Fordham Law Review

Volume 28 | Issue 2 Article 4

1959

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Cover Page Footnote
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THE EVOLUTION OF COVERAGE UNDER THE MILLER ACT

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RECENT years have witnessed an ever increasing number of public improvement projects undertaken by the Federal Government. The contracts for these improvements aggregate in the billions of dollars yearly.[1] Such enormous expenditures naturally stimulate the economy and produce a heavy concentrated market for supplies of building materials and construction equipment. Inherent, however, in projects of this nature are the dangers to which materialmen and suppliers are subject when they extend credit to the contractor or his subcontractors. A contractor who is careless or neglects to include all the costs and an adequate profit in his bid price soon becomes a menace to his suppliers and may find himself faced with bankruptcy. He may be harrassed by unforeseeable difficulties; labor problems, increased costs, or unexpected ground conditions can place him in a tenuous financial position with consequent hazards to his suppliers. If the improvement were made upon private property, the supplier could, in the event of nonpayment, claim a lien against the real property to the extent of the value of the materials delivered and incorporated into the work. However, policy and common sense prohibit such security upon a public project. Instead, the supplier may be granted a lien upon the funds due from the public authority for payment of the improvement,[2] or, as in the federal sphere, he may be granted a direct right of action upon the payment bond required to be posted by the contractor. The "Miller Act"[3] requires the contractor on any federal project exceeding $2,000 in amount to supply a payment bond "for the protection of all persons supplying all labor and materials in the prosecution of the work provided for in said contract."[4] Section 2 of the Act confers upon a laborer or materialman the right to sue the surety upon the payment bond where he has not been paid for a period of 90 days from the date when the last of the materials or services were supplied.[5] The benefit of the Act extends not only to

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1. The U.S. Department of Labor, Bureau of Labor Statistics reports that the total value of contracts awarded for Federal construction in the calendar year 1958 was $2,959,400,000; the value of such contracts in New York for that period was $119,200,000.

2. See, e.g., N.Y. Lien Law § 5.

3. 49 Stat. 793-94 (1935), 40 U.S.C. §§ 270(a),(b) (1952).

4. 49 Stat. 793 (1935), 40 U.S.C. § 270(a) (1952).

5. 49 Stat. 794 (1935), 40 U.S.C. § 270(b) (1952).

suppliers of the contractor but also to suppliers of a subcontractor, provided certain statutory conditions are met.[6]

The terms of the standard bond issued pursuant to the Act incorporate verbatim the statutory language relating to coverage:

> If the principal shall promptly make payment to all persons supplying labor and material in the prosecution of the work provided for in said contract . . . then this obligation to be void; otherwise to remain in full force and virtue.[7]

Thus, since "the surety's liability under the Miller Act must be at least co-extensive with the obligation imposed by the Act, if the bond is to have its intended effect," the supplier's "rights against the surety depend upon, and are to be measured by, the applicable provisions of § 2(a) of the Act."[8]

While it has long been established that the Act should be liberally construed in favor of the materialman,[9] coverage nevertheless has been the subject of a rather slow and tedious development. That development can be understood only by examining the law as it preceded the Miller Act.

BACKGROUND

Prior to 1935 when the Miller Act was passed, the applicable statute was the "Heard Act"[10] which granted to a supplier of a contractor on a federal improvement a right of action for labor or materials *used* in the construction; the right of action arose six months after the date of final settlement of the contract. The Heard Act was designed to afford protection to the supplier in the absence of his normal recourse to a lien upon the improvement itself. Thus, coverage was predicated upon analogy to mechanic's lien statutes,[11] and became coextensive with the extent to which the value of the material furnished added to the value of the completed improvement.[12] Coverage therefore unquestionably extended to building materials and supplies which were designed for and

6. Written notice must be given to the prime contractor within 90 days after the delivery of the last of the materials. 49 Stat. 794(2)(a) (1935), 40 U.S.C. § 270(b)(a) (1952).

7. U.S. Standard Form No. 25-A, 41 U.S.C. App. § 54.16 (1952).

8. United States ex rel. Sherman v. Carter, 353 U.S. 210, 216 (1957).

9. United States ex rel. Sherman v. Carter, supra note 8; Brogan v. National Sur. Co., 246 U.S. 257 (1918); United States ex rel. Hill v. American Sur. Co., 200 U.S. 197 (1906); Glassell-Taylor Co. v. Magnolia Petroleum Co., 153 F.2d 527 (5th Cir. 1946); United States ex rel. Purity Paint Prods. Corp. v. Aetna Cas. & Sur. Co., 56 F. Supp. 431 (D. Conn. 1944).

10. Ch. 280, 28 Stat. 278 (1894), as amended, ch. 778, 33 Stat. 811 (1905), as amended, ch. 231, § 291, 36 Stat. 1167 (1911), repealed by ch. 642, § 5, 49 Stat. 793-94 (1935).

11. Illinois Sur. Co. v. John Davis Co., 244 U.S. 376, 380 (1917). Cf. American Sur. Co. v. Lawrenceville Cement Co., 110 Fed. 717 (D. Me. 1901).

12. Maryland Cas. Co. v. Ohio River Gravel Co., 20 F.2d 514 (4th Cir. 1927).

which were in fact incorporated into the completed project. Coverage also reached certain items which, while not directly incorporated into the work, indirectly contributed to the accomplishment of the finished product.[13] Under this general test, certain cases concluded that coverage should be based upon consumption of the item upon the bonded project.[14] Thus, in *United States v. Ambursen Dam Co.*,[15] the court, being concerned with coverage of tires supplied for the contractor's vehicles, remarked that "the theory of construction followed in the more recent and best-considered cases is that the statute was intended to cover *all things* which contributed to the enterprise whether directly by going physically into the construction or indirectly by being entirely used and consumed in the construction."[16] The court also noted that upon the proof of consumption it was appropriate to consider the time when the tires were purchased and began to be used, the character of the terrain and the roads upon which the tires were to be used, the weight loads of the vehicles upon which the tires were mounted, etc.[17]

Therefore, whether the item supplied was a building material designed for incorporation into the work or a tool or appliance designed for use as part of the contractor's equipment upon the project, the coverage of such items was determinable at the termination of the job and was based upon objective proof of their use and exhaustion in the course of the bonded improvement. No distinction apparently was made or intended as to the type of equipment supplied—whether it was a capital item or a mere appliance or accessory.

Another view, however, emphasized the "inherent character" of the items supplied, rather than the length of time for which or the manner in which they happen to be used. In *National Sur. Co. v. United States ex rel. Pittsburgh & Buffalo Co.*,[18] the circuit court, in discussing coverage of rope, wire cable and chains, stated: "Things of this class are not normally intended for specific use and exhaustion upon the work where they are first sent. They are facilities for doing that work and any other work to which they may be applied."[19] While this concept subsequently

13. Brogan v. National Sur. Co., supra note 9, at 261 stated: "This court has repeatedly refused to limit the application of the act to labor and materials directly incorporated into the public work."

14. United States v. Charles H. Tompkins Co., 72 F.2d 383 (D.C. Cir. 1934) (lumber for construction of concrete forms); United States ex rel. Galliher & Huguely, Inc. v. James Baird Co., 73 F.2d 652 (D.C. Cir. 1934) (decking and timbers).

15. 3 F. Supp. 548 (N.D. Cal. 1933).

16. Id. at 553. (Emphasis added.)

17. Id. at 552.

18. 228 Fed. 577 (6th Cir. 1916), rev'd on other grounds sub nom. Brogan v. National Sur. Co., 246 U.S. 257 (1918).

19. Id. at 586.

received some judicial recognition,[20] it seems to have been rejected by the Supreme Court in the *National Surety* case. There the Court stated:

> The Circuit Court of Appeals deemed immaterial the special circumstances under which the supplies were furnished and the findings of fact by the trial court that they were necessary to and wholly consumed in the prosecution of the work provided for in the contract and bond. In our opinion these facts are not only material, but decisive. They establish the conditions essential to liability on the bond.[21]

Thus, under the Heard Act, the supplier's rights were considerably circumscribed—his right of action did not arise until six months after final settlement of the contract and, as a condition precedent to recovery, he was obliged to prove that the materials supplied (and over which he had relinquished all surveillance and control) were used and consumed upon the bonded project. While bond protection was, therefore, extended by the statute, its scope was not determinable by the supplier upon delivery of his materials. Coverage remained undecided until the materials were used and used to an extent whereby it could be concluded that they were consumed upon the job.

The Miller Act

The Miller Act was apparently designed to dispense with proof of consumption as a test of coverage. The Act granted a supplier a right of action ninety days after the last of the materials had been delivered.[22] It is plain, therefore, that the Act did not contemplate a criterion for bond protection which, running the length of the job, could conceivably exceed the ninety day period by many months or even a year. This conclusion is fortified by the fact that the statute deleted the word "used" as it had appeared in the Heard Act and instead granted protection simply to those supplying all the labor and materials in the prosecution of the work.[23] What, then, was to be the test of coverage?

In *United States ex rel. Purity Paint Prod. Corp. v. Aetna Cas. & Sur. Co.*,[24] the problem received close consideration. The plaintiff had supplied paint to a subcontractor on the bonded job, but it had been rejected and returned. In an action upon the contractor's bond, the surety contended that proof of incorporation or consumption was a condition precedent to recovery. The court rejected this argument, showing by an examination of the statute that such alleged proof was inconsistent with its provisions. While declining to define the limits of coverage, the

20. United States ex rel. Baltimore Cooperage Co. v. McCay, 28 F.2d 777, 780 (D. Md. 1928).

21. Brogan v. National Sur. Co., supra note 9, at 262.

22. 49 Stat. 794 (1935), 40 U.S.C. § 270(b) (1952).

23. 49 Stat. 794 (1935), 40 U.S.C. § 270(b) (1952).

24. 56 F. Supp. 431 (D. Conn. 1944).

court held, in effect, that upon delivery of the paint to the subcontractor the protection of the bond attached. Subsequent cases dealing with building materials have almost uniformly used delivery as a criterion for coverage.[25] However, the Tenth Circuit Court of Appeals, while granting a recovery for building materials supplied but not used,[26] gave particular emphasis to the fact that the materials became a part of the contractor's inventory replacing similar materials which had been withdrawn from inventory and installed in the project. One wonders whether the same result would have been reached if there had not been a constructive installation of the materials in the project. The Tenth Circuit has elsewhere indicated that where suppliers of tools and equipment seek the protection of the bond, consumption is still the test. Thus, in *Continental Cas. Co. v. Clarence L. Boyd Co.*,[27] the court held that repair parts for vehicles were within the bond only if there was proof that they were necessary to and wholly consumed in the performance of the work; as authority for this interpretation of the Miller Act, the court cited several cases[28] decided under the Heard Act. The court reiterated the principle, prevalent under the Heard Act, that the payment bond did not cover items of equipment and replacement parts which added materially to the contractor's equipment and rendered it available for other work. The recent decision of the Tenth Circuit in *St. Paul-Mercury Indem. Co. v. United States ex rel. Jones*[29] indicates that the view enunciated in the *Continental Cas.* case still persists.

The Fifth Circuit, on the other hand, declined, shortly after passage of the Miller Act, to apply the same meaning as that given to the earlier statute. In *Massachusetts Bonding and Ins. Co. v. United States*,[30] numerous automotive parts, including new motors, had been supplied to a contractor on a levee project. The issue as framed by the court was whether the parts constituted capital replacements or whether they were in the nature of current repairs and maintenance. To resolve the issue,

25. United States ex rel. Color Craft Corp. v. Dickstein, 157 F. Supp. 126 (E.D.N.C. 1957) (paint); United States ex rel. J. A. Edwards & Co., v. Bregman Constr. Corp., 156 F. Supp. 784 (E.D.N.Y. 1957) (electrical supplies); Montgomery v. Unity Elec. Co., 155 F. Supp. 179 (D.P.R. 1957). Cf. United States ex rel. Westinghouse Elec. Supply Co. v. Robbins, 125 F. Supp. 25 (D. Mass. 1954) (electrical supplies).

26. Fourt v. United States ex rel. Westinghouse Elec. Supply Co., 235 F.2d 433 (10th Cir. 1956), affirming 131 F. Supp. 584 (W.D. Okla. 1955); Commercial Standard Ins. Co. v. United States ex rel. Crane Co., 213 F.2d 106 (10th Cir. 1954).

27. 140 F.2d 115 (10th Cir. 1944).

28. Brogan v. National Sur. Co., supra note 9; Maryland Cas. Co. v. Ohio River Gravel Co., supra note 12; United States ex rel. Galliher & Huguely, Inc. v. James Baird Co., supra note 14.

29. 238 F.2d 917 (10th Cir. 1956).

30. 88 F.2d 388 (5th Cir. 1937).

the court looked to the nature of the work being prosecuted. It noted that the conditions on the job were extraordinary and that truck parts which might last several years under normal conditions rapidly wore out. Under these circumstances, it concluded that the materials were "consumable" and, therefore, within the coverage of the bond. The test applied was based upon the expected life of the materials on the date of delivery, not upon their actual use and consumption on the job. If the items were consumable in the normal course of the bonded project, they were covered by the bond; if, on the other hand, they would normally survive the job to be used elsewhere by the contractor, they were capital items for which the Act provided no right of recovery.

In a subsequent case,[31] the Fifth Circuit elaborated further on its concept of coverage under the Miller Act. The materials for which recovery was sought were gasoline and oil. On appeal from a judgment in favor of the supplier, the defendants contended that sale and delivery had not been proved, and that, even if proved, much of the material was not used in the work and a considerable portion thereof never reached the job site. The court stated:

> There is no provision in the statute [the Miller Act] requiring that materialmen must deliver the materials at the job site or that the materials "be used" in the prosecution of the work. The statute only requires that the materials be furnished in the prosecution of the work. . . . Whether or not the materials were wholly consumed "in the prosecution of" the work provided for in the contract and bond is not controlling. What is important is the fact that these materials were "supplied" to the subcontractor in the prosecution of the work provided for.[32]

The court also granted judgment for gasoline which had been diverted to private use, holding that it would be "manifestly unjust" to deny a recovery merely because some of the material beyond the plaintiff's disposition and control had been used elsewhere than on the bonded project.

More recently, the Second Circuit has further crystallized the matter of coverage under the Act with respect to items of equipment. In *United States ex rel. J. P. Byrne & Co. v. Fire Ass'n*,[33] the defendant's principal was a prime contractor on the St. Lawrence Seaway project. The use-plaintiff supplied the contractor with materials and services consisting primarily of new tires and tubes for its large earth-moving vehicles and the recapping of these tires. Upon the contractor's default in payment, the use-plaintiff sued the surety upon the bond. Both the district court and the court of appeals found that the working conditions at the excavation site were unusual. The earth moving equipment was being

31. Glassell-Taylor Co. v. Magnolia Petroleum Co., 153 F.2d 527 (5th Cir. 1946).

32. Id. at 529.

33. 260 F.2d 541 (2d Cir. 1958).

operated at an average of over 100 hours per week; the temperature ranged from 10° to 25° below zero.[34] The vehicles had to negotiate a steep incline from the excavation area to the dumping area. The repair and replacement of tires was admittedly a constantly recurring item, and the estimate of average life of the tires ranged from 300 hours (by plaintiff's expert) to 1800 hours (by defendant's experts).[35] The court of appeals, in modifying[36] and affirming the judgment of the district court in favor of the use-plaintiff, based its decision upon the degree of "expected consumption of the items on the particular job for which they were furnished."[37] The court stated:

> At the time of their delivery, the facts unequivocally show that both the use plaintiff and the construction company reasonably expected them [i.e., the tires] to have been substantially used up in the work under the contract. Although many of these items may not in fact have been consumed prior to the unexpected work stoppage, there is not the slightest taint in this case of an attempt by the contractor, within the constructive knowledge of its suppliers, to build up its permanent capital investment at the Surety's expense.[38]

Several factors which have been previously discussed obviously influenced the court's decision in this case:

1. The deletion of the word "used," as contained in the Heard Act, and the insertion of the word "furnished" in the Miller Act;
2. The obvious conflict between the requirement of actual consumption and the statutory grant of an immediate right of action 90 days after delivery of the materials;
3. The impossible burden which would be cast upon the supplier if he were obliged to prove consumption of materials over which he had relinquished all control;
4. The frustration of the protective purpose of the Act if the materialman could not predict coverage of his materials at the time of delivery.

The court also took cognizance of certain abuses apprehended by the defendant surety as a probable consequence of the decision of the district court. It was urged: (1) that the contractor could wait until the termination of the job and then refurbish his equipment at the expense of the surety; (2) that the contractor could fraudulently or innocently divert the materials from the bonded work to another project.[39]

34. Id. at 543.

35. Id. at 543.

36. The appellate court reduced the judgment by $276.46, representing the cost of certain highway truck tires concerning which no proof of expected consumption had been introduced. Id. at 545.

37. 260 F.2d at 544.

38. Id. at 544.

39. Id. at 545.

In either event, the court held, recovery should not be denied under the Act unless the supplier had constructive knowledge of the contractor's intentions.[40]

The degree to which the court in the *J. P. Byrne* case applied its doctrine of "expected consumption" is especially apparent from the fact that the tires and tubes were delivered between February 27 and April 7, 1956. The job terminated on April 11, 1956 by joint action of the government and the contractor. The great majority of tires and recapped tires could not therefore have been consumed upon the job even if their anticipated life was only 300 hours, as contended by the use-plaintiff. Of course, if the job had been completed on April 11th, rather than being unexpectedly terminated, it could not have been said that the parties at the time of delivery anticipated that the materials would be substantially consumed in the work under the contract.

CONCLUSIONS

It is apparent from the weight of authority that delivery of materials at the job site is not a prerequisite to coverage under the Miller Act, nor does innocent or fraudulent diversion of materials from the bonded project by the contractor affect coverage so long as the supplier has no knowledge, actual or constructive, of the contractor's intent.

As to items normally intended for incorporation into the completed project, coverage arises upon delivery irrespective of whether the items are subsequently used or incorporated. As to items constituting part of the contractor's equipment, coverage arises upon delivery provided it may then be reasonably expected that they will be substantially used up in the course of the bonded job. Whether an item comes within the bond does not necessarily depend upon its inherent character but rather upon its anticipated use on the project.

The question of coverage is therefore regulated by the doctrine of "expected consumption" rather than "actual consumption." Items which, under normal circumstances, might be deemed capital equipment because of their durability and the likelihood that they would survive the bonded job might, nevertheless, be subject to coverage where the work was prosecuted under extraordinary conditions whereby it could reasonably be anticipated that the equipment could not survive the job.

40. Id. at 545.