

Caught in the Federal Procurement Fish Bowl

26th Annual Ounce of Prevention Seminar

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Contracting with Small Businesses in the Wake of Expanding SBA Programs and Scrutiny

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- Background: Expanding Programs & Scrutiny
- Maximizing Large Business Opportunities
- Proposed Changes To Mentor-Protégé JV Rules
- Top 5 Things You Should Know About ANCs
- Increasing Subcontracting Percentages

SBA Challenges for 2010: Expanding SBA Programs & Scrutiny

U.S. Small Bus. Ass'n Office of Inspector Gen. Report No. 10-02, Fiscal Year 2010 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration, October 16, 2009

- SBA staff sizes have decreased while: (a) most set-aside programs have grown significantly; (b) value of federal SB contracts increased by > 50%
- Procurement “loopholes” allow large firms to obtain SB awards and agencies to count those contracts toward SB goals
- Agencies misreport contracts as awarded to SBs as a result of dubious self-certifications or misapplication of SB contracting rules
- GSA MAS contracts that contain multiple NAICS codes allow companies to identify themselves as “small” although they do not meet the size criteria for all orders
- Programs need to increase number of firms that receive assistance by: (a) developing clear and objective standards to measure disadvantage; (b) insuring that firms follow regulations when they complete contracts; (c) graduating firms that become “business successes”

SBA Program Goal: “Insure against fraud, waste and abuse”

Preventative Controls

- Self-certification with “adequate” supporting documentation
- Use third party data to certify program eligibility
- Use data-mining techniques and financial analysis to verify objective criteria

Detection / Monitoring

- Collect and maintain current and accurate firm data
- Review SBA business specialist work loads, training, and potential conflicts of interest
- Unannounced site visits at certification and annual reviews that create face-to-face contact

Investigation / Prosecution

- Cancel contract award when awardee is determined ineligible and decertify ineligible firms
- Impose suspension and debarment for a reasonable time for status misrepresentation
- Refer to SBA OIG those firms that knowingly misrepresent status

Lever 1: Preventative Controls

Example – HUBZone Program

GAO-09-440 and GAO-09-519T, HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas, March 25, 2009

GAO-09-532T, Small Business Administration: Status of Efforts to Address Previous Recommendation on the HUBZone Program, March 25, 2009

- SBA lacks mechanisms to certify firm eligibility or monitor continuing eligibility
- Firms participate in Historically Underutilized Business Zone program despite failing to meet eligibility standards
 - Principal office location is often not in HUBZone
 - 35% of employees are often not residents of HUBZone
- SBA does not promptly remove ineligible firms from the HUBZone program

Lever 1: Preventative Controls Recommendations

Recommendations

HUBZone Problems Identified:

- SBA lacks controls to certify and monitor firms
- Firms participate in the benefits of the program despite failing to meet eligibility
- SBA does not promptly remove fraudulent firms from the HUBZone program

- Establish front-end controls at application stage
- Obtain documentation from firms supporting self-certification
- Use third party data sources to verify eligibility
- Conduct more frequent site visits
- Use risk analysis to identify firms for unannounced site visits as part of screening process
- Formalize and adhere to time frames for decertifying ineligible firms

Lever 2: Detection / Monitoring

Example – 8(a) Program

GAO-10-353, Small Business Administration: Steps Have Been Taken to Improve Administration of the 8(a) Program, but Key Controls for continued Eligibility Need Strengthening, March 30, 2010

GAO-10-425, 8(a) Program: Fourteen Ineligible Firms Received \$325 Million in Sole-Source and Set-Aside Contracts, March 30, 2010

- SBA relies primarily on annual review process to ensure continued eligibility
- But approximately 55% of participants fail to complete annual review procedures
 - Lack specific evaluation criteria that relate to eligibility requirements (e.g., thresholds by industry for size, limits to personal compensation or assets)
 - SBA business development specialists both monitor and advocate for firms
 - SBA's electronic systems lack data integrity
- Therefore, firms that have outgrown the program continue to receive 8(a) benefits

Lever 2: Detection / Monitoring Recommendations

8(a) Problems Identified:

- Undefined evaluation criteria
- Specialist conflict of interest
- Specialist work load too high
- Data sources poor
- No face-to-face experience with companies

Recommendations

- Enact regulations to tighten program metrics for income and asset calculations
- SBA administrator to monitor specialists and provide guidance and training
- Collect and maintain up to date data on firms, including complaint data and mentor-protégé agreements
- Use data-mining to detect ineligibility
- Make face-to-face contact through unannounced site visits to verify firm-reported data
- Perform timely eligibility reviews
- Review specialist work loads

Lever 3: Investigation / Prosecution

Example – SDVOSB

GAO-10-108 and GAO-10-255T, Service-Disabled Veteran-Owned Small Business Program: Case Studies Show Fraud and Abuse Allowed Ineligible Firms to Obtain Millions of Dollars in Contracts, October 23, 2009 and November 19, 2009

- The Department of Veterans Affairs maintains a database of Service-Disabled Veteran-Owned and Veteran-Owned Small Businesses
 - SBA and contracting officers do not have access to this information
 - Firms are not required to submit documents to prove eligibility
- But firms not infrequently misrepresent status regarding being a service-disabled veteran, controlling day-to-day operations, and acting as a pass-through entity for contracts
 - SBA and contracting officers rarely verify the eligibility of SDVOSB and VOSB firms unless in response to a protest
 - There is no statutory obligation to do so prior to award
- Agencies are not required to terminate ineligible firms even after protest of status and ineligible firms have retained the contract after protest and secured additional work
- SBA asserts that it has limited responsibility over the SDVOSB program and does not have a role in eligibility verification

Lever 3: Investigation / Prosecution Recommendations

Recommendations

SDVOSB Problems Identified:

- No access to VA database on SDVOSB and VOSB firms
- Firms are not required to substantiate eligibility up front
- SBA and contracting officers do not verify eligibility up-front
- Enforcement is through bid protest process
- Ineligible firms often retain contract awards once given
- Ineligible firms sometimes received additional awards
- SBA has limited responsibility

- Secure access to VA's "verified" database to validate firms prior to award
- Disbar for reasonable time those contractors who knowingly misrepresent their status
- Submit cases of misrepresentation to the SBA Office of Inspector General for further review
- Congress should provide VA with authority and resources necessary to expand its SDVOSB and VOSB eligibility verification to all contracts, not just VA contracts

Meeting SBA Program Goal: A Successful Program (SBIR)

GAO-09-956T, Small Business Innovation Research: Observations on Agencies' Data Collection and Eligibility Determination Efforts, August 6, 2009

“Successful” because . . .

- Awards are based on technical merit and generally of good quality
- Program attracts many qualified companies
- High level of competition
- High number of first time participants
- Program serves agency missions and meets R&D needs

Preventative Controls

- A firm may self-certify, but the contracting agency is under an obligation to verify eligibility of a participating firm

Detection / Monitoring

- Data is collected in a government-use database to share information and enhance monitoring and evaluation of firms (active since Oct. 2008)
- Data entry is constrained to consistent format

Investigation / Prosecution

- If the contracting agency cannot verify eligibility of a firm, it must refer the firm to the SBA
- If the SBA determines that the firm is ineligible, the determination is reported on the SBA website

Meeting SBA Program Goal: Through Rulemaking (WOSB)

13 CFR Parts 121, 127, and 134, Women-Owned Small Business Federal Contract Program, 75 Fed. Reg. 42, *Proposed Rule Mar. 4, 2010, comments closed May 3, 2010*

Preventative Controls

- A firm may certify as a WOSB through a Federal Agency, State Government, or SBA-approved third-party
- A firm may self-certify as a WOSB with the CO, but must supply “adequate” supporting documentation

Detection / Monitoring

- Establish a WOSB Program Repository to store certification supporting documentation to be supplemented each year, or as needed (e.g., recertification, protest, program examination)
- Require program examinations of WOSB firms at any time, including random examinations to insure against fraud, waste and abuse in the program

Investigation / Prosecution

- Failure to file supporting documentation requires the contracting officer to file a protest with the SBA and not award a contract to the alleged WOSB
- If the CO does not believe that the apparent successful offeror meets program requirements, the CO must file a protest with the SBA regarding the firm’s status

For Your Information: Recent Rules or Proposed Rules

- 13 CFR Part 126, HUBZone Program, *effective* May 3, 2010
 - Expands and clarifies the definition of “employee” to satisfy HUBZone requirements to include: (a) all individuals employed so long as the individual works a minimum of 40 hours per month; (b) includes those employed through a temporary agency, leasing concern, union agreement, or professional employer organization agreement allowing for co-employment
- 13 CFR Parts 121, 127, and 134, Women-Owned Small Business Federal Contract Program, 75 Fed. Reg. 42, *Proposed Rule* Mar. 4, 2010, *comments closed* May 3, 2010
 - Proposes to: (a) eliminate need for agency by agency determination of discrimination against women; (b) use a count of WOSBs and the value of money awarded to WOSBs to measure under representation in any NAICS; (c) use Central Contractor Registration database as data source for determination of under representation of women in any NAICS
 - Identifies 45 under represented industries and 38 “substantially” under represented industries (compare to Oct. 1, 2008 proposed rule identifying 4 total industries)
- 13 CFR Parts 121 and 124, Small Business Size Regulations; 8(a) Business Development/Small Disadvantaged Business Status Determinations, 74 Fed. Reg. 207, *Proposed Rule* Oct. 29, 2009, *comments closed* Dec. 28, 2009
 - Changes intend to: (a) eliminate abuse of joint ventures between tribally-owned or ANC-owned firms and large businesses; (b) clarify existing SBA requirements; (c) reduce certain 8(a) program restrictions

For Your Information: Recent Cases

- *Delex Systems, Inc.*, 23 CGEN ¶ 112,697, B-400403 (Oct. 8, 2008)
 - GAO ruled that the “Rule of Two” applies not only to contract award, but also task and delivery order competitions among multiple-award contract holders
 - The SBA “Rule of Two” requires an agency to limit competition to small businesses when it concludes that it has a reasonable expectation of receiving offers from at least two responsible small businesses and an award can be made at a fair and reasonable price
- *Mission Critical Solutions*, 24 CGEN ¶ 112,839, B-401057 (May 4, 2009) and *Int'l Program Group, Inc.*, 23 CGEN ¶ 112,686, B-400278, B-400308 (Sept. 19, 2008)
 - Prioritization of HUBZone small businesses over 8(a) Program and Service-Disabled Veteran-Owned businesses is mandatory when the HUBZone program’s enumerated conditions are met
 - OMB later instructed agencies to disregard the GAO decisions and consider multiple small business programs in line with SBA “parity” policies (July 10, 2009)
- *Infiniti Info. Solutions, LLC v. U.S.*, Case No. 09-750C, ___ Fed. Cl. ___ (April 2, 2010)
 - Set aside 8(a) award because agency acted arbitrarily by claiming that Service-Disabled Veteran-Owned status was a “preference,” not a requirement
 - Determined that agency improperly issued a statement of work despite SBA regulations allowing only for informal assessments of participants’ capabilities

For Your Information:

Reports Referenced (1 of 2)

- GAO-10-353, Small Business Administration: Steps Have Been Taken to Improve Administration of the 8(a) Program, but Key Controls for continued Eligibility Need Strengthening, March 30, 2010
- GAO-10-425, 8(a) Program: Fourteen Ineligible Firms Received \$325 Million in Sole-Source and Set-Aside Contracts, March 30, 2010
- GAO-10-108 and GAO-10-255T, Service-Disabled Veteran-Owned Small Business Program: Case Studies Show Fraud and Abuse Allowed Ineligible Firms to Obtain Millions of Dollars in Contracts, October 23, 2009 and November 19, 2009
- GAO-09-956T, Small Business Innovation Research: Observations on Agencies' Data Collection and Eligibility Determination Efforts, August 6, 2009
- GAO-09-440 and GAO-09-519T, HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas, March 25, 2009
- GAO-09-532T, Small Business Administration: Status of Efforts to Address Previous Recommendation on the HUBZone Program, March 25, 2009

For Your Information: Reports Referenced (2 of 2)

- U.S. Small Bus. Ass'n Office of Inspector Gen. Report No. 10-07, SBA Regulations Relating to Unconditional Ownership Requirements for Indian Tribes, January 25, 2010
- U.S. Small Bus. Ass'n Office of Inspector Gen. Report No. 10-02, Fiscal Year 2010 Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration, October 16, 2009
- U.S. Small Bus. Ass'n Office of Inspector Gen. Report No. 9-15, Participation in the 8(A) Program by Firms Owned by Alaska Native Corporations, July 10, 2009
- Majority Staff Analysis, Senate Comm. on Homeland Security & Governmental Affairs, Subcomm. on Contracting Oversight, New Information About Contracting Preferences for Alaska Native Corporations (Part II), July 15, 2009 (prepared for Chairman Claire McCaskill)

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Maximizing Large Business Subcontract Opportunities under Set Asides

- If Sub, understand how the limitations on subcontracting are calculated
- Focus on what does NOT count:
 - Services: 49% of the cost of the contract incurred for personnel; materials; supplies; overhead that does not have only direct labor as its base; profit; and fees
 - Supplies: 49% of the cost of manufacturing the supplies; costs not incurred in production of the end item; materials, off-the-shelf items; required special tooling or test equipment; profit; and fees
 - Construction: 74% of the cost of the contract; materials; profit and fees
- Also consider nonmanufacturer rule, if applicable
- Must still consider other affiliation factors – “totality of the circumstances”

Maximizing Large Business Prime Contract Opportunities under Set Asides

SBA's Mentor-Protégé (M-P) Program

- SBA's M-P Program as affiliation exception for JVs and up to an additional 40% equity interest in Protégé
- Since generally only one Protégé permitted (more allowed if demonstrate they will not be competitors), conduct due diligence before selection
- Types of assistance offered pursuant to M-P agreement should be as broad as possible (umbrella to avoid affiliation consideration)
- Avoid commitments Mentor is not willing to provide
- Understand unique advantages of ANCs and other tribally-owned entities – consider as possible Protégés
- Leave adequate time for SBA approval!

Maximizing Large Business Prime Contract Opportunities under Set Asides

- Specific M-P JV requirements, including:
 - Designate Protégé as Managing Venturer
 - Employee of Protégé designated as Project Manager
 - At least 51% of net profits of JV distributed to Protégé
 - Each party obligated to ensure performance of the contract even if member withdraws
 - JV must comply with limitations on subcontracting
 - Protégé must perform a “significant portion” of the contract
 - SBA must approve (1) JV agreement before contract award and (2) any amendments to JV agreement
- Protégé must maintain control over JV
 - Majority voting rights with limited exceptions
 - Caution with quorum, blocking rights, and supermajority requirements

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Proposed Changes to Mentor-Protégé JV Rules

- SBA issued proposed changes to 8(a) and size regulations on 10/28/09 – still awaiting Final Rule
- JVs for multiple procurements:
 - Change limit from 3 offers to 3 awards
 - For second and third awards, provide SBA w/ an addendum to original JV agreement
- If JV is a separate legal entity, JV must be populated (note that the SBA also recognizes “informal joint ventures” based solely on agreement without formation of new legal entity)
- Eliminate requirement for Protégé to receive 51% of profits and replace with requirement for it to receive profits from JV commensurate with work performed

Proposed Changes to Mentor-Protégé JV Rules

- For M-P JV with ANCs, if sole source award, Mentor cannot also be a subcontractor to the JV
- Requirements in 13 C.F.R. § 124.513(c),(d) must be met for 8(a) and SB set asides for exception to affiliation to apply
- Require that Protégé perform at least 40% of the work performed by the JV (and, as before, JV must comply with the limitations on subcontracting)
- M-P JV can also qualify as small for subcontracts
- Possible sanctions if Mentor fails to provide promised assistance to Protégé:
 - Stop work order
 - M-P agreement termination
 - 2-year bar on serving as Mentor
 - Debarment proceedings

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Top 5 Things You Should Know About ANCs

#1 -- Can Be Large, Multi-Tiered Organizations

- ANCs permitted to create multiple 8(a) subsidiaries
- Tribe cannot own 51% or more of another firm which, either at the time of 8(a) application or within the previous 2 years, has been operating in the 8(a) program under the same primary NAICS code

Top 5 Things You Should Know About ANCs

#2 -- Affiliation Exception

- Normally – parent, subsidiaries, sister entities deemed affiliated for size purposes
- No affiliation because of common ownership, management, or sharing of administrative services
- Administrative services of large organization of significant benefit in proposal preparation, accounting, performance, etc.

Top 5 Things You Should Know About ANCs

#3 -- No limit sole-source awards

- 8(a) contracts may be awarded on sole source basis if anticipated price will not exceed \$5M for manufacturing or \$3.5M for all others (13 C.F.R. § 124.506(a)(2)(ii))
- No monetary cap on sole source awards to ANCs (13 C.F.R. § 124.506(b))
- Sole source awards not subject to protest (13 C.F.R. § 124.517(a))

Top 5 Things You Should Know About ANCs

#4 – Legislative purpose of ANCs is to distribute land and monetary benefits to Alaska Natives in lieu of reservation system

- Purpose is NOT to require Alaska Natives to perform the work under the awarded contracts
- Individual responsible for control and management of ANC-owned 8(a) need not establish personal social and economic disadvantage

Top 5 Things You Should Know About ANCs

#5 -- Delegation of credit for subcontracting goals

- General rule: only first-tier subcontracts count towards satisfaction of subcontracting goals
- Exception: Lower-tier ANCs may designate higher-tier subcontractors as entities entitled to receive subcontracting credit (FAR 52.219-9(d)(1)(ii))

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Key Strategies for Increasing Subcontracting Percentages

- Goals/reports (eSRS) only include first-tier subcontracts
- Goals increasingly tied into proposal evaluation
- Goals expressed as “percentages of total planned subcontracting dollars” for SBs, VOSBs, SDVOSBs, SDBs, WOSBs, HUBZone
- Goals can increase with decrease in total subcontracted value – BUT total subcontracted dollars still reported
- Purchases from affiliates are not counted
- Proposed Regulations: Count 100% of subcontracts with M-P JVs as small and 8(a)
- Size re-certification requirements do not apply at the subcontractor level – what matters is size at time of subcontract award (13 C.F.R. § 121.404(e))