

CLIENT NEWS BRIEF

Recent Appellate Court Ruling Provides Guidance on Contractor's Delay Damages and on Challenging a Performance Bond Surety's "Lack Of Notice" Defense

The appellate court in *JMR Construction Corp. v. Environmental Assessment and Remediation Management, Inc.* (December 30, 2015, M105497) 2015 Cal.App.Lexis 1172 (*JMR Construction*), recently affirmed a trial court's six-figure judgment in favor of a general contractor against its subcontractor and the subcontractor's performance bond surety arising from a federal works project. The judgment included an award of damages for, among other things, the subcontractor's delay and deficient work. The ruling addresses the requirement for "proving up" a contractor's delay claim and recovery for such a claim and also highlights for public works owners a potential avenue of attack against a performance bond surety where the surety contends it has no liability under the performance bond because it was not provided "proper notice" under the performance bond's terms.

In *JMR Construction*, the surety argued that it had no liability under the performance bond because the general contractor did not provide the surety notice of the subcontractor's failure to perform as required under its subcontract. Such a failure would constitute a "default" under the subcontract. The surety argued that "a declaration of default was a condition precedent" to its liability. While it was true that the general contractor neither formally declared the subcontractor in "default under the subcontract" nor requested that the surety complete the bonded work under the subcontract, the court held that the surety's "receipt of a declaration of default [by the general contractor] is not a condition precedent to triggering [the surety's] liability under the bond." This was because (1) the performance bond did not *expressly* require such notice is a condition precedent to liability, and (2) the underlying subcontract, which the performance bond incorporated by reference, did not contain notice provisions requiring the general contractor to notify the surety of its claims against the subcontractor.

Without an express contractual requirement to provide "notice of default," the court refused to endorse the surety's argument that a "declaration" or "notice of default" is a condition precedent *implied* from the language of the bonds or underlying subcontract. Coupled with the bond and subcontract's language, the court cited Civil Code sections 2806 and 2807 holding that the surety's obligation was deemed unconditional unless otherwise agreed to (Civil Code § 2806) and that "a surety who has assumed liability for payment or performance is liable to the creditor immediately upon the default of the principal, *and without demand or notice.*" (Emphasis in the original.)

The *JMR Construction* decision highlights for public works owners a potential avenue to overcome a performance bond surety's technical defense that it was not provided proper notice sufficient to trigger its bonded obligations. Unless the express terms of the bond and/or underlying contract require such notice, a surety cannot simply argue that a "declaration" or "notice of default" is an implied requirement before it can have exposure under the performance bond. For these reasons, it is important that public agencies review the terms of performance bonds on public works projects closely before agreeing to them.

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Another notable aspect of this decision for public works owners is that *JMR Construction* is the first California reported decision recognizing the “*Eichleay*” formula for calculating a contractor’s home office overhead costs in connection with a delay claim. The *Eichleay* formula is an established methodology in federal court cases allocating a contractor’s home office overhead costs to a project that has been extended or delayed. The court here held that the *Eichleay* formula was a legally permissible method of determining the general contractor’s home office overhead damages against the subcontractor and its surety and applies in California state cases. This is important to public works owners in this state because general contractors now have a legally recognized method to calculate home office overhead delay damages against such owners, which could result in an increase in damages against public works owners who are found to be responsible for the contractor’s delay.

For more information on issues arising from public works construction disputes, including surety defenses and contractor delay claims, please contact one of our [nine offices](#) located statewide. You can also visit our [website](#), follow us on [Facebook](#) or [Twitter](#), or download our [Client News Brief App](#).

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