United States Bankruptcy Court
District of New Mexico

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UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF NEW MEXICO

In re:
GALLUP AUTO SALES, INC.,
Debtor. No. 7-99-12361 SF

NORVIN LEE, et al.,
Plaintiffs,
v. Adv. No. 99-1213 S

WESTERN SURETY COMPANY,
Defendant.

MEMORANDUM OPINION ON DEFENDANT'S MOTION TO DISMISS

This matter is before the Court on defendant Western Surety Company's ("Western's") motion to dismiss for failure to state a claim upon which relief could be granted, and the response thereto by plaintiffs. Western appeared through its attorneys Miller, Stratvert & Torgeson, P.A. (Stephen M. Williams and Michael C. Ross). Plaintiffs appeared through their attorney Richard N. Feferman. Having considered the arguments of counsel, and being otherwise sufficiently informed, the Court finds that the motion to dismiss is well taken and should be granted. The parties to this action have consented to the Court's jurisdiction over this non-core proceeding.

A dismissal for failure to state a claim is appropriate only when it appears that the plaintiff can prove no set of facts in support of the claims that would entitle plaintiff to relief. Sharp v. United Airlines, Inc., 967 F.2d 404, 406 (10th Cir.

1992). The court must accept all the well-pleaded allegations of the complaint as true and must construe them in the light most favorable to the plaintiff. Id. In the context of a Fed.R. Bankr.P. 7012(b)(6) motion, which incorporates Fed.R.Civ.P. 12(b)(6), it is inappropriate for the court to consider or examine matters outside the pleadings. Lawrence National Bank v. Edmonds (In re Edmonds), 924 F.2d 176, 180 (10th Cir. 1991). Therefore, in ruling on this motion the Court has considered only the complaint and its attachments, the motion to dismiss and the legal arguments of the parties (without considering the exhibits attached to the motion to dismiss).

Plaintiffs' complaint is based upon a federal court fraud judgment rendered in their favor against debtor Gallup Auto Sales in case Civil No. 96-1525 WWD/LCS. Exhibit A to the complaint is the special verdict, Exhibit B is the judgment, and Exhibit C is a Memorandum Opinion and Order related to attorney's fees for the case. Western issued a motor vehicle dealer surety bond for Gallup Auto Sales pursuant to New Mexico Statute 66-4-7 on December 31, 1998, attached to the complaint as Exhibit D. The face amount on the bond is $50,000, and it provides in relevant part:

> NOW THEREFORE, if the above bounden principal shall well and truly comply with the provisions of Section 66-4-7, NMSA 1978 Comp, as amended, and all subsequent amendments thereto, then no liability shall attach to the surety on this bond.

> PROVIDED, however, that this bond is executed and accepted subject to the following conditions: That the effective date of this bond is December 31, 1998 and the bond is continuous in form and shall remain in full force and effect concurrently with the aforesaid license unless terminated by the surety as provided herein.

The Court of Appeals for the Tenth Circuit has long recognized the general rule that a suretyship contract is construed to cover only losses or liabilities incurred after the execution of the contract in the absence of provisions manifesting an intention that it shall cover past transactions. American Surety Co. of New York v. Scott, 63 F.2d 961, 964 (10th Cir. 1933)(collecting cases); Commercial Insurance Company of Newark, New Jersey v. Watson, 261 F.2d 143, 146 (10th Cir. 1958)("Of course the bond would not be retroactive for frauds perpetrated prior to [the bond's] effective date.") See also Leucadia, Inc. v. Helmke, 864 F.2d 964, 971 (2nd Cir. 1989)(In absence of clearly expressed contrary intent, fidelity guaranty contracts have prospective operation only and do not cover defaults occurring prior to effective date; in absence of language specifying time frame for covered acts, contract is presumed to have prospective operation only.); St. Paul Fire & Marine Insurance Company v. Commodity Credit Corporation, 646 F.2d 1064, 1074 (5th Cir. 1981)("A surety insures performance of a contingent obligation; he is not a guarantor for an existing default.") and King v. Jones, 971 S.W.2d 916, 919-20 (Mo. Ct.

App. 1998)(“The general rule is that in the absence of an express agreement, the surety is not responsible for the acts of the principal occurring prior to the execution of the bond.”); Crisafulli Brothers, Inc. v. Clanton, 512 N.Y.S.2d 927, 928, 128 A.D.2d 963, 964 (N.Y. App. 1987)(“A contract of surety shall not be construed to have retroactive operation unless express words or necessary implication dictate such effect.”); Stock v. Meissner, 309 N.W.2d 86, 89, 209 Neb. 636, 639-40 (1981)(“A bond does not cover defaults of the principal occurring prior to the effective date of the bond, unless the bond expressly provides otherwise...for it cannot be assumed that the surety intended to be bound by the past delinquencies of the principal.”)(citation omitted.); Peterson v. Schrieber, 238 N.W.2d 722, 724, 71 Wis.2d 498, 501 (1976)(General rule is that suretyship is not retrospective.); State of Illinois Department of Agriculture v. Ackerman, 341 N.E.2d 48, 49-50, 34 Ill. App.3d 796, 797 (1975)(“A bond does not cover defaults of the principal occurring prior to the effective date of the bond, unless the bond expressly provides otherwise....”); Massachusetts Bonding & Ins. Co. v. Bank of Aurora, 238 P.2d 872, 874, 124 Colo. 485, 488 (1951)(Bond issued pursuant to Motor Vehicle Dealers Act not liable for damages resulting from frauds which took place prior to the date the bond became effective.) Compare United States v. Sisson, 927 F.2d 310, 312 (7th Cir. 1991)(Miller Act bond that referred to

specific government contract was deemed to cover entire contract, not just events after execution of bond.); State of New Mexico ex rel. Mountain States Mutual Casualty Company v. KNC, Inc., 740 P.2d 690, 692, 106 N.M. 140, 141 (1987)(Surety "specifically agreed" to be liable for materials and supplies of entire contract.); Reed v. Maryland Casualty Company, 244 F.2d 857, 862 (5th Cir. 1957)(Bond incorporated state statute requiring all labor and material obligations incurred by a contractor in connection with a project to be paid; surety held liable for all material and labor before and after execution of the bond.)

The Court finds that there is no language in the bond that would indicate that Western was expressly undertaking liability for any acts that took place before the effective date, stated as December 31, 1998. Rather, the very existence of an "effective date" indicates that the parties anticipated a fixed date for the commencement of liability. The Court therefore concludes that the bond covers only liability arising on or after December 31, 1998.

The federal case complaint is not in evidence, so the Court cannot find the exact date on which liability accrued. The case caption, however, shows that the case was filed in 1996. Therefore, the Court finds that the liability represented by plaintiff's judgment predates the bond.

Plaintiffs also have argued that the non-payment of their

judgment is an event that would trigger liability on the bond. The Court disagrees. Liability under 66-4-7 is triggered when a motor vehicle dealer engages in any of the prohibited acts, not when a dealer fails to pay a judgment. See also Employers' Liability Assur. Corporation v. State of Indiana ex rel Union Trust Co. of Franklin, 34 N.E.2d 936, 938, 110 Ind.App. 86 (In. Ct. App. 1941)("It also seems immaterial when the bank actually suffered the pecuniary loss so long as it is clear what acts caused the loss, for the bonds in force at the time of the acts of dishonesty which caused the loss would be liable and not the bond in force at the time the loss was actually suffered."); Stock v. Meissner, 309 N.W.2d 86, 88-89, 209 Neb. 636, 639 (1981)(discussing logistical problems of statutes of limitations if action against surety is deemed to arise at time other than underlying action against principal.); King v. Jones, 971 S.W.2d 916, 922 (Mo. App. 1998)(The breach that caused damages occurred before bonding company issued its bond; failure to repay during the term of the bond did not make bonding company liable.)

Based on the foregoing, there is no set of facts upon which Western could be liable. The motion to dismiss should be granted[1]. The Court will enter an Order dismissing this action.

[1]Defendant also argued in its motion to dismiss that Gallup Auto Sales' actions were not the type covered by the bond. Because the court is dismissing on the time period of coverage issue it does not need to address this additional argument.

Honorable James S. Starzynski
United States Bankruptcy Judge

I hereby certify that, on the date file stamped above, a true and correct copy of the foregoing was either electronically transmitted, faxed, mailed, or delivered to the listed counsel and parties.

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