

Sub-subcontractor Gets Day in Court, Not Arbitration

By James R. Keller

This article appeared in *St. Louis Construction News and Real Estate* p. 32-33, March-April 2009.

The Eighth Circuit Court of Appeals affirmed that a sub-subcontractor will be able to proceed in court rather than arbitration on its claim for unpaid money for renovation work at a federal building in St. Louis. The sub-subcontractor, Lighting and Power Services, Inc (LPS), had a contract through general contractor Interface Construction Corp. (Interface) to renovate portions of this building.

The case is *United States of America v. Interface Construction Corp.*, 2009 WL 196362 (C.A.8 (Mo.)), decided January 29. The general contractor, Interface Construction Corporation (Interface), moved in the district court to compel arbitration based on the contract that its subcontractor, Henderson Electrical Systems, LLC (Henderson) had with LPS. Under this contract, Henderson gave LPS written notice to proceed with providing labor for electrical work on the project. Henderson's proposal to Interface for this work was for \$237,760 and stated that this proposal was to be made an attachment to its sub-contract with LPS.

Interface entered into its prime contract with the United States and Western Surety issued a payment bond required by the Miller Act in favor of all subcontractors having a direct relationship with Interface or its subcontractors, which included LPS. The Miller Act is a federal statute that requires a contractor that works on a federal building or property to post a bond to ensure payment to its subcontractors. This is to allow subcontractors to recover against the bond if the contractor does not pay them. That is what happened here.

The Miller Act is designed to replace a lawsuit to enforce a mechanic's lien. Contractors and subcontractors cannot file a mechanic's lien on federal property because of a public policy against allowing them to foreclose upon and possibly own federal property. Instead, they can recover against this bond that the Miller Act requires the general contractor to obtain.

LPS sued the bond company, Western Surety, as well as Henderson and Interface under the Miller Act after requesting but not receiving payment for \$98,516. LPS also stopped work on the project. Interface argued that LPS could not sue, but must arbitrate its Miller Act claim instead.

Interface and Henderson had signed a standard agreement subcontract form, AIA Document A401-1997. As far as the Eighth Circuit could tell, the subcontract did not refer to LPS and LPS's proposal to Henderson was not attached to the subcontract. Nor was there any written agreement to arbitrate between LPS and Henderson.

The subcontract between Interface and Henderson, however, did contain a requirement for binding arbitration with the American Arbitration Association. LPS argued that it never agreed to arbitrate its Miller Act claim. Interface argued that LPS was required to arbitrate given the statement that its proposal to Henderson was to be made an attachment to Henderson's subcontract with Interface and was to incorporate by reference the terms of Henderson's subcontract with Interface. One of those terms was binding arbitration.

Ironically, the party that referenced an arbitration provision in its proposal—sub-subcontractor LPS—contended that its proposal was not a binding agreement to arbitrate. The general contractor, who was not directly a party to the sub-subcontract, argued that it was.

The court concluded that Interface could not succeed on its claim that LPS had incorporated binding arbitration into its contract. First, the incorporation could not legally exist as the contract to which this incorporation was to attach—the contract requiring a payment bond—did not yet exist at the time the proposal was made.

The Eighth Circuit reaffirmed that a court—not an arbitrator—decides whether the parties have agreed to arbitration. Since LPS sued only under the Miller Act, and did not assert an additional claim for breach of contract, LPS was not seeking any direct relief under its sub-subcontract. Thus, any reference in its contract or proposal to arbitration was not applicable or determinative of its Miller Act claim.

The Eighth Circuit also rejected Interface's equitable estoppel argument. Interface argued that it would be inequitable to allow LPS to pursue a breach of contract claim without enforcing the arbitration provision in that same contract. The court held that the only claim LPS was pursuing was a claim under the Miller Act—a federal statute—and this claim was independent of any breach of contract claim. Thus, this claim was not bound by any contract requirement for arbitration, even if one otherwise existed. Further, a Miller Act claim could proceed against the bonding company without regard to Interface's fault.

James R. Keller is a partner at Herzog Crebs LLP where he concentrates his practice on construction law, complex business disputes, real estate and ADR. He also is an arbitrator and a mediator.