

No. 27778 -- Gateway Communications, Inc., a corporation v. John R. Hess, Inc., a corporation; Insurance Company of North America, a corporation; and Steiglitz, Steiglitz, Tries, P.C., Architects/Planners, a corporation

FILED

Starcher, J., dissenting:

January 11, 2001
RORY L. PERRY II, CLERK
SUPREME COURT OF APPEALS
OF WEST VIRGINIA

RELEASED

January 12, 2001
RORY L. PERRY II, CLERK
SUPREME COURT OF APPEALS
OF WEST VIRGINIA

The majority opinion incorrectly holds that the “sole issue” in this case is whether appellee Insurance Company of North America could legally insert a 2-year limitation period into the performance bond purchased for the benefit of appellant Gateway Communications. There is another, more important question in this case, a question that is totally avoided by the majority opinion, which is this: when does a cause of action “accrue” against a performance bond so as to trigger the limitation period?

W.Va. Code, 33-6-14 [1957] prohibits any insurance contract from “limiting the time within which an action may be brought to a period of less than two years from the time the cause of action accrues. . . .” The purpose of such a limitation period “is to discourage fraud by preventing the assertion of claims after such lapse of time that it is difficult if not impossible to ascertain the truth. It is not the purpose of the statute to deprive a party of rights because of fraud.” *Restatement of the Law of Suretyship and Guaranty, Third* (1995), § 66, comment (a). We have therefore held that a cause of action accrues, and “the statute of limitations begins to run when the breach of contract occurs or *when the act breaching the contract becomes known.*” *McKenzie v. Cherry River Coal & Coke Co.*, 195 W.Va. 742, 749, 466 S.E.2d 810, 817 (1995) (*per curiam*) (emphasis added). In other words, the “discovery rule” applies to toll the deadline for filing lawsuits until the aggrieved party “discovers” the existence of a breach of the insurance contract’s terms.

The *Restatement of the Law of Suretyship and Guaranty, Third* (1995) makes clear that the discovery rule should apply to insurance contracts such as the performance bond at issue in this case.¹ The *Restatement* reasons that if the “principal obligor” on a contract -- the construction company in this case -- fails to perform and then hides that breach of the contract by making a “pretended performance,” then the principle obligor continues to be responsible for the completion of the contract. The innocent “obligee” can continue to demand performance of the contract, and the principal obligor cannot take advantage of his pretended performance to rely upon the statute of limitation. If a “secondary obligor” -- such as the performance bond company in the instant case -- is guaranteeing the performance of the principal obligor, then the secondary obligor’s responsibility persists as well.² The cause of action does

¹Section 66 of the *Restatement of the Law of Surety and Guaranty, Third* (1995) states:

§ 66. Effect of Principal Obligor’s Concealment of Default on Statute of Limitations With Respect to Secondary Obligation.

When the principal obligor’s concealment of facts giving rise to a cause of action against it under the terms of the underlying obligation prevents the running of the statute of limitations with respect to the underlying obligation until discovery of those facts, the statute does not begin to run with respect to a cause of action against the secondary obligor arising from those facts until the obligee discovers or reasonably should discover them.

²Comment (a) to Section 66 states, in part:

Where the principal obligor makes a pretended performance or conceals a default, it is easy to conclude that the principal obligor cannot take advantage of that act to obtain the benefit of the statute of limitations. Where the secondary obligor has participated in the fraud, the same result follows as to the running of the period of limitations as to the secondary obligor. Where, however, the secondary obligor is innocent, the equities of the situation do not provide a clear answer. If the principal obligor defaults and the default is concealed from the obligee, so far as the latter’s knowledge is concerned there is no enforceable right against the secondary obligor. Thus, the failure of the obligee to pursue the secondary obligor is also innocent. Therefore, a choice must be made

(continued...)

not accrue, and the statute of limitation does not begin to run, until the innocent obligee discovers or reasonably should discover the facts giving rise to a cause of action against the principal obligor.

In this case, the construction company breached the contract in 1984 by failing to correctly install an underground drainage system for the appellant. In other words, the construction company pretended to perform the contract and concealed the fact that it never performed the contract. The appellant did not discover the facts giving rise to a cause of action for breach of contract until 1989.

Therefore, the instant contract cause of action did not accrue until 1989. *W.Va. Code*, 33-6-14 requires insurance contracts to cover any claim filed within 2 years of the accrual of the claim. The instant case was filed in April 1990.

I therefore believe that the performance bond at issue in this case -- by requiring that any action against the bond be filed within 2 years of the last payment on the underlying contract -- improperly limited the time for filing a claim to a period less than 2 years from when the cause of action accrued. The appellant's cause of action was timely filed within 2 years of the date the action was discovered and accrued. Consequently, the circuit court erred by enforcing the limitation period against the appellant.

²(...continued)

between two innocent persons, the obligee and the secondary obligor. The choice is made in favor of the obligee so long as it cannot reasonably be expected to discover the principal obligor's default. So long as the original duty of the principal obligor continues, the liability of the secondary obligor persists. Moreover, in many cases the relations of principal obligor and secondary obligor are such that the secondary obligor is in a better position than the obligee to know the facts regarding the principal obligor's performance.

Accordingly, I respectfully dissent. I am authorized to state that Justice McGraw joins in this dissent.