



Federal Subcontracting

How Subcontractors Can Get a Piece of the Pie

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About PilieroMazza

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Overview

- Overview of federal subcontracting
- How small business (“SB”) subcontractors help prime contractors meet their subcontracting requirements
- Using mentor-protégé and joint venture relationships to meet subcontracting requirements
- Rules to protect SB subcontractors at the subcontract level
- Recent statutory and regulatory developments

Federal Subcontracting Opportunities

- The federal government spends approximately \$400 billion each year on contracts, and approximately \$90-\$100 billion goes to subcontracts
- SBA works with agencies to establish SB subcontracting goals
- Baseline federal SB goals:
 - WOSB: 5%
 - SDB: 5%
 - SDVOSB: 3%
 - HUBZone: 3%

Subcontracting Goal Performance in FY16

- 32.2% of all federal subcontracting dollars went to small businesses (SBs)
- 5.5% went to small disadvantaged businesses (SDBs)
- 5.7% went to women-owned small businesses (WOSBs)
- 1.6% went to service-disabled veteran-owned small businesses (SDVOSBs)
- 1.1% went to historically underutilized business zones (HUBZone) small businesses
 - Note: other than SB, all of these percentages declined from FY15

Subcontracting Goal Performance in FY16

- All agencies except HHS, VA, USDA, and USAID spent at least 30% of their subcontracting dollars on SBs
- SDB and WOSB goals generally met by all agencies; fewer than half of the agencies met their SDVOSB subcontracting goals
- Energy, Labor, NRC, and OPM met all of their subcontracting goals
- Only Energy, Labor, NRC, and OPM met their HUBZone subcontracting goals
- Commerce, ED, HUD, DOI, and EPA met all of their subcontracting goals except HUBZone
- USDA did not meet any of its subcontracting goals except SB; VA did not meet any subcontracting goals

Why Government Has Subcontracting Spending Goals

- Congress has determined that utilization of SBs at the subcontract level is key to the government's objective of maximizing SB participation in federal procurements
- SBA works with agencies each year to establish and monitor prime and subcontracting SB spending goals
- To ensure the goals are met, SB subcontracting requirements are found in several parts of the FAR and CFR:
 - FAR Subpart 19.7
 - FAR 52.219-8, Utilization of Small Business Concerns
 - FAR 52.219-9, Small Business Subcontracting Plan
 - Also found in SBA's rules at 13 C.F.R. § 125.3

Two Key Subcontracting Requirements

- Provide maximum practicable opportunities for SBs
 - Requirement of most prime contracts
 - Must be flowed down to subcontracts that offer lower-tier subcontracting opportunities
- Implement a subcontracting plan
 - Applies to prime contracts that offer subcontracting possibilities and are greater than \$700,000 (or \$1.5 million for construction)
 - Only applies to large businesses; not applicable to SBs or set-aside prime contracts
 - Must be flowed down to subcontracts meeting the same dollar thresholds, except subcontracts to SBs and subcontracts for commercial items

What Is a Subcontracting Plan?

- Written document establishing the contractor's spending goals for SB subcontractors
- A subcontracting plan includes:
 - The contractor's subcontracting spending goals based on total planned subcontracting dollars
 - Separate goals for each type of SB
 - Methods used to develop goals and identify potential SB subs
 - How the contractor will make a good faith effort to comply with its plan

Importance of Compliance with Subcontracting Plan

- Increased focus on subcontracting compliance on Capitol Hill
- SBA audits are up, and trend is expected to continue
- Stakes are higher for noncompliance
 - Breach of contract
 - Adverse past performance rating
 - Poor evaluation for new proposals
 - Liquidated damages

Compliance Impacts in Bid Protests

- Graybar, B-410886 (Mar. 4, 2015): protester was properly excluded from competitive range based in part on its consistent failure to meet its SB subcontracting goals on previous contracts
- Kellogg Brown & Root Services, Inc., B-298694.7 (June 22, 2007): protester's score lower than awardee's due in part to less SB utilization in prior contracts
- Coastal Maritime Stevedoring, LLC, B-296627 (Sept. 22, 2005): agency improperly rated offeror's incomplete plan as satisfactory
- SEEMA, Inc., B-277988 (Dec. 16, 1997): awardee's aggressive subcontracting goals were one of the decisive factors in award

SBA's Role in Monitoring Compliance

- SBA area offices review subcontracting plan compliance
- SBA will conduct onsite visit and review data and documents
- SBA is looking at goal performance as well as good faith efforts to comply with the plan through assessments of:
 - Methodology used in developing and reporting goals and performance
 - Recordkeeping, in particular whether prime has written representations from its SB vendors that are tied to and timely for its subcontracts
 - How prime flows down requirements to and monitors subcontractors
 - Overall commitment to the program, including management support

SB Subcontractors Can Help Prime Contractors Fill Multiple Buckets

- Prime contractors can take credit for subcontracting to all diversity categories applicable to a subcontractor
 - Example 1: If a prime subcontracts \$500,000 to a WOSB, the prime can take credit for subcontracting \$500,000 to a WOSB and \$500,000 to a SB
 - Example 2: If a prime subcontracts \$500,000 to a WOSB that is also an SDVOSB, the prime can take credit for \$500,000 to a WOSB, \$500,000 to an SDVOSB, and \$500,000 to a SB
- Therefore, if you can help primes check multiple boxes, this is a strong selling point in addition to your capabilities

Finding Subcontracting Opportunities

- Check SBA's SUB-Net for Notices of Sources Sought or Requests for Proposal posted by primes
- Keep your SAM and DSBS profiles up to date
- Participate in business matchmaking events
- Attend pre-bid conferences, industry days for key contracts, and events held by each agency's OSDDBU or comparable office
- Have a solid capabilities statement available to provide to primes
- Contact SBA CMRs to find primes looking for SB subcontractors
- Research prime contract holders of large contracting vehicles and reach out to them directly

Assigning the Best NAICS Code to a Subcontract

- The prime contractor has discretion to assign each subcontract the NAICS code and corresponding size standard that best describes the principal purpose of the subcontract
 - According to SBA rules, the NAICS code that best describes the principal purpose of the subcontract is based on the industry descriptions in the NAICS Manual, the subcontract statement of work, and the relative weight of each task to be performed
- Opportunity for advocacy
 - Often times, there are multiple NAICS codes that could potentially fit a subcontract
 - Since the prime contractor has flexibility in selecting the NAICS code, subcontractors can advocate for a NAICS code that allows the prime to take SB credit for your subcontract

Reps and Certs for Subcontracts

- Subcontractor must represent its size/status in writing to the prime contractor, either relying on SAM.gov or a representation in the subcontract
- Subcontractor must make the representation at the time of submitting its proposal for the subcontract
- **Important:** SBA's "presumed loss rule" applies to representations made for subcontracts
 - Rule establishes significant penalties, up to the entire value of the subcontract, for willful and intentional misrepresentation of size or status

Size Protests at the Subcontract Level

- Size protests are common at the prime contract level, but did you know they can also be filed at the subcontract level?
- Size protests may be filed against a subcontractor by:
 - Prime contractor
 - SBA
 - Other potential subcontractors or interested parties
- A size protest must be filed within 5 business days of bid opening or notification of the successful subcontract offeror

Competition for Subcontracts

- Prime contractors must select subcontractors on a competitive basis to the maximum practical extent consistent with the objectives and requirements of the contract when:
 - The contract is a negotiated procurement
 - The contract amount is expected to exceed \$150,000
 - The contract is not expected to be a firm-fixed-price, time-and-materials, labor-hour, or architect-engineer contract
- This may help you in advocating to a prime when there should be a competition, or in helping the prime to confirm competition is not necessary

Obtain Necessary Subcontract Approval

- The prime contractor has to obtain the CO's written consent before entering into a subcontract if:
 - The prime contract is a fixed-price contract and the subcontract is under an unpriced contract action and the prime contractor does not have an approved purchasing system
 - The contract is a cost-reimbursement, time-and-materials, or labor-hour contract and the prime contractor does not have an approved purchasing system
 - Subcontracts under 8(a) sole source contracts
- Build language into your teaming and subcontract agreements that commits the prime contractor to undertake its best efforts to secure approval of the subcontract, if necessary

Increased Subcontracting Opportunities on Set-Aside Contracts

- Under a new SBA rule, work performed by “similarly situated subcontractors” counts towards the prime contractor’s performance requirement on set-aside contracts
 - Example: If the SB prime contractor must perform 50% of the work, the prime could do 20% and the remaining 30% could be performed by a “similarly situated subcontractor”
- What is a “similarly situated subcontractor”?
 - A subcontractor that meets the set-aside requirement(s) assigned to the prime contract – i.e., for an SDVOSB set-aside, a similarly-situated subcontractor must be an SDVOSB
 - The subcontractor must also be small under the NAICS code that the prime contractor assigned to the subcontract

Opportunities at Lower Subcontracting Tiers

- SBs that subcontract at lower tiers can also help prime contractors satisfy subcontracting requirements
 - Prime contractors must include a lower-tier subcontracting goals in their subcontracting plans
 - Only applies to prime contractors with individual subcontracting plans
- SBA has finalized this rule, but it is not in the FAR yet

Utilizing Mentor-Protégé and Joint Ventures as a Subcontractor

- An SB JV can be used at the subcontract level to help large primes satisfy their subcontracting goals
 - The JV will satisfy any subcontracting goal for which the lead JV partner qualifies
 - For example, if the lead partner in the JV is HUBZone and SDVOSB, large primes can take HUBZone, SDVOSB, and SB credit for subcontracts to the JV
- Adding a mentor-protégé allows a small business to JV with a large business and still satisfy the prime's subcontracting goals
 - The mentor-protégé JV will satisfy any subcontracting goal for which the protégé qualifies
 - For example, if the protégé is 8(a) and WOSB, large primes can take SDB, WOSB, and SB credit for subcontracts to the mentor-protégé JV

Steps for Using a Mentor-Protégé JV

- **Step 1:** Form mentor-protégé relationship, submit to SBA for approval (right now, it could be approved in a few weeks)
- **Step 2:** Form JV (give yourself one month)
- **Step 3:** JV submits proposal
 - If the mentor is a large business, SBA must approve mentor-protégé relationship **before** JV submits proposal

Protections for SB Subcontractors

- Many found in FAR 19.7 and 52.219-9
- The subcontracting plan between prime and government must include assurances that:
 - Prime will make a good faith effort to use SB subcontractors to the same extent as set forth in its proposal
 - Prime will submit a written explanation to the CO if it fails to use SB subcontractors to the same extent as set forth in its proposal
 - Prime will not prohibit a subcontractor from talking with the CO regarding any payment to or utilization of a subcontractor
 - Prime will pay its SB subcontractors on time and in accordance with the terms of the subcontract and will notify the CO if it makes a reduced or untimely payment to the SB subcontractor

Protections for SB Subcontractors

- For all competitive SB subcontracts over the simplified acquisition threshold, primes must inform unsuccessful SB subcontract offerors of the subcontract awardee in writing prior to awarding the SB subcontract
- Primes may rely on SB subcontractors' representations in SAM.gov, but primes cannot require use of SAM for purposes of representing size or socioeconomic status for a subcontract
- Prime's failure to comply with subcontracting plan requirements may be considered a material breach of contract, subject to damages, and is part of its past performance evaluation

Protections for SB Subcontractors

- Primes cannot identify an SB in their proposal without first notifying the SB subcontractor in writing
- Primes cannot require SB subcontractors to establish their own subcontracting plans
 - But SB subcontractors can be encouraged to provide maximum practicable opportunities to other SBs
- Prime must prepare a written report for the CO at the end of the contract if it did not meet its subcontracting goals
- Any affected party can contact SBA's Office of Inspector General concerning a prime's performance of its subcontracting obligations

Recent Subcontracting Developments

- Contracting officers may establish subcontracting goals at the order level for IDIQ contracts
 - Starting in November 2017, a prime contractor must report subcontracting data at the order level under single-award, IDIQ contracts intended for use by multiple agencies and multiple-award, IDIQ contracts in use by multiple agencies
 - But, this rule does not mandate separate subcontracting plans at the order level for IDIQ contracts
- SBA rule on limitations on subcontracting allows primes to treat similarly situated subcontractors as prime contractors (for purposes of counting subcontracted funds), but FAR provision on limitations on subcontracting not yet updated

Recent Subcontracting Developments

- 2017 National Defense Authorization Act created a pilot program to allow SBs to gain past performance ratings as subcontractors
 - The pilot program will be open to SBs without a past performance rating as a prime and performing on a covered contract as a first-tier subcontractor
 - Pilot program will last for three years once established by SBA, but NDAA did not give SBA a deadline to get it started
- 2018 National Defense Authorization Act would amend Small Business Act to define duties for Commercial Market Representative, including:
 - Counseling primes on maximizing subcontracting opportunities
 - Counseling SBs on how to promote themselves to primes
 - Conducting periodic reviews of primes under SB subcontracting program

Thank you

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