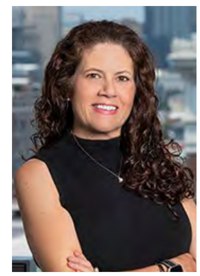
American Bar Association
Tort Trial and Insurance Practice Section

Winter 2025

# COMMITTEE NEWS

Fidelity & Surety Law

## Delay Claims – Part II
## Methods Of Proving Delays And Required Documentation

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***Editor's Note:*** *Part I of this two-part article examining delay claims on construction projects appeared in the Fall 2024 edition of the FSLC Newsletter, which can be accessed here.*

### I. Methods of Proving Delays

When a party experiences a delay and determines that the delay is excusable and compensable, the party must then determine how to properly quantify the damages associated with the delay. Such damages may include many different types of added expenses and costs, including increased labor costs, equipment costs, material costs, subcontractor costs, jobsite overhead costs, home office overhead costs, and lost productivity. With so many types of damages that could result from delays, it is as important to understand how to effectively present such a claim, as it is to determine which damages may be compensable under the circumstances.

*Read more on page 20*

## In This Issue

## Chair Message

Our core mission is to empower claim and legal professionals in the fidelity and surety industries through authoritative publications, outstanding educational programs, and unmatched networking events, and we delivered all of that in spades at our 2025 FSLC Midwinter Conference in Austin, TX held on January 15 – 17, 2025. With fantastic attendance and a spirit that animated the entire conference, we presented three stellar programs. Thank you to Rob Niesley, John Sebastian, and Michele Killebrew for Co-Charing the Construction Program, *Contracting with the Feds: A Survival Guide*; to Co-Chairs Frank Marisco, Ken West and Scott Schmookler of the Fidelity Program, *Trial and Error? How Jurors Actually Perceive Common Fidelity Issues and Evidence*; and Co-Chairs Dave Kotnik, Amy Bentz, and Matt Davis of the Surety Program, *A Deep Dive into Advanced Performance Bond Strategies.* All three programs received rave reviews and continued to set the bar for industry-leading programs that advance the knowledge of cutting-edge legal issues in the construction, fidelity, and surety industries.

**Blake Wilcox**
*Liberty Mutual Insurance Company*

*FSLC Chair 2024 – 2025*

*Executive Vice President Chief Claims Officer*

It was a deep personal honor for me to recognize and honor Chad L Schexnayder as the recipient of the Martin J. Andrew Award for his extraordinary lifetime contribution to advancing the interest of—and his leadership in—the FSLC. Equally so was the pride I felt in our collective efforts to develop new leaders in the FSLC with our hugely successful Emerging Leaders Program, and our many other outreaches to welcome and involve a diverse new generation of attorneys and industry professionals into the FSLC. We are built to harness the power of experience to inspire the leaders of tomorrow, and you can feel it in the excitement and pride of our members.

We are committed to help you stay better connected to FSLC starting with our improvements to our ABA – FSLC Website. As a member, you have access to our FSLC Members Portal where we house our vast resources, including our Leadership Org Chart, FSLC Members Directory, archived Newsletters, Prior-Year Conference Material, and so much more. Connect with us on LinkedIn by following the TIPS site, and connect with me, Chair-Elect Bruce Corriveau and Chair-Elect Designee Amy Bentz. Help us spread the word by reposting as much as possible.

We also hope that you will enjoy and benefit from the expanded scope of articles now present in our Newsletter, in addition to our exemplary legal articles and case notes. Our intent is to leverage the Newsletter to keep you better informed of the expansive activities of FSLC, recognize the contribution of our members, and share the excitement of our vibrant FSLC community. And in that vein, don't miss the article on the upcoming 2025 Spring Surety Conference on May 21 through May 23, 2025, at the barrier island of Isle of Palms, South Carolina. Alana Porrazzo, Brian Kantar and Nina Durante are co-chairing the program this year with the theme *New and Old Frontiers for the Surety in Bankruptcy Court*.

Looking forward to seeing you at Isle of Palms!

## Connect with Fidelity & Surety Law

website

## Stay Connected with TIPS

We encourage you to stay up-to-date on important Section news, TIPS meetings and events and important topics in your area of practice by following TIPS on **X** @ ABATIPS, joining our groups on **LinkedIn**, following us on **Instagram**, and visiting our **YouTube** page! In addition, you can easily connect with TIPS substantive committees on these various social media outlets by clicking on any of the links.

# 2025 TIPS Fidelity and Surety Sponsors

We are proud and honored to recognize this all-star lineup of top-tier Sponsors for the Fidelity and Surety Law Conferences scheduled in 2025. Since 1933, the FSLC's mission is to funcion as the preeminent authority and resource on fidelity and surety law for the industry. This support by so many distinguished Sponsors is a testament to FSLC's reach and impact to FSLC's indusry-setting standard of excellence. We feel privileged to have the support of such a distinguished group of law firms and companies. –Blake Wilcox, FSLC CHair, 2024-2025.

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# Equitable Subrogation Issues: A Circuit by Circuit Survey

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## I. Introduction.

Subrogation is an important right of the surety. It is the means by which a surety can minimize or ameliorate its losses by assuring its priority to contract funds remaining in the hands of the obligee. Consequently, the surety and its counsel will want to make certain that the surety has taken all possible steps to preserve and assert such rights. This article will serve to acquaint the newcomer with the doctrine of subrogation and sharpen the saw for those more seasoned practitioners.

In 2023, this publication provided a piece authored by Alexis Breedlove that covered the topic of equitable subrogation through a focused analysis of Federal Court of Claims cases.[1] However, this article will analyze the published decisions of certain other federal circuit courts of appeals[2] that have examined the issue outside of the federal claims context. Likewise, some cases, while not explicitly addressing the doctrine of subrogation, demonstrate that certain issues can impede a surety's recovery.

## II. Discussion.

### *1. Surety's Equitable Subrogation Rights Preserved (or at least recognized).*

#### a. Eighth Circuit.

*Pennsylvania National Mutual Casualty Insurance Co. v. City of Pine Bluff*[3] best represents the paradigm of the surety/owner relationship and how the surety preserved its right to subrogation. The City of Pine Bluff (the "City") hired a general contractor, David Mitchell Construction ("Mitchell"), to clean up the aftermath of severe ice storms, and the surety, Pennsylvania National Mutual Casualty Insurance Company ("Penn"), issued performance and payment bonds for the project.[4] The work was to be paid through funds received from the Federal Emergency Management Agency ("FEMA").[5] Arguments between the City and Mitchell led to the termination of Mitchell's contract.[6] Subsequently, Penn sent the City a letter that identified its

*Read more on page 27*

1 Alexis Breedlove, *Subrogation Notice: Did the Surety Trigger the Owner?*, 2023 A.B.A. Fid. & Sur. L. Comm. Newsl. (A.B.A, Chicago, Ill.), at 11, 25–28.

2 This article includes opinions from the Eighth, Ninth, Eleventh, and D.C. Circuit Courts of Appeals.

3 354 F.3d 945, 949 (8th Cir. 2004).

4 *Id.* at 949.

5 *Id.*

6 *Id.*

# Fighting Back Against Bankruptcy Abuses: Objections to Discharge and Dischargeability

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"How did you go bankrupt?"
"Two ways. Gradually, then suddenly."
– Ernest Hemingway, The Sun Also Rises

Dealing with principals and indemnitors filing for bankruptcy is something those in the surety world inevitably have to deal with. Most of the time, the bankruptcy process plays out as intended: assets are gathered and hopefully maximized, creditors get in line, and a distribution is made. However, occasionally a surety will be faced with a bankruptcy situation where something seems off. Maybe project funds or materials cannot be accounted for. Or maybe the indemnitors are suddenly saying they have no assets while somehow launching a new business enterprise and living a lavish lifestyle. Understanding how to sniff out and combat potential attempts to abuse the bankruptcy process can be an effective tool in your arsenal. This article explains and provides a few practical pointers for making use of two available methods to respond to bankruptcy abuses: objections to discharge and dischargeability.

## I. Objections to Discharge and Dischargeability

One of the fundamental tenants of the bankruptcy process is the idea of a "fresh start" when emerging from bankruptcy.[1] While this typically entails a discharge of the debtor's prepetition obligations and liabilities, the Bankruptcy Code provides exceptions that may either preclude a discharge generally or that may preclude a discharge of a specific debt. As discussed in more detail below, objections to discharge under Section 727 of the Bankruptcy Code focus on the debtor's bad faith actions relating to the bankruptcy process itself. On the other hand, objections to dischargeability under Section 523 focus on particular debts that arose through some kind of fraud, theft, or other bad act. If successful, an objection to discharge generally precludes any discharge of the debtor, while an objection to dischargeability will preclude a discharge for a particular debt.[2]

### *A. Objection to Discharge*

Section 727 of the Bankruptcy Code sets forth circumstances where the debtor may not be eligible for a discharge. The relevant grounds for objecting to discharge typically

*Read more on page 36*

1 *See* Local Loan Co. v. Hunt, 292 U.S. 234, 244 (1934).
2 *Cf.* 11 U.S.C. §§ 727, 523 (2024).

# Grain Bond Basics for the Uninitiated: Practical Similarities and Differences

**Jacob Doleshal**
*McCarthy, Leonard, Kaemmerer & Miller*

***Jacob Doleshal** is a partner in the Kansas City office of McCarthy, Leonard, Kaemmerer & Miller.*

## I. Introduction

Experienced surety practitioners are familiar with most forms of indemnity agreements and bonds. Payment, performance, and maintenance bonds are part and parcel of the trade, and these products often arise in the construction context. On a long enough timeline, the surety client will introduce a grain bond or agricultural commodity bond into the surety practitioner's familiar world. At first blush, the practitioner may find comfort in the familiarity of the indemnity agreement and the bond. However, as the practitioner digs deeper, material differences must be observed to properly process the grain bond claim. Variations in state statutes render a straightforward analysis difficult.[1]

This article is meant to serve as a primer for surety practitioners to use as a jumping off point as they embark on what may be an unfamiliar journey. It is also a cautionary tale that claims on less familiar "miscellaneous bonds" require our immediate attention to learn their specific characteristics.

## II. Grain Bond Basics

During a grain harvest, grain producers (farmers) routinely gather their harvest and deposit grains into grain storage facilities owned by licensed operators. The grains are graded[2] and receipts for the deposited grain commodities are given to the producers. The receipts can be exchanged later for grain from the same storage facility. In other words, the storage facility acts as a grain bank where the commodity can be deposited and later withdrawn. For instance, a producer may deposit an exact quantity (bushels) of grain with a certain grade and can later expect to receive the same amount and grade, or a different amount and grade with an equivalent value. The facility operator must keep and maintain sufficient stores to cover the deposits made by producers.

The harvested grains are comingled in the storage facility with the grains of other producers. Upon deposit, a bailment is created and the facility operator, who takes charge of the grain on behalf of the producer, must safeguard the grain from

*Read more on page 41*

1 Grain commodity transactions often involve analysis under U.C.C. Article 7 (Am. L. Inst. & Unif. L. Comm'n 2022), which this article does not address. However, the practitioner must be aware of this potential and analyze the contracts to determine Article 7 applicability.

2 "Grading" a grain is the process of assigning a quality designation, which determines its market value. Grading requirements are set forth by the US Department of Agriculture, Official US Standards for Grain, and grains are graded based upon minimum weight per bushel, moisture content, percentage of foreign material present, weathered kernels, and other assessment parameters. *See* 7 C.F.R. §810.101 (2019).

# William F. Haug
## February 27, 1931 - December 12, 2024

One of our committee's distinguished past leaders passed last month at the age of 93. Bill Haug served as FLSC chair in 1983-84. In 2001, he was recognized by this committee as the fourth recipient of the Martin J. Andrew Award for Lifetime Achievement in Fidelity and Surety Law.

The Surety Association of America awarded Bill the SIO Silver Award in 1998, recognizing his outstanding contributions to the development of surety law nationwide. Bill leaves us with a catalog of surety and fidelity scholarship, as well as a long list of reported decisions.

Bill not only served the FSLC and the surety and fidelity industries, but was a leader in his community and local bar. He was president of the Arizona State Bar Association and the Maricopa County Bar Association and served for years on the board of directors of both bar associations. Bill was instrumental in founding the charitable arms of both bar associations, and was recognized by Arizona's governor for this work. Bill served as president of a school district, a church, and a little league, he coached youth sports and was an avid sports fan and outdoorsman his entire life.

While Bill was not a man of large physical stature, he was a giant in every way that mattered. Thanks to his legal acumen, his national reputation, his dedication to serving the community and the bar, and in his role as husband, father, grandfather and great-grandfather, Bill positively impacted the lives of many. He believed strongly in professionalism and treating everyone with respect and collegiality, legal adversaries included. Bill is much remembered for his kindness and welcoming personality. He formed many lifelong friendships with members of our committee. Bill is survived by a large family. He and his wife Nancy celebrated their 70th wedding anniversary last summer. He will be missed.

**–Chad L. Schexnayder, Esq.**

# Everything's Bigger in Texas – Including FSLC's 2025 Midwinter Conference!

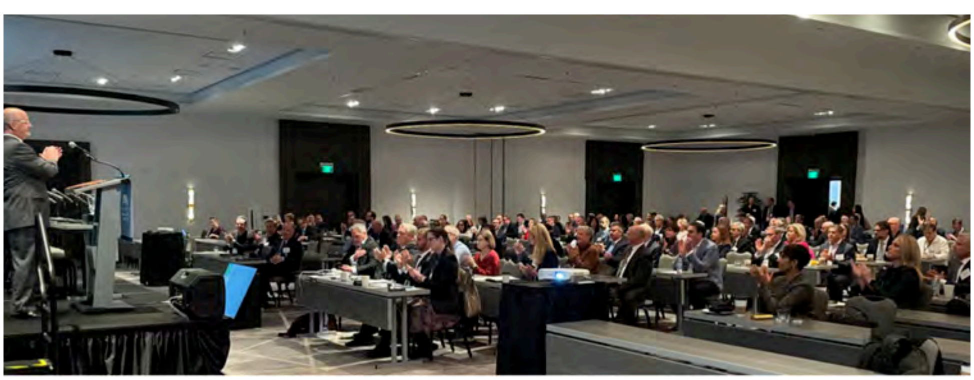
Everything is bigger in Texas, and the 2025 FSLC Midwinter Conference, held in Austin from January 15–17, 2025, was no exception. With record-breaking attendance and an atmosphere brimming with camaraderie, the event showcased the best of what the FSLC has to offer.

The conference featured three stellar programs that captivated attendees and earned rave reviews:

- **Construction Program:** *"Contracting with the Feds: A Survival Guide"* – Co-Chaired by Rob Niesley, John Sebastian, and Michele Killebrew.
- **Fidelity Program:** *"Trial and Error? How Jurors Actually Perceive Common Fidelity Issues and Evidence"* – Co-Chaired by Frank Marisco, Ken West, and Scott Schmookler.
- **Surety Program:** *"A Deep Dive into Advanced Performance Bond Strategies"* – Co-Chaired by Dave Kotnik, Amy Bentz, and Matt Davis.

The programs provided exceptional content, advancing the conversation on critical legal issues in construction, fidelity, and surety law.

FSLC Chair Blake Wilcox summed up the success of the event, saying, *"This year's Midwinter Conference exemplified the collaboration, dedication, and expertise that make FSLC such a vibrant community. A heartfelt thank you to the Co-Chairs, speakers, and all who attended for making this event truly extraordinary."*



# 2025 FSLC Spring Meeting
# May 21 – 23, 2025

**From a unique barrier island on the coast of South Carolina comes a unique opportunity to learn about New and Old Frontiers in Bankruptcy – The 2025 FSLC Spring Meeting**

We are excited to invite you to attend the 2025 FSLC Spring Meeting on May 21 through May 23, 2025, at the barrier island of Isle of Palms. The area is known for its pristine beaches, clear water, natural wildlife as well as fishing, biking, kayaking and world class dining. Isle of Palms was voted #6 among Top 10 North America Islands by Conde Nast Traveler's Reader's Choice Awards. You get to explore all this, plus you get to explore the wonderful world of Bankruptcy!

Alana Porrazzo of JHKM Law, Nina Durante of Liberty Mutual, and Brian Kantar of CSG Law are co-chairing the program this year, which will be a 1 ½ day exploration of how bankruptcy law has evolved over the years and hot topics addressing what may be coming in the next five years. We are very excited about this topic, and we hope you are, too. Each of our distinguished panelists brings a fresh and different perspective to Surety Bankruptcy.Our panelists consist of surety professionals, expert consultants and outside surety counsel. We are looking forward to showcasing these experts at this interesting and informative program.

Topics will include a bankruptcy primer for those newer to surety bankruptcy as well as discussions about quirks of Bankruptcy Procedure, Plan Injunctions, Third Party Releases, collateral, oil and gas bonds, workers' compensation bonds, customs bonds, Subchapter V and Chapter 15. We will also have segments on Canadian Insolvency and Restructuring Proceedings and Puerto Rico Bankruptcy and PROMESA.

Finally, the program will include a panel of seasoned leaders of the surety bankruptcy bar who will reflect on the evolution of surety bankruptcy from when they began practicing, what trends they have seen and continue to see and what they would like to see from surety bankruptcy practitioners in the next five years. This highly anticipated panel is expected to provide a dynamic and interactive discussion with a good deal of audience participation. Come ready with your questions for our experts!

We are excited and hope to see you at next year's FSLC Spring Meeting at the beautiful Isle of Palms.


Join us at the Wild Dunes Resort,
Isle of Palms, Charleston, SC!
New and Old Frontiers for the
Surety in Bankruptcy Court
FSLC Spring Meeting: May 21-23, 2025
Program Co-Chairs
Nina Durante
Liberty Mutual
Seattle, WA
Alana Porrazzo
JHKM Law
Phoenix, AZ
Brian Kantar
CSG Law
Roseland, NJ

# Fidelity and Surety Law Committee's Emerging Leaders Program

The Fidelity and Surety Law Committee kicked off its 2nd annual Emerging Leaders Program at the 2025 Midwinter Meeting held in Austin, TX. The Emerging Leaders Program is committed to identifying and developing emerging leaders in the fidelity and surety community. The program provides leadership programming and social opportunities to the participants to assist them in identifying various leadership opportunities within the FSLC. The program will be held annually, with a different class of participants selected each year. Program participants are asked to attend both the FSLC Midwinter Meeting and the Spring Meeting.

The Emerging Leaders Class of 2025 is comprised of Austin Brakebill (Great American Insurance Company), Adam Brinkley (Berkley Surety), Kelsey Bilodeau (Gottesman Law), Megan Daily (Krebs Farley), Connie J. Boudreau (Liberty Mutual), Ted Lansdale (Travelers), Brian Padove (Watt Tieder), Amanda Miceli (CSG), and Brittany Rose (Travelers). Please congratulate these Emerging Leaders on their selection to the program and contributions to our industry.

On Tuesday, January 14, the day prior to the start of the 2025 Midwinter Meeting, the Emerging Leaders participated in a full day of programming planned and coordinated by David Bresel (Markel) and Jennifer Whritenour (Intact). After an exercise designed to get to know one another, program participants learned about the inner workings of the FSLC from past chair Chris Ward and current chair Blake Wilcox and about the Tort Trial & Insurance Practice Section, the umbrella committee over FSLC, from past chair Jeff Price. Program participants also had an in-depth roundtable discussion with future FSLC chair Bruce Corriveau on the future of leadership in the FSLC. After a presentation and caucus on generational differences and stress, program participants enjoyed social time at dinner in Austin. On Wednesday, January 15, program participants attended FSLC business meetings and were introduced at the Vice-Chairs Meeting.

A few of this year's participants have provided testimonials about their experience so far with the Emerging Leaders Program:

> "When nominated to be a part of the Emerging Leaders Program, I was honored and interested to learn more about all of the benefits being a member of the FSLC offers. After hearing the stories from the seasoned members of the FSLC, it really hit home that the FSLC not only provides

great scholarship, but also, promotes comradery throughout the FSLC community. I look forward to becoming actively involved in the group and continuing the invaluable network of peers I met as part of the program."

– **Brian Padove,** *Watt Tieder*

"The Emerging Leaders program was invaluable in initiating a path to leadership in the FSLC and providing a forum for guidance from past, current, and future chairs of the Committee. This program inspired me to get involved in the FSLC while connecting me to colleagues I would not have met otherwise, some of whom I am certain will be lifelong friends."

– **Amanda Miceli,** *CSG Law*

The final installment of the inaugural Emerging Leaders Program for this year's class will take place at the Spring Meeting at Wild Dunes Resort, Isle of Palms, SC. Our Emerging Leaders will continue with programming, team building exercises, social activities, and further discussions about advancing the FSLC.

If you are interested in learning more about the FSLC Emerging Leaders Program or being a part of a future class of Emerging Leaders, please contact Jennifer Whritenour (jwhritenour@intactinsurance.com), Melissa Lee (mlee@manierherod.com) and/or David Bresel (david.bresel@markel.com).

# Fidelity School Makes Its Debut at the 2025 FSLC Mid-Winter Meeting

The 2025 FSLC Mid-Winter Meeting included the maiden voyage of Fidelity School. Modeled after the wildly successful Surety School, the curriculum was “Fidelity 101”, and focused on the basics of interpreting fidelity/crime policies and investigating claims. Fidelity School students included in-house claim handlers, outside attorneys, accountants, and other consultants. The students were eager, attentive, and engaged. It was a free-flowing discussion, with “no bad questions” serving as a ground rule.

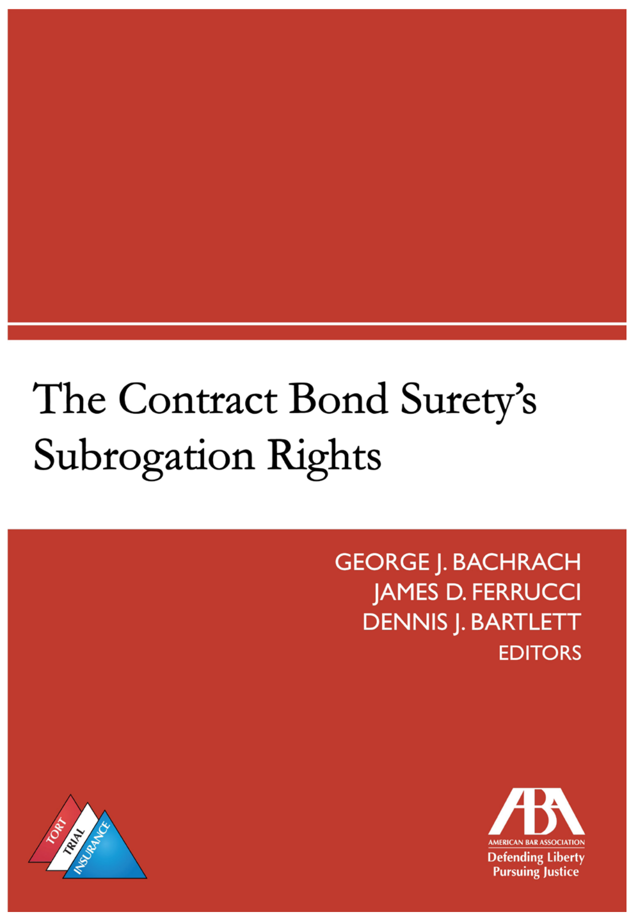
The Fidelity School reviews were extremely positive, and the FSLC plans for it to become a regular portion of the Mid-Winter meeting. Many thanks to the all-volunteer faculty for providing first class analysis and making this a worthwhile endeavor for all involved. A special thanks to Scott Williams and Gina Lockwood for their guidance in getting Fidelity School off the ground.

# The Contract Bond Surety's Subrogation Rights (2013)

The Contract Bond Surety's Subrogation Rights is a comprehensive book that flows from the general principles and required elements of the surety's subrogation rights to the application of those rights in specific situations. The chapters address: (a) the basic issues and rights of the contract bond surety's asserting its common law right to equitable subrogation, the treatment of the surety's subrogation rights in the Restatement of the Law (Third) Suretyship & Guaranty, and the parties' rights to which the surety may assert its subrogation rights (Chapters 1-3); (b) the necessity of the principal's default, the surety's performance upon the principal's default, and the surety's notice of the assertion of its subrogation rights (Chapters 4-6); (c) the surety's assertion of its subrogation rights to the bonded contract funds and other property in competition with the obligee, the principal, the principal's subcontractors and suppliers, assignees/lenders, trustees and debtors in bankruptcy, taxing authorities and other governmental lien creditors, and the principal's general and judgment creditors (Chapters 7-13); and (d) the surety's subrogation rights to the obligee's and principal's common law and contractual setoff rights, the many issues involving the surety's subrogation rights and claims against the federal government (including jurisdictional and substantive issues), and the surety's assertion of its subrogation rights against third parties such as design professionals, lenders, insurers and others (Chapters 14-16).

The Table of Contents for the book serves as an outline of the structure, issues and topics addressed in each of the chapters to enable the reader not only to go right to the cases and discussions that may be of assistance in their particular case, but also to absorb the very basic, necessary and critical understandings of the contract bond surety's subrogation rights that are addressed not only in detail in the first six chapters of the book, but also within the substance of the very chapter that the reader chooses to review for their particular case.

[Order Today](#)



*Delay Claims... continued from page 1*

There are multiple methods for proving delays and each has its pros and its cons. Attorneys and claimants must be sure that the method chosen is best for the available facts and data surrounding the delay and that the analysis will be accepted as reliable and credible by those that ultimately review and determine whether the delay claim has merit. Determining which method to use when dealing with delay claims will depend on the quality and supportability of the overall analysis, which will ultimately depend on the facts and the data available to support the claimed delay. Some common methods of delay analysis include (1) the Total Cost Method, (2) the Modified Total Cost Approach, (3) the Jury Method, and (4) the Measured Mile Method.

### *A. Total Cost Method*

In general, the Total Cost Method is a process used to calculate damages as the difference between total actual costs incurred (plus overhead and profit) and the bid amount.[1] The basic calculation subtracts the contractor's bid estimate from the total of all project costs incurred and seeks recovery of the overrun cost as the damages caused by the delay. While one of the simplest methods for calculating delay damages, it tends to carry the least amount of weight with those opposing delay claims, as it does not eliminate the possibility that the party seeking the delay claim may have been responsible for some of the delay, or that the contractor may have underbid the project.

The Total Cost Method is often subject to attack including (1) the validity and accuracy of the original estimate; (2) errors and deviations from the work plan by the contractor that result in added costs; and (3) events increasing the cost (such as weather) that are not the fault of the owner.[2] If the total cost method is used, each of these points must be addressed by the claimant in any claim presentation as part of its burden of proof.[3] Additionally, one of the main concerns with the Total Cost Method arises from the possibility of bidding inaccuracies.[4] Many courts, such as the Federal Circuit in *Servidone*, are openly critical of the Total Cost Method and have even noted that the Total Cost Method should be used with caution and as a last resort.

### *B. Modified Total Cost Approach*

The Modified Total Cost Approach was created in response to the complaints surrounding the Total Cost Method. It is preferred over the Total Cost Method as it

1 Safeco Ins. Co. of Am. v. S & T Bank, 2010 U.S. Dist. LEXIS 18914, *24 (W.D. Pa. Mar. 3, 2010). *See also* Raytheon Co. v. White, 305 F.3d 1354, 1365 (Fed. Cir. 2002).

2 Safeco Ins. Co. of Am., at 25.

3 Id.

4 Servidone Constr. Corp. v. U.S., 931 F.2d 860, 861-62 (Fed. Cir. 1991).

eliminates sole reliance on the contractor's original estimate by taking into account deficiency or performance issues caused by the contractor and also assesses non-compensable delays, such as "Acts of God." With this method, a plaintiff will normally reduce its claim by the amount of bid errors, costs arising from contractor actions, and costs arising from actions of parties other than the owner.[5] Courts explain that when using the Modified Total Cost Approach, safeguards must be used to ensure that the burden of excess expenses falls on the party responsible for those expenses.[6] In *Raytheon Co. v. White*, the Federal Circuit clarified that a plaintiff utilizing a Modified Total Cost methodology must prove that (1) the nature of the losses make it impossible or highly impracticable to determine them with a reasonable degree of accuracy; (2) the plaintiff's bid or estimate was realistic; (3) its actual costs were reasonable; and (4) it was not responsible for the added expenses.[7] If a plaintiff is successful, the plaintiff may recover the total cost of the contract minus the bid price with various adjustments for delays the contractor caused or any miscalculations.[8]

### *C. The Jury Method*

The Jury Method is another analysis often used when the claimant lacks sufficient documentation to link damages to causation. This very simple method involves a party seeking compensation related to delays to establish its losses to the best of its ability and based on its limited data and documentation, with the intent to obtain an equitable adjustment. In general, the contractor presents the jury or court with the best evidence available and hopes for an equitable solution. While the Jury Method is disfavored due to the lack of evidentiary support to determine damages with any certainty, a claimant, such as a contractor, may have no choice if there is little to no direct evidence of the delays and resulting costs.

### *D. Measured Mile Method*

The Measured Mile Analysis is the most reliable, and thus the preferred method for calculating lost productivity and delay damages. Under this technique, a non-impacted period or area of activity of construction work is compared with another period or area of activity of construction work that has been disrupted. The assumption underlying the Measured Mile Method is that the difference between the labor or equipment hours expended per unit of work performed in the non-impacted and impacted periods represents the loss to the contractor due to the impact or

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5 Safeco Ins. Co. of Am., at 26.

6 Raytheon Co. v. White, 305 F.3d 1354, 1366 (Fed. Cir. 2002).

7 Id.

8 Propellex Corp. v. Brownlee, 342 F.3d 1335, 1339 (Fed. Cir. 2003).

disruption for which another party is responsible.[9] Basically, the method compares productivity during a non-impacted period with productivity during an impacted period. Ideally, the Measured Mile analysis uses productivity data from the same project and relies upon actual productivity rates and not bid productivity rates. If there is no "measured mile" available on the same project, then a "measured mile" may be used from a similar project utilizing a similar crew to represent a non-impacted productivity rate.[10]

The chief advantage of this methodology is its ability to isolate the productivity loss during an impacted period from other project factors via achieved progress in a non-impacted period. The ability to isolate the productivity loss is one of the most significant reasons why contractors prefer this method of measuring damages.

### *E. Contracts and Delay Methods*

Most sophisticated contracts specifically include terms which address the methodology required to calculate and prove delays, as typically established through specific schedules, pre-determined methods of analyses, and specific documentation. For example, under FAR 52.235-15, Schedules for Construction Contracts, the federal government specifies the deadline for the contractor to submit its schedules, the format and content that must be included in the schedules, and the dates on which the contractor contemplates starting and completing the several salient features of the work.[11] In the case of federal contracts, if the contractor fails to comply with these requirements, then the Contracting Officer may withhold approval of progress payments until the contractor submits a schedule in compliance with FAR 52.235-15.[12]

It is also important to understand all relevant contract clauses concerning delays, such as notice requirements and certain methods for establishing delays. Courts routinely enforce contract clauses that set forth specific elements for establishing a delay claim and the calculation of the damages arising from such claims.[13] Well-drafted construction contracts will also address notice requirements as a prerequisite for any claim for additional compensation under the contract, and how quantum for the delay claim is to be calculated. For example, under FAR 52.211-13, time extensions may only be submitted based on the following:

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9 U.S. ex rel. Salinas Constr., Inc. v. W. Sur. Co., No. C14-1963JLR, 2016 U.S. Dist. LEXIS 88267, at *9 (W.D. Wash. July 7, 2016). *See also* Identifying, Quantifying, and Proving Loss of Productivity, ASCE 71-21 (2021).

10 Identifying, Quantifying, and Proving Loss of Productivity, Standard ASCE 71-21 (2021).

11 *See* FAR 52.235-15 (Schedules for Construction Contracts) (Apr. 1984).

12 *Id.*

13 *See e.g.,* R.P. Wallace, Inc. v. U.S., 63 Fed. Cl. 402 (2004); Manuel Bros., Inc. v. U.S., 55 Fed. Cl. 8 (2002); Morganti Nat'l, Inc. v. U.S., 49 Fed. Cl. 110 (2001).

> (a) If the Contractor requests an extension of the time for substantial completion, the Contractor shall base its request on an analysis of time impact using the project schedule as its baseline, and shall propose as a new substantial completion date to account for the impact. The Contractor shall submit a written request to the Contracting Officer setting forth facts and analysis in sufficient detail to enable the Contracting Officer to evaluate the Contractor's entitlement to an extension of time.
>
> (b) The Contractor shall only be entitled to an extension of time to the extent that-
>
>> (1) Substantial completion of the work is delayed by causes for which the Contractor is not responsible under this contract; and
>>
>> (2) The actual or projected substantial completion date is later than the date required by this contract for substantial completion.
>
> (c) The Contractor shall not be entitled to an extension of time if the Contractor has not updated the project schedule in accordance with the contract.
>
> (d) The Government shall not be liable for any costs to mitigate time impacts incurred by the Contractor that occur less than 30 calendar days after the date the Contractor submits a request for extension of time in compliance with this clause.[14]

## II. Required Documentation

### *A. Documentation for Delays*

Regardless of the method chosen to prove the delay, the party asserting the delay claim has the burden of establishing entitlement on the claim, and the finder-of-fact is entitled to consider whether the claiming party was partially responsible for causing the delay based on the weight of the evidence presented through documentation and testimony.[15] As explained in our prior article on Delays — Part I, a party should first determine what type of delay they are dealing with (critical vs. non-critical, excusable vs. non-excusable, compensable vs. non-compensable) and also understand if the delay they are experiencing is or is not a concurrent delay. Concurrent delays occur "where both parties are responsible for the same period

14 *See* FAR 52.211-13 (Apr. 1984).

15 Newell Machinery Co., Inc. v. Pro Circuit, Inc., 596 S.W.3d 635, 653-654 (Mo. Ct. App. 2020).

of delay,"[16] and when concurrent delays exist, neither party may benefit monetarily from the delay.[17]

If a party determines that they are entitled to some type of recovery for the delay, the party making a claim for delay, such as a contractor, must have the proper back-up to assist in proving its delay claims. Without the proper back-up, contractors will likely be unable to recover all of the additional costs and expenses associated with the delays or, at best, recover only an "equitable" amount. Courts are not justified in fixing damages in the absence of definite proof. Generally, damages must be proved with reasonable certainty and may not be based on speculation or conjecture.[18] Thus, it is crucial for a party to have the proper documentation to support a delay claim, if the goal is to fully recover the damages associated with the delay.

Courts routinely uphold a contractor's decision to demand sufficient backup documentation and other evidence to support a claim for payment, prior to submitting the claim to an owner.[19] To establish delay damages, parties preferably should use the actual project records illustrating all changes, delays, and related costs from the course of the project. The best documentation will include items that are contemporaneous with the delay event(s). Not every project will have the same documentation, as every project is different. To assist in proving a delay claim and related damages, some key documents may include:

- dated progress photos and drone videos;
- daily, weekly, and monthly progress reports created at the time of the delay rather than those that may have been created after the fact;
- project meeting minutes that were distributed to various parties as opposed to draft meeting minutes in a word processing software;
- project schedules and any schedule updates;
- requests for information (RFIs);
- change orders and change order requests;
- construction change directives (CCDs);

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16 Plato Gen. Constr. Corp./EMCO Tech Constr. Corp., JV, LLC v. Dormitory Auth. of State of New York, 89 A.D.3d 819, 826 (App. Div. 2nd Dept. 2011).

17 Otis Elevator Co. v. W.G. Yates & Sons Constr. Co., 2016 U.S. Dist. LEXIS 26748, *30 (N.D. Ala. Mar. 3, 2016) (citing 5 Bruner & O'Conner & O'Conner on Construction Law, § 15:67 (West 2002)).

18 Baker DC, LLC v. Baggette Constr., Inc., 378 F. Supp. 3d 399 (D. Md. 2019).

19 *See generally* In re Central States Mechanical, Inc., Case No. 09-12542, 2011 WL 1637991 (Bankr. D. Kan. Apr. 29, 2011) (collecting cases); Systemaire, Inc. v. St. Charles County, 432 S.W.3d 783 (Mo. App. 2014) (finding a genuine issue of material fact as to what documents were required under the construction documents prior to payment).

- correspondence, such as letters, emails, and texts, between the project team;
- delay logs;
- delay notices;
- payroll records;
- time and material reports;
- diaries and witness statements;
- quality control and inspection reports;
- payment requisitions;
- invoices and receipts for costs incurred due to delays; and
- any other documentation helping to establish the delay.

A best practice of any contractor is to place the owner on notice of delays and to submit all change orders for review and approval before proceeding with extra work that might cause delays. Alternatively, a contractor can continue with the contract work in the face of delays caused by third parties, regardless of whether the contract requires written notice of delays or a delay claim. However, doing so may be at the contractor's risk, as courts will not interfere with the terms of contracts made by competent parties, and generally hold parties to contract terms which require written notice and specific documentation of delay claims and claims for extras.[20]

The lack of documentation may not necessarily bar all claims of delay, however. Depending on the jurisdiction, written modification provisions may be waived orally or by course of dealing. For example, Missouri courts hold that, even if a subcontract requires that all change orders be authorized in writing, the requirement can be waived: "Habitual acceptance of work done on oral change orders in connection with

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20 Razorback Contractors of Kansas, Inc. v. Board of Cty. Com'rs of Johnson Cty., 43 Kan.App.2d 527, 227 P.3d 29 (2010) (rejecting contractor's claim that substantial performance sufficed to preserve its claims, when the contract required written notice of claims for extra to be given to specific entities and within a specified time-period). *See also* T L James & Co. v. Traylor Bros., 294 F.3d 743 (5th Cir. 2002) (applying Louisiana law and denying a contractor's claims for extra work due to contractor's failure to follow terms of the contract and provide notice); In re Central States Mechanical, Inc., Case No. 09-12542, 2011 WL 1637991 (applying Iowa law and denying a subcontractor's delay claims based on the contractor's failure to strictly comply with the contract's provision to provide written notice of delays and delay claims and rejecting the argument that contractor had waived the subcontract's preconditions based on its prior actions). *Compare with* Central Iowa Grading, Inc. v. UDE Corp., 392 N.W. 2d 857, 860 (Iowa App. 1986) (citing Berg v. Kucharo Constr. Co., 237 Iowa 478, 489, 21 N.W. 2d 561, 567 (1946)) (holding that a course of dealing that repeatedly disregards the written change order requirements and promises to pay for work that was orally requested, can be sufficient to waive the subcontract's written change order requirements).

a contract, and payment therefore, results in waiver of a contract clause providing that all orders must be signed."[21]

Because construction project delays are common, project participants such as owners, sureties, and contractors will eventually be faced with some type of delay on a construction project. Thus, it is important to understand the different types of delay and whether or not a delay is compensable. At the same time, it is also important to understand the different delay claim methodologies to understand what information and project documentation will assist in proving entitlement to recovery for damages due to delays. While you may eventually have to retain a delay expert to assist with the claim, it is important to understand delays and delay claims and the evidence required to support such claims so that you can proactively support any such claims.

21 Brockman v. Soltysiak, 49 S.W.3d 740, 745 (Mo. App. 2001). *See also* Missouri Dept. of Transp v. SAFECO Ins. Co., 97 S.W.3d 21, 36-37 (Mo. App. 2002) (holding that the subcontractor had presented sufficient evidence that the general contractor had requested and agreed to extra work and that the subcontractor had performed it, thereby waiving the requirement in the subcontract that all change orders be approved by the contractor in writing).

*Equitable... continued from page 9*

subrogation rights and demanded the City not release funds related to the project without the surety's consent.[7] Despite the notice, the City "approved a settlement and release with Mitchell . . . paying Mitchell and [its] creditors approximately $2 million" for work completed prior to Michell's contract's termination.[8] The circuit court observed that the record did not indicate whether the settlement amount constituted funds received from FEMA prior to the letter from Penn, but it was clear that the total funds received from FEMA were only $1.8 million.[9] Thus, the FEMA funds constituted the contract funds that should have been used to make the surety whole on claims it had paid.[10]

Penn brought suit, and the district court found that equitable subrogation did *not* provide the surety a cause of action against the City—a decision which was reversed by the Eighth Circuit.[11] The appellate court's analysis noted the basic principles of equitable subrogation (under Arkansas law), which allows a surety "to acquire and assert the rights of those parties whom the surety pays."[12] The right exists when the surety's payments achieve "full satisfaction of any underlying debt or obligation."[13]

The Eighth Circuit held Penn had provided the City with sufficient notice of the principal's default, or potential default, such that the City was liable to Penn for release of the contract funds.[14] Additionally, the contract and payment bond "created two relevant obligations: removal of specified debris and payment for labor and materials. The City unilaterally removed the former obligation, so [Penn] was charged with satisfying the latter" (payment) due to the bond—which it did.[15] The appellate court further noted Arkansas and other states recognize when a surety satisfies its obligation under a payment bond, "equitable subrogation permits the surety to proceed against retainage and remaining contract funds for reimbursement."[16] Thus, Penn was entitled to the retainage the City should have held.[17]

The court further explained that "[i]f, after appropriate notice of default, the [City] chooses to pay funds to the general contractor that are or become equitably owed

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7 *Id.*

8 *Id.*

9 *Id.*

10 *See id.*

11 *Id.* at 949–50, 954.

12 *Id.* at 951 (citing Welch Foods, Inc. v. Chicago Title Ins. Co., 17 S.W.3d 467, 470 (Ark. 2000)).

13 *Id.* (citing Am. Sur. Co. of New York v. Westinghouse Elec. Mfg. Co., 296 U.S. 133, 137 (1935)).

14 *Id.* at 954.

15 *Id.* at 951.

16 *Id.* at 952 (citing Equilease Corp. v. U.S. Fid. & Guar. Co., 565 S.W.2d 125, 126 (Ark. 1978); *Pearlman v. Reliance Ins. Co.*, 371 U.S. 132, 139 (1962)).

17 *Pennsylvania Nat'l*, 354 F.3d at 952.

to [Penn], the [City] is liable for the actual loss visited upon" Penn.[18] Consequently, the case was remanded to the district court with directions to enter judgment in favor of Penn.[19]

**b. Ninth Circuit.**

In *United Bonding Insurance Co. v. Catalytic Construction Co.*,[20] the surety, United Bonding Insurance Company ("United Bonding"), provided performance and payment bonds for a subcontractor, Miranti Construction Company ("Miranti"). The subcontractor's work involved multiple contracts for a government project wherein Catalytic Construction Company ("CATCO") was the general contractor.[21] When Miranti notified United Bonding that it could not financially complete the projects, United Bonding financed Miranti to assure completion of the contracts and also paid multiple claims on the payment bonds.[22] United Bonding made a telephone call to CATCO to request funds be withheld from Miranti on all the contracts and to assert its subrogation rights.[23] Based upon instructions from the Atomic Energy Commission and the United States Attorney's Office, CATCO continued to make progress payments to Miranti.[24] By this point, United Bonding had taken "control of the CATCO-Miranti contracts," and advanced money for payroll and "other expenses, and ensured that all of the contracts were fully performed."[25] The record does not indicate whether Miranti had been terminated.[26]

The record indicated that the parties agreed that the equitable right of subrogation applied only to five of the contracts in the case without explicitly stating the basis for such a conclusion.[27] Under those contracts, Miranti was to receive $32,800.00 as of the date of notice from the surety; the balance of $2,430.22 was retained by CATCO.[28] CATCO paid the remaining funds to Miranti and a secured creditor (a bank).[29] Although CATCO called the payments on the other contracts "progress payments," there was evidence that, in fact, those contracts had been completed at the time of the payments.[30]

18 *Id.* at 953.
19 *Id.* at 954.
20 533 F.2d 469, 472 (9th Cir. 1976).
21 *Id.* at 472.
22 *Id.*
23 *Id.*
24 *Id.*
25 *Id.*
26 *See id.*
27 *Id.* at 474.
28 *Id.*
29 *Id.*
30 *Id.* at 475–76.

United Bonding sued CATCO on the theory that CATCO had wrongfully disbursed the remaining funds ($25,000).[31] The district court entered judgment for United Bonding on only one of its claims, which was for the funds still held by CATCO on one contract.[32] The district court rejected the surety's claims to recover funds that had been wrongfully paid to Miranti and the bank on the other contracts. In reaching its decision, the district court primarily relied on an erroneous interpretation of the Assignment of Claims Act.[33] A small judgment was entered in favor of United Bonding for only $2,430.22 "on the basis of a scholarly and comprehensive opinion," in the words of the appellate court.[34]

United Bonding appealed the district court's denial of its claims for the wrongfully paid contract funds.[35] Although the appeal involved several issues,[36] equitable subrogation was ultimately the key issue the court addressed.[37] The surety's general right of subrogation was not challenged. Instead, the court addressed how that right interrelated with the status of the work and whether CATCO "received effective notice of the bond company's rights."[38]

Thus, the question on appeal was "whether CATCO is liable for having paid someone other than United Bonding after receiving notice of the bond company's rights."[39] The court of appeals acknowledged that "United Bonding acquired an equitable right to payments due Miranti under the contracts, to the extent of its net costs."[40] The appellate court stated "[t]his right relates back in time to the bonding agreement and has priority over the rights of the contractor or an assignee."[41] The appellate court, however, then discussed two scenarios where the right of subrogation could be different.[42]

If the contracts had been fully performed by Miranti by the time payment was due, CATCO would have been a "stakeholder faced with conflicting claims of Miranti" and

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31 *Id.* at 474.

32 *Id.* at 472.

33 *Id.* at 472–74; *see also* 31 U.S.C. § 3727.

34 *United Bonding*, 533 F.2d at 472.

35 *Id.*

36 CATCO had made an argument that the assignment from Miranti to United Bonding was void under the Assignment of Claims Act. *See id.* at 472–74. The appellate court rejected the applicability of the Act because the contract was between private parties and not with the United States. *Id.* at 474. The court also noted that, to the extent the surety was relying on the assignment as opposed to equitable subrogation, the surety had to give clear notice of the assignment. *Id.* at 472. These issues were distinct from the court's discussion of equitable subrogation. *See id.* at 472–74.

37 *See id.* at 474–76.

38 *Id.* at 472.

39 *Id.* at 475.

40 *Id.* at 474.

41 *Id.* at 475 (citing Nat'l Shawmut Bank v. New Amsterdam Cas. Co., 411 F.2d 843, 848-49 (1st Cir. 1969)).

42 *See id.* at 475–76.

United Bonding, and "[p]ayment to the contractor would not discharge liability if the surety subsequently established a right to the funds."[43] The appellate court noted that "once a construction project is physically completed, continued payment to the contractor instead of the subrogee is unlikely to be justified."[44]

Conversely, CATCO would not be a "stakeholder" if the project was not complete when it needed to make a progress payment because "[t]he interest in obtaining timely completion of the contracts could give CATCO a legitimate reason" for paying the contractor.[45] In the latter situation, the appellate court noted "the contracting party has discretion to continue paying the contractor and is liable to the surety only for an abuse of that discretion."[46] If CATCO abused its discretion in making payments to Miranti after receiving notice from United Bonding, it is liable.[47]

These two different scenarios also affected the appellate court's evaluation of the notice given by United Bonding.[48] The Ninth Circuit reasoned that "the degree of notice must be balanced against the extent of CATCO's interest in continuing its payments to the contractor."[49] Where projects are physically completed, "the interest in continuing to receive performance is not likely to be substantial; thus a relatively summary notice to CATCO would be sufficient to make it liable to the bond company for subsequent wrongful disbursements."[50] Because the evidence was ambiguous as to whether the Miranti contracts had been completed at the time of the notice, the court remanded with instructions for the district court to determine "which, if any, of the contract payments were made after CATCO received notice that the assignment to United Bonding was effective."[51] As the case was being remanded, the appellate court did not address the validity of the payment to Miranti's bank.[52]

*United Bonding* offers valuable insights when a surety is acting in response to notice from its principal of an impending default and takes steps such as financing to support the principal. First, the surety should clearly notify the obligee, in writing, of the surety's actions and subrogation rights. For contracts still in progress, the surety should also notify the obligee of the actions that the surety is taking to complete the work by supporting its principal, and demand the progress payments be made to the surety.

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43 *Id.* at 475.
44 *Id.* at 476.
45 *Id.* at 475.
46 *Id.*
47 *Id.* at 476.
48 *See id.* at 475–76.
49 *Id.* at 476.
50 *Id.*
51 *Id.*
52 *Id.*

### c. Eleventh Circuit.

In a case from the Eleventh Circuit, the surety, National Fire Insurance Company of Hartford ("NFIC"), issued performance and payment bonds on behalf of Arkin Construction Company ("Arkin"), a subcontractor to the general contractor, Fortune Construction Company ("Fortune").[53] Arkin defaulted; Fortune and NFIC attempted to resolve how the projects would be completed.[54] There was "a flurry of letters between attorneys for Fortune and [NFIC]" in which the parties disputed the obligations each owed the other.[55] NFIC "made payments to payment bond claimants on both projects" and both projects were "completed by Fortune as the general contractor."[56] Fortune sent NFIC "an accounting of its 'performance' costs to complete the Arkin subcontracts."[57] NFIC responded with "an accounting of the net remaining contract proceeds," which NFIC contended "exceeded Fortune's costs of completion" and thus Fortune owed NFIC a credit for the difference.[58]

NFIC sued Fortune for, among other things, equitable subrogation.[59] The district court entered summary judgment for NFIC and held that it "had a right to equitable subrogation 'under the payment and performance bonds,'" and the "right to the contract balances was superior to Fortune's right to set off its claims against Arkin."[60] The lower court held that "to the extent the contract balances exceeded Fortune's reasonable costs to complete construction. . . 'the excess is to be paid to [NFIC] up to the amount of [NFIC]'s payment bond expenditures.'"[61]

Fortune appealed.[62] The court of appeals looked to the applicable Florida law, which stated "a performance and payment bond surety's rights to equitable subrogation depend upon the nature of the obligation fulfilled by the surety under the terms of the bonds."[63] The appellate court also looked to the precedent from the First and Fifth federal circuit courts, both of which had previously acknowledged the right of a surety to subrogation.[64] The Eleventh Circuit held that, in a case where

53 Nat'l Fire Ins. Co. of Hartford v. Fortune Const. Co., 320 F.3d 1260, 1263 (11th Cir. 2003).

54 *Id.* Arkin eventually dissolved which left negotiations mainly between Fortune and NFIC. *Id.* at 1263–64.

55 *Id.* at 1263.

56 *Id.* at 1263–64.

57 *Id.* at 1265.

58 *Id.*

59 *Id.*

60 *Id.*

61 *Id.* at 1266. The circuit court reviews summary judgment rulings de novo. *Id.* at 1267.

62 *Id.* at 1267–68.

63 *Id.* at 1269.

64 *Id.* at 1269–71; *see Transamerica Ins. Co. v. Barnett Bank of Marion County*, 540 So.2d 113, 115–16 (Fla. 1989) (citing Nat'l Shawmut Bank v. New Amsterdam Cas. Co., 411 F.2d 843, 844–45 (1st Cir. 1969)); *see also* Trinity Universal Ins. Co. v. United States, 382 F.2d 317, 318–21 (5th Cir. 1967).

surety must perform or provide payment under performance and payment bonds, "the surety's subrogation rights exist only to extent of the surety's performance" or fulfillment of such payment obligations.[65] As NFIC disbursed payment to laborers and materialmen for work on the projects but did not perform according to the performance bond, "it [had] acquired equitable subrogation rights only with respect to its payment bonds."[66] The court concluded that such subrogation rights would not give the surety priority to receive contract funds that the obligee actually used to complete the work.[67]

Like *United Bonding*, *Fortune* addressed the different subrogation rights a surety might obtain by acting under a payment bond versus a performance bond.[68] A surety who elects not to perform under both the performance and payment bonds might end up with less comprehensive subrogation rights to the contract funds if the obligee is required to finish the bonded contract.

### *2. Surety Did Not Acquire Equitable Subrogation Rights*

#### a. D.C. Circuit.

The case from the D.C. Circuit Court of Appeals, *American Fidelity Co. v. National City Bank of Evansville*, represents the limits of a surety's subrogation rights. Regent Contracting Company ("Regent") contracted with the Federal Government to construct a steam plant.[69] The sureties, American Fidelity Company ("AFC") and New Hampshire Fire Insurance Company ("NHFI"), provided bonds for the project.[70]

Regent "executed a loan agreement to [t]he National City Bank of Evansville" (the "Bank") and assigned to the Bank progress payments from the project to secure the loan,as authorized by the Assignment of Claims Act,[71] and stated "that it would obtain a subordination agreement from the sureties," of which the Government and the sureties were given notice.[72] Subsequently, the sureties did not agree to subordinate their interests, and AFC's attorney sent the Bank a letter "claiming 'equitable rights in the contract proceeds superior to the assignment which has been given to you by the contractor.'"[73]

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65 *Fortune,* 320 F.3d at 1270.
66 *Id.* at 1271–72.
67 *Id.* at 1272.
68 *See id*; *see also United Bonding*, 533 F.2d at 472–76.
69 Am. Fid. Co. v. Nat'l City Bank of Evansville, 266 F.2d 910, 912 (D.C. Cir. 1959).
70 *Id.*
71 *Id*; *see* 31 U.S.C. § 3727; *see also* 41 U.S.C. § 6305.
72 *Am. Fid. Co.,* 266 F.2d at 912.
73 *Id.* at 913.

Pursuant to the Assignment, the Government made three progress payments to the Bank. After these payments were made, Regent's contract was terminated and the Government contracted out the rest of the project.[74] Of course, the completion of the project resulted in additional costs, which the sureties paid.[75] The sureties also paid out funds under the payment bond for labor and materials left unpaid by Regent.[76]

After a series of lawsuits, the cases were consolidated in the D.C. federal court.[77] In the consolidated case, the Bank's complaint and the sureties' counterclaim were dismissed, but judgment for the Bank was entered against Regent for $89,530 plus interest.[78] The district court concluded that, as a result of the Act, the sureties, as a matter of law, "could not recover from the [B]ank the three progress payments made to it by the Government under the assignment," and that the progress payments were not received by the [B]ank with an attached "equitable lien or trust in [the sureties] favor to the extent they had been forced to pay under the bonds."[79]

The sureties appealed and presented the issue of whether the sureties "on the contractor's performance and payment bonds [could] recover such payments from the [B]ank to reimburse them for sums paid by them because the contractor defaulted after the [B]ank had collected the progress payments."[80] The sureties argued that the lower court erred when it failed "to hold that the three progress payments were received by the [B]ank impressed with an equitable lien or trust in their favor to the extent they have been forced to pay under the bonds."[81]

The court of appeals affirmed.[82] While the sureties argued for an "equitable lien," the appellate court concluded that the "lien" is, in reality, the right of subrogation.[83] The court acknowledged the doctrine of subrogation and held that a payment bond surety on a Government contract who "makes a payment thereunder to suppliers of labor or material. . . is subrogated to the rights and preferences of such suppliers as to sums due or to become due under the contract; and again the subrogation relates back to the date of the bond."[84]

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74 *Id.*
75 *Id.*
76 *Id.*
77 *Id.* at 913.
78 *Id.*
79 *Id.* at 913–14.
80 *Id.* at 912.
81 *Id.* at 913–14.
82 *Id.* at 917.
83 *Id.* at 914–15.
84 *Id.*

Ultimately, the appellate court ruled the Act preempted the sureties' ability to recover against the Bank because the assignments were legitimate.[85] Based upon the plain language of the Act, as the government could not recover against the Bank under the Act, neither could the surety.[86]

While the sureties would be entitled to subrogation against others for the amounts they paid for the benefit of the contractor under the payment bond,[87] the appellate court concluded, as to the claim against the Bank, that "neither the Government, the contractor, nor those who furnished labor or materials could recover" against the Bank on the assignments.[88] As a result, "there was no right to or claim against those payments to which the sureties could be subrogated. . . ."[89] Consequently, the lower court was affirmed.[90]

There are a few takeaways from the case. First, the assignment to the Bank was authorized by the Assignment of Claims Act. Here again, timing is everything. The three payments to the Bank were made prior to the default and prior to the time the surety incurred either payment or performance bond losses. Here, the surety was suing to recover the pre-loss payments under the relation back aspect of equitable subrogation, including its notice of subrogation rights it sent to the Bank even before any progress payments were made. As this case demonstrates: (1) the surety's subrogation rights are inchoate until the actual loss occurs; (2) the surety steps into the shoes of the owner on the performance bond loss and into the shoes of the laborers and materialmen on the payment bond loss; (3) existing prohibitions on recovery at the time of the loss also are limitations on the surety's rights; (4) for the performance bond losses, the Assignment of Claims Act precluded the Government (whose shoes the surety stood in) from recovering from the Bank; and (5) for the payment bond losses, the laborers and materialmen (whose shoes the surety stood in) would never have had a right to recover against the Government or a third party such as the Bank that received the funds under a lawful assignment.

At the same time, the case reflects that the doctrine of "relation back" is not a magic bullet, and parties might take steps after bonds are issued—but before a loss occurs that "vests" subrogation rights—that create legal bars to a surety's exercise of subrogation rights. It is noteworthy that the surety's notice to the Bank, which

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85 *Id.* at 914, 916.

86 *Id.* at 916.

87 *Id.*

88 *Id.*

89 *Id.*

90 *Id.* at 917.

was made before the Bank received any funds and before the surety had incurred any losses, was not sufficient to make the Bank's rights to the funds under the assignment inferior to the surety's subrogation rights.

## III. Conclusion.

A close reading of the cases demonstrates that payment or a risk of payment by the surety is the first step in effectuation of its rights. Although the common law right of subrogation seems to be well established in favor of the surety, it would appear that early annunciation to the owner of the surety's rights is the key to protecting the surety's entitlement to subrogation, provided the surety has made payment or otherwise performed.[91]

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91 Great Am. Ins. Co. v. Norwin Sch. Dist., 544 F.3d 229 (3rd Cir. 2008) is a case with issues beyond the scope of this article but is worth a mention. At first glance, the case appears to be relevant to the discussion. However, the surety, owner, and principal settled their claims related to the Surety's subrogation rights prior to trial and the appellate case turns on whether the trial court's decision to not admit evidence of the settlement was error. *Id.* at 242.

*Fighting Back... continued from page 10*

address bad faith actions by the debtor during the bankruptcy or within a year before the bankruptcy that are designed to circumvent the bankruptcy process and give the debtor more than they are entitled to under the Bankruptcy Code. These generally include fraudulently transferring, misusing, or concealing property of the estate (or of the debtor within the last year); withholding or falsifying financial information or documents; making false statements in connection with the bankruptcy; making or receiving payments to influence actions relating to the bankruptcy; failing to explain a loss or deficiency of assets; or improperly failing to obey orders of the court.[3]

Grounds for objecting to discharge in the surety context can arise in a number of ways. Most common is some attempt by a principal or indemnitor to hide assets from the bankruptcy process by failing to make full disclosures, whether through simply failing to disclose assets being held, or attempting to conceal assets through transfers or undisclosed arrangements. For an objection to discharge to be sustained on these grounds, the surety will typically need to show that a false statement was knowingly made with the intent to defraud and was material to the bankruptcy case.[4]

As a practical matter, establishing that a debtor is hiding assets is often not an easy task. It will be important to carefully review and compare what is disclosed by the debtor voluntarily in the bankruptcy with the information that can be discerned from the records collected through investigation, underwriting, and discovery. Failure to disclose or be able to explain large bank transfers or disbursements—particularly in self-dealing situations—should be considered a red flag. Sureties should also be aware of whether equipment, machinery, materials, or facilities simply "disappear" either through an undisclosed sale or by being "acquired" by a new entity without any formalities or consideration. Other potential concerns include things like accumulation of large amounts of cash or spending that is lavish or inconsistent with reported income.

### B. Objection to Dischargeability

Section 523 of the Bankruptcy Code identifies certain types of debts that are non-dischargeable based on how the debt arose, including debt obtained by or resulting from: fraud or false pretenses (except as to the debtor's financial condition) under part (a)(2); fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny under part (a)(4); and willful and malicious injury or property damage under part (a)(6).[5]

Potential objections to dischargeability can also come up for sureties in a number of ways. For example, complaints of a principal absconding with project materials

3 *See* 11 U.S.C. § 727(a)(2)-(6) (2024).

4 *See, e.g.*, *In re Beaubouef*, 966 F.2d 174, 178 (5th Cir. 1992).

5 *See* 11 U.S.C. § 523(a)(2)-(6) (2024).

that are the property of the owner are not unheard of, and the surety is often required to foot the bill for the replacement. Depending on the situation, those costs may be nondischargeable to the extent that they are found to be a result of larceny or fraud. In a similar vein, after a contentious dispute, the principal may intentionally damage materials or work already in place while walking off a project. Again, the costs to repair or replace that damage may implicate the property damage exception to discharge.

Another common consideration for sureties is whether project funds have been misappropriated in some manner that could be construed as fraud or defalcation while acting as a fiduciary. The first question will be whether the principal was acting as a fiduciary for the surety. Bankruptcy courts have tended to require a formal fiduciary arrangement as opposed to quasi-fiduciary relationships that commonly occur when acting on behalf of another.[6] In the surety context, the key to meeting the fiduciary requirement will typically be the trust provision language in the indemnity agreement which is relatively standard.

The second element is establishing that the debt arose from fraud or defalcation. "Defalcation" is not defined by the bankruptcy code, but in this context generally means misuse or misappropriation of funds by someone who has a legal financial duty, such as a trustee. Generally, the term defalcation is broader than fraud and can include misuse resulting from negligence, which resulted in a longtime split among the circuit courts on whether negligent defalcation by itself was sufficient for nondischargeability. However, the Supreme Court has now clarified that a showing of wrongful intent, reckless conduct, or gross deviation from the ordinary standard of conduct is required for all of the wrongful acts set out in 523(a)(4).[7]

In the surety context, a number of courts have found that misuse of project funds amounts to defalcation of while acting as a fiduciary when there is express trust agreement language in the indemnity agreement.[8] A surety or its counsel should also check to see if the jurisdiction has a trust fund statute which provides that contractors receiving contract balances hold those funds in trust for its suppliers or subcontractors. However, given the Supreme Court's clarification that defalcation requires a showing of wrongful intent, it will be important for a surety intending to assert this objection to gather sufficient evidence to establish that the principal's misuse of funds was performed knowingly or that there was some element of recklessness or gross deviation from the standard of care involved.

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6 *See* In re Blair, 569 B.R. 224, 229 (Bankr. M.D. Pa. 2017) ("It is generally held a '[c]onstructive or implied trust or trust ex maleficio is not sufficient to create [a] fiduciary relationship within [the] meaning of 11 U.S.C.A. § 523(a)(4).'"

7 *See* Bullock v. BankChampaign, 569 U.S. 267 (2013).

8 *See, e.g.*, In re Herndon, 277 B.R. 765, 769 (Bankr. E.D. Ark. 2002).

## II. Tools for the Investigation

Armed with a better idea of the types of information to look for, the next question is how to obtain the evidence needed to support these objections. In the surety context, the investigation often begins before a bankruptcy is even filed. Information about the principal and indemnitors can and should come from thorough underwriting and regular requests for updated financials. Also, when a surety gets involved with a project over concerns about a potential default, gathering project records and financials is an important step to both identify potential issues that may already be occurring and to establish a baseline of the financial scenario. If the indemnity agreement in place has a books and records clause, this is a good time to consider making a formal request, particularly if the surety is being asked to facilitate completion in some manner.

Once the bankruptcy process begins, additional tools for investigation become available. Debtors are required to file bankruptcy schedules and a statement of financial affairs that are designed to elicit a relatively complete snapshot of the debtor's financial situation at the time bankruptcy was filed. The 341(a) meeting of the creditors is also helpful for gathering initial information and is typically scheduled three to seven weeks after the petition date.[9] The meeting will be led by the trustee or the trustee's counsel, but creditors or their counsel are also given an opportunity to ask the debtor questions directly.

Additional information can be also gathered under Rule 2004 of the Federal Rules of Bankruptcy Procedure, which provides that, on a motion from any party in interest, the court may order an examination of the debtor or any other entity relating "to the acts, conduct, or property or to the liabilities and financial condition of the debtor, or to any matter which may affect the administration of the debtor's estate, or to the debtor's right to a discharge."[10] When relevant, "the examination may also relate to the operation of any business and the desirability of its continuance, the source of any money or property acquired or to be acquired by the debtor for purposes of consummating a plan and the consideration given or offered therefor, and any other matter relevant to the case or to the formulation of a plan." The bankruptcy court may decide the motion *ex parte* or may require a hearing. If the court approves and orders the examination, the procedure for compelling attendance is similar to the standard federal subpoena procedures.

## III. Procedural Considerations

Objections to discharge and dischargeability may be brought by a creditor or the trustee and are made through the filing of a complaint to initiate an adversary proceeding in the court where the bankruptcy is pending. For the relevant objections to dischargeability,

9 *See* 11 U.S.C. § 341(a) (2024).

10 *See* Fed. R. Bankr. P. 2004.

a complaint must be filed no later than sixty days after the first date set for the meeting of creditors under 341(a).[11] A motion to extend this deadline can be filed before the deadline runs, but requires a showing of cause by the party seeking an extension. One point to note is that once an adversary proceeding is commenced, the Bankruptcy Code allows for use of standard discovery requests without prior approval from the Court.

The process and deadline to file a complaint to object to discharge will depend on the type of bankruptcy case. In a Chapter 11, the deadline is the first date set for the hearing on confirmation.[12] In a Chapter 7 or 13 case, the deadline is sixty days after the first date set for the meeting of creditors under 341(a).[13] Motions to extend should again be brought before the deadline has passed; however, in contrast to the procedures for objecting to dischargeability, Bankruptcy Rule 4004 expressly provides that a creditor may seek an extension to object to discharge after the deadline has passed based upon the discovery of new facts that provide a basis for denying discharge.

## IV. Conclusion

Objections to discharge and dischargeability are useful tools to address situations where a principal or indemnitor is attempting to abuse the bankruptcy process. However, raising these objections successfully often requires a detailed investigation that preferably begins long before the bankruptcy petition is filed. In situations where fraud or misappropriation might be a concern, retaining counsel early in the process may prove helpful.

11 *See* Fed. R. Bankr. P. 4007.

12 *See* Fed. R. Bankr. P. 4004(c).

13 *See* Fed. R. Bankr. P. 4004(a).


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*Grain Bond... continued from page 11*

damages and keep sufficient stores.[3] If the producer later returns to retrieve the grain, the grain bin must have sufficient grains on hand to cover the deposit to the producer. In this way, the deposit records kept by the facility operator are incredibly important.[4]

Each state has its own requirements, governed by statute, for the issuance of a license to the storage facility operators. Those requirements include the demonstration of a minimum financial responsibility by the operator, and usually the issuance of a bond or irrevocable letter of credit to cover the deposits made by grain producers.

State departments of agriculture are given police powers to protect the public interest of the producers. Many states empower the committees or boards of the agriculture department to take control of the facilities and appoint receivers to distribute the assets of the facility, which can include the stored grains, letters of credit, bank deposits, and the bonds. The bonds obtained by the facility operator are issued for the benefit of the state and the facility operator is named as the principal.

Upon receipt of the notice of the bond claim, the surety practitioner should obtain the agreement of indemnity, the bond, and the records gathered by the state's administrative authority to determine the validity of the claim or claims against the bond. Interviews are often obtained by the administrative authority, and independent investigation into the principal's record keeping and practices is warranted. The principal's bank records should also be reviewed.

## III. Indemnity Agreements

In exchange for the issuance of a grain bond, the principal will typically execute a general agreement of indemnity ("GIA"). The GIA obligates the principal to indemnify the surety against all liability for losses, costs, damages, and expenses of whatever kind or nature, including attorney's fees, that the surety may incur as a result of having issued bonds or as a result of the principal's breach of the GIA. The principal is obligated to procure the release of the surety as against any claims on a bond, and if the principal fails to obtain release of the claims, the surety may proceed in its discretion to procure or attempt to procure its discharge. The principal is obligated to provide sufficient collateral upon demand of the surety, and the surety may use the collateral at any time to compromise or pay any claim, judgment, liability, or loss. The surety also has the exclusive authority to determine whether any claim,

3 U.C.C. §7-204

4 Peter E. Karney and John F. Fatino, *The Surety Relationship in Agricultural Commodity Storage Context and Grain Indemnity Funds: A Jurisdictional Survey,* 40 Creighton L. Rev. 41, *45 (2006).

suit, or judgment shall be paid, compromised, defended, or appealed. The surety is sometimes bound to make this determination upon a "reasonable belief of liability."[5]

The surety practitioner will find familiarity in the GIA and the remedies provided therein. However, the practitioner must also carefully examine the laws, including agricultural regulations, of the jurisdiction where the claim arises to determine the proper procedures and the methods it uses to investigate, evaluate, and discharge the claim.

## IV. Bonds

Grain bonds typically follow a prescribed form issued by the states. The bonds name the facility operator as principal and declare the penal sum of the bond. The bond binds the principal and surety to the state for "the benefit of all persons, firms, corporations or associations interested" in the amount of the penal sum of the bond.

The conditions of the bonds are such that, if the principal shall faithfully perform all of the duties of a licensed public warehouseman and if the principal complies with all of the obligations of the local state laws, then the obligations of the bond shall be void.[6] Other state forms for grain dealers vary slightly, conditioning the bond upon principal's breach of "one or more credit sale contracts issued under the principal's grain dealer license."[7]

Here the surety practitioner will find familiarity with the form of bond, which does not differ in material ways from a typical statutory bond used to discharge a mechanic's lien. But again, state statutes often dictate the surety practitioner's next steps and must be carefully observed.

## V. Sample State Statute Comparisons

### *A. Missouri*

Missouri Revised Statute § 411.275 sets forth the licensing and bond requirements for warehouse facility operators in Missouri.[8] Missouri Revised Statute § 411.275(1) requires the facility operator to "file a bond other than personal security with the director executed by the warehouseman as principal and by a corporate surety."[9]

5 The provisions referenced in this section have been found in a cross-section of indemnity agreements reviewed in this context.

6 Mo. Ann. Stat. § 411.275 (West 1986).

7 Iowa Department of Agriculture, Grain Dealer Bond Form (2024), https://iowaagriculture.gov/forms-and-licensing (Forms available upon request.)

8 *See* Mo. Ann. Stat. §411.275 (West 1986).

9 Mo. Ann. Stat. §411.275(1) (West 1986).

The bond "shall be in favor of the state of Missouri for the "benefit of all persons storing grain" and "conditioned upon the faithful performance of (his or her) duties" relating to the storage of grain.[10]

Missouri Revised Statute § 411.275(7) is the most interesting provision in this statute, and the section that must be most closely observed. It states that, upon demand of the Director of the Department of Agriculture (or designated representatives), the "surety shall either pay over to the director the sum demanded up to the full face amount of the bond or shall deposit the sum demanded in an interest-bearing escrow account at the highest rate of interest available."[11] The Director then interpleads the funds into court or holds an administrative hearing "to determine the liability of the surety."[12] Most critically, the surety has only **ten days** from the date of demand to pay over the sum demanded or the entire penal sum of the bond. Failure to do so is grounds for the "withdrawal of the surety's license and authorization to conduct business in this state" or grounds for "the court to penalize the surety for refusal to pay or to deposit, within the ten days of demand, in the amount of twenty-five percent of the full face amount of the bond, plus interest at the rate of nine percent, or at the rate that the director can establish he would have received had the money been paid or deposited by the surety, whichever rate of interest is higher."[13]

If the warehouse facility operator is a licensed grain dealer, there may be separate bond requirements pursuant to Missouri Revised Statute § 276.426.[14] A grain dealer is one that is essentially buying grain and taking title to the grain at the time of purchase. Under the state regulatory scheme, the facility operator is obligated to pay for the delivered grain either at the time of delivery or upon later demand of the producer.[15] If the facility operator becomes insolvent, the bond may provide protection for producers damaged by the insolvency. The statute has similar bond requirements as a warehouseman's bond. Notably, Missouri Revised Statute. § 276.426(6) obligates the surety issuing the grain dealer's bond to pay over or escrow the demanded sum to the Director within 10 days of demand.[16] The statute creates the potential for the withdrawal of licensing in the state and the same penalties as set forth above.

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10 *Id.*

11 Mo. Ann. Stat. §411.275(7) (West 1986).

12 *Id.*

13 *Id.*

14 The formula for determining the minimum amount of a Grain Dealer's Bond can be found in R.S.Mo. §276.436.

15 In Missouri, licensed Class I grain dealers may enter into deferred price contracts, and sellers of grain under these contracts have no right to recovery under the Grain Dealer's Bond, assuming the deferred price contact was properly executed. *See* Mo. Ann. Stat. § 411.275(7) (West 1986).

16 *See* Mo. Ann. Stat. § 411.275(7) (West 1986).

In operation, the Director will send written demand to the surety under one or both of these statutes, giving the surety **ten days** to pay over the penal sum of one or both of the bonds. This demand will typically occur after warehouseman[17] or grain dealer license revocation and after the principal's administrative appeals have been exhausted. Often, the principal is represented by independent counsel throughout the administrative process.

The surety must then provide the sums to the Director or face statutory penalties. The state agent or general counsel for the department of agriculture will typically provide the documents and materials from the state's investigation for review, and the surety practitioner will perform an independent investigation into the claims. An administrative hearing will be held to determine the surety's liability under the claims, and all or a portion of the penal sum of the bond or bonds will be refunded based on the administrative body's determination.

### *B. Kansas*

In Kansas, the bond requirements for facility operators can be found in Kansas Statutes Annotated § 34-229. This statute sets the minimum bond amounts based on the licensed capacity of the facility. For example, if such capacity is one million bushels, the bond must be in the amount of $0.20 per bushel.[18] The bond is conditioned on the faithful performance of the licensed facility operator's duties, and any producer damaged by the facility operator may bring suit on the bond.[19]

A notable feature of the Kansas statute is that if the producer prevails in litigating its claim against the surety, and the court has found that the surety refused to pay the bond claim without just cause, the producer may be entitled to recover its attorney's fees.[20] The surety practitioner should take heed of that provision in the statute and carefully evaluate the claim or claims to ensure that just cause exists before denying the claim or risk the imposition of collection fees at the end of the litigation.

The facility operators should keep meticulous records because, upon demand of the state agency, the facility operator must be able to produce records related to the deposit receipts that it has received and cancelled, its grain liabilities, the total unencumbered grain in its facility, and the total amount of grain stored.[21] These same records will be critical in the surety practitioner's review of any claims made upon the bond.

17 The author acknowledges the lack of inclusiveness in this traditional use of this term and the fact that this term is imbedded in the various state statutes.

18 *See* Kan Stat. Ann. § 34-229(a) (West 2000).

19 *See* Kan Stat. Ann. § 34-229(c) (West 2000).

20 *See* Kan Stat. Ann. § 34-229(g) (West 2000).

21 *See* Kan Stat. Ann. § 34-249a (West 2011).

Kansas has a statutory provision dealing with lost receipts that may give rise to the issuance of a bond provided by the producer.[22] Upon depositing grain into the facility, the producer is given a deposit receipt (that is either negotiable or non-negotiable) and that receipt must be surrendered by the producer when the grain is retrieved from the facility.[23] If the producer loses the receipt, or if the receipt is destroyed, they may obtain a "duplicate" receipt from the facility operator.[24] To obtain a duplicate receipt, the producer must provide an affidavit verifying that they did lawfully possess the deposit receipt, that it has not been assigned, how it was lost, and their efforts to locate the deposit receipt.[25] The producer must also provide a bond with a penal sum that is twice the value of the grain represented by the lost or destroyed receipt.[26] The bond related to a lost receipt protects the facility operator from any loss, liability, or expenses the facility operator may incur as a result of having issued the duplicate receipt.[27]

The surety issuing a bond can become liable under the bond if the facility operator is guilty of neglect in storing the grain and the perishable grain becomes "out of condition."[28] Producers holding valid deposit receipts may make a claim under the bond and join other claimants to that action.[29]

If the secretary of the Department of Agriculture determines upon inspection that the facility operator does not have sufficient grain to cover its outstanding receipts or sales tickets, the secretary may demand that the facility operator cover the shortage or provide additional bonds to cover the shortage.[30] If the facility operator fails to do so within twenty-four (24) of the demand, the secretary can petition the court for possession and control of the stored grain and records.[31] The statute also provides for the appointment of a receiver. The secretary may retain control of the property and the records until such time as the surety satisfies all claims made under the bond.[32]

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22 *See* Kan Stat. Ann. §34-257a (West 1997).

23 *See* Kan Stat. Ann. §§ 34-254 & 34-255 (West 1970).

24 *See* Kan Stat. Ann. § 34-257 (West 1997).

25 *Id.*

26 *Id.*

27 *Id.*

28 *See* Kan Stat. Ann. § 34-237 (West 2000).

29 *See* Kan Stat. Ann. § 34-273 (West 2000).

30 *See* Kan Stat. Ann. §§ 34-2,104 (West 2000).

31 *See* Kan Stat. Ann. §§ 34-2,104 (West 2000); Pursuant to Kan. Admin. Regs. § 4-25-2 (2022), a facility operator is obligated to retain the records for six (6) years from the scale tickets, evidence of cancelled checks, customer ledgers, records of daily grain position, insurance records, and warehouse receipts. These are the type of documents the surety practitioner can expect to receive and inspect when analyzing bond claims.

32 *See* Kan Stat. Ann. §§ 34-2,104 (West 2000).

Finally, if a judgment is rendered against the surety that has issued the bond, and it is found that the that the surety refused to satisfy the claim without just cause, there can be negative implications for the surety. The claimant, having prevailed in the action, can also recover reasonable attorney's fees as part of their costs.[33]

### *C. Iowa*

Iowa grain dealers are licensed pursuant to Iowa Code Chapter 203, which sets forth different minimum standards of financial responsibilities for various classes of dealer licenses. For instance, a Class 1 dealer must maintain a minimum net worth of at least $75,000.00.[34] If a Class 1 dealer cannot meet the minimum financial requirements, they may obtain a deficiency bond in the amount of $2,000.00 for each $1,000.00 of deficiency.[35]

Iowa follows a regulatory scheme where the legislature established the Grain Depositors and Sellers Indemnity Fund (the "Fund").[36] All licensed grain dealers and licensed warehouse operators must participate in the Fund.[37] The Fund collects fees from license applications, per-bushel fees paid by licensed grain dealers, and delinquency penalties.[38]

The Fund is used to indemnify producers and sellers, and claims against the Fund are regulated pursuant to Iowa Code Annotated § 203D.6. The Grain Indemnity Fund Board (the "Board") reviews and determines claims.[39] If the Board determines that a claim is eligible for payment, the Board will issue payment from the fund for 90% of the claim, with a $300,000.00 cap.[40]

A grain dealer in Iowa that enters into credit-sales contracts must also post a bond pursuant to Iowa Code Annotated § 203.15. The bond must be in the amount of $100,000.00 and is payable to the Iowa Department of Agriculture. The bond is used to indemnify sellers in the event of a breach of the credit-sales contract.[41]

The existence of the Fund may limit the surety practitioner's role in Iowa in that producers make their claims directly to the Board. However, there may be instances where the surety practitioner is called upon to defend claims made for breach of a credit-sales contract.

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33 *See* Kan Stat. Ann. §§ 34-229(g) (West 2000).
34 Iowa Code Ann. § 203.3(4)(a) (West 2008).
35 Iowa Code Ann. § 203.3(4)(d)(1) (West 2008).
36 Iowa Code Ann. § 203D.3 (West 2023).
37 Iowa Code Ann. § 203D.2 (West 1993).
38 Iowa Code Anan. § 203D.3.2 (West 2023).
39 Iowa Code Ann. § 203D.4.2 (West 2023).
40 Iowa Code Ann. § 203D.6.8 (West 2012).
41 Iowa Code Ann. § 203.15(4) (West 2023).

### *D. Nebraska*

Nebraska sets forth different bond requirements for grain warehouse operators and grain dealers. The grain warehouse operator requirements are set forth in Nebraska Revised Statutes § 88-530. The grain dealer obligations are set forth in Nebraska Revised Statutes § 75-903. Both statutes require the facility operator to provide a bond or irrevocable letter of credit.

The Nebraska regulatory scheme requires that producers make a claim against the facility operator's security by providing notice of the claim to the Nebraska Public Service Commission within 10 days of the apparent loss.[42] The statute requiring the notice to the Public Service Commission is a bar to claims against the facility operator's security, and the surety practitioner should pay careful attention to the claims period when evaluating claims.

## VI. Conclusions

The surety practitioner accustomed to reviewing more traditional indemnity agreements and bonds will find many similarities when first reviewing indemnity agreements and bonds related to the grain warehouse trade. Upon reviewing the indemnity agreement and bond, the surety practitioner should seek out and review the state statutes and regulations related to warehouse and grain dealer licensing and bonding. Each state has its own peculiarities and regulatory schemes. The surety practitioner will find that agents of the state will be of great assistance gathering the documents needed to evaluate the claim.

The surety practitioner should interview the principal and gather other facts and documents needed to evaluate the various claims. Deposit receipts and grain storage reports will be critical during the initial review, but often it is apparent that the facility operator has become insolvent, and application of the bond proceeds is required. In many cases, the facility operator will have already taken part in the administrative review process. In any event, careful consideration of the state statutes must be given to ensure that the surety client does not run afoul of the state statutory requirements.

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42 Neb. Rev. St. Ann. § 75-906 (West 1985); *see also* *Fecht v. Quality Processing, Inc.*, 244 Neb. 522, 525, 508 N.W.2d 236, 238 (1993).

## Calendar

| | | |
|---|---|---|
| February 20-22, 2025 | **Insurance Coverage Litigation Conference**<br>Contact: Janet Hummons – 312/988-5656<br>Yasmin Koen – 312/988-5653 | **Estancia La Jolla Hotel**<br>La Jolla, CA |
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| March 13-15, 2025 | **Transportation Mega Conference**<br>Contact: Janet Hummons – 312/988-5656 | **Hilton New Orleans Riverside**<br>New Orleans, LA |
| March 13-15, 2025 | **Admiralty Disruption 2025**<br>Contact: Theresa Beckom – 312/988-5672 | **Hilton New Orleans Riverside**<br>New Orleans, LA |
| April 23-25, 2025 | **Motor Vehicle Product Liability Conference**<br>Contact: Janet Hummons – 312/988-5656<br>Yasmin Koen – 312/988-5653 | **Omni Scottsdale Montelucia**<br>Scottsdale, AZ |
| May 7-10, 2025 | **TIPS Section Conference**<br>Contact: Janet Hummons – 312/988-5656<br>Theresa Beckom – 312/988-5672 | **Capital Hilton**<br>Washington, DC |
| May 22-24, 2025 | **Fidelity & Surety Law Spring Conference**<br>Contact: Janet Hummons – 312/988-5656<br>Yasmin Koen – 312/988-5653 | **Wild Dunes Resort**<br>Isle of Palms, SC |
| June 2025 | **TIPS/ABOTA National Trial Academy**<br>Contact: Janet Hummons – 312/988-5656 | **National Judicial College**<br>Reno, NV |
| August 6-12, 2025 | **ABA Annual Meeting**<br>Contact: Janet Hummons – 312/988-5656<br>Theresa Beckom – 312/988-5672 | **TBD**<br>Toronto, CA |