

SUBCONTRACTING SHORTCOURSE

By Andrew Mohr and Kelly Kroll

In times of economic turmoil commercial entities often turn to the federal marketplace to try and recoup falling commercial revenue. Yet dealing directly with the federal government presents unique challenges and requirements akin to wading waist deep through a vat of melted marshmallows. As an alternative to direct contracting, newbie vendors often choose to subcontract with federal prime contractors rather than placing themselves in a prime contract with the federal government. While subcontracting is a good way of sticking in one's toes to test the waters (or melted marshmallows), subcontracting with federal prime contractors presents its own set of issues. This article tries to identify some of the more common problems we see subcontractors make repeatedly and suggests ways to avoid them.

Reject Unnecessary Flow Downs. Once awarded a federal contract, the prime contractor is obligated to pass on or "flow down" certain federal regulations contained in its federal contract to subcontractors that the prime contractor hires to work on the federal contract. Out of an abundance of caution or pure laziness, however, most prime contractors flow down all the federal clauses in their prime contract regardless of their applicability to the subcontract. Subcontractors, eager to seal the deal, often agree to these clauses without a thought. But accepting these clauses has serious implications. For example, prime contractors often flow down clauses containing cost or pricing data disclosure requirements, clauses implicating the Cost Accounting Standards or clauses providing the prime contractor with unintended data and property rights. In reality, these clauses apply to very few subcontracts. Small business subcontractors are exempt from many of these provisions and vendors of commercial items exempt from many more. In fact, for commercial items the list of clauses that a prime must flow

down to its subcontractors can usually be counted on one hand. To avoid unintended consequences, a subcontractor should review its subcontract very carefully and either strike out clauses that don't apply or mark such clauses as inapplicable. This process may hold up the subcontract negotiations by a few days, but is well worth it in the end.

Carefully Carve Out the Scope of Work. All too many times the scope of work to be performed under a subcontract is not carefully defined, leading to misunderstandings between the parties. Subcontractors sometimes begin working outside the scope of the original contract, so when issues arise, the terms of the subcontract are ineffective to resolve the dispute. Of particular importance is any limitation of funds or costs provisions that may cap the amount the federal prime contractor is required to pay. If the scope of work changes, subcontractors should strive to modify the subcontract in writing to correspond to the changed work.

Price Carefully. Prime contractors are notorious for asking subcontractors for their Most Favored Customer ("MFC") pricing, or GSA Schedule pricing if the subcontractor is a GSA Schedule vendor. Before providing such pricing, however, a subcontractor should review its other existing contracts to make sure it hasn't already provided MFC pricing to another customer, or, in the case of GSA Schedule pricing, inadvertently trigger a price reduction. Obviously a subcontractor can't provide MFC pricing to everyone; someone's got to get the best price. With respect to GSA, what triggers a price reduction varies from one subcontractor to the next, but many subcontractors labor under the mistaken notion that because the end user is the federal government, that providing GSA pricing to a federal prime contractor never triggers a price reduction. This simply is not the case. Prime contractors are considered commercial customers, and depending on the deal negotiated with GSA, a great price to a prime contractor could result in a price reduction under the subcontractor's GSA Schedule.

Negotiating Tips. Read the fine print and don't be afraid to make revisions to the subcontract language. If a flow down clause doesn't apply, then tell the prime that it is inapplicable and notate the subcontract as such. Prime contractors usually have no issue with striking certain clauses once apprised of their inapplicability. With respect to pricing, let the prime contractors know up front of your limitations on pricing. This may be a deal breaker, but subcontractors must be able to walk away from unprofitable work.

Teaming Agreements. Before a subcontractor helps a prime contractor with its proposal effort, they should be sure to enter into a Teaming Agreement stating the parties rights and obligations during the proposal process and upon award. While Teaming Agreements are sometimes less than perfect from the subcontractor's perspective, a written Teaming Agreement gives the subcontractor more rights than it would have on a handshake. A carefully worded Teaming Agreement can help a subcontractor get the work promised at a fair price. At a minimum, the Teaming Agreement should require the prime to identify the subcontractor as a member of its team, and require the prime to award a subcontract to the subcontractor if the prime gets the award.

In sum, prime – subcontractor relations and negotiations are a matter of give and take. And that doesn't mean the subcontractor always has to take it on the chin. To paraphrase a well-known rock song, a subcontractor may not always get what it wants, but if it tries sometimes, it will get what it needs.

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