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MEMORANDUM

TO: RPPTL Construction Law Committee

FROM: Ty G. Thompson
Surety & Insurance Subcommittee

DATE: September 12, 2011

RE: Case Law Update

Conditions Precedent

In *Stonington Water Street Assoc., LLC v. Hodess Building Co., Inc.*, 2011 WL 861688 (D. Conn. March 9, 2011) the owner of a Connecticut condominium project sued its contractor and the contractor's surety due to significant delays and the contractor's inability to complete the project and pay its subcontractors. The construction contract was the AIA A121 form with the incorporated AIA A201 general conditions. The performance bond was the industry-standard, AIA A312 performance bond.

In early 2005, the surety, owner, and contractor met to discuss the contractor's deteriorating financial condition. However, the contractor continued to perform work on the project. In 2006, the owner sent a letter to the surety notifying it that it was considering declaring a contractor default and requested a meeting in accordance with paragraph 3.1 of the performance bond. At the meeting, the contractor informed the owner and surety that it did not have the funds to complete the project. Notwithstanding the owner's recognition that it needed to terminate the contractor, and over the surety's advice, the owner decided to not declare a contractor default opted to keep the contractor on the project.

Seven months after the 3.1 meeting (and four months after the contractor ceased its involvement on the project), the owner notified the surety that it was terminating the contractor's right to complete the contract and was declaring a contractor default under

paragraph 3.2 of the performance bond. The surety responded to the owner's notice of default and termination, denying liability primarily due to the owner's failure to comply with the performance bond's conditions precedent.

The surety moved for summary judgment, arguing, among other things, that the owner materially breached the terms of the performance bond by failing to comply with paragraphs 3.2 and 3.3, and that the owner's hiring of a replacement contractor to complete the contract eviscerated one of the surety's completion options under the performance bond.

The court granted summary judgment in the surety's favor. In doing so, the court concluded that the performance bond establishes mandatory conditions precedent in order to trigger the surety's obligations to perform. Because the owner failed to terminate the contractor when reason arose, failed to properly effect the termination under section 14.2.2 of the general conditions, hired successor contractors without the surety's consent, and disbursed the entire contract balance without the surety's consent.

Pitfalls of Representing a Surety and Principal

In *Carles Construction, Inc. v. Travelers Casualty & Surety Co.*, 2011 WL 3651110 (S.D. Fla. August 19, 2011), the court granted the surety's motion and disqualified the attorney and her firm. The court reasoned that because the surety and the plaintiffs' attorney had an attorney-client relationship in several substantially related matters, an irrefutable presumption attached that confidential and privileged information was exchanged. This required the disqualification of the plaintiffs' counsel under Rule 4-1.9 and the entire firm under Rule 4-1.10.

Sufficiency of Allegations re Federal Question Jurisdiction

In *Scarborough v. Carotex Construction, Inc.*, 2011 WL 902222 (11th Cir. March 15, 2011), an individual acting as a surety sued the obligee, the principal, indemnitors, and numerous payment bond claimants. In his amended complaint, he pled only diversity jurisdiction under 28 U.S.C. § 1332 and did not plead federal question jurisdiction under 28 U.S.C. § 1331. The obligee moved to dismiss the suit for lack of subject matter jurisdiction due to the absence of complete diversity between the parties. In response, the surety raised federal question jurisdiction for the first time. The United States District Court for the Southern District of Florida dismissed the amended complaint without prejudice, concluding that there was no diversity jurisdiction or federal question jurisdiction under the Miller Act.

The Eleventh Circuit Court of Appeals affirmed the dismissal, concluding that the allegations of the amended complaint did not meet the well-pleaded complaint rule as to federal question jurisdiction under the Miller Act.

Presentation and Reservation of Grounds of Review

In *Fisk Electric Co. v. Solo Construction Corp.*, 2011 WL 891797 (11th Cir. March 16, 2011) a subcontractor that performed work at the Miami Dade Airport sued the general contractor and its surety for unpaid contract balances and additional expenses incurred due to construction delays. Following a jury trial, the United States District Court for the Southern District of Florida awarded the subcontractor \$964,976 against the general contractor and \$410,989 against the surety.

The subcontractor filed a motion to modify the jury verdict to make the surety and general contractor jointly and severally liable for the total 1,375,965 award. The District Court denied the motion. On appeal, the Eleventh Circuit Court of Appeals affirmed the denial because the subcontractor failed to raise an objection to the verdict before agreeing to the jury's dismissal. Interestingly, the Eleventh Circuit recognized that the subcontractor might have been able to seek an amendment to the jury verdict by way of motion, but it failed to do so with the District Court or on appeal. The Court stated the "District Court committed no reversible error by failing to grant relief not asked for: that is, amending the verdict to make [the surety] jointly and severally liable for the same sum awarded against [the contractor]."