Civil No. C066827

IN THE COURT OF APPEAL, STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

EGGERS INDUSTRIES,

Plaintiff and Respondent,

vs.

FLINTCO, INC., FIDELITY & DEPOSIT COMPANY OF MARYLAND and FEDERAL INSURANCE, CO.,

Defendants and Appellants.

AMICUS CURIAE BRIEF OF AMERICAN SUBCONTRACTORS ASSOCIATION IN SUPPORT OF RESPONDENT EGGERS INDUSTRIES

Appeal from the Judgment of the Sacramento Superior Court
Case No. 34-2009-00033002, Honorable Steven H. Rodda, Judge Presiding

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CERTIFICATE OF INTERESTED ENTITIES OR PERSONS

Pursuant to California Rules of Court, Rule 8.208, Amicus Curiae provides the following information:

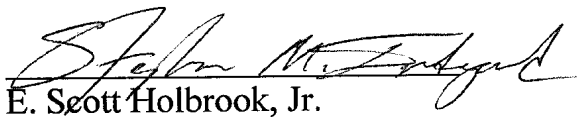
American Subcontractors Association is the Amicus Curiae, and has made the primary monetary contribution for the preparation and filing of its brief.

Other entities that have made monetary contributions to the preparation and filing of this brief are as follows:

Window & Door Manufacturers Association

Dated: July 25, 2011

CRAWFORD & BANGS, LLP



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ISSUE TO BE BRIEFED

The issue that must be decided is whether the undertaking of a contractual obligation to provide "specially manufactured" materials to construct a definite and substantial portion of a work of improvement defines a "subcontractor," regardless of whether the actual special manufacturing is further subcontracted to and performed by a lower tier subcontractor; or as Appellants contend, one can lose the "subcontractor" designation simply by subcontracting the actual special manufacturing to a lower tier subcontractor.

INTRODUCTION

American Subcontractors Association, Inc. ("ASA"), the *Amicus Curie* submitting this brief, is a national non-profit corporation supported by business membership dues paid by its approximately 5000 member businesses trading as construction subcontractors and suppliers throughout the country. More than 400 member subcontractor firms are located in California and are members of one of ASA's five California chapters. The primary purpose of ASA is to promote fairness in the construction industry and assure the equitable treatment of subcontractors. In this regard, ASA is actively involved in the promotion of legislative action across the nation and has regularly intervened in legal actions that affect the construction industry at large.

In this case, Appellant Flintco, Inc. (hereinafter "Flintco") entered into a subcontract with Architectural Security Products

(hereinafter "ASP") whereby ASP was to provide specially manufactured doors and other materials pursuant to plans and specifications for a work of improvement known as the Robert Mondavi Institute for Wine & Food Science (hereinafter "Project"). ASP then entered into a subcontract with Respondent Eggers Industries (hereinafter "Eggers") whereby Eggers was to perform all the special manufacturing of the doors and other materials for the Project. ASP failed to pay Eggers for the special manufacturing work and Eggers filed an action which included a cause of action against the payment bond on the Project.

The decision of the Sacramento Superior Court finding Eggers was a "claimant" entitled to payment bond rights is in accord with established case law and statutes regarding the distinction between a subcontractor and a material supplier to enforce mechanics' liens, stop notices, and payment bonds. If this Court affirms the Sacramento Superior Court, the law regarding mechanics' liens, stop notices, and payment bonds will be maintained, along with the equities which have been established through the development of such law which all interested parties involved in public and private construction count on to provide security and certainty for their respective interests.

On the other hand, if this Court rules in favor of Appellants, subcontractors such as ASP and Eggers will lose their security for payment for manufacturing off-site work pursuant to project plans and specifications simply by subcontracting work to a lower tier. In addition to the severe inequity that would be suffered by respondent Eggers, such a ruling would create uncertainty in the construction

industry, place a restriction on the ability of subcontractors to further subcontract out their work, and negatively affect the trend of off-site prefabrication, manufacturing and modularization work in the construction industry[1] which benefit all concerned from project owners to lower tier subcontractors and material suppliers.

As the primary basis for their appeal, Appellants contend that pursuant to case law and the Civil Code ASP should not be classified as a subcontractor, and as a result, Eggers may not enforce its claim against the payment bond on the Project. However, a thorough analysis of the relevant case law and statutes, as follows in this brief, will show that there is no support for Appellants' position in case law or statutes, and it is clear that ASP should be classified as a subcontractor according to controlling case law, the plain language of the relevant statutes, and public policy.

STATEMENT OF THE CASE

To conserve the Court's resources, the Amicus Curiae opts to omit this section and relies upon the statement of factual and procedural history as set forth in the Opposition Brief of Respondent Eggers.

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[1] McGraw-Hill Construction, Smart Market Report (20110 Prefabrication and Modularization: Increasing Productivity in the Construction Industry, discussed infra at p. 30.

ARGUMENT

I. *THEISEN* IS CONTROLLING LAW

A. The Holding of Theisen Applies to the Facts of this Case.

In *Theisen v. County of Los Angeles* (1960) 54 Cal.2d 170, 174, the first tier subcontractor, Petterson, entered into a subcontract to furnish 64 custom manufactured doors for a work of improvement. Petterson entered into a contract with Durand to manufacture 20 of the 64 doors. (*Ibid.*) The issue in the case was whether Petterson should be classified as a subcontractor, as opposed to a material supplier, even though Petterson did not contract to provide any installation of the doors or any on-site work at the project. (*Id.* at p. 179.) The classification of Petterson as a subcontractor or material supplier was necessary in order to determine whether Durand was entitled to invoke the stop notice procedure to recover payment for the 20 doors it manufactured for the project. (*Id.* at p. 176.) The *Theisen* court held that despite the fact that Petterson did not perform any work at the project site, it was still classified as a subcontractor because it agreed with the general contractor to furnish a definite and substantial part of the work of improvement. (*Id.* at p. 183-184.)

On these facts, Appellants argue that *Theisen* is distinguishable from the facts of this case. (Opening Brief, p.7). Appellants argue that since ASP did not actually perform the special manufacturing of the doors and other materials for the Project, but instead further subcontracted the work out to Eggers, it did not construct a definite and substantial portion of the Project, and therefore, is not a

subcontractor according to *Theisen* (Opening Brief, p.7-8; Reply Brief, p. 1-2); however, Appellants are wrong.

The Court's analysis of the issue in *Theisen* centered only on whether Petterson was a subcontractor even though it did not perform any work at the project site. (*Theisen v. County of Los Angeles, supra*, 54 Cal.2d at p. 179.) The court did not address at all whether the fact that Petterson actually manufactured 44 of the 64 doors, as opposed to subcontracting out all 64 doors to Durand, was any factor in determining whether Peterson was a subcontractor. Appellants state in their Opening Brief that the court in *Theisen* identified "the 'central feature' of a distinction between a subcontractor and a material supplier is that the subcontractor 'constructs' a portion of the work, not that he contracts for the work." (Opening Brief, p.8). The Court in *Theisen* made no such statement and did not even allude to such a holding in any manner. Appellants misquote the court in *Theisen* and misstate the holding of the court and that is why they are unable to cite to any part of *Theisen* in support of their statement. The actual statement of the court is:

> In our opinion the essential feature which constitutes one a subcontractor rather than a materialman is that in the course of performance of the prime contract he constructs a definite, substantial part of the work of improvement in accord with the plans and specifications of such contract, *not that he enters upon the job site and does the construction there.* (*Id.* at p. 183) (Emphasis added).

The key words in the court's holding are "not that he enters upon the job site and does the construction there." This is the language which

goes to the core of the Court's holding in *Theisen*. The court went on to state:

> [W]e conclude that one who *agrees* with the prime contractor to perform a substantial specified portion of the work of construction which is the subject of the general contract in *accord with the plans and specifications* by which the prime contractor is bound has *'charge of the construction'* of that part of the work of improvement (Code of Civ. Proc. s 1182, subd. (c)) and is a subcontractor . . . (*Ibid.*) (Emphasis added).

Appellants attempt to take the *Theisen* court's statements and holding out of context. The court was only focusing on where the work was performed, not whether Petterson actually performed the work as opposed to further subcontracting it out. The *Theisen* court specifically points out that a subcontractor that agrees to provide work in accordance with plans and specifications has *charge of the work of improvement* is a subcontractor, not that he actually does the work that he is obligated to furnish under the terms of the subcontract. (*Theisen v. County of Los Angeles, supra*, 54 Cal.2d at p. 183.) If *Theisen* involved facts which showed that Petterson subcontracted out all of the work to Durand, and on that basis the Court found that Petterson was not a subcontractor, then Appellant would have an argument that there is authority for its position. However, that is not the case, and Appellant's are taking the Court's mere statement of facts (that Petterson subcontracted to Durand for manufacture of 20 of the 64 doors) and specific language used by the Court ("constructs a definite and substantial part of the work of improvement") out of context from the Court's opinion and holding as a whole in an effort

to sway this Court to find that there is some legal support for its position, which otherwise has no valid legal support.

ASP agreed with Flintco, Inc. (hereinafter "Flintco"), the general contractor on the on the Project, to perform a *substantial specified portion of the Project,* and as a result, ASP had *charge of a specific portion of the Project* which was the subject of the general contract in accord with the plans and specifications by which Flintco was bound. ASP provided the work as obligated under its subcontract with Flintco as a result of the special manufacturing performed by ASP's subcontractor, Eggers. The fact that ASP subcontracted out the *special manufacturing/fabrication work* that it was obligated to provide pursuant to its subcontract with Flintco does not alter the fact that *specialized manufacturing* was performed pursuant to the project specifications and as such, the holding in *Theisen* still applies and ASP is a subcontractor under *Theisen.* Nothing in *Theisen* specifies, or even reasonably implies, that further subcontracting out all special manufacturing prevents classification as a subcontractor.

B. Case Law Subsequent to Theisen has Acknowledged that It is Controlling Law on the Issue of Distinguishing Between a Subcontractor and Material Supplier

Subsequent to *Theisen,* the California Court of Appeals has followed the holding of *Theisen* and acknowledged that it is controlling law on the issue of determining whether one is a subcontractor or material supplier. (*Vaughn Materials Co. v. Security Pacific National Bank* (1985) 170 Ca.App.3d 908, 917; *Tesco*

Controls v. Monterey Mechanical Co. (2004) 124 Cal.App.4th 780, 803.)

Appellants argue that *Vaughn* actually supports its position based on the Court's holding that the plaintiff therein, which contracted directly with the owner, was only a material supplier and not an original contractor because it only supplied materials (lumber) to the project and did not perform any work on the project (Opening Brief, p.10). In support of their position, at page 10 of their Opening Brief, Appellants cite to the *Vaughn* court's statement that "[p]laintiff has cited no cases for the contention that one who supplies materials to a construction site, but who does not provide any labor or engage in any construction work at all, qualifies as either an original contractor or a subcontractor within the mechanic's lien law." (*Vaughn Materials Co. v. Security Pacific National Bank, supra*, 170 Cal.App.3d at p. 912.) Appellants further argue this point in their Reply Brief at pages 4 through 5 when they quote (without citing) the *Vaughn* Court's use of the Court's language in *Theisen*. However, again, the problem with Appellant's argument is that the statements are taken out of context because *Vaughn* did not involve a first tier subcontractor further subcontracting out all special manufacturing work to a second tier subcontractor.

There is no dispute with the Court's findings in *Vaughn*; however, the court's statements are made within the context of the facts of that case, which did not include a subcontractor subcontracting out all or a majority of its work. The *Vaughn* Court never stated that a contractor or subcontractor that contracts to provide

work on a project, and then further subcontracts out that work, is not a contractor or subcontractor even if it had entered into a subcontract with the general contractor to provide work which would otherwise make it a subcontractor under *Theisen.* The *Vaughn* case is important to show that *Theisen* is controlling law regarding the distinction between a subcontractor and material supplier, but it does not stand for the proposition that a subcontractor who further subcontracts out all special manufacturing work, which it is contractually obligated to provide to a work of improvement, loses its status as a subcontractor because the character or substance of the work changes to just the supply of materials when the work is further subcontracted to a lower tier subcontractor.

Apparently, what Appellants fail to recognize is that ASP did not just provide materials to the project, or act as a "broker" (Reply Brief, p.1); it contracted with Flintco to provide *specially manufactured doors and other items for the Project according to project plans and specifications*. Although ASP further subcontracted out the manufacturing/fabrication work, it did provide the work and materials as it was obligated to do under the subcontract with Flintco. Either ASP entered into a subcontract with Flintco to provide only materials and no work, or it entered into a subcontract which obligated it and Eggers, by way of its subcontract with ASP, to provide *special manufacturing work* sufficient for both to be considered subcontractors under *Theisen.* Whether ASP further subcontracted out the work is of no matter; it was still under the obligation to provide the work, which it did. In addition, regardless of the actual title of the

document that functions as the subcontract between ASP and Flintco, whether it be "subcontract," "purchase agreement," etc., the substance of the document is a subcontract if it *requires special manufacturing rather than the mere supply of common or stock materials.*

A holding that ASP is a material supplier because it further subcontracted out all the special manufacturing can only mean that the character and substance of the work inexplicably changed from special manufacturing pursuant to the plans and specifications to merely providing materials or nothing at all upon further subcontracting out the work to Eggers. At no point in *Theisen*, *Vaughn* or any other case has a court supported such a position and Appellants have not cited to any authority in support of such a position. In addition, although Appellants claim that ASP was a material supplier, they have basically admitted that the work which ASP subcontracted to provide made ASP a subcontractor when they stated at page 10 in their Opening Brief that "[i]f Eggers had contracted with Flintco and performed the same work . . . it would arguably fall into the category of a subcontractor rather than a material supplier." Appellants are just trying to make the argument that since ASP did not actually perform the special manufacturing itself that it is not a subcontractor. This position is unsupported by the law and logic. The term at issue here is "subcontractor" not "sub-worker" or "sub-manufacturer."

Regarding Appellants' argument at page 9 of their Opening Brief and page 5 of their Reply Brief that *Tesco* was decided on issues that differ from those present in this case, such an argument is

irrelevant. The relevance of *Tesco* with respect to the *Theisen* decision is that the Court in *Tesco* looked to *Theisen* for authority on the distinction between a subcontractor and a material supplier. The fact that the *Theisen* definition of a subcontractor was used to resolve an issue that is different from that in this case is of no matter; the fact is that the *Tesco* Court followed *Theisen* regarding the distinction between a material supplier and subcontractor as it is controlling law. Appellants essentially argue in their Opening Brief at page 12 (lines 2 through 3) that *Theisen's* distinction between a material supplier and subcontractor is obsolete. In the alternative, Appellant's read the *Theisen* opinion with tunnel vision so as to fit it to the position they are taking in this matter. The fact is that *Theisen* is not obsolete and it does not lend any support for Appellant's position.

C. Continuing to Follow *Theisen* Will Not Have Any Inequitable Effects

At pages 10 through 11 of their Opening Brief and page 5 of their Reply Brief, Appellants claim that to hold that ASP is a subcontractor "would potentially give lien rights to second or third tier suppliers who might fabricate a custom product pursuant to specification requirements," and that "would require general contractors to enquire into the scope of work for all tiers of suppliers under the original material supplier to determine if any components were of special manufacture." This statement simply is not accurate and ignores statutory preliminary notice requirements of lower tier subcontractors to give notice of all on a project as done by Eggers in this case.

To hold that ASP is a subcontractor is consistent with the law set forth in *Theisen* and followed by California courts since 1960. Furthermore, if a general contractor enters into a contract with a material supplier for common or stock materials that do not require special manufacture or fabrication, then it does not need to concern itself as to whether there are other tiers of suppliers under the material supplier that it contracted with because a material supplier is not a statutory agent of the owner for purposes of lien rights, stop notices and payment bonds. (Civ. Code, § 3110.) A material supplier cannot just decide on its own that it will do special manufacturing/fabrication for a project without authority by the general contractor or a higher tier subcontractor.

On the other hand, if a general contractor enters into a contract for materials that must be specially manufactured/fabricated pursuant to the plans and specifications for the work of improvement, as in this case, then the general contractor has entered into a subcontract with a subcontractor, regardless of the title of contract document(s), and if it wishes to adequately protect itself, it will assure that if there is a lower tier of subcontractors or suppliers under the subcontractor that have served preliminary notices, as in this case, that such lower tier subcontractors or suppliers provide the necessary lien releases prior to payment to the subcontractor that it entered into the subcontract with.

This is the way it has been and the way it should be. Adequate protection is afforded to subcontractors and material suppliers who follow the procedures set by statute, such as preliminary notice requirements, and general contractors and owners are able to

adequately protect themselves through monitoring preliminary notices and assuring that the necessary lien releases are obtained prior to making payments. The problem that Flintco faces in this case is that it did not obtain the necessary lien releases prior to payment to ASP despite receipt of a preliminary notice by Eggers. Whether Flintco's failure to obtain the necessary lien releases is because it made an incorrect legal conclusion that ASP was a material supplier or it inadvertently failed to obtain the lien release from Eggers after it filed a preliminary notice, the fact is that Flintco could have protected itself, and failed to do so with notice of the claim.

When Flintco contracted with ASP to provide doors and other items *which required special manufacturing pursuant to the plans and specifications* for the Project, and then received a preliminary notice from Eggers, it should have obtained lien releases from Eggers prior to payment to ASP and it did not. Eggers, on the other hand, acted as all subcontractors and/or materials suppliers should to protect themselves; it timely served a preliminary notice in compliance with the Code, and as a result, Eggers is entitled to collect against the payment bond on the Project as it entered into a subcontract with ASP, which is a subcontractor under the holding of *Theisen* and the Civil Code, and Eggers followed the procedures required by the Civil Code.

D. *Theisen* Has Not Been Overturned By Subsequent Statutory Changes.

In Section 6 of its Opening Brief, Appellants essentially argue that the holding in *Theisen* regarding the distinction between a

subcontractor and materialman is obsolete since the Legislature codified Civil Code sections 3090, 3104, and 3248. Flintco states that the only rational conclusion that can be drawn from enactment of said statutes is that the "Legislature intended that someone who supplies material but not labor remain a materialman," implying that since ASP did not do the actual special manufacturing that it contracted to provide, it is not a subcontractor. (Opening Brief, p.12).

First, Appellants' conclusion regarding the intent of the Legislature in codifying and enacting Civil Code sections 3090, 3104, and 3248 is incorrect. In 1969, the Legislature codified (enacted 1971) Title 15 of the Civil Code entitled "Works of Improvement" sections 3082 et seq. The Legislature consolidated all the existing law regarding mechanic's liens, stop notices, and payment bonds within Title 15. The codification and enactment of Title 15 of the Civil Code included Civil Code sections 3090, 3104, and 3248. The Legislature's *express* intent regarding Title 15 is that it be construed as a declaration of preexisting law, and is not to be construed as a change in the law. (Statutes of California (1969) Chapter 1362, Section 10; Cal. Constr. L. Manual (6th ed. 2010) § 6:1).) At the time of the codification and enactment of Title 15 of the Civil Code, *Theisen* was already established case law followed by courts in California. The only actual logical conclusion to be drawn is that if the Legislature intended that any existing law, including that set forth in *Theisen*, was to be rendered obsolete by enactment of Title 15, the Legislature would have so stated.

Further, despite the Legislature's express intent regarding Title 15 of the Civil Code and case law subsequent to the enactment of said statutes which clearly states that *Theisen* is controlling on the issue regarding the distinction between a subcontractor and a material supplier, an analysis of the language of the statutes cited by Appellants shows that ASP, and those similarly situated, are subcontractors under the law, and that *Theisen* and said statutes actually work together to set the standard for who is a subcontractor for the purposes of lien rights, stop notices and payment bonds.

Civil Code section 3090 defines a material supplier as "any person who furnishes materials or supplies to be used or consumed in any work of improvement." Civil Code Section 3104 defines a subcontractor as "any contractor who has no direct contractual relationship with the owner." These sections make no mention of *Theisen* and the plain words of the statutes in no way conflict with the holding of *Theisen.* It is axiomatic that a statute, which in no way conflicts with the holding of a case decided prior to the enactment of the statute, does not overturn the holding of the case or render it obsolete. *Theisen* provides that one who contracts to provide a definite and substantial portion of a work of improvement is a subcontractor, whether or not any portion of the work is actually performed at the site of the work of improvement. (*Theisen v. County of Los Angeles, supra,* 54 Cal.2d at p. 183.) Under Civil Code section 3248, those who are mentioned in Civil Code section 3110 are entitled to a claim against a payment bond on a work of improvement. Civ Code section 3110 essentially provides that anyone who contributes labor or

materials to a work of improvement is entitled to a lien on the work of improvement, and specifically states that "[f]or the purposes of this chapter, every contractor, subcontractor, sub-subcontractor . . . or other person *having charge of a work of improvement or portion thereof* shall be held to be the agent of the owner." (Emphasis added.)

Absolutely nothing in the language of the statutes cited by Appellants, or any other statute for that matter, conflicts with the holding of *Theisen*. *Theisen* merely clarifies and confirms that when work which constitutes a definite and substantial portion of a work of improvement is performed off-site, the person or company who undertakes the obligation to provide such work is a subcontractor. As the Legislature has expressly stated its intent that no portion of Title 15 of the Civil Code is to be construed as a change in the law, there is no basis to find that any portion of Title 15, including sections 3090, 3104, and 3248 conflict with the holding of *Theisen* and/or render it obsolete; it is still controlling law.

Moreover, Appellants state that the Legislature intended that someone who supplies material but not labor remain a materialman. (Opening Brief, p.12). Yet Appellants fail to recognize that even if this was exactly the Legislature's intent, ASP is still a subcontractor under all the relevant statutes and case law. ASP did provide labor, which was special manufacturing. ASP contracted to provide the special manufacturing. Although ASP did not actually perform the special manufacturing as it further subcontracted out the work, it did provide the work as obligated pursuant to the terms of the subcontract; otherwise, Flintco would not have paid ASP. As a result, ASP

provided labor, it is a subcontractor and statutory agent that further subcontracted directly with Eggers, and Eggers is entitled to collect against the payment bond. To hold otherwise, would both limit the ability of subcontractors to further subcontract out work and wipe out a lower tier of subcontractors that the Legislature clearly intended to protect.

II. ASP QUALIFIES AS A SUBCONTRACTOR PURSUANT TO *THEISEN* AND SUBSEQUENTLY ENACTED STATUTES.

At page 11 of Appellants' Opening Brief, they cite to Civil Code sections 3090 and 3104 for the definitions of a materialman and subcontractor, and to Business & Professions Code section 7026 for the definition of a contractor. After setting forth the definitions, Appellants then conclude that "[a] subcontractor supplies material and installs it," and "[o]ne who supplies material but does not install it is a materialman or a material supplier." (Opening Brief, p.11). Appellants' interpretation of Civil Code sections 3090 and 3104, and Business & Professions Code section 7026 are misleading and fail to acknowledge the plain language of the statutes.

Civil Code section 3090 defines a material supplier as "any person who furnishes materials or supplies to be used or consumed in any work of improvement." Civil Code section 3104 defines a subcontractor as "any contractor who has no direct contractual relationship with the owner." As Civil Code Section 3104 uses the term "contractor" in its definition of a subcontractor, Appellants cite to the definition of "contractor" in Business & Professions Code

section 7026; however, Appellants cherry pick the definition and do not include the full language of the definition. Nevertheless, as will be discussed, even the language of the statute that is actually provided in Appellants' Opening Brief is sufficient to show that ASP is within the scope of the definition of a contractor set forth in section 7026.

Appellants only include a portion of the definition of "contractor" in Business & Professions Code section 7026 as follows:

> A "contractor is one who undertakes to, or does construct, alter, repair, add to, subtract from, improve, move, wreck, or demolish a building." (Opening Brief, p.11)

However, additional language of section 7026, which was left out by Appellants and is relevant to the issues in this case, should be included as well as follows:

> A contractor is any person who undertakes to, or does *himself or herself or by or through others*, construct . . . any building. (Bus & Prof. Code, § 7026.) (Emphasis added.)

Clearly, Appellants' selective citation to Business & Professions Code section 7026 does not show the complete definition. The plain language of the actual definition clearly provides that a "contractor" includes a company that subcontracts out 100% of the work that it contracted to furnish. Even if 100% of the work is further subcontracted out, the first tier subcontractor still "undertook" the obligation to provide the work and the work was done "by or through others." This literal reading is supported by the fact that if a contractor or subcontractor undertakes a contractual obligation to perform work

which requires a contractor's license (installation on work of improvement), regardless of whether the subcontractor further subcontracts all of the work, it must be a licensed contractor. (Cal. Bus. & Prof. Code, § 7031; *Ranchwood Communities Limited Partnership v. Jim Beat Construction Co.* (1996) 49 Cal.App.4th 1397, 1415; *Currie v. Stolowitz* (1959) 169 Cal.App.2d 810, 813-814; 11 Cal. Jur. 3d Building and Construction Contracts § 217.) When applied to Civil Code section 3104, ASP would fit the definition of a contractor as it undertook to specially manufacture doors and other materials for the Project, and the work was done through ASP's subcontractor, Eggers. Regarding Civil Code section 3090, since ASP undertook the obligation to specially manufacture doors and other materials for the Project, it would not be classified as a materialman under the Civil Code as it contracted to provide work over and above merely supplying common or stock materials for use in construction of the Project.

Appellants have taken Civil Code sections 3090, 3104, and Business & Professions Code section 7026 and drawn legal conclusions which are not supported by the clear language of the statutes or any other authority and has attempted to cherry pick at least one of the statutes, section 7026, in an attempt bend it to conform to their unsupported legal conclusions. None of these statutes prevent classification of ASP as a subcontractor. In fact, the statutes work together to classify ASP as a subcontractor. ASP fits the definition of a subcontractor under Civil Code Section 3104 as it had no direct contractual relationship with the owner of the Project and is a

contractor under Business & Professions Code section 7026. In addition, the holding in *Theisen* does not conflict in any way with any of these statutes.

In their Opening Brief, Appellants state that Civil Code section 3248 (Payment Bond Requirements) "restricts claimants against a public works payment bond to those who have a contract with the original contractor or a subcontractor." (Opening Brief, p.12). Appellants offer this proposition under the assumption that ASP is not a subcontractor, which it is. Civil Code section 3248(c) provides that a payment bond shall inure to the benefit of any persons named in Civ Code Section 3181, which refers to those persons who are entitled to file a stop notice and includes any person mentioned in Civil Code section 3110. As stated above, Civil Code section 3110 essentially provides that anyone who contributes labor or materials to a work of improvement is entitled to a lien on the work of improvement. Most importantly, Civil Code section 3110 states "[f]or the purposes of this chapter, every contractor, subcontractor, sub-subcontractor . . . or other person *having charge of a work of improvement or portion thereof* shall be held to be the agent of the owner." (Emphasis added.) Note that Civil Code section 3110 does not state that in order to be a subcontractor and be held to be the agent of the owner that one must actually perform work, it only states that one must have "charge of the work."

ASP contracted with Flintco to provide specially manufactured doors and other materials pursuant to plans and specifications for the project. As a result, ASP had charge of construction of a portion of the

Project, not just the supply of common materials. Pursuant to *Theisen*, it does not matter that ASP never contracted for the installation of anything on the Project or did not contract to provide any on-site work. As long as ASP contracted to provide a definite and substantial part of the work of improvement, ASP is a subcontractor under *Theisen*. In addition, since ASP had charge of a portion of the Project, it is a subcontractor under Civil Code 3110 and is a statutory agent of the owner. Since Civil Code 3248 inures to the benefit of those mentioned in Civil Code section 3110, Eggers is entitled to collect against the payment bond as it contracted with a statutory agent of the owner, ASP as a subcontractor, and Eggers as a lower tier subcontractor, served a preliminary notice in compliance with the Civil Code.

III. ASP DOES NOT NEED TO HAVE A CONTRACTOR'S LICENSE IN ORDER TO BE CLASSIFIED AS A SUBCONTRACTOR

At pages 11 through 12 of their Opening Brief, Appellants cite to Business & Professions Code section 7045 for the proposition that "[a] material supplier is not required to have a contractor's license;" implying that since ASP did not have a contractor's license it is not a subcontractor. This is simply not an accurate implication. An unlicensed contractor or subcontractor is still a contractor or subcontractor. (*Piping Specialties Co. v. Kentile, Inc.* (1964) 229 Cal.App.2d 586, 590 fn.2.)

Business & Professions Code section 7045 (Articles not fixed part of structure; finished products) provides that "[t]his chapter

[Chapter 9. Contractors] does not apply to . . . a material supplier or manufacturer furnishing finished products, materials, or articles of merchandise who does not install or contract for the installation of those items." Chapter 9 (Contractors) of the Business & Professions Code contains, amongst other things, all the statutes regarding licensing of contractors and subcontractors. Therefore, Business & Professions Code section 7045 provides that the licensing requirements within Chapter 9 of the Business & Professions Code do not apply to material suppliers; and more importantly, it also provides that it does not apply to manufacturers furnishing finished products or materials if the manufacturer does not install or contract for their installation. Therefore, a company like ASP can be a subcontractor and a statutory agent of the owner for purposes of lien rights, stop notices and claims against a payment bond, but not required to have a contractor's license under the licensing law. Case law is in accord with this. (See: *Tesco Controls v. Monterey Mechanical Co.* (2004) 124 Cal.App.4th 780, 803; *Steinbrenner v. J.A. Waterbury Constr. Co.* (1963) 212 Cal.App.2d 661, 664-666.)

The reason that a company, such as ASP, can be classified as a subcontractor under *Theisen* and the Civil Code and not a subcontractor under Chapter 9 of the Business & Professions Code is that the purposes for the mechanic's lien law and the licensing statutes within Chapter 9 of the Business & Professions Code differ. One of the primary purposes of the mechanic's lien law is to provide financial security for suppliers and subcontractors, even if they do no actual installation work, but whose custom made products have little

economic value except as part of the building for which they were designed. (*Steinbrenner v. J.A. Waterbury Constr. Co., supra*, 212 Cal.App.2d at p. 666.) On the other hand, the primary purpose of the contractor's licensing law is the protection of the public from incompetent and unreliable contractors. (*Ibid.*) Considering the purposes of the different statutory schemes, it is only logical that a subcontractor, such as ASP, who subcontracts to provide special manufacturing for a work of improvement, may be classified as a subcontractor, but since it did not subcontract to provide any installation of the specially manufactured products or materials, it is not required to be a licensed contractor.

The same logic and application of case law and statutes applies to Eggers as well. To hold otherwise would wipe out the security for a lower tier of subcontractors who contract with first tier subcontractors that undertake to construct a definite and substantial part of a work of improvement without providing any installation work or even entering onto the construction site. This would subvert one of the primary purposes of the mechanic's lien law and related statutes.

IV. CALIFORNIA COURTS HAVE ALREADY PERMITTED LOWER TIER SUBCONTRACTORS TO COLLECT ON A PAYMENT BOND WHEN THE FIRST TIER SUBCONTRACTOR SUBCONTRACTED OUT 100% OF ITS WORK.

In *Union Asphalt, Inc. v. Planet Insurance Company* (1994) 21 Cal.App.4th 1762, the California Court of Appeal, Second District, addressed the issue of whether a third tier subcontractor could collect on a payment bond for a public work of improvement. In that case, the

first tier subcontractor, Spiess Construction, on a public work of improvement subcontracted out 100% of its work to lower tier subcontractors. (*Id.* at 1764.) Although the issue in the case was whether Civil Code section 3267 precluded third tier subcontractors and material suppliers from a right of action on a payment bond, which the Court held that it did not, the third tier subcontractor and material supplier were both allowed to collect against the payment bond despite the fact that the first tier subcontractor subcontracted out 100% of its work. (*Id.* at 1763.)

The Court in *Union Asphalt* did not deem the first tier subcontractor as merely a "broker" because it subcontracted out 100% of its work. In fact, the Court recognized the fact that Spiess Construction subcontracted out 100% of its work and acknowledged that it was the first tier subcontractor. If the Court did not recognize Spiess Construction as the first tier subcontractor as a result of subcontracting out 100% of its work, it would never have gotten to the issue of whether third tier subcontractors and material suppliers can collect against a payment bond because the chain of statutory agents would have been broken with Spiess Construction. However, this was obviously not the case, and the Court in *Union Asphalt* clearly recognized that the determining factor in defining a subcontractor is that it agrees with the general contractor to provide a definite and substantial part of a work of improvement, not the actual performance of the work. (*Id.* at 1767.)

Union Asphalt is in direct contradiction with the position that Appellant's have taken in this case; yet *Union Asphalt* fits perfectly with *Theisen* and all relevant statutes.

V. CLASSIFICATION OF ASP AS A SUBCONTRACTOR IS SUPPORTED BY ESTABLISHED PUBLIC POLICY REGARDING MECHANICS' LIEN RIGHTS AND THE ALTERNATIVE REMEDIES ON PUBLIC WORKS PROJECTS.

The Constitution of the State of California provides that "[m]echanics, persons furnishing materials, artisans, and laborers of every class, shall have a lien upon the property upon which they have bestowed labor or furnished material for the value of such labor done and material furnished; and the Legislature shall provide, by law, for the speedy and efficient enforcement of such liens." (Cal. Const., art. XIV, § 3.) "The mechanic's lien is the only creditors' remedy stemming from constitutional command and our courts 'have uniformly classified the mechanics' lien laws as remedial legislation, to be liberally construed for the protection of laborers and materialmen." (*Hutnick v. United States Fidelity & Guaranty Co.* (1988) 47 Cal.3d 456, 462; *Wm. R. Clarke Corp. v. Safeco Ins. Co.* (1997) 15 Cal.4th 882, 888-889.) The purpose of a mechanics' lien is to prevent unjust enrichment of the property owner at the expense of laborers or material suppliers. (*Basic Modular Facilities, Inc. v. Ehsanipour* (1999) 70 Cal.App.4th 1480, 1483.) The policy of the State of California strongly supports the preservation of laws which give the laborer and materialman security for their claims. (*Connolly Development, Inc. v. Superior Court* (1976) 17 Cal.3d 803, 827;

Truestone, Inc. v. Simi West Industrial Park II (1984) 163 Cal.App.3d 715, 723.)

As mechanic's liens against public property are not permitted, performance and payment bonds are intended as substitutes for those who furnish labor and materials on public works of improvement. (*John A. Artukovich Sons, Inc. v. American Fidelity Fire Ins. Co.* (1977) 72 Cal.App.3d 940, 946.) Except for the original contractor, anyone who would have a right to a mechanic's lien but for the project being a public work of improvement is protected by the payment bond. (Marsh, Cal. Mechanics' Lien Law (6th ed. 2000) Representing A Stop Notice And Payment Bond Claimant On California Public Works, § 6.15.) As a result, it follows that the policies which support mechanic's lien rights also support rights against payment bonds.

Regardless of whether ASP actually performed any special manufacturing for the Project, it was still contractually obligated to provide specially manufactured doors and other materials. Eggers actually performed the special manufacturing pursuant to its subcontract with ASP, and is entitled to payment. Considering the public policy supporting the mechanic's lien law and alternative remedies on public works projects, it is clear that both ASP and Eggers are within the scope of entities and persons that the mechanics' lien law and alternative remedies are intended to protect. ASP entered into a subcontract with Flintco to provide the specially manufactured doors and materials, and it should be afforded security that it will be paid for the work it provided to the Project. ASP then

further subcontracted with Eggers to perform the special manufacturing. Regardless of whether ASP got paid by Flintco, it was contractually obligated to pay Eggers once Eggers completed the work it contracted to perform. If Flintco had failed to pay ASP, then ASP would have rightfully looked to the payment bond on the Project as security for payment. Likewise, Eggers is entitled to the same security that it will be paid for its work for the Project.

Appellants are attempting to break the chain of intended beneficiaries under the mechanics' lien law and alternative remedies on public works projects by arguing that since ASP did not actually perform the special manufacturing that it contracted to provide, those that contracted with ASP, such as Eggers, are not entitled to the security provided by such statutes on the argument that ASP cannot be classified as a subcontractor. Clearly, this is not in accord with the purpose and supporting policy of such statutes. The Project was improved by the labor and materials provided by Eggers as a result of its subcontract with ASP. Eggers followed all procedures required by the Civil Code to provide Flintco with notice of the work that Eggers was performing which gave Flintco an opportunity to protect itself through requiring releases before making payment to ASP. The only entity in this case that ignored its opportunity for protection, Flintco, now seeks to take away the security for payment to Eggers despite the fact that Eggers acted in compliance with the law and specially manufactured materials for the Project.

The fact that Flintco now sits in a position in which it has already made payment to ASP for the specially manufactured doors

and materials and now will likely ultimately be liable to its surety as principal on the payment bond after Eggers collects on its claim is only the fault of Flintco because it, unlike Eggers, failed to protect itself. The mechanics' lien law and the alternative remedies on public works projects were not enacted to protect those who sleep on their rights; however, entities such as Eggers are the exact companies that are the intended beneficiaries.

In addition, holding that a company, such as ASP, which has contracted with the general contractor to provide specially manufactured materials to a work of improvement, may not further subcontract out the work to a lower tier subcontractor and still be classified as a statutory agent of the owner would in effect be a restriction on the right to contract because a company, such as ASP, would be forced to retain a portion of the work to perform itself, even if subcontracting out the entire amount of the work would be more efficient. Contractors and subcontractors, for various reasons, at times will further subcontract out all of the work to be performed on a work of improvement. Regardless of whether a subcontractor, such as ASP, further subcontracts out all of its work or only a portion of it, the subcontractor is still obligated to provide the work and materials that it contracted to provide. Whether the work is performed by the subcontractor's employees or performed in whole or in part by a lower tier subcontractor is of no matter and all entities providing the work to the project are entitled to security for payment provided they follow the required procedures set forth in the Civil Code.

Moreover, holding that in order for ASP to be classified as a subcontractor it must have actually constructed some portion of the work that it contracted to provide would open the floodgates to further litigation on the issue. For example, such a holding would open up the question as to how much work must actually be performed by the first tier subcontractor. Another issue would be whether a subcontractor that has contracted to perform several scopes of work (i.e., grading, concrete, and plumbing) must actually perform a portion of each type of work in order to be considered a statutory agent with respect to a specific portion of the work of the project, such as plumbing. Considering these two potential likely issues, it is reasonable to assume there would be other unforeseen issues, which would bring an element of uncertainty into the mechanics' lien law and the alternative remedies on public works projects.

Yet, this is simply not necessary. Applying relevant case law, such as *Theisen*, and the clear language of the relevant statutes can lead only to the conclusion that ASP is a subcontractor and a statutory agent of the owner, and Eggers is entitled to enforce its claim against the payment bond on the Project because it subcontracted with ASP and provided specially manufactured doors and other materials for the Project for which it is entitled to payment. Flintco had notice that Eggers was providing such work to the Project through service of a preliminary notice by Eggers; and Flintco had an opportunity to protect itself but did not take advantage of such opportunity.

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VI. CLASSIFICATION OF ASP AS A SUBCONTRACTOR IS NECESSARY FOR CONTINUED INNOVATIVE BUILDING IN THE CONSTRUCTION INDUSTRY

Consideration must be given to current and future developments of prefabrication and modularization in the construction industry. A 2011 Smart Market Report "Prefabrication and Modularization: Increasing Productivity in the Construction Industry" estimates that 84% of contractors are using prefabrication and modularization on some construction projects, and that by 2013, 98% of all industry players (contractors, engineers, and architects) will be using prefabrication and modularization on some projects. (McGraw-Hill Construction, Smart Market Report (2011) Prefabrication and Modularization: Increasing Productivity in the Construction Industry, p.4.) Prefabrication and modularization has direct benefits to construction projects, such as improvement to productivity, reduction in project schedules, reduced costs, and reduction in on-site waste; as well as benefits to the environment through greener building. (Smart Market Report at p.5-30). Clearly, the future in the construction industry for both public and private projects involves a significant increase in off-site work, and it is reasonable to anticipate that the number of instances where a subcontractor will further subcontract out either all of its work or a specific scope of work will increase as well.

Confirming that companies such as ASP are classified as subcontractors if they subcontract to *provide* a definite and substantial portion of a work of improvement can only further benefit all players in the construction industry, from the owners to lower tier

subcontractors and material suppliers. Whether a company such as ASP further subcontracts out work that it has contracted to provide should not determine its classification; instead, and consistent with current law, it should be the substance of the work which it contracts to provide that is the determining factor. On the other hand, holding that ASP is not classified a subcontractor would only create confusion, inequities, and negatively affect future developments in the construction industry.

CONCLUSION

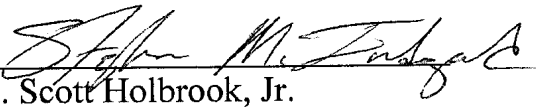
ASP undertook the contractual obligation to provide specially manufactured doors and other materials for the Project, which constituted a definite and substantial portion of the Project. As a result, ASP had charge of that specific portion of the Project, and according to *Theisen* and the Civil Code, ASP is a subcontractor and statutory agent of the owner of the Project. Eggers entered into a subcontract with ASP and specially manufactured the doors and other materials for the Project, and it is entitled to look to the payment bond on the Project for payment for the cost of the labor and materials it provided. Therefore, the judgment of the Sacramento Superior Court should be affirmed.

CERTIFICATE OF COMPLIANCE PURSUANT TO CALIFORNIA RULES OF COURT, RULE 8.204(c)(1)

Pursuant to California Rules of Court, Rule 8.204(c)(1), and in reliance upon the word count feature of the software used to prepare this document, I certify that the foregoing Amicus Curiae Brief of American Contractors Association In Support of Respondent Eggers Industries contains 8,073 words, excluding those materials not required to be counted under Rule 8.204(c)(3).

Dated: July 25, 2011

CRAWFORD & BANGS, LLP



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