

Appellate Court of Maryland Construes Notice Conditions of A312 Performance Bond in Favor of Surety

By: Joel P. Williams
Towson, MD
11.16.23

The Appellate Court of Maryland issued a reported opinion in a case construing an American Institute of Architects (“AIA”) A312 performance bond. In *Wildewood Operating Company, LLC v. WRV Holdings, LLC, et al.* 2023 Md. App. LEXIS 720 (Oct. 30, 2023), the Appellate Court of Maryland held that a performance bond surety was discharged from liability where the owner/obligee failed to give the surety notice of the contractor’s default termination until after a third party had completed the work.

The project concerned the construction of an assisted living facility in St. Mary’s County, Maryland. The owner, Wildewood Operating Company, LLC, entered into an A312-2010 performance bond with Clark Turner Construction, LLC, as contractor, and First Indemnity of America Insurance Company, as surety. When Clark Turner failed to complete certain stormwater management work adjacent to the site, Wildewood, Clark Turner, and other parties entered into a Work Agreement to address completion of the work. The surety was not a party to the Work Agreement.

When the work was still not completed under the Work Agreement, a third party completed the work at Wildewood’s expense under the terms of the Work Agreement. Wildewood subsequently made a claim to First Indemnity under the performance bond for those completion costs. By the time Wildewood declared Clark Turner in default, terminated the contract, and notified the surety, the work had already been completed. First Indemnity denied Wildewood’s bond claim, and Wildewood filed suit in the circuit court for St. Mary’s County, Maryland.

The trial court granted summary judgment in favor of First Indemnity on two bases: (1) Wildewood breached a condition precedent of the performance bond by failing to provide notice of the contractor’s default termination until after the work had been completed, and (2) First Indemnity’s obligation under the performance bond was discharged by the Work Agreement. Wildewood appealed to the Appellate Court of Maryland, which affirmed the entry of summary judgment in favor of the surety in a published opinion.

The opinion discusses the role and importance of bonding in the construction industry, recognizing that the bond is a contract and must be construed as such. Section 3 of the A312 performance bond addresses the owner’s notice obligations, including under Section 3.1 the owner’s obligation to provide notice that it is considering declaring a contractor default, and Section 3.2 addressing notice by the owner that it has declared a contractor default and terminated the construction contract. Importantly, Section 5 of the performance bond describes the remedies available to the surety when the owner has satisfied the notice requirements, including completing the construction contract itself, obtaining bids from qualified contractors, or making payment to the owner.

Although the bond did not contain an explicit *timely* notice requirement of the contractor’s default termination, the court construed the bond as a whole, holding that the bond required the owner to notify the surety of the default before a third party took over remedial work, noting that “[t]o read otherwise would render meaningless the options set forth in Section 5 of the Bond and ‘gut rights’ specifically afforded to First Indemnity.” Applying established rules governing conditions precedent, the appellate court concluded that the owner’s failure to comply with a condition precedent of the bond discharged the surety from liability.

Section 4 of the A312 performance bond states that a “[f]ailure on the part of the Owner to comply with the notice requirement in Section 3.1 shall not constitute a failure to comply with a condition precedent or to the Surety’s obligations, or release the surety from its obligations, except to the extent the surety demonstrates actual prejudice.” The court recognized that Section 4 of the bond only required the surety to demonstrate actual prejudice for a failure of the owner to provide notice of its intention to declare a default under Section 3.1 and does not apply to the owner’s obligation to provide notice of default termination under Section 3.2. Notably, the court concluded that even if the actual prejudice requirement did apply, First Indemnity was prejudiced as a matter of law when it was precluded from exercising its rights under Section 5 of the bond. The appellate court stated:

While we recognize that the purpose of the performance bond is to secure the owner against loss under the bonded contract and impose on the surety an obligation to cure the default of the contractor, that purpose ‘is not a blank check to the judicial power to rule out the pacts and agreements between the parties.’

The court did not reach the additional basis relied upon by the trial court in entering summary judgment – that by entering the Work Agreement the surety’s obligations under the bond were discharged.

The *Wildewood* decision is a case of first impression in Maryland, establishing the rule that an owner cannot unilaterally exercise self-help remedies in response to a contractor default in contravention of the surety’s rights to participate in the remedy under an A312 performance bond, and adds to a developing trend of cases in favor of sureties on this issue.

For additional information, please contact Joel P. Williams, Counsel (williamsj@whiteandwilliams.com; 443-761-6507) or a member of the Construction and Surety practice. White and Williams’ Maryland office successfully represented the surety in this matter.

This correspondence should not be construed as legal advice or legal opinion on any specific facts or circumstances. The contents are intended for general informational purposes only and you are urged to consult a lawyer concerning your own situation and legal questions.