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SURETY

CLARITY, MATERIALITY, AND CONTRACTS

By: Keith Langley

BOND

Clarity, materiality, and contracts. A Performance Bond is all about getting the job done, right. Here is a discussion of the L&A case, Mustang Pipeline, and Flintco, which factor into the equation.

Contracts and Clarity. "Before a declaration of default, sureties face possible tort liability for meddling in the affairs of their principals."*L&A Contracting Co. v. Southern Concrete Services, Inc.*, 17 F.3d 110 (5th Cir. 1994). The Court stated: "the declaration must inform the surety that the principal has committed a material *breach* or series of material breaches of the subcontract, that the obligee regards the subcontract as terminated, and that the surety must immediately commence performing under the terms of its bond."

Materiality. The Texas Supreme Court has distinguished between a material and a non-material breach as: "It is a fundamental principle of contract law that when one party to a contract commits a material breach of that contract, the other party is discharged or excused from further performance." By contrast, when a party commits a non-material breach, the other party "is not excused from future performance but may sue for the damages caused by the breach" *Mustang Pipeline Co., Inc. v. Driver Pipeline Co., Inc.*, 134 S.W.3d 195 (Tex. 2004).

In *Mustang Pipeline*, the Texas Supreme Court outlined several factors in the Restatement that are "significant in determining whether a failure to perform is material." 134 S.W.3d at 199 (citing RESTATEMENT (SECOND) OF CONTRACTS § 241 (Am. Law Inst. 1981)). These factors include: (a) the extent to which the injured party will be deprived of the benefit which he reasonably expected; (b) the extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived; (c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture; (d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of the circumstances including any reasonable assurances; (e) the extent to which the behavior of the partyfailing to perform or to offer to perform comports with standards of good faith and fair dealing.

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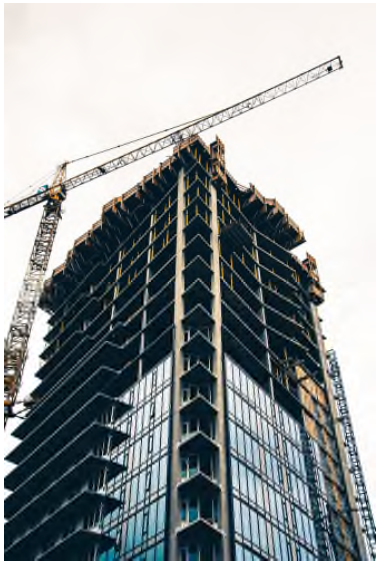
To "Go Green", our firm uses recyclable paper or ceramic cups and no longer uses Styrofoam cups. In addition, we have adopted a less-paper office environment.

We hope that these changes make big differences in the future.

Well done is better than well said.

- Benjamin Franklin



"Although the terms 'breach' and 'default' are sometimes used interchangeably, their meanings are distinct in construction suretyship law. Not every breach of a construction contract constitutes a default sufficient to require the surety to step in and remedy it. A legal default requires a: (1) material breach or series of material breaches (2) of such magnitude that the obligee is justified in terminating the contract. Usually, the principal is unable to complete the project, leaving termination of the contract the obligee's only option." *Id.* at 110.

Where the breach involves a time is of the essence contract provision (as is often the case), the owner may elect to continue performance or cease performance and sue for breach. *See Western* Irrigation *Co. v. Reeves County Land Co.*, 233 S.W.2d 599, 602-03 (Tex.Civ.App.-E1 Paso 1950, no writ; 3 WILLISTON ON CONTRACTS, §1334, at p. 2389 (3d ed. 1961). Crucial to the Texas court's ruling was including a "time is of the essence" clause in the parties' contract. By its own language the provision was "essential" to the contract, and delay was an issue that threatened the parties' bargain.

Other courts have noted the mere presence of such a clause is not necessarily enough to establish a material *breach. See, e.g., CFS Forming Structures Co., Inc. v. Flintco, Inc.*, 39 Fed. Appx. at 144, 2010 WL 3278247 at *7 (observing that the *Mustang Pipeline* court "*did not hold* that, in every case a "time is of the essence" provision *ipso facto* makes *any* delay a *material* breach." (Emphasis supplied by court); *GCC Constructors, Inc. v. American Home Horizon Concrete*, 2007 WL 926652, *5 (Tex. App.--Houston [1st Dist., Mar 29, 2007, n.p.h.) (refusing to find that delay was a material breach even though the contract specified time was "of the essence"). The holdings make clear that not only must the particular clause be central to the agreement, but also the specific violation must be so severe that it justifies excusing the other parties' contract performance.

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