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Contract Has Been Awarded... NOW WHAT? Subcontracting Compliance (From TA to SubK, Key Provisions, Flowdowns, L.O.S., SB Subcontracting Plans, and more!)



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Overview

- Teaming Arrangements (from TA to SubK)
- Key Subcontracting Provisions
- Flowdowns under the FAR
- Prime/Sub Workshare Issues
- Limitations on Subcontracting and Performance of Work Requirements
- Small Business Subcontracting Plans
- Questions



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Disclaimer

The following presentation is for informational and educational purposes only and does not constitute legal advice. For legal advice on specific situations and circumstances, please contact an attorney familiar with federal Government Contracting regulations.



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Teaming Arrangements

- FAR 9.601 “Contractor team arrangement” defined as follows:
 - (1) Two or more companies form a partnership or joint venture to act as a potential prime contractor; or
 - (2) A potential prime contractor agrees with one or more other companies to have them act as its subcontractors under a specified Government contract or acquisition program.
- FAR 9.602 General Description
 - (a) Contractor team arrangements may be desirable from both a Government and industry standpoint in order to enable the companies involved to—
 - (1) Complement each other’s unique capabilities; and
 - (2) Offer the Government the best combination of performance, cost, and delivery for the system or product being acquired.



Teaming Arrangements, cont.

- Under FAR 9.601 BOTH JVs and Teaming Agreements are considered “Teaming Arrangements”
- High Level - Teaming Agreements vs. JVs
 - Teaming Agreement – only ONE party with direct contractual privity with the Government
 - No enforcement rights between Subcontractor and the Government
 - Joint Ventures – BOTH parties have contractual privity with the Government
 - Enforcement rights between parties governed by the JV Agreement and there are enforcement rights between BOTH contractors and the Government



Teaming Arrangements, cont.

- When do federal contractors form Teams or JVs?
 - When a contractor needs outside:
 - Strengths/capabilities/qualifications
 - Expertise
 - Staffing
 - Financial/bonding capability
 - Concern about revenue for Size purposes
 - Need a firm commitment, locked-in via a JV or teaming agreement, with the teammate
 - REVIEW THE RFP! Many times, Solicitations require the TA or JV Agreement to be submitted with the Prime's proposal



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Teaming Arrangements, cont.

- When else are Teaming Agreements used?
 - For SBA small business or other socio-economic set-aside procurements, when a large business wants to participate with small business (the large business would be ineligible to bid directly); and/or,
 - One or both of the Teammates want to lock each other in, and perhaps lock in pricing/work-share should government award the Contract to the Prime Contractor



From TA to Subcontract

- There are risks associated with entering into teaming agreements Cyberlock Consulting, Inc. v. Info. Experts, Inc. (EDVA Apr. 3, 2013)
- Court found the Teaming Agreement entered into to be UNENFORCEABLE under Virginia law
- Teaming Agreement considerations (from both Prime and Sub Perspective)
 - Shall award, may award, negotiation
 - Scope of work, percentage of work
 - Price
 - Terms of Subcontract



Entering Into the Subcontract Post-Award

- FIRST, Look to the terms of the Teaming Agreement
 - Teaming Agreement should be clear on obligations to negotiate (and any timelines), obligations to award a Subcontract, and potentially agreed upon terms (work share) for the Subcontract
- If negotiations are delayed, consider a Letter Contract, ATP, or similar stop-gap measure



Privity of Contract and Contract Administration

- The Subcontractor does NOT have privity of contract with the Government
- Why does this matter?
 - Payment
 - Disputes
 - Changes
 - Claims
 - Contract administration issues
 - Communication with the Government customer



Agency Consent to Subcontract

- In certain circumstances, the Agency may be required to consent to subcontracts
 - Particularly in cost-reimbursement, time-and-materials, labor-hour, and certain larger fixed-price scenarios
- Additionally, the Agency may require advanced notification of subcontracting
- This potential for Agency Consent should be accounted for in all Teaming Agreements
 - i.e., the Prime should be sure that “Agency Consent” is a prerequisite to Subcontract, if required



Key Provisions for Inclusion and Negotiation

- Definition of Subcontractor's Work
- Term and Termination
- Disputes/Dispute Resolution
- Protection of Confidential Information/Intellectual Property
- Litigation (Choice of Law/Forum/Venue)
- Indemnity Provisions
- Non-Solicit/Non-Hire



Definition of Subcontractor's Work

- In set-aside procurements, Prime Contractor MUST comply with the limitation on subcontracting/ self-performance requirements of 13 C.F.R. 125.6
- Problems with 50/50 split (with services contracts)
- Split of Revenue (must define)
- Non-traditional Subcontracts (i.e., profit split/incentive fee)
- Clear definition of work – reference to S.O.W.



Subcontract Period of Performance

- The Term/Period of Performance of the Subcontract should be consistent with the Prime Contract (including option periods)
- Because of the potential for modifications, Subcontractors should be sure to include ANY extensions of the prime contract (through modification or otherwise)



Termination for Convenience/Default

Pro-Prime Teaming Agreement

Termination for Default/
Convenience:

- No “material” default required, minimal cure period
- T for C NOT tied to Customer Termination for Convenience

Pro-Sub Teaming Agreement

Termination for Default/
Convenience:

- Tied to MATERIAL default, 10-30 day cure period
- T for C TIED to Customer Termination for Convenience



Disputes

Pro-Prime Teaming Agreement

- Prime contractor has exclusive discretion to decide whether to pursue dispute in mediation, arbitration or litigation
- Exclusive forum selection clause (where to file), typically favorable to the prime

Pro-Sub Teaming Agreement

- Specify mediation, arbitration or litigation
- Forum of dispute resolution should be the place of the project



Dispute Resolution Mechanisms

1. Requirement for written notice of claim
2. Time limit for filing written claim
3. Negotiation first by upper-level management within limited number of days
4. Mediation as a condition precedent to arbitration
5. Arbitration to be filed within a limited number of days if mediation unsuccessful
6. Arbitration hearing to take place within specified time period



Litigation

- Mediation as a condition precedent to Litigation
- Choice of Law Provision (which law applies?)
- Perhaps the MOST Important litigation provision – Choice of FORUM AND VENUE
- Costs of Litigation
- Injunctive Relief (confidentiality, employment, etc.)
- Attorneys' Fees
 - One-way provision (stay away from these)
 - Prevailing party provision
 - “reasonableness” of attorney’s fees



Protection of Confidential/ Proprietary Information

- Parties should already be parties to a Confidentiality Agreement/NDA
- Should provide for the identification and disclosure of confidential information (i.e. “marking” requirements)
- Provision should not be so onerous that parties will not comply, exclusions for publically available info and other circumstances
- Provide for appropriate level of care
- Provide a term that allows for injunctive relief in the event confidentiality terms are breached



Protection of Intellectual Property

- For IP, both parties RETAIN IP brought into the Subcontracting relationship (Patents, Trademarks, Copyrights)
- Typically, joint ownership of any IP created by the Prime and Sub working together—however, carefully review
- Look out for “work for hire” and IP assignment language
- If there is a possibility that valuable IP may be developed as part of the subcontract work, it is recommended to have an attorney review these terms



Indemnification

- Indemnification provisions (like insurance requirement provisions) should always be reviewed by attorney AND insurance professional
- Key is to always push for mutuality – always push back against one-sided indemnity provisions
- Not uncommon for Primes to attempt to obtain indemnification even in the event of the Prime's own negligence (typically gross negligence is the standard)
- If possible, exclude indemnity for negligence caused by other party



Non-Solicitation/Non-Hire

- Subcontracts typically include provisions to prevent the “poaching” of employees during contract performance and for a certain additional period
 - Sometimes these provisions are mutual, but sometimes unilateral
- Terms must not be too restrictive and account for an employee’s freedom to seek out publicly posted job opportunities
- Closely review LENGTH of Restriction



FAR Flowdowns: *5 Unfortunate Realities*

- Prime Contractors tend to “flow down” ALL FAR clauses, whether required or not
- Subcontractors tend to accept those flowdown clauses
- Very few parties read the ENTIRE contract/ subcontract
- Even fewer read the FAR/DFARS clauses UNTIL there is a problem
- Sooner or later, there will be a problem



Flowdown of FAR Clauses

- Almost all commercial contracting relationships have an outside regulatory/legal compliance component (i.e. environmental, labor/employment, etc.)
- Same for U.S. Government contracts
- The FAR additionally mandates that certain contract clauses be “flowed down” to subcontractors in order to implement U.S. Government policies covering everything from cyber security to labor, employment, and socioeconomic issues to data and patent rights



Flowdown of FAR Clauses

- Clauses included in the Prime Contract are what binds the Prime and Subcontractors
 - *But...* a legal doctrine known as the “Christian Doctrine” could read these clauses into the Prime Contract anyway
- Myth – ALL FAR clauses in the Prime Contract must be flowed down – WRONG
 - Mandatory vs. Non-Mandatory Flowdown Clauses



Mandatory vs. Non-Mandatory Flowdowns

- Mandatory Flowdowns:
 - Specifically require the Prime to include them in subcontracts
 - Mandatory Flowdowns are NOT NEGOTIABLE
- Non-Mandatory Flowdowns
 - Prime contract does NOT explicitly require the prime to include in subcontracts
 - Even so, Prime must ensure subcontractor compliance with requirements of Prime contract
 - Several clauses should also be flowed down even if not required (e.g., Changes and Termination for Convenience clauses)



What if Mandatory Clauses are not Flowed Down?

- The Prime Contractor
 - Could be found to be in breach of Prime Contract and subject to numerous remedies, including, but not limited to, withholding of payments, termination of contract for default and suspension or debarment
- The Subcontractor
 - Possibly could be subject to mandatory flow downs, even if not included in subcontract, under the “Christian Doctrine” (though, U.S. District Court decisions have been inconsistent on this point)
 - Key to determining this is whether the requirement is part of a regulatory scheme applicable to subcontractor anyway



How Can I Tell if Clause Needs to be Flowed Down?

- Read the clause—it will specify
 - Some clauses MUST be flowed down verbatim
 - “Contractor shall include this clause in subcontracts”
 - Other clauses can be modified
 - “Contractor shall include the substance of this clause in subcontracts”
- Read the text reference that prescribes use of the clause (e.g., conditions or thresholds)



Contract Type/Value Matters for Flow Downs

- Type of goods or services
 - Commercial Items vs. Non-Commercial Items
- Prime and subcontract payment terms
 - Fixed price vs. Cost Reimbursement
- Contract value
 - Multiple value thresholds included throughout FAR
 - OFCCP/Socio-Economic Clauses: \$10,000
 - Simplified Acquisition Threshold: \$250,000 (FAR 2.101)



Typical Flowdown Clauses

- The FAR flowdown clauses below are required in commercial items contracts:

1	FAR 52.203-13	Code of Business Ethics and Conduct
2	FAR 52.203-15	Whistleblower Protections Under the American Recovery and Reinvestment Act
3	FAR 52.203-19	Prohibition on Requiring Certain Internal Confidentiality Agreements or Statements
4	FAR 52.204-21	Basic Safeguarding of Covered Contractor Information Systems
5	FAR 52.204-23	Prohibition on Contracting for Hardware, Software, and Services Developed or Provided by Kaspersky Lab and Other Covered Entities



Typical Flowdown Clauses

6	FAR 52.204-25	Prohibition on Contracting for Certain Telecommunications and Video Surveillance Services or Equipment
7	FAR 52.219-8	Utilization of Small Business Concerns
8	FAR 52.222-21	Prohibition of Segregated Facilities
9	FAR 52.222-26	Equal Opportunity
10	FAR 52.222-35	Equal Opportunity for Veterans
11	FAR 52.222-36	Affirmative Action for Workers with Disabilities
12	FAR 52.222-37	Employment Reports on Veterans
13	FAR 52.222-40	Notification of Employee Rights Under the National Labor Relations Act



Typical Flowdown Clauses

14	FAR 52.222-50	Combat Trafficking in Persons
15	FAR 52.222-55	Minimum Wages under Executive Order 13658
16	FAR 52.222-62	Paid Sick Leave Under Executive Order 13706
17	FAR 52.224-3	Privacy Training
18	FAR 52.225-26	Contractors Performing Private Security Functions Outside the United States
19	FAR 52.232-40	Providing Accelerated Payments to Small Business Subcontractors
20	FAR 52.247-64	Preference for Privately Owned U.S.-Flag Commercial Vessels



Typical Flowdown Clauses

- For Non-Commercial Items Contracts, additional clauses would be required covering issues such as:
 - Anti-kickback
 - Audit and records requirements
 - Patent rights
 - Cost or pricing data
 - Service Contract Act
 - DFARS Cyber Clause
- Subject to the value and type thresholds discussed earlier



How to Incorporate the Flowdown Clauses in the Subcontract

- A generic “comply with all requirements of the prime contract” (or similar language) does not cut it
 - See, e.g., U.S. ex rel. Quality Tr., Inc. v. Cajun Contractors, Inc., 486 F. Supp. 2d 1255 (D. Kan. 2007)
- Review and modify terms and conditions for non-mandatory flowdowns (i.e. changes, termination, etc.)
- Include the mandatory clauses at least by reference in a list or table and some language modifying to the prime-subcontractor relationship
- From the Prime perspective: best practice to include additional protective language as well



Prime/Sub Workshare

- Considerations:
 - Teaming Agreement Terms
 - Prime Contract Requirements
 - For Small Businesses – specific workshare and self-performance requirements
 - Much more to come on Limitations on Subcontracting



JV Performance of Work Requirement

- For any Small Business (or other set-aside category) JV, *the small business MUST perform at least 40% of the work performed by the Joint Venture*
 - *This should NOT be confused with the Limitation on Subcontracting*
- The work performed by the small business (or other set-aside category) MUST be more than administrative or ministerial functions so that it gains substantive experience
- The amount of work done by the JV partners will be aggregated, and the work done by the small business (or other set-aside category) must be 40% of the total done by BOTH of the JV partners (excluding third-party subcontractor work)
 - In determining compliance, the work done by a Mentor and any “affiliate” of the Mentor at any subcontracting tier will be counted



Limitations on Subcontracting/Self-Performance Requirement

- Limitation on Subcontracting Rule is a self-performance requirement that prevents small business Prime Contractors from acting as “pass throughs”
- The Rule is found in both the Small Business Regulations and the FAR
- Over the last few years, the two sets of rules have been inconsistent
- Although the DFARS has been updated (through a class deviation), the FAR STILL has not been updated to be consistent with the SBA regulations



Limitations on Subcontracting, etc.

- Applies to ALL Small Business and Socio-Economic Set-Asides
 - Importantly, does NOT explicitly apply to Small Business Subcontracting (i.e., small business and socio-economic work as prime and sub under a subcontracting plan)
- Generally, the NEW Rule (i.e., the SBA Rule and the DFARS/DoD Rule) bases compliance on REVENUE RECEIVED by the small business
 - Based on a Percentage of TOTAL CONTRACT VALUE
 - Ability to subcontract to “Similarly Situated” entities
- The LOS Rule is different for each type of contract



Limitations on Subcontracting, etc.

- Here is the rule for Small Business and Socio-Economic Set Aside Contracts for Services:
 - In the case of a contract for services (except construction), [the small business] will not pay more than 50% of the amount paid by the government to it to firms **that are not similarly situated**. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded.



Limitations on Subcontracting, etc.

- Here is the rule for Small Business and Socio-Economic Set Aside Contracts for Supplies:
 - In the case of a contract for supplies or products (other than from a non-manufacturer of such supplies), it will not pay more than 50% of the amount paid by the government to it to firms ***that are not similarly situated***. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded. Cost of materials are excluded and not considered to be subcontracted.



Limitations on Subcontracting, etc.

- Here is the rule for Small Business and Socio-Economic Set Aside Contracts for General Construction:
 - In the case of a contract for general construction, it will not pay more than 85% of the amount paid by the government to it to firms ***that are not similarly situated.*** Any work that a similarly situated subcontractor further subcontracts will count towards the 85% subcontract amount that cannot be exceeded. Cost of materials are excluded and not considered to be subcontracted.



Limitations on Subcontracting, etc.

- Here is the rule for Mixed Contracts:
 - Where a contract combines services and supplies, the contracting officer shall select the appropriate NAICS code. . . The contracting officer's selection of the applicable NAICS code is determinative as to which limitation on subcontracting and performance requirement applies. In no case shall the requirements of [both supplies and services] both apply to the same contract. The relevant limitation on subcontracting . . . ***shall apply only to that portion of the contract award amount.***



Limitations on Subcontracting, etc.

- “Similarly Situated Entities” and “own employees”:
 - A small business concern prime contractor that receives a [set-aside contract] and spends contract amounts on a subcontractor that is a similarly situated entity shall not consider those subcontracted amounts as subcontracted for purposes of determining whether the small business concern prime contractor has violated [the limitation on subcontracting] ***to the extent the subcontractor performs the work with its own employees.*** Any work that the similarly situated subcontractor does not perform with its own employees shall be considered subcontracted SBA will also exclude a subcontract to a similarly situated entity from consideration under the ostensible subcontractor rule [13 CFR 121.103(h)(4)].



Limitations on Subcontracting, etc.

- Independent Contractors:
 - Work performed by an independent contractor shall be considered a subcontract and may count toward meeting the applicable limitation on subcontracting where the independent contractor qualifies as a similarly situated entity.



Limitations on Subcontracting, etc.

- “**Similarly situated entity**” is a subcontractor that has the same small business program status as the prime contractor. This means that: For a HUBZone requirement, a subcontractor that is a qualified HUBZone small business concern; for a small business set-aside, partial set-aside, or reserve a subcontractor that is a small business concern; for a SDVO small business requirement, a subcontractor that is a self-certified SDVO SBC; for an 8(a) requirement, a subcontractor that is an 8(a) certified Program Participant; for a WOSB or EDWOSB contract, a subcontractor that has complied with the requirements of part 127. In addition to sharing the same small business program status as the prime contractor, *a similarly situated entity must also be small for the NAICS code that the prime contractor assigned to the subcontract the subcontractor will perform.*



Limitations on Subcontracting, cont.

- Penalties (including MANDATORY fines of at least \$500,000)
 - The proposed rule provides that violations of an applicable subcontracting limitation may result in a variety of significant penalties, *including suspension, debarment, administrative remedies, fines, and even imprisonment. If a fine is imposed as a result of a violation, the fine will be “the greater of either \$500,000 or the dollar amount spent in excess of the permitted levels for subcontracting.”*



Limitations on Subcontracting, cont.

- The FAR Rule (FAR 52.219-14)
 - Services (except construction). At least 50 percent of the cost of contract performance incurred for personnel shall be expended for employees of the concern.
 - Supplies (other than procurement from a nonmanufacturer of such supplies). The concern shall perform work for at least 50 percent of the cost of manufacturing the supplies, not including the cost of materials.
 - General construction. The concern will perform at least 15 percent of the cost of the contract, not including the cost of materials, with its own employees.
 - Construction by special trade contractors. The concern will perform at least 25 percent of the cost of the contract, not including the cost of materials, with its own employees.



Small Business Subcontracting Plans

- Small Business subcontracting requirements are in place to further help flow government contracting dollars to small businesses
- Generally, the Prime Contractor will be required to submit a Small Business Subcontracting Plan and then comply with reporting requirements during contract performance
- Requirements generally found in FAR Subpart 19.7 and the clause at FAR 52.219-9 SMALL BUSINESS SUBCONTRACTING PLAN (Jun 2020)



Who Is Required to Submit Small Business Subcontracting Plans?

- Requirement generally included in all contracts that is expected to exceed \$750,000 (\$1.5 million for construction)
- But, not required for:
 - Small business concerns;
 - Personal services contracts;
 - OCONUS Contracts or Contract Mods; or
 - Modifications that are within the scope of the contract and the contract does not contain the clause at 52.219-8, Utilization of Small Business Concerns (i.e., contract was originally under the SAT).



What Is Required for Small Business Subcontracting Plans?

- Small Business Subcontracting Plans must contain all the required elements found at FAR 52.219-9 SMALL BUSINESS SUBCONTRACTING PLAN (Jun 2020)
- Generally:
 - Must outline goals for small businesses and specific socioeconomic categories (including percentage and dollar amounts)
 - Assurances that Prime Contractor will comply in good faith with the plan, submit required reports, participate in studies, and flow down required FAR clauses involving small business subcontracting



What are the Prime Contractor's Obligations under the Plan?

- The Prime Contractor must make a “good faith effort” to meet its small business subcontracting goals
- The Small Business Regulations and the FAR outline examples such as:
 - Negotiating in good faith with small businesses
 - Conducting market research and outreach efforts
 - Announcing opportunities in a timely manner to encourage small business participation
 - Timely submission of Subcontracting Reports
 - Maintaining records and designating an employee to manage the program



What are the consequences of non-compliance?

- Consequences for failure to make the good faith effort described before can be quite severe
 - Clause at FAR 52.219-16 LIQUIDATED DAMAGES-SUBCONTRACTING PLAN (Jan 1999) provides for liquidated damages in a probably amount “equal to the actual dollar amount by which the Contractor failed to achieve each subcontract goal.”
 - Small Business Regulations state that non-compliance is a “material breach” of the contract – grounds for a Termination for Default
 - False Claims Act liability
 - Bad Past Performance ratings in CPARS



How Does the Prime Contractor Determine Size?

- The Prime Contractor assigns a certain NAICS Code to the Subcontract (best practice to include this prominently in the Subcontract)
 - Code should “best describe[] the product or service being acquired by the subcontract.”
- Prime Contractor can rely in good faith upon the subcontractor’s representation as to its size/status
 - Can look either to the subcontractor’s SAM reps/certs or a separate written certification
- Consequences for Subcontractor size/status misrepresentation



Prime Contractor Best Practices

- Ensure plans are accurate and track with small business goals
- Ensure subcontracts contain robust protections (e.g., clear representations, indemnification, correct flowdowns)
- Designate an employee to maintain a compliance file and track all reporting requirements
- DOCUMENT all compliance efforts!!



QUESTIONS???

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