

**FOURTEENTH ANNUAL
NORTHEAST SURETY AND FIDELITY
CLAIMS CONFERENCE**

SEPTEMBER 18-19, 2003

**THE ADVANTAGES OF RAISING THE IMPAIRMENT OF
SURETYSHIP DOCTRINE**

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I. Introduction¹

The “impairment of suretyship” doctrine discharges a surety from its obligation to perform whenever the obligee increases the surety's risk of loss without the surety's consent. This doctrine is set forth in the RESTATEMENT (THIRD) OF SURETYSHIP & GUARANTY §§ 37-44 (1996), which explains that when an obligee acts to increase the surety's risks by increasing its potential cost of performance or decreasing its ability to have its principal meet their obligations, the surety is entitled to relief. RESTATEMENT § 37 a.

The impairment doctrine presents a unique approach to surety claims because it is much broader and more malleable than other bond defenses. Consequently, the doctrine can be shaped to fit the facts in your case and avoid the pitfalls of other long-standing surety defenses. For example, asserting the impairment doctrine under the RESTATEMENT could eliminate a surety's notice requirement. In public contract cases especially, the government does not ordinarily owe an equitable duty of care to the surety without the surety's notification of a contractor's potential default. Conversely, an impairment claim can hinge on an obligee's contractual failing, increasing the surety's risk, and does not require notice of any kind. This application to public construction cases marks a fundamental change from previous case law, which held that the government's duty to the surety was only triggered by the surety's notice to the government of a contractor's potential default. By presenting your action as an impairment claim, sureties may by-pass the “equitable duty” rigors and simply maintain that the government increased the surety's risk resulting in a potential discharge of the surety's obligations.

Second, because the doctrine applies any time the obligee increases the surety's risk of loss, an impairment claim eliminates the necessity of proving a material breach or material alteration of a contract or bond provision. Instead, under the impairment doctrine a surety could require strict compliance with contract or bond terms and a failure to adhere to even the slightest term could discharge the surety to the amount that the alteration effected the suretyship status (*pro tanto*). Accordingly, the surety has a lesser burden of proof than under ordinary bond or contract defenses and may be discharged from performance after simply showing that the obligee increased the surety's risk beyond that for which it contracted.

Finally, the RESTATEMENT recognizes a complete defense and total discharge in situations in which the obligee fundamentally alters the risks imposed upon the surety. In those instances, “the [surety] is discharged from *any* unperformed portion of the secondary obligation.” RESTATEMENT § 37(2)(b) (emphasis added). This remedy represents one alternative in the RESTATEMENT'S bifurcated approach to the impairment doctrine, which ordinarily discharges a surety proportional to its actual loss or prejudice. Thus, while in most impairment instances a surety is discharged only to the extent it is injured, when an obligee fundamentally alters the surety's risk, the RESTATEMENT allows the surety to be discharged completely. See RESTATEMENT § 37 cmt. b.

¹ Special thanks to Scott P. Fitzsimmons for his contributions in preparing this article.

Although the RESTATEMENT identifies numerous instances where an obligee's conduct gives rise to impairment, the prevailing application of the doctrine in the construction setting has been in the context of the premature release of funds. While "unearned" payment cases neatly fit within the doctrine, the RESTATEMENT permits expansion to virtually any situation in which the obligee increases the surety's risk. Therefore, the doctrine's potential application is seemingly greater than has been evaluated by the courts and may apply in a much broader context.

This briefing analyzes the advantages of raising the impairment doctrine by construction sureties, identifies previous applications of the impairment doctrine as defined by the RESTATEMENT and analogous case law, and recognizes a potentially marked expansion of the impairment of suretyship doctrine.

1. The Advantages of Raising the Impairment of Suretyship Doctrine

Since the RESTATEMENT'S revision in 1996, there has been little federal case law analyzing the impairment doctrine in a construction bond scenario. However, the cases that have addressed this doctrine as defined by the RESTATEMENT reflect the potential advantages of raising an impairment claim. The advantages of raising an impairment of suretyship status claim fall into three categories: 1) notice is not necessarily required; 2) showing of actual breach or material deviation is not necessarily required; 3) expanded remedial options, including the potential for a complete discharge.

a. Notice Not Necessarily Required

Asserting the impairment doctrine under the RESTATEMENT could eliminate a surety's notice requirement. See Nat'l Sur. Corp. v. United States, 118 F.3d 1542 (Fed. Cir. 1997). Shortly after the RESTATEMENT'S revision in 1996, the Federal Circuit affirmed the impairment doctrine's application in National Surety, when it found the government liable to a surety that completed work on a construction project after its principal defaulted. The contract in National Surety required the government to withhold a ten percent retainage until the contractor submitted a critical path "arrow diagram." See id. at 1543. Although the contractor never submitted the diagram, the government failed to withhold ten percent retainage as contractually required. See id. at 1543-44. The surety sued the government for damages. The government denied liability claiming that the surety's failure to notify the government of the principal's default defeated the surety's right to the retainage. See id. at 1547. Relying on the RESTATEMENT § 37 and previous case law, the Federal Circuit Court found that the government's unauthorized payment was a departure from the contract terms that increased the surety's risk for which the surety had a right of recovery - notwithstanding lack of prior notice from the surety. See id. at 1547; see also Westchester Fire Ins. Co. v. United States, 52 Fed. Cl. 567, 577 (2002) (upholding National Surety, declaring that a surety may be discharged where the obligee "derogated from the governing contractual provisions and thereby caused injury to the surety," but requiring notice where the obligee does not deviate from the contract terms and the surety relies solely on its equitable rights).

The Court's holding in National Surety marks a departure from previous case law requiring a surety's notice. See Fireman's Fund Ins. Co. v. United States, 909 F.2d 495, 498 (Fed. Cir.1990) (requiring notice before discharging a surety). As the Federal Circuit noted in National Surety, ordinarily "the government as obligee owes no equitable duty to a surety. . . unless the surety notifies the government that the principal has defaulted under the bond." National Surety, 118 F.3d at 1547. Under the RESTATEMENT, however, the only requirement necessary is that an obligee increases the surety's risk of loss in some manner. As such, the surety can assert arguments based on either the contract or its equitable rights. Thus, by framing the case based on a contractual right, the notice hurdle can be avoided.

b. No Need to Establish Material Breach

The impairment doctrine, as defined by the RESTATEMENT, releases a surety from its obligations any time an obligee increases the surety's risk beyond that for which the surety contracted. This rule stands in contrast to previously existing case law requiring a material alteration of the sureties' rights before relief would be granted. Under the RESTATEMENT'S approach, a surety may potentially bring an impairment claim without having to prove a material breach of contract by the obligee. Such potential was addressed by the United States District Court for the Eastern District of Utah in Capital Indemnity Corp. v. Price Municipal Corp., 2002 WL 818064 (E.D. Utah Apr. 25, 2002).

In one of the most recent federal decisions analyzing the impairment doctrine, the Price Municipal court adopted the RESTATEMENT'S definition of the impairment of suretyship doctrine. 2002 WL 818064 (E.D. Utah Apr. 25, 2002). In Price Municipal, the surety brought suit against a municipality for releasing contract funds to the contractor without the surety's consent. The construction contract provided that the principal contractor's application for final payment must include the surety's consent and required the city engineer to review the application to ensure that it included all required documentation. See id. at *2. Without obtaining the surety's consent, the city paid the primary contractor. See id. at *4. Although the court reviewed the surety's breach of contract claim, the court's decision to grant summary judgment on the city's liability ultimately turned on the impairment doctrine. RESTATEMENT § 37. See id. at *4. The court held that by paying the principal contractor without the surety's required consent, the city "clearly increased [the surety's] risk of loss" and impaired "[the surety's] ability to make the contractor pay its subcontractors." Price Municipal, 2002 WL 818064 at *4. Thus, it was ultimately the increased risk imposed upon the surety by the obligee that determined the court's decision and not, necessarily, the magnitude of the breach.

The departure from the materiality requirement is also supported by National Surety, discussed above. 118 F.3d 1542 (Fed. Cir. 1997). In National Surety, the court reviewed whether the government breached the payment requirements when it issued progress payments without withholdings after receiving a "progress curve" when the contract specifically required an "arrow diagram." Although both were required under the contract and both provided similar information, the court found the government liable for making the payment before receiving the "arrow diagram." In its opinion, the court did not state that the government's actions constituted a material breach of the contract. Instead, the court stated that the government "simply departed from the contractually required retainage" and

impaired the surety's collateral. See National Surety, 118 F.3d at 1545. Thus, while there was not a material breach, a strict compliance rule could be established discharging a surety whenever an obligee increases the surety's risk by failing to follow even the slightest contract terms.

c. Impairment May Provide A Complete Discharge

The final, and perhaps most significant advantage of raising the impairment doctrine is its added remedial options, including the potential for a complete discharge. The RESTATEMENT takes what it terms as a bifurcated, or two-pronged approach when addressing a surety's remedial options. The RESTATEMENT explains that when the obligee fundamentally alters the risks imposed on the surety, the resulting situation is no longer that for which the surety bargained. Accordingly, the surety is discharged from any unperformed duties upon such action by the obligee. See RESTATEMENT § 37 cmt. a,b. Thus, the surety may receive a complete discharge if it can show that the obligee's actions fundamentally altered the risk bargained for by the surety.

By permitting the opportunity for a complete discharge, the RESTATEMENT's impairment of suretyship doctrine stands apart from the modern judicial trend of limiting a compensated surety's relief to a *pro tanto* discharge. Granting a complete discharge of a surety's obligation is by far the minority view in the courts. Yet, as some courts have adopted the RESTATEMENT, and the impairment doctrine in particular, it can be argued that this element of the RESTATEMENT may revive a surety's claim for complete discharge in situations in which the obligee does fundamentally alter the surety's risk. See Preferred Nat'l Ins. Co. v. United States, 54 Fed. Cl. 600, 605 (2002) ("a surety will be discharged entirely from its obligations where the change . . . imposes fundamentally different risks on the surety than those to which it had agreed."). The majority view is represented by the second half of the RESTATEMENT's bifurcated approach, holding that a surety is discharged only to the extent it is actually injured by the obligee's actions. See Preferred, 54 Fed. Cl. at 605 ("Where the alteration is less than cardinal, the surety's obligation 'is reduced to the extent of loss due to the modification.'") (citing National Surety and the RESTATEMENT).

2. Analogous Over Payment Cases Confirming the Impairment Doctrine's Applicability

As demonstrated in National Surety and Price Municipal, the courts that have analyzed the impairment doctrine's application in the construction surety context have done so in actions involving a premature release of funds or failure to comply with a condition precedent to payment. In National Surety, the government failed to obtain a required arrow diagram before payment. In Price Municipal, the city failed to obtain a surety's consent before payment. Although not identifying the sureties' position as an "impairment of suretyship claim," analogous cases, some decided before the RESTATEMENT was modified, confirm the impairment doctrine's relevance. Similarly, these cases are defined by situations in which the obligee increases the surety's risk of loss by failing to comply with express terms of a payment provision or failing to fulfill a condition precedent to payment.

A failure to conform to payment provisions or a condition precedent to payment without the surety's consent may discharge the surety, in whole or in part, from its obligations. See e.g. Cont'l Ins. Co. v. City of Va. Beach, 908 F. Supp. 341 (E.D. Va. 1995) (granting a surety a *pro tanto* discharge upon the city's failure to inspect a project before issuing payments to the contractor); Southwood Builders, Inc. v. Peerless Ins. Co., 366 S.E.2d 104 (Va. 1988) (awarding a complete discharge to a subcontractor's performance bond surety following the contractor's payment to the subcontractor without the architect's approval). Such actions are particularly prejudicial to the surety because they increase the surety's risk of loss if called upon to perform, reduce the amount of contract funds remaining, and diminish the contractor's incentive to complete the contract or pay its outstanding debts. See National Surety, 118 F.3d at 1548.

One example of a premature payment case in the federal government context is presented by United Pacific Insurance Co. v. United States, 16 Cl. Ct. 555 (1989). In United Pacific, a surety brought suit against the government on an emergency power system contract for making a progress payment to a defaulting contractor before properly inspecting materials delivered to the site. Id. at 556. When the contractor failed to pay its subcontractors, the surety stepped in and paid them, then went after the government for the erroneous payment. The Claims Court held that by not going beyond a simple initial inspection, the government "utterly failed" to protect the surety's interests. See id. at 558. While not using the term "impairment," the court held that by failing to fulfill a condition precedent to payment, i.e. the inspection, the government increased the surety's risk of loss by reducing the amount of contract funds available to pay the subcontractors. Consequently, the surety was entitled to recover its losses as measured by the overpayment.

In a similar situation, the Supreme Court of Mississippi held that when an owner's full-time inspector negligently inspected an airport roof before issuing payments to the principal, the surety was permitted to seek indemnity from the owner. See U.R.S Co. v. Gulfport-Biloxi Reg'l Airport Auth., 544 So. 2d 824 (Miss. 1989). In its decision, the court found that the architect breached his duty to the surety by improperly inspecting the roof before releasing funds. This negligence by the owner impaired the surety's status by "depriv[ing] the surety the right to resort to those funds." Id. at 828.

United Pacific and U.R.S. are representative of the majority of cases in which the impairment doctrine could apply. Both cases, along with National Surety and Price Municipal, in which the impairment doctrine was applied, address early release of funds and failure to adhere to a condition precedent to payment. Therefore, these cases and others like them, recognize that the impairment doctrine, even if not always identified as "impairment" is an established and recognized surety claim. See e.g., N. Am. Specialty Ins. Co. v. Chichester Sch. Dist., 2000 WL 1052055 (E.D. Pa. July. 20, 2000) (negligent second payment to contractor impaired surety's rights to contract funds); see also Westchester Fire Ins. Co. v. United States, 52 Fed. Cl. 567 (2002).

3. Extending the Doctrine's Advantages Beyond Payment Issues

Although the impairment doctrine is most often applied in release of funds cases, sureties should recognize the potential of raising the doctrine in almost any situation in which an obligee increases a surety's risk of loss. Indeed, the RESTATEMENT itself permits expansion of the impairment doctrine beyond those cases to which it is seemingly confined. While the RESTATEMENT § 37 provides specific examples of a few areas that the impairment doctrine could be applied, the RESTATEMENT § 44 recognizes the significance of weighing the result of an obligee's action and not the action itself in determining whether or not an obligee's conduct rises to impairment. The RESTATEMENT acknowledges that "[m]ost often, the impairment of recourse [is] . . . a release, extension or other modification of the underlying contract. However, other acts of the obligee may impair the . . . secondary obligor's right of restitution or subrogation." RESTATEMENT § 44. Therefore, "the fact of such impairment, and not the particular act bringing it about, gives rise to the [surety's] loss and resulting discharge." Id.

a. Maladministration of the Termination Process

One area where sureties should recognize the impairment doctrine's application is where an obligee exercises discretion when administering the contract in a manner that increases the surety's risk of loss. An example of this use of the doctrine would be a scenario where an obligee fails to terminate a defaulting contractor. In public contracts in particular, the government is provided seemingly broad discretion to manage the contract to meet its interests in the project. See Argonaut Ins. Co. v. United States, 193 Ct. Cl. 483, 495 (1970). However, the government must take into account the interests of the surety while wielding such discretion. See Ohio Cas. Ins. Co. v. United States, 12 Cl. Ct. 590, 591 (1987) ("the surety does not contract to assume the risks of unreasonable conduct by a contracting officer. . ."). And an abuse of discretion, which increases the surety's risk, could discharge the surety's obligations under a performance bond. See id. at 592.

In Argonaut, the surety claimed the government increased its risk by failing to terminate a defaulting contractor in a timely manner. See Argonaut, 193 Ct. Cl. at 490. The Court of Claims held that even if there were grounds for terminating, the decision whether to terminate was discretionary, and where performance charts showed that the contractor's progress was satisfactory, the government did not abuse its discretion by not terminating the contractor. See id. at 495. In its decision, the court analyzed the government's discretion provided in the contract and held that the government's refusal to terminate the contractor was well within the range of discretion conferred on the contracting agency by the terms of the contract and the applicable regulations. See id. at 496.

When faced with a similar fact pattern seventeen years later, the court held that a contracting officer's abuse of discretion could discharge a surety from its obligations. See Ohio Casualty 12 Cl. Ct. at 591. In Ohio Casualty, the court reviewed the actions of a U.S. Navy contractor to build five steel buildings. After numerous delays by the contractor, and several warnings from the surety concerning the contractor's potential default, the Navy failed to terminate the contract. The court held that the government's failure to terminate the contract after clear evidence of the contractor's incompetence was an abuse of discretion

impairing the surety's rights. See id. at 594. Thus, under Ohio Casualty and subsequent cases such as United Pacific, a surety could potentially claim impairment where an obligee fails to timely terminate a faltering contractor. See United Pacific, 16 Cl. Ct. 555 (1989) (defining the discretion permitted by a contracting officer).

b. Failure to Satisfy a Condition Precedent to Contract

Another area where sureties should recognize potential use of the impairment doctrine is when a contractor must fulfill certain obligations before contracting or performing on a contract. Such requirements could be in the form of permits or licenses required for contracting purposes. This situation was recently presented to the Florida District Court of Appeals in Kvaerner Construction, Inc. v. American Safety Casualty Insurance Co., 2003 Fla. App. Lexis 5459 (Fla. Dist. Ct. App. April 17, 2003). In Kvaerner, a construction company brought suit against a subcontractor's performance bond surety for failing to complete a contract after the contractor terminated the subcontractor. The contractor declared the subcontractor in default because the subcontractor failed to obtain a permit necessary to complete its work. See id. at *2. After determining that the contractor was aware that the subcontractor did not possess the proper license, the court declared the contract illegal under a Florida Statute and dismissed the surety from its obligations. See id. at *13. In doing so, the court recognized the obligee's duty to ensure the subcontractor obtained the proper license before entering into the contract and a surety's subsequent discharge if the obligee neglects to ensure such requirements are fulfilled.

A similar situation was reviewed by the Fourth Circuit in 1974. See Bd. of Sup. of Henrico Va. v. Ins. Co. of N. Am., 494 F.2d 660 (4th Cir. 1974). In Henrico, the Fourth Circuit held that where a state government allowed a principal to continue work without a permit required by the performance bond, the contract and state regulations, the government extended the contractor's obligations without the surety's consent. See Henrico, 494 F.2d at 671. The court held that while a failure to obtain a permit was not in itself a breach of the contract with the surety, it extended the principal's authority to perform, thus increasing the surety's risk. See id. The court found that the government negligently managed the contract by failing to properly ensure adherence to state regulations and contract provisions. See id. This failure placed the surety at greater risk than it anticipated when it entered the bond contract, and therefore released the surety from its obligations.

Expanding the court's reasoning in Henrico and Kvaerner, one could envision the potential for analogizing these cases with situations in which the government is required to ensure other qualifications required by the contract provisions. For example, failure of the government to ensure the proper qualifications of an individual performing services for a contract, i.e. training or education, could increase the surety's risk and potentially discharge a surety from its obligations under a contract.

c. Government's Failure to Comply with its Own Regulations

Another area in which the impairment doctrine may extend is where the government, as an obligee, waives its contract requirements or fails to uphold its responsibilities as set forth in its own regulations. For example, as a general rule, under contracts with the federal government, any inspection by the government is done for the benefit of the government, and the government's right to inspect does not relieve the principal of its obligation to ensure materials and labor meet contract specifications. See Kaminer Constr. Corp. v. United States, 488 F.2d 980 (Cl. Ct. 1973). However, by failing to uphold its inspection responsibilities and waiving a final or critical inspection, the government could release the surety from its obligation.

In John C. Kohler Co. v. United States, the Court of Claims held that a contractor was not liable for an exploded boiler where the government failed to undergo a final inspection before taking possession and operating the boiler. See Kohler, 498 F.2d 1360 (Cl. Ct. 1974). While Kohler addresses the contractor's liability, a surety in the same instance should be discharged as well. The responsibility for final inspection was on the government, and where the government waived its inspection rights, the court determined that any potential liability by the contractor was also waived. Kohler, 498 F.2d at 1366.

A unique argument that can be asserted against the government is that a surety may be discharged when the government fails to follow its own regulations. This argument has met resistance when brought by a contractor. In that context, the hurdle of determining whether specific regulations are intended to protect the contractor or the government becomes the dispositive inquiry. For example, in D.V. Gonzales Electric & General Contractors v. United States, a contractor claimed that the government failed to follow its own regulations in resolving disparities between the contractor's offer price and the government's estimated fair market price of a construction contract. See Gonzales, 55 Fed Cl. at 452. In denying the contractor's claim, the court held that to maintain its cause of action, the contractor must prove that the regulation existed for the benefit of the contractor and not the government.

Although the contractor in Gonzales did not prevail, the case poses a potentially unique argument regarding a surety's reliance on the government following its own regulations. If a surety enters a contract after weighing its risks against the government's regulations, it can be argued that the surety's rights were impaired when the government chooses not to follow those regulations. By not adhering to established regulations, the government would increase the surety's risk of loss.

Under the RESTATEMENT's impairment doctrine, a surety could potentially be discharged from its obligations anytime an obligee increases the surety's risk, whether or not that act or omissions involves premature payment. Consequently, the impairment doctrine with its evidentiary and remedial advantages has the potential of expanding beyond its usual inclusion in premature payment actions.

4. The Surety's Degree of Discharge is Dependant Upon the Effect of the Obligee's Actions, Not the Magnitude of the Breach

The RESTATEMENT takes a two-pronged approach to potential discharge under the impairment doctrine. Where an obligee fundamentally alters the surety's risk, the surety may be discharged completely; however, where the impairment is only slight, the surety is discharged accordingly. The following sections address the RESTATEMENT'S different approaches and supporting case law.

a. A Surety Will Most Often Be Discharged To The Amount of its Injury

One prong of the RESTATEMENT'S bifurcated approach to impairment provides for a *pro tanto* discharge. In those instances, a surety's recovery for potential loss depends upon the surety proving actual prejudice or injury, and its discharge will be effective *pro tanto*, or only to the extent of such injury. See Nat'l Union Ind. Co. v. G.E. Bass Co., 369 F.2d 75 (5th Cir. 1966) (recognizing a *pro tanto* rule of discharge based on actual prejudice or injury); N. Am. Specialty Ins. Co v. Chichester Sch. Dist., 2000 WL 1052055 (E.D. Pa. 2000) (negligent double payments to a contractor constitutes a material breach of the contract for which the surety is discharged to the extent it is injured); Mergentime Co. v. Wash. Metro. Area Transit Auth., 775 F. Supp. 14 (D.D.C. 1991) (discharge is dependent upon proof of actual injury).

Mergentime involved the construction of two Metro stations in the District of Columbia area. The surety argued that in the course of performance, the contractor and WMATA materially altered the payment clauses of the original contract without notifying the surety, thereby discharging the surety from its obligations under the bond. Mergentime, 775 F. Supp at 15. The court held that the obligee and principal indeed altered and modified the contract, but that the alteration was not so sweeping as to discharge the surety in its entirety. Id. In its decision, the court determined that the appropriate inquiry for discharge is; 1) whether the contract was materially altered, and 2) whether the alteration actually prejudiced the surety. See id. at 20.

Likewise, in Chichester, 2000 WL 1052055 at *13, although the court found that the obligee School District's negligent double payment to a defaulted prime contractor reduced the contractor's incentive to complete the contract, thereby impairing and increasing the risk to the surety, the surety could recover only the amount that it was actually prejudiced by the actions of the obligee. See id. at *13.

b. The Restatement Permits a Complete Discharge

While the requirement to show injury is the prevailing view in most jurisdictions, the RESTATEMENT permits a complete discharge. RESTATEMENT § 41. Consistent with the RESTATEMENT, at least one court in a construction setting has held that a surety need not show any injury before being discharged of its obligations. See Southwood Builders, Inc. v. Peerless Ins. Co., 366 S.E.2d 104,108 (Va. 1988). In Southwood, a surety was discharged from performance after an obligee paid a principal before receiving required approval from the architect. In analyzing the surety's potential discharge, the court stated "a separate showing of prejudice is unnecessary because a material deviation, in itself, establishes sufficient prejudice." Id. at 108. Like the RESTATEMENT's approach, here the fundamental character of the breach led to a complete discharge.

Some courts have also analyzed the effects early payment may have on a contractor's incentive to complete a project. Specifically, courts have recognized that early payments may reduce the contractor's incentive to finish the contract or pay its subcontractors, thereby increasing the risk to the surety. It has been recognized that the effects of such disincentive may be immeasurable. For example, in National Surety, the court stated that a total defense might be available "because of the impossibility of determining with exactitude the degree to which premature payment removes the incentive to perform." See National Surety, 118 F.3d at 1548 (quoting Hochevar v. Maryland Cas. Co., 114 F.2d 948 (6th Cir. 1940); see also Chichester, 2000 WL 1052055 at * 13 ("unauthorized advances reduce the principal's incentive to complete the contract, which increases the surety's risk. . ."). Therefore, if the contractor's incentive to perform has been significantly affected, the surety should argue that it be completely discharged.

5. Conclusion

Recognizing the potential advantages the impairment doctrine presents, a surety is best served by arguing impairment any time an obligee increases its risk. This approach may allow a surety to avoid the evidentiary requirements of notice and materiality of breach and widen the remedial options available. Although the impairment doctrine is most often applied when an obligee impairs the surety by releasing funds, this application represents only a limited spectrum of possibilities. By relying on the RESTATEMENT (THIRD) OF SURETYSHIP & GUARANTY, and analogizing similar cases, a surety could potentially apply the impairment doctrine, and avail itself of its advantages, in any situation in which an obligee increases the surety's risk without its consent.