LEGAL ADVISOR

A PilieroMazza Update for Federal Contractors and Commercial Businesses

It's Time to Tell Your Subcontract to Say "Aaah": Before You Ink That Upcoming Subcontract, You Would Be Wise to Undergo a Check-up

By Paul Mengel

Most of us undergo annual physicals, periodically tune up our vehicles, and perform routine maintenance on items in our personal lives. In a similar vein, as the busy subcontracting season approaches, to help preserve the figurative health of your business as a prudent prime or subcontractor, you would be well-advised to perform a "checkup" on documents upon which you rely, in particular, your "form" subcontract. While it is impossible to draft a document that will completely insulate your company from disputes, you should consider a thorough review of your subcontracts in order to help minimize the risk, and the attendant expense, of resolving a potential dispute through costly litigation.

1 Avoid the use of "Subcontracts R Us."

You might be surprised by the number of matters in which we have been engaged wherein the client has provided a copy of the subject subcontract, which it had downloaded from the internet and executed largely unchanged, aside from plugging in names, dates, and subject matter. In many such cases, the client's penny-wise, but pound-foolish, failure to tailor the document to the needs of, and to the advantage, of the company comes back to haunt it in the form of an adverse outcome in the dispute.

2 Review your dispute resolution provision.

Oftentimes subcontracts contain a rote dispute resolution statement, which may be as simple as: "All claims and disputes arising under or relating to this Agreement are to be settled by binding arbitration in the State of __." While each party may be equally ill-served by this language, your subcontract should work to your advantage wherever possible. So consider: does it provide for litigation of disputes in a forum friendly to one party, in terms of venue? Does it contain a waiver of jury trial, which can add significantly to the expense of litigation? If litigation is the chosen dispute resolution mechanism, is there a "loser pays" clause as to legal fees? Has the availability of equitable/injunctive relief been addressed? If arbitration is chosen, are specifics provided as to the conduct of the arbitration, e.g., the number of arbitrators and scope of discovery, or does it defer to the rules of an arbitration provider, such as the AAA? And has the company been advised as to the relative advantages and disadvantages of arbitration vs. litigation? The foregoing is merely representative of the considerations that go into the drafting of the critical dispute resolution provision, each of which can have a substantial impact on the relative rights of the parties and the cost of resolving the issue.

3 Ensure that the subcontract indemnification provision provides sufficient protections.

Your subcontract should contain a comprehensive indemnification provision that sufficiently indemnifies the company from claims, both direct and third-party, arising from the acts and omissions of your counterpart.

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The covered claims should include, at a minimum, those arising from: negligence (simple and gross); fraud; bad faith conduct; breaches of the reps and warranties in the subcontract; violations of the law and/or relevant FAR clauses and submission of false claims; infringement of intellectual property rights; injury, death, or property loss; and claims made by the other's employees. Anything less could needlessly expose your company to risks that should be borne by the other.

4 Check for robust confidential information protection.

Your company's confidential information ("CI") must be guarded zealously, and the subcontract provisions related to CI are vital to protecting these critical assets. Subcontract language must, at a minimum: classify CI with clarity; provide detailed direction as to its dissemination, including identifying to whom it may be revealed; clearly state the scope and duration of the restrictions; provide for the return/destruction of the CI upon concluding the relationship; and provide strict and legally enforceable penalties for its unauthorized use.

5 Confirm clarity with regard to termination.

Litigation often arises as to whether termination of a subcontract was proper under the circumstances. Your termination provision should state with specificity the events resulting in termination, including default, acts of which must be clearly defined. The effect of termination for convenience by the government should be addressed, if appropriate. And there should be no doubt as to the parties' relative rights and obligations upon termination.

Every provision of your subcontract is important, and you should approach your review of the document as if there is no such thing as "boilerplate." While clearly some provisions are more critical than others, each is there for a reason, and each has the potential to affect in some manner the likelihood, length, cost, and/or outcome of disputes. While the foregoing five suggested areas of scrutiny are representative of the subject matter of much of the subcontract litigation we encounter, as you conduct your periodic review and tailor your subcontract to the best interests of your company, do not leave any provision behind, as that may be the one that tips the scale in favor of your adversary in a dispute.

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