

DECISION



19248 *Ayer*
**THE COMPTROLLER GENERAL
OF THE UNITED STATES**
WASHINGTON, D. C. 20548

FILE: B-199740

DATE: August 26, 1981

MATTER OF: Department of the Army - Request
for Advance Decision

DIGEST:

1. United States may properly assert priority for debts owed to it. Since Small Business Administration (SBA), by virtue of assignment from assignee bank, may, under assignment, declare all of contractor's secured loans to be "due and payable," SBA is owner of loan debts. Thus, contractor's debts are owed to United States and SBA has priority for Federal Government in contract's proceeds.
2. GAO approach in resolving competing private interests of assignee banks and payment bond sureties in contract balances (namely, allowing mutual agreements as to disposition of balances given conflicting court decisions), is not for application where, under assignment, defaulted bank loans secured by assignment are now owed to United States. Thus, SBA may not concede any of contract balance to payment bond surety even if surety has paid all claims under bond.
3. SBA enjoys benefit of "no set-off" provision of Assignment of Claims clause of contract by virtue of assignment from assignee bank. Thus, debt owed SBA has priority over possible IRS lien.

The Corps of Engineers, Department of the Army (Army), has requested an advance decision as to the proper disbursement of \$41,810 constituting the final balance due under contract No. DACW64-73-C-0076 with the Small Business Administration (SBA) which

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subcontracted the entire construction project to Roy L. Owens Interests, Inc. (Owens), in accordance with section 8(a) of the Small Business Act, 15 U.S.C. § 637(a) (1976). Notwithstanding the subcontract, the Army retained the right to administer the contract.

The Army recites that Owens is unwilling to execute the release and suggests that SBA could not properly execute the release on behalf of the company. Consequently, the Army requests our decision as to the proper disbursement of the contract balance of \$41,810.

Based on our review of the record, we conclude that SBA is entitled to all of the funds in question.

Background

The contract was awarded to Owens on January 26, 1973. At that time, the surety executed the required performance and payment bonds. SBA agreed to guarantee the surety 90 percent of any loss that might be sustained under the bonds. On June 18, 1973, Owens assigned the contract proceeds to the bank. This assignment was also 90 percent guaranteed by SBA. On April 18, 1975, the project was completed.

On June 4, 1975, Owens requested the surety's assistance under the payment bond. Later in June, the bank assigned its interest in the contract proceeds to SBA. Thereafter, the surety moved to block any further payments by the Army to either Owens or the bank, as assignee.

On October 5, 1975, Owens submitted several claims against the Army related to the contract. Throughout 1976, Owens and the Army negotiated the claims. A tentative settlement in the amount of \$41,810 was reached; however, on September 13, 1976, Owens disavowed it. Subsequently, on June 14, 1977, the Army contracting officer issued a final decision on the claim in the amount of \$22,767. On July 29, 1977, Owens appealed the contracting officer's decision to the Armed Services Board of Contract Appeals (ASBCA). There ensued 2 more years of further negotiation

between Owens and the Army; on July 2, 1979, the parties agreed to a settlement in the amount of \$41,810. On August 20, 1979, in view of the settlement, the ASBCA dismissed Owens' appeal with prejudice.

It appears from the record that the Internal Revenue Service (IRS) may have a lien for unpaid taxes amounting to \$16,000 against Owens. SBA also states that it paid the assignee bank \$62,103.61 or 90 percent of the bank's loss of \$69,004.01 under its loan to Owens. The SBA further states that the "bank assigned the note and all the collateral to SBA at the time of SBA's purchase of the loan guaranty." It is also clear that the surety expended approximately \$67,600 to pay off various suppliers and subcontractors under the payment bond and that SBA reimbursed the surety 90 percent of its loss, or approximately \$59,700.

The SBA has proposed that the SBA and the surety share the \$41,810 balance in proportion to a 90-10 share formula reflecting the reimbursement of the SBA and the remaining loss of the surety under the payment bond.

In K.B.J. Engineering, Inc., B-190181, December 8, 1977, 77-2 CPD 445, involving a similar SBA guarantee to a surety, we agreed that "SBA would be subrogated to the rights of the surety" when the surety was reimbursed for its loss. Nevertheless, we consider it unnecessary to determine the rights of SBA to the contract balance as a subrogee of the surety. In our view, SBA may properly assert priority for the Federal Government as to the Owens' bank debt of \$62,103.61 which must now be viewed as owed to the United States.

The United States may properly assert priority for debts owed to it. As stated in United States v. Brocato, 403 F.2d 105 (5th Cir. 1968), concerning that court's holding in Bulls v. United States, 356 F.2d 619 (5th Cir. 1966):

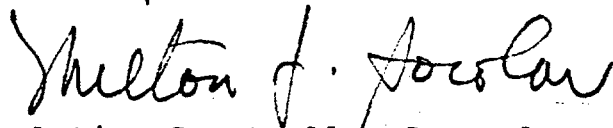
"* * * we held that the Federal Housing Commissioner could not assert any priority for the Federal Government until the mortgage title was actually acquired by

the Federal Housing Commissioner through the foreclosure proceedings. In other words, it was not until the foreclosure that a debt was due the United States
* * *."

The present record contains a copy of the assignment which was transferred to the SBA concerning the proceeds of the contract. Under the "Obligation" section, the assignment listed all "advances, of whatever type, by bank to debtor," as being secured by the assignment and gave, "to the benefit of [the bank's] assigns," the right, among other rights, to "declare all obligations secured hereby immediately due and payable" upon Owens' default. Further, the bank gave the assignment "without recourse" to the SBA. Especially since SBA was given the right to declare all of Owens' obligations to the bank to be "due and payable," we consider that SBA is the owner of the debts. Thus, Owens' debts must be considered to be owed to the United States and the SBA has priority for the Federal Government in the contract proceeds in accordance with the above precedent.

SBA has proposed to permit the surety--assuming the surety has paid all claims under the payment bond--to recover \$4,181 or 10 percent of the balance. This proposal may reflect its recognition of our precedent which allows a competing assignee and surety to "settle their differences by mutual agreement" in recognition of conflicting court decisions concerning the respective rights of assignees and sureties in these circumstances. See Air Force Request for Advance Decision, B-198100, December 16, 1980, 80-2 CPD 433, and court decisions cited. The conflicting court decisions stem from situations where only competing private interests were involved, however, unlike the case here. To apply our precedent here would effectively ignore the court's decision in Bulls v. United States, above, which held that the Federal Government has priority for debts owed to it regardless of how the debt originated. Thus, SBA may not concede any of the contract retainage to the surety by means of a "mutual agreement."

As between the SBA and the IRS--to the extent an IRS tax lien exists against Owens--it is our view that SBA may take advantage of the "no set-off" provision of the Assignment of Claims clause of Owens' contract. That clause expressly permitted reassignment of the bank's assignment to any Federal lending agency in addition to providing that the assignee was to take the assigned proceeds free from setoff. Thus, the SBA takes the proceeds of the contract even if there is an IRS lien.

A handwritten signature in dark ink, reading "Milton J. Fowler". The signature is written in a cursive, flowing style with a large initial "M".

Acting Comptroller General
of the United States