



Big Changes for Small Business: Recent Regulatory Developments

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Purpose of Training



- SBA requirements impact fundamental eligibility issues for competition
- When and how large and small businesses work together lies at the heart of most compliance issues
- Keep informed of the complex and fluctuating rules and regulations applicable to small business and companies contracting with them
 - Be prepared for the FAR and SBA size and status protest and appeals rules to be consistent again
 - Be aware of the expansion of SBA's mentor-protégé program and potential opportunities (and pit-falls) for your business
 - Be informed of how to calculate and comply with new formulas for limitations on subcontracting – a key issue in affiliation and responsibility determinations
 - Beware of continued expansion of oversight and enforcement

Agenda



- Small business basics
- Preview of proposed rules for small business size and status protests
- Significant expansion of mentor-protégé program
- New formulas for limitations on subcontracting
- Sources of oversight and enforcement
- Questions?

What Is a Small Business?



- SB is independently owned and operated and is not dominant in its field of operation (market share / controlling influence nationally)
- SBA does not maintain a list of SBs
- Size requirements vary to reflect industry differences (based on number of employees or average annual receipts)
- SBA developed a table of size standards to match the North American Industry Classification System (“NAICS”) (13 CFR 121.201)
- NAICS code is identified in the solicitation
- Offeror certifies in SAM that it is small for the size standard in that procurement (may be small for some procurements but not others); primes get written self-certifications from subs

When Is Size Determined?



- Size status determined as of date contractor submits self-certification that it is small to the procuring agency as part of an initial offer (or other formal response to solicitation) which includes price
- If solicitation modified so initial offers are no longer responsive, contractor must recertify when submitting a responsive offer including price
- 8(a), SDB, HUBZone applicants must qualify as small in the primary industry classification on date application submitted to SBA and on date of SBA certification
- If small when receive contract, then small for entire duration (even if grow beyond size standard)
 - But several key exceptions such as merger, acquisition, novation
 - FAR re-certification requirement

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SB Size & Status Protests Background (1)



- Size/status protests differ from bid protests – file with the SBA under even tighter timelines
- Contractor may have to pursue size protest with SBA at same time as bid protest
- Low threshold to file; difficult/burdensome to respond; document production obligations and certifications for protested entity (SBA Form 355)
- Proposed rule issued 3/7/13 to amend FAR provisions related to small business size and status protests; 60 day comment period
- Most revisions are long overdue and consistent with 1/2/11 and 1/12/12 revisions to SBA regulations, which are already being applied by SBA in considering protests

SB Size & Status Protests Background (2)



Current FAR Size & Status Protest Procedures:

- Eligible offerors (does not include large businesses unless only 1 offer submitted), CO, and SBA may challenge size status
- File protest with CO within 10 days; SBA Gov't Contracting Area Office decides; appeals to OHA
- But, negotiated procurements – protest w/in 5 business days of notice award; awardee has 3 days to respond
- Size protest must relate to a particular procurement and be specific to be considered
- SBA to issue a size determination w/in 10 business days, “if possible”
- Burden of persuasion is with the concern whose size is challenged
- Appeals are available for size and certain status determinations (not available for SDB or SDVOSB)
- Status protests have slightly different procedures for each category
- NAICS code appeals also have own procedures

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SB Size & Status Protests Effect of Determination



- If a concern is found to be other than a small business
 - A CO shall not award a contract to the concern for the procurement in question
 - If the determination is received after award, the CO shall terminate the award if no appeal filed
 - If an appeal is filed, the CO must determine if performance can be suspended until an appellate decision is rendered
 - If the CO allows performance to proceed and the concern is found to be other than small on appeal, the CO shall either terminate the contract or not exercise the next option
- Once a concern is determined to be other than small
 - It cannot reduce its size to become eligible
 - Is ineligible for future procurements authorized for entities of that size or smaller unless SBA recertifies or OHA reverses
 - Recertification is not required if ineligibility was based only on affiliation due to joint venture (*e.g.*, ostensible subcontractor)

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SB Size & Status Protests Penalties for Misrepresentation



- Size protests can lead to determinations that entity is not small or not eligible for particular SBA status
- Investigations, suspension/debarment, other penalties could follow an adverse size/status determination
- The Small Business Act provides for severe criminal penalties for knowingly misrepresenting small business size status:
 - Fine of not more than \$500,000 or by imprisonment for not more than 10 years, or both
 - Subject to administrative penalties for fraud
 - Subject to suspension and debarment
 - Ineligible to participate in any program or activity conducted by the SBA for up to 3 years
- May also be subject to:
 - Investigations
 - Civil or criminal False Claims Act penalties

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Proposed Rules: New Status Protest Procedures



- Increases time that SBA has to make a size determination of a protested concern to 15 business days and allow the CO to extend that time, if needed
- No award made until SBA makes size determination or 15 days since SBA receipt of protest (whichever first); CO may award if determine in writing necessary to protest public interest
- If no SBA determination in 15 days (or granted extension), CO may award contract if determine in writing immediate need to award
- Clarifies that SBA may reopen a formal size determination to correct an error if still within appeal period and no appeal has been filed
- Clarifies that it is within the discretion of OHA to accept an appeal
- SBA decision if received before award, applies to the pending acquisition
- Provides for a CO to determine whether to suspend an award to a party whose size determination has been timely appealed
- Provides that a contract to a concern found ineligible by OHA, and award had already been made, must be terminated unless not in best interests of Gov't; no options or orders to be exercised

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Proposed Rules: New Status Protest Procedures



- Amends FAR 19.306 through 19.308 to provide consistent guidance on the application of protest and appeal decisions
 - Will affect HUBZone small businesses, SDVOSBs, EDWOSBs, and WOSBs
 - Does not affect protests of SDB status
- Revisions would address:
 - Information that the protest must contain to be considered
 - Timeframes for submission of a protest
 - CO responsibilities
 - Procedures for a concern determined to be ineligible for a given status to regain that status
- Protest requirements by status:
 - SDVOSB – protester must present evidence that either the owner cannot prove that VA declared owner to be a service-disabled veteran OR that no single or group of service-disabled veterans owns 51% or more of the business
 - EDWOSB or WOSB – protester must present evidence that the business is not 51% (or more) owned by an EDWOSB or WOSB
 - HUBZone – protester must present evidence that the business’s principal office is not located in a HUBZone or that less than 35% of the business’s employees reside in a HUBZone

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Proposed Rules: Misc. Other Revisions



- Clarifies requirements for “nonmanufacturers”
 - SB must be primarily in the retail or wholesale trade
 - Must sell the item in its normal course of business
 - Must take ownership or possession of item, consistent with industry practice
 - Must supply an end item made in the US (or outlying areas)
- States that CO must update the status of an ineligible concern in the Federal Procurement Data System (FPDS) once a final size determination is made
- Provides additional guidance to COs regarding NAICS determinations
 - Instructs that CO shall select NAICS code that best describes “principal purpose” of product or service
 - Including changes to the appeal process

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Mentor-Protégé: 8(a) Program Background (1)



Mentor-Protégé (M-P) Program - Key Benefits:

- SBA's M-P Program as affiliation exception for JVs; large business can have shared responsibilities as prime contractor
- JV qualifies as small and 8(a) on set-asides and for subcontracts (can be used to meet subcontracting goals)
- Ability to form multiple JVs to exceed regulatory limit of 3 awards in 2-year period
- Mentor can have up to 40% equity interest in Protégé
- Assistance provided under M-P agreement is exempt from affiliation
- Eligibility requirements for Mentor and Protégé; currently Protégés limited to 8(a) contractors
- Mentors generally limited to 1 Protégé; prohibited from more than 3; multiple Protégés cannot be competitors
- Protégé benefits from true mentorship, increase awards due to JV combined capabilities

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Mentor-Protégé: 8(a) Program Background (2)



SBA v. Other M-P Programs:

- Only SBA program provides exemption from affiliation for M-P joint venture
- Other agency-specific M-P programs with varying benefits; only exempt from affiliation for assistance provided between Mentor and Protégé if M-P program authorized by statute or SBA
- Differing approval process, benefits, eligibility, and reporting under other programs
- Most designed to operate when Protégé is acting as subcontractor to Mentor (DoD)
- Other types of benefits: subcontracting credit; reimbursement for costs of assistance; evaluation credit; awards and recognition

Mentor-Protégé Program Expansion



- Section 1641 of FY13 NDAA authorizes expansion of SBA 8(a) M-P program to all SBs
- Expanded program similar to 8(a) program but may modify to extent necessary given types of SB protégés
- Agency M-P plans (except for DoD) no longer permitted unless minimum requirements satisfied
- Requires SBA approval of agency plans, based on
 - Finding that the plan assists protégé to compete for federal prime and subcontracts
 - Complies with regulations to be issued, including assurance that protégé is protected against mentors that may:
 - Adversely affect protégé size status; or
 - Provide disproportionate benefits to mentor over protégé

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Mentor-Protégé Program Expansion



- SBA must issue proposed regulations for M-P program within 270 days (subject to notice and comment)
- Agencies with M-P programs must submit conforming plans within 6 months of promulgation of new SBA rules
- Approved M-P agreements not impacted and may continue for duration of term of agreement

Mentor-Protégé Program Expansion - Questions



- Limitations on number of protégés?
- What if protégé is certified in more than one category?
- Why does the new definition of a mentor eliminate non-profits?
- Will there be overall limits on numbers of agreements?
- How will this impact competitions on set-aside procurements?
- When should companies start researching for potential pairings?

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Limitations on Subcontracting: “Current” Limitations (1)



- Prime must perform certain percentage of cost of contract (does not include profit/fee charged at prime level):
 - **Services (Non-Construction).** $\geq 50\%$ of the cost of the contract incurred for personnel with its own employees – includes any overhead which has only direct labor as its base and SB’s G&A rates multiplied by the labor cost.
 - **Supplies or Products (Other Than Procurement from a “Non-Manufacturer”).** $\geq 50\%$ of the cost of manufacturing the supplies or products (not including the cost of materials). This includes the costs incurred by the SB in the production of the end item being acquired. It does not include costs of the materials purchased, shipping and handling, off-the-shelf items, or special tooling and test equipment.
 - **General Construction.** At least 15% of the cost of the contract with its own employees (not including the cost of materials).
 - **Specialty Trade Construction.** At least 25% of the cost of the contract with its own employees (not including cost of materials).
- Directed subcontracts do not count and subcontracts with affiliates of SB do not count as part of prime’s percentage

Limitations on Subcontracting: “Current” Limitations (2)



- 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
 - **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
 - **Construction:** 84% of the cost of the contract, materials
 - **Specialty Trade Construction:** 74% of the cost of the contract, materials
- Also consider non-manufacturer rule, if applicable
- Must still consider other affiliation factors – “totality of the circumstances”

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Limitations on Subcontracting: “Changing” Limitations



- **New rule for services**: SB prime may not spend on subs more than 50% of the amount paid to the SB under the contract
- **New rule for supplies**: (other than from a regular dealer), SB may not spend on subs more than 50% of the amount paid under the contract, less cost of materials
 - **Supplies from regular dealer**: must supply the product of a domestic small business manufacturer or processor, unless waived by SBA under certain circumstances
- **Added test**: Also determine whether supplies or services represent the greatest percentage of the contract, and SB prime may not spend more than 50% of that amount on subs
- Similarly situated entities are not “subs”
- SBA may establish rules for categories of contracts not covered here; must establish similar rules for construction projects

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Limitations on Subcontracting: Potential Impact



- Major questions raised by these changing limitations include:
 - When will implementing regulations be issued? For SBA regulations and FAR? What about in the interim?
 - How is a “subcontractor” to be defined?
 - Will this result in more or less work performed by the SB prime?
 - If it requires greater self-performance, will it decrease competition?
 - Why was the calculation on construction not addressed?
 - Any requirements or obligations for determining that a subcontractor is a “similarly situated entity”? Is small business status determined based on NAICS code for the prime contract or most appropriate code for the subcontract?

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Oversight and Enforcement: Overarching Policies



- Ensure that small businesses are the true beneficiaries of set-aside dollars
- Encourage small business skill development in government contracting
- Assure use of small businesses as contemplated by contract awards
- Avoid fraud in contracting

Oversight and Enforcement: 2013 NDAA Provisions



- Penalties associated with new limitations on subcontracting
 - Greater of \$500K or amount in excess of the limitations on subcontracting spent on subs
- Provisions for reporting the fraud of a prime
 - SBA to establish a reporting mechanism to allow a sub or potential sub to report fraudulent activity or bad faith by a prime with regard to a subcontracting plan
- Requirement for Suspension and Debarment
 - SBA directed to implement regulations for a suspension and debarment program to ensure that “fraudulent” businesses are suspended or debarred

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Oversight and Enforcement: Prop Rule: “Subcontract Integrity”



- Relates to “covered contracts” for which SB subcontracting plan is required (construction over \$1.5M; others over \$650K)
- Allows funding agency to monitor prime’s small business subcontracting and to encourage it to meet subcontracting plan
 - Prime must represent that it will make good faith efforts to award subcontracts to small businesses at same percentage as indicated in plan
 - Provide written justification and explanation to CO for failure to meet percentage
 - Notify CO if pay reduced price to subcontractor
 - Allow funding agency to establish goals at individual level for multi-agency, FSS, MAS, and IDIQ contracts

Oversight and Enforcement: Mentor-Protégé



- “Enforcement” Recently Added to the Mentor-Protégé Program: revised SBA regulations identify consequences for a Mentor that fails to provide the assistance it committed to provide in its Mentor/Protégé agreement:
 - SBA may recommend that the procuring agency issue a stop work order for each Federal contract for which the Mentor and Protégé are performing as a small business joint venture; protégé may be permitted as substitute for mentor/protégé joint venture
 - Authorizes SBA to terminate a mentor/protégé agreement when the mentor has failed to provide the agreed upon developmental assistance, and render the mentor firm ineligible to again act as a mentor for a period of two years from termination of agreement
 - Failure to comply with terms and conditions of mentor/protégé agreement may be grounds for suspension/debarment

Oversight and Enforcement: Examples (1)



- October 2011 Suspension of GTSI: the “Wake-Up Call” on Small Business Issues
 - No prior warning – simultaneous with *Washington Post* headlines
 - Suspension based on:
 - Adequate evidence of commission of fraud or criminal offense in connection with obtaining, attempting to obtain, or performing a contract or subcontract; and
 - Adequate evidence indicating lack of business integrity/honesty casting doubt on GTSI’s responsibility
- GTSI key issue was compliance with limitations on subcontracting:
 - GTSI’s prime contractors had little to no involvement (0-.5%) in performing set-aside contracts
 - GTSI concealed the extent of its involvement as a subcontractor
 - Suspension lifted only after removal of CEO, GC, and others, and agreement to turn over internal business documents to government
 - Subsequent suspensions of GTSI small business prime contractors (EG Solutions and MultimaxArray)

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Oversight and Enforcement: Examples (2)



- Subcontracts found unenforceable: *Morris-Griffin Corp. v. C & L Servs. Corp.*
 - District Court found that a subcontract between a SB prime and large business sub was unenforceable because it was in violation of the SBA regulations and the limitation on subcontracting
 - Court found that SB’s size certification was false and “conceived in fraud” and noted that set-asides are “susceptible to finagling”

Oversight and Enforcement: Examples (3)



- Caddell Construction Co. Non-Prosecution Agreement (NPA) with DOJ to resolve criminal fraud allegations on two contracts
 - Related to overstatement of development assistance provided to SDB under DoD program
 - Related to participation in mentor-protégé program and participation in DoD Native-American business rebate program
 - False statements of Native-American business' size and income
 - Also regarding technical capabilities and business infrastructure
 - And requests for rebate against services largely completed by Caddell, not Native-American business
 - Caddell voluntarily disclosed issues
 - \$2 million penalty and NPA

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