

Rhode Island Affirms The Principle That Sureties Must be Provided Notice of Default Before They Can be Held Liable for Principal's Default

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Most bond forms in use today, including the standard form AIA A312-2010, contain express condition precedents that trigger a surety's obligations under the bond. Under a performance bond, the bond obligee is required to provide formal notice to the surety that the principal has materially defaulted and that the surety must begin to perform under the terms of the bond. This principle is grounded in the idea that the surety should have an opportunity to address the default and investigate the claim so as to mitigate its own liability. Failure to provide sufficient notice will discharge the surety of its obligations under the bond.

The critical importance of providing a performance bond surety with notice of a principal's default was the basis of a recent decision by the Rhode Island Supreme Court. In *Apex Development Company, LLC v. Department of Transportation*, 291 A.3d 995 (R.I. 2023), the Court affirmed the grant of summary judgment for the sureties due to the failure of the owner of the project to provide any formal notice of default. Here, the Rhode Island Department of Transportation (RIDOT) filed a third-party complaint against the sureties for indemnification after a landowner alleged that RIDOT trespassed and damaged its property during the reconstruction of a portion of the I-95 highway. The sureties filed a motion for summary judgment arguing that the bond only applied to direct construction costs and not to third-party damages. The sureties further argued that the bond became null and void upon substantial completion of the project, and even if it did not, the sureties' obligation under the bond was discharged because of RIDOT's failure to give notice of the alleged contractor default to the sureties. RIDOT argued that the sureties' interpretation was too narrow because the public works bond was more expensive than other bonds, and it also covered all the contractor's responsibilities under the contract, including indemnification. The lower court granted the sureties' motion for summary judgment, which the Supreme Court affirmed. It reaffirmed the principle that the purpose of a bond is to guarantee the work in question was to be completed and not intended to compensate for indirect losses or for indemnification. Moreover, the Court also found that the obligations of the sureties under the bond is conditional. Specifically, "[i]n order to trigger surety's obligation to perform under a bond, it must first have notice of the principal's default or breach." In this case, RIDOT failed to meet these conditions as it never notified the sureties of the claims arising out of the contractor's alleged trespass and, thus, the sureties were discharged from all obligations under the bond.

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