Public Construction Projects: Not Always a Hollywood Ending

Workshop A: The Subcontracting Game: From Flirting with Disaster to Happy Marriages on Public Projects

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Anatomy of the Relationship

- Part I: The Subcontracting Game
  - Courtship: picking the right subcontractor
- Part II: Sub Connection
  - Getting hitched: negotiating the subcontract
- Part III: The Newly-Sub Game
  - Therapy: work together or fall apart
- Part IV: Inside the Attorneys’ Studio
Part I: The Subcontracting Game

PICKING THE RIGHT SUBCONTRACTOR

WITH YOUR HOST: JON WALDEN!
Welcome

- Our Subcontractors: Aaron Silberman
  - Sub #1: Guy from “Good Guy Electrical”
  - Sub #2: Buzz from “Live Wire Electric”
  - Sub #3: Chipper from “24-Hour Power & Electric”

- Our Prime: Jennifer Dauer
  - “Black Widow Contracting”
What Is a DBE?

- **Small Business**
  - Beware *affiliation* with a larger business (e.g., through family)

- **At Least 51% Owned by Disadvantaged Individual(s)**
  - Women or racial minorities (may vary by location)
  - Beware *community property*

- **Controlled by the Disadvantaged Individual(s)**
  - Control over key issues, such as contracts, employment, and financial
  - Control over the Board
  - Necessary experience and/or licenses to control
“Good Faith Efforts” (GFE) to Meet Stated Participation Goal
- Necessary steps, reasonably expected to obtain participation at stated goal
- “Actively and aggressively” trying to meet goal
- Advertising; outreach to DBEs; not rejecting DBE bids without “sound reasons”
- Failure to meet goal or show GFE makes bid unavailable for award

Percentage Participation
- Full credit for work DBE performs
- Material suppliers
  - 100% for manufacturers
  - 60% for “regular dealers”
  - Commission only for brokers
Ways Companies Work Together

- **Joint Ventures**
  - May need *separate license*
  - *Joint responsibility* and liability
  - Enables use of all members’ past experience where subcontractor experience is not to be considered

- **Subcontracting**

- **Teaming Agreements**
  - *Exclusive* or non-exclusive
  - Benefits subcontractor where no requirement to use subcontractor participating in bid
Efforts to **eliminate competition or restrain trade**
- kickbacks
- collusive bidding
- follow-the-leader pricing
- rotated low bids
- collusive price estimating systems
- sharing of business
- other antitrust violations (e.g., loss leader)

Typically require **rejection of offer or contract termination (render void)**
- may also result in civil and criminal liability and debarment
The Subcontracting Game

TUNE IN NEXT WEEK!
Part II: Sub Connection

GETTING HITCHED! (NEGOTIATING THE SUBCONTRACT)
Bidders Conference
Subcontractor Bids

- Often Come in Close to Bid Deadline
  - Work with key trades to get non-price information early
- Check **Scope** for Excluded Work
- Check **Time** Until Price Expires
- Check **Terms** to Be Included in Subcontract
- Check **Licensing**, Including DBEs
Bid Mistakes

- Bidder Must Establish
  - Mistake
  - Making bid “materially different”
  - Clerical error (typographical or arithmetical); not judgment error
  - Timely notice


- May Withdraw Bid Without Forfeiting Bid Bond
- Subcontractor Error Is Not Grounds For Withdrawal
- Claiming Error May Preclude Participating In Rebid
Time to Vote!

- Let Black Widow know with whom you would choose to subcontract
  - Sub #1: Guy from Good Guy Electrical
  - Sub #2: Buzz from Live Wire Electric
  - Sub #3: Chipper from 24-Hour Power & Electric
Bid Shopping/Peddling and Subcontractor Listing

- **Bid Shopping**: using a sub’s bid to coerce lower bids from other subs after contract award
- **Bid Peddling**: underbidding successful subcontractor
- To avoid bid shopping and bid peddling
  - List subcontractor name, location, license number, DIR registration number, and portion of work > .5%
  - Prime must perform work for which no subcontractor is listed
  - Must use listed subcontractors or request substitution
Survey Says . . .
Flowdown Clauses

▲ General Flowdown
   ▶ No gaps between subcontract and prime contract
   ▶ May be unclear or create conflicts

▲ Specific Flowdowns
   ▶ May have gaps between subcontract and prime contract
   ▶ Identified during negotiation; more likely to catch conflicts
   ▶ Prevailing wage and other labor requirements
   ▶ Payment requirements and timing
   ▶ Changes
   ▶ Claims and disputes, including certification and pass-through
Payment Provisions

- Pay-if-Paid vs. Pay-when-Paid
  - PIP: owner payment of prime condition precedent to prime obligation to pay sub – unenforceable in some states (e.g., Cal.)
  - PWP: governs timing of prime’s payment obligation; must pay when paid by owner or within reasonable time – enforceable

- Prompt Payment
  - Within 7 days of payment
  - Interest penalties for violation
    - Cal. Bus. & Prof. Code §7108.5
Disputes

- Disputes Involving Owner
  - Flow down
  - Subcontractor participation in the process?
  - Subcontractor share of deducts (e.g., LDs) or payments
  - Who pays attorneys’ fees?

- Disputes Between Prime Contractor and Subcontractor
  - Jurisdiction/Venue – may be required where project is located
  - ADR
  - Attorneys’ fees
Claims

- Pass through claims
  - Liquidating agreement
  - Certification requirement/False Claims concerns
    - Prime contractor due diligence
    - Subcontractor responsiveness to prime concerns
  - Cooperation

- Subcontractor claims vs. Prime contractor
  - Tolling agreement
Termination Clauses

- **Termination for Cause/Default**
  - Material breach
  - Notice to cure

- **Termination without Cause/for Convenience**
  - Flow down
  - Allows termination in “gray area”
  - Convert termination for default into convenience if court finds no default

- Dovetails with **Substitution**
Let’s Get Working!
Sub Connection!

TUNE IN NEXT WEEK!
Part III:
The Newly-Sub Game

THERAPY! (WORK TOGETHER OR FALL APART)
Payment Disputes

- Invoicing issues
  - Keep track of “force account” (changed) work carefully
  - Certification of accuracy may be required
  - Prime may require reasonable supporting documentation
  - Prime may withhold disputed amounts

- Prompt Payment
  - After Owner has paid Prime
  - No bona fide dispute over specific payment sought

- Subcontractor’s Statutory Remedies
  - Liens? No
  - Stop Payment Notices/Constructive Trusts? Maybe
  - Payment Bond Claims? Yes (subject to defenses)
Payment Bond Claims

- Surety Generally May Rely on Same Defenses to Payment as May Its Principal (here, the Prime)

- But Federal Courts Have Held that Contingent Payment Clause Defenses Are Not Available to Sureties on Federal Projects (at least if not expressly incorporated into the bond)

- Will Courts on State/Local Public Projects Do the Same?
Substitution of Listed Subcontractors

- **California Grounds** (similar standards may apply in other listing states)
  - Failure/refusal to execute a subcontract
  - Bankruptcy or insolvency
  - **Failure/refusal to perform subcontract**
  - Failure/refusal to post bonds (if required)
  - Inadvertent subcontractor listing (clerical error)
  - Unlicensed subcontractor
  - Work is **unsatisfactory** or subcontractor **substantially delays** work
  - Ineligibility to work as a result of Labor Code violations
  - Awarding authority finds subcontractor **not responsible**

- **Penalties** for improper substitution
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What Can They Win?!

- You get paid!
- You won’t be terminated!
- Not criminally prosecuted!
Contract Changes

- **Deductive Change**
  - May result in *re-pricing* ("equitable adjustment") remaining work
  - Partial termination for convenience?

- **Additive Change**
  - May require separate bidding

- **Change in Character**
  - Is it *material*? If yes . . .
    - Does the listed subcontractor have skill/experience to perform?
    - Must the prime use the listed subcontractor?
Pass-Through Claims

- Sub Duty to Provide **Timely** Notice and Support
- Sub Duty to Verify/Certify (if required)
- Prime Duty to Sub to Cooperate
  - Prime risks owing sub and not recovering from owner
- Prime Duty to Verify
  - Prime risks False Claims Act liability if claim is inadequate
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What Did the GC and Sub Win?

- **Black Widow**
  - Avoided false claims liability
  - Defend 24-Hr’s breach of contract claim for nonpayment
  - Defend payment bond claim its surety will tender

- **24-Hr**
  - Must litigate for its (added?) costs
  - Avoided discovery of his bid rigging with Live Wire Electric
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