Review:** The CPA performs inquiries and analytical procedures to determine that the financial statement is in compliance with GAAP and includes all disclosures.

**CPR:** Certified payroll report.

**Current Assets:** Cash, marketable securities, accounts receivable, and stored materials.

**Current Liabilities:** Trade credit, bank loans, and accrued short-term liabilities.

**Davis-Bacon Fair Wages Act/Davis-Bacon Act (DBA):** Establishes the requirement to pay local prevailing wages on public works projects for laborers and mechanics. It applies to "contractors and subcontractors performing on Federally funded or assisted contracts in excess of $2,000 for the construction, alteration, or repair (including painting and decorating) of public buildings or public works." Certified weekly payrolls must be submitted on form WH-347. CDGB-funded residential rehabilitation has an exemption for residential property that contains up to seven units. Labor standards provisions apply to any contract for the construction of 12 or more HOME-assisted units.

**DBRA:** Davis-Bacon and related acts.

**DOL:** Department of Labor.

**Delivery Float:** Time delay between contractor installing a component and when it is approved for payment by the architect.

**Disadvantaged or Minority Business Enterprise (MBE):** Government contracting gives preference in awarding a portion of each project to companies that qualify under an established category:

- At least one objective distinguishing feature such as race, ethnic origin, gender, physical handicap, long-term residence `in an environment isolated from the mainstream of American society, or other similar causes not common to individuals who are not socially disadvantaged.
- Personal experiences of substantial and chronic social disadvantage in American society, not in other countries.
- Negative impact on the individual's entrance into or advancement in the business world because of the stated disadvantage(s).

**E-App System:** An online surety bond application system automatically that prompts you to print, sign, and mail the required forms to your surety company or agent.

**EEOC:** Equal Employment Opportunity Commission.

**Factoring:** A type of debt finance in which a business sells its accounts receivable (i.e., construction draws) to a third party (called a factor) at a discount in order to raise cash for working capital.

**FHA:** Federal Housing Administration.

**FLSA:** Fair Labor Standards Act.

**FedBizOpps.gov:** The online site where Federal Government agencies post procurement opportunities over $25,000.

**Financial Ratios:** Used to determine the efficiency and profitability of a company and its capacity for borrowing or bonding. Using the financial statements, ratios compare one number to another. See Appendix C.

## Financial Statements:

**Balance Sheet:** Provides a company's assets, liabilities, and equity position at a particular point in time (e.g., as of December 31, 2015).

**Income Statement:** Or Profit and Loss Statement Reports; Shows the revenue/sales/income, expenses, and profits of a company over a period of time (e.g., from January 1 to December 31, 2015).

**Statement of Cashflows:** Provides details regarding a company's cashflow activities with regard to operating, investments, and financing activities over a period of time.

**Statement of Retained Earnings:** Explains the changes in a company's portion of net income undistributed by the company to its owners or shareholders.

**Funds Control:** The services of a third-party organization to oversee, collect, and disburse the monies collected on a construction project throughout its completion.

**HOME Investment Partnerships Program:** Provides formula grants to States and localities that communities use to fund a wide range of activities, including building, buying, and/or rehabilitating affordable housing for rent or homeownership or providing direct rental assistance to low-income people. It is the largest Federal block grant to State and local governments designed exclusively to create affordable housing for low-income households. HOME funds are often used in partnership with local nonprofit groups.

**HUBZone Business:** Historically Underutilized Business Zone – A small business with 35 percent of its staff living in a HUBZone. The company must also maintain a "principal office" in one of these specially designated areas.

**HUD:** Department of Housing and Urban Development.

**Image Goals:** Statements defining how you wish your firm to be perceived by your employees, partners, and customers.

**Indemnity Agreement:** Obligates the named indemnitors to protect the surety company from any loss or expense caused by the contractor's failure to fulfill its bonded obligation on the project(s) and any resultant loss under the surety bond. This gives the surety assurance that the contractor will use its talent and financial resources to resolve any difficulties that may arise in the performance of the bonded work.

**IHA:** Indian Housing Authority.

**IHBG:** Indian Housing Block Grant.

**Invoice Discounting:** Borrowing that involves the use of accounts receivable assets as collateral for the loan.

**Joint Venture:** In the SBA Mentor-Protégé Program, an agreement between a certified 8(a) firm and a mentor firm to pursue a joint venture as a small business for a Government contract.

**LINC:** Leveraging Information and Networks to Access Capital – An online referral tool to connect small business borrowers with participating SBA lenders. Prospective borrowers complete a short online questionnaire, and their responses are forwarded to participating SBA lenders.

**Local Business:** For Section 3 compliance, local is the city or county in which the project resides.

**LCA:** Local contracting agency.

**LDP:** Limited denial of participation.

**Maintenance Bond:** Guarantees that any defects in workmanship or materials will be remedied within a specified period (usually 1 to 2 years).

**Markup:** Overhead, profit, and contingency as a percentage of total job cost.

**MBE:** Minority business enterprise – See "Disadvantaged Business."

**Net Working Capital:** Current assets less current liabilities.

**Obligee:** Project owner who contracts with the principal for the performance of a contract. If the principal defaults on a project, then the obligee is made whole by the surety. The obligee (project owner) may be a private individual, a company, or a government agency.

**OSHA:** Occupational Safety and Health Administration – Part of DOL.

**Over-Billings:** Billings that exceed the actual incurred costs and earnings on the job to date; also termed "Billings in Excess of Costs and Estimated Earnings."

**O/T:** Overtime.

**Payment Bond:** Guarantees that subcontractors, labor, and material suppliers will be paid for their work.

**Performance Bond:** Guarantees that the contract will be successfully completed in accordance with the contract's terms, specifications, and requirements.

**Preferences:** Congress first enacted a procurement goal in prime contracting for small business in 1988. See Appendix B.

**Preferred Surety Bond Program:** A bonding program in which selected sureties receive a 70-percent bond guarantee and are authorized to issue, service, and monitor bonds without prior SBA prior approval.

**Principal:** Small business/contractor or its owner(s).

**Prior Approval Program:** Bond guarantee applications are submitted to SBA for prior review and approval. SBA guarantees 90 percent of the losses incurred on: (1) contracts up to $100,000 and (2) contracts awarded to the following types of businesses:

- Socially and economically disadvantaged small businesses.
- HUBZone small businesses.
- 8(a) Business Development Program small businesses.
- Veteran- or Service-Disabled Veteran-Owned small businesses.

The SBA offers an 80-percent guarantee on bonds for all other individual contracts up to $6.5 million, or up to $10 million if a Federal contracting officer certifies that the SBA's guarantee is necessary for the small business to get a bond.

**Processing Float:** Delay between approval to draw payment and its receipt in the general contractor's or subcontractor's account.

**PHA:** Public housing agency.

**Risk Mitigation:** Process, products, services, timing, and tools that increase the probability of achieving a business objective—including team selection, design and specification, performance guarantees, production maintenance, and change order management—which serve to increase the probability of completing a project per spec, on time, and under budget.

**SAC:** State Apprenticeship Council/Agency.

**SAM:** System for Award Management – Database located at www.sam.gov. All current and potential Government vendors are required to register in this database to be eligible for contract awards and payments.

**SBA Small Business Forms:** See Appendix D.

**Section 3:** Provision of Housing and Urban Development Act of 1968 that helps foster local economic development, neighborhood economic improvement, and individual self-sufficiency by promoting and rewarding firms that hire lower-income and local employees.

**Sensitivity Analysis:** The formal name of "What if?" or plan B analysis. Sensitivity analysis answers the business planning question, "If these variables deviate from expectations, what will the effect on the business be?"

**Service-Disabled Veteran-Owned Small Business:** A small business that is at least 51-percent owned by one or more service-disabled veterans. The service-disabled veteran (SDV) must have a service-connected disability, as determined by the Department of Veterans Affairs or Department of Defense.

**Set-Asides:** Various Federal, State, and local funding programs require that a portion of their funding be set aside for disadvantaged and/or local contractors. Federal Government purchases that have an anticipated dollar value exceeding $3,000, but not over $150,000, are automatically reserved or set-aside for small businesses.

**Small Business:** SBA loan programs and contracting opportunities are reserved for small business concerns.

**SBIC:** Small business investment companies – Privately owned and managed investment funds, licensed and regulated by SBA, that use their own capital plus funds borrowed with an SBA guarantee to make equity and debt investments in qualifying small businesses.

**S/T:** Straight-time.

**Surety:** Corporate entity legally responsible for paying claims after a principal has defaulted; SBA's program partner.

**Surety bonds:** Three-party agreements in which the issuer of the bond (the surety) joins with the second party (the principal) to provide protection to a third party (the obligee) regarding the fulfillment of an obligation on the part of the principal. An obligee is the party (person, corporation, or government agency) to whom a bond is given. The obligee is also the party protected by the bond against loss.

**TDHE:** Tribally designated housing entity.

**UPCS:** Uniform Physical Conditions Standards – An inspection protocol developed by HUD to certify that residents live in decent, safe, and sanitary housing. The UPCS has become a minimum construction standard in multifamily and other subsidized properties.

**WH-347:** This form or a similar one must be used by contractors to submit certified weekly payrolls for contracts subject to the Davis-Bacon Act.

**WOSB:** Women-Owned Small Business – A small business that is at least 51-percent directly and unconditionally owned and controlled by one or more women who are citizens (born or naturalized) of the United States. An Economically Disadvantaged Women-Owned Small Business (EDWOSB) is a small business that is 51-percent owned by one or more economically disadvantaged women who also manage the daily business operations of the concern.

**Working Capital:** The cash available for day-to-day business operations. This is a commonly used measure of liquidity and short-term financial health.

**Work-in-Progress Schedule:** A surety and lender underwriting tool to track the progress and financial performance of a contractor's uncompleted projects.

# Preference Goals

| Program | Prime | Subcontracting | Statutory Reference |
|---|---|---|---|
| Small Business | 23 | | Public Law 95-507 § 221 (1978) and 105-135 § 603(b) (1997; increase to 23%) |
| Small Disadvantaged Business | 5 | 5 | Public Law 100-656 § 502 (1988) |
| Women-Owned Small Business | 5 | 5 | Public Law 103-355 § 7106(a) (1994) |
| HUBZone Business | 3* | | Public Law 105-135 § 603(b) (1997) |
| Service-Disabled Veteran-Owned Small Business | 3 | 3 | Public Law 106-50 § 502(b) (1999) |

# Financial Ratios

| LIQUIDITY | | |
|---|---|---|
| **Ratios** | **Calculation** | **Generally Accepted Comfort Range** |
| Number of Days of Cash | Cash + Equivalent x 360 / Annual Revenue | 7 days or more |
| Accounts Receivable Turnover | Accounts Receivable x 360 / Revenue | 45 days or less (excluding retentions) |
| Accounts Payable Turnover | Accounts Payable x 360 / Cost of Earned Revenue | 45 days or less (excluding retentions) |
| Current Ratio | Current Assets / Current Liabilities | Greater than 1.2 |
| This ratio is an indication of a firm's ability to handle its current liabilities. The higher ratio shows a numerical superiority of current assets over current liabilities. However, the composition and quality of current assets is a critical factor in the analysis of liquidity. | | |
| Working Capital to Backlog | Working Capital / Cost-to-Complete backlog | 5% to 10% or greater |
| Quick or Acid Test | Cash & Receivables / Current Liabilities | Greater than 1.1 |
| Any value of less than 1 to 1 implies dependency on inventory or other current assets to liquidate short-term debt. | | |

# Financial Ratios continued

| NET WORTH | | |
|---|---|---|
| **Ratios** | **Calculation** | **Generally Accepted Comfort Range** |
| Debt to Net Worth | $\frac{\text{Total Debt}}{\text{Net Worth}}$ | 2.1 to 3.1 |
| This ratio expresses the relationship between capital contributed by creditors and that contributed by owners. The higher the ratio, the greater the risk assumed by creditors. A low debt-to-net-worth ratio usually implies greater flexibility to borrow; a more highly leveraged company has a more limited debt capacity. | | |
| Fixed Assets to Net Worth | $\frac{\text{Fixed Assets}}{\text{Net Worth}}$ | 10% to 40 % |
| This ratio measures the extent to which the owner's equity (capital) has been invested in plant and equipment (fixed assets). A lower ratio indicates a smaller investment in fixed assets in relation to net worth and a better position for creditors in case of liquidation. | | |
| Net Worth to Backlog | $\frac{\text{Net Worth}}{\text{Cost-to-Complete Backlog}}$ | 5% to 10% or greater |
| Sales to Net Worth | $\frac{\text{Annual Revenue}}{\text{Net Worth}}$ | Should not exceed 13 times net worth; Could indicate overtrading capital resources. |

| PROFITABILITY | | |
|---|---|---|
| **Ratios** | **Calculation** | **Generally Accepted Comfort Range** |
| Gross Profits to Sales | $\frac{\text{Gross Profits}}{\text{Annual Revenue}}$ | 5% to 10% |
| Overhead to Sales | $\frac{\text{General \& Administrative Expenses}}{\text{Annual Revenue}}$ | 5% to 10% |
| Overhead to Net Worth | $\frac{\text{General \& Administrative Expenses}}{\text{Net Worth}}$ | 60% or less |
| Net Profit Before Taxes to Sales | $\frac{\text{Net Profit Before Taxes}}{\text{Annual Revenue}}$ | 2% or more |
| Return on Equity | $\frac{\text{Net Profit of Prior Year}}{\text{Net Worth of Prior Year}}$ | 15% or less |
| This ratio shows the rate of return on capital. While it can serve as an indicator of management performance, it should be used in conjunction with other ratios. A high return, usually associated with effective management, could indicate an undercapitalized firm. A low return, usually an indicator of inefficient management performance, could reflect a highly capitalized, conservatively operated business. | | |

# Small Business Administration Forms

**SBA Form 413 – Personal Financial Statement:**

https://www.sba.gov/document/sba-form-413-7-a-504-sbg-personal-financial-statement

**SBA Form 912 – Statement of Personal History:**

https://www.sba.gov/document/sba-form-912-statement-personal-history

**SBA Form 991 – Surety Bond Guarantee Addendum:**

https://www.sba.gov/document/sba-form-991-surety-bond-guarantee-agreement-addendum

**SBA Form 994 – Application for Surety Bond Guarantee Assistance:**

https://www.sba.gov/document/sba-form-994-application-surety-bond-guarantee-assistance

**SBA Form 994F – Schedule of Work in Process:**

https://www.sba.gov/document/sba-form-994f-schedule-work-in-process

**SBA Form 990A – Quick Bond Guarantee Application and Agreement:**

https://www.sba.gov/document/sba-form-990a-quick-bond-guarantee-application-agreement