

Small Business Status ... Don't Cross The Line!



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Outline

I. The “Line” Is Not Easily Discerned

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A. Audits

B. Protests

C. Qui Tam Law Suits

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FAR § 52.219-1

Small Business Program Representations (Apr 2011)

(a)(1) The North American Industry
Classification System (NAICS) code for this
acquisition is _____

[insert NAICS code].

(a)(2) The small business size standard is
_____ *[insert size standard].*

FAR § 52.219-1

Small Business Program Representations (Apr 2011)

(b) *Representations.*

(1) The offeror represents as part of its offer that it ☐ is, ☐ is not a small business concern.

The Line Not Easily Discerned

Different Rules

- Subcontracting
- Joint Ventures
- Mentoring

The Line Not Easily Discerned

FAR § 9.601

“Contractor team arrangement,” means an arrangement in which --

- (1) Two or more companies form a partnership or **joint venture** to act as a potential prime contractor; or
- (2) A potential **prime contractor** agrees with one or more other companies to have them act as its **subcontractors**”

The Line Not Easily Discerned

“Line” if Subcontracting

- SB must be prime
- FAR § 52.219-14 Limitations on Subcontracting

The Line Not Easily Discerned

“Line” if JV

Small Business	FAR 19.101 (7)
HUBZone	FAR 19.101; FAR 19.1303(c); CFR 126.616
SDVOSB	FAR 19.1403; 13 CFR 125.15(b)
8(a)	13 CFR 124.513

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“Line” if JV – General Rule

If unbundled requirements and revenue-based size standard applies:

Does the estimated contract value, including options, exceeds one-half of the applicable size standard?

No. Look to combined revenue

Yes. Look to revenue of largest JV member

The Line Not Easily Discerned

“Line” if JV – General Rule

If unbundled requirements and employee based size standard applies:

Does the estimated contract value, including options, exceeds \$10 million?

No. Look to combined number of employees

Yes. Look to the number of employees of largest JV member

The Line Not Easily Discerned

“Line” if JV

<i>Status</i>	<i>Allowable JV Team Members</i>
Small Business	Other Small Businesses
HUBZone	Only other HUBZone vendors
SDVOSB	Other Small Businesses
8(a)	Other Small Businesses

The Line Not Easily Discerned

“Line” if Mentoring

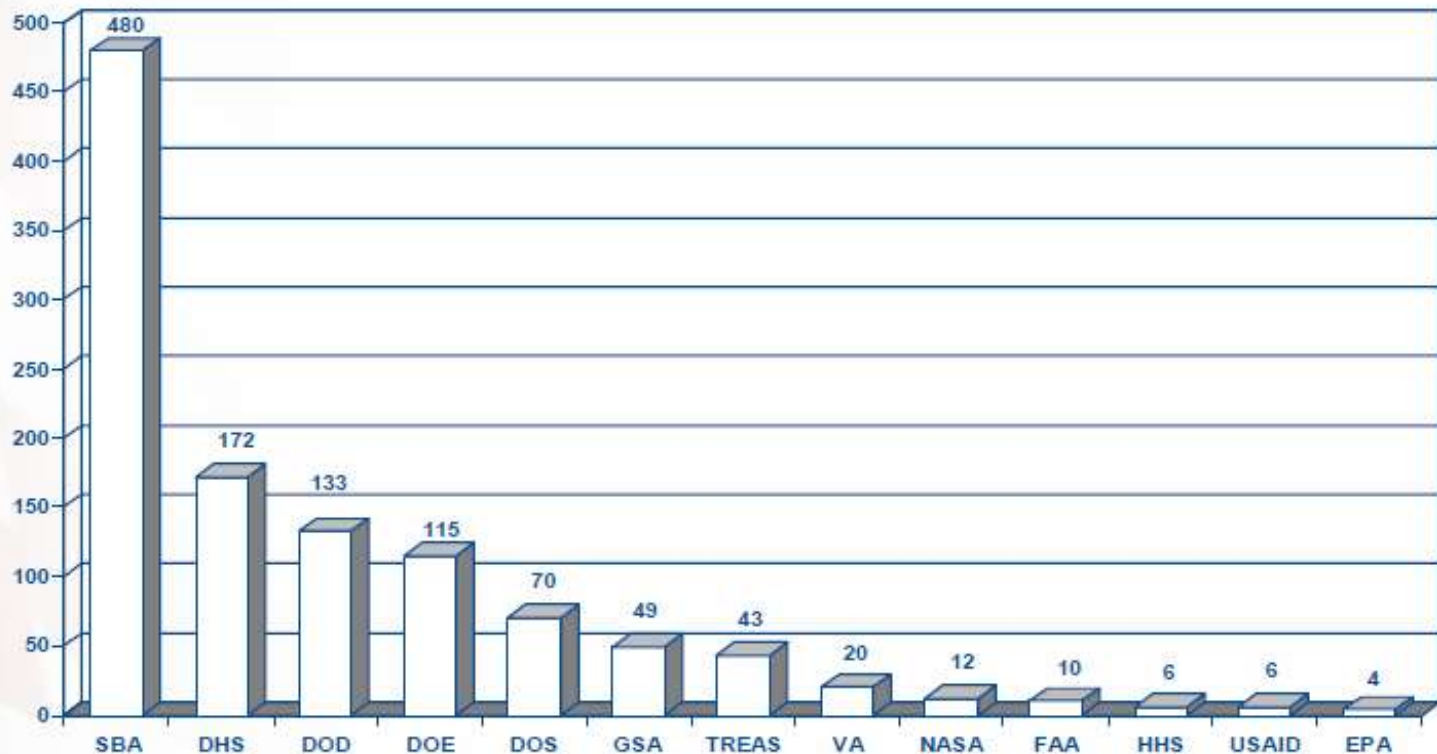
- Protégé must perform 40%
- Protégé must manage venture
- Mentor-Protégé team can only be awarded 3 contracts in 2 years

The Line Not Easily Discerned

“Line” if Mentoring
SBA can waive the affiliation
rule for joint ventures
between mentors and 8(a)
protégés

The Line Not Easily Discerned

Number of Mentor Protégé Agreements Across the Federal Government, as of December 2010



The Line Not Easily Discerned

Agency	Business Size (Large/Small)	Eligible for Federal Contracts	Ability to Help Protégé	Current Prime or Sub Contractor	Multiple Protégés Allowed
DHS	L	✓	✓		✓
DOD	L/S	✓	✓	Prime	✓
DOE	L/S	✓	✓	Prime	✓
DOS	L/S	✓	✓		✓
FAA	L/S	✓	✓		✓
EPA	L/S	✓	✓	Prime	✓
GSA	L/S	✓	✓	Prime	✓
HHS	L	✓	✓	Prime	✓
NASA	L	✓	✓	Prime	✓
SBA	L/S	✓	✓		✓ (with limitations)

The Line Not Easily Discerned

Gotcha's

1. The “affiliation” rule
2. The “ostensible subcontractor” rule
3. The “new organization” rule



THE RULES

They may be stupid, arbitrary and irritating, but god help you if you break them.

I. How Does The Gov't Find Out?



Audits

Indicative GAO Audit Report #1

“We identified 10 case-study examples of firms that did not meet SDVOSB program eligibility requirements, which received approximately \$100 million in SDVOSB contracts, and over \$300 million in additional 8(a), HUBZone, and non-SDVOSB government contracts.”

GAO-10-255T

Indicative GAO Audit Report #2

“We identified 19 firms ... that clearly do not meet program requirements. In 2006 and 2007, federal agencies obligated nearly \$30 million to these 19 firms for performance as the prime contractor on HUBZone contracts.”

GAO-09-519T

Indicative GAO Audit Report #2

“An information technology firm in Huntsville, AL failed to meet both principal office and 35 percent residency requirements. From FY year 2006 through FY year 2007, federal agencies obligated over \$5 million in HUBZone awards to this firm.”

GAO-09-519T

Indicative GAO Audit Report #3

“We identified 14 firms that received set-aside or sole-source 8(a) contracts worth \$325 million through fraud or abuse. These 14 firms received another \$1.2 billion in other federal obligations since entering the 8(a) program....”

GAO-11-440T

I. How Does The Gov't Find Out?



Protests

Basis For Most Protests

Service: “At least 50% of the cost of contract performance incurred for personnel shall be expended for employees of the concern.”

Supplies: (*other than procurement from a nonmanufacturer of such supplies*) “The concern shall perform work for at least 50% of the cost of manufacturing the supplies, not including the cost of materials.”

FAR § 52.219-14

Basis For Most Protests

Tybrin Corp., B-298364, March 13, 2007

SB set aside where the awardee's proposal demonstrated that only 44% of the cost of contract performance incurred for personnel would be for the awardee's own personnel. Air Force thought it permissible to count first tier small business subcontractors (which totaled 66% percent).

Protest Basis: The Affiliation Rule

- ❑ “Concerns are affiliates of each other when one concern controls or has the power to control the other, or a third party controls or has the power to control both”.
- ❑ SBA considers factors such as ownership, management, previous ties to another concern, and contractual relationships, in determining whether affiliation exists.

Protest Basis: The Affiliation Rule

- ❑ SBA considers “individuals or firms that have identical or substantially identical business or economic interests, such as family members, persons with common investments, or firms that are economically dependent through contractual or other relationships, may be treated as one party with such interests aggregated.”

13 CFR §121.103



"I'm disappointed; if anyone should have seen the red flags, it's you."

Protest Basis: The Affiliation Rule

“SBA counts the receipts or employees of the concern whose size is at issue and those of all its domestic and foreign affiliates, regardless of whether the affiliates are organized for profit, in determining the concern's size.”

13 CFR § 121.103(a)(4)

Protest Basis: The Affiliation Rule

“Concerns bidding on a particular procurement as joint venturers are affiliated with each other with regard to performance of that contract.”

13 CFR § 121.103(f)

Affiliation Rule

Best Harvest Bakeries, SBA (2003)

- ❑ Best Harvest was previously owned by Fresh Start Bakeries, a LB
- ❑ Fresh Start owned 25% of Best Harvest.
- ❑ Best Harvest and Fresh Start were in the same line of work, and both were major bun suppliers to single customer

Affiliation Rule

Best Harvest Bakeries (continued)

- ❑ Fresh Start provided Best Harvest with many services
- ❑ Fresh Start must agree to any changes in Best Harvest's pricing protocols.
- ❑ Fresh Start could require Best Harvest to buy its interest out if certain decisions are not made unanimously

Affiliation Rule

TPG Consulting, SBA (2011)

NASA procurement to maintain web sites. NASA challenged apparent winner, eTouch, status as SB. SBA sustained challenge. Award to TPC. eTouch challenges TPC's SB status. Challenged sustained because TPG received more than 70% of its revenue from Toyota. SBA held: "It does not matter whether control is exercised, so long as the power to control exists."

Protest Basis: Ostensible Subcontractor

A contractor and subcontractor are treated as joint venturers if the ostensible subcontractor will perform primary and vital requirements of a contract or if the prime contractor is unusually reliant upon the ostensible subcontractor.

13 CFR § 121.103(f)

Ostensible Subcontractor

Seven Part Test

1. Who will manage the contract?
2. Which party possesses the requisite background and expertise to carry out the contract?
3. Which party chased the contract?
4. What degree of collaboration was there on the bid or proposal?

Ostensible Subcontractor

Seven Part Test

5. Are there discrete tasks to be performed by each or is there a co-mingling of personnel and material?
6. What is the relative amount of work to be performed by each?
7. Which party performs the more costly and complex functions?



Ostensible Subcontractor

General Maintenance Engineering
SBA No. 4405, June 27, 2000

Violation of *Ostensible Subcontractor Rule* where:

1. The subcontractor had previously been the prime contract
2. The subcontractor was not eligible to submit a proposal
3. The prime will extensively use the subcontractor's key personnel
4. Sub's participation enhances the competitive status of the proposal

Protest Basis:

Newly Organized Concern

“Affiliation may arise where former officers, directors ... or key employees of one concern organize a new concern in the same or related industry ... and serve as the new concern’s officers, directors ... or key employees, and the one concern is furnishing or will furnish the new concern with contracts, financial or technical assistance”

13 CFR § 121.103(g)

Newly Organized Concern

Sabre88, SBA Oct. 19, 2010

“The purpose of the rule is to prevent circumvention of the size standards by the creation of “spin-off” firms that appear to be small, independent firms but are, in fact, affiliates or extensions of large firms.”

Newly Organized Concern

Sabre88, SBA Oct. 19, 2010

- ❑ Owner was very involved with old company
- ❑ Same core businesses
- ❑ Old company was either directly or indirectly involved with 100% of new company's revenue
- ❑ Both companies 8(a)s

Protest Procedure

1. If RFP, interested party must protest to C.O. within 5 business days of learning of award
2. Within 3 business days of receipt of protest, awardee must submit a completed SBA form 355 to C.O.

Protest Procedure

3. Within 10 business days of receipt of form 355, regional SBA office must determine size status of awardee
4. If protest made before award, C.O. cannot award until SBA makes size determination (unless award necessary to protect public interest)

I. How Does The Gov't Find Out?



Qui Tam Law Suits

Qui Tam Law Suit

U.S. ex rel. Longhi v. Lithium Power Techs.
(5th Cir. July 9, 2009)

Laid off employee bring action stating fraudulent statements in the SBIR proposals:

- ❑ same work on BMDO & AF SBIRs
- ❑ misrepresented facilities
- ❑ misrepresented “cooperative arrangements” with existing laboratories
- ❑ claimed corporation had more experience

Held: numerous False Claims Act violations

II. Possible Consequences

Loss Of Contract

Tybrin Corp., B-298364, March 13, 2007

Facts: the awardee's proposal demonstrated that only 44% of the cost of contract performance incurred for personnel

Consequences: Awardee lost the contract.

Loss Of Contract

Tiger Enterprises, Inc., GAO, Jan 20, 2004

“Where the awardee was found by the SBA to be other than small based on a timely size protest filed after award on a small business set-aside, and this determination was not appealed, the agency, in the absence of legitimate countervailing reasons, should have terminated the contract and obtained these services from a small business.”

15 U.S.C. § 645

“Whoever misrepresents the status of any concern as a small business concern ... in order to obtain -

- (A) A prime contract *[set aside for a SB]*
- (B) A subcontract *[designated for a SB]*
- (C) subcontract that is to be included as part of a goal in a subcontracting plan shall be subject to...

15 U.S.C. § 645

- (1) a fine of not more than \$500,000
- (2) imprisonment for not more than 10 years
- (3) subject to suspension and debarment as specified in FAR Subpart 9.4.

False Claims Consequences

U.S. ex rel. Longhi v. Lithium Power Techs.
(5th Cir. July 9, 2009)

The court computed the damages for the False Claims Act violations as triple the amount of the contracts plus \$43,000. The total amount paid under the SBIR contracts was \$1,657,455. The total amount of damages was \$5,015,365.

False Claims Consequences

Small Business Jobs Act of 2010

“In every contract... which is set aside... for award to small business concerns, there shall be a presumption of loss to the United States based on the total amount expended on the contract.”

[Limited to willful misrepresentations]

15 USC 632(w)

Another Consequence

Too late to protest? A displaced offeror might consider:

- (1) suing under state law to have a constructive trust placed on the profits from the fraudulently awarded contract, and
- (2) being named the beneficiary of the trust.

Service Engineering v. Southwest Marine,
719 F.Supp. 1500 (1989)

IGNORANCE OF THE LAW
IS NO EXCUSE, DUMMY!

