



Washington State Court of Appeals Misstates Basic Surety Law Involving Release of Lien Bond Claim

by Paul Friedrich

Washington's Release of Lien Bond statute, RCW 60.04.161, allows a property owner or contractor to "release" real property from a construction lien, prior to the lien claim being resolved, by issuing a release of lien bond. Recording the bond does not destroy the lien entirely, but instead **transfers the lien from the real property to the bond**. *DBM Consulting Eng'rs, Inc. v. U.S. Fid & Guar. Co.*, 142 Wn.App.35, 42 (2007) (emphasis added) (holding that the "lien bond releases the property from the lien, but the lien is then secured by the bond").

In *CalPortland Co. v. LevelOne Concrete, LLC*, 180 Wn.App. 379 (2014), the Court of Appeals, Division II, held that the principal and the surety were the proper parties in a lawsuit against the release of lien bond. In *CalPortland, supra*, a material supplier, CalPortland, provided building materials to LevelOne Concrete, LLC, a subcontractor working on the construction of a new Costco. 180 Wn.App. at 382. Ferguson Construction, Inc., served as the general contractor. *Id.* After LevelOne failed to pay for the materials, CalPortland recorded a lien against Costco's property and then filed suit to foreclose the lien. *Id.* Before the lawsuit was filed, however, Ferguson recorded a 'bond in lieu of claim' (release of lien bond) pursuant to RCW 60.04.161. The bond was issued by Travelers Casualty and Surety Company ("Travelers") and released the Costco property from the lien. CalPortland sued Ferguson and Travelers, but not Costco. *Id.*

The trial Court entered summary judgment in favor of Ferguson and Travelers because CalPortland

had not served the summons and complaint on Costco. CalPortland appealed, arguing that Costco was not a necessary party to the suit, and did not have to be sued or served, because it no longer was the owner of the property serving as collateral for the lien. The Court of Appeals agreed, finding that Costco's property – the physical site of the project – was not property subject to the lien, and that the principal and surety – not Costco – were the proper parties in the lawsuit.

Recently, however, the Washington State Court of Appeals, Division III, reached a different conclusion. *Inland Empire Dry Wall Supply Co. v. Western Surety Co.*, 197 Wn. App. 510, 389 P.3d 717 (2017). Inland Empire Dry Wall Supply Co. ("Inland") was a sub-tier subcontractor for the Project. While the general contractor, Fowler General Construction ("Fowler"), paid its subcontractor, Eastern Washington Drywall & Paint ("Eastern"), Eastern did not pass those funds to Inland. Inland, in turn, recorded a lien on the Project. Fowler subsequently obtained a release of lien bond from Western Surety Company ("Western") in order to release the lien from the real property. After the release of lien bond was recorded, Inland filed suit but named only one party as a Defendant, Western Surety Company. Inland did not name Fowler, the bond principal.

Western filed a summary judgment motion to dismiss the lawsuit on the basis that Inland failed to name a necessary party, Fowler, the bond principal. The trial court granted summary judgment,

stating that the requirement to serve the property owner under RCW 60.04.141 is replaced by an analogous requirement to serve the bond principal and surety. The trial court ruled that because only Western, the surety, was served, the statute of limitations was not met, and Western was discharged from liability.

The Court of Appeals, however, reversed, finding that the bond principal was not a necessary party to a claim against the release of lien bond. The Court relied on the omission of any reference to the bond principal in RCW 60.04.141, for its holding that a bond principal need not be included in the suit. The Court went on to state as follows: "The general suretyship principle that a claimant may seek relief only against a surety is fully consistent with Washington law." *Inland Empire Dry Wall Supply Co.*, 197 Wash. App. at 519. The Court's failure to grasp basic surety law, i.e., that a surety's liability is strictly derivative of the bond principal's liability, is troubling and could pose issues for sureties in Washington, as it could be interpreted to suggest that sureties have liability irrespective of the bond principal's liability.

On May 2, 2017, the Supreme Court granted Western's Petition for Review and oral argument is scheduled for September 28, 2017. It will be interesting to see if the Washington State Supreme Court clarifies or corrects Division III's overly-simplistic and erroneous statements regarding Washington surety law.

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Washington Supreme Court Decision Exposes Sureties to Increased Risk for Disputing Claims

by William Hansen

On July 6, 2017, the Washington State Supreme Court addressed two important issues for sureties in Washington: (1) whether extending statutory attorney fees to public works projects provides the sole fee remedy for those projects; and (2) whether the fees between King County's claims against the principal and sureties could be segregated. The Court answered both questions in the negative.

With regard to the first question, the sureties argued that the enactment of RCW 39.04.240 revealed intent by the legislature to supplant all other available fee remedies, including the equitable fee remedy under *Olympic S.S. Co. v. Centennial Ins. Co.*, 117 Wn.2d 37 (1991) and *Colorado Structures, Inc. v. Ins. Co. of the W.*, 161 Wash. 2d 577 (2007), the landmark decision which extended the availability of *Olympic Steamship* attorney fees to claims against private performance bonds. The Court, however, found no language in the statute indicating an intent to foreclose alternative fee remedies. Moreover, the Court held that the two remedies serve distinct purposes. Specifically, fees are awarded under *Olympic Steamship* when the surety denies coverage. In contrast, statutory fees are awarded when the surety acknowledges coverage but disputes the value of the claim. Ultimately, the Court held that fees were available under *Olympic Steamship*, because the sureties refused to perform and forced litigation.

A significant result of the Court's decision to apply the fee remedy under *Olympic Steamship* is how

broadly it defined the term "coverage dispute." According to the Court, a coverage dispute involves any question of (1) whether there is a contractual duty to pay; (2) who is insured; (3) what type of risk is insured; and (4) whether an insurance contract exists at all. Essentially, if the surety disputes more than the extent of damages it may expose itself to *Olympic Steamship* attorney fees.

Additionally, the sureties argued that the Court should segregate the County's claims against the principal from its claims against the sureties. The Court disagreed, and held that the two claims were inseparable because, by adopting the defenses of the principal, the sureties made the two claims indistinguishable and forced the County to deal with the counterarguments of both the principal and the sureties. Accordingly, the Court refused to segregate the fees associated with those claims.

The Court's decision in *King County v. Vinci Constr. Grand Projects, et al.*, No. 92744-8, is informative as it provides guidance on when different fee provisions will apply. However, the decision also increases the potential risk for sureties that adopt the defenses of their principal in litigation. As always, the Surety Team at Williams, Kastner & Gibbs is available to update you on legal developments in the surety industry and answer any questions or concerns you may have.

¹ Additionally, the Court rejected the sureties' request to overturn *Colorado Structures* and, significantly, extended the availability of *Olympic Steamship* attorney fees to claims made against public works performance bonds.



Amendments to Washington's Retainage Statute Expose Sureties to Additional Risk

by William Hansen

In February 2017, the Surety Team at Williams, Kastner & Gibbs wrote an article regarding a proposed amendment to Washington's retainage statute, RCW 60.28.011(6). House Bill 1538, which became effective on July 23, 2017, was largely supported and advanced by subcontractor trade groups in an effort to relieve cash flow constraints on public projects. However, the practical result of the law will increase risk and underwriting costs for the surety industry.

A host of amendments to Washington's retainage statute made the statute a trap for the surety industry by (1) exposing Release of Retainage bonds to liability for tax claims on non-bonded projects, and (2) subordinating sureties' subrogation interest in retainage funds on public works projects. Prior to the enactment of HB 1538, a subcontractor's ability to submit a Release of Retainage bond in lieu of retainage was dependent on the general contractor

first choosing to procure its own retainage bond. Thus, the amount of Release of Retainage bonds issued was limited in practice.

However, HB 1538 provides the subcontractor with the means to force the contractor to submit a Release of Retainage to the public owner. The statute, as amended, allows a subcontractor at any point prior to formal acceptance of the project to request the contractor to submit a bond to the public owner for the portion of the retainage pertaining to the subcontractor. Within thirty days of the request, the contractor *must* provide, and the public owner *must* accept, the bond unless (1) the public owner demonstrates good cause for refusing to accept the bond; (2) the surety determines that the bond is not commercially available; (3) the subcontractor refuses to pay the premiums on the bond; or (4) the subcontractor refuses to provide the contractor with a like bond.

The practical effect of HB 1538 is that sureties will be called upon to issue a growing number of Release of Retainage bonds. As stated above, this will expose sureties to greater risk, while also diminishing their subrogation interest in the retained funds. This increased exposure may result in the need for sureties to demand additional collateral. Moreover, requests from multiple subcontractors on large public projects may result in increased administrative and underwriting costs for sureties when issuing Release of Retainage bonds.

The issues presented above are only a few of the possible scenarios which may arise under the revised RCW 60.28.011. The Surety Team at Williams, Kastner & Gibbs is prepared to answer any questions you may have and assist you in navigating the new statute.



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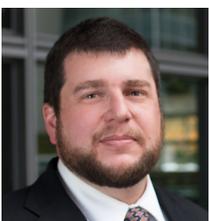
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