

Congress of the United States
U.S. House of Representatives
Committee on Small Business
2361 Rayburn House Office Building
Washington, DC 20515-6515

To: Members, Subcommittee on Contracting and the Workforce, Committee on Small Business
From: Committee Staff
Date: November 16, 2015
Re: Hearing: "Continuing Challenges for Small Contractors."

The Committee on Small Business Subcommittee on Contracting and Workforce will meet for a hearing titled, "*Continuing Challenges for Small Contractors.*" The hearing is scheduled to begin at **10:00 A.M. on Wednesday, November 18, 2015, in Room 2360 of the Rayburn House Office Building.**

As part of the Subcommittee's ongoing effort to improve the competitive viability of small contractors, the hearing will examine two issues affecting small contractors. First, it will look at the issue of transparency in federal contracting programs designed to assist small businesses. Second, it will allow small subcontractors to explain the unique problems they face in the federal arena.

I. Executive Summary

a. Goaling and Transparency

As discussed in Section II, SBA reports annually to Congress on the small business accomplishments during the prior year, but the Subcommittee is concerned that the report does not accurately reflect whether the federal government is meeting the small business goals. This section will discuss SBA's exclusions from the goaling base, and additional areas where transparency would further Congress' small business policies.

b. Subcontracting

Statutory and administrative goals are intended to provide small businesses with significant subcontracting opportunities. Unfortunately, a lack of attention, consequences, and systems continues to plague the program. This section will discuss issues small subcontractors face when attempting to obtain work.

II. Goaling

Recognizing the importance of small businesses to the economy, Congress has established a series of programs to assist small businesses competing for federal contracts.¹ It did so because the use of small businesses as contractors is “in the interest of maintaining or mobilizing the Nation’s full productive capacity, [. . .] in the interest of war or national defense programs, [and . . .] in the interest of assuring that a fair proportion of the total purchases and contracts for property and services for the Government in each industry category are placed with small-business concerns.”² To achieve these aims, the Act establishes a series of goals.

a. Types of Goals

There are three types of small business goals: numerical goals, industrial goals, and maximum practicable utilization. The most commonly recognized of these goals are the numerical goals, and of those the prime contracting goals are the most prominent, and it is these that are pertinent to this memorandum. Section 15(g) of the Act requires that the federal government have a government-wide goal of awarding “not less than 23 percent of the total value of all prime contracts awards for each fiscal year” to small business concerns. Additionally, there is a goal of awarding three percent of all prime contract dollars to service-disabled veteran-owned small businesses (SDVOSBs), and three percent to qualified small businesses located in historically underutilized business zones (HUBZones).³ Further, there is a goal of awarding five percent of all prime contract dollars to small business concerns owned and controlled by socially and economically disadvantaged individuals (SDBs) and five percent to small business concerns owned and controlled by women (WOSBs).⁴ In FY 2013, the Small Business Administration (SBA) reported that the federal government met the 23 percent goal, and exceeded the SDB and SDVOSB goals.⁵ In FY 2014, the SBA again reported that the federal government exceeded the small business goal SDB goal and SDVOSB goal.⁶

The federal government has subcontracting goals as well as prime contracting goals. The SBA sets the subcontracting goal at 36 percent of subcontracted dollars during the fiscal year, and statute sets the goals for SDBs, HUBZones, WOSBs, and SDVOSBs at the same level as the respective prime contracting goals.⁷ Subcontracting goals only apply to contracts awarded to

¹ For information on these programs, please see Committee Memorandum, *Small Business Act Programs for Federal Contractors* (February 2013), available at http://smallbusiness.house.gov/uploadedfiles/small_business_act_programs_for_small_federal_contractors.pdf (last accessed November 13, 2015).

² The Act, § 15(a), 15 U.S.C. § 644(a).

³ The Act, §§ 15(g)(1)(ii)-(iii), 15 U.S.C. §§ 644(g)(1)(ii)-(iii).

⁴ The Act, §§ 15(g)(1)(iv)-(v), 15 U.S.C. §§ 644(g)(1)(iv)-(v).

⁵ SBA, “FY 2013 Procurement Scorecard,” available at https://www.sba.gov/sites/default/files/files/FY13_Government-Wide_SB_Procurement_Scorecard_Public_View_2014-04-28.pdf (last accessed November 13, 2015).

⁶ SBA, “FY 2014 Procurement Scorecard,” available at https://www.sba.gov/sites/default/files/files/FY14_Government-Wide_SB_Procurement_Scorecard_Public_View_2015-04-29.pdf (last accessed November 13, 2015).

⁷ The Act, § 15(g)(1), 15 U.S.C. § 644(g)(1).

other-than-small business concerns.⁸ In FY 2013 and FY 2014, the federal government met only the WOSB and SDB subcontracting goals.⁹

b. SBA's Role in Prime Goaling

SBA negotiates each agency's goals on an annual basis.¹⁰ It then reports annually on the numerical goals through its scorecard process. SBA's scorecard awards a letter grade to the federal government and each agency.¹¹ Data on an agency's achievements is collected from the Federal Procurement Data System (FPDS) which gathers data directly from each contracting agency.¹² However, the SBA then directs FPDS to exclude certain categories of contracts from the goaling base.¹³ This results in the percentage of dollars awarded to any category of prime contractor being artificially inflated.

Specifically, SBA excludes all contracts awarded to participants in the Ability One contracting program, the American Institute of Taiwan or to Unicor.¹⁴ Likewise, contracts awarded and performed abroad are excluded, although contracts awarded domestically but performed abroad are included.¹⁵ Purchases of less than \$3,500 made via government credit cards are excluded, even though agencies track these purchases.¹⁶ If a purchase is made for a foreign government, using federal funds or a third party's funds, it is excluded.¹⁷ Finally, contracts funded predominately with agency generated sources rather than appropriations, personal services contracts, and contracts not subject to the Federal Acquisition Regulations are not included in the goaling base.¹⁸

As a result of these exclusions, in FY 2014 roughly 18 percent of all federal contract dollars were excluded from the base.¹⁹ Thus, rather than goaling the federal government against over \$444 billion in contracts, SBA only goaled the federal government against \$367 billion. For some agencies, this means that the majority of the dollars they spent were not captured. As the following table illustrates, five agencies excluded over half of the total amount spent, while 30 agencies excluded some portion of their contract obligations.²⁰

⁸ The Act, § 8(d), 15 U.S.C. § 637(d).

⁹ SBA, "FY 2013 Procurement Scorecard"; SBA, "FY 2014 Procurement Scorecard."

¹⁰ The Act, § 15(g)(1)(B), 15 U.S.C. § 644(g)(1)(B).

¹¹ The process for calculating grades was described in Committee Memorandum, "*Contracting and the Industrial Base II: Bundling, Goaling, and the Office of Hearings and Appeals*" (March 2015), available at http://smbiz.house.gov/uploadedfiles/3-17-2015_hearing_memo.pdf (last accessed November 13, 2015).

¹² SBA, GOALING GUIDELINES FOR THE SMALL BUSINESS PREFERENCE PROGRAMS FOR PRIME AND SUBCONTRACT FEDERAL GOALS & ACHIEVEMENTS 7 (2003), available at https://www.sba.gov/sites/default/files/goals_goaling_guidelines.pdf (last accessed November 13, 2015).

¹³ *Id.*

¹⁴ *Id.* at 7-8. Ability One is a program for contracting with entities employing the blind and severely disabled. Unicor is the federal prison industries contracting program.

¹⁵ GOALING GUIDELINES FOR THE SMALL BUSINESS PREFERENCE PROGRAMS FOR PRIME AND SUBCONTRACT FEDERAL GOALS & ACHIEVEMENTS at 8.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.* at 9.

¹⁹ FPDS Report generated November 13, 2015 (on file with the Committee).

²⁰ *Id.*

Goaling Base versus Total Amount Spent for FY 2014

Agency	Goaling Base	Total Spend	Percentage Included in Goaling Base
Department of Transportation	\$1,769,220,337	\$6,222,227,612	28%
Agency for International Development	\$1,347,092,200	\$3,846,862,344	35%
Department of State	\$3,354,225,558	\$9,065,754,878	37%
General Services Administration	\$3,964,810,955	\$9,091,849,366	44%
Department of the Treasury	\$2,749,604,524	\$5,579,278,415	49%
National Science Foundation	\$275,673,117	\$454,899,833	61%
Department of the Interior	\$2,715,201,216	\$4,187,767,500	65%
Millennium Challenge Corporation	\$66,205,661	\$94,703,935	70%
Broadcasting Board of Governors	\$116,461,791	\$158,854,940	73%
Department of Defense	\$231,382,278,810	\$284,213,075,735	81%
Court Services and Offender Supervision Agency	\$40,660,707	\$48,301,707	84%
Office of Personnel Management	\$873,910,228	\$1,032,293,944	85%
Trade Development Agency	\$15,684,692	\$18,526,603	85%
Smithsonian Institution	\$258,900,704	\$287,241,753	90%
National Aeronautics and Space Administration	\$13,598,215,631	\$15,011,895,633	91%
Department of Justice	\$6,509,989,896	\$7,169,962,898	91%
National Archives and Records Administration	\$147,088,312	\$161,640,039	91%
Department of Energy	\$23,262,991,122	\$25,390,299,345	92%
J.F. Kennedy Center for the Performing Arts	\$11,049,222	\$11,829,707	93%
International Boundary and Water Commission U.S.- Mexico	\$61,674,931	\$66,031,125	93%
Peace Corps	\$108,469,032	\$114,524,848	95%
Federal Energy Regulatory Commission	\$52,079,444.29	\$54,220,235	96%
Overseas Private Investment Corporation	\$15,108,366	\$15,618,860	97%
Department of Education	\$2,863,787,659	\$2,935,446,323	98%
Corporation for National and Community Service	\$71,109,170	\$72,879,454	98%
Federal Trade Commission	\$92,214,634	\$94,443,605	98%
Department of Health and Human Services	\$21,140,131,457	\$21,522,368,442	98%
International Trade Commission	\$10,481,983	\$10,650,837	98%
National Transportation Safety Board	\$13,397,613	\$13,540,260	99%
Railroad Retirement Board	\$42,380,935	\$42,677,370	99%

Interestingly enough, of the agency’s receiving letter grades from SBA, every agency that excluded more than ten percent of its spending received an “A” or “A+” from SBA for FY 2014.²¹

Agency	% of Spend Included in Goaling Base	SBA Letter Grade for FY 2014
Department of Transportation	28%	A
Agency for International Development	35%	A+
Department of State	37%	A
General Services Administration	44%	A
Department of the Treasury	49%	A
National Science Foundation	61%	A
Department of the Interior	65%	A
Department of Defense	81%	A
Office of Personnel Management	85%	A

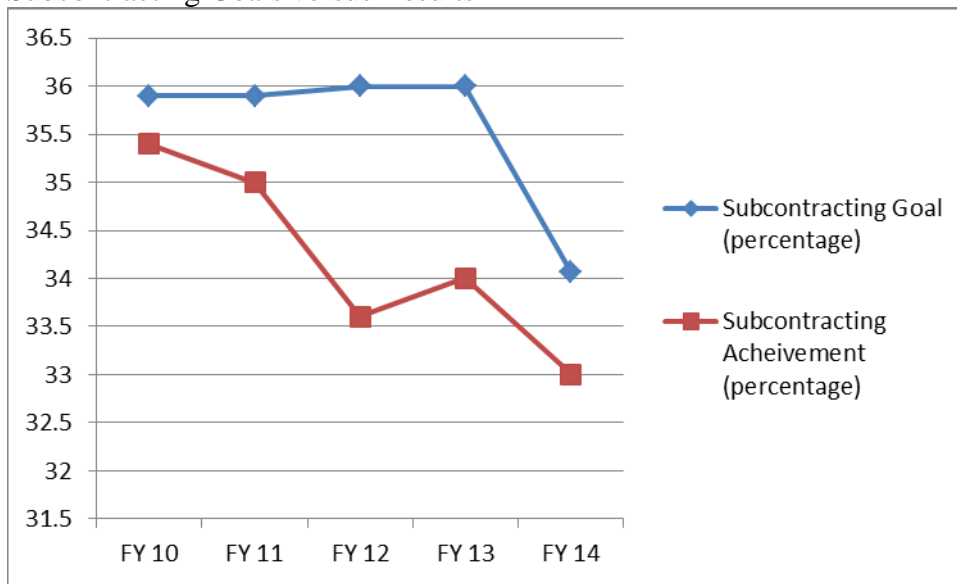
Thus, it appears that the exclusions are carefully drawn so as to ensure that agencies may still succeed on their scorecard while not meeting their goals. For example, when the Department of Transportation’s actual small business achievements are calculated, only 13 percent of its prime contracts are awarded to small businesses, rather than the nearly 46 percent reported by SBA. Likewise, while SBA states that the General Services Administration awarded 40 percent of its contracts to small businesses, in reality only 17 percent actually went to small firms.

c. SBA’s Role in Subcontract Goaling

Unlike the small business prime contract goal, the small business subcontract goal is administratively rather than statutorily determined. This allows SBA to adjust the subcontracting goal based on what it perceives to be the real opportunities for subcontracting. However, as the graph below illustrates, while SBA has steadily decreased the subcontracting goals from 36 percent to 34 percent over the last five years, subcontracting achievements have fallen from 35 percent to 33 percent. Each time SBA decrease the goals, agencies manage to subcontract less with small businesses. This results in real losses to small businesses. For example, FY 2013, small businesses received \$86.7 billion in subcontracts, which is just about \$5 billion less than they received in prime contracts. If federal agencies had met the then-goal of 36 percent, subcontract would have accounted for more dollars to small business than prime contracts. The fact that the goal keeps decreasing indicates that less and less is being provided to small subcontractors.

²¹ *Id.*

Subcontracting Goals versus Results²²



d. Questions Before the Subcommittee

i. Should Exclusions from the Goaling Base be Permitted?

When the concept of small business contracting goals was introduced through Public Law 95-507²³ and the Business Opportunity Development Reform Act of 1988 (BODRA),²⁴ none of the Congressional authors believed that the phrase “the total value of all prime contract awards for each fiscal year” needed further explanation to define the types of contracts to which the goal applied, or that agencies needed encouragement to reach the goals. However, in 1991 the Office of Federal Procurement Policy (OFPP) began allowing²⁵ DOE to count subcontracts awarded by its management and operations (M&O) contractors as if they were prime contracts awarded by the DOE.²⁶ This allowed DOE to count 18 percent of its prime contract dollars as being awarded to small businesses until 1999, when OFPP reversed its decision on the M&O contracts,²⁷ and it became apparent that DOE had only been awarding 3 percent of its prime contract dollars to small businesses. Over a decade later, DOE only has a goal of 6 percent small business participation, so the goals are clearly not motivating the agency to improve its performance.

²² Graph based on data from FY 2014 Procurement Scorecard, FY 2013 Procurement Scorecard; SBA “FY 2012 Procurement Scorecard,” *available at* https://www.sba.gov/sites/default/files/files/FY12_Final_Scorecard_Government-Wide_2013-06-20.pdf (*last accessed* November 16, 2015); SBA, “FY 2011 Procurement Scorecard,” *available at* https://www.sba.gov/sites/default/files/files/FY11%20Final%20Scorecard%20Government-Wide_2012-06-29.pdf (*last accessed* November 16, 2015); SBA, “FY 2010 Procurement Scorecard,” *available at* https://www.sba.gov/sites/default/files/files/FY10%20SB%20Procurement%20Scorecard_FINAL_GOVERNMENT%20WIDE.pdf (*last accessed* November 16, 2015).

²³ This Act has no common name and is simply An Act of October 24, 1978.

²⁴ Pub. Law No. 100-656 (1988).

²⁵ OFPP Policy Letter 91-1 (1991)

²⁶ *See, e.g.,* Acquisition Regulation: Implementation of Section 3021 of the Energy Policy Act of 1992, Notice of Proposed Rulemaking, 59 Fed. Reg. 35,294, 35,295 (July 11, 1994).

²⁷ OFPP Policy Letter 99-1 (1999) rescinding OFPP Policy Letter 91-1.

After OFPP changed course on the inclusion of M&O subcontracts, SBA in rules published in 2003²⁸ began allowing agencies to exclude certain types of contracts from consideration before the goal achievements were calculated. Under this method, approximately 18 percent of all prime contract dollars are excluded from the contracting base before the goals are calculated, thus inflating the performance of all agencies, but as explained earlier some agencies are excluding up to 72 percent of the contracted dollars spent during a fiscal year.

If all federal prime contract dollars were included in the goaling base, small businesses could expect an additional \$11 billion in prime contract awards. Thus, the Subcommittee wishes to explore whether there is any reason to permit the continued use of exclusions.

ii. Should SBA Be Required to Explain Its Subcontracting Formula?

SBA's subcontracting goals are arbitrary. In an attempt to improve this process, the National Defense Authorization for FY 2013 required that:

Not later than 180 days after the date of the enactment of this part, the Administrator of the [SBA] shall review and revise the Goaling Guidelines for the Small Business Preference Programs for Prime and Subcontract Federal Procurement Goals and Achievements to the extent necessary to ensure that . . . agency subcontracting goals are established on the basis of realistically achievable improvements to levels of subcontracting rather than on the basis of an average of previous years' subcontracting performance.²⁹

However, nearly three years after the President signed the NDAA, SBA has not issued new subcontracting goaling guidelines. Indeed, instead of implementing goals that reflect "achievable improvements" the SBA has decreased the subcontracting goal since 2013. The Subcommittee wishes to learn whether a higher subcontracting goal would improve opportunities for small subcontractors.

iii. Is the Data in FPDS Reliable?

The prior concerns all assume that contracts coded as awarded to small businesses in FPDS were indeed awarded to small businesses. However, as recently as September 2014, the SBA Inspector General issued a report that identified over \$400 million in FY 2013 contract actions that may have been awarded to ineligible firms, and over \$1.5 billion dollars in contract actions for which the firms were in the 8(a) or HUBZone programs at the time of contract award, but were no longer in these programs in FY 2013.³⁰ One of the key issues appears to be that while agencies are allowed

²⁸ SBA, GOALING GUIDELINES FOR THE SMALL BUSINESS PREFERENCE PROGRAMS FOR PRIME AND SUBCONTRACT FEDERAL PROCUREMENT GOALS AND ACHIEVEMENTS, 68 Fed. Reg. 43,566 (July 23, 2003).

²⁹ Pub. Law No. 112-239 §1631(c) (2013).

³⁰ SBA Office of the Inspector General, AGENCIES ARE OVERSTATING SMALL DISADVANTAGED BUSINESS AND HUBZONE GOALING CREDIT BY INCLUDING CONTRACTS PERFORMED BY INELIGIBLE FIRMS 7 Report 14-18 (2014) available at

<https://www.sba.gov/sites/default/files/oig/Agencies%20Are%20Overstating%20SDB%20and%20HUBZone%20Goal%20ing%20Credit.pdf>.

to continue receiving credit for work awarded to a firm that is later acquired by a large business, FPDS does not distinguish these awards. Given that the FPDS system is expected to be renovated starting in FY 2016, this may be a field worth adding to the system.

III. Subcontracting Issues

As previously discussed, the Executive branch has a nonstatutory goal of awarding 34.06 percent of all dollars subcontracted from federal prime contracts to small businesses.³¹ It also has statutory goals of awarding 5 percent of subcontracted dollars to WOSB and SDB firms, and 3 percent to SDVOSB and HUBZone firms. To achieve these goals, a contract awarded to an other-than-small business for more than \$650,000 must include a subcontracting plan enumerating the opportunities for small businesses to participate as subcontractors and the plan must assign both percentage and dollar value goals to these opportunities.³² The failure of an other-than-small business to make a good faith effort to comply with the subcontracting plan is supposed to result in the government collecting liquidated damages from the contractor.³³ However, the compliance with subcontracting plans remains a challenge.

a. Overview of the Operation of Subcontracting Programs

The SBA Procurement Center Representative (PCR),³⁴ when available, provides an opinion to the contracting officer on the appropriate subcontracting goals, and then the Commercial Market Representative (CMR)³⁵ and contracting officer assume responsibility for post-award compliance. Agencies and prime contractors are required to report on subcontract performance, and compliance with the subcontracting goal is reflected in past performance reports on prime contractors.³⁶ However, given the sheer number of other-than-small prime contractors and the fact that there are fewer than 35 full and part time CMRs,³⁷ it is not surprising that in FY 2006, the SBA OIG found that CMRs monitored less than half of the 2,200 largest prime contractors.³⁸ Consequently, contracting officers are the primary official responsible for ensuring compliance with subcontracting plans.

³¹ SBA, GOVERNMENTWIDE 2010 SMALL BUSINESS PROCUREMENT SCORECARD (2011). Interestingly, in 2003, the goal was 40 percent, and in 1978, this Committee amended the Small Business Act to address the fact that small businesses were receiving only 37.5 percent of subcontract dollars – 1.6 percent more than the current goal. SBA, GOALING GUIDELINES FOR THE SMALL BUSINESS PREFERENCE PROGRAMS FOR PRIME AND SUBCONTRACT FEDERAL PROCUREMENT GOALS AND ACHIEVEMENTS 6 (2003).

³² 15 U.S.C. § 637(d). H.R. REP. NO. 95-949, at 5 (1978) [hereinafter, 1978 Report].

³³ *Id.* at (5). The damages are calculated as the actual dollar amount by which the contractor failed to achieve each subcontracting goal. 48 C.F.R. § 19.705-7.

³⁴ According to the SBA, PCRs “increase the small business share of Federal procurement awards by initiating small business set-asides, reserving procurements for competition among small business firms; providing small business sources to Federal buying activities; and counseling small firms. In addition, PCRs, advocate for the breakout of items for full and open competition to affect savings to the Federal Government.” SBA, GOVERNMENT CONTRACTING FIELD STAFF DIRECTORY (2011) [hereinafter FIELD STAFF DIRECTORY], available at <http://www.sba.gov/content/government-contracting-field-staff-directory>.

³⁵ CMRs also assist small businesses seeking subcontracts through counseling and matchmaking. FIELD STAFF DIRECTORY.

³⁶ 48 C.F.R. § 19.704.

³⁷ The average CMR is responsible for 90 to 200 prime contractors. GAO, IMPROVEMENTS NEEDED TO HELP ENSURE RELIABILITY OF SBA’S PERFORMANCE DATA ON PROCUREMENT CENTER REPRESENTATIVES 2 (2011).

³⁸ SBA OIG, OFFICE OF THE INSPECTOR GENERAL, REVIEW OF SBA’S SUBCONTRACTING ASSISTANCE PROGRAM, 2007 (No. 7-33).

Specifically, the contracting officer is responsible for “assisting in evaluating subcontracting plans, and for monitoring, evaluating, and documenting contractor performance under the clause prescribed in [48 C.F.R. §] 19.708(b) and any subcontracting plan included in the contract.”³⁹

This includes providing:

- (e) Immediate notice if, during performance, the contractor is failing to meet its commitments under the clause prescribed in [48 C.F.R §] 19.708(b) or the subcontracting plan;
- (f) Immediate notice and rationale if, during performance, the contractor is failing to comply in good faith with the subcontracting plan; and
- (g) Immediate notice that performance under a contract is complete, that the goals were or were not met, and, if not met, whether there is any indication of a lack of a good faith effort to comply with the subcontracting plan.⁴⁰

To be put on the notice contemplated by this provision, the contracting officer is supposed to monitor the contractor’s subcontracting activities. Firms with subcontracting plans are required to submit semiannual individual contract reports, a report within 30 days of contract completion, and summary subcontracting reports annually, except that the Department of Defense (DoD) and the National Aeronautics and Space Administration (NASA) require summary reports semiannually. These reports used to be submitted on SF 294 and SF 295, but have since been replaced by the Electronic Subcontracting Reporting System (ESRS).

Since the liquidated damages penalty is triggered by failure to make a good faith effort to comply with a subcontracting plan rather than failure to achieve the goals in the plan, the important issue becomes how the SBA defines good faith efforts. A prime contractor can demonstrate that it has made a good faith effort in one of three ways: (1) by meeting its goals; (2) by overachieving in some categories to make up for an underachievement in other categories; or (3) by performing one of a laundry list of actions.⁴¹ These other actions include:

- (i) Breaking out contract work items into economically feasible units, as appropriate, to facilitate small business participation;
- (ii) Conducting market research to identify small business subcontractors and suppliers through all reasonable means, such as performing on-line searches on the Central Contractor Registration (NCR), posting Notices of Sources Sought and/or Requests for Proposal on SBA's SUB-Net, participating in Business Matchmaking events, and attending pre-bid conferences;
- (iii) Soliciting small business concerns as early in the acquisition process as practicable to allow them sufficient time to submit a timely offer for the subcontract;

³⁹ 48 C.F.R. § 19.706.

⁴⁰ *Id.*

⁴¹ 13 C.F.R. § 125.3(d).

- (iv) Providing interested small businesses with adequate and timely information about the plans, specifications, and requirements for performance of the prime contract to assist them in submitting a timely offer for the subcontract;
- (v) Negotiating in good faith with interested small businesses;
- (vi) Directing small businesses that need additional assistance to SBA;
- (vii) Assisting interested small businesses in obtaining bonding, lines of credit, required insurance, necessary equipment, supplies, materials, or services;
- (viii) Utilizing the available services of small business associations; local, state, and Federal small business assistance offices; and other organizations;
- (ix) Participating in a formal mentor-protégé program with one or more small-business protégés that results in developmental assistance to the protégés.⁴²

This list is so broad that it makes it almost impossible for a contracting officer to issue a notice that a large prime contractor has failed to make a good faith effort to comply with its subcontracting plan. However, if such notice is issued, the contracting officer is then responsible for “[i]nitiating action to assess liquidated damages.”⁴³

The threat of liquidated damages is empty for many prime contractors. In over 30 years, there is no record of any company paying these damages, essentially neutering any deterrent the liquidated damages provision was intended to provide. Some agencies have made an effort to incentivize compliance. For example, some multiple award contracts use subcontracting performance on prior task orders as an evaluation factor for awarding additional task orders.⁴⁴ However, GAO has repeatedly found that even on the most high profile contracts, agencies fail to ensure that the ESRS reports are even filed.⁴⁵ Indeed, the Committee has received reports of prime contractors sponsoring agency small business conferences in order to ensure a finding of good faith – writing a check to agencies rather than writing subcontracts to small businesses.⁴⁶ Thus, small businesses continue to struggle to receive subcontracting opportunities.

b. Subcontracting Systems

The federal government has two systems to track subcontracting, and one to advertise subcontracting opportunities. As previously discussed, the first, ESRS, tracks other-than-small businesses’ subcontracting achievements. When a contracting officer makes a prime contract award, the data is reported to FPDS, and if a subcontracting plan is required it populates the correct

⁴² *Id.* at (b)(3).

⁴³ 48 C.F.R. § 19.705-6(f).

⁴⁴ *See, e.g.*, General Services Administration’s (GSA) National Broker Contract II.

⁴⁵ *See, e.g.*, GAO, FEDERAL CONTRACTING IN THE AFTERMATH OF HURRICANES KATRINA AND RITA, (2011) (GAO-11-942T) (23 percent of contractors failed to file subcontracting reports); GAO, DOD NEEDS MEASURES FOR SMALL BUSINESS SUBCONTRACTING PROGRAM AND BETTER DATA ON FOREIGN SUBCONTRACTS (2004) (GAO-04-381) (data concerns with DOD subcontracting plans) GAO, AGENCY CONTRACTING DATA SHOULD BE MORE COMPLETE REGARDING SUBCONTRACTING OPPORTUNITIES FOR SMALL BUSINESSES (2007) (GAO-07-698T).

⁴⁶ Conversations with Committee staff.

file in ESRS. While ESRS makes the calculation of the government-wide subcontracting achievements easier, the system does not readily lend itself to compliance. ESRS does not integrate into any of the other databases or systems routinely used by the contracting officer. If a firm fails to file a report, or if its reports do not conform to the subcontracting plan, ESRS does not notify the contracting officer, the SBA, or the agency's Office of Small and Disadvantaged Business Utilization (OSDBU) of the problem. Instead, the system remains a passive receptacle of data that once a year calculates the Administration's subcontracting achievements.

The second system is the Federal Subcontracting Reporting System (FSRS), which was created by the Federal Funding Accountability and Transparency Act (FFATA).⁴⁷ FFATA required that all prime contractors and prime grant award recipients report any subcontract or subgrant executed. This information is then published at www.USASpending.gov.⁴⁸ However, even though FSRS collects subcontracting data, no effort is made to reconcile its data with that in ESRS, or to use that data to track compliance with limitation on subcontracting provisions. FSRS does not notify the contracting officer, the SBA, or the agency's OSDBU if a business fails to file reports, or if the reports indicate a problem. Instead, the system remains a passive receptacle of data.

The final system is the SBA Subcontracting Network (SUB-Net). The Small Business Act requires that prime contractors publish any subcontracting opportunities over \$10,000 through a publication known as Commerce Business Daily (CBD).⁴⁹ At the time this provision was added, CBD also reported all prime contract opportunities. On January 1, 2002, CBD was replaced by Federal Business Opportunities (FBO) a website that provides all prime contract opportunities over \$25,000 at www.fbo.gov. SBA introduced Sub-Net, which was intended to replace the subcontracting function. Unfortunately, Sub-Net has never been fully adopted. For example, on September 28, 2011, Sub-Net contained fewer than 150 small business subcontracting opportunities. In contrast, on the same day, FBO documented over 39,700 active prime contract opportunities. The FAR does not even mention SUB-Net, so it remains unclear how prime contractors would be required to use the system. The system does not communicate with FPDS, FSRS or ESRS.

c. Issues Before the Subcommittee

i. Subcontracting Plan Issues

There are six issues before the Subcommittee regarding large business subcontracting plans. The first concerns the negotiation of goals. When subcontracting goals are negotiated, PCRs and CMRs are allowed to review the goals, but only in an advisory capacity. In a recent report on the PCR program,⁵⁰ GAO found PCRs identified the inability to appeal subcontracting goals as one of the primary challenges faced by the program. Additionally, through its own investigations, the Committee has found that PCRs are told that a prime contract will contain a certain level of

⁴⁷ Pub. L. No. 109-282, 120 Stat. § 1186 (2006).

⁴⁸ This information appears to be incomplete. For example, a non-ANC 8(a) firm that received over \$120 million in prime contracts in FY 2010 does not list any subcontracts.

⁴⁹ 15 U.S.C. § 637(d)(8)(k).

⁵⁰ GAO, IMPROVEMENTS NEEDED TO HELP ENSURE RELIABILITY OF SBA'S PERFORMANCE DATA ON PROCUREMENT CENTER REPRESENTATIVES (2011).

subcontracting goals in order to convince the PCR to sign off on the procurement strategy. However, the resulting contract has much lower goals than those promised to the PCR. Consequently, the Subcommittee will consider whether the PCR or CMR must be allowed to delay a procurement to see that the appropriate goals are assigned to a contract.

Second, there is the issue of noncompliance with the reporting requirements. If a firm does not file its subcontracting reports in ESRS, it is not complying with its contract, and it is a good indicator that the firm is not tracking subcontracts with small businesses. While each is a breach of the contract, it is nearly impossible to prove damages because the harm to the government is difficult to prove. The Subcommittee will consider whether compliance with these requirements could be improved if a penalty was imposed for failure to comply, or if ESRS notified the contracting officer, SBA, or the OSDBU if a company is failing to comply.

Third, the SBA's standard operating procedures for the subcontracting plan assumes that SBA will audit a prime contractor's compliance.⁵¹ However, as previously discussed, CMRs are unable to review the vast majority of subcontracting plans. The Defense Contract Audit Agency (DCAA) currently conducts routine audits of DoD contractors with cost accounting systems. These systems require that a contractor have an auditable subcontracting process. As DCAA is already reviewing subcontracting processes, SBA should consider entering into a cooperative agreement with DCAA to review for compliance with subcontracting plans.

Fourth, prime contractors are responsible for ensuring that their large subcontractors in turn subcontract with small businesses. ESRS accounts for these subcontracts, and credits the government with the dollars when calculating the government-wide subcontracting achievements. However, the prime contractor is not allowed to take credit for lower tier subcontracting. In some cases, this exclusion is warranted. For example, if the large business has a commercial type subcontracting plan, its subcontract report covers all subcontracting opportunities for the year rather than subcontracting opportunities related to the prime contract. In such cases, it would make it difficult to account for lower tier subcontracting without double counting dollars. In other cases, such as contract specific subcontracting plans, allowing the prime to receive credit for lower tier accomplishments would make the prime contractor more aggressive when monitoring its lower subcontractors, which could in turn result in more opportunities for small businesses. The Subcommittee will review whether such changes are desirable.

Fifth, requiring prime contractors to publish subcontracting opportunities on SUB-Net could lead to greater opportunities for small businesses, and would be consistent with the intention of the Small Business Act. However, it could harm small businesses that participated with the prime contractor on the successful bid. For example, a small firm might enter into a teaming agreement with a large firm to pursue a large government contract together, with the large business acting as the prime. Pursuant to the agreement, the small firm could spend months of its time helping to develop the successful offer, and be listed a proposed subcontractor in the bid. However, since teaming agreements are not usually enforceable, there are cases where the prime then awards the subcontract to a different business rather than to its teaming partner. In such cases, the Small Business Jobs Act requires the prime contractor to either use that subcontractor or justify to the

⁵¹ SBA, SUBCONTRACTING ASSISTANCE PROGRAM 21-31 (2003) (SOP 60 03 6).

contracting officer the decision not to use the subcontractor.⁵² If all subcontract opportunities are posted on SUB-Net, these small business team partners could be injured, so perhaps an exception to this policy is necessary for team members. The Subcommittee will consider how best to use SUB-Net to ensure that small businesses are given opportunities as subcontractors.

Finally, the Subcommittee will consider whether a statutory subcontracting goal is needed. As previously discussed, the subcontracting goals negotiated by the SBA have been declining over the past decade. In FY 2006, the subcontracting goal was 40 percent.⁵³ It is now only 35.9 percent, and actual achievements are only 35.4 percent. This means that the subcontracting goals are lower than subcontracting achievements were in 1978, when the current subcontracting program was implemented.⁵⁴

ii. System Issues

As discussed in the prior two subsections, the systems issues regarding ESRS, FSRS and SUB-Net can be distilled to two simple concepts: use and relevancy. In each case, there are issues of businesses not reporting the required information to the systems, and there are no penalties for these failures. Likewise, in each case, the Contracting Officers are not using the systems to track compliance. To make these systems relevant, the Subcommittee will consider requiring that ESRS and FSRS actively notify contracting officers, OSDBUs and SBA of problems, rather than passively collecting data. Additionally, as the Executive branch is in the process of merging ESRS and FSRS, the Subcommittee will consider issues arising from that merger.

iii. Personnel Issues

The aforementioned CMRs serve an important role, give that over \$210 billion of federal prime contract dollars is spent with subcontractors each year. However, they are an afterthought in the Act, mentioned only when describing the education requirements for the position. Therefore the Subcommittee is interested in examining whether additional clarity around the role of the CMR would improve ability of these individuals to deliver results for small businesses.

iv. Past Performance

When awarding prime contracts, contracting officers review the past performance of offerors to ensure that successful contractor is a responsible party.⁵⁵ In more complex procurements, “*past performance* considerations may play a dominant role in source selection.”⁵⁶ This poses two challenges.

First, even though the Act directs that failure of a large business to make a good faith effort to meet its subcontracting goals “shall be a material breach of such contract or subcontract and may be considered in any past performance evaluation of the contractor.”⁵⁷ However, since companies

⁵² 15 U.S.C. § 637 note.

⁵³ SBA goaling website, http://archive.sba.gov/aboutsba/sbaprograms/goals/SBGR_2006_SCGR.html.

⁵⁴ 1978 Report at 5.

⁵⁵ F.A.R. part 9.104-1.

⁵⁶ *Id.* at 15.101

⁵⁷ The Act at § 8(d)(4)(G).

are never found in breach of this provision, this factor has little to no importance. Therefore, the Subcommittee wishes to consider whether a prime contractor's results on its subcontracting goals should always be considered part of its past performance.

Second, this requirement for past performance makes it very difficult for small businesses only performing as subcontractors to make the transition to prime contracting. The Subcommittee will ask what changes could be made to assess the past performance of small subcontractors.

IV. Conclusion

As small businesses struggle to compete for federal contracts and subcontracts, this Subcommittee will consider whether legislative changes could better protect and promote these businesses. In doing so, the Subcommittee seeks greater competition, innovation, and job creation.