

IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

IN AND FOR NEW CASTLE COUNTY

MILLSBORO FIRE COMPANY, a )  
Delaware corporation, )

Plaintiff, )

v. )

CONSTRUCTION MANAGEMENT )  
SERVICE, INC., a Delaware corporation, )

Defendant, Counter-claimant, )  
Third-Party Plaintiff, )

v. )

R. CALVIN CLENDANIEL )  
ASSOCIATES, P.A., MAHAFFY & )  
ASSOCIATES, INC., a Delaware )  
corporation, VOLAIR CONTRACTORS, )  
INC., a Delaware corporation, B.D. ABEL, )  
INC., and PIERCE MORETTA & CO., )  
d/b/a Shure-Line Excavating, )

Third-Party Defendants. )

C.A. No. 05C-06-137 MMJ

PEARCE & MORETTO, INC., )  
 )  
 )  
 Third-Party Defendant/Fourth )  
 Party Plaintiff, )  
 )  
 v. )  
 )  
 J&D CONCRETE, INC., a Maryland )  
 corporation, THORO-GOOD'S )  
 CONCRETE CO., INC., a Delaware )  
 corporation, )  
 )  
 Fourth-Party Defendants. )

Submitted: March 16, 2009

Decided: March 31, 2009

On Defendant/Third Party Plaintiffs  
Construction Management Service Inc.'s and  
Fidelity and Deposit Company of Maryland's  
Motions for Summary Judgment.

**DENIED.**

**MEMORANDUM OPINION**

Jeffrey M. Weiner, Esquire, Wilmington, Delaware, Attorney for Plaintiff

Paul G. Enterline, Esquire, Georgetown, Delaware, Attorney for Defendant CMSI

James S. Yoder, Esquire, Robert Carlton, Esquire (argued), White & Williams,  
Wilmington, Delaware, Attorneys for Fidelity and Deposit Company of Maryland

**JOHNSTON, J.**

The Millsboro Fire Hall needed rejuvenation. The Millsboro Fire Company (“MFC”) hired Construction Management Services Incorporated (“CMSI”) as general contractor for the renovation and additions to the Fire Hall. MFC retained R. Calvin Clendaniel Associates, P.A. (“Clendaniel”) to provide architectural services, including design and construction contract administration. Fidelity and Deposit Company of Maryland (“Fidelity”) issued a Performance Bond and a Payment Bond as surety for the project.

Certain aspects of the construction did not live up to MFC’s expectations. The main disputes were in three areas: interior concrete, exterior concrete and HVAC. Eventually, MFC demanded arbitration. CMSI declined to arbitrate, claiming that MFC had failed to follow the dispute resolution procedures required by contract as precedent to arbitration. CMSI filed suit in the Court of Chancery to enjoin arbitration. The Chancery action was voluntarily dismissed, without prejudice.

This Superior Court case was filed on June 10, 2005 against CMSI. MFC moved to join Fidelity as a defendant on June 1, 2007. The motion was granted. CMSI and Fidelity now have moved for summary judgment. CMSI argues that MFC is not entitled to relief because MFC failed to follow contractually-required

dispute resolution procedures. Fidelity asserts that MFC's claims against it are time-barred by the contractual limitations period.

This is the Court's decision on defendants' motions.

## **SUMMARY OF FACTS**

### ***Construction Issues Arise***

Construction began on August 17, 2001. The parties agree that construction was substantially completed by October 31, 2002, except for mechanical work.

MFC sent architect Clendaniel a letter dated September 30, 2002, stating that the concrete pad was cracked and not in acceptable condition. MFC requested that the concrete pad be removed and replaced. On November 11, 2002, a deficiency report was forwarded to the project's HVAC subcontractor. The subcontractor notified Clendaniel of the HVAC problems by letter dated January 14, 2003. MFC claims that between October 2002 and June 2003, CMSI did little or nothing to address the concrete and HVAC issues.

Clendaniel submitted its final statement for services rendered on April 24, 2003. Once final payment was due, the position of architect technically became vacant. However, Clendaniel remained involved with the project in an effort to resolve outstanding issues.

Clendaniel, CMSI and MFC representatives met at the Fire Hall on July 11, 2003. Following the meeting, Clendaniel prepared a revised list of items to be completed. Between July 31, 2003 and October 20, 2003, Clendaniel's representative communicated by letter and memo with CMSI and its subcontractors regarding the HVAC. Through a subcontractor, CMSI performed the last work on the project on November 24, 2003. By letter dated December 3, 2003, CMSI stated that its contractual obligations had been completed and final payment was due.

MFC subsequently obtained two opinions. By "Preliminary Draft" dated August 6, 2004, Weldin Engineering identified numerous deficiencies in the HVAC system. Service Unlimited estimated that the cost of remediating the deficiencies would be approximately \$500,000. By letter dated October 14, 2004, Keith Iott, AIA, P.E. opined as to deficiencies in the exterior and interior concrete. Atkinson Enterprises estimated the cost for correcting the deficiencies as \$388,122.25.

CMSI disagreed and declined to perform the work outlined in the two opinions.

***MFC's Surety Claims and Ensuing Chancery Court Litigation***

The following correspondence reflects MFC's attempts to assert a claim against the Performance Bond issued by Fidelity.

\* February 15, 2005 - MFC notified Fidelity<sup>1</sup> of its claim against the Performance Bond. MFC enclosed 22 documents.

\* February 28, 2005 - Fidelity confirmed receipt and suggested that MFC contact Fidelity's Senior Claims Counsel.

\* March 2, 2005 - MFC wrote Senior Claims Counsel, requesting a proof of claim form.

\* March 3, 2005 - MFC informed CMSI of its intention to demand arbitration and make a claim against the Performance Bond.

\* March 18, 2005 - CMSI denied any obligation to perform additional repairs until receipt of payment in full.

\* March 21, 2005 - MFC filed an American Arbitration Association ("AAA") Demand for Arbitration.

\* March 23, 2005 - MFC provided Fidelity with a copy of the arbitration demand, and asked if any additional documentation was required by Fidelity to perfect MFC's claim regarding CMSI.

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<sup>1</sup>Fidelity now is owned by Zurich North America. Although MFC's correspondence was with Zurich, the surety was issued by Fidelity. Therefore, this opinion will refer to Fidelity for ease of reference.

\* March 25, 2005 - CMSI asserted that its ability to address MFC's claims was hampered by MFC's failure to follow the contractual claims resolution procedures.

\* March 25, 2005 - CMSI informed the AAA of its position that the arbitration was premature because MFC did not abide by the claims and disputes procedures and also failed to properly serve notice of intention to arbitrate as required by 10 *Del. C.* § 5703(c).

\* April 11, 2005 - CMSI filed an action in the Delaware Court of Chancery, seeking to enjoin arbitration.

MFC and CMSI began discussing whether arbitration was the best way to resolve their differences. MFC filed this action in the Superior Court on June 10, 2005. CMSI agreed to dismiss the Chancery action and arbitration proceedings, without prejudice.

Fidelity was added as a party on June 21, 2007. In its answer filed July 31, 2007, Fidelity denied liability under the Performance Bond. Prior to the answer, Fidelity had not advised MFC that Fidelity disputed or denied any claim asserted by MFC.

### ***Contractual Limitations Provisions***

The standard American Institute of Architects (“AIA”) contract between MFC and CMSI contains provisions for Resolution of Claims and Disputes.<sup>2</sup> All disputes “shall be referred initially to the Architect for decision. An initial decision by the Architect shall be required as a condition precedent to mediation, arbitration or litigation of all Claims between the Contractor and Owner arising prior to the date final payment is due, unless 30 days have passed after the Claim has been referred to the Architect with no decision having been rendered by the Architect.”<sup>3</sup> All claims are “subject to mediation as a condition precedent to arbitration or the institution of legal or equitable proceedings by either party.”<sup>4</sup>

The contract sets forth a limitations period.

**4.3.2. Time Limits on Claims.** Claims by either party must be initiated within 21 days after occurrence of the event giving rise to such Claim or within 21 days after the claimant first recognizes the condition giving rise to the Claim, whichever is later. Claims must be initiated by written notice to the Architect and the other party.

The Fidelity Performance Bond provides:

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<sup>2</sup>AIA Contract § 4.4 *et seq.*

<sup>3</sup>AIA Contract § 4.4.1.

<sup>4</sup>AIA Contract § 4.5.1.



Any proceeding, legal or equitable, under this Bond may be instituted in any court of competent jurisdiction in the location in which the work or part of the work is located and shall be instituted within two years after Contractor Default or within two years after the Contractor ceased working or within two years after the Surety refuses or fails to perform its obligations under this Bond, whichever occurs first.<sup>5</sup>

## ANALYSIS

### *Summary Judgment Standard*

This Court will grant summary judgment only when no material issues of fact exist. The moving party bears the burden of establishing the non-existence of material issues of fact.<sup>6</sup> Once the moving party meets its burden, the burden shifts to the non-moving party to establish the existence of material issues of fact.<sup>7</sup>

Where the moving party produces an affidavit or other evidence sufficient under Superior Court Civil Rule 56 in support of its motion and the burden shifts, the non-moving party may not rest on its own pleadings, but must provide evidence showing a genuine issue of material fact for trial.<sup>8</sup> If, after discovery, the non-

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<sup>5</sup> Performance Bond ¶ 9.

<sup>6</sup> *Moore v. Sizemore*, 405 A.2d 679, 680 (Del. 1979).

<sup>7</sup> *Id.* at 681.

<sup>8</sup> Super. Ct. Civ. R. 56(e); *Celotex Corp. v. Catrett*, 477 U.S. 317, 322-23 (1986).

moving party cannot make a sufficient showing of the existence of an essential element of the case, summary judgment must be granted.<sup>9</sup>

A court deciding a summary judgment motion must identify disputed factual issues whose resolution is necessary to decide the case, but the court must not decide those issues.<sup>10</sup> The court must evaluate the facts in the light most favorable to the non-moving party.<sup>11</sup> Summary judgment will not be granted under circumstances where the record reasonably indicates that a material fact is in dispute or if it seems desirable to inquire more thoroughly into the facts in order to clarify the application of law to the circumstances.<sup>12</sup>

### ***Dispute Resolution Procedures as Conditions Precedent***

#### ***Submission of Claims to Architect***

The contract between CMSI and MFC contains provisions outlining a claims procedure. Paragraph 4.3.1. defines a “claim” as “a demand or assertion by one of the parties seeking, as a matter of right, adjustment or interpretation of

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<sup>9</sup> *Burkhart v. Davies*, 602 A.2d 56, 59 (Del. 1991), *cert. denied*, 504 U.S. 912 (1992); *Celotex Corp.*, 477 U.S. at 322-23.

<sup>10</sup> *Merrill v. Crothall-American, Inc.*, 606 A.2d 96, 99 (Del. 1992).

<sup>11</sup> *Id.*

<sup>12</sup> *Ebersole v. Lowengrub*, 180 A.2d 467, 468-69 (Del. 1962).

Contract terms, payment of money, extension of time or other relief with respect to the terms of the contract...” Claims must be initiated by written notice.

Paragraph 4.3.2. specifies that claims must be initiated “within 21 days after occurrence of the event giving rise to the Claim or within 21 days after the claimant first recognizes the condition giving rise to the Claim, whichever is later.” Paragraph 4.4.1. requires that claims “shall be referred initially to the Architect for decision. An initial decision by the Architect shall be required as a condition precedent to mediation, arbitration or litigation of all Claims between the Contractor and Owner arising prior to the date final payment is due....” Under Section 4.5, “[a]ny Claim arising out of or related to the Contract ... shall, after initial decision by the Architect or 30 days after submission of the Claim to the Architect, be subject to mediation as a condition precedent to arbitration or the institution of legal or equitable proceedings by either party.”

CMSI argues that MFC failed to follow the contractual claims resolution procedures. Specifically, CMSI asserts that MFC never submitted its claims in writing to the architect; and that MFC did not request mediation.

MFC counters that it provided the architect with the first deficiency lists by fax dated September 18, 2002. These lists included complaints relating to the

exterior concrete. The architect advised CMSI by letter dated September 30, 2002 of its decision that the concrete pad was to be removed and replaced.

MFC retained consultants to assess the HVAC issues. By letter dated January 14, 2003, the consulting engineer informed the architect of numerous deficiencies in the HVAC system. The architect wrote CMSI on June 12, 2003, attaching a punch list, including unresolved problems with the HVAC system and concrete pad.

Following a meeting on the job site and more engineering consultation, the architect informed CMSI by letter dated July 31, 2003 that if CMSI failed to address the HVAC problems, MFC would complete the work itself. Paragraph 2.4.1 of the contract gives the owner the right to carry out work.

2.4.1 If the Contractor defaults or neglects to carry out the Work in accordance with the Contract Documents and fails within a seven-day period after receipt of written notice from the Owner to commence and continue correction of such default or neglect with diligence and promptness, the Owner may after such seven-day period give the Contractor a second written notice to correct such deficiencies within a second seven-day period. If the Contractor within such second seven-day period after receipt of such second notice fails to commence and continue to correct any deficiencies, the Owner may, without prejudice to other remedies the Owner may have, correct such deficiencies. In such case an appropriate Change Order shall be issued deducting from payments then or thereafter due the Contractor the cost of correcting such deficiencies, including compensation for the Architect's additional services and expenses made necessary by such default, neglect or failure. Such action by the Owner and

amounts charged to the Contractor are both subject to prior approval of the Architect. If payments then or thereafter due the Contractor are not sufficient to cover such amounts, the Contractor shall pay the difference to the Owner.

Other memos and deficiency lists from the architect to CMSI followed.

CMSI and its subcontractor concurred with certain aspects of the engineering reports, but disputed that CMSI was responsible for all of the work. By letter dated December 3, 2003, CMSI stated that it had fulfilled its contractual obligations and final payment was due.

Failure to submit claims to the architect, as a condition precedent to dispute resolution or litigation, is a material breach of contract.<sup>13</sup> The record demonstrates that exterior concrete and HVAC claims were referred to architect, and the architect provided written notice to CMSI of deficiencies. However, it does not appear from the present record that the interior concrete claim was ever presented in writing to the architect, as required by the contract.

With regard to the exterior concrete and HVAC problems, it appears that the architect failed to take action within 30 days of MFC's claims. Paragraph 4.3.2 provides that a decision by the architect is a condition precedent to arbitration or litigation, except in the event that "the architect has failed to take action...within

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<sup>13</sup>*Commonwealth Const. Co. v. Cornerstone Fellowship Baptist Church, Inc.*, 2006 WL 2567916, at \*21-22 (Del. Super.).

30 days after the claim is made [or] 45 days have passed after the Claim has been referred to the Architect.”

The Court finds that MFC followed the claims procedure by referring the exterior concrete and HVAC issues to the architect in writing. The architect subsequently notified CMSI in writing of its decisions. Although the architect’s decisions may not have been rendered within 45 days of the claims, MFC had fulfilled its contractual obligations, regarding claims procedures, as precedent to demanding arbitration.

### **Mediation**

CMSI also argues that MFC must request mediation as a prerequisite to arbitration. The contract states that all claims are “subject to mediation as a condition precedent to arbitration or the institution of legal or equitable proceedings by either party.”<sup>14</sup> MFC concedes that it did not ask for mediation. However, neither did CMSI.

It is clear that had either party requested mediation, arbitration and litigation would have been stayed pending mediation.<sup>15</sup> The Court does not read the contract as mandating that MFC must affirmatively seek to resolve any differences

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<sup>14</sup>AIA Contract § 4.5.1.

<sup>15</sup>AIA Contract § 4.5.2.

through mediation before filing an arbitration demand. Rather, the contract gives either party the right to insist on mediation, and to stay all other proceedings for 60 days, or longer by agreement of the parties.

At any point, CMSI could have demanded mediation and would have been entitled to a halt in arbitration. Instead, CMSI chose to file in Chancery Court to enjoin arbitration. CMSI informed MFC that it objected to arbitration because: “(1) the AAA fees are outrageously high 2) Most of the available arbitrator fees are likewise high.. 3) The inability to join the architect/engineer on the Hvac claim is, in particular, a major problem for us given the design problems. 4)The absence of an appeal to serve as a check against an erroneous decision.”

By mutual agreement, the Chancery action was dismissed, without prejudice. CMSI has filed a motion for summary judgment in this Superior Court action. Had CMSI exercised its prerogative to mediate, and MFC refused, MFC would have been in breach of contract. While CMSI may have been entitled to a stay, pending mediation, MFC’s unilateral failure to request pre-arbitration/pre-litigation mediation is not a breach.

The purpose of mediation as a condition precedent obviously is to make available the most efficient and economical means of dispute resolution in the first instance. The dispute resolution procedure necessarily becomes increasingly

cumbersome and expensive, only if the parties are unable to settle their differences. At this point in this case, the Court finds that CMSI has waived its contractual privilege to require mediation before arbitration or litigation. In fact, the parties engaged in unsuccessful mediation during the pendency of this action. Therefore, the condition precedent to proceeding with this litigation has been met.

### ***Time Limitations Under the Performance Bond***

Under the Performance Bond, MFC as owner and Fidelity as surety, agreed to a limitations period. “Any proceeding...under this Bond... shall be instituted within two years after Contractor Default or within two years after the Contractor ceased working or within two years after the Surety refuses or fails to perform its obligations under this Bond, whichever occurs first.”<sup>16</sup> A Contractor Default is a “Failure of the Contractor, which has neither been remedied nor waived, to perform or otherwise to comply with the terms of the Construction Contract.”<sup>17</sup>

For purposes of summary judgment, the Court must view the facts in the light most favorable to the non-moving party. The latest date of Contractor Default was December 3, 2003, when CMSI declared that it had fulfilled its contractual obligations and final payment was due. The date CMSI ceased work

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<sup>16</sup>Performance Bond ¶ 9.

<sup>17</sup>Performance Bond ¶12.3.



was November 24, 2003, when CMSI's subcontractor performed the last work on the project.

On February 15, 2005, MFC formally notified Fidelity of its claim against the Performance Bond. Fidelity confirmed receipt of MPC's notification. MFC requested a proof of claim form from Fidelity Senior Claims Counsel. On March 23, 2005 MFC again asked Fidelity if there was any additional documentation required by Fidelity to perfect MFC's claim against CMSI. It was not until Fidelity filed its answer in this action, on July 31, 2007, that Fidelity denied liability under the Performance Bond. Prior to the answer, Fidelity had not advised MFC that Fidelity disputed or denied MFC's claim. Therefore, the latest date the surety refused or failed to perform its obligations under the Performance Bond was July 31, 2007.

The earliest of these three dates is November 23, 2003. Fidelity was added as a party on June 27, 2007 – well over two years later. The issue is whether this limitations period is enforceable, barring MFC's claim under the Performance Bond.

Having found no precedent directly on point, the Court looks to analogous authority. In *Allstate v. Spinelli*,<sup>18</sup> the Delaware Supreme Court held that an action

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<sup>18</sup>443 A.2d 1286 (Del. 1982).

by an insured, against the automobile insurance carrier, sounds in contract. Under general principles of contract law, the time limitation begins to run from the date of breach. The Court concluded that the limitations period “does not begin to run, until the insurer denies coverage and notifies its insured of rejection of any claim for such benefits.” Until denial of coverage, there is no justiciable controversy.<sup>19</sup>

By statute, an insurer may not engage in unfair claim settlement practices, including:

- b. Failing to acknowledge and act reasonably promptly upon communication with respect to claims arising under insurance policies;
- c. Failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies;

\* \* \*

- e. Failing to affirm or deny coverage of claims within a reasonable time after proof of loss statements have been completed;

\* \* \*

- n. Failing to promptly provide a reasonable explanation of the basis in the insurance policy in relation to the facts or applicable law for denial of a claim or for the offer of a compromise settlement.<sup>20</sup>

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<sup>19</sup>*Id.* at 1287, 1292.

<sup>20</sup>18 *Del. C.* § 2304(16)(b), (c), (e) and (n).

The question of the triggering of contractual rights recently was addressed by the Supreme Court in *LaPoint v. Amerisourcebergen*.<sup>21</sup> Plaintiff had brought a claim for breach of a merger agreement. Plaintiff did not request contractual indemnification against defendant as part of the lawsuit.

After the Court of Chancery entered its final judgment in favor of plaintiff, plaintiff filed a second action in Superior Court seeking indemnification. The defendant moved for summary judgment, arguing that the indemnification claim was barred by the statute of limitations and *res judicata*. On appeal, the Supreme Court found that “a prior judgment ‘cannot be given the effect of extinguishing claims which did not even then exist.’”<sup>22</sup> The determination that defendant had breached the agreement was found to be the condition precedent to the right to indemnification. Even though indemnification (as a claim incident to breach of the agreement) could have been decided in the Chancery Court action, plaintiff’s claim was deemed timely filed because the limitations period was measured from the time defendant was found to be in breach of contract, as affirmed on appeal.<sup>23</sup>

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<sup>21</sup>2009 WL 623288 (Del.).

<sup>22</sup>*Id.* at \*6, quoting *Petromanagement Corp. v. Acme-Thomas Joint Venture*, 835 F.2d 1329, 1336 (10<sup>th</sup> Cir. 1988).

<sup>23</sup>*Id.* at \*7, 10-11.

Clearly, each of the cited authorities can be distinguished. However, the underlying principle is that a claim cannot be extinguished before it is ripe. In this case, MFC had no way of knowing whether Fidelity would pay its claims under the Performance Bond until Fidelity denied the claims. In fact, the course of conduct reasonably led MFC to believe that Fidelity was considering the claims, up to the time Fidelity answered the Superior Court complaint. To find otherwise would require a property owner to file suit against a surety whether or not the dispute resolution procedures under the contract were still ongoing. Such a requirement is contrary to public policy. It is difficult to believe that surety companies would welcome the expense and time as parties to lawsuits when no claim had been made, or was required to be made, under the surety contract.

In any event, the Court cannot grant summary judgment in favor of Fidelity. Genuine issues of material fact exist as to whether Fidelity, as surety, dealt fairly with MFC in responding to MFC's requests for Fidelity's position on payment of claims. MFC has presented a *prima facie* case that it was misled to its detriment in assuming there was no need to file suit within the time limitations imposed by the Performance Bond. A triable issue of estoppel against Fidelity exists.<sup>24</sup>

### **CONCLUSION**

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<sup>24</sup>See *Closser v. Penn Mutual Fire Insurance Co.*, 457 A.2d 1081, 1081, 1088-89 (Del. 1983).

Viewing the facts in the light most favorable to the non-moving party, the Court finds that MFC fulfilled its contractual obligations precedent to demanding arbitration and initiating litigation.

The Court finds that MFC's cause of action against Fidelity was not ripe until Fidelity denied the claims under the Performance Bond. Further, genuine issues of material fact exist as to whether Fidelity should be estopped from enforcing the contractual limitations period.

**THEREFORE**, Defendant/Third Party Plaintiffs Construction Management Service Inc.'s and Fidelity and Deposit Company of Maryland's Motions for Summary Judgment are hereby **DENIED**.

**IT IS SO ORDERED.**

*/s/ Mary M. Johnston*  
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The Honorable Mary M. Johnston