

APTAC Body of Knowledge Competency Guide

C. Basics of Contracting with Government Entities

C.14 Subcontracting – General Principles

Description

A subcontract is an agreement whereby a party which has entered into a contract with another party to perform a certain scope of work enters into a separate agreement with a third party to perform a portion of its scope on its behalf. Therefore, subcontracting involves multiple levels of relationships in performance of a contractual scope of work. However, the direct legal relationship between two parties, known as “privity”, is limited to adjacent levels only, so there is never any privity between the customer and the contractor’s subcontractor(s). Thus, subcontract management is both a professional discipline and an art.

Terminology. The ultimate end user is typically referred to as the “customer”, usually the government agency. The agreement between that customer and its contractor is known as the “prime contract”, prime meaning first tier in a series of cascading relationships. When the prime contractor engages a third party for a portion of the prime contract scope of work, that third party agreement is known as a “subcontract”, from the Latin word for “under”. When the subcontractor engages yet another party to perform a portion of the subcontract, that action is loosely called “subbing out” and the agreement is known as a “lower tier subcontract”. When multiple tiers, or levels, are involved, they are usually referred to by the number of tiers below the original prime contract, as 1st tier, 2nd tier, 3rd tier subcontracts. Included in the term “subcontract” are purchase orders, leases, consultants, inter-departmental transfers, and all other acquisitions within the contract scope.

Benefits and risks. Various features of the subcontracting relationship may differ depending on whether the client is the prime contractor or a subcontractor, and whether the customer is federal, state, or local, and which industry is involved (construction, R&D, manufacturing, services, for example). A few points are summarized below.

What it means to the customer. The customer is receiving goods or services from a 3rd party it has no contractual relationship with. The customer is relying on the prime contractor to take responsibility for the entire scope, including what the 3rd parties do. If the customer has other prime contractors working on the same project (such as A/E consultants in addition to a General Construction Contractor), the customer has to ensure the relationships are maintained correctly.

What it means to the prime contractor. The contractor has a huge responsibility for satisfying the customer with the entire scope including all subs. Failure by a subcontractor never excuses the prime contractor from this responsibility, and the contractor can be held in default for failure of a subcontractor. The contractor must manage all privity issues. The contractor might have to finance the whole job and must manage performance and quality by all subcontractors. The prime contractor is relying on its 3rd party subcontractors in order to satisfy the customer. Socio-economic policies and laws require that large prime contractors must have an approved Small Business Subcontracting Plan and most large contractors are required to have approved purchasing procedures.

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What it means to the subcontractors. They are delivering items to a customer that is not the end user, since their immediate customer is an upper-tier sub or the prime, not the government. So, acceptance of their work depends on their customer's customer being satisfied. In this crack-the-whip game, the lowest-tier subcontractor is at the end of the whip. Often, the lower tiers don't even know who their customer's customer is.

A teamwork approach. The above examples of complexities encountered in multi-tier relationships illustrate the importance of all parties involved being on good terms with each other. The government is never a party to the subcontract, but is certainly interested in the success of each subcontract to ensure success of the project. The prime contractor is responsible for maintaining control of the project management and contract management functions, and success depends heavily on good communications and documentation, with mutual respect and professionalism. A large complex project can benefit greatly from weekly progress meetings that include all involved parties, with minutes promptly distributed, and with errors promptly corrected. With modern technology, these meetings need not require time-consuming trips to a central location; often the project team is in one location and subcontractors might be in various other locations, connected via teleconference. The more complex the project, the more important is the attention that must be given to a teamwork approach, and to including people who are skilled in functioning as a team.

Counseling clients. The PTAC counselor should ascertain which role the client is in before advising them, because the advice might be different for a subcontractor than for the sub's customer. Because a subcontract is, by its nature, a complex matter involving multiple tiers, the client should be asked to provide its entire document to the counselor. Unfortunately, unsophisticated clients may have no written agreement and the problem might require legal advice. The counselor can explain the problem but not the solution, and may provide a list of attorneys that are competent in government contracts law, for the client to select from, or explain how to contact the Public Law Section of the American Bar Association for a referral. The DLA will not reimburse the PTAC for resources utilized in helping the client sue the government and PTACs typically have a policy of not providing any legal advice even if a counselor has a law degree. In any event, the counselor should make sure the client reports the subcontract award for the PTAC's 1806. See Sections 14.1, 14.2, 14.3, and 14.4 for more detailed information on Subcontracting.

References and resources

Books published by Management Concepts, Fed Pubs, WestLaw, Irwin, and NCMA may be helpful to have on hand in the PTAC library, if selected carefully to be appropriate for counseling clients.

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FAR Part 44 and relevant agency supplements

The client's contract document (each one will be different, so have the client provide the whole document)

Any of the client's policies and procedures relating to subcontract/purchasing management or administration.