

# SELLING COMMERCIAL SERVICES TO THE FEDERAL GOVERNMENT

Andrew Turnbull, Morrison & Foerster

Locke Bell, Morrison & Foerster

Karen Yankosky, Salesforce

December 10, 2019

# Agenda

---

Selling to the government

What is a “Commercial Item”

Regulatory requirements for commercial item contractors

Flow downs for commercial item subcontractors

How to avoid becoming subject to regulatory requirements

Best practices for mitigating risk as a commercial contractor

# The Government as a Customer

---

- The United States government is one of world's largest customers and has stable market
  - Procurement spending back on the rise:
    - FY 2016: ~\$475 billion
    - FY 2017: ~\$500 billion
    - FY 2018: ~\$550 billion
  - Commercial items make up a significant portion
    - In FY 2015, more than 25% obligated using commercial item procedures
      - **Does not** include subcontracts for commercial items.
- Transparency into funding and opportunities

# The Government as a Customer

---

- Federal funds come with strings.
  - Influence of public policy through power of the purse
  - Accountability to taxpayers
  - Federal contracts are highly regulated – contain a number of mandatory provisions that create compliance obligations.
    - Christian Doctrine: courts read in some clauses even if omitted.
- Government agencies also have restrictions on how they spend federal funds
  - Appropriations considerations, unauthorized commitments
  - Statutorily imposed competition requirements
- Sovereign immunity (and limited waivers thereof)
- The Contractor's failure to follow the rules can result in civil and criminal penalties, and potential termination from future contracts and funding opportunities.

# The Government as a Customer

---

- Generally must accept all contract terms as presented
  - Taking exception in a negotiated procurement can result in having proposal rejected as nonresponsive.
- Changes
  - As a general rule, USG can unilaterally modify contract terms (within scope).
    - Contractor may be entitled to an equitable adjustment.
- Authority to bind USG is limited to warranted contracting officers
  - Technical representatives and others with apparent authority cannot bind the government
  - Contractor performs at risk without written direction from contracting officer
- Limits on Confidentiality
  - Amount of contract is matter of public record
  - Freedom of Information Act means information disclosed to the Government could become accessible to the public
- Performance must continue while claims or disputes are pending

# Paths to Market

---

- Bid directly
  - Federal solicitations and RFPs posted on FedBizOpps.gov
- General Services Administration (“GSA”) Federal Supply Schedule (“FSS”) contracts
  - Specifically for commercial items
  - Direct orders vs. blanket purchase agreements (“BPAs”)
- Become a subcontractor or supplier to a prime contractor.
- Acquire a company with existing federal contracts
- Establish a subsidiary or business unit dedicated to Federal sales

**MORRISON**  
**FOERSTER**

# WHAT IS A COMMERCIAL ITEM?

# Commercial Item Contracting

---

- The Government has simplified policies and procedures for purchasing commercial items that more closely resemble those found in the commercial marketplace
  - Applies to commercial items/services as defined by Federal Acquisition Regulation (“FAR”) 2.101
- Contractors still required to comply with certain FAR clauses and reporting requirements, in particular those related to labor and employment
  - List of mandatory flowdowns in FAR; primes sometimes add others
- Unique considerations with use of commercial licenses
  - Government rules, including those related to choice of law and forum, indemnification, no apparent authority, still apply



# What is a Commercial Item?

---

“Commercial item” means --

(1) Any item, other than real property, that is **of a type** customarily **used by the general public** or by non-governmental entities for purposes other than governmental purposes, and--

- (i) **Has been sold**, leased, or licensed to the general public; or,
- (ii) **Has been offered for sale**, lease, or license to the general public;

(2) Any item that evolved from an item described in paragraph (1) of this definition through advances in technology or performance and that is not yet available in the commercial marketplace, but **will be available** in the commercial marketplace **in time to satisfy the delivery requirements** under a Government solicitation;

# Commercial Items

---

(3) Any item that would satisfy a criterion expressed in paragraphs (1) or (2) of this definition, but for --

(i) **Modifications of a type customarily available** in the commercial marketplace; or

(ii) **Minor modifications** of a type not customarily available in the commercial marketplace made to meet Federal Government requirements.

- Minor modifications means modifications that **do not significantly alter the nongovernmental function or essential physical characteristics** of an item or component, or change the purpose of a process.
- Factors to be considered in determining whether a modification is minor include the value and size of the modification and the comparative value and size of the final product. Dollar values and percentages may be used as guideposts, but are not conclusive evidence that a modification is minor;

# Commercial Items

---

(4) Any **combination** of items meeting the requirements of paragraphs (1), (2), (3), or (5) of this definition that are of a type customarily combined and sold in combination to the general public;

(5) **Installation services, maintenance services, repair services, training services, and other services** if--

- (i) Such services are procured for support of an item referred to in paragraph (1), (2), (3), or (4) of this definition, regardless of whether such services are provided by the same source or at the same time as the item; and
- (ii) The source of such services **provides similar services contemporaneously to the general public** under terms and conditions similar to those offered to the Federal Government;

# Commercial Items

---

(6) **Services of a type** offered and sold competitively in substantial quantities in the commercial marketplace based on **established catalog or market prices** for specific tasks performed or specific outcomes to be achieved and under standard commercial terms and conditions. For purposes of these services—

- (i) “Catalog price” means a price included in a catalog, price list, schedule, or other form that is regularly maintained by the manufacturer or vendor, is either published or otherwise available for inspection by customers, and states prices at which sales are currently, or were last, made to a significant number of buyers constituting the general public; and
- (ii) “Market prices” means current prices that are established in the course of ordinary trade between buyers and sellers free to bargain and that can be substantiated through competition or from sources independent of the offerors.

# Commercial Items

---

(7) Any item, combination of items, or service referred to in paragraphs (1) through (6) of this definition, notwithstanding the fact that the item, combination of items, or service is **transferred between or among separate divisions, subsidiaries, or affiliates of a contractor;**  
or

(8) A **nondevelopmental item**, if the procuring agency determines the item was **developed exclusively at private expense** and sold in substantial quantities, on a competitive basis, to **multiple State and local governments**.

# Commercial Off-The-Shelf Items

---

“Commercially available off-the-shelf (COTS) item--”

(1) Means any item or supply that is—

(i) A commercial item;

(ii) Sold in substantial quantities in the commercial marketplace; ***and***

(iii) Offered to the Government, under a contract or subcontract at any tier, without modification, in the same form in which it is sold in the commercial marketplace.

# Commercial Computer Software

---

- Civilian Agencies (FAR)
    - “Commercial computer software” means any computer software that is a commercial item.
    - Defines “computer software” as programs including instructions, rules, routines or statements, plus source code listings, algorithms, formulas, etc., but **not** including computer databases or computer software documentation (owners’ or user’s manuals, instructions, etc.).
  - Department of Defense (DFARS)
    - Definition of “computer software” excludes databases and computer software documentation like FAR definition; but software documentation is treated and marked like software. DFARS 252.227-7013(a)(3).
    - “Commercial computer software” means software developed or regularly used for nongovernmental purposes which—
      - 1) Has been sold, leased, or licensed to the public;
      - 2) Has been offered for sale, lease, or license to the public;
      - 3) Has not been offered, sold, leased, or licensed to the public but will be available for commercial sale, lease, or license in time to satisfy the delivery requirements of this contract; or
      - 4) Satisfies a criterion expressed in paragraph (a)(1)(i), (ii), or (iii) of this clause and would require only minor modification to meet the requirements of this contract.
- DFARS 252.227-7014(a)(1)

# Commercial Computer Software

---

- Commercial computer software “***shall*** be acquired under licenses customarily provided to the public to the extent such licenses
  1. Are consistent with **Federal law** and . . .
  2. . . . otherwise satisfy the **Government’s needs.**”

FAR 12.212(a); DFARS 227.7202-1(a) (substantively the same).

- **Civilian Agencies**: Look out for FAR 52.227-19, “Commercial Computer Software License,” which gives USG the same rights in commercial software as with noncommercial software provided with “Restricted Rights.”



**MORRISON**  
**FOERSTER**

**REGULATORY  
REQUIREMENTS FOR  
COMMERCIAL  
CONTRACTORS**

# What is the “FAR”?

---

- The Federal Acquisition Regulation, 48 CFR Parts 1-52
  - Parts 1-51 describe rules for all Executive Branch agencies to follow when procuring goods or services with appropriated funds.
  - Part 52 contains the clauses that are required to be placed in prime contracts to implement Parts 1-51.
    - Some of these clauses must be flowed down to subcontracts.
- Does not apply to Federal grants or cooperative agreements.
- Each agency can supplement the FAR, *e.g.*, Department of Defense FAR Supplement (“DFARS”), 48 CFR Parts 201-252

# Representations and Certifications

---

- All government contractors and grantees must register on the System for Award Management (SAM) ([www.sam.gov](http://www.sam.gov))
- Deal with size status, type of business, suspension/debarment, etc.
- Annual update requirement
- Accuracy is very important

# FAR 52.203-13, Code of Business Ethics and Conduct

---

- Company must have Code of Conduct and formal ethics awareness training
- Mandatory disclosure requirements for covered contracts and subcontracts
  - When a contractor has “credible evidence” of (a) significant contract overpayments, or (b) a violation of laws involving fraud, conflict of interest, bribery or gratuities; or civil FCA laws, the contractor must disclose the known overpayment or violation in writing
  - Failure to comply may result in suspension or debarment
- Improper business activities
- Bribery, Gratuities and Gifts
  - Contractor cannot offer, and USG employee cannot accept, anything of value in exchange for favorable treatment in connection with a contract
  - *De minimus* exceptions

# Acquisition-Related Requirements

---

- Covenant against contingent fees
- Conflicts of interest
- Procurement Integrity Act
- Hiring restrictions for certain former government officials
- Anti-Kickback Act
- Gifts/Gratuities and Lobbying restrictions
  
- ***Overarching Goal:*** Avoid even appearance of impropriety.

# Contingent fees

---

- Federal law allows the use of contingent fee arrangements only if the fee is paid to an employee as part of his/her regular compensation scheme or to a “bona fide agent.”
- In either case, the amount paid must be reasonable and consistent with industry standards.

# Conflicts of Interest

---

- Two types – personal and organizational
- **Personal** any situation that may make it difficult to perform your work objectively and effectively (e.g. outside employment or investments)
- **OCI** arise when a contractor has past, present, or planned interests that:
  - Directly or indirectly relate to work to be performed under a Government contract; and
    - May bias its judgment or otherwise diminish its ability to give impartial, technically sound assistance; OR
    - Gives (or creates the impression that) a contractor has an unfair competitive advantage

# OCI Types

---

- A company is presumed to have ***impaired objectivity*** if it is evaluating or recommending its own product or service.
- A ***biased ground rules*** OCI will result if a company participates in development of the statement of work or other contract requirements.
- An ***unequal access*** OCI is created if a company is given access to proprietary information of a third party or to non-public source selection related information.



# Procurement Integrity Act (“PIA”)

---

- Prohibits disclosing or obtaining certain sensitive information before award of a federal Government contract, including:
  - Bid or proposal information (information submitted by the competing bidders or offerors).
  - Source selection information (internal agency documents or information about the procurement process or decision).
- Restrictions on recruiting and employing current or former Government employees:
  - Bidders on Government contracts cannot discuss employment opportunities or offer post-government employment to federal agency officials involved in the contracting process.
  - Lifetime Bar – Agency officials may not communicate with agency on a particular matter in which he or she personally and substantially participated.
  - One-Year Bar – Agency officials involved in procurements worth over \$10 million cannot accept compensation from certain contractors for one year after the award decision.

# Kickbacks

---

- Federal law prohibits giving a **kickback** to a prime contractor or subcontractor for the purpose of improperly obtaining or rewarding **favorable treatment** in connection with a federal government prime contract or subcontract.
- “Favorable treatment” includes receiving a subcontract, receiving confidential information about a competitor’s bid, obtaining unwarranted waivers of deadlines, and obtaining acceptance of non-conforming goods.

# Government Policy on Gifts & Gratuities

---

- For Government officials and employees - the Government's Gift Policy is very strict!
- Contractors are prohibited by criminal statutes and regulations, with limited exceptions, from providing gifts or gratuities to Government employees.
- This prohibition encompasses many activities that are common in the commercial arena (*e.g.*, providing meals or entertainment to customers).
- Applies to all Government employees and their immediate family members.

# The Definition of Gifts

---

- What is a gift?
  - A “gift” includes “any gratuity, favor, discount, entertainment, hospitality, loan, forbearance, or other item having monetary value, as well as services such as training, transportation, lodging and meals, whether provided in-kind, by purchase of a ticket, payment in advance, or reimbursement after the expense has been incurred.”
- Examples of gifts include tickets to sporting events, covering the cost of a meal or a taxi ride, or co-signing a loan.

# Exceptions to the Gifts & Gratuities Policy

---

- Certain items are not considered to be “gifts” or are exceptions to the gift rules.
  - Modest items of food or refreshments (*e.g.*, soft drinks, coffee, cookies, etc.) not part of a meal.
  - Non-cash gifts of \$20 or less, not to exceed \$50 annually from any one person or the Company (*e.g.*, book, CD, golf balls, mouse pad, plaques).
  - Gifts based on a personal relationship (*e.g.*, to a relative).
- Because these rules are so strict, Company policy is that **NOTHING** of value should be given to a government customer without pre-approval.

# Bribery

---

- Criminal law and regulations prohibit bribery and illegal gratuities to government employees
- Federal regulations say government employees cannot accept gifts from contractors or other federal fund recipients Limited exceptions for items of modest value

## ***Definition of “Bribery”***

- Bribery is defined as directly or indirectly corruptly giving, offering or promising anything of value to any public official or person selected to be a public official with intent to influence any official act, or to influence a public official to commit fraud on the U.S., or to induce a public official to do or omit to do any act in violation of the person's lawful duty

# Socioeconomic Requirements

---

- Affirmative action laws
- Prevailing wage laws
- Prohibitions on human trafficking
- Drug-Free workplace
- E-Verify
- Domestic Preference and Supply Chain
- Ban on texting while driving

# Affirmative Action Laws

---

- OFCCP enforces three laws
  - Executive Order 11246
  - Section 503 of the Rehabilitation Act
  - The Vietnam Era Veterans Readjustment Assistance Act
- These laws generally require covered federal contractors and subcontractors to:
  - Not discriminate based on race, gender, sexual orientation, gender identity, national origin, religion, disability status, and veteran status
  - Create affirmative action programs for females, minorities, individuals with disabilities, and protected veterans
- OFCCP conducts random audits of contractors compliance with these laws, even without formal complaints
  - OFCCP findings of discrimination can result in significant monetary recovery of back pay and hiring quotas
  - Noncompliance can result in burdensome, ongoing reporting obligations to OFCCP or possible debarment actions



# Affirmative Action Laws (continued)

---

- Create AAPs annually for each U.S. establishment with 50+ employees
- Review hires, promotions, terminations, and compensation for systemic discrimination issues
- Ongoing outreach efforts to females, minorities, IWD, and veterans
- Evaluation and tracking of accommodation process for IWDs
- Job listing with state job banks
- Flowdowns and notices to subcontractors
- Notices to employees and applicants
- Annual VETS 4212 report
- Record retention

# Prevailing Wage Laws

---

- ***Service Contract Act*** – Service contractors must pay “service employees” no less than locally prevailing wage rates and fringe benefits (H&W, vacation, and holiday) required by applicable wage determinations or the rates in the predecessors CBA
- ***Davis Bacon Act*** - Contracts for construction, alteration, or repair of public works or public buildings must pay laborers and mechanics no less than locally prevailing wages and fringe benefits.
- ***Harsh penalties*** for noncompliance
  - Mandatory debarment for 3 years from all government contracts (SCA and non-SCA contracts) unless showing of “unusual circumstances”
  - Personal liability for corporate officials and others who control, supervise, or manage contract performance
  - Withhold or offset contract payments to recoup back pay and interest
  - Terminate contract and hold contractor liable for the government’s resulting costs

# Human Trafficking Regulations

---

- All federal contracts and subcontracts must have (FAR 52.222-50)
  - Policy prohibiting employees, agents, and subcontractors from engaging in human trafficking activities, including using forced labor, procuring commercial sex act, having misleading or fraudulent recruitment practice
  - Notify employees and subcontractors of that policy and consequences for not complying (e.g., termination of employment or subcontract)
  - Must report credible violations to CO and applicable agency IG
- Non-COTS contracts with an estimated value exceeding \$500K for supplies acquired abroad or performance of services outside the U.S. must have:
  - Written and posted compliance plan that meets certain minimum requirements
  - Certify annually to the government that:
    - Compliance plan implement; and
    - No violations found for contractor or its subs after reasonable due diligence

# Other Socioeconomic Policies

---

- Drug Free Workplace requirements
- E-Verify
  - Web-based program administered by U.S. Citizenship and Immigration Service (“USCIS”), part of Homeland Security
  - Compares employee information to central databases run by USCIS and the Social Security Administration to confirm employment eligibility
- Domestic Preference and Supply Chain
  - Trade Agreements Act
  - Buy American Act
  - Reporting counterfeit parts
- Ban on texting while driving
  - Executive Order requires contractors to have anti-texting while driving policy for workers on contracts

# Enforcement Matters

---

- False Claims Act
  - Criminal False Claims Act punishes intentional fraud
  - Civil False Claims imposes liability on any contractor that “knowingly” submits a false claim for payment to the federal government
  - Whistleblower provision
  - Treble damages plus penalties
- False Statements
- Export Controls (ITAR/EAR)
- Foreign Corrupt Practices Act
- Suspension & Debarment
  - Temporary or more permanent (up to three years) ban on receiving new government contracts or extensions of existing contracts
- Adverse Past Performance Ratings
- Government claim under the Contract Disputes Act

**MORRISON**  
**FOERSTER**

**APPLICATION OF  
REGULATORY  
REQUIREMENTS TO  
COMMERCIAL  
CONTRACTORS**

# Methods for Becoming Covered

---

Direct business with a governmental entity

Doing business with a company whose products and services are sold to the federal government

Close corporate relationship with company that does business with the federal government

# Direct Contract

---

## Are you doing business with the federal government?

- **An agreement** (includes GSA Schedules, bills of lading, IDIQs)
- **With a federal entity**
  - Executive agencies (e.g., DoD, Treasury, DHS, VA, etc.)
  - Federal entities regardless of whether appropriated or non-appropriate funds (e.g., AFES)
- **For purchase, sale, or use of goods or services**
  - Not grants or loans
  - Includes contractor purchasing items from the government (e.g., lease of federal land)

## Does your contract meet the dollar thresholds for coverage?

- 10K for EO 11246
- 15K for Section 503
- 150K for VEVRAA

## Any exemptions apply?

- Certain religious organizations or work on or near Indian reservations
- TRICARE



# Who is a Subcontractor?

---

- “Subcontractor” means:
  - ***Any*** supplier, distributor, vendor, or firm. . .
  - . . . that furnishes **supplies or services**
  - . . . **to or for** a **prime contractor** or another **subcontractor**.

FAR 44.101.

- **Keep in mind:**
  - No privity of contact between a subcontractor and the government,
  - ***Responsibility falls to the prime*** and will only flow down from there if adequately covered in subcontract.
  - **Christian Doctrine** – mandatory federal procurement clauses are incorporated as a matter of law into federal contracts

# Is it a Subcontract? (cont'd)

---

- OFCCP has stated that subcontracts include:
  - **Any agreement or arrangement . . .**
  - . . . between a contractor and **any person** [excluding employee agreements]:
    - (1) For the purchase, sale or use of personal property or nonpersonal services which, **in whole or in part**, is **necessary** to the performance of any **one or more** contracts; **or**
    - (2) Under which **any portion of the contractor's obligation** under any one or more contracts is performed, undertaken or assumed.

41 C.F.R. § 60-1.3.

# Subcontractor Is Broadly Interpreted

---

## *Scenario*

- Power company had a GSA contract to supply power to federal facilities
- Railroad transported coal from coal mines to only one of the power company's facilities
- Government used about 0.4% of electricity generated by that facility
- OFCCP claimed railroad was a covered subcontractor

## *Was It a Covered Subcontract?*

- Services were not necessary because plant produced electricity without interruption even when railroad transported no coal
- No way to show that coal transported by railroad was used to produce electricity that went to the government
- Facility only supplied .04% of the power to the government

## *ALJ Said Covered Subcontract*

- Railroad performed the “type of service” that was necessary to performance of power company's contract to supply electricity to government
- Although the coal the railroad hauled was comingled with other coal, at least a portion of it was used to perform the federal contract of providing electricity to the gov.
- Made no difference whether power supplied by plant was small or insignificant

## *OFCCP v. Monongahela Railroad Company*

# Practical Examples (continued)

---

- **Question:** I have a private cloud-to-cloud agreement to exchange data with another commercial enterprise. The associated costs will be allocated to various government contracts. Am I a covered subcontractor?
- Answer: **Yes.**
  - It is a “contract” entered into by a “supplier distributor, vendor, or firm” to “furnish supplies or services to or for a prime contractor or another subcontractor”
- **Question:** I sell a commercially available off-the-shelf software to a company that has contracts with the federal government. Am I a covered subcontractor?
- Answer: **Possibly**
  - Yes, if the performance of a government contract requires your software, even if that software will be used for other non-government contracts
  - No, if the software is for general commercial use, and simply happens to also benefit government work (e.g., back office accounting software)

# Rules of Thumb

---

- Are any products or services provided included within the scope of work for the prime contract (or higher tier subcontract)?
  - Then it **is** a subcontract.
- Are the products or services necessary for performance of any prime contracts (or higher tier subcontracts)?
  - Then it **is** a subcontract.
- Are the products or services merely ancillary to work on a prime contract (or higher tier subcontract)?
  - Then it **is not** a subcontract.
  - *E.g.*, staffing agency providing back office administrative support workers; software to improve generally applicable processes.

# Single Entity Analysis

---

- Even if no government business, can be covered if a “single entity” with a related business (e.g., parent, subsidiary, affiliate, JV)
- Focus on interrelatedness with federal contractor
- Test primarily considers:
  - Common ownership
  - Common officers and directions
  - Day-to-day control through policies and management
  - Common or centralized personnel policies
  - Operations are dependent on each other
- Control of personnel functions most important for OFCCP (although not dispositive)

# Single Entity Example

---

## Scenario

- Manheim Inc., wholesaler of automotive remarketing, owned MAGS
- MAGS was federal contractor, but only had 8 employees
- Manheim had 23K employees but no federal contracts

## ALJ Held Manheim and MAGS Were Single Entity

- Had common ownership – Manheim owned MAGS
- Had common directors and officers – 1/3 of MAGS directors were directors of Manheim and majority of MAGS officers were Manheim officers
- Exercised de facto control – Manheim approved all MAGS budgets, invoices, and processing contract payouts
- Unity of personnel policies – Shared HR department and Manheim did MAGS EEO-1 reports
- MAGS was dependent on Manheim – Manheim stripped MAGS of its contracts and awarded them to a different entity

# Practical Ways to Avoid Single Entity

---

## Have separate HR functions and policies

- Do not make employment decisions or share HR managers between entities
- Have separate handbooks, even if policies are virtually identical
- Use separate payroll and bank accounts
- File separate EEO-1 reports

## Maintain separate corporate formalities

- Avoid overlapping directors or officers
- Allow federal contractor ability to exercise discretion on day-to-day operations, particularly on HR items
  - Can retain broad control of corporate direction
- Charge other company for sharing items
- Limit movement of employees between entities
- Avoiding holding companies out as the same entity (e.g., same letterhead, website, etc.)



**MORRISON**  
**FOERSTER**

# COMMERCIAL ITEM SUBCONTRACT FLOWDOWNS

# Flowdowns: Basic Rules

---

- Federal statutes, Executive Orders, and the FAR (and, where applicable, other agency supplemental regulations) require inclusion of certain clauses and obligations in all government subcontracts.
- Where the subcontract is for a commercial item or commercial service, the list of mandatory flowdowns is more limited.
- It is not possible to put together a comprehensive list of all potential flowdowns because the prime contract terms may dictate additional clauses.
- Thus, a review of each prime contract (or higher tier subcontract) is necessary.

# Noncommercial Subcontracts

---

- Each clause in a prime contract must be examined.
- Numerous FAR (and FAR supplement) clauses must be flowed down, but the requirement may be conditioned.
- For example:
  - FAR 52.203-6 – Restrictions on Subcontractor Sales to the Government:
    - (c) The Contractor agrees to incorporate the substance of this clause, including this paragraph (c), in all subcontracts under this contract which exceed the simplified acquisition threshold.
  - FAR 52.203-13 – Contractor Code of Business Ethics and Conduct:
    - (d)(1) The Contractor shall include the substance of this clause, including this paragraph (d), in subcontracts that have a value in excess of \$5.5 million and a performance period of more than 120 days.
  - FAR 52.204-21 – Basic Safeguarding of Covered Contractor Information Systems:
    - (c) The Contractor shall include the substance of this clause, including this paragraph (c), in subcontracts under this contract in which the subcontractor may have Federal contract information residing in or transiting through its information system.

# Commercial Item Subcontracts

---

- The FAR provides a convenient list of clauses that must be flowed down to commercial item subcontracts.
  - **But**, the DFARS and other agency supplements do not, so you must still examine those clauses.
- The list varies for commercial and noncommercial prime contracts.
  - Commercial item prime contracts: *see* **FAR 52.212-5(e)**.
  - Noncommercial prime contracts: *see* **FAR 52.244-6**.
  - The lists are mostly the same, but there are some differences.
- Neither list is truly definitive:
  - FAR 52.212-5(e)(2): “While not required, the Contractor may include in its subcontracts for commercial items a **minimal number** of additional clauses necessary to satisfy its contractual obligations.”
  - FAR 52.244-6(c)(2): “While not required, the Contractor may flow down to subcontracts for commercial items a **minimal number** of additional clauses necessary to satisfy its contractual obligations.”

# Commercial Subcontracts under Noncommercial Prime Contracts

---

(1) The Contractor shall insert the following clauses in subcontracts for commercial items:

(i) **52.203-13, Contractor Code of Business Ethics and Conduct (Oct 2015)** (41 U.S.C. 3509), if the subcontract exceeds \$5.5 million and has a performance period of more than 120 days. In altering this clause to identify the appropriate parties, all disclosures of violation of the civil False Claims Act or of Federal criminal law shall be directed to the agency Office of the Inspector General, with a copy to the Contracting Officer.

(ii) **52.203-15, Whistleblower Protections Under the American Recovery and Reinvestment Act of 2009 (Jun 2010)** (Section 1553 of Pub. L. 111-5), if the subcontract is funded under the Recovery Act.

(iii) **52.203-19, Prohibition on Requiring Certain Internal Confidentiality Agreements or Statements (Jan 2017).**

# Commercial Subcontracts under Noncommercial Prime Contracts

---

(iv) **52.204-21, Basic Safeguarding of Covered Contractor Information Systems (JUN 2016)** other than subcontracts for commercially available off-the-shelf items, if flow down is required in accordance with paragraph (c ) of FAR clause 52.204-21.

(v) **52.204-23, Prohibition on Contracting for Hardware, Software, and Services Developed or Provided by Kaspersky Lab and Other Covered Entities (JUL 2018)** (Section 1634 of Pub. L. 115-91).

(vi) **52.219-8, Utilization of Small Business Concerns (Oct 2018)** (15 U.S.C. 637(d)(2) and (3)), if the subcontract offers further subcontracting opportunities. If the subcontract (except subcontracts to small business concerns) exceeds \$700,000 (\$1.5 million for construction of any public facility), the subcontractor must include 52.219-8 in lower tier subcontracts that offer subcontracting opportunities.

# Commercial Subcontracts under Noncommercial Prime Contracts

---

- (vii) **52.222-21, Prohibition of Segregated Facilities (Apr 2015).**
- (viii) **52.222-26, Equal Opportunity (Sep 2016)** (E.O. 11246).
- (ix) **52.222-35, Equal Opportunity for Veterans (Oct 2015)** (38 U.S.C. 4212(a));
- (x) **52.222-36, Equal Opportunity for Workers with Disabilities (Jul 2014)** (29 U.S.C. 793).
- (xi) **52.222-37, Employments Reports on Veterans (Feb 2016)** (38 U.S.C. 4212).
- (xii) **52.222-40, Notification of Employee Rights Under the National Labor Relations Act (Dec 2010)** (E.O. 13496), if flow down is required in accordance with paragraph (f) of FAR clause 52.222-40.

# Commercial Subcontracts under Noncommercial Prime Contracts

---

(xiii) (A) **52.222-50, Combating Trafficking in Persons (Jan 2019)** (22 U.S.C. chapter 78 and E.O. 13627).

(B) **Alternate I (Mar 2015)** of 52.222-50 (22 U.S.C. chapter 78 and E.O. 13627).

(xiv) **52.222-55, Minimum Wages under Executive Order 13658 (Dec 2015)**, if flowdown is required in accordance with paragraph (k) of FAR clause 52.222-55.

(xv) **52.222-62, Paid Sick Leave Under Executive Order 13706 (JAN 2017)** (E.O. 13706), if flow down is required in accordance with paragraph (m) of FAR clause 52.222-62.

(xvi)(A) **52.224-3, Privacy Training (JAN 2017)** (5 U.S.C. 552a) if flow down is required in accordance with 52.224-3(f).

•(B) **Alternate I (JAN 2017)** of 52.224-3, if flow down is required in accordance with 52.224-3(f) and the agency specifies that only its agency-provided training is acceptable.



# Commercial Subcontracts under Noncommercial Prime Contracts

---

(xvii) **52.225-26, Contractors Performing Private Security Functions Outside the United States (Oct 2016)** (Section 862, as amended, of the National Defense Authorization Act for Fiscal Year 2008; 10 U.S.C. 2302 Note).

(xviii) **52.232-40, Providing Accelerated Payments to Small Business Subcontractors (Dec 2013)**, if flow down is required in accordance with paragraph (c) of FAR clause 52.232-40.

(xix) **52.247-64, Preference for Privately Owned U.S.-Flag Commercial Vessels (Feb 2006)** (46 U.S.C. App. 1241 and 10 U.S.C. 2631), if flow down is required in accordance with paragraph (d) of FAR clause 52.247-64.

•Also must include **FAR 52.244-6, Subcontracts for Commercial Items (Jan 2019)**

# Commercial Subcontracts under Commercial Prime Contracts

---

(e)(1) Notwithstanding the requirements of the clauses in paragraphs (a), (b), (c) and (d) of this clause, the Contractor is not required to flow down any FAR clause, other than those in this paragraph (e)(1) in a subcontract for commercial items. Unless otherwise indicated below, the extent of the flow down shall be as required by the clause—

(i) **52.203-13, Contractor Code of Business Ethics and Conduct (Jan 2019)** (41 U.S.C. 3509).

(ii) **52.203-19, Prohibition on Requiring Certain Internal Confidentiality Agreements or Statements (Jan 2017)** (section 743 of Division E, Title VII, of the Consolidated and Further Continuing Appropriations Act, 2015 (Pub. L. 113-235) and its successor provisions in subsequent appropriations acts (and as extended in continuing resolutions)).

(iii) **52.204-23, Prohibition on Contracting for Hardware, Software, and Services Developed or Provided by Kaspersky Lab and Other Covered Entities (Jul 2018)** (Section 1634 of Pub. L. 115-91).

# Commercial Subcontracts under Commercial Prime Contracts

---

- (iv) **52.219-8, Utilization of Small Business Concerns (Oct 2018)** (15 U.S.C. 637(d)(2) and (3)), in all subcontracts that offer further subcontracting opportunities. If the subcontract (except subcontracts to small business concerns) exceeds \$700,000 (\$1.5 million for construction of any public facility), the subcontractor must include 52.219-8 in lower tier subcontracts that offer subcontracting opportunities.
- (v) **52.222-17, Nondisplacement of Qualified Workers (May 2014)** (E.O. 13495). Flow down required in accordance with paragraph (1) of FAR clause 52.222-17.
- (vi) **52.222-21, Prohibition of Segregated Facilities (Apr 2015)**.
- (vii) **52.222-26, Equal Opportunity (Sep 2016)** (E.O. 11246).
- (viii) **52.222-35, Equal Opportunity for Veterans (Oct 2019)** (38 U.S.C. 4212).
- (ix) **52.222-36, Equal Opportunity for Workers with Disabilities (Jul 2014)** (29 U.S.C. 793).

# Commercial Subcontracts under Commercial Prime Contracts

---

- (x) **52.222-37, Employment Reports on Veterans (Feb 2016)** (38 U.S.C. 4212).
- (xi) **52.222-40, Notification of Employee Rights Under the National Labor Relations Act (Dec 2010)** (E.O. 13496). Flow down required in accordance with paragraph (f) of FAR clause 52.222-40.
- (xii) **52.222-41, Service Contract Labor Standards (Aug 2018)**, (41 U.S.C. chapter 67).
- (xiii) (A) **52.222-50, Combating Trafficking in Persons (Jan 2019)** (22 U.S.C. chapter 78 and E.O. 13627).  
  
(B) **Alternate I (Mar 2015)** of 52.222-50 (22 U.S.C. chapter 78 E.O. 13627).
- (xiv) **52.222-51, Exemption from Application of the Service Contract Labor Standards to Contracts for Maintenance, Calibration, or Repair of Certain Equipment--Requirements (May 2014)** (41 U.S.C. chapter 67.)

# Commercial Subcontracts under Commercial Prime Contracts

---

(xv) **52.222-53, Exemption from Application of the Service Contract Labor Standards to Contracts for Certain Services--Requirements (May 2014)** (41 U.S.C. chapter 67)

(xvi) **52.222-54, Employment Eligibility Verification (Oct 2015)** (E. O. 12989).

(xvii) **52.222-55, Minimum Wages Under Executive Order 13658 (Dec 2015).**

(xviii) **52.222-62, Paid sick Leave Under Executive Order 13706 (JAN 2017)** (E.O. 13706).

(xix) (A) **52.224-3, Privacy Training (Jan 2017)** (5 U.S.C. 552a).

(B) **Alternate I (Jan 2017)** of 52.224-3.

# Commercial Subcontracts under Commercial Prime Contracts

---

(xx) **52.225-26, Contractors Performing Private Security Functions Outside the United States (Oct 2016)** (Section 862, as amended, of the National Defense Authorization Act for Fiscal Year 2008; 10 U.S.C. 2302 Note).

(xxi) **52.226-6, Promoting Excess Food Donation to Nonprofit Organizations. (May 2014)** (42 U.S.C. 1792). Flow down required in accordance with paragraph (e) of FAR clause 52.226-6.

(xxii) **52.247-64, Preference for Privately-Owned U.S. Flag Commercial Vessels (Feb 2006)** (46 U.S.C. Appx 1241(b) and 10 U.S.C. 2631). Flow down required in accordance with paragraph (d) of FAR clause 52.247-64.

- **No** requirement to include FAR 52.212-5(e).

- Slight variation in FAR 52.212-5, Alternate II for contracts using funds under the American Recovery and Reinvestment Act of 2009.

# Why We Care About Flowdowns

---

1. We can be in default of our contract if a flowdown is expressly required.
2. We make promises about what types of items will be purchase and what employees will be paid - and we are accountable.
3. If a subcontractor violates a regulation, the Government will look to us for payment.
4. The Government may review our purchasing system for consistency and reliability.

**MORRISON**  
**FOERSTER**

# PRACTICAL CONSIDERATIONS



# Mitigating Risk

---

- Survey the market for potential opportunities
- Know where regulatory requirements might attach (FAR/DFARS clauses, flowdowns, OFCCP requirements)
- Consider creating a firewalled entity for the government business
  - May limit many compliance requirements to Federal-dedicated entity; others require company-wide diligence
- Work closely with business development and program teams to understand work to be performed, project-specific requirements, and identify potential compliance concerns.

# Negotiating Subcontracts

---

- A subcontractor should want the prime contractor to successfully perform the prime contract.
  - The prime contractor should receive the rights and assurances it needs to perform its prime contract and systems integration responsibilities
  - **But** a prime contractor may not:
    - Flow down more clauses to commercial item subcontractors than necessary. See FAR 52.212-5(e)(2), 52.244-6(c)(2).
    - Use subcontract award as leverage for obtaining rights in subcontractor's intellectual property. See FAR 52.227-11(k)(3) (patents), DFARS 252.227-7013(k)(4), 252.227-7014(k)(2).
- Know what is **mandatory by law** and what special requirements RFP/prime contract contains, if any.
- Push back on unacceptable terms that are not mandatory

**MORRISON**  

---

**FOERSTER**

\*Disclaimer: The information provided in this presentation does not, and is not intended to, constitute legal advice.