

**DECISION**



*in Mitchell 11-20*

**THE COMPTROLLER GENERAL  
OF THE UNITED STATES  
WASHINGTON, D. C. 20548**

**8081**

FILE: B-192516

DATE: November 8, 1978

MATTER OF: American Fidelity Fire Insurance Co.

**DIGEST:**

Army, although a mere stakeholder, became liable to Miller Act surety where surety notified Army of unpaid claims against contractor and asserted its prior rights to contract retainages, but where through clerical error, Army mailed final payments to contractor rather than to surety as agreed by all parties. Surety may be paid upon submission of evidence that all outstanding claims have been paid and surety assigns to Government any right it may have to recoup erroneous payments made to contractor.

The Department of the Army, Finance and Accounting Center, Indianapolis, Indiana, has requested a decision as to whether the claim of a bonding company should be paid. The American Fidelity Fire Insurance Company (American Fidelity) has filed claims for \$5,413.15 and \$1,303.96 under Army contracts DAKF48-76-C-A011 and DAKF48-77-C-0013, for modifications to buildings at Fort Hood, Texas. American Fidelity was surety under Miller Act (40 U.S.C. § 270) performance and payment bonds furnished by the prime contractor, H. C. Hodge General Contractors (Hodge). The record indicates the following sequence of events.

On May 10, 1977, counsel for American Fidelity advised the contracting officer that certain claims from subcontractors under DAKF48-76-C-A011 had been received. Because Hodge had not paid these suppliers, the surety requested that all further payments to the contractor be withheld pending further instructions. On June 6, 1977, the surety advised the contracting officer of the contractor's failure to make payments under DAKF48-77-C-0013 and made the same request concerning further payments by the Army under the second contract.

On June 16, 1977, the contracting officer received a letter from Hodge stating that "all monies due or to be due to the contractor under the second contract have been paid."

assigned to American Fidelity." On June 17, 1977, an identical letter was received from Hodge concerning contract -A011.

In letters dated July 13, 1977, the contracting officer advised both the contractor and the surety that the Government considered itself a mere stakeholder in this instance. The contracting officer commented that the assignments did not qualify under the Assignment of Claims Act, 31 U.S.C. § 203, 41 U.S.C. § 15 (1976). It was suggested to both parties that the Army make checks for final payment payable to Hodge and send them to the surety in care of its counsel. The contracting officer requested the contractor and the surety to consent in writing to the proposed procedure. The contractor consented to this payment method.

According to the record, the contracts were completely performed by Hodge. Final payment request and contractor release forms were completed by the contractor, through the surety's attorneys. (The release forms executed by the contractor on September 18, 1977, provided that payment was to be to Hodge and American Fidelity.)

In a letter dated September 26, 1977, surety's counsel returned all necessary forms to the contracting officer with the request that final payment be made jointly to Hodge and American Fidelity and mailed to surety's attorney. Ultimately the surety authorized the final payment checks to be made payable to Hodge and mailed to American Fidelity.

On November 14, 1977, the contracting officer requested that the Army finance office send final payment under both contracts to the contractor and listed the mailing address as that of the surety's attorney. Final payment vouchers dated November 21, 1977, specify payment to H. C. Hodge, but, the contractor's mailing address is indicated.

From December 19, 1977 until mid-January of 1978, the record indicates that the procurement agent made numerous phone calls in a futile attempt to locate

Hodge. American Fidelity was also unsuccessful in its attempts to contact the contractor following his receipt of the checks. The record indicates, however, that at some point the checks were indorsed and cashed by H. C. Hodge.

By letter of January 19, 1978, American Fidelity made demand for immediate payment in the amount of the final payments under both contracts.

While the surety is no longer claiming the rights of an assignee, we note our agreement with the Army's determination that the attempted assignments were improper, since American Fidelity does not qualify as a "financing institution" under the Assignment of Claims Act. Regardless, the central issues here involve the rights of a surety and the obligations of the Government as a stakeholder. As stated in Home Indemnity Co. v. United States, "[t]he rights of the surety in the final contract payment have long been recognized." 376 F.2d 890, 892 (1967). In accordance with the decision of the Court of Claims in that case, immediately upon notification by American Fidelity that Hodge was in default on payments due to various subcontractors, the Army owed a higher duty of care to the surety in regard to the contract retainages.

The facts of Home Indemnity are substantially similar to those presented here. The surety in that case notified the contracting officer of the unpaid claims of subcontractors and requested that no further contract payments be made to the contractor. The contract was fully performed and final payment was claimed by both the contractor and the surety. In pertinent part, the court in Home Indemnity stated:

"When the contract involved here was completed, the Government was the stakeholder of the final payment or security for which there were two contending claimants, the surety and the contractor. In view of [the surety's] equitable rights in the fund, which were superior to those of the contractor, the Government had no right as a stakeholder to settle the question unilaterally by paying the fund to the contractor."

In the instant case, the Army contends that, in mailing the final payment checks to Hodge, it did not attempt to "settle the question unilaterally." Rather, it is the Army's position that the checks were improperly mailed due to a "clerical inadvertence" for which it should not be held liable. While we agree that the Army's purpose was not to settle the question unilaterally, we must conclude that under the circumstances the Army's intention is irrelevant. Our decision here must turn on the effect of the Army's action in mailing the checks to the contractor's address.

In looking to the result of the Army's clerical error, it would appear that the facts of the instant case almost parallel those of Newark Ins. Co. v. United States, 169 F. Supp. 955, 144 Ct. Cl. 655 (1955). In that case the court stated:

"If it is made to appear that the Government's officials, after due notice of the facts giving rise to an equitable right in the [surety], and of the [surety's] assertion of such a right, paid out without a valid reason for so doing, the money in question to someone other than the [surety], the surety will be entitled to a judgment." 169 F. Supp. 955, 957. [Emphasis added.]

Based upon the cases discussed, it is our conclusion that the Army paid funds to Hodge in which American Fidelity had a prior right and, therefore, that the Government is liable to the surety in the amount of the final payments made under both contracts, provided of course, that the surety has not been able to retrieve such payments from the contractor.

As a general rule, for a payment bond surety to share in contract retainages, it must first pay all legitimate claims of the laborers and materialmen irrespective of the limits of its bond. American Fidelity Fire Insurance Co. v. United States, 206 Ct. Cl. 570, 575, 513 F.2d 1375, 1378 (1975); B-163427, March 1, 1968; B-161093, March 6, 1967;

B-155504, November 16, 1965. Moreover, Home Indemnity, supra, is consistent with this rule. American Fidelity may be paid the contract retainages as a payment bond surety when it submits reasonable evidence to the Army that it has paid all the outstanding claims under the contracts and assigns to the Government any right it may have to recoup the final contract payments which erroneously were sent to the contractor.

*R. G. Kinn*  
Deputy Comptroller General  
of the United States