



## 29TH ANNUAL OUNCE OF PREVENTION SEMINAR

Weathering the  
Rough Seas of  
Regulation



# Small Business: Enforcement Shakedown and Legislative Shakeup

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# Agenda

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

# 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

# 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

# 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”

# 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

# 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



# Oversight and Enforcement: Mentor-Protégé

- “Enforcement” under the Mentor-Protégé Program: 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

# SB Penalties for Misrepresentation

- Size protests can lead to determinations that entity is not small or not eligible for particular SBA status
- 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

# Oversight and Enforcement: “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: Example (1)

- 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

# Oversight and Enforcement: Example (2)

- Virginia Security Contractors Pled Guilty to Illegally Obtaining \$31 million in Contracts Intended for SDBs
  - Formed one company with African-American woman as CEO in 2001 to participate in 8(a) program; she left in 2003 and company lost status
  - Formed second company in 2003, listing another minority woman as “figurehead owner,” but who would not actually manage the company
    - Misled SBA through 2012, including falsely certifying status under size protest
    - Also agreed to pay a bribe to US contracting official to secure contracts
  - Investigated by numerous IGs (NASA, SBA, GSA, DHS) and DCIS
  - Principal conspirator faces 10 years and multi-million fine for fraud; 5 years for conspiracy to commit bribery; forfeiture of \$6.3 million
  - Four other co-conspirators also pled guilty and will be sentenced this summer

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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 5 business days; SBA Gov't Contracting Area Office decides; appeals to OHA
- Awardee has 3 business days to respond; may request extension
- 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
- Status protests have slightly different procedures for each category
- NAICS code appeals also have own procedures



# 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)

# Proposed Rules: New Size 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 protect the 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

# Recent Size Appeal Cases

- *Professional Project Servs., Inc.*, SBA No. SIZ-5411 (2012) (NAICS Code omitted from GSA Schedule task order competition)
- *Metters Indus., Inc. v. United States*, 109 Fed. Cl. 444 (2013) (government enjoined from making award prior to OHA decision)
- *Miles Constr., LLC v. United States*, 108 Fed. Cl. 792 (2013) (reinstating protester to SDVOSB program)

# New Rule: Woman-Owned Small Businesses

- Previously, agencies could only set-aside contracts valued at \$4 million (\$6.5 million for manufacturing) for WOSBs or EDWOSBs
- NDAA for FY 2013 removed dollar value restrictions
- SBA issued Interim Final Rule effective immediately
- Contracting Officers now may set-aside any dollar value contract for WOSBs or EDWOSBs
  - in industries where WOSBs or EDWOSBs are underrepresented,
  - a reasonable expectation two or more entities will submit offers, and
  - the government can award a contract at fair and reasonable prices

# 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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