

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

GATECO, INC. d/b/a/	:	CIVIL ACTION
GATEWAY INDUSTRIAL SERVICES	:	
	:	
v.	:	
	:	
SAFECO INSURANCE COMPANY	:	
OF AMERICA, and EMPLOYERS	:	
INSURANCE OF WAUSAU	:	NO. 05-2869

MEMORANDUM

Bartle, C.J.

July 24, 2006

Plaintiff Gateco, Inc. ("Gateco"), a citizen of Pennsylvania, has sued Safeco Insurance Company of America ("Safeco"), a citizen of Washington, to collect payments allegedly due for materials and services it rendered as a sub-subcontractor on a project for the Port Authority of Allegheny County, Pennsylvania ("Port Authority"). As explained on prior occasions, the project concerned the reconstruction and modernization of a five mile portion of track that is a part of the Light Rail Transit System known as the "Overbrook Line." Defendant Safeco is a surety which issued a payment bond as required by Pennsylvania law on behalf of the general contractor, A&L, Inc. ("A&L").

Before the court is Safeco's motion for summary judgment on the ground that Gateco is barred as a matter of law from collecting under the bond at issue.

I.

Rule 56(c) of the Federal Rules of Civil Procedure permits us to grant summary judgment only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to summary judgment as a matter of law." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248 (1986); see also Celotex Corp. v. Catrett, 477 U.S. 317 (1986). A dispute is genuine if the evidence is such that a reasonable jury could return a verdict for the non-moving party. See Anderson, at 254. We review all evidence and make all reasonable inferences from the evidence in the light most favorable to the non-movant. See In re Flat Glass Antitrust Litig., 385 F.3d 350, 357 (3d Cir. 2004). The non-moving party may not rest upon mere allegations or denials of the moving party's pleadings but must set forth specific facts showing there is a genuine issue for trial. Lujan v. Nat'l Wildlife Fed'n, 497 U.S. 871, 888 (1990).

II.

It is undisputed that Safeco issued a payment bond to A&L in the amount of \$54,522,035.70 for the Overbrook Line project as mandated by Pennsylvania law. The bond states in relevant part:

every person, co-partnership, association or corporation who, whether as subcontractor or otherwise, has furnished material or supplied or performed labor in the prosecution of the [work], and who has not been paid therefore,

may sue in assumpsit on this bond, in its own name, and prosecute the same to final judgment for such sum or sums as may be justly due it ...

Labor & Materialman's Bond, at 2. A&L, the general contractor on the Overbrook Line project, subcontracted work to Capital-Williams, LP ("Capital-Williams"). In connection with the project, a closely held Pennsylvania corporation known as Capital Sign Company, Inc., d/b/a Capital Manufacturing ("Capital Manufacturing") contracted with Gateco for the latter to supply and install various fences and canopies. It is undisputed that Employers Insurance of Wausau ("Wausau") issued a payment bond to Capital Manufacturing/Williams Graphics, Inc., Capital Joint Venture in the amount of \$2,732,511.00.

Safeco maintains that Capital Manufacturing and Capital-Williams are distinct legal entities and points out that there is no evidence Gateco had any contractual relationship with A&L or any of its subcontractors. Gateco counters that this court should pierce the corporate veil and hold that Capital Manufacturing is the alter ego of Capital-Williams. Whether or not Capital Manufacturing and Capital-Williams are separate corporations is significant under the law of this circuit. Were we to pierce the corporate veil of Capital Manufacturing and hold it is the alter ego of Capital-Williams, Gateco would be considered a second-tier claimant or a sub-subcontractor of A&L. As such it could proceed against Safeco on the bond Safeco issued to A&L. If, however, we do not pierce the corporate veil, Gateco

would be barred from recovering against Safeco under Nicholson Construction Company v. Standard Fire Insurance Company, 760 F.2d 74 (3d Cir. 1985).

In Nicholson, the City of Philadelphia contracted with a joint venture led by Buckley & Company ("Buckley") as general contractor to build a sewage treatment plant. Buckley obtained a payment bond from various entities collectively acting as sureties, including the Standard Fire Insurance Company. Id. at 75. The bond contained language identical to that set forth above. Id. Buckley subcontracted some work on the sewage project to C. Hannah Construction Company, which in turn subcontracted to Geofreeze Corporation ("Geofreeze"). Geofreeze entered into a subcontract with Nicholson Construction Company ("Nicholson") for specialized drilling services. When Geofreeze did not pay Nicholson for its services, the latter sued the sureties of Buckley on the payment bond. On appeal the issue was whether the phrase "as subcontractor or otherwise" contained in the payment bond covered Nicholson, which was three steps removed from the general contractor. Our Court of Appeals held that third-tier subcontractors such as Nicholson were too "remote from the prime contractor" to fall within the phrase "or otherwise" under Pennsylvania law. Id. at 77. Rather, the language in the bond protects only those entities that have "supplied labor or materials to the prime contractor or his subcontractors." Id.

As noted above, Safeco argues that Nicholson bars Gateco from recovering from it because it did not supply labor or

materials to the prime contractor, A&L, or any of its immediate subcontractors. Gateco does not dispute our description of the holding in Nicholson but urges the court to pierce the corporate veil of Capital Manufacturing and find it is the alter ego of Capital-Williams. In so doing, Gateco would be considered a second-tier claimant under Nicholson with standing to sue Safeco as surety to the A&L and its subcontractors.

III.

"The alter ego concept is a tool of equity [that] is appropriately utilized when the court must prevent fraud, illegality or injustice, or when recognition of the corporate entity would defeat public policy or shield someone from public liability for a crime." Carpenters Health & Welfare Fund v. Ambrose, 727 F.2d 279, 284 (3d Cir. 1983) (internal quotations omitted), overruled on other grounds, McMahon v. McDowell, 794 F.2d 100 (3d Cir. 1986). When two corporate entities are involved, the alter ego theory comes into play when "a subservient corporation is acting as an alter ego of a dominant corporation." Bd. of Trustees of Teamsters Local 863 Pension Fund v. Foodtown, Inc., 296 F.3d 164 (3d Cir. 2002). Our Court of Appeals has explained that

Pennsylvania ... does not allow recovery unless the party seeking to pierce the corporate veil on an alter ego theory establishes that the controlling corporation wholly ignored the separate status of the controlled corporation and so dominated and controlled its affairs that its separate existence was a mere sham. In other words, [] Pennsylvania ... require[s] a threshold

showing that the controlled corporation acted robot- or puppet-like in mechanical response to the controller's tugs on its strings or pressure on its buttons.

Eastern Minerals, 225 F.3d at 333 n.6 (citation omitted).

Our Court of Appeals has set forth certain factors to be considered under Pennsylvania law regarding the specific application of the alter ego theory. They include, but are not limited to, the following: the failure to observe corporate formalities and distinctions; non-payment of dividends; insolvency of the corporation; siphoning the funds from the subservient corporation by the controlling corporation or dominant shareholders; non-functioning of officers and directors; absence of corporate records; the existence of the corporation as a mere facade for the operations of another corporation or a common shareholder or shareholders; and gross undercapitalization. See Lutyk, 332 F.3d at 194; Eastern Minerals & Chem. Co. v. Mahan, 225 F.3d 330, 333 n.7 (3d Cir. 2000). In essence, where one corporation so dominates and controls another to the point where its separate existence is a sham, a court may pierce the corporate veil of the subservient corporation and hold that it and the dominant corporation are one.

There is a strong presumption in Pennsylvania against piercing the corporate veil. Limax Indus., Inc. v. Aultman, 669 A.2d 893, 895 (Pa. 1995). A party that seeks the application of the alter ego theory to pierce the corporate veil bears the

burden of proof to show by clear and convincing evidence that such a remedy is warranted. See Tr. of Nat'l Elevator Indus. Pension, Health Benefit and Educ. Funds v. Lutyk, 332 F.3d 188, 194 (3d Cir. 2003); Kaplan v. First Options of Chicago, Inc., 19 F.3d 1503, 1522 (3d Cir. 1994).

Gateco's contention that Capital Manufacturing is the alter ego of Capital-Williams is based on the affidavit of Debra Winter, the Chief Financial Officer of Gateco and a declaration of Gateco's attorney Anne Manley. Gateco offers no testimony from any officer or employee of either Capital-Williams or Capital Manufacturing to support its contention that this court should pierce the corporate veil. Instead, Gateco relies on its own employee and attorney who do not appear to have any personal knowledge of the structure or operation of either corporation. See Fed. R. Civ. P. 56(e); Brown v. Muhlenberg Twp., 269 F.3d 205, 212 n.5 (3d Cir. 2001). Attached to the affidavit and declaration of Gateco's employee and attorney are various documents. At best these documents show that Capital-Williams and Capital Manufacturing share the same address, as well as some employees and some equipment.

Without more, there is insufficient evidence under Pennsylvania law to pierce a corporate veil and hold the two entities are alter egos. Gateco has provided no evidence that either Capital Manufacturing or Capital-Williams dominated or controlled the other. Gateco has not clearly and convincingly demonstrated that either entity failed to observe corporate

formalities, refused to pay dividends, was insolvent, was a victim of pilfering or syphoning of assets by dominant shareholders or the other corporation, lacked corporate records, was a mere facade for the operations of common shareholders or the other corporation, or was significantly undercapitalized. Furthermore, Gateco has not argued that the failure to pierce the corporate veil will result in fraud, illegality or injustice to innocent parties such as itself or Safeco. In short, Gateco cannot show by clear and convincing evidence that the extreme remedy of piercing the corporate veil is warranted.

Gateco relies on Ragan v. Tri-County Excavating, Inc., 62 F.3d 501 (3d Cir. 1995), to argue that Capital Manufacturing is the alter ego of Capital-Williams because A&L, Gateco, and Safeco have treated the entities as one corporation. Our Court of Appeals held in Ragan that a subcontractor was the alter ego of a general contractor and that therefore the corporations could be treated as one entity. Id. at 509-10. There, a general contractor, Mele Construction Co., Inc. ("Mele"), purchased a bond from Hartford Fire Insurance Company ("Hartford"), as surety, that required any prospective claimant on the bond not in a direct contractual relationship with Mele to give Hartford written notice of any claim within 90 days of completing work. The plaintiff was a union that had a collective bargaining agreement with Tri-County Excavating, Inc. ("Tri-County"), a subcontractor of Mele. The union filed a tardy claim with Hartford and sued when the latter denied it. The union asked the

district court to pierce the corporate veil and hold Tri-County and Mele were alter egos. This district court agreed with the union and the Court of Appeals affirmed. Mele and Tri-County were two entities of a six corporation "group" controlled by the extended family of John Mele. Id. at 506. Tri-County was owned by three daughters of John Mele and over the decades preceding the litigation worked exclusively for Mele. Id. In holding Mele and Tri-County were alter egos, the Court of Appeals noted that the "sole function" of Tri-County was to provide engineers to Mele, its officers knew little or nothing about the daily operation of the corporation, it had never paid a dividend, and was grossly undercapitalized for the work it contracted to perform. Id. Because Hartford treated Tri-County and Mele as one entity, the late 90-day notice did not apply to the union's claim against it.

The facts here are in stark contrast to those in Ragan. Merely showing that Capital Manufacturing and Capital-Williams share the same address and some of the same employees and equipment does not make them alter egos. While the Court of Appeals observed that Hartford, the surety, had consistently treated the two companies as one, the present record is devoid of any evidence that Safeco has treated Capital-Williams and Capital Manufacturing as one corporation during the underlying events of this case. See Ragan, 62 F.3d at 510.

Finally, we note that Gateco is not left without a remedy for the harms it has alleged. At the very least there

appears to be no reason why it could not sue Employers Insurance of Wausau, the surety for Capital Manufacturing. Indeed, in this action Gateco originally sued both Safeco and Wausau. In an order dated October 12, 2005, we held that the forum selection provision in Wausau's bond barred Gateco from proceeding in this venue. Nothing in that order prevents Gateco from suing Wausau or any other appropriate entity for damages.

IV.

In sum, Gateco cannot meet its burden to prove by clear and convincing evidence that this court should pierce the corporate veil of Capital Manufacturing or Capital-Williams in a manner consistent with Pennsylvania law. Accordingly, Gateco is barred under Nicholson from recovering on the payment bond issued by Safeco, and the motion of Safeco for summary judgment will be granted.

IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

GATECO, INC. d/b/a/ GATEWAY INDUSTRIAL SERVICES	:	CIVIL ACTION
	:	
	:	
v.	:	
	:	
SAFECO INSURANCE COMPANY OF AMERICA, and EMPLOYERS INSURANCE OF WAUSAU	:	NO. 05-2869

ORDER

AND NOW, this 24th day of July, 2006, for the reasons set forth in the accompanying Memorandum, it is hereby ORDERED that:

- (1) the motion of defendant Safeco Insurance Company of America for summary judgment is GRANTED; and
- (2) judgment is entered in favor of defendant Safeco Insurance Company of America and against plaintiff Gateco, Inc. d/b/a/ Gateway Industrial Services.

BY THE COURT:

/s/ Harvey Bartle III

C.J.