

Risk Topics

Subcontractor prequalification

A subcontractor prequalification program is an effective tool to mitigate the risk of subcontractor default.

Introduction

Successful general contractors carefully evaluate whether or not to include a subcontractor in bidding opportunities. An effective subcontractor pre-qualification program can help contractors avoid failure by identifying preferred subcontractors that meet their operational and financial requirements.

Discussion

Evaluating a subcontractor's qualifications prior to bid is an essential tool to establish a subcontractor's capabilities for performing the scope of work. Factors include current capacity, reputation, financial capability and expertise in a particular area of work. Information should be initially submitted via a questionnaire. It is the contractor's responsibility to verify the submitted information and evaluate the qualifications relative to the work being bid.

Guidance

A general Contractor's typical subcontractor prequalification procedure will request the subcontractor to provide the following documents:

Prequalification Questionnaire

Surety Capacity Letter

Certified Financial Statement

Consider including the following in any subcontractor Prequalification Questionnaire:

- Company Name, Address, Phone Number, Fax Number and Website address
- Type of work the subcontractor specializes in.
- Years in Business.
- Form of business (Corporation, Subchapter S Corporation, Partnership, Proprietorship, LLC)
- Is the company union or open shop?

- Federal Tax ID#
- Date Founded and State of Formation.
- Indicate if the business qualifies as a DBE, MBE, SBE or WBE. Provide certification number.
- List the jurisdictions in which the organization is legally qualified to do business.
- Key Personnel.
- Does the subcontractor have a full time safety representative?
- Does the subcontractor have a formal written Safety Manual/Program?
- Does the subcontractor have a full time QA/QC representative?
- Does the subcontractor have a formal Quality Control Manual/Program?
- Experience
 - List the largest contracts completed under the current management. Indicate the type of contract, e.g. fixed price, cost plus, GMP, owner, architect, date of completion, percentage of work performed with own forces and contract amount. Include project references.
 - What is the largest project completed?
 - What is the current backlog?
- Claims and Suits
 - Has the subcontractor ever failed to complete any work awarded to it?
 - Are there any judgments, claims, arbitration proceedings or pending lawsuits against the organization?
 - Has the subcontractor filed any lawsuits or requested arbitration with regard to construction contracts in the last five years?
- References
 - Trade References
 - Five Major Suppliers
 - Five General Contractors with whom the subcontractor has worked in the last three years
 - Three Architects and/or Engineers for whom the subcontractor has worked in the last three years
 - Bank Reference
 - Surety Reference
 - Include bonding capacity
- Financial Information
 - The last five years of financial statements, preferably audited, including the organization's latest balance sheet and income statement.
 - Name and address of the firm preparing the financial statement.

- Were daily reports submitted in a timely manner?
- Were shop drawings and submittals provided timely and accurately?
- How did the subcontractor respond to the punch list and warranty issues?
- Insurance
 - Is the insurance underwritten by a US domiciled firm licensed to conduct business in the state for which the work is to be performed and rated A.M. Best (A-) or better?
 - Does the policy coverage lapse before the end of the project warranty period?
 - Does the insurance certificate identify the general contractor, designer and owner as additional insured?
 - Can the insurance covered by the certificate be cancelled or materially altered without notice to the additional insured?
 - Does the certificate contain “endeavor to” or similar phrases such as “failure to do so shall create no obligation or liability of any kind on the insured, its agents, or representatives”?
 - Does the insurance coverage apply to all subcontractors and/or sub-subcontractors?
 - Is the insurance primary and non-contributory basis to General Contractor insurance?
 - Does the certificate declare exclusions for residential, condominium, multifamily or apartment projects?
 - Is there a mold exclusion clause under the liability policy?
 - If yes, is mold coverage carried in another capacity?
- Safety
 - Does the subcontractor have a documented safety program?
 - Has the subcontractor submitted a copy of the documented safety program?
 - Does the subcontractor have dedicated safety personnel?
 - Does the subcontractor conduct project safety meetings and how often?
 - Does the subcontractor have a drug-free workplace program including pre-employment and random testing?
 - Has the subcontractor ever received any fines or citations from OSHA?
 - Has the subcontractor ever experienced any worker fatalities?
 - Secure a copy of the subcontractor’s OSHA 300 logs and OSHA 300A summaries. Evaluate the following:
 - Is the Experience Modification Rate (EMR) less than or equal to 1.00?
 - Incidence Recordable Rate (IRR) = (Number of Injuries and/or illnesses) x 200,000 / (Total Hours worked by all employees). Is it less than 4.00?
 - Lost Day Case Rate (LDCR) – (Number of lost day cases) x 200,000 / (Total Hours worked by all employees). Is it less than 0.80?

- Quality Assurance/Quality Control
 - Does the subcontractor have a written quality control program? (if so, request a copy)
 - Does the subcontractor have a full-time quality control director?
 - Does the subcontractor have an apprenticeship training program?
 - Does the subcontractor have a tradesman training program?
 - What other types of training programs does the subcontractor require of its employees?
 - Does the subcontractor retain a third party inspection and testing consultant?
 - Does the subcontractor develop and use preconstruction/constructability plans?
 - Does the subcontractor erect sample panels and/or mock ups?
 - Have inspection checklists been developed?
 - How does the subcontractor monitor delivery and sources of materials?
 - What type of effort does the subcontractor extend to protecting stored materials on-site and off-site?
 - Does the subcontractor perform its own winter weather protection of installed and stored materials?

- Surety Capacity Letter
 - How long has the subcontractor been with its present surety?
 - Who was the subcontractor's previous surety during the past 5 years, and the reasons for the change?
 - Are there any current or previous disputes or claims with owner's, general contractors, subcontractors, or suppliers on any bonded projects?
 - Has the subcontractor's surety ever completed a project?
 - Has the subcontractor ever had a bond request denied or granted with conditions considered unacceptable?
 - Has the subcontractor ever had its bond credit terminated?
 - Is the letter written on the Surety's letterhead?
 - Is the letter addressed to the General Contractor?
 - Is the letter signed by Attorney-in-Fact and dated?
 - How long ago was the letter issued, and does the letter expire prior to contract award?
 - Is the Power of Attorney attached?
 - The Surety should be rated "A-" or better by A.M. Best Company.
 - Is the surety listed on the U.S. Treasury Department Circular 570 (T-List).
 - The Surety should have Treasury Listing Capacity of 100% subcontract amount.
 - Does the letter state single project and aggregate work program limits?

- Does the subcontract amount fall within the per project and aggregate limits?
- Is the subcontractor's backlog, including a single project, less than the aggregate limits?
- Certified Financial Statement
 - Does the financial statement cover the fiscal year-end period ending within the past 12 months?
 - How often are financial statements prepared?
 - Does the financial statement include a CPA opinion letter, balance sheet, income statement, and CPA notes?
 - Is the percentage of completion accounting used?
 - Is less than 50% of the bank line of credit in use?
 - Do the CPA notes indicate compliance with bank covenants?
 - Do the CPA notes reference any pending litigation or contingencies?
 - A general contractor should evaluate a subcontractor's capital base, working capital, profitability, asset utilization, overhead expenses, notes accompanying the financial statement, completed contract and work-in-progress schedules, ratio and trend analysis, credit reports, banking credit and the qualifications of the CPA preparing the financial statement.
 - In the absence of the subcontractor's Certified Financial Statement, a General Contractor can consider obtaining a Dunn & Bradstreet Comprehensive and Business Information Report.

Conclusion

Ultimately the General Contractor must decide to award, or not to award, work to the applicant subcontractor. There are many proprietary subcontractor prequalification scoring systems utilized in the industry, many of which are available for purchase; however, you can use this RiskTopic as a resource to help you develop your own subcontractor prequalification form or help you evaluate a subcontractor for hire on a construction project.

Appendices

Zurich's Subguard® program - Subcontractor prequalification guidebook. Please access this document via the link below:

[Zurich subcontractor prequalification guidebook](#)

A sample Subcontractor Qualification Statement/prequalification form is available to all Builder's Risk insureds. To obtain a copy, contact your risk engineering account coordinator.

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