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Overview of the Miller Act Subcontractor Protection in Federal Projects

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Summary

The Miller Act ("Act") protects persons who have furnished labor or materials to contractors engaged in the construction, alteration, or repair of any public building or public work of the United States. The measure was enacted in 1935, in response to protests by subcontractors and suppliers about their inability to collect their debts from contractors. The Act requires a government contractor to post two surety bonds, a performance bond and a payment bond, in any federal construction contract in excess of $100,000.[1] The performance bond guarantees the United States that the construction work will be performed to completion. The payment bond assures payment to subcontractors and suppliers supplying labor and materials in the course of performance of the contract. Any subcontractor or supplier who has so furnished labor or material under a contractual relationship with the contractor and who has not been paid in full within 90 days after the last labor was performed or material supplied, may bring suit on the payment bond for the unpaid balance. Subcontractors and suppliers to second or lower-tiered subcontractors are not protected by the Miller Act.

The remedy under the Miller Act is exclusive. The Miller Act is designed to protect those persons who cannot take advantage of state lien laws because of United States Government involvement in the transaction.[2] Consequently, the payment bond required by the Miller Act is in lieu of state mechanic's liens.

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[1] There is no such requirement where the work under contract is to be performed in a foreign country. See 40 U.S.C. § 270a(b).

[2] See F.D. Rich Co. v. United States for the Use of Indust. Lumber Co., 417 U.S. 116 (1974) (The Act was designed as an alternative to the mechanic's lien available in ordinary private construction disputes because a lien cannot attach to government property).

This short report is divided into three sections. The first section summarizes the substance of the Act. The second section provides the historical and legislative developments of the Act. Finally, the third section highlights recent legislative and legal developments under the Act.

The Miller Act

The Miller Act[3] provides that, before a contract that exceeds $100,000[4] in amount for the construction, alteration, or repair of any building or public work of the United States is awarded to any person, that person shall furnish the United States with the following:

1) A performance bond which constitutes a guarantee that the construction work will be performed to completion and is in an amount that the government's contracting officer regards as adequate for the protection of the United States.[5] The bond amount is normally 100 percent of the contract price.[6]

2) A separate payment bond which protects and assures payment to subcontractors and suppliers supplying labor and materials in the course of performance of the contract.[7] The sum of the payment bond is equal to 50 percent of the contract price when the contract is less than $1 million and 40 percent when the contract is from $1 - 5 million.[8] Contracts in excess of $5 million require a payment bond in the amount of $2.5 million.[9]

The Miller Act payment bond covers first-tiered subcontractors and suppliers of material who have direct contacts with the prime contractor.[10] These are called first-tier claimants.[11] Subcontractors and material suppliers, who have contracts with a subcontractor,[12] are also covered and are called second-tier claimants.[13] Anyone further down the contract chain is considered too remote and cannot assert a claim against a Miller Act payment bond posted by the contractor.[14]

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[3] 40 U.S.C.A. § 270a-f.

[4] 40 U.S.C.A. § 270d-1.

[5] 40 U.S.C.A. § 270a(a)(1).

[6] See 48 C.F.R 28.102-2(a).

[7] 40 U.S.C.A. § 270a(a)(2).

[8] Id.

[9] Id.

[10] 40 U.S.C.A. § 270b(a).

[11] See J.W. Bateson Co. v. United States ex rel. Board of Trustees, 434 U.S. 586, 594 (1978).

[12] Id.

[13] J.W. Bateson, supra, Id.

[14] F.D. Rich Co. v. United States for the Use of Indust. Lumber Co., 417 U.S. 116, 122 (1974).

A subcontractor or supplier who has a direct contact with the prime contractor has no duty to provide any notice to the prime contractor before filing a suit on the bond.[15] When the claimant is a second-tier subcontractor or material supplier, however, formal notice must be given to the prime contractor within 90 days of the last date the claimant furnished labor or material for the project.[16]

The final step in perfecting a claim on a payment bond is filing a lawsuit. For both first and second-tier claimants, suit must be filed no sooner than 90 days after the last labor and material were furnished and no later than one year after that date.[17] Suit must be brought in the name of the United States for the use and benefit of the person suing and filed in the federal district court in which the contract was to be performed.[18]

The Army, Navy, Air Force, or Coast Guard may waive cost-plus-a-fixed fee and other cost-type contracts from the applicability of the Miller Act.[19] The Secretary of Transportation may waive contracts pertaining to vessels from the applicability of the Miller Act.[20]

Historical and Legislative Developments

In response to protests by subcontractors and suppliers of government construction contractors about their inability to collect their debts, Congress passed the Heard Act in 1894.[21] Before the passage of the Heard Act, a subcontractor or supplier of a government contractor had little recourse against the government contractor, since the subcontractor or supplier could not assert a lien against property owned by the United States. Government contracts awarded during that period only rarely had clauses requiring the prime contractor to pay its debts to subcontractors and suppliers or permitting the government to withhold payments to the contractor if it did not.[22]

The Heard Act granted a right of action in the name of the United States against a prime contractor and its surety for unpaid labor and materials used in the prosecution of contract work. In 1905, Congress amended the Heard Act by adding the phrase "labor or materials used in the construction of any public building or public work."[23] This expression placed a heavy burden of proof on subcontractors and suppliers seeking to recover from a surety. As a condition to establishing a liability on the bond, the

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[15] 40 U.S.C.A. § 270b(a).

[16] Id.

[17] 40 U.S.C.A. § 270b(b).

[18] Id.

[19] 40 U.S.C.A. § 270e.

[20] 40 U.S.C.A. § 270f.

[21] Heard Act, 28 Stat. 278 (1894).

[22] Greenville Savings Bank v. Lawrence, 76 F. 545 (4th Cir. 1896).

[23] Heard Act, 28 Stat. 278 (1894), as amended by the Act of February 24, 1905, 33 Stat. 811.

subcontractor or supplier had to show that the supplies or labor furnished were necessary to and wholly consumed in the prosecution of the contract work.[24]

Occasionally, it was difficult for the courts to determine whether particular labor or materials had a relation to the object of the contract so as to fall within the coverage of the Heard Act. Under the Heard Act, as amended, a subcontractor or supplier was required to bring its suit within one year after final settlement of the contract. The subcontractor or supplier could not at the time of delivery determine whether a particular transaction was covered by the Act because conceivably the supplies might not be used in the prosecution of the work. Coverage could only be determined after the work was completed, and the right of action did not arise until six months afterwards.

Noting these deficiencies, Congress repealed the Heard Act and replaced it with what is popularly referred to as the Miller Act in 1935.[25] As originally enacted, the Miller Act applied to all construction contracts exceeding $2,000 awarded by the United States Government. The threshold amount was subsequently raised to $25,000,[26] and finally to $100,000.[27] Congress also amended the Miller Act to delete references to final settlement and established a one-year statute of limitations for the filing of Miller Act suits by subcontractors and suppliers.[28]

The passage of the Miller Act resulted in the simplification of the burden of proof for recovery for subcontractors and suppliers. While it covers the same subject matter as the Heard Act, the Miller Act eliminated the term "used." Thus, subcontractors and suppliers now have a less onerous burden of proof, since the "consumed in prosecution of the work" test has been replaced by the "reasonable expectation of consumption."[29]

A surety cannot expect the subcontractor or supplier to always be in a position to prove that all the material and equipment supplied by the subcontractor and supplier was used by the prime contractor in the particular project protected by the bond. Therefore, the subcontractor or supplier must prove only that the material or equipment was furnished by it with reference to the particular contract and was accepted by the prime contractor for use in the fulfillment of the government contract.[30]

Recent Legal and Legislative Developments

Legal precedent establishing the Miller Act is quite settled. Legal disputes centering around the Act are largely fact specific.

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[24] Brogan v. National Surety Co., 246 U.S. 257 (1918).

[25] Miller Act, 49 Stat. 793 (1935) (current version at 40 U.S.C. § 270a-f).

[26] Miller Act, 49 Stat. 793, as amended by Act of November 2, 1978, 92 Stat. 2484.

[27] Miller Act, 49 Stat. 793, as amended by Act of October 13, 1994, 108 Stat. 3341.

[28] Miller Act, 49 Stat. 793, as amended by Act of August 4, 1959, 73 Stat. 279.

[29] United States ex rel. Byrne & Co. v. Fire Association of Philadelphia, 260 F.2d 541 (2d Cir. 1958).

[30] Aetna Casualty & Surety Co. v. Circle Equipment Co., 377 F.2d 160 (D.C. Cir. 1961).

The latest legislative development under the Miller Act has come in response to small contractors and subcontractors who were unable to obtain surety bonding due to industry underwriting standards. Congress passed the Small Business Administration Reauthorization and Amendment Act of 1988[31] which established a preferred surety bond guarantee program. This program assists small business contractors and subcontractors by extending payment and performance bond guarantees to a surety against losses in order to make bonding more easily available.[32]

In establishing the program, Congress intended to encourage major surety companies to participate in the program by delegating the Small Business Administration's (SBA) authority to approve surety companies to issue bonds without prior SBA approval.[33] Specifically, the Act allows the SBA to authorize any surety, without further SBA approval, to issue, monitor, and service surety bonds subject to the SBA guarantee provided the SBA determines that such surety has underwriting expertise and the capability to approve, issue, monitor and service such bonds.[34]

Ordinarily, a contractor or subcontractor would apply for bonding through its surety. The surety will either deny or approve the application based upon the information contained in the application. In the case of small businesses which might not meet industry standards, the surety has the option to forward the application to the SBA for a bonding guarantee. In this case, the surety would provide the bonding if the SBA guarantees the issued bond against losses if the small business breached the contract. If the SBA denies the application, the surety would not provide the bonding. The preferred surety bond guarantee program, operates as a third option for the small business contractor or subcontractor. A preferred surety bond insurer has already been approved by the SBA for the authority to issue SBA guaranteed bonding without the SBA's approval. Therefore, when the small business concern applies for bonding, a preferred surety bond insurer, can approve the application immediately. The benefit to the surety is that it can approve the application without SBA approval and can still get reimbursed, for up to 70% of any loss incurred in the breach of the contract.[35] The benefit to the small business concern is that it may receive bonding when it did not qualify for SBA approval or when a surety would not provide the bonding unless it was reimbursed by the SBA for the loss.

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[31] The Small Business Administration Reauthorization and Amendment Act of 1988, P.L. 100-590, 102 Stat. 2989.

[32] H.R. Rep. No. 100-694 (1988), reprinted in 1988 U.S.C.C.A.N. 3999, 4010-11.

[33] Id. at 4010.

[34] Id. at 4011.

[35] 8 C.F.R. § 115.68.