December 2022

LITIGATION

LITIGATION

By: Keith Langley

Surety wins on motion for preliminary injunction with order that the principal post collateral and provide the surety free access to the principal's books, records, and accounts. *Frankenmuth Mut. Ins. Co. v. Nat'l Bridge Builders, LLC*, 2022 U.S. Dist. LEXIS 205753 (W.D.N.C. Nov. 13, 2022). The surety issued several bonds. After several payment and performance claims had been asserted against multiple bonded projects, the principal informed the surety that it lacked the financial means to pay its vendors, subcontractors, and employees on its bonded contracts and needed $1.5 million to complete the projects. The surety initially advanced $750,000 but informed the principal that the remaining $750,000 was contingent upon the principal providing the surety full and complete access to the books and records of the principal and indemnitors. The principal never provided the surety access to its books and records, so the surety did not advance the remaining $750,000. The principal then defaulted on multiple bonded contracts. After the principal failed to satisfy the surety's repeated collateral demands for $16 million, the surety filed suit and pursued a preliminary injunction that would require the principal to post collateral and provide the surety with access to its books and records.

The court evaluated the surety's motion under the common four-factor framework for equitable relief: 1) the surety's likelihood of success on the merits; 2) whether the surety would suffer irreparable harm absent the injunctive relief; 3) the balance of equities weighs in favor of the surety; 4) the injunction would be in the public interest.

LANGLEY BAINS LLP
ATTORNEYS & COUNSELORS

LANGLEY BAINS LLP
ATTORNEYS & COUNSELORS

Texas • Florida
Oklahoma • Arkansas

Texas (Dallas Area)
8813 N. Tarrant Parkway
Suite 224
North Richland Hills, TX 76182
(214) 722-7160

Florida (Miami Area)
P.O. Box 654303
Miami, Florida 33265

info@l-llp.com

www.langley.law

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

With respect to the likelihood of success on the merits factor, the court found that the surety had satisfied its burden with respect to both its request for collateral and access to the principal's books and records. The principal argued that the surety was unlikely to succeed on the merits because the surety had allegedly "agreed" to advance the full $1.5 million and its failure to do so allegedly "caused" the principal to default. The court was unpersuaded, noting that no provision in the indemnity agreement required the surety to advance funds to the principal. In contrast, the indemnity agreement – the validity of which was not disputed by the principal – specifically required the principal to deposit collateral upon demand "in an amount *as determined by [the surety].*" With respect to the surety's access to the principal's books and records, the court found that the indemnity agreement gave the surety "free access" to all of the principal's books and records but the available evidence indicated that the principal had only provided the surety with checks, invoices, lien waivers, and financial statements related to the $750,000 advanced by the surety.

The court likewise found that the surety had met its burden under the irreparable harm factor. With respect to the request for collateral, the court quoted precedent stating: "Courts routinely recognize that a surety's loss of its right to collateralization cannot be adequately remedied through monetary damages…This is so because the surety holds a bargained-for right to collateral security and, without enforcement of such right, assumes the risk of becoming a general unsecured creditor and of being unable to collect a subsequent judgment in its favor." Concerning the surety's access to the principal's books and records, the court noted that "absent access to books and records, a surety is in the dark as to its chances of successful performance of the contract and has no idea whether and to what extent an indemnitor can satisfy their indemnity obligation."

The court easily found that the balance of equities factor favored the surety, as the surety had specifically bargained for the right to demand collateral and inspect the principal's books and records in the indemnity agreement, so granting the injunction "would merely require [the principal] to perform as [it] contractually obligated [itself] to do."

Finally, the court found that the public interest factor weighed in the surety's favor, as "[t]he public has an interest in ensuring that contracts are enforced… Further, enforcing the collateral security provision of an indemnity agreement in the construction setting serves an important public interest: to encourage sureties to continue to provide bonds for public construction contracts."

Consequently, the court granted the surety's motion and ordered the principal to deposit the full amount of collateral requested by the surety and to furnish the surety free access to the principal's books, records, and accounts.

Keith Langley is a Partner at Langley Bains LLP and may be contacted at klangley@l-llp.com or mobile (214) 207-5324.