
Coates' Canons Blog: Subdivision Performance Guarantees: A Little More Clarity

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In North Carolina, a developer can get final plat approval before he completes the required infrastructure—but only if the developer provides financial assurance to guarantee the infrastructure completion. North Carolina's General Statutes allow cities and counties to permit these performance guarantees in conjunction with subdivision approvals.

Two fairly recent cases provide some additional clarity about the scope and enforcement of performance guarantees. The key issues from these cases include:

- Courts generally will enforce the terms of the performance guarantee and financial instruments.
- The benefits of a performance bond may be assigned from a county to a municipality.
- For enforcement, local governments may not be time-barred by the standard statute of limitations.

This blog will consider each of these topics as they are addressed in *Developers Surety & Indemnity Co. v. City of Durham* and *The Town of Black Mountain v Lexon Insurance Company*.

I have described the basics of performance guarantees in this blog before. But, here's a quick refresher. Suppose Developer David wants to subdivide some land into 100 single family home lots. As is typical around the state, the local subdivision ordinance requires David to construct and dedicate neighborhood streets to serve all of those lots, to install stormwater facilities to handle the increased stormwater run-off from the pavement and rooftops, and to provide water and sewer to each lot.

Given the market and challenges of cash flow, David needs to complete the development in phases. The local ordinance could require David to complete all improvement before a final plat is approved. The ordinance also could allow for phased final plat approval—requiring the improvements of a particular phase to be completed before the final plat of that phase. Or, alternatively, the local ordinance could allow for final plat approval if David guarantees that he will complete the necessary improvements along with a financial assurance to back that guarantee. Many subdivision ordinances allow for these performance guarantees.

Now, let's consider the issues from recent cases.

Enforcing the Terms of the Agreement

Prior cases have noted that courts will enforce the authorized and agreed-upon terms of the performance guarantee. "Under North Carolina law . . . 'a public performance bond is a contract, governed by the law of contracts. Parties entering into public performance bond are free to contract for any terms they so desire.' Therefore, the contractual terms of the Bonds are controlling . . ." *Cnty. of Brunswick v. Lexon Ins. Co.*, 425 F. App'x 190, 192 (4th Cir. 2011) (unpublished)(quoting *Town of Pineville v. Atkinson/Dyer/Watson, Architects P.A.*, 114 N.C. App. 497, 442 S.E.2d 73, 74 (1994)).

A recent case from Durham re-affirms that fact. In *Developers Surety & Indemnity Co. v. City of Durham*, No. 1:11CV515, 2014 WL 4677181 (M.D.N.C. Sept. 18, 2014), pursuant to the ordinance, the developer contracted for surety bonds to ensure completion of the required infrastructure, including completion of streets and stormwater facilities.

The city argued that the bonds should pay for *all* remaining construction of infrastructure to meet city standards. The city argued that the surety company stepped into the shoes of the developer and must complete all necessary improvements.

The surety company—pointing to the language of the surety bonds—argued that the bonds only cover minimal completion of facilities already constructed.

The court rejected the city's argument that the surety company had the same obligations as the developer. Rather, the court ruled that under the terms of the bonds, the surety had limited obligations. For streets, the court found the plain reading of the bond language to cover only the completion of the final inch of asphalt for roads (not full construction of un-improved roads). For stormwater maintenance bonds, the sureties were obligated to *operate and maintain* already-constructed stormwater ponds, but were not obligated to complete un-constructed facilities.

The court enforced the contracted terms of the bonds. To be sure, the parties could have contracted for greater obligations upon the surety. But, after the terms are set, the city cannot require the surety to do more than the terms of the agreement.

This case is a strong reminder for cities and counties that allow performance guarantees: Make sure that infrastructure obligations are clearly spelled out in the language of the guarantee and financial instrument.

Assigning a Performance Bond

In my past blog on performance guarantees, I noted the open question about assignment of rights. Many questions remain, but in at least one case, a court has allowed the rights of a performance bond to be assigned from a county to a municipality.

In *Town of Black Mountain v. Lexon Ins. Co.*, 768 S.E.2d 302 (N.C. Ct. App. 2014) *review denied*, No. 28P15, 2015 WL 1809356 (N.C. Apr. 9, 2015), the developer obtained four subdivision performance bonds from the insurance company, with the county as the beneficiary. Over the course of development, the property was annexed into the town. After the development company failed, the county sought the insurer's consent for the county to assign the bonds to the town. The insurer refused, but the county assigned the bonds to the town anyway. The town adopted a resolution of developer default. The insurer refused payment and, at trial, challenged the town's standing and argued the claims were barred by the statute of limitations.

On standing, the insurer argued that when the town annexed the property, the bonds were extinguished because the county (the contractual beneficiary) no longer had jurisdiction. The court agreed that the county no longer had standing to enforce its subdivision ordinance or performance bond. The court, however, found nothing in the law or the bond agreements to prevent the county from assigning those bond agreement rights to the town. Indeed, the court "believe[d] public policy favors assignability under these facts." If the town could not call the bond, the insurer "would in effect receive a windfall."

Even with this case, communities should make sure that guarantees may be assigned upon change of jurisdiction.

Statute of Limitations

The court in *Black Mountain v. Lexon* also addressed statutes of limitation for performance guarantee enforcement. Under G.S. 1-52(1) claims arising out of contracts have a three year statute of limitations. The insurance company claimed that the town's case was time-barred. The town asserted the doctrine of *nullum tempus occurrit regi* which allows governmental bodies to be exempt from statutes of limitation for civil lawsuits. North Carolina caselaw states that, if the state is not expressly included in the statute of limitation, then the doctrine of *nullum tempus* applies to governmental functions (but not proprietary functions). Citing prior caselaw, the court in *Black Mountain v. Lexon* found that subdivision control—including enforcement of a performance bond—is a governmental function because it is "a duty owed to the general public, not a specific individual." As such, the municipality was not subject to the three year statute of limitations

for claims to enforce the performance guarantee.

Conclusion

Performance guarantees are a useful tool for balancing developers' need for flexibility and the community's need to protect purchasers and the public interest. These recent cases point to some flexibility in performance bond enforcement—assigning rights from county to city and avoiding the statute of limitations. That said, the recent cases also point to a critical issue for performance guarantees—communities need to make sure that guarantees and bonds have terms sufficient to protect the lot purchasers and public interest.

Links

- www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_160A/GS_160A-372.html
- www.ncleg.net/EnactedLegislation/Statutes/HTML/BySection/Chapter_153A/GS_153A-331.html
- canons.sog.unc.edu/?p=7521
- appellate.nccourts.org/opinions/?c=2&pdf=32175