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# **Incorporating FAR Subcontractor Flowdown Terms in Government Contracts: Guidance for Primes and Subs**

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Today's faculty features:

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Elizabeth N. Jochum, Member, **Smith Pachter McWhorter**, Tysons Corner, Va.

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# Incorporating Prime Contract “Flow-Down” FAR Clauses in Government Subcontracts: Guidance for Primes and Subs

**Devon E. Hewitt**, Protorae Law PLLC

**Elizabeth Jochum**, Smith Pachter McWhorter PLC

February 6, 2020

# Presenter Biography

## Devon E. Hewitt



- Represented all types and all sizes of government contractors in over 150 protests before federal agencies. SBA, GAO and the Court of Federal Claims
- Editor, ABA Guide to Service Contracts Flow-Down Terms and Conditions
- Routinely drafts and negotiates teaming agreements, subcontracts, joint venture agreements, M&A agreements, and non-disclosure/non-compete/non-solicitation agreements

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**Practice**

- Government Contracts
- Litigation/Disputes
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**Education**

- University of Virginia School of Law, JD
- Smith College, BA

**Bar Admission**

- Virginia
- District of Columbia

# Presenter Biography

## Elizabeth N. Jochum



- Government contracts counseling and dispute resolution
- Bid protests and claims before the GAO and COFC
- Teaming agreements and subcontract negotiations and disputes
- Government investigations, audits, False Claims Act investigations and litigations

<ul style="list-style-type: none"><li>◆ Elizabeth Jochum, Partner</li><li>◆ Smith Pachter McWhorter</li><li>◆ 703-839-8135</li><li>◆ ejochum@smithpachter.com</li><li>◆ Tysons, VA</li></ul>	<p><b>Practice</b></p> <ul style="list-style-type: none"><li>• Government Contracts</li><li>• Litigation and Dispute Resolution</li><li>• False Claims Act Defense</li></ul>	<p><b>Education</b></p> <ul style="list-style-type: none"><li>• Antonin Scalia Law School, George Mason University, JD</li><li>• University of Virginia, BA</li></ul>	<p><b>Bar Admission</b></p> <ul style="list-style-type: none"><li>• Virginia</li></ul>
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# Understanding the FAR Flow-Down Process

## ◆ Need to understand:

- The Federal Acquisition Regulation (“FAR”) and its applicability to government prime contracts
- Prime government contractor’s responsibility to “flow-down” a prime contract clause
- What qualifies as a subcontract
- The difference between mandatory and discretionary “flow-down” clauses
- How to “flow-down” FAR clauses
- Risks associated with “flowing-down” prime FAR contract clauses to subcontractors
- Interplay between standard subcontract terms and conditions and prime contract clauses “flowed-down” to a subcontractor

# The Federal Acquisition Regulation (“FAR”)

- ◆ **Set of regulations that govern federal procurements and the management and administration of government contracts**
  - Some agencies have agency-specific “supplements” to the FAR regulations; i.e., the Department of Defense (known by “252” reference)
- ◆ **The regulations primarily address responsibilities of agency officials but some provisions apply to contractors directly**
- ◆ **With respect to government contracts, the FAR instructs agency officials to include certain contract clauses in government prime contracts which also need to be included in subcontracts**

# The Federal Acquisition Regulation (“FAR”) *cont.*

- ◆ FAR clauses are included in Part 52 of the FAR
  - FAR 52.000- 52.214-35
- ◆ Each FAR clause refers back to the FAR provision that requires the FAR clause to be included in a government prime contract
- ◆ Each FAR clause contains a date reflecting a version of the language of that clause
  - FAR 52.203-13 – Contractor Code of Business Ethics and Conduct (Oct 2015)

# FAR Clauses Incorporated Into Prime Contracts

- ◆ **Nearly all FAR clauses included in a prime contract are non-negotiable**
- ◆ **Many FAR clauses implement general policies associated with the Government's role in distributing taxpayer dollars**
  - Clauses address equal opportunity and affirmative action, labor, bribery/ethics, drug control, and clean air/water issues etc.
- ◆ **Many factors determine which FAR clauses will be included in a prime contract**
  - Type of prime contract, value of prime contract, purpose/nature of prime contract

## Issues Prime Should Consider Before “Flowing-Down” a FAR clause

- ◆ What does the FAR consider a “subcontract”?
- ◆ Is the FAR clause mandatory or discretionary or applicable to the subcontract work?
- ◆ How does the prime “flow-down” the FAR clauses in its prime contract to the subcontractor?
- ◆ What risks are created with respect to “flowing-down” a FAR clause to a subcontractor?

## What does the FAR consider a “subcontract” or “subcontractor”?

- ◆ Many FAR clauses include language requiring the prime contractor to flow-down the clause to its subcontractors
  - E.g. “The Contractor shall include the substance of this clause, including this paragraph, in subcontracts that...”
- ◆ But FAR doesn’t include a standard definition of “subcontract” or “subcontractor”
  - The Section 809 panel (convened to address acquisition reform) stated that the FAR and DFARs have 27 “separate, sometimes overlapping, definitions’ of “subcontractor”

## What does the FAR consider a “subcontract” or “subcontractor”? *cont.*

- ◆ Common approach is to consider any contractor that is providing goods and services identified in the prime contract’s scope of work a subcontractor
- ◆ Contractors that provide goods and services that benefit the *company as a whole* or enable a company to perform the contract work generally are not considered a subcontractor for the purpose of the “flow-down” process

# Is the FAR clause Mandatory and Applicable to the Subcontract Work?

- ◆ **Mandatory clauses are those that include language requiring prime contractor to include a “substantially similar” clause in its subcontracts**
  - Failure of a prime to comply with FAR clause “flow-down” obligations may lead to contractor being terminated for default
- ◆ **FAR includes a “matrix” that shows mandatory/discretionary nature of each FAR clause (48 C.F.R. Subpart 52.301)**
- ◆ **Not all mandatory flow-down FAR clauses are applicable to the subcontract work**
  - FAR clauses in prime contract may apply only to contracts above or below certain dollar thresholds /certain types of contracts (i.e., fixed price, cost reimbursement/certain types of work (i.e., supplies vs. services, international vs. domestic etc.)

# “Flow-downs” for Commercial Item Subcontracts

- ◆ Subcontracts for commercial items are subject to fewer “flow-down” requirements than other subcontracts
- ◆ Commercial items are defined at length in FAR 2.101, but generally include items customarily used by the public for “non-governmental purposes”, as well as minor modifications, evolutions, combinations and support services provided for such items
- ◆ Only clauses identified in FAR 52.244-6 are required in subcontracts for commercial items or commercial components
- ◆ The FAR then permits the prime to flow down “a minimal number of additional clauses necessary to satisfy its contractual obligations”

# “Flow-downs” for Commercial Item Subcontracts

- ◆ **FAR 52.244-6 Subcontracts for Commercial Items, requires the prime contractor to flow down no more than 10 clauses, some of which are only required under certain circumstances:**
  - 52.203-13, "Contractor Code of Business Ethics and Conduct"
  - 52.203-15, "Whistleblower Protections Under the American Recovery and Reinvestment Act of 2009"
  - 52.219-8, "Utilization of Small Business Concerns"
  - 52.222-26, "Equal Opportunity"
  - 52.222-35, "Equal Opportunity for Special Disabled Veterans, Veterans of the Vietnam Era, and Other Eligible Veterans"
  - 52.222-36, "Affirmative Action for Works with Disabilities"
  - 52.222-39, "Notification of Employee Rights Concerning Payment of Union Dues or Fees"
  - 52.222-50, "Combating Trafficking in Persons"
  - 52.247-64, "Preference for Privately Owned U.S.-Flag Commercial Vessels"

# If discretionary, is it still necessary to “flow-down” the FAR clause to a subcontractor?

- ◆ Prime contractor should assess its risk exposure and the subcontractor's role in prime contract performance
  - Buy American Act clauses
  - Trade Agreements clauses
  - Changes
  - Termination for Convenience
  - Stop Work Order
  - Intellectual Property Clauses

# How does a prime contractor “flow-down” a FAR clause to a subcontractor?

- ◆ **Most common method is to include an appendix or attachment to a subcontract identifying the FAR “flow-down” clauses**
  - Appendix or attachment typically “flows down” *all* prime contract FAR clauses
  - Prime contractor typically includes a “substitution paragraph” in the subcontract indicating that the term “prime contractor” should be substituted any time the term “agency” or “Contracting Officer” is referenced in a FAR “flow-down” clause etc.
- ◆ **Some primes include a broad statement in a subcontract that all obligations of the prime flow-down to the subcontractor**
  - Subcontractor should reject or delete this clause

# Risks Associated with FAR Flow-down Process

## ◆ ***Christian Doctrine***

- Based on case called *G.L. Christian & Assoc. v. United States*, 312 F.2d 418 (Ct. Cl. 1963)
- FAR clause not physically in prime contract may be incorporated by reference in the prime contract if mandated by law or regulation
- But certain public policy FAR clauses are incorporated as a matter of law in subcontracts such as clauses relating to affirmative action, labor issues, equal opportunity

## ◆ **General Substitution and Dates**

- Ensure that subcontract “flow-down” clauses have due dates in advance of due dates included in prime contract FAR clauses
- Version control
- Include exemptions in substitution paragraph

# Risks Associated with FAR Flow-down Process

- ◆ **Inconsistencies between subcontract terms and conditions and FAR clauses in an attachment/appendix**
  - Subcontract is a mix of commercial terms and FAR clauses
- ◆ ***Order of Precedence clause***
  - Order of Precedence clause in body of contract will affect outcome if the provisions of a FAR “flow-down” clause in an attachment conflicts with a provision in the body of subcontract
  - FAR Order of Precedence clause

# Risks Associated with FAR Flow-down Process

## ◆ *Disputes*

- **Commercial**
  - Choice between courts/arbitration
  - Can make losing party pay dispute fees
  - Parties negotiate limitation on liability provisions
- **FAR**
  - Requirement that performance must continue notwithstanding a dispute
  - Subcontractor has no privity with the Government, needs “sponsorship” language
    - Separate disputes provisions into two categories: disputes with the government and disputes with the prime contractor
    - Prime contractor should ensure that its liability for disputes with the Government is not greater than subcontractor’s recovery from the Government

# Risks Associated with FAR Flow-down Process

## ◆ *Changes clause*

- **Commercial**
  - Modification to subcontract terms only with mutual consent
- **FAR**
  - Government can make unilateral changes to drawings, designs or specifications
  - Method of shipping or packing
  - Place of delivery
  - Must submit claim within 30 days if contractor wants an “equitable adjustment” in cost/price or schedule as a result of the change

# Risks Associated with FAR Flow-down Process

## ◆ *IP Clauses*

- **Commercial**
  - Work for hire
  - License
  - Patent
- **FAR**
  - Government license rights vs. prime contractor rights
  - Legending requirements
  - Patent filing protocol
  - Limitation on use of subcontractor IP

# Risks Associated with FAR Flow-down Process

## ◆ *Termination*

- **Commercial**
  - Termination for default, opportunity to cure
  - Either party can terminate upon reasonable notice
- **FAR**
  - Prime contractor must stop work immediately
  - Prime contractor must deliver works in progress
  - Prime contractor must file termination claim within 1 year
    - Prime contractor should adjust claim due date in subcontract
    - Subcontractor should only accept unilateral termination if government terminates prime contract unilaterally

# Prime Contractor Best Practices

- ◆ **Prime wants to transfer all risk to subcontractor**
  - Most large contractors have generic documents that list FAR flow-down clauses in different columns that vary according to type of subcontract (FFP v. CPFF, domestic vs. international, supplies vs. services etc.)
- ◆ **Include provision in subcontract that allows prime to “flow-down” clauses added during contract performance (new versions, *Christian doctrine*)**
- ◆ **Ensure that timeframes in “flow-down” clauses allow prime adequate time to comply with FAR clauses in prime contract**
- ◆ **Be careful to ensure that “flow-downs” are consistent with subcontract terms and conditions**

# Practical Tips for Managing Mandatory “Flow-down” FAR clauses

- ◆ **Build matrices or documents with mandatory “flow downs” based on contract value, type and government agency**
  - Non-commercial
  - Commercial
  - DOD
  - Other agency
  - IDIQ/GWAC-specific
  - FFP/CP/T&M/LH
  - Goods vs
- ◆ **Cross-reference with prime contract**
- ◆ **Ensure frequent review for regulatory changes**

# Subcontractor Best Practices

- ◆ Reject blanket statements
- ◆ Ask for list of prime contract “flow-down” clauses; don’t accept vague references in subcontract
- ◆ Ensure that general substitution paragraph includes “as applicable” language
- ◆ Include IP/audit/government property exceptions to general substitution paragraph
- ◆ Strike those clauses clearly inapplicable to the work
- ◆ Negotiate language of discretionary FAR clauses “flowed-down”
- ◆ Identify potentially inconsistent subcontract provisions

# Resources

- ◆ **American Bar Association, Section on Public Contract Law**
  - Guide to Supply Flow-Down Clauses
  - Guide to Services Flow-Down Clauses
- ◆ **National Defense Industrial Association**
  - *Study of the Applicability of FAR Clauses to Subcontracts Under Prime Defense and NASA Contracts*
- ◆ **Large Contractors**
  - Lockheed Martin and other contractors publish subcontract terms and conditions on their websites