

STATEMENT OF ANGELA B. STYLES
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SUBCOMMITTEE ON CONTRACTING AND WORKFORCE
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CHAIRMAN HANNA, CONGRESSWOMAN MENG, AND MEMBERS OF THE SUBCOMMITTEE, I appreciate the opportunity to appear before you today to discuss the impact of the Small Business Administration's failure to implement federal contracting reforms mandated in the National Defense Authorization Act for FY 2013 ("NDAA"). SBA's failure to act has created significant ambiguity for federal contractors—both small and large. While this uncertainty keeps the lawyers busy, it costs government contractors—and ultimately results in higher prices for the federal government and taxpayers. As the chair of Crowell & Moring's government contracts group, the Coordinator of the Defense Industry Initiative on Business Ethics and Conduct and the former Administrator of the Office of Federal Procurement Policy at the Office of Management and Budget, I work with government contractors effected by SBA's inaction -- every day. What we have started to see is a dramatic increase in compliance questions related these unimplemented provisions. Businesses are concerned and confused by SBA's failure to implement a number of NDAA provisions. This legal uncertainty, and the resulting increased compliance costs, need not exist.

Subcontracting Limits

In a much needed reform, the NDAA modified the Small Business Act to add a new provision relating to limitations on subcontracting for federal prime contracts awarded to small businesses under "set-aside" programs. So, for example, when a federal procurement is "set-aside" for competition among small businesses, the winning small business prime contractor is restricted from subcontracting more than a certain percentage of the amount paid by the federal government to a large business. For service contracts awarded as a "set-aside", the new statute provides that the small business prime contractor "may not *expend on subcontractors* more than 50 percent of the amount paid to" the small business prime contractor by the federal government.¹ The new NDAA statutory provision is a meaningful change in two ways. First, the limitation on subcontracting regulations for many years (and still existing in the current unmodified form) require small business prime contractors awarded a prime contract on a set-aside basis to agree that "[a]t least 50 percent of the cost of contract performance incurred for personnel shall be expended for employees of" the small business prime contractor.²

¹ 15 U.S.C. § 657(s)(a)(1) (2014).

² 48 CFR 52.219-14(c)(1) (emphasis added).

In practice, what constitutes the “cost of contract performance” for personnel has been impossible to understand or implement. So for example, if a small business prime contractor was awarded a \$100,000 contract to maintain trucks at a military base and the small business prime contractor wants to subcontract engine maintenance to a large business, the small business prime contractor would have to convert the firm fixed price into a “cost of performance” metric and compare their cost of performance for personnel to the cost of performance of the large business subcontractor. No one (the businesses or the government) really knows if they are administering the limitations on subcontracting correctly and this uncertainty has led to many disputes with the government and between prime and subcontractors. Fortunately, the NDAA changed this vague requirement into a simple calculation. In our example, the small business prime contract awarded a set aside contract could subcontract \$50,000 of the award to a large business – simple and easy to administer.

The problem, however, is the SBA’s failure to implement new regulations consistent with the new NDAA limitations on subcontracting statutory provision. A new contract (executed by a federal agency today) would contain the old regulation (FAR 52.219-14) which requires the contractor by contract term to ensure that “[a]t least 50 percent of the cost of contract performance incurred for personnel [is] expended for employees of” the small business prime contractor. The contract clause, however, does not exempt the small business prime contractor from also complying with the new NDAA statutory provision on limitations on subcontracting. Compliant and diligent small business are left in the position of implementing two inconsistent provisions, a statute that allows them to subcontract 50% of the amount they are paid and a contract clause which requires them to perform 50% of the cost of performance with their own employees.³ This inconsistency is adding millions of dollars to compliance costs for small businesses.

Second, the new statute allows a small business prime contractor winning a set-aside contract to subcontract any amount of work to similarly situated small business. Under the existing regulation, with minor exceptions, the limitation on subcontracting applies to subcontracts with both large and small businesses. So a small business prime contractor winning a “set-aside” award has significant limitations on the amount of work that could be subcontracted to another small business – treating subcontracts with large business the same as subcontracts with small businesses. The regulation also prevents joint ventures among small businesses where for example 45 percent of work would be completed by one small business in a joint venture, 45 percent by another small business in that joint venture, and only 10 percent subcontracted to outside business entities. The NDAA clarified this restriction with a simple rule that would allow the prime small business subcontractor to subcontract any dollar amount to a similarly situated small business.

SBA needs to immediately begin this rulemaking process to resolve the uncertainty and improve the business climate. First, the SBA needs to change its regulations to reflect the laws Congress explicitly changed.⁴ That action will spur the Federal Acquisition Regulation Council

³ In accordance with 41 U.S.C. 429 - 431, commercial item contracts and contracts below the simplified acquisition threshold are likely not subject to the new NDAA statutory provision until a determination is made by the Federal Acquisition Regulatory Council as to their applicability.

⁴ 13 C.F.R. 125.6(a).

to change the FAR's limitation on subcontracting clause.⁵ Neither of these entities has taken action, and that failure is increasing the cost of doing business with the government.

Other Unimplemented Reforms

Small Business Opportunities Website

Finding federal contracting opportunities can be an intimidating proposition. Even large contractors with hundreds of federal contracts under their belt have questions about the intricacies of the process. For small businesses, especially those that have never competed for these contracts, finding federal opportunities can be doubly hard. Faced with that complexity, many small businesses are deterred from the process altogether.

To help allay those fears, Congress mandated that SBA establish a website to allow large businesses to post subcontracting opportunities for small businesses.⁶ SBA has not yet implemented that requirement, and thus, it has denied small businesses from having a user-friendly means to access and compete for federal subcontracts. Not only should SBA implement such a website, but it should also expand the website's reach by allowing existing small business prime contractors to access the forum to post their own subcontracting opportunities. SBA has still not completed this relatively simple act, and is depriving small businesses of the access to contracting opportunities that Congress hoped to give them.

Mentor-Protégé Program

In another attempt to encourage inexperienced small businesses to compete for federal contracts, Congress established a mentor-protégé program—pairing small businesses with larger, more experienced federal contractors.⁷ Congress tasked SBA with outlining the requirements for the program, including which contractors would be eligible for the program and the types of assistance mentors could provide their protégés.⁸ If properly implemented, this program could significantly expand the number of small businesses actively competing for government contracts. However, without SBA implementation, the program will never materialize. Congress gave SBA 270 days to issue regulations governing this program;⁹ today, 562 days later, SBA has still not done so.

Safe Harbor for Good Faith Efforts to Comply with Size Regulations

Prior to the NDAA, well-meaning small businesses that misinterpreted the complex small business size regulations could be convicted of fraud, subjecting them to fines of up to \$500,000 and 10 years of imprisonment for misrepresenting their status as a “small business concern.”¹⁰ Recognizing that this rule might inadvertently punish successful and honest small businesses trying to comply with size restrictions, Congress mandated that SBA to create a “safe harbor”

⁵ 48 C.F.R. 52.219-14.

⁶ 15 U.S.C. 637(k)(1) (2014).

⁷ 15 U.S.C. § 657(r)(a)(1) (2014).

⁸ 15 U.S.C. § 657(r)(b)(3)(A-J) (2014).

⁹ 15 U.S.C. § 657(r)(b)(3) (2014).

¹⁰ 15 U.S.C. § 645(d) (2014).

process for small businesses to obtain a written advisory from a Small Business Development Center or Procurement Technical Assistance Center for good faith attempts to comply with these size regulations.¹¹ Congress gave SBA 270 days to issue rules defining the contours of this provision;¹² today, 562 days later, SBA has only found the wherewithal to issue a proposed rule for public comment. It is difficult to fathom why SBA, taking the effort to draft and issue proposed rule for comment, did not simply issue the rule as an immediately effective interim rule. By issuing a proposed rule, the harshness of potential penalties remains for an unlimited period of time.

Other Reforms

Recognizing the complexity of the federal contracting process, Congress mandated that SBA create a compliance guide for small businesses attempting to determine their size status. This guide would “assist business concerns in accurately determining their status as a small business concern” to prevent inadvertent fraudulent misrepresentations.¹³ A relatively straightforward task, Congress gave SBA 270 days to conduct this revision;¹⁴ today, 562 days later, SBA has not taken any action.

Congress mandated that SBA issue clear guidance listing the Administration’s standard operating procedures for suspension and debarment, as well as publicizing the name of the “senior individual responsible for suspension and debarment proceedings.”¹⁵ Congress gave SBA 270 days to take these simple actions;¹⁶ today, 562 days later, SBA has not issued any guidance. SBA, however, continues to actively suspend and debarment companies and individuals without standard operating procedures.

Conclusion

If SBA continues to withhold these regulations, federal contractors may have legal standing to sue the SBA over its failure to act. The Administrative Procedure Act, which governs agency rulemaking procedures, allows a court to compel an agency to act if the agency has “unlawfully withheld” or “unreasonably delayed”¹⁷ some “*discrete* agency action [the agency] is *required to take*.”¹⁸ Such failure to act, the Supreme Court has made clear, includes “the omission of an action without formally rejecting a request—for example, the failure to promulgate a rule or make some decision by a statutory deadline.”¹⁹ SBA has failed to promulgate the rules that Congress mandated that it promulgate. SBA was under a clear legal obligation to issue several sets of regulations within 270 days; its inaction for nearly twice that

¹¹ National Defense Authorization Act for FY 2013, Pub. L. No. 112-239, § 1681(a) (2012).

¹² *Id.*, at § 1681(b).

¹³ *Id.*, at § 1681(c).

¹⁴ *Id.*

¹⁵ *Id.*, at § 1682(c).

¹⁶ *Id.*

¹⁷ Administrative Procedure Act § 706(1); *see also* Administrative Procedure Act § 551(13) (stating that agency action, under the APA, is defined to include “the *whole or a part of an agency rule, order, license, sanction, relief, or the equivalent or denial thereof, or failure to act*”) (emphasis added).

¹⁸ *See Norton v. S. Utah Wilderness Alliance*, 542 U.S. 55, 64 (2004) (emphasis in original).

¹⁹ *Id.*, at 63.

amount of time constitutes both an unlawful withholding and an unreasonable delay. But what small business has the money to launch such legal action?

The Small Business Administration’s mission is to “aid, counsel, assist and protect the interests of small business concerns.”²⁰ SBA’s failure to act is crippling the very small businesses it is supposed to protect and assist. Congress enacted common-sense reforms in the NDAA—reforms that (1) clarify the complex limitations on subcontracting, (2) allow small businesses to team to more effectively, (3) eliminate regulatory compliance burdens, and (4) provide opportunities for new small businesses to get into the government contracting business. SBA’s failure to act has denied these benefits to federal contractors large and small, resulting in inefficiencies and lost opportunities for economic growth.

This concludes my prepared remarks. I am happy to answer any questions you may have.

²⁰ U.S. Small Business Administration, Mission (June 10, 2014), http://www.sba.gov/about-sba/what_we_do/mission.