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Irreparable Harm: Indemnitor Failure to Deposit Collateral Is Not Enough

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A recent decision by the New York State Supreme Court, New York County, rejected a surety's argument that it would sustain irreparable harm from its indemnitors' default on their obligations to deposit collateral security, finding that the surety's contractual right to specific performance did not satisfy entitlement to preliminary injunctions without a further showing of irreparable harm.[1] The court thus denied the surety's requests for preliminary injunctions because the surety failed to meet that burden despite the likelihood of success on its specific performance claims and agreement that the remedy at law was inadequate.[2]

Following obligee claims of over $13 million on commercial surety bonds, surety US Fire Insurance Company ("US Fire") sought specific performance by the bonds' indemnitors ("Indemnitors") to post collateral security under the General Agreement of Indemnity ("GAI"). US Fire then filed two motions for preliminary injunctions for the security deposits and enjoining Indemnitors from dissipating assets.

In arguing a strong probability of success on the merits of its specific performance action, US Fire pointed to GAI Paragraph 3, where Indemnitors agreed *inter alia*:

> that Surety may, in its sole discretion, demand that Indemnitors deposit collateral security equaling any undischarged liability under the bonds, that the surety will have no adequate remedy at law should Indemnitors fail to deposit collateral, that the surety is entitled to specific performance of the obligation to post collateral, and that Indemnitors waive all defenses to provision of collateral.

US Fire maintained that the Indemnitors' failure to deposit collateral security constitutes irreparable harm, warranting injunctive relief under the New York Appellate Division case *Landmark Unlimited*.[3] It argued that the equities were in its favor because, absent such an injunction, US Fire would be deprived of the collateral security it bargained for under the GAI, while the Indemnitors would receive a windfall.

The court disagreed. Recognizing that preliminary injunctions are "drastic" remedies that should be used "sparingly," the court's analysis "start[ed] and end[ed] with irreparable harm." Irreparable harm must be imminent, not remote or speculative, said the court, and though US Fire identified adverse claims and potential exposure that may arise, it failed to show it "incurred, or will ultimately incur" costs related to the claims. US Fire's failure to set reserves or demonstrate that it expended funds or will soon expend funds to satisfy its claim obligations supported this lack of imminency, the court reasoned. Indeed, the court viewed US Fire's motions for the bonds' full penal sum to be merely "easily quantifiable monetary awards" further supporting US Fire's failure to establish "extreme" or "very serious" and irreparable harm.

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Prior Breach: Calculated Risk, Crap Shoot, or Both?

NELL M. HURLEY

When a principal is terminated, the surety must suss out the strength of its principal's claims and defenses in short order, including whether the obligee may have breached the contract, to decide how to respond to the likely performance bond claim. If the facts support it, the surety may determine that the best thing to do is deny the claim, betting that it can show a prior material breach by the obligee discharged its bond obligations.[1]

Sometimes this works out well for the surety, as in a recent case from New York where the U.S. Court of Appeals for the Second Circuit upheld a district court's trial determination that the obligee-general contractor's failure to clear impediments to delivery and installation of windows by the principal-subcontractor was a breach of the subcontract that discharged the surety's bond obligations.[2]

The matter involved construction of luxury condominiums in Manhattan in which the sub was to supply and install custom windows per a $1.85 million subcontract, with an AIA A312 subcontractor performance bond running to the general contractor-obligee. The obligee later terminated the sub for failure to timely perform and made a claim on the bond. The surety denied the claim, saying the obligee had

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The court specifically addressed US Fire's reliance on *Landmark Unlimited* for the proposition that an indemnitor's default on its collateral security obligation necessarily results in irreparable harm to the surety, observing that "nothing in *Landmark* stands for such a sweeping proposition." Instead, explained the court, adhering to such a rule would remove the requirement that sureties make *any* showing of irreparable harm to warrant the drastic remedy of preliminary injunction.

The court further noted significant factual distinctions with *Landmark*. Unlike US Fire, the surety in *Landmark* had already established a reserve in the amount of the bond's full penal sum. Perhaps more importantly, the parties in *Landmark* expressly agreed in their general agreement of indemnity that failure to deposit collateral "shall cause irreparable harm" and that the surety "shall be entitled to injunctive relief for specific performance of such obligation." Here, the GAI provided only that the "Surety will have no adequate remedy at law should [Indemnitors] fail to post any collateral…and that Surety is entitled to specific performance of the obligation to post collateral." The difference, the court stated, is that while the lack of an adequate remedy may suffice for purposes of establishing a claim for specific performance, "it does not follow that any such harm is, *a fortiori*, irreparable."

Critical to this outcome, the court concluded, is that although there are circumstances that could exist to warrant a different result, US Fire failed to carry its burden of establishing the element of irreparable harm because it was based solely on the Indemnitors' failure to deposit collateral as required under the parties' GAI.

While this case underscores the difference between proving specific performance claims versus obtaining preliminary injunctive relief, we are also reminded that the express terms of the parties' indemnification agreement is an important factor. The GAI here showed agreement only as to specific performance relief and lack of an adequate remedy at law. Had the parties also expressly agreed that Indemnitors' default regarding collateral security expressly constitutes irreparable harm and a right to injunctive relief as did the parties in *Landmark*, perhaps things would have gone better for US Fire. The surety's strongest case for injunctive relief for indemnitor collateral security will likely involve a combination of factors: the broadest possible language in favor of the surety in the indemnity agreement, the establishment of reserves for the bond claims and/or the imminent payment or obligation for payment of the claims among them. E&D

1 *MLCJR, LLC v. PDP Grp., Inc.*, 229 N.Y.S.3d 909 (Sup Ct New York County March 21, 2025).

2 Entitlement to preliminary injunctive relief in New York requires demonstrating: (i) probability of success on the merits; (ii) danger of irreparable injury in the absence of the injunction; and (iii) a balancing of the equities in its favor.

3 *Atlantic Specialty Ins. Co. v Landmark Unlimited, Inc.*, 214 A.D.3d 472 (1st Dept. 2013).

Brian Streicher, left, and Cavan Boyle attended the AGC's Surety Bonding and Construction Risk Management Conference in Bonita Springs, FL, January 27-29, 2025.

Brian Streicher, left, Mike Higgins, center, and Cavan Boyle at JBX Rochester's 2025 Bowling Tournament benefiting the Veterans Outreach Center, Inc. E&D fielded two teams and was a Drinks Sponsor.

E&D was awarded the "Best Team Shirts" trophy at the JBX bowling event for this stylish yet classic design.

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breached first, constituting an "owner default" under the bond such that the surety's obligation did not arise. The obligee then sued the surety for its costs to complete the subcontract.

At issue was a letter between the contracting parties with a revised schedule that the obligee argued the sub had failed to meet. The letter also set forth a condition that required the obligee to ensure that the site was free of debris and protrusions prior to window installation. After a four-day bench trial, the district court found that the letter's terms became a part of the subcontract and that numerous obstructions prevented the sub from delivering windows to the site, resulting in a prior breach of the subcontract by the obligee.

In a post-trial motion, the obligee argued that the letter never became a part of the subcontract because the "subcontract required that modifications be made with a signed writing" so that its terms were not enforceable against the obligee.[3] The district court, and then the Second Circuit, found that the argument was waived since it was not raised until after the court's determination, including no mention of it in the obligee's proposed findings of fact and conclusions of law after the trial. The dismissal of the action against the surety by the district court was affirmed.

A similar recent federal case tells a different story.[4] There, the subcontractor bond applied to a $2.6 million contract in which the principal-subcontractor was to fabricate, supply and install metal panels, metal screens, and architectural louvres on a high-rise building in Virginia as part of a larger project by the general contractor-obligee. Following delays, the obligee terminated the subcontract and called on the bond. The surety denied the bond claim based upon evidence that the obligee had breached first, electing not to remedy the default or complete the subcontract.

The sub later sued the obligee, alleging the obligee issued late/defective design documents, was negligent in its management of the project, interfered in the sub's work, failed to pay, and wrongfully terminated the subcontract. The obligee counterclaimed against the sub alleging the sub breached the subcontract by failing to: submit shop drawings, complete fabrication of metal panels, timely mobilize work, install and complete installation of the panels. The obligee also sued the surety on the bond for its costs to complete the subcontract.

The Maryland federal district court ultimately held a five-day trial. In a detailed 32-page decision, the court found the sub's claims against the obligee for late/defective design documents and delays to be largely unsubstantiated. Instead, said the court, the sub had materially breached the subcontract by failing to timely mobilize, failing to timely complete fabrication of the panels, and failing to timely progress and complete panel installation. The court further found that the surety was thus liable to the obligee for "all expenses, including attorneys' fees, of completion" up to the penal sum of the bond ($2.6 million).[5]

What explains the differing results? Unfortunately for sureties, every default situation is factually, contractually, and financially unique, requiring a multi-factor assessment of the surety's response. There was strong evidence supporting a prior breach by the obligee in both cases and each reached trial, meaning resolution required fact-finding, including the credibility of witnesses and experts. But trial itself is inherently risky, making it difficult to reliably forecast the result. As such, these cases show that where there is a denial of liability, even the most thorough investigation and analysis may culminate in a decision by the trier of fact, making the outcome unpredictable and requiring the surety to expect the unexpected. E&D

1 Industry standard performance bonds typically include a pre-condition that the obligee be free from its own default to recover under the bond.

2 *E & T Skyline Constr., LLC v. Talisman. Cas. Ins. Co., LLC*, 2025 WL 100621 (2d Cir. Jan. 15, 2025).

3 Interestingly, the obligee relied upon the letter's revised schedule in its notices of default.

4 *Bunting Graphics, Inc. v. Whiting-Turner Contr. Co.*, 2025 WL 299211 (D. Md. Jan. 23, 2025).

5 While the specific bond form used was not clear, its terms limited the surety's obligation to the penal sum of the bond where the surety does not remedy the default or complete the subcontract as permitted by the bond.

E&D Welcomes New Office Manager

Ernstrom & Dreste is pleased to announce Erin Warr as its new Office Manager. Erin will guide the critical day-to-day management functions previously administered by Clara Onderdonk, CLM®, who recently retired after a career of nearly 40 years with the firm.

Erin brings two decades as a legal professional to the position, encompassing both direct client-facing duties and business administration and management obligations, including human resources. Her vast and proficient skill set, and her positive professional energy, inform Erin's demonstrated leadership, financial, and administrative capabilities to successfully manage the business of the firm with the highest professional standards.

Erin Warr

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Ernstrom & Dreste, LLP also publishes the ContrACT Construction Risk Management Reporter. If you would like to receive that publication as well, please contact Jenna Ellis at jellis@ed-llp.com. Copies of ContrACT Construction Risk Management Reporter and The Fidelity & Surety Reporter can also be obtained at Ernstrom & Dreste, LLP's website (ernstromdreste.com).

FIRM NEWS

Todd Braggins and Cavan Boyle participated in the 2025 TIPS/ABA Fidelity & Surety Law Midwinter Conference in Austin, TX January 15-17, 2025. Cavan also completed the ABA/TIPS inaugural full-day *Fidelity School 2025* held in conjunction with the Midwinter Conference.

Brian Streicher and E&D Office Manager Erin Warr attended the leadership keynote event "*TOP GUN – Lessons Learned*" by Patrick Houlahan, former Marine Fighter Pilot and TOPGUN graduate, presented by AGC CLC in East Syracuse, NY in February 2025.

Brian Streicher was a featured speaker on the topic of "Contracts, Cost, and Compliance" on April 30, 2025, for JBX, Junior Builders Exchange of Rochester's 6-part program *Breaking Ground: Perspectives on Project Teamwork*.

Brian Streicher and Todd Braggins plan to attend the National Bond Claims Association's Annual Meeting in Carlsbad, CA in October 2025.

Clara Onderdonk, Certified Legal Manager (CLM)®, recently retired from E&D after nearly four decades of exemplary service and commitment to the firm.

E&D plans to transition from our printed format newsletters to a digital-only format. If you want to ensure receipt of the digital version, please email Jenna Ellis at **Jellis@ed-llp.com**. Email addresses will only be used for newsletter distribution.