January 12, 2006

VIA ELECTRONIC MAIL AND FAX SIMILE

National Reconnaissance Office
Office of Contracts
14675 Lee Road
Chantilly, VA 20151-1715

Attn: Lieutenant Colonel Michael M. Hale (Michael.hale@nro.mil)

Re: NRO Acquisition Manual Clause 52.244-002 (Draft) Subcontract Reporting, Monitoring, and Consent

Dear Lieutenant Colonel Hale:

On behalf of the Section of Public Contract Law of the American Bar Association ("the Section"), I am submitting comments on the above-referenced matter. The Section consists of attorneys and associated professionals in private practice, industry, and Government service. The Section’s governing Council and substantive committees have members representing these three segments to ensure that all points of view are considered. 1 By presenting their consensus view, the Section seeks to improve the process of public contracting for needed supplies, services and public works.

The Section is authorized to submit comments on acquisition regulations under special authority granted by the ABA’s Board of Governors. The views expressed herein have not been approved by the House of Delegates or the Board of

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1 The Honorable Mary Ellen Coster Williams, a Council Member of the Public Contract Law Section, did not participate in the Section’s consideration of these comments, and she abstained from voting to approve and send this letter.

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Governors of the American Bar Association and, therefore, should not be construed as representing the policy of the American Bar Association.²

Recently, several companies received the Subcontract Reporting, Monitoring, and Consent clause proposed by the National Reconnaissance Office ("NRO"), and the communication included a request by the NRO for review and comments or recommendations. This NRO clause would create a new contract deliverable in order to collect and provide subcontractor information. In this clause, a subcontractor is defined as any supplier, distributor, vendor, or firm that furnishes supplies or services to or for a prime contractor or to another subcontractor regardless of the dollar value of the prime or subcontract. Efforts performed outside of the main contractor location, division, or facility awarded the contract, also known as interorganizational transfers or IOTs, are considered subcontracts for the purpose of this clause. In addition to creating a new quarterly reporting requirement, there is a comprehensive monitoring aspect to this new requirement, and the NRO is to take an active role in monitoring subcontractor source selection and performance. The following discussion provides the Section’s comments on this proposed clause.

1. Subcontracting is an important part of the acquisition process, and is addressed in the FAR. The NRO’s proposed clause goes beyond the FAR.

As noted in the NRO’s explanation provided with the proposed clause, agencies need information on the subcontracting activities of contractors. That is the reason for Federal Acquisition Regulation (FAR) coverage of this topic, such as FAR Part 42 and Part 44.

Contract administration is addressed in Part 42. FAR 42.202(e)(2) notes that:

The prime contractor is responsible for managing its subcontracts. The CAO’s [contract administration office’s] review of subcontracts is normally limited to evaluating the prime contractor’s management of subcontracts (see Part 44). Therefore, supporting contract administration shall not be used for subcontracts unless —

² This letter is available in pdf format at http://www.abanet.org/contract/Federal/regscomm/home.html under the topic “Subcontracting and Teaming.”
(i) The Government would otherwise incur undue cost;

(ii) Successful completion of the prime contract is threatened; or

(iii) It is authorized under paragraph (f) of this section [which addresses special surveillance for major system acquisitions] or elsewhere in this regulation.

The NRO in its proposed clause intends to go far beyond the evaluation of prime contractors’ management of subcontracts. The monitoring aspects in the proposed clause are not found in the FAR, and are not used by any other agency. Also, FAR 43.302(a)(51) lists as a contract administration function normally delegated by a contracting officer to a CAO the ability to “[r]eview, approve or disapprove, and maintain surveillance of the contractor’s purchasing system (see Part 44).” The NRO, in contrast, is interested in access to specific meetings and sessions between the prime contractor and potential or actual subcontractors.

For the most part, agency involvement in the subcontracting process has traditionally been focused on the adequacy of the prime contractor’s system for selecting and administering its subcontracts, including IOTs. For subcontracts that warrant special attention and are specifically identified by the contracting officer in the subcontracts clause of the contract, the agency can mandate that consent be obtained to subcontract. FAR Part 44, “Subcontracting Policies and Procedures,” prescribes the policies and procedures for consent to subcontracts, and for the review, evaluation, and approval of contractor purchasing systems. The objective of such a review “is to evaluate the efficiency and effectiveness with which the contractor spends Government funds and complies with Government policies when subcontracting.” FAR 44.301. The proposed NRO clause adds to the existing regulatory process in several ways.

2. The quarterly reporting requirement in the NRO proposed clause goes beyond existing FAR requirements, which are the basis of contractors’ purchasing systems, internal procedures, and existing data collection and reporting mechanisms. The effort and cost associated with new requirements, including data collection and report preparation, should be considered.

The proposed clause seeks at a minimum thirteen types of data. The collection of these data is apparently intended to assist the agency in accounting for the subcontractors supporting its prime contractors, and the agency commentary with the proposed clause states that this requirement is being driven by security and
counter-intelligence concerns, recurring Congressional requests for information, and the need to track subcontractor progress. As noted by the agency, however, there is no standard industry approach for the collection and recording of subcontractor data. As a result, NRO contractors will be developing a new report, which will be a contract deliverable on NRO contracts but not on other agency contracts. The effort and cost associated with this effort should be considered in light of the probable minimal benefit to the NRO, the cost of implementation, and the potential for interference in contract performance discussed below.

This proposed clause would require establishment of a unique recording system for the NRO not otherwise required by the FAR or other agencies. Because other agencies are not seeking the same information, the cost will be associated with a requirement of one agency, and will be borne by that agency’s contracts, either as direct charges to each contract or by way of the development and Defense Contract Audit Agency approval of an NRO-unique special indirect cost pool.

This new record collection activity, however, cannot be imposed without the prior approval of the Office of Management and Budget. Under 44 USC § 3501 et seq, OMB must approve record collection activities unless the record keeping requirement could be deemed usual and what a contactor would maintain in the normal course of business. That exception, however, is inapplicable here as it is inconsistent with the commentary provided by the agency with this proposed clause. The commentary indicates that not all this information is collected by contractors.

In addition, the Federal Government is adopting the Electronic Subcontract Reporting System (also known as “E-SRS”) to consistently, uniformly and electronically capture subcontractor data across agencies. There is a possibility that there will be a conflict between the E-SRS, once fully implemented, and this NRO reporting requirement. See http://www.esrs.gov/index?cck=1#faqs. There also may be an issue with the ability of E-SRS to handle classified contracts. We suggest that the NRO should review this developing E-SRS system to see if it will address the NRO’s needs without imposing an agency-unique requirement.

3. The monitoring aspect of the proposed clause will generate the most questions and issues. Interjecting the NRO into negotiations between two private parties and the potential effects of this intrusion should be carefully considered, as it will affect the subcontracting process.

The proposed clause states that the agency “shall take an active role in monitoring subcontract performance” under the contract that it awards. While the
agency clearly has a legitimate interest in, and a right to review, subcontracting under its prime contracts in order to protect the public interest, relevant regulations and practice provide for the prime contractor to have the responsibility to select its subcontractors, price the effort, ensure adequate performance, and bear the risk of adverse past performance ratings and contractual remedies if its subcontractors fail to perform. Thus, an appropriate balancing is necessary. The Section is concerned with the overly-intrusive monitoring in the proposed clause, which provides that the agency:

- shall have the right to observe all source selection or other competitive sourcing activities with or for subcontractors or potential subcontractors
- shall have the right to observe all fact-finding and negotiation sessions with subcontractors or potential subcontractors
- shall have the right to observe any subcontractor test, verification, validation, or other similar event
- shall have the right to attend any subcontractor status meeting, milestone review, design review, program review, or other similar event

This interjection of the customer into this range of activity would be unique to the NRO and is the most problematic aspect of the proposed clause. One area of concern is that many of these activities with potential subcontractors take place prior to source selection by the customer, and are preceded by the negotiation, preparation, and signing of nondisclosure agreements and often the negotiation of teaming agreements. If the monitoring is triggered by the award of a contract containing this proposed clause, many, if not most, major subcontractors already will have been selected by the prime contractor as recognized by FAR 9.602(c). The clause’s obligations would be triggered by the award of contract, which often would be after the key meetings and decisions to select major subcontractors. Moreover, monitoring would not be practical during the preaward stage because discussions prior to award of the prime contract, which cover proposal and competitive strategies addressing the customer’s procurement, would raise serious issues of access to competitive information. The agency also would have to carefully consider the potential impacts under the Procurement Integrity Act if monitoring were to occur during the preaward stage. Thus, because much of the significant subcontracting decisions occur prior to contract award, the clause’s utility is likely to be limited and it would not give the agency insight into the key subcontracting determinations it is seeking by implementing this clause.

Post-award monitoring access of this nature is not addressed in the FAR and does not occur at present. The primary areas of concern are with the first two listed monitoring situations, which address source selection of subcontractors and the related fact-finding and negotiation sessions. The presence or potential presence of
the customer in such sessions is likely to have an adverse effect upon subcontracting activities. Such a presence could serve to stifle the free, candid and open exchanges of positions, which could include discussion of other collaborative efforts and even future competitive pursuits unrelated to the instant procurement. The entire scope of past, present, and future work between the prime contractor and the subcontractor is often addressed during such sessions. In addition, issues that have arisen are openly discussed, and often debated. Such issues could include the formulation of responses to customer inquires, or resolution of potential disputes between a prime contractor and its subcontractors, which could be affected by customer presence. The presence of a key customer in such sessions could well dampen the effectiveness of such discussions, constructive debate, as well as negotiations. Moreover, sensitive, company private information and strategies often are discussed and the parties frequently will have executed a nondisclosure agreement to facilitate such discussions. Will agency personnel execute similar nondisclosure agreements? If they do not, these important exchanges of information are likely to end..

In addition, it would be extremely difficult for any contractor to comply with the literal terms of this proposed clause. Literally read, the clause would require the contractor to advise the government every time one of the members of the contractor’s purchasing organization picks up the phone to ask a question of a potential subcontractor on a procurement action, or when members of the organization discuss any aspect of potential subcontracting under a contract. This is inconsistent with the dynamic nature of the procurement process and would cause the entire purchasing operation to all but grind to a halt, as well as substantially increase costs.

Finally, involvement in such activities would tax existing agency resources. As a result, the careful selection of specific acquisitions for the monitoring and oversight contemplated by the proposed clause, although still subject to the concerns expressed in this comment may be a more prudent approach than the blanket application of this requirement. Such a high level of oversight into the business negotiations between private parties may also cause commercial companies to avoid contracts with the agency.

4. **The proposed clause’s requirement for customer consent for all subcontracts exceeding $50 million or 10 percent of the contract’s value does not acknowledge that major subcontractors will usually have been selected before award of the contract.**

   As noted earlier, the integrity of the acquisition process requires that the selection and administration of subcontractors reside with the prime contractor.
Nevertheless, the Section supports the safety valve identified in the FAR for key subcontracts, which is the consent right retained by the customer for selection of specifically identified subcontracts. See FAR Subpart 44.2. The proposed clause is inconsistent with the FAR’s approach in stating that consent is required prior to “placement, award, or definitization of any subcontract whose total value exceeds $50 million or 10 percent of this contract’s total value.” The Section recommends that, should this clause be implemented, the scope of the clause be limited to subcontracts in key performance areas and meet the existing FAR oversight rules.

Moreover, there is an important timing issue with use of the post award consent right for significant subcontracts. In preparing to compete for prime contract awards, prime contractors seek teammates\(^3\) that will combine complementary capabilities with their own and those of other subcontractors in order to address and fulfill contract requirements, to be competitive, and to meet the source selection criteria. As a result, teams are formed very early in the procurement process, often before the final solicitation is released. All members of the team then work together in proposal preparation in order to win the contract. Frequently, the team members share the bid and proposal expense, and prepare a proposal highlighting the relevant past performance and experience of the entire team.

The commitments made by a potential prime contractor may be affected by the agency’s right to withhold consent to a subcontract. Most standard teaming agreements used by prime contractors condition the prime contractor’s obligation to award a subcontract on obtaining any necessary customer consent, but in practice this very rarely becomes an issue. In reality, it appears that deference is given to subcontractors brought early into the proposal process by the potential prime contractor to assist as teammates in defining the strategy for pursuit of a contract.

The FAR itself states that the integrity of teaming arrangements should be upheld. FAR 9.603. The “Policy” section of FAR subpart 9.6 states that the integrity and validity of contractor team arrangements will be recognized, and that the “Government will not normally require or encourage the dissolution of contractor team arrangements.” Id. The Section believes that this is a sound policy, and the customer’s right to grant or withhold consent should not be utilized to dissolve such arrangements absent extraordinary circumstances. In addition, relevant case law indicates that formation of a teaming arrangement may create rights and obligations between the teammates that go significantly beyond a

\(^3\) The Section is aware of the NRO prohibition against exclusive teaming, and previously submitted comments on that NRO rule.
commitment that a team member can later compete for a subcontract.\textsuperscript{4} Also, the evaluation criteria and the agency’s source selection decision in competitive procurements frequently are based in part on the offeror teams’ composition, their collective past performance, and the each team’s collective experience. Thus, a post-award change in team composition resulting from the customer exercising its consent right could undermine not only the obligations of the parties, but also the integrity of the procurement process, raising questions about the validity of the source selection decision. The Section therefore recommends that guidance should be given in this area so that procurement personnel understand the relevant considerations in light of existing FAR policy to recognize the integrity and validity of teaming arrangements and the overall procurement process.

5. The flowdown to all subcontractors at all levels is excessive.

The proposed clause also requires that it be included in every subcontract at any tier. The definition of subcontractor suggests that there is no dollar threshold to this requirement.

The Section recommends that NRO place a limit on this flowdown requirement. Because this is an NRO-unique clause that imposes new record collection and record keeping requirements and also requires contractors to revise subcontracting practices in order to provide the agency with access to source selection and subcontract administration activities, the impact on the willingness of potential contractors or subcontractors to do business with NRO should be considered. Some companies may opt not to engage in such unique requirements, and forego potential contracting opportunities for NRO work. As one goes farther down the subcontract chain, one typically finds more and more companies that largely operate in the commercial sector. Few companies operating in the commercial marketplace, however, could comply with this clause. This clause thus could limit competition and have the effect of effectively eliminating commercial products from the NRO supply chain. This result is directly contrary to one of the primary thrusts of the last decade or more of procurement reform. The NRO should also consider whether this clause should be included in subcontracts for commercial items.

The Section appreciates the opportunity to provide these comments and is available to provide additional information or assistance as you may require.

Sincerely,

[Signature]

Robert L. Schaefer
Chair

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