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SUBMITTED THROUGH WWW.REGULATIONS.GOV

Lois Mandell
Regulatory-Secretariat Division
U.S. General Services Administration
1800 F Street NW, 2nd Floor
Washington, DC 20405

Re: Comments Submitted in Response to RIN 9000-AN35
Federal Acquisition Regulation:
Revision of Limitations on Subcontracting

Dear Ms. Mandell:

We are writing to submit comments in response to the proposed rule issued on December 4, 2018, by the U.S. Department of Defense, General Services Administration, and National Aeronautics and Space Administration, acting through the Federal Acquisition Regulatory Council (the "FAR Council"), RIN 9000-AN35—Federal Acquisition Regulation: Revision of Limitations on Subcontracting. According to the notice of this rulemaking in the Federal Register, these comments are timely submitted prior to the February 4, 2019 deadline. See 83 Fed. Reg. 61365 (Nov. 29, 2018).

Our firm represents government contractors operating across the government contracting spectrum, and many of these companies serve as prime contractors and subcontractors on contracts fully or partially set aside for all types of small businesses. Our clients have struggled to understand and comply with the limitations on subcontracting in recent years because of the different requirements in the Federal Acquisition Regulation ("FAR") and the U.S. Small Business Administration's ("SBA") regulations, which were updated in 2016 to implement changes to the Small Business Act.

Against that backdrop, we want to commend the FAR Council for proposing changes to the FAR that will conform the FAR to the SBA regulations that have been in place since 2016. Having uniform requirements for contractors will avoid confusion and make it easier for firms to comply.

SBA has already issued a thorough body of regulations dealing with the limitations on subcontracting, and SBA has the authority under the Small Business Act to mandate the level of performance by prime contractors on small business set-aside contracts. Therefore, SBA's regulations represent the appropriate standard for the limitations on subcontracting, and we agree

with the FAR Council's efforts to conform the FAR with SBA's rules. However, as discussed in more detail below, we believe the proposed FAR clauses require further revisions to ensure they are consistent with the existing SBA regulations.

Our further comments on the proposed rule are as follows:

- **We Support the FAR Council's Revisions to FAR 52.219-4, But This Clause Requires Further Modifications to Align with SBA's Limitations on Subcontracting Rules for HUBZone Joint Ventures**

We commend the FAR Council for its proposed revisions to FAR 52.219-4, Notice of Price Evaluation Preference for Historically Underutilized Business Zone ("HUBZone") Small Business Concerns, which correspond with SBA's limitations on subcontracting regulations. 83 Fed. Reg. at 62542, 62548. The proposed revisions to FAR 52.219-4 will clarify for HUBZone concerns their contractual and regulatory obligations regarding their limitations on subcontracting.

That said, we submit that FAR 52.219-4 requires further revisions to bring the clause into alignment with SBA's limitations on subcontracting rules for HUBZone joint ventures. Proposed FAR 52.219-4(e) provides: "[a] HUBZone joint venture agrees that the aggregate of the HUBZone small business concerns to the joint venture, not each concern separately, will perform the applicable requirements specified in paragraph (d) of this clause." 83 Fed. Reg. at 62548. This is not fully consistent with SBA's limitations on subcontracting rules for HUBZone joint ventures because those rules do not simply provide that in all instances the HUBZone small business concerns in a joint venture must perform the applicable percentage of work requirements in the aggregate. See 13 C.F.R. § 126.616(d). SBA's rules also address HUBZone joint ventures in which there is only one HUBZone firm, as follows:

> For any HUBZone contract to be performed by a joint venture between a qualified HUBZone [small business concern ("SBC")] and a small business concern or its SBA-approved mentor authorized by § 125.9 or § 124.520 of this chapter, the joint venture must perform the applicable percentage of work required by § 125.6 of this chapter, and the HUBZone SBC partner to the joint venture must perform at least 40% of the work performed by the joint venture.

13 C.F.R. § 126.616(d)(2) (emphasis added).

Proposed FAR 52.219-4(e) does not account for the joint venture options afforded to HUBZone concerns under SBA's regulations. Instead, as currently drafted, it imposes a blanket requirement that "the HUBZone small business concerns to the joint venture . . . will perform the

applicable requirements specified in paragraph (d) of this clause." 83 Fed. Reg. at 62548. In other words, even if a HUBZone joint venture has a non-HUBZone joint venture partner, including an SBA-approved mentor, and is only required under SBA's rules to perform 40% of the joint venture's work, proposed FAR 52.219-4(e) would require the HUBZone concern to perform 100% of the applicable limitations on subcontracting requirement specified in proposed FAR 52.219-4(d). This requirement is appropriate where the HUBZone joint venture is made up entirely of HUBZone concerns, see 13 C.F.R. § 126.616(d)(1), but it is inconsistent with SBA's rules when a HUBZone firm forms a joint venture with another small business or its SBA-approved mentor. Thus, as written, proposed FAR 52.219-4(e) will undoubtedly result in confusion for HUBZone concerns and contracting officers alike regarding what a HUBZone joint venture under 13 C.F.R. § 126.616(d)(2) will be required to perform to comply with the applicable limitations on subcontracting.

To avoid this confusion, and to bring proposed FAR 52.219-4 into alignment with SBA's regulations, we recommend replacing paragraph (e) with the following language:

> ***(e) Limitations on Subcontracting for HUBZone Joint Ventures. A HUBZone joint venture agrees that—***
>
> ***(1) For any HUBZone contract to be performed by a joint venture between a qualified HUBZone small business concern and another qualified HUBZone small business concern, the aggregate of the qualified HUBZone small business concerns to the joint venture, not each concern separately, must perform the applicable requirements specified in paragraph (d) of this clause.***
>
> ***(2) For any HUBZone contract to be performed by a joint venture between a qualified HUBZone small business concern and a small business concern or its SBA-approved mentor authorized by 13 C.F.R. § 125.9 or 13 C.F.R. § 124.520, the joint venture must perform the applicable requirements specified in paragraph (d) of this clause, and the HUBZone small business concern partner to the joint venture must perform at least 40% of the work performed by the joint venture.***

- **We Applaud the FAR Council's Revisions to FAR 52.219-14, But This Clause Should Be Further Revised to Address the Limitations on Subcontracting for Mixed Contracts**

We support the FAR Council's revisions to FAR 52.219-14, Limitations on Subcontracting, which aim to "make it easier and less burdensome for small business prime contractors to comply with requirements related to how much work they may subcontract under

Federal contracts and task and delivery orders (i.e. the "limitations on subcontracting")." 83 Fed. Reg. at 62543. While a number of the proposed revisions accomplish this goal, the examples used to explain the revisions are difficult to follow and, moreover, reveal a lack of explanation and corresponding regulatory changes for contracts involving both supplies and services (i.e., mixed contracts).

In the Expected Cost Savings portion of the preamble, the FAR Council provided examples of how prime contractors may comply with the revised limitations on subcontracting regulations in comparison to the current regulations. 83 Fed. Reg. at 62644. These examples are confusing and potentially misleading. For instance, the main example provides for a $1,000 services contract and states that, under the new limitations on subcontracting rule, the cost of contract performance incurred for personnel is not tracked. The example then provides that the concern "may pay up to $500 to a non-similarly situated entity . . . AND/OR subcontract to a similarly situated entity without limitation." Id. Following this, the preamble then provides several examples of how a firm could comply with the new rule, each of which confusingly fails to add up to $1,000.

The bigger issue here, in our view, is that the examples reflect the failure of the revised FAR 52.219-14 to address mixed contracts. If the $1,000 example contract is a mixed contract, with $800 for labor and $200 for supplies, the example wrongly concludes that the prime contractor could not subcontract greater than $500. According to SBA regulations, in such a scenario, the prime contractor could subcontract a total of $600: $400 of the labor and the $200 for supplies. This is because the $1,000 contract is predominantly for services, meaning the limitations on subcontracting applies only to the services portion of the contract (i.e., the $800) and the prime contractor is not restricted in subcontracting the $200 supply portion of the contract. See 13 C.F.R. § 125.6(b) (stating that, for mixed contracts involving services and supplies, the applicable limitation on subcontracting depends on the type of North American Industry Classification System ("NAICS") code assigned to the contract and the applicable limitation on subcontracting "shall apply only to that portion of the contract award amount."). And, if the $200 represents materials on a services contract, that $200 also would be excluded from the total contract value for purposes of calculating how much a prime contractor could subcontract to a non-similarly situated subcontractor (which, in this example, still would be $400).

To resolve this confusion and to bring proposed FAR 52.219-14 into alignment with SBA's regulations, another sub-paragraph should be added to FAR 52.219-14(d) to address mixed contracts. The language we proposed below is comparable to SBA's rule on mixed contracts found at 13 C.F.R. § 125.6(b).

> ***(5) Mixed Contracts. The contracting officer's selection of the applicable NAICS code is determinative as to which limitation on subcontracting and performance requirement applies where a***

> ***contract combines services and supplies. In no case shall the requirements of paragraph (d)(1) and (d)(2) of this clause both apply to the same contract. The relevant limitation on subcontracting in paragraph (d)(1) or (d)(2) of this clause shall apply only to that portion of the contract award amount.***

- **The FAR Council Should Propose Revisions to the HUBZone Price Evaluation Preference Clause**

Despite proposing numerous changes to the limitations on subcontracting through the FAR, the FAR Council is not revising FAR 52.219-4 regarding the Notice of Price Evaluation Preference for HUBZone Small Business Concerns "because the application of the nonmanufacturer rule to acquisitions in which the HUBZone price evaluation preference is used is still under review." FAR 52.219-4 currently provides that, if the value of a contract for supplies exceeds $25,000 and the HUBZone small business seeking the price evaluation preference is a nonmanufacturer, then it agrees to furnish a product manufactured or produced by HUBZone small business concerns.

We are glad that the FAR Council and others are reviewing the application of the nonmanufacturer rule to acquisitions involving the HUBZone price evaluation preference. This needs careful review—and modifications to the existing requirements—because the current rules put HUBZone distributors at a significant disadvantage by effectively preventing them from taking advantage of the HUBZone price evaluation preference.

The HUBZone price evaluation preference only applies to full-and-open procurements. If a HUBZone firm is required to fully comply with the nonmanufacturer rule to take advantage of the HUBZone price evaluation preference, this effectively makes it impossible for the HUBZone nonmanufacturer to utilize the price preference in most cases. That is because the nonmanufacturer rule requires the HUBZone distributor to meet four requirements, one of which is to supply a product made by a small business unless SBA grants a waiver. But, under SBA rules, it would only grant a waiver of the nonmanufacturer rule for set-aside contracts. This means SBA would never grant a contract-specific waiver of the nonmanufacturer rule for a full-and-open procurement. And that, in turn, means a HUBZone nonmanufacturer could not qualify for the HUBZone price evaluation preference unless it supplies a product made by a small business, without any hope of a waiver for the many circumstances in which the full-and-open procurement seeks products that are only made by large businesses.

We do not believe Congress or SBA intended it to be so difficult for HUBZone distributors to benefit from the HUBZone price evaluation preference. This unique contracting tool can help agencies to increase their HUBZone spending, which has been declining for many years. Because there is no way that a HUBZone nonmanufacturer could obtain a waiver of the nonmanufacturer rule from SBA for a full-and-open contract, the HUBZone nonmanufacturer should be permitted to supply a product of any business when utilizing the HUBZone price

evaluation preference. This fairly accounts for the impossibility of obtaining a nonmanufacturer rule waiver from SBA on such contracts, as well as the fact that the contract was issued on an unrestricted basis.

Moreover, a waiver of the nonmanufacturer rule, when obtainable from SBA, only waives the requirement to supply the product of a small business. A waiver does not exempt the nonmanufacturer from meeting the other three elements of the rule. We think it makes sense to follow a comparable approach here—the HUBZone distributor would not be required to supply the product of a small business when taking advantage of the HUBZone price evaluation preference, but it would be required to satisfy the other three elements of the nonmanufacturer rule.

Based on the comments above, we recommend the following revision to FAR 52.219-4(f):

> ***(f) A HUBZone small business concern agrees that in the performance of the contract, in the case of a contract for supplies from a nonmanufacturer, it may provide an end item manufactured by other than small business concerns provided it is primarily engaged in the retail or wholesale trade and normally sells the type of item being supplied, it will take ownership or possession of the item(s) with its personnel, equipment, or facilities in a manner consistent with industry practice, and it does not exceed 500 employees.***

If the FAR Council does not agree with this proposed change and FAR 52.219-4 requires full compliance with the nonmanufacturer rule for HUBZone distributors, then the waiver rules must be modified to permit SBA to issue a waiver of the nonmanufacturer rule, upon request of a HUBZone firm, for a full-and-open contract when the price evaluation preference is utilized. The current contract-specific waiver rules require the request to come from the contracting officer. This is not feasible here, however, because a contracting officer would be unlikely to request a waiver of the nonmanufacturer rule for a full-and-open contract. The HUBZone firm, or SBA itself, must have the ability to issue the contract-specific waiver if waivers are necessary to permit HUBZone distributors to take advantage of the HUBZone price evaluation preference for procurements involving products that are only made by large businesses.

Finally, if HUBZone distributors are not permitted to supply products of any size business as we argued for above, FAR 52.219-4 should at least be modified to permit HUBZone distributors to provide products of any type of small business (rather than the current requirement to supply products made by other HUBZone small businesses). Such a change would be consistent with the changes in this rulemaking to permit a HUBZone nonmanufacturer to supply the product of any small business.

❖ **The Proposed Nonmanufacturer Rule FAR Clause Needs Revision to Conform to SBA's Nonmanufacturer Rule**

We appreciate the FAR Council's proposal to create a separate nonmanufacturer rule solicitation provision, to be added at FAR 52.219-XX. However, the proposed solicitation provision is lacking key information necessary to conform to SBA's nonmanufacturer rule. First, the provision does not state that the nonmanufacturer rule requirements can be waived by SBA, either on an individual or class basis. To avoid any confusion and ensure that small business nonmanufacturers can take advantage of waivers of the nonmanufacturer rule when they exist, the nonmanufacturer rule provision should state that the requirement to provide an end item manufactured by a small business can be waived. The FAR Council should modify the proposed language to section (c)(1) to state that the Contractor shall:

> ***(i) Provide an end item that a small business has manufactured, processed, or produced in the United States or its outlying areas, unless the U.S. Small Business Administration has already approved a class waiver or issues an individual waiver of such requirement pursuant to 13 C.F.R. § 121.406(b)(5);***

Additionally, SBA has proposed to eliminate its rule about "kit assemblers," and we suggest that the FAR Council similarly remove all rules about "kit assemblers." Our proposed change to (c)(1) eliminates the reference to kit assemblers.

Moreover, the new nonmanufacturer rule solicitation provision does not state that nonmanufacturers need to have no more than 500 employees. This requirement is in proposed FAR 19.103, but it should also be included in the solicitation provision at FAR 52.219-XX. A fourth requirement should be added to section (c)(1) to require the Contractor to:

> ***(iv) Not exceed 500 employees.***

❖ **The Limitations on Subcontracting Should Not Be Applied to Any Contracts Below the Simplified Acquisition Threshold**

The FAR Council states that it is adopting SBA's policy that the limitations on subcontracting, including the nonmanufacturer rule, do not apply to small business set-asides below the simplified acquisition threshold, but these requirements do apply to all other types of set-aside contracts regardless of the dollar value. As discussed below, the FAR Council should expand the exemption from the limitations on subcontracting to all types of small business set-asides below the simplified acquisition threshold because this is consistent with the Small Business Act.

The Small Business Act includes the limitations on subcontracting at 15 U.S.C. § 657s. This provision explicitly states that the limitations on subcontracting apply to contracts awarded under 15 U.S.C. §§ 637(a), 637(m), 644(a), 657a, and 657f. Notably absent is a mention of set-asides under 15 U.S.C. § 644(j). Thus, the limitations on subcontracting, by statute, do not apply to set-asides under 15 U.S.C. § 644(j).

15 U.S.C. § 644(j) provides that all contracts between the micro-purchase threshold and the simplified acquisition threshold "shall be reserved exclusively for small business concerns unless the contracting officer is unable to obtain offers from two or more small business concerns that are competitive with market prices and are competitive with regard to the quality and delivery of the goods or services being purchased." 15 U.S.C. § 644 is not exclusive to set-aside contracts for small businesses as opposed to other types of small business programs, and there is nothing in 15 U.S.C. § 644(j) that restricts the reservation for "small business concerns" to set-asides for small businesses only and not, for example, HUBZone small businesses. Indeed, the term "small business concern" is defined in the Small Business Act and does not exclude any of the small business programs. See 15 U.S.C. § 632. Rather, the term encompasses all types of small businesses.

Additionally, the 2010 Small Business Jobs Act (Pub. L. 111-240) made changes to other aspects of the Small Business Act to confirm that there is parity between the small business programs, and that contracting officers have discretion to choose which small business program to use when conducting a small business set-aside. See, e.g., 15 U.S.C. § 657a(b)(2)(B) (stating that a contracting officer may do a HUBZone small business set-aside if there are two or more qualified HUBZone small business concerns that will submit offers, not that he or she must).

For these reasons, we do not see a statutory basis to limit the exemption from the limitations on subcontracting to small business set-asides below the simplified acquisition threshold. The Small Business Act clearly exempts "644(j)" set-asides from the limitations on subcontracting, and these 644(j) set-asides are for all types of small businesses. Accordingly, the Small Business Act supports exempting all small business set-asides, of any type, from the limitations on subcontracting when the set-aside is conducted under 15 U.S.C. § 644(j).

We believe this conclusion is further confirmed by historical practice related to the nonmanufacturer rule, which is part of the limitations on subcontracting. Historically, the nonmanufacturer rule did not apply to contracts below the simplified acquisition threshold (which in the past was $25,000). The current FAR 19.102 states the nonmanufacturer rule does not apply to procurements that are not anticipated to exceed $25,000, which was adopted when $25,000 was the simplified acquisition threshold. And until June 29, 2016, SBA's 13 C.F.R. § 121.406, which sets out the nonmanufacturer rule for small business, service-disabled veteran-owned small business, women-owned small business, and 8(a) set-asides, stated that it did not apply to contracts processed under the Simplified Acquisition Procedures with an anticipated cost that will not exceed $25,000. The FAR Council should follow this historical precedent, and the foregoing interpretation of the Small Business Act, and exempt from the limitations on

subcontracting (including the nonmanufacturer rule) all small business set-aside contracts of any type at or below the simplified acquisition threshold.

Finally, we submit that all references to $150,000 should be changed to "the simplified acquisition threshold" so that the FAR provisions do not need to be updated in the event the simplified acquisition threshold is later increased. In fact, the simplified acquisition threshold currently is $250,000 (see 41 U.S.C. § 134), which means all references in the proposed rule to $150,000 as the simplified acquisition threshold are already outdated. For this reason, all references to $150,000 in the proposed rule should be replaced with the words "the simplified acquisition threshold."

Very truly yours,

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