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DECISION

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

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FILE B-187806 DATE: January 11, 1979

MATTER OF Universal Aircraft Parts, Inc.
DL600569

DIGEST:

[Request by Subcontractor For Reimbursement of Cost of Parts Supplied To Prime Contractor]

1. Subcontractor who supplied, but was not paid by, prime contractor (currently the subject of bankruptcy proceedings) with parts and materials for use in performing Government contracts may not recover purchase price of supplies from United States where subcontractor did not establish privity with Government under recognized theories of agency, implication, or third-party beneficiary.

2. Reporting claim to Congress under Meritorious Claims Act for relief of Government subcontractor requesting reimbursement for materials supplied to, but not paid for by, Government prime contractor (currently the subject of bankruptcy proceedings) for use in performing contracts would not be justified because claim contains no elements of unusual legal liability or equity, and to do so would constitute preferential treatment over prime's other unsecured creditors who must satisfy their claims in pending bankruptcy proceeding and over other unpaid subcontractors in similar circumstances.

~~DL600512~~ Universal Aircraft Parts, Inc. (Universal), requests reimbursement from the United States in the amount of $190,753.68 for engine parts and aircraft frames (including attorneys' fees) supplied to Gary ~~DL600545~~ Aircraft Corporation (Gary) for use in performing several United States Air Force contracts (Nos. F41608-71-D-0666, January 1, 1971; F41608-71-D-0289, December 1, 1971; F41608-72-D-1273, April 28, 1972; F41608-73-D-3000, July 27, 1973; F41608-74-D-1054, March 29, 1974; F41603-74-D-1064, April 30, 1974; and F-41608-74-D-1645, September 1, 1974). The claim arises from Gary's failure to pay Universal for approximately $160,000 worth of materials. Universal obtained a judgment against Gary on August 27, 1976, for the claimed amount, but has been

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unable to satisfy the judgment. Alternatively, Universal has requested that we recommend the claim to Congress for private relief under the Meritorious Claims Act, 31 U.S.C. § 236 (1976).

The record shows that by letter of August 25, 1976, the contracting officer notified the Defense Contract Administration Service (DCAS) that Gary was presenting invoices for reimbursement for material it had not paid for and requested DCAS to investigate the practice and to provide a remedy if warranted. In an August 31, 1976, reply DCAS concurred in the contracting officer's conclusion and noted that one of the unpaid suppliers was the General Services Administration (GSA), and that the amount owed GSA was being withheld from monies due Gary until Gary paid GSA. In a letter of June 2, 1978, Universal asks why the same protection could not have been afforded to Universal.

The authority relied upon by DCAS in withholding amounts due GSA from Gary is not apparent from the record. Nevertheless, such action was an appropriate exercise of the common law right of all creditors to apply the unappropriated monies of their debtors in their hands to the extinguishment of debts due. See, United States v. Munsey Trust Co., 332 U.S. 234 (1947); 49 Comp. Gen. 44 (1969).

On October 28, 1976, Gary filed a petition under chapter XI of the Bankruptcy Act, 11 U.S.C. § 721 (1976), and was continued as a debtor in possession of its property and authorized to operate its business pending disposition of the bankruptcy petition. Universal views its chances as a creditor to recover any portion of the amount owed as "extremely dim if not totally hopeless" and has made this claim against the Government on the theory that Gary acted as an authorized agent of the United States in purchasing materials from Universal. The Government has paid Gary for the materials obtained from Universal.

With the exception of the relief provided subcontractors on Government construction contracts under the Miller Act, 40 U.S.C. § 270a (1976), which requires the furnishing of payment bonds by prime contractors, parties contracting with prime Government contractors generally are limited to their remedies at law in any controversy

arising out of the failure of the prime contractor to pay the subcontractor for supplies and services. In similar circumstances, we denied a request by a subcontractor holding a State court judgment against a prime contractor (whose contract was terminated by the Government for convenience) that the Government withhold from its payment to the prime contractor the money owed to the subcontractor and require it to be paid directly to the subcontractor. We held that since there is not privity of contract between the Government and the subcontractor under prime Government contracts, there was no legally permissible way for the Government to enforce the subcontractor's rights against the prime contractor, or for the subcontractor to make a claim directly against the Government. B-160329, November 7, 1966.

However, we have recognized three situations which will establish privity between the subcontractor and the Government.

1. Agency--There is a contractual relationship between a subcontractor and the Government arising from a provision in the prime contract which expressly makes the prime contractor the agent of the Government. 21 Comp. Gen. 682 (1942).

2. Implication--Privity may be implied where a subcontractor furnishes supplies after receiving the Government's express or implied promise to make payment. B-171255, January 5, 1972; B-171868, August 20, 1971.

3. Third-Party Beneficiary--A subcontractor may obtain the benefits of privity as a third-party beneficiary of a Government prime contract. Cf. B-136469, April 30, 1959; B-78596, May 29, 1950; A-18357, February 11, 1930.

Universal contends that Gary was acting as a duly authorized agent for the United States when purchasing the aircraft engine parts and aircraft frames from Universal. We have recognized that where the effect of prime contractors' transactions legally binds the Government to make payment directly to a third party for supplies and services which contractors may order from a third party

for the account of the Government, such contractors may be considered as agents of the Government. 21 Comp. Gen., supra. On the other hand, where the legal effect of the contractors' transactions is to bind themselves, rather than the Government, such contractors may not be regarded as agents of the Government. See, Alabama v. King and Boozer, 314 U.S. 1 (1941), and Curry v. United States, 314 U.S. 14 (1941).

Each of the prime contracts in question is a firm, fixed-price, indefinite-quantity or requirement-type instrument which provides for material reimbursement to the prime contractor. However, the fact that Gary had cost-reimbursement-type contracts with the Government, alone, does not establish its subcontractor's right to payment by the Government. B-175550, December 19, 1972. Construing a similar Government contract which provided that the contractor should be reimbursed for any State or local taxes paid, expressly designated the contractor as the purchasing agent of the Government, and stated that "the Government shall be directly liable to the vendors for the purchase price," the Supreme Court found that the United States was itself the purchaser of materials procured by the contractor as purchasing agent and that no liability of the purchasing agent to the vendor arose from the transaction. Kern-Limerick, Inc. v. Scurlock, 347 U.S. 110 (1953). In the Court's view, not only the contractor's designation as purchasing agent but also the provisions appearing on the purchase order clearly identifying the Government as the actual purchaser were determinative of the Government's liability. The Court noted that the purchase order provisions were in accordance with the contract arrangements making the contractors purchasing agents for the Government and that the contract required specific Government approval to the agent for each purchase. Such circumstances, the Court said, clearly gave no rise to legal liability of the contractor-purchasing agent to the seller.

In our view, the facts of the present case are substantially different. Universal has not pointed out, nor have we found, any language in the prime contracts which expressly designates Gary as a Government purchasing agent or which can be construed to authorize Gary to hold itself out as such. Neither did the contracts require Government approval for Gary's purchases. Further,

the representative purchase orders here, unlike those considered in Kern-Limerick, do not contain express provisions obligating the Government to the vendor for the purchase price. Some of Gary's purchase orders do contain language that the supplies are for the "account of the Government." However, in the absence of an express designation of Gary as purchasing agent, we do not think that the inclusion of such language fell within Gary's authority or that it was sufficient to permit Gary to avoid liability for the supplies. That Gary and not the United States is legally liable for the purchase price of materials ordered from Universal is made apparent by the judgment obtained by Universal against Gary. Accordingly, we must conclude, as apparently did Universal in bringing suit against Gary, that the legal effect of the transactions was to bind Gary to pay for the supplies. Thus, there is no basis on which to find that Gary was acting as an agent for the Government.

All of the prime contracts between Gary and the Air Force included the payment clause found in Armed Services Procurement Regulation § 7-103.7 (1958 Jan.) which states that "the Contractor shall be paid, upon the submission of proper invoices or vouchers, * * * for supplies delivered and accepted or services rendered and accepted." Further, contracts -74-D-1054 and -1064 each requires that proper invoices or vouchers "be supported by contractor paid invoices at time of submission." Contracts -71-D-0289 and -0666 contain language whereby Gary agreed to "support all material charges by paid invoices."

We asked the Air Force to explain how, in the face of the foregoing contract provisions, Gary obtained payment without submitting "contractor paid invoices" with vouchers for reimbursement. We also asked the Air Force to comment on the reason for the inclusion in the four contracts of language requiring submission of "paid invoices." The Air Force replied, in a letter of April 4, 1978, that the additional contract language requiring "paid invoices" was inserted in the four contracts "to provide for reimbursement in the same manner as a standard cost reimbursement type supply contract." Further, the agency noted that:

"* * * The standard ASPR 7-203.4 payment clause for cost reimbursement type supply contracts, entitled, 'Allowable Cost, Incentive Fee and Payment,' defines 'costs' as those recorded costs which have been paid for by cash, check, or other forms of reimbursement. Under this procedure, Gary was to have paid for the materials prior to submitting a voucher accompanied by a statement of cost. Gary did follow a vouchering procedure by which it received provisional payments subject to later audit, but did not always pay its suppliers prior to billing.

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"* * * The 'contractor paid invoice' and 'paid invoices' covenants were included as assurance that Gary Aircraft recognized the requirement for direct materials to be paid for before such costs would qualify as incurred costs for payment purposes."

In this regard, Universal points out by letter of June 2, 1978, that the obligation of Gary to pay for the material prior to submitting vouchers existed under all the contracts, not only those which contained the special provisions regarding "paid" invoices; the requirement in ASPR § 7-103.7, supra, for "proper" invoices or vouchers to be submitted with requests for payment, imposed a duty upon Gary to support submissions by true and accurate invoices and vouchers; and if a voucher falsely indicates that suppliers' costs have been paid, they cannot be deemed as "proper."

The record shows that the procedure under which Gary obtained payment did not require Gary to submit paid invoices with reimbursement vouchers. An internal Air Force telex dated February 14, 1978, justified the procedure as follows:

"The contracts state that the vouchers will be supported by contractor paid invoices at time of submission. We interpret this to mean that the vouchered material costs will be supported by paid invoices and that these

> invoices will be maintained by Gary Aircraft and not submitted with the public vouchers.
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> "The contracts do not require Gary Aircraft to submit paid invoices with its public vouchers for material costs. Prior to voucher payment by the finance officer, DCAA reviews vouchers for material to determine proper billing format, unusual items and compliance with specific contract clauses. After this review, the vouchers are provisionally approved subject to later audit of detailed supporting documentation. Therefore, we would not have knowledge at the time of provisional approval of any delinquent payments of material vendor invoices. The audit approval states: 'Approved for provisional payment subject to later audit.'"

Nevertheless, Universal continues to argue that the vouchering procedure was improper and that the contract provisions required Gary to submit paid invoices as a condition precedent to payment. Our Office has held on numerous occasions that a Government contractor is entitled to be paid even though there are unpaid claims for labor and material outstanding. 52 Comp. Gen. 377 (1972); 37 id. 115 (1957); 23 id. 655 (1944); 10 id. 433 (1931). Even assuming that the contracts' payment provisions can be construed to require submission of a paid invoice with the public voucher, such a construction does not aid Universal's claim in the absence of privity with the United States.

We have noted above that privity will be implied where a subcontractor furnishes supplies on the basis of an express or implied promise of the Government to make payment. In an apparent attempt to establish that the contract provisions when construed to require submission of "paid invoices" imply the existence of privity between the Government and the prime's subcontractors, Universal noted that:

> "The Air Force has enjoyed the benefits of approximately $160,000 worth of materials and engine parts at Universal's expense, but through no fault of Universal. The only party in a position to control the supposed 'reimbursements' to Gary was the Air Force, and the prime contracts payment provisions provided the Air Force with authority to require proof by Gary of the validity of its alleged costs. There can be no doubt that the contract clauses requiring material charges to be supported by 'paid invoices' (or at least by 'proper invoices') were intended to assure control over the reimbursement procedures, and protection of the supplier interests."

Even assuming that the provisions in question were intended to protect Gary's suppliers, we cannot say that they gave rise to a direct contractual arrangement between the Government and the suppliers. In one case in which we found circumstances sufficient to imply privity, the subcontractor had furnished supplies to the prime only after receiving assurances from the contracting officer that he would take steps to see that payment would be made upon receipt of the supplies. It was also shown that the Government had assumed financing of the contract and established a special account from which to make payment. B-171868, August 20, 1971. Here, however, there are no facts in the record to indicate that Universal received any direct assurances of payment from the Government. Further, the record shows that Universal did not become aware of the prime contract provision upon which it now relies until receiving copies of the contracts pursuant to a Freedom of Information Act request made after the aircraft parts were supplied to Gary. Accordingly, we conclude that the requirement for Gary to submit "proper invoices" prior to payment does not give rise to an express assurance of payment by which the Government induced Universal to furnish Gary with supplies.

Further, we cannot view the provisions in question nor the Air Force's use of parts supplied by Universal as an implied promise to pay Gary's subcontractors. Although an implied promise to pay is sufficient to establish privity between the Government and a subcontractor, that

promise, although implied, must still run directly from the Government to the subcontractor. Cf., United States v. Georgia Marble Co., 106 F.2d 955 (5th Cir. 1939); B-147131, March 2, 1962. The record does not show nor does Universal contend that it was induced through any course of direct dealing with the Government, except through Gary, to supply the parts required for the performance of the prime contracts.

Under certain circumstances, a subcontractor may be made a third-party beneficiary of a contract between the Government and a prime contractor. Daniel Hamm Drayage Co. v. Willson, 178 F.2d 633 (8th Cir. 1949); B-136469, April 30, 1959. However, in any third-party beneficiary case, it must appear that the contracting parties had the interest of the third party in mind when they entered into the contract. United States v. Huff, 165 F.2d 720 (5th Cir. 1948). Therefore, before the Government may be held liable, a claimant must demonstrate that the protection of third parties was contemplated. United States v. Aleutian Homes, Inc., 193 F. Supp. 571 (D.C. Alaska 1961).

We believe that the contract provisions relied upon by Universal could be considered protection for Gary's suppliers from nonpayment. However, the payment procedure in each of the prime contracts as implemented by the Air Force included a subsequent audit of Gary's vouchers. Gary's agreement to support material charges with paid invoices also served the purpose of providing the Government protection by insuring that the expenditures for which Gary was reimbursed had actually been made. Universal has not presented any evidence from which we can conclude that "paid invoice" provisions were made a part of the prime contracts for the purpose of protecting subcontractors rather than, or in addition to, the Government. Further, payment by the United States to Universal as a third-party beneficiary of the Government's prime contracts with Gary would require us to imply from the "paid invoice" requirement authority for the Government to have retained a part of the contract price and to settle directly with the subcontractors. Cf., B-160329, November 7, 1966.

In view of the absence of clear evidence as to the reason for including the "paid invoice" provisions in the prime contracts and the doubt raised by the necessity to imply authority for direct settlement with subcontractors from those provisions in order to pay Universal's claim, we must resolve the doubt in favor of that course which will result in the conservation of appropriated funds. Charles v. United States, 19 Ct. Cl. 316 (1884); Longwill v. United States, 17 Ct. Cl. 288 (1881).

Accordingly, Universal's claim for payment under the contracts is denied.

Universal has also requested relief under the Meritorious Claims Act in the event our Office concludes that there is no legal basis to allow reimbursement for materials supplied to Gary. The Meritorious Claims Act provides that when a claim is filed in this Office and may not be lawfully adjusted by use of an appropriation therefor made, but which claim, in our judgment, contains such elements of legal liability or equity as to be deserving of the consideration of Congress, it shall be submitted to the Congress with our recommendations. This remedy is an extraordinary one and its use is limited to extraordinary circumstances.

The cases we have reported for the consideration of the Congress generally have involved equitable circumstances of an unusual nature which are unlikely to constitute a recurring problem, since to report to the Congress a particular case when similar equities exist or are likely to arise with respect to other claimants would constitute preferential treatment over others in similar circumstances. See, B-175278, April 12, 1972. Subcontractors have on other occasions found themselves in similar circumstances whereby the prime contractor was reimbursed for materials supplied by vendors who were in turn unable to collect from prime contractors. In one case where contract termination charges were collected from the Government by the prime on behalf of the subcontractor, the subcontractor could not, in the absence of a contract with the United States, maintain a suit on the ground that equity and good conscience required the Government to make payment a second time. Aerovox Corporation v. United States, 89 F. Supp. 873

(D.C. Mass. 1950). Likewise, we find no unusual elements of law or equity in the present case sufficient to justify a second payment by the Government, particularly where Universal had no contract with the Government and could have refused to extend unsecured credit to Gary.

Further, we are advised that Gary's voluntary bankruptcy proceedings are still pending. In Congressional Reference Case No. 1-72, Arizona Insurance and Investment Co. v. United States, October 29, 1976, the Court of Claims responded to the Senate's inquiry as to whether, relative to a proposed private relief bill, the unliquidated claims of materialmen and laborers of a certain prime Government contractor could be brought against the debtor in the bankruptcy proceedings then pending in relation to the prime contractor and whether they constituted a valid legal or equitable claim against the United States by stating:

> "* * * All the claims made, proven and unproven, could have been brought against the debtor in the pending bankruptcy proceedings, and were so brought. * * *
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> "The United States has not wronged the plaintiff in any way, and plaintiffs have no legal claim against the United States. There is no equitable ground for singling these plaintiffs out from all other suppliers who are excluded from any benefits under the Miller Act. Any payment to plaintiffs would be a mere gratuity."

In the present circumstances, we cannot conclude that Universal has a basis to recover from the Government. We have also been informally advised that Universal has filed a claim against Gary in the pending bankruptcy proceeding. In our view, Universal must look to that proceeding to satisfy its judgment against Gary. Accordingly, we decline to report Universal's claim to Congress since to do so would constitute preferential treatment over Gary's other creditors who also seek to

satisfy claims through the bankruptcy proceedings and other unpaid subcontractors in similar circumstances.

R.F. Keller

Deputy Comptroller General
of the United States