

PAYMENT BOND SURETY HELD LIABLE FOR ATTORNEY FEES

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In what is generally viewed as the exception rather than the rule, a unanimous panel of a New York appellate court held that a subcontractor could recover interest and attorneys' fees from the Payment Bond Surety.

Section 137(4)(c) of the State Finance Law provides, in part, that a court may (i.e. within its discretion) award attorney's fees to either party when, upon review of the entire record, it appears that either the original claim or the defense interposed to such claim is without substantial basis in fact or law.

In this case, a subcontractor sought to collect from the payment bond surety the value of a change order work it performed for the general contractor on a New York City Transit Authority project. The surety denied the claim. We (and the Court) believe unreasonably, hopelessly maintaining that the change order work was of such a nature that it was "not fairly within the contemplation of the parties at the time of the original underlying contract was made...", and thus no labor and materials for the change order was covered under the payment bond.

Bad faith claims against the sureties are an ugly business, and, in any event, counterproductive since New York law is extremely "conservative" in this regard and almost never countenances on finding compensable bad faith against a surety. However, the award of attorney's fees on a payment bond claim does provide some opportunities for the claimant that has been recently dealt with by a surety to achieve some redress. When is this available? This 2001 appellate court decision provides some insight into the thinking of New York Courts.

The appellate court unanimously held that the change order work was not only similar in nature to the work performed under the base contract, it was “indispensable to the achievement of the contract’s essential purpose.” In so ruling, the court concluded that the contractor should be reimbursed for its attorney’s fees and interest because the surety’s defense to payment was “without substantial basis since there was no plausible ground for its claim that the change order in question was not issued pursuant to the covered contract...” The court distinguished a total lack of any plausible grounds for a defense from a merely unsuccessful defense, which would not, if supported by the facts or the law, form the basis for a recovery of attorneys’ fees.

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The appellate court seems to be adopting a similar test to that which is used under court rules in New York State for the imposition of sanctions against law firms for frivolous litigation. Surety counsel has a right and obligation to vigorously defend an unjustified payment bond claim. However, counsel exposes its surety client to interest and attorney’s fees when it really “churns” a case for no good reason other than to prolong litigation and delay the proper processing of a valid payment bond claim.