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United States General Accounting Office
Washington, DC 20548

Office of
General Counsel

In Reply
Refer to: B-196704

AUG 11 1980

C. G. Caras
General Counsel
Maritime Administration
U.S. Department of Commerce
Washington, D.C. 20230

Dear Mr. Caras:

Subject: Applicability of Cargo Preference Act of 1954 to Subcontractors on Federal Contracts

By letter of November 1, 1979, you request that we concur in your opinion that § 901(b)(1) of the Merchant Marine Act, 1936, as amended, 46 U.S.C. § 1241(b)(1) (1976) (Cargo Preference Act), applies to shipments of equipment, materials and commodities by subcontractors and suppliers in the fulfillment, directly or through an intermediate tier, of the ultimate requirements of Federal Government procurement contracts for construction and supplies.

The Cargo Preference Act states in pertinent part that:

"(1) Whenever the United States shall procure, contract for, or otherwise obtain for its own account . . . any equipment, materials, or commodities, within or without the United States . . . the appropriate agency or agencies shall take such steps as may be necessary and practicable to assure that at least 50 per centum of the gross tonnage of such equipment, materials, or commodities . . ., which may be transported on ocean vessels shall be transported on privately owned United States-flag commercial vessels * * *." [emphasis added]

In your submission, you state your belief that the statute's language is general and not limited to the finally assembled product. You assert that any manufactured product procured, contracted for or otherwise obtained incorporates items supplied

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by subcontractors and suppliers and thus these items are subject to the Cargo Preference Act. You believe that the statute's language and its legislative history support your view. You also refer to Senate Commerce Committee correspondence with Executive Departments which you believe demonstrates the intent of Congress and the Departments that subcontractors on Government contracts must comply with the Act.

We agree with your opinion to this extent. We believe the Cargo Preference Act is applicable to subcontractors where the subcontracted item is the end product or service that the United States is essentially contracting for or the subcontracted item or service is clearly identified to a Government contract.

As we have consistently noted in prior decisions, the Cargo Preference Act was enacted to assure that at least 50 percent of Government-sponsored cargoes transported on ocean vessels would be moved on privately-owned United States-flag ships. Congress believes that this requirement is necessary to the maintenance of an adequate merchant fleet. 55 Comp. Gen. 1097 (1976); S. Report No. 1584, 83d Cong., 2nd Sess. 1 (1954); 100 Cong. Rec. 4158, 4159 (1954); 39 Comp. Gen. 758, 760 (1960). In a Presidential Directive in 1962, President Kennedy stated that, "The statutes . . . are designed to insure that U.S. Government-generated cargoes move in substantial volume on American-flag vessels." S. Report No. 2286, 87th Cong., 2nd Sess. 43, 44 (1962).

The legislative history of the Cargo Preference Act supports a broad application of the Act to Federally owned or financed ocean cargoes purchased here or abroad. See 100 Cong. Rec. 8227-28, (1954). The Senate Report on the Cargo Preference Act stated that the Act:

> "plugs existing loopholes . . . with respect to . . . programs financed in any way by Federal funds . . . and eliminates the . . . procedures by which a high percentage of exports from this country, and offshore purchases contracted for, financed or furnished by the United States, have been routed in foreign vessels in violation of the spirit if not the letter of existing cargo-preference legislation."

S. Rep. No. 1584, 83d Cong., 2nd Sess. 5 (1954).

We also note that the 1954 Cargo Preference law was enacted to codify and broaden existing law, not to derogate from it. 41 Op. Atty. Gen. 192, 196 (1954); 42 Op. Atty. Gen. 203 (1963).

With respect to the language of the Act, Cargo Preference applies, whenever the United States shall procure, contract for or otherwise obtain for its own account equipment, materials or commodities. The language literally does not refer to subcontractors. However, we have previously stated that the Cargo Preference Act applies to the shipment of cargo whose purchase is financed by the United States. B-155185, November 17, 1969.

There is no difficulty with regard to application of the Act to shipments made for the United States after it has acquired title to the commodities, etc., involved since these are clearly items identifiable as procured, contracted for or otherwise obtained for the Government's account. Senator Butler, the primary proponent of the 1954 Cargo Preference legislation, stated that, ". . . the bill covers only cargoes which are paid for or owned by the Government. It has nothing to do with any other commerce of the U.S." 100 Cong. Rec. 8227 (1954).

In our view, when the Government contracts it generally seeks an end product or service and we believe that shipments of these items are subject to the Cargo Preference Act. Thus, in B-155185, November 17, 1969, we determined that the Agency for International Development (AID) was financing the procurement of urea for use in Asia and that the place of packaging was incidental to the procurement for purposes of the Cargo Preference Act. Once the shipment of urea was identified with the AID procurement, the Cargo Preference Act applied.

However, a subcontractor or supplier of raw materials, as an example, may not necessarily identify a particular shipment as consigned for a Government contract. In our decision, B-194528, March 3, 1980, 59 Comp. Gen. ___, it was our opinion that the language, the legislative history, and our prior decisions concerning the Cargo Preference Act did not support application of the Act where there was an inability to identify particular purchases as Government-financed. We believe the same theory is applicable to procurement by subcontractors where the purchases or work performed are not necessarily paid for with Federal funds.

Thus, we believe the Cargo Preference Act would be applicable where the subcontracted item is the end product or service that the United States essentially contracted for or the subcontracted item or service is clearly identified to a Government contract.

For example, if DOD contracts with a United States firm to supply and install a generator and the United States' firm subcontracts for the generator with a foreign firm, the Cargo Preference

Act would apply to the shipment of the generator to the United States. However, a prime contractor who contracts with the Government to supply helicopter engines and imports certain parts from foreign sources would not necessarily be required to comply with the Cargo Preference Act unless either the parts could be considered the essential items contracted for and not just incidental to the ultimate goal of contract, or alternately, the parts could be clearly identified to the Government contract.

In this connection, DOD's position with regard to issuance of duty-free certificates to subcontractors for defense items imported from foreign sources is instructive.

With regard to purchases abroad, the Defense Acquisition Regulations (DAR) (1976 ed.) § 6-603.2 authorizes issuance of duty free entry certificates to subcontractors only as follows. First, cost reimbursement type subcontractors are authorized to ship duty free where no fixed-price prime or fixed-price subcontract intervenes between the purchaser and the Government, in other words where there is a direct relationship between the Government and the subcontractor. Second, cost reimbursement, cost type, or fixed price subcontractors are authorized to ship duty free where a fixed-price prime or fixed-price subcontract intervenes between the purchaser and the Government, provided that,

> ". . . the subcontractors concerned certify that the supplies so purchased are to be delivered to the Government or incorporated in Government-owned property or in an end product to be furnished to the Government, and that the duty will be paid if such supplies or any portion thereof are utilized for other than the performance of the Government contract . . ." DAR § 6-603.2(c) (1976 ed.)

Thus, duty free benefits inure to subcontractor shipments on DOD prime contracts where either there is no intervening prime or subcontractors between the Government and the purchaser or where the shipment is clearly identified to a Government contract. Under similar circumstances, we believe the Cargo Preference Act could be extended to subcontractors.

In considering your request for an opinion, we note that application of the Cargo Preference Act to particular shipments will depend upon the circumstances and specific facts of the case. In this connection, in prior decisions, this Office has applied

the Cargo Preference Act in situations where the United States does not have an owner's interest in the shipments of materials because "reliance upon the circumstances involved to support non-applicability would operate as a device to evade the purpose of the Act." B-155185, supra, 39 Comp. Gen. 758 (1960). However, we do believe that individual agencies such as DOD have certain discretion to determine when the Cargo Preference Act does apply, see, for example, DAR § 1-1402 (1976 ed.), and we would not question such a determination without substantial evidence that the agency's action operates as a device to evade the purpose of the Act. B-155185, supra, 39 Comp. Gen. 758.

Sincerely yours,

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Milton J. Socolar
General Counsel