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Contractual Flow-Down Clauses: Deterrence to Non-Traditional Defense Contractors from Doing Business with DoD

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- For a sampling of DoD major defense acquisition programs (MDAPs): Are there instances of clear misapplication of Federal Acquisition Regulation (FAR) and Defense FAR Supplement (DFARS) flow-down clauses from prime contractors to their 1st tier subcontractors?
- Have FAR/DFARS flow-down clauses had any effect on DoD MDAPs in terms of access to advanced research and technology capabilities available in the private sector?

Congressional perceptions

- Belief that increase in FAR/DFARS in past decade has fueled flow-down of clauses to subcontractors
 - Belief that many are of dubious value
- Primes are flowing down the “kitchen sink” of FAR/DFARS clauses to subcontractors
 - “clear mis-application”
- FAR/DFARS flow-downs are a deterrence to firms doing business with DoD
 - DoD losing access to advanced technologies and capabilities due to red tape

What is a FAR/DFARS flow-down clause?

- No direct contractual relationship between US Government (USG) and subcontractor (no privity of contract)
- But, USG exercises control via contractual clauses with Prime
- “Boilerplate” clauses that seek to control on a diverse array of matters

Types of flow-down clauses

- Mandatory per USG
- Customary (recommended/optional)
 - Usually depends upon contract/facts
 - Prime “terms & conditions” (T&Cs)
 - Primes flow-down to legally protect the firm

- Sample of 5 diverse MDAPs (missile, ship, etc.)
 - DoD to Prime MDAP contracts and Prime to 1st tier subcontracts
 - Scored flow-down clauses as Mandatory or Customary [Optional] per categorization established by Richard Ginman (ret ADM)
 - Analysis of scored clauses: Clear misapplications
 - Not administrative or extraneous
- Interviews concerning flow-down clauses and DoD access to advanced research and technology capabilities in the private sectors
 - Industry
 - Government
 - Academic

Results: FAR Flow-down Clauses

	MDAP 1	MDAP 2	MDAP 3	MDAP 4	MDAP 5
Quantity of Clauses in Subcontract vs. Prime Contract	97 (79%)	110 (151%)	81 (58%)	78 (103%)	83 (84%)
FAR to Prime	123	73	140	76	99
FAR Clauses in DoD-Prime flowed-down to Subcontractor	70	43	51	39	80
Additional FAR clauses from Prime Terms & Conditions to Subcontractor	27	67	30	39	3

Prime Clauses to Subcontractor

	MDAP 1	MDAP 2	MDAP 3	MDAP 4	MDAP 5
Total	70	43	51	39	80
Mandatory	42 (60%)	25 (58%)	30 (59%)	25 (64%)	33 (41%)
Customary	22 (31%)	16 (37%)	13 (25%)	11 (28%)	30 (38%)
Neither Mandatory nor Customary	6 (9%)	2 (5%)	7 (14%)	3 (8%)	17 (21%)
Solicitation Provisions	0	0	1 (2%)	0	0
Misapplications*	4 (6%)	0	1 (2%)	0	0

*They appear to be administrative errors or contract drafting oversight, not necessarily clear misapplications.

Prime T&Cs to Subcontractor

	MDAP 1	MDAP 2	MDAP 3	MDAP 4	MDAP 5
Total	27	67	30	39	3
Mandatory	17 (63%)	22 (33%)	17 (57%)	26 (67%)	0 (0%)
Customary	4 (15%)	30 (45%)	10 (33%)	7 (18%)	3 (100%)
Neither Mandatory nor Customary	1 (4%)	9 (13%)	1 (3%)	3 (8%)	0
Solicitation Provisions	5 (19%)	6 (9%)	2 (7%)	3 (8%)	0
Misapplications*	5 (19%)	6 (9%)	2 (7%)	3 (8%)	0

*It appears to be administrative error or contract drafting oversight not necessarily a clear misapplication.

Observed same pattern of flow-down of Prime clauses and Prime T&Cs with DFARS clauses

- Literature review supplemented by input from USG, Industry, and Academia
- Insights
 - DoD is no longer the dominant or driving force in many technologies
 - Commercial markets more lucrative; thus, regulatory burden of FAR/DFARS demotes DoD in customer preference (other factors equal)
 - Presently – work-arounds utilized if an issue arises with access
 - Defense Innovation Unit Experimental (DIUx) is paving the way for a more dynamic approach (e.g., Other Transaction Authorities)
- Potential for future negatives – but nothing yet substantiated

Flow-down clauses by DoD or Primes to MDAP 1st tier subcontractors

- Key findings:
 - No widespread practice of burdensome flow-down misapplication
 - Primary driver of flow-down clauses appears to be ever-expanding size of FAR/DFARS along with prime contractor rote standardization and defensive risk management
 - FAR/DFARS clauses protect government, but can burden primes and subs
- Recommendations:
 - Cull FAR/DFARS of regulations that do not directly affect the quality and performance of the acquired product in order to reduce the volume of regulations and flow-downs
 - Quantify costs to assist in reduction of FAR/DFARS clauses
 - Restrict new regulations to those that can accelerate weapons development and production and achieve cost efficiencies

DoD access to advanced research and technologies

- Key findings:
 - Commercial firms have strategically chosen not to pursue DoD business
 - DoD is no longer the dominant or driving force in some important technologies
 - FAR/DFARS regulations are a barrier to doing business with DoD
- Recommendations:
 - Conduct primary research on non-participating firms that possess technologies of interest to DoD to understand incentives/disincentives, and propose legal and regulatory changes that may encourage participation
 - Learn from DIUx experiences – including statutory and regulatory changes to incorporate insights.