



Federal Contracting and Subcontracting with Small Businesses: Issues in the 112th Congress

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Summary

Congress has generally broad authority to impose requirements upon the federal procurement process, or the process whereby agencies obtain goods and services from the private sector. One of the many ways in which Congress has exercised this authority is by enacting measures intended to promote contracting and subcontracting with “small businesses” by federal agencies. Among other things, these measures (1) declare a congressional policy of ensuring that a “fair proportion” of federal contract and subcontract dollars are awarded to small businesses; (2) establish government-wide and agency-specific goals for the percentage of contract and/or subcontract dollars awarded to small businesses; (3) require or authorize agencies to conduct competitions in which only small businesses may compete (i.e., set-asides), or make noncompetitive awards to them in circumstances when such awards could not be made to other businesses; and (4) task the Small Business Administration (SBA) and officers of the procuring agencies with reviewing and helping to restructure proposed procurements so as to maximize opportunities for small business participation. A companion report, CRS Report R42391, *Legal Authorities Governing Federal Contracting and Subcontracting with Small Businesses*, by Kate M. Manuel and Erika K. Lunder, provides an overview of these statutes, the regulations implementing them, and the various judicial and other tribunals that construe them.

This report describes and analyzes measures that Members of the 112th Congress have enacted or proposed in response to particular issues pertaining to small business contracting and subcontracting. The majority of such measures appear to address (1) the standards under which firms’ size is measured, including the establishment of size standards for “early stage” small businesses and “mid-sized” firms (H.R. 585, H.R. 1812, H.R. 3184, H.R. 3987, H.R. 4121, H.R. 4310, S. 1590); (2) government-wide or agency-specific goals for contracting and subcontracting with small businesses (H.R. 2424, H.R. 2921, H.R. 2949, H.R. 3184, H.R. 3438, H.R. 3779, H.R. 3850, H.R. 4048, H.R. 4310, H.R. 5829, H.R. 6078, S. 180, S. 1110, S. 1154, S. 1334, S. 3213); and (3) eligibility for the set-aside programs for particular types of small businesses (e.g., HUBZone small businesses) (H.R. 598, H.R. 2131, H.R. 2416, H.R. 2424, H.R. 2921, H.R. 3754, H.R. 5729, S. 236, S. 633, S. 976, S. 1334, S. 1756, S. 1874, S. 2157).

Other measures address federal contractors’ obligations vis-à-vis small business subcontractors (H.R. 2424, H.R. 3893, H.R. 4310, S. 370, S. 1334); limitations on the amount of work that may be subcontracted under contracts awarded under the authority of the Small Business Act (H.R. 3893, H.R. 4310); expedited payment of small business contractors (S. 1736); increases to the maximum surety bond amount that SBA may guarantee (H.R. 12, H.R. 2424, H.R. 4310, S. 1334, S. 1549, S. 1660, S. 2187, S. 3442); bundling and consolidation of requirements into contracts unsuitable for award to small businesses (H.R. 2424, H.R. 4081, H.R. 4310, S. 1334); and agency “insourcing” of functions performed by small businesses (H.R. 3851, H.R. 3893, H.R. 3980, H.R. 4310). Yet other measures address the responsibilities of SBA Procurement Center Representatives and agency Offices of Small and Disadvantaged Business Utilization (H.R. 3851, H.R. 3980, H.R. 4310; S. 3442); the circumstances in which agencies may set aside contracts for small businesses or make non-competitive awards to them (H.R. 240, H.R. 4118, H.R. 4203, S. 129, S. 2172); the use of small businesses when making “small purchases” (H.R. 2424, S. 1334); mentor-protégé programs wherein large businesses provide financial and other assistance to small businesses (P.L. 112-81, H.R. 3985, H.R. 4310); the deterrence and punishment of fraud in small business contracting programs (H.R. 3184, H.R. 4206, H.R. 4310, S. 633, S. 914, S. 1184, S. 3442); and contracting or subcontracting with small businesses by particular agencies (P.L. 112-74, P.L. 112-81, H.R. 4310, H.R. 6004, S. 1546, S. 3405).

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Introduction

Congress has generally broad authority to impose requirements upon the federal procurement process, or the process whereby agencies obtain goods and services from the private sector.¹ One of the many ways in which Congress has exercised this authority is by enacting measures intended to promote contracting and subcontracting with “small businesses” by federal agencies. Among other things, these measures (1) declare a congressional policy of ensuring that a “fair proportion” of federal contract and subcontract dollars are awarded to small businesses;² (2) establish government-wide and agency-specific goals for the percentage of contract and/or subcontract dollars awarded to small businesses;³ (3) require or authorize agencies to conduct competitions in which only small businesses may compete (i.e., set-asides), or make noncompetitive awards to them in circumstances when such awards could not be made to other businesses;⁴ and (4) task the Small Business Administration (SBA) and officers of the procuring agencies with reviewing and helping to restructure proposed procurements so as to maximize opportunities for small business participation.⁵ A companion report, CRS Report R42391, *Legal Authorities Governing Federal Contracting and Subcontracting with Small Businesses*, by Kate M. Manuel and Erika K. Lunder, provides an overview of these statutes, the regulations implementing them, and the various judicial and other tribunals that construe them.

This report describes measures that Members of the 112th Congress have enacted or proposed in response to particular issues pertaining to small business contracting and subcontracting (e.g.,

¹ See, e.g., *Perkins v. Lukens Steel Co.*, 310 U.S. 113, 127 (1940) (“Like private individuals and businesses, the Government enjoys the unrestricted power to produce its own supplies, to determine those with whom it will deal, and to fix the terms and conditions upon which it will make needed purchases.”). The U.S. Constitution does, however, impose a few limits upon Congress’s power in this regard, most notably by guaranteeing all persons equal protection of the law. U.S. Const. amend. V (guaranteeing due process of law); *Bolling v. Sharpe*, 347 U.S. 497 (1954) (finding that due process under the Fifth Amendment includes equal protection, or the constitutional assurance that the government will apply the law equally to all people and not improperly prefer one class of people over another). Equal protection issues arise most frequently with contracting preferences based on race or gender. Race and gender are “suspect classifications,” which means that the government must demonstrate that any programs that classify individuals on this basis are narrowly tailored to further a compelling government interest, in the case of race-conscious programs, or are substantially related to important government objectives, in the case of gender-conscious programs. See, e.g., *Adarand Constructors, Inc. v. Peña*, 515 U.S. 200 (1995) (“strict scrutiny” applied to program that classified individuals on the basis of race); *Craig v. Boren*, 429 U.S. 190, 197 (1976) (“intermediate scrutiny” applied to program that classified individuals on the basis of sex).

² See 15 U.S.C. §631(a) (“It is the the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise, to insure that a fair proportion of the total purchases and contracts for property and services for the Government (including but not limited to contracts for maintenance, repair, and construction) be placed with small-business enterprises, to insure that a fair proportion of the total sales of Government property be made to such enterprises, and to maintain and strengthen the overall economy of the Nation.”).

³ See, e.g., 15 U.S.C. §644(g)(2) (requiring agencies, in consultation with the Small Business Administration (SBA) to set goals for the percentage of federal contract and/or subcontract dollars awarded to small businesses that “realistically reflect” the ability of small businesses to participate in such contracts or subcontracts).

⁴ See, e.g., 15 U.S.C. §637(a) (authorizing set-asides and sole-source awards to small businesses owned and controlled by socially and economically disadvantaged individuals participating in SBA’s Minority Small Business and Capital Ownership Development Program (commonly known as the 8(a) Program)).

⁵ See, e.g., 15 U.S.C. §634(b)(11) (requiring SBA to appoint Procurement Center Representatives (PCRs) to work with the procuring agencies); 13 C.F.R. §125.2(b) (requiring PCRs to review all acquisitions not set aside for small businesses to determine whether a set-aside is appropriate and to identify alternate strategies to maximize small business participation as contractors or subcontractors, among other things).

increasing SBA's size standards, increasing government-wide or agency-specific goals for contracting and/or subcontracting with small businesses). In particular, it analyzes changes to existing law that would be made were these measures enacted, and discusses legal issues potentially raised by certain types of measures. Although a number of bills are included in this discussion, the report does not attempt to address all bills, or all provisions of any bills that are included. Rather, these bills are presented as examples of particular approaches to issues of interest to the Congress. In addition, this report's discussion of the legal questions potentially raised by various types of approaches to current issues (e.g., creation of additional set-aside programs) should not be construed to mean that any specific bill cited in the report would necessarily raise these questions. Much would depend upon the drafting and details of particular bills, the analysis of which is outside the scope of this report.

The report will be updated regularly, as additional legislation is introduced, while the 112th Congress is in session.

Size Standards

The Small Business Act currently gives the Administrator of Small Business considerable discretion as to what firms qualify as small for purposes of the act, or for certain other purposes of federal law. The act requires only that small businesses be "independently owned and operated," be "not dominant in their field of operations," and meet any size standards established by the Administrator.⁶ The Administrator first promulgated regulations specifying standards for size in various industries in 1956 under the authority of the Small Business Act of 1953, which established SBA on a temporary basis.⁷

Between the early 1980s and 2007, SBA conducted no comprehensive reviews of the size standards, instead making only intermittent changes to the standards for particular industries.⁸ Its failure to do so prompted some Members of Congress and commentators to question whether the standards adequately reflected recent trends in industry or government procurement.⁹ Partly in response to such concerns, the 111th Congress enacted legislation that requires SBA to conduct a "detailed review" of at least one-third of the size standards every 18 months, and make "appropriate adjustments" to them to reflect market conditions.¹⁰ The legislation also includes certain provisions regarding "small business size and status integrity" intended to combat fraud in

⁶ 15 U.S.C. §632(a)(1)-(2). *But see* Small Business Size Standard Flexibility Act of 2011, H.R. 585 (requiring the SBA's Chief Counsel for Advocacy, as opposed to the Administrator of Small Business, to specify definitions or standards of size for purposes of any acts other than the Small Business Act or the Small Business Investment Act, and to approve all size standards except those prescribed by the Administrator).

⁷ *See, e.g.*, Small Bus. Admin., Small Business Size Standards, 21 *Federal Register* 79 (January 5, 1956). For more on the history of the size standards, see generally CRS Report R40860, *Small Business Size Standards: A Historical Analysis of Contemporary Issues*, by Robert Jay Dilger.

⁸ *See, e.g.*, SBA Proposes to Increase Small Business Size Standards for Three NAICS Sectors, *Fed. Cont. Daily*, October 22, 2009.

⁹ *Id.*

¹⁰ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1344, 124 Stat. 2545-46. The act further specifies that each size standard shall be reviewed "not less frequently than once every five years." *Id.* It is important to note that the provisions of the Small Business Job Act authorizing SBA to promulgate "alternative" size standards pertain only to loan programs. *See* P.L. 111-240, §1116, 124 Stat. 2509.

the small business programs that are discussed below.¹¹ Following the enactment of this legislation, SBA completed its first “comprehensive” review of the size standards since the 1980s, and has promulgated or proposed regulations that could reportedly result in as many as 8,350 additional firms becoming eligible for small business programs.¹² Some increases to the size standards took effect in March 2012; other increases are still pending.¹³

Concerns about the size standards and, in particular, SBA’s discretion in crafting them have persisted, however, notwithstanding the legislation enacted by the 111th Congress and the changes made or proposed by SBA. Some Members of the 112th Congress have introduced legislation that would expressly require SBA to

- establish a new classification system to replace the current system based on North American Industrial Classification System (NAICS) codes;¹⁴
- repeal the “nonmanufacturer rule,” an SBA regulation that permits firms with fewer than 500 employees which supply the products of small businesses (or obtain a waiver from SBA) to qualify as small in certain procurements;¹⁵
- make available certain information (e.g., a detailed description of the industry and its competitive environment) whenever SBA conducts rulemaking to revise, modify, or establish size standards;¹⁶
- make available a justification demonstrating that any single size standard for a grouping of four-digit NAICS codes is appropriate for each individual industry classification included in the grouping;¹⁷ and

¹¹ See *infra* notes 214-216 and accompanying text.

¹² See, e.g., Andrew Lapin, SBA Redefinition of Small Business Draws Mixed Reactions, *Gov’t Exec.*, February 15, 2012, available at <http://www.govexec.com/contracting/2012/02/sba-redefinition-small-business-draws-mixed-reactions/41215>.

¹³ See, e.g., Small Bus. Admin., Size Standards: Transportation and Warehousing: Final Rule, *77 Federal Register* 10934 (February 24, 2012) (increasing the size standards for 22 industries, effective March 26, 2012); Small Bus. Admin., Small Business Size Standards: Professional, Technical, and Scientific Services: Final Rule, *77 Federal Register* 7490 (February 10, 2012) (increasing the size standards for 35 industries, effective March 12, 2012); Small Bus. Admin., Small Business Size Standards: Utilities, *77 Federal Register* 42441 (July 19, 2012) (requesting comments on proposed size standards for 9 industries by September 17, 2012).

¹⁴ Fairness for Small Businesses in Federal Contracting Act of 2011, S. 1590, §2. The new system would have to (1) consist of not more than 20 industries; (2) include, as industries, manufacturing, construction, professional services, wholesale, and retail; and (3) be “based on market conditions as identified by the most recent Economic Census of the United States.” *Id.* SBA would also be required to review the new classification system periodically, as provided in the Small Business Jobs Act. According to its sponsor, this legislation is specifically “aimed at keeping large firms from winning contracts meant for small businesses” by “gaming” an “overly complex and flawed classification system.” David Hansen, McCaskill Bill Would Replace NAICS System for Small Business Contracting, *96 Fed. Cont. Rep.* 308 (September 27, 2011) (quoting Senator McCaskill).

¹⁵ Fairness for Small Businesses in Federal Contracting Act of 2011, S. 1590, §2. In place of the nonmanufacturer rule, SBA would be required to promulgate regulations directing contracting officers to “use the size standards established by the Administrator for retail and wholesale industries in procurements for products and services by the Federal Government that are not manufactured by the offeror,” and to use only size standards established by the SBA for manufacturing industries if the contract involves the purchase of goods or services manufactured by the offeror. *Id.*

¹⁶ National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1661.

¹⁷ Small Business Protection Act of 2012, H.R. 3987, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1661. These measures are intended to address issues such as those raised in 2011 by the SBA’s proposed grouping of architect and engineer services. Applying the same standards to architect and engineering firms would reportedly have resulted in 97.8% of all architecture firms qualifying as small under the SBA’s proposed (continued...)

- exclude firms that are publicly traded, or more than 50% directly or indirectly owned by “individuals” who are not U.S. citizens, from programs under the Small Business Act.¹⁸

Other Members have proposed the creation of set-aside programs for firms that are very small and/or new,¹⁹ and for “mid-sized” firms.²⁰ In both cases, the proposals reflect fears that particular firms may be included in, or excluded from, existing small business programs because of the size standards. Proposals to create set-aside programs for mid-size firms reflect concerns that such firms are too big to qualify as “small” under the size standards, but too small to compete effectively with “large” government contractors.²¹ Conversely, proposals to create set-asides specifically for “early stage small businesses”—or particularly small and/or new businesses—reflect concerns that the current size standards can encompass firms of very different sizes, and that the smallest such firms may be unable to compete effectively against the larger ones.

Depending upon how eligibility for any new set-aside program is defined, certain programs could potentially be vulnerable to challenge upon equal protection or other grounds.²² The current 8(a)

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size standard. *See, e.g.*, Committee Members Introduce Additional Legislation to Reform Small Business Contracting, February 8, 2012, *available at* <http://smallbusiness.house.gov/News/DocumentSingle.aspx?DocumentID=278695>; Objections to Proposed Size Standard Change Raised at House Small Business Hearing, 95 *Fed. Cont. Rep.* 484 (May 10, 2011).

¹⁸ Fairness and Transparency in Contracting Act of 2011, §4; Act for the 99%, H.R. 3638, §1304 (adding to the Small Business Act a definition of “independently owned and operated” that excludes such entities). Among the statutory criteria that firms must meet to qualify as small under the act is that they are independently owned and operated. 15 U.S.C. §632(a)(1). It is unclear what effect the citizenship provisions, in particular, would have since the owners of disadvantaged, HUBZone, and women-owned small businesses must currently be citizens. 13 C.F.R. §124.1002 (small disadvantaged businesses); 13 C.F.R. §126.103 (HUBZone small businesses); 13 C.F.R. §127.102 (women-owned small businesses).

¹⁹ *See, e.g.*, Early Stage Small Business Contracting Act of 2012, H.R. 4121 (requiring agencies to award contracts whose value is between \$3,000 and “less than half the upper threshold of Section 15(j)(1) of the Small Business Act” to “early stage small business concerns,” or firms with fewer than 15 employees that have average annual receipts of not more than \$1 million (unless the concern is in an industry with an average annual revenue standard of less than \$1 million); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1693a. Agencies would seemingly have discretion as to whether such contracts are awarded via a set-aside or on a sole-source basis, although they would appear to be required to award any contract identified as suitable for award to such entities to them. SBA would help to determine what contracts are suitable for award to early stage businesses.

²⁰ *See, e.g.*, Small Business Growth Act, H.R. 1812, §2 (granting the General Services Administration temporary authority to set aside contracts for firms that are not small businesses provided that the firms have fewer than 1,500 employees and participate, as mentors to small businesses, in GSA’s mentor-protégé program); Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, §§201-209 (establishing a set-aside program for businesses “owned or controlled by historically disadvantaged individuals” to be administered by the Department of Commerce’s Minority Business Development Agency (MBDA)); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1611 (granting defense agencies temporary authority to set aside certain contracts for firms that are independently owned and operated, not dominant in their fields of operations, and have fewer than twice the number of employees (or fewer than three times the average annual receipts) permitted under the SBA size standard for their industry).

²¹ *See, e.g.*, Matthew Weigelt, Small-biz Definitions Put Hurt on Midsize Contractors, *Wash. Tech.*, June 28, 2010, *available at* <http://washingtontechnology.com/articles/2010/07/05/policy-midsize-company-squeeze.aspx>.

²² Hasidic Jews are among the groups currently recognized as disadvantaged by the MBDA, and set-asides for them could potentially raise First Amendment issues if this were viewed as a religious, rather than a cultural, classification. *Cf. Bd. of Ed. of Kiryas Joel Village School Dist. v. Grumet*, 512 U.S. 687, 741 (1994) (Scalia, J., dissenting) (suggesting that the New York law in question, which resulted in a village that was a religious enclave being carved out as a separate school district, could be seen as reflecting cultural, rather than religious, groupings).

Program, which incorporates a rebuttable presumption that members of certain racial and ethnic groups are disadvantaged, has been challenged on the grounds that it deprives individuals who are not members of these groups of equal protection of the law in violation of the U.S. Constitution.²³ Programs that include a similar presumption, or otherwise define eligibility in a manner that could be found to constitute a *de facto* racial classification, could face similar challenges.²⁴

Government-Wide and Agency-Specific Goals

Congress amended the Small Business Act in 1978 to require that agency heads, in consultation with the SBA, set goals for the percentage of federal contract and subcontract dollars awarded to small businesses each year.²⁵ Congress further amended the act in 1988 to require the President to set government-wide goals for the percentage of federal contract and/or subcontract dollars awarded annually to various categories of small businesses.²⁶ These goals must be equal to or exceed certain percentages specified in statute (i.e., 23% of federal contract dollars awarded to small businesses; 5% of federal contract and subcontract dollars awarded to women-owned small businesses; 5% to small disadvantaged businesses; 3% to HUBZone small businesses; and 3% to service-disabled veteran-owned small businesses).²⁷ Agency performance in meeting the small business contracting and subcontracting goals is of perennial interest to Congress because it is arguably the clearest indicator of whether the stated congressional “policy” of encouraging contracting with small businesses is being implemented.²⁸ In particular, commentators frequently note the government’s failure to meet either government-wide or agency-specific goals,²⁹ and some have suggested that the current government-wide goals are too low and do not adequately

²³ See *DynaLantic Corp. v. U.S. Dep’t of Defense*, 2012 U.S. Dist. LEXIS 114807 (D.D.C. August 15, 2012) (finding that the 8(a) Program is not unconstitutional on its face, but that it is unconstitutional as applied in the military training and simulation industry); *Rothe Dev., Inc. v. Dep’t of Defense*, No. 1:12-cv-00744-EGS (D.D.C., filed May 9, 2012) (challenging the constitutionality of the 8(a) Program). See also *supra* note 1.

²⁴ In *Rothe Development Corporation v. Department of Defense*, the government did not contest whether the presumption regarding race and disadvantage underlying the Department of Defense’s (DOD’s) small disadvantaged business program constituted a racial classification. See 545 F.3d 1023 (Fed. Cir. 2008). However, some courts had previously denied firms or individuals standing to challenge programs with racial presumptions like that underlying DOD’s program on the grounds that the would-be plaintiffs were denied the contract because of inability to demonstrate social and economic disadvantage, not because of race. See, e.g., *Interstate Traffic Control v. Beverage*, 101 F. Supp. 2d 445 (S.D. W.Va. 2000); *Ellsworth Assocs. v. United States*, 926 F. Supp. 207 (D.D.C. 1996). It is unclear whether a court would apply similar logic at this date, in light of subsequent developments in the case law. See generally CRS Report RL33284, *Minority Contracting and Affirmative Action for Disadvantaged Small Businesses: Legal Issues*, by Jody Feder.

²⁵ An Act to Amend the Small Business Act and the Small Business Investment Act of 1958, P.L. 95-507, §221, 92 Stat. 1771 (October 24, 1978) (codified at 15 U.S.C. §644(g)(2)). These goals must “realistically reflect the potential” of small businesses to perform federal prime contracts and subcontracts.

²⁶ Business Opportunity Development Reform Act (BODRA), P.L. 100-656, §502, 102 Stat. 3853, 3881 (November 15, 1988) (codified, as amended, at 15 U.S.C. §644(g)(1)).

²⁷ 15 U.S.C. §644(g)(1).

²⁸ See 15 U.S.C. §631(a) (“It is the declared policy of the Congress that the Government should aid, counsel, assist, and protect, insofar as is possible, the interests of small-business concerns in order to preserve free competitive enterprise [and] to insure that a fair proportion of the total purchases and contracts or subcontracts for property and services for the Government ...be placed with small-business enterprises.”).

²⁹ See, e.g., Jeff Kinney, SBA Notes Drop in Small Business Contract Awards for FY2011, 98 *Fed. Cont. Rep.* 27 (July 10, 2012).

reflect the availability of minority-, women-, and service-disabled veteran-owned small businesses in today's marketplace.³⁰

Partly in response to such concerns, the 111th Congress enacted legislation requiring that senior procurement executives, senior program managers, and directors of Small and Disadvantaged Business Utilization communicate to their subordinates "the importance of achieving small business goals."³¹ In addition, some Members of the 112th Congress have introduced legislation that would increase the goals, or create greater incentives for agencies to meet their goals. The first category includes bills that would (1) increase the statutorily set government-wide goals;³² (2) require a specific agency to meet a goal;³³ or (3) direct entities that may be exempt from the requirements of the Small Business Act to establish goals for contracting with small businesses.³⁴ Some bills also address the related issue of how to count contracts for purposes of determining whether the goals have been met by

- expressly permitting certain contracts to be counted for goaling purposes;³⁵

³⁰ See, e.g., *Doing Business with the Government: The Record and Goals for Small, Minority, and Disadvantaged Businesses: Hearing Before the Subcommittee on Economic Development, Public Buildings, and Emergency Management of the Committee on Transportation and Infrastructure, House of Representatives, 110th Cong., 2d Sess.*, at 1 (March 6, 2008). The most recently established statutory goal is that for contracting with service-disabled veteran-owned small businesses, which was created in 1999. The goals for contracting with other types of small businesses were established at earlier dates.

³¹ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1333, 124 Stat. 2542 (codified at 15 U.S.C. §644(g)(2)(F)(i)-(ii)).

³² Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §2 (increasing the overall goal from 23% to 25% of all prime contracts and setting a goal of 40% of all subcontracts; establishing prime contracting goals of 3% and subcontracting goals of 3% for service-disabled veteran-owned and HUBZone small businesses; establishing prime contracting goals of 5% and subcontracting goals of 5% for small disadvantaged businesses and women-owned small businesses); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1631 (same); Small Business Goaling Act of 2012, S. 3213, §2 (same); Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, tit. I, §105 (increasing the overall goal from 23% to 25% and the 5% goals to 10%); Expanding Opportunities for Small Businesses Act of 2011, H.R. 2921, §3 (increasing the goal for small disadvantaged businesses from 5% to 8%); Small Business Opportunity Expansion Act of 2011, H.R. 2949, §2 (increasing the overall goal from 23% to 24%, the 3% goals to 4%, and the 5% goals to 6%); Small Business Contracting Opportunities Expansion Act of 2012, H.R. 6078, §§2, 4 (increasing the overall goal from 23% to 26% of prime contracts (27%, effective in FY2017) and 40% of subcontracts, as well as increasing the goals for contracting and subcontracting with various types of small businesses). The latter bill also calls for a study of the feasibility of creating a government-wide goal for contracting with small businesses owned by veterans who do not have a service-incurred or -aggravated disability.

³³ An Act to Require the Department of Defense to Meet the Annual Goal for Participation in Procurement Contracts by Small Business Concerns Owned and Controlled by Veterans with Service-connected Disabilities, H.R. 3438, §1. The bill does not specify what the consequences might be if the Department failed to meet this goal.

³⁴ Prisoner Opportunity, Work, and Education Requirement (POWER) Act, S. 180, §5 (requiring Federal Prison Industries (FPI), in consultation with SBA, to establish and strive to meet or exceed "realistic goals" for entering into contracts with one or more small businesses). The Small Business Act has an arguably broader reach than the Federal Acquisition Regulation (FAR) in that it applies to all "agencies," as that term is defined in 5 U.S.C. §551(1), while the FAR applies to all executive-branch agencies that are not expressly excluded from its coverage. See, e.g., 15 U.S.C. §632(b). However, there are certain entities, such as FPI, who may not be agencies for purposes of the Small Business Act.

³⁵ Small Business Fairness Act, S. 1110, §2; H.R. 5829, §2 (providing that, if an 8(a), HUBZone, woman-owned, or service-disabled veteran-owned small business performed the obligations of a prime contractor under a "contractor team arrangement," then the agency could count the contract for purposes of its goals). See also An Act to Amend Title 38, United States Code, to Clarify the Contracting Goals and Preferences of the Department of Veterans Affairs with Respect to Small Business Concerns Owned and Controlled by Veterans, H.R. 4048, §2 (directing the Secretary of Veterans Affairs to include goods and services acquired through the Federal Supply Schedules "[f]or purposes of (continued...)")

- limiting to two the number of categories in which one business could be counted (e.g., HUBZone and women-owned),³⁶
- specifying that certain types of businesses (e.g., foreign-owned) not be included in the count,³⁷ and
- otherwise directing SBA on how to count certain contracts.³⁸

The second category includes bills that seek to improve the government's performance in meeting existing contracting and subcontracting goals. These types of measures tend to focus on increasing reporting by the agencies or SBA and publicizing the information,³⁹ or requiring SBA or the Government Accountability Office (GAO) to study the activities of federal agencies and provide recommendations on how to improve goaling performance.⁴⁰ Other provisions appear intended to improve performance through better training,⁴¹ or by penalizing agencies that fail to

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meeting the goals" under the Veterans Benefits Act).

³⁶ Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, tit. I, §105.

³⁷ Fairness and Transparency in Contracting Act of 2011, H.R. 3184, §4; Act for the 99%, H.R. 3638, §1304 (amending definitions in the Small Business Act so that no publicly-traded business or its subsidiary, or foreign-owned business or its subsidiary, may be considered a small business for purposes of federal contracting, including procurement goals).

³⁸ Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1631 (removing SBA's discretion to exclude certain contracts when determining the total value of contract dollars awarded each year because of (1) where these contracts are awarded or performed; (2) whether federal law mandates that the contract be performed by an entity other than a small business; (3) whether funding for a contract subject to the Competition in Contracting Act (CICA) was made available in an appropriations act; or (4) whether the contract was subject to the FAR); Small Business Contracting Opportunities Expansion Act of 2012, H.R. 6078, §2 (same). SBA has historically used its discretion to exclude certain contracts from these calculations, such as contracts performed outside the United States and contracts awarded through the Javits-Wagner-O'Day (JWOD) Program. *See, e.g.*, Small Business Goaling Report: Fiscal Year 2010, available at https://www.fpds.gov/downloads/top_requests/FPDSNG_SB_Goaling_FY_2010.pdf (listing exclusions); Small Bus. Admin., Office of Inspector General, Small Business Administration's Rationale for Excluding Certain Types of Contracts from the Annual Small Business Procurement Calculations Needs to be Documented, Advisory Memorandum Report No. 12-04, December 6, 2011 (copy on file with the authors).

³⁹ Fairness and Transparency in Contracting Act of 2011, H.R. 3184, §6; Act for the 99%, H.R. 3638, §1306 (requiring that each federal agency list on its website all of the businesses that received a contract because they were identified as small businesses); Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §3 (requiring SBA to report to Congress on the goaling performance of each agency and the federal government as a whole, as well as information about small business contracting broken down by category of small business and type of preference, within 60 days of receiving a report from each agency); Honoring Promises to Service-Disabled Veterans Act of 2011, S. 1154, §3 (requiring agencies to report quarterly to SBA on their contracting with service-disabled veteran-owned small businesses and requiring SBA to then rank the agencies and publish the results on a publicly accessible website, as well as requiring SBA to report annually to Congress on the progress of federal agencies in meeting their goals for contracting with service-disabled veteran-owned small businesses and to include recommendations on whether any prime contractor should be recognized by Congress for "outstanding progress" in contracting with such businesses); Small Business Goaling Act of 2012, S. 3213, §3 (requiring certain reports by the procuring agencies and SBA).

⁴⁰ Expanding Opportunities for Small Businesses Act of 2011, H.R. 2921, §3 (requiring GAO to report on the 5 most and 5 least successful agencies with regards to meeting the goals and to provide recommendations on how to improve the performance of the least successful ones); Small Business Contracting Opportunities Expansion Act of 2012, H.R. 6078, §3 (requiring GAO to report on improving internal processes of agencies engaged in contracting, and on outreach to groups that are the subject of procurement goals).

⁴¹ Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §§2, 4 (requiring senior procurement employees and program managers to communicate to subordinates the importance of achieving goals, and that senior executives in federal agencies be trained about federal procurement requirements, including contracting requirements under the Small Business Act); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1633 (requiring that training programs for senior executives include federal procurement requirements, (continued...))

meet their goals.⁴² However, the latter type of provisions could potentially raise constitutional issues to the degree that any penalties for failure to meet goals for contracting and subcontracting with minority- or women-owned small businesses, in particular, were seen as transforming these goals into quotas. To date, the courts have generally upheld aspirational goals that reflect classifications among small businesses based on the race or gender of their owners, among other factors, on the grounds that such goals are not mandatory and, thus, do not constitute disparate treatment of small business owners by the federal government.⁴³ However, if legislation were to impose mandatory goals, or change the nature of the existing goals so that they were effectively mandatory, then questions could be raised as to whether the goal was essentially a quota that required minority- or women-owned small businesses to get fixed percentages of government contracts.⁴⁴

Eligibility for Existing Set-Aside Programs

Ever since Congress established the first set-aside program in 1978,⁴⁵ the criteria governing eligibility for such programs have periodically been of interest to Members of Congress and the public.⁴⁶ Currently, the primary concerns appear to center upon eligibility for the 8(a) and

(...continued)

including contracting requirements under the Small Business Act).

⁴² Small Business Growth and Federal Accountability Act of 2012, H.R. 3779, §2 (prohibiting any federal agency that fails to meet a goal from expending for the procurement of goods or services an amount greater than 90% of the amount expended for the procurement of goods or services during the year for which it failed to meet the goal); Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §4 (providing that if an agency failed to meet any goal, no senior executives within that agency could receive an incentive award or be granted a sabbatical during the following year); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1631 (prohibiting SBA from establishing or implementing any pilot program unless it issues certain required reports regarding government performance vis-à-vis the small business contracting goals); Small Business Contracting Opportunities Expansion Act of 2012, H.R. 6078, §2 (same).

⁴³ See *Adarand Constructors*, 228 F.3d at 1181 (upholding the constitutionality of aspirational goals on the grounds that such goals are not mandatory). However, the constitutionality of the federal government's aspirational goals under 15 U.S.C. §644(g) has been challenged. See *DynaLantic Corp.*, 503 F. Supp. 2d 262.

⁴⁴ For example, in upholding the 8(a) Program against a facial challenge, the U.S. District Court for the District of Columbia recently emphasized that federal goals for contracting with small disadvantaged businesses (including 8(a) firms) are aspirational, not "rigid numerical quotas," and that there are no "penalties" for failure to meet the goals. *DynaLantic Corp.*, 2012 U.S. Dist. LEXIS 114807, at *10. See also *City of Richmond v. J.A. Croson Co.*, 488 U.S. 469 (1989) (holding that a municipal ordinance requiring the city's prime contractors to award at least 30% of the value of each contract to minority subcontractors was unconstitutional); *Rothe Dev. Corp.* 545 F.3d 1023 (striking down a statute that established, as a goal, that the Department of Defense (DOD) award 5% of its contracts to small disadvantaged businesses and other entities, and authorized DOD to apply a 10% price evaluation adjustment to the bids or offers of such entities in order to reach this goal).

⁴⁵ An Act to Amend the Small Business Act and the Small Business Investment Act of 1958, P.L. 95-507, §202, 92 Stat. 1761-63 (October 24, 1978) (codified, as amended, at 15 U.S.C. §637(a)). Prior to the 1978 amendments to the Small Business Act, SBA had implemented a set-aside program for certain minority-owned businesses in the absence of express statutory authority to do so. See generally CRS Report R40744, *The "8(a) Program" for Small Businesses Owned and Controlled by the Socially and Economically Disadvantaged: Legal Requirements and Issues*, by Kate M. Manuel and John R. Luckey.

⁴⁶ See, e.g., *Federal Contracting: Removing Hurdles for Minority-Owned Businesses: Hearing of the House Committee on Oversight and Government Reform, Subcommittee on Government Management, Organization and Procurement*, 110th Cong., 1st Sess. (2007) (discussing the 8(a) Program specifically); *Are Government Purchasing Policies Failing Small Businesses? Hearing of the Senate Committee on Small Business and Entrepreneurship*, 107th Cong., 2d Sess. (2002) (discussing various small business programs).

HUBZone programs, for various reasons discussed below. Proposals to create new set-aside programs for “early stage” small businesses or mid-sized firms are discussed above, under the heading “Size Standards.”⁴⁷ Proposals to grant agencies additional authority to conduct competitions in which only women-owned small businesses may compete, or to make sole-source awards to them, are discussed below, under the heading “Restricted Competitions and Non-Competitive Awards.”⁴⁸

8(a) Program

The Small Business Act requires SBA to establish a “small business and capital ownership development program” to provide non-financial assistance to certain small businesses owned and controlled by socially and economically disadvantaged individuals,⁴⁹ and to enter into contracts with other government agencies that are subcontracted to such firms.⁵⁰ Taken together, these requirements form the basis for SBA’s 8(a) Program.⁵¹ In addition, the act defines socially disadvantaged individuals as “those who have been subjected to racial or ethnic prejudice or cultural bias because of their identity as a member of a group without regard to their individual qualities,”⁵² and economically disadvantaged individuals as

those socially disadvantaged individuals whose ability to compete in the free enterprise system has been impaired due to diminished capital and credit opportunities as compared to others in the same business area who are not socially disadvantaged.⁵³

However, outside of limiting participation in the 8(a) Program by firms and individual owners to a maximum of nine years,⁵⁴ and finding that members of certain groups are socially disadvantaged,⁵⁵ the Small Business Act generally gives SBA considerable discretion as to the criteria for eligibility for the 8(a) Program.⁵⁶ This is particularly true where economic

⁴⁷ See *supra* notes 19-24 and accompanying text.

⁴⁸ See *infra* notes 171-186.

⁴⁹ 15 U.S.C. §636(j)(10). This program shall be “exclusively” for such firms and shall, among other things, assist small business concerns participating in the program (either through public or private organizations) to develop and maintain comprehensive business plans which set forth the Program Participant’s business targets, objectives, and goals ... [and] provide for such other nonfinancial services as deemed necessary for the establishment, preservation, and growth of small business concerns participating in the Program, including but not limited to (I) loan packaging, (II) financial counseling, (III) accounting and bookkeeping assistance, (IV) marketing assistance, and (V) management assistance.

⁵⁰ 15 U.S.C. §637(a)(1)(A).

⁵¹ For more on the 8(a) Program, see generally CRS Report R40744, *The “8(a) Program” for Small Businesses Owned and Controlled by the Socially and Economically Disadvantaged: Legal Requirements and Issues*, by Kate M. Manuel and John R. Luckey.

⁵² 15 U.S.C. §637(a)(5).

⁵³ 15 U.S.C. §637(a)(6)(A).

⁵⁴ 15 U.S.C. §636(j)(10)(C)(i) (nine-year term); 15 U.S.C. §637(a)(9) (termination and early graduation); 13 C.F.R. §124.301 (exiting the 8(a) Program); 13 C.F.R. §124.302 (early graduation); 13 C.F.R. §124.303 (termination from the Program).

⁵⁵ 15 U.S.C. §631(f)(1)(C) (finding that such groups “include, but are not limited to, Black Americans, Hispanic Americans, Native Americans, Indian tribes, Asian Pacific Americans, Native Hawaiian Organizations, and other minorities”).

⁵⁶ See, e.g., 13 C.F.R. §124.101 (limiting participation in the program to small businesses that are “unconditionally owned and controlled by one or more socially and economically disadvantaged individuals [or groups] who are of good character and citizens of the United States” that demonstrate “potential for success”).

disadvantage is concerned. The current net worth standards—which preclude individuals from having personal net worth of more than \$250,000 at the time of entry into the 8(a) Program (\$750,000 for continuing eligibility)⁵⁷—are established by regulation, not statute.⁵⁸

Recently, there has been particular concern about whether some persons who could benefit from the 8(a) Program are excluded from it due to the net worth standards,⁵⁹ which were set in 1989⁶⁰ and have not been adjusted for inflation since then.⁶¹ Relatedly, some have expressed concern that firms are not adequately prepared to compete for federal or other contracts upon leaving the program,⁶² and that certain firms receive a disproportionately large share of all 8(a) contracts, leaving other firms with diminished opportunities to grow and develop.⁶³ Partly in response to such concerns, the 111th Congress enacted legislation requiring GAO to study whether the 8(a) mentor-protégé program and similar programs, discussed below, are “effectively supporting the goal of increasing the participation of small business concerns in Government contracting.”⁶⁴

Members of the 112th Congress have also introduced measures specifically addressing eligibility for the 8(a) Program, some seeking to expand eligibility, and others to restrict it, at least for certain owners and firms. The former category includes measures that would allow firms to participate in the program for more than nine years and require SBA to provide technical assistance to those who are no longer eligible to participate, as well as measures that would

⁵⁷ 13 C.F.R. §124.104(c). Individuals’ ownership interests in the small business and equity in their primary personal residences are excluded when determining net worth.

⁵⁸ It should also be noted that the Department of Transportation adjusted the net worth standards for its Disadvantaged Business Enterprise program—which had previously corresponded to SBA’s standards—by regulation in 2011, without being required to do so by statute. Dep’t of Transportation, Disadvantaged Business Enterprise Program: Program Improvements, 76 *Federal Register* 5083, 5085-86 (January 28, 2011) (codified at 49 C.F.R. §26.27(a)(2)(i) (increasing the net worth threshold from \$750,000 to \$1.32 million).

⁵⁹ See, e.g., Not Too Small to Succeed in Business Act of 2011, H.R. 3754, §2 (finding that the 8(a) Program does not adequately prepare firms for graduation, in part, because of the “reliance of the [SBA] on outdated measures of . . . net worth in determining whether a company participating in the program continues to be economically disadvantaged”).

⁶⁰ See Small Bus. Admin., Minority Small Business and Capital Ownership Development Program: Final Rule, 54 *Federal Register* 34692 (August 21, 1989) (amending the SBA regulations to adopt the current net worth standards).

⁶¹ The SBA’s net worth standards are not acquisition-related thresholds subject to periodic adjustment for inflation under the Ronald W. Reagan National Defense Authorization Act for FY2005. See, e.g., Dep’t of Defense, Gen. Servs. Admin., & Nat’l Aeronautics & Space Admin., Inflation Adjustment of Acquisition-Related Thresholds, 75 *Federal Register* 5716, 5717 (February 4, 2010) (“Examples of thresholds that are not viewed as ‘acquisition-related’ as defined [here] are thresholds relating to claims, penalties, withholding, payments, required levels of insurance, small business size standards, liquidated damages, etc.”). Congress could, however, enact legislation requiring periodic adjustment of the net worth standards for inflation.

⁶² See, e.g., Not Too Small to Succeed in Business Act of 2011, H.R. 3754, §2 (finding that the 8(a) Program “has a record of graduating companies that are not sufficiently prepared to compete for contracts with large and established companies in the private sector, resulting in a large number of former participants in the program failing to remain in business shortly after leaving the program”); Small Business Contracting Fraud Prevention Act of 2011, S. 633, §5 (requiring GAO to report periodically to Congress on the effectiveness of the 8(a) Program, including the percentage of businesses that continue to operate during the three-year period after successfully completing the program); SUCCESS Act of 2012, S. 3442, §525 (same). For more on this and other provisions of S. 633, see *infra* notes 218 to 221 and accompanying text.

⁶³ See, e.g., Gov’t Accountability Office, Federal Contracting: Monitoring and Oversight of Tribal 8(a) Firms Need Attention, GAO-12-84, January 2012, available at <http://www.gao.gov/assets/590/588101.pdf> (reporting that while tribal 8(a) firms comprised 6.2% of all 8(a) firms in FY2010, they received nearly 33% of all 8(a) obligations). Most obligations to tribal-owned firms were to ANC-owned firms. *Id.*

⁶⁴ Small Business Jobs Act of 2010, P.L. 111-240, tit. I, subtitle C, §1345, 124 Stat. 2546.

increase the net worth threshold.⁶⁵ The second category—legislation intended to restrict the participation of certain populations in the 8(a) Program—includes measures that would subject firms owned by Alaska Native Corporations (ANCs) to the same eligibility and other requirements to which individually owned 8(a) firms are subject.⁶⁶ This legislation, which responds to the widely reported increase in federal contract dollars awarded to ANCs and their subsidiaries over the past decade,⁶⁷ would remove the alleged “special ... advantages”⁶⁸ that ANC-owned firms enjoy in contracting under Section 8(a) of the Small Business Act by

- amending the Alaska Native Claims Settlement Act so that ANCs would no longer be deemed to be socially or economically disadvantaged for purposes of Sections 7(j) and 8(a) of the Small Business Act;
- redefining “Indian tribe” for purposes of the 8(a) Program to exclude ANCs;
- prohibiting ANC-owned firms from receiving additional sole-source awards when the total amount of competitive and sole-source awards they have received in any year exceeds the total amount of competitive and sole-source awards that individually owned firms may receive (approximately \$100 million⁶⁹);
- prohibiting SBA from exempting ANC-owned firms from any time limitations on participation in the 8(a) Program to which individually owned 8(a) firms are subject;
- prohibiting ANCs from conferring eligibility to participate in the 8(a) Program on more than one firm at a time; and
- precluding ANC-owned 8(a) firms from acquiring ownership interests in other 8(a) firms that exceed the ownership interests that individually owned 8(a) firms may acquire.

⁶⁵ Expanding Opportunities for Small Businesses Act of 2011, H.R. 2921, §2 (extending the nine-year time limitation on 8(a) Program participation to 12 years and requiring SBA to develop a program to provide technical assistance to firms during the two-year post-eligibility period); Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, tit. 1, §102 (providing that the nine-year time limitation on program participation would not apply to small businesses that have not yet completed an 8(a) contract and providing that individuals with a net worth of up to \$1.5 million may be considered economically disadvantaged); Not Too Small to Succeed in Business Act of 2011, H.R. 3754, §3 (extending the nine-year limitation to 11 years and providing that individuals with a net worth of up to \$750,000 (\$2.25 million for continued eligibility) may qualify as economically disadvantaged).

⁶⁶ An Act to Eliminate the Preferences and Special Rules for Alaska Native Corporations under the Program under Section 8(a) of the Small Business Act, H.R. 598; S. 236. For further discussion of this legislation and the rules currently governing contracting with ANC-owned firms participating in the 8(a) Program, see CRS Report R40855, *Contracting Programs for Alaska Native Corporations: Historical Development and Legal Authorities*, by Kate M. Manuel, John R. Luckey, and Jane M. Smith.

⁶⁷ See, e.g., Federal Contracting, *supra* note 63, at 12 (reporting that obligations to ANC-owned firms increased from \$1.9 billion in FY2005 to \$4.7 billion in FY2010). Obligations to 8(a) firms overall increased during this period, from \$11.3 billion to \$18.8 billion, with obligations to tribally-owned firms (including ANC-owned firms) representing a 160% increase. Obligations to non-tribal 8(a) firms, in contrast, increased only 45%.

⁶⁸ Office of the Inspector General, Small Bus. Admin., Participation in the 8(a) Program by Firms Owned by Alaska Native Corporations (July 10, 2009), at pg. 2, available at http://www.sba.gov/sites/default/files/oig_reptbydate_july9-15_0.pdf.

⁶⁹ See 13 C.F.R. §124.519 (generally prohibiting 8(a) firms from receiving additional sole-source awards once they have received a combined total of competitive and sole-source awards in excess of \$100 million, in the case of firms whose size is based on their number of employees, or in excess of an amount equivalent to the lesser of (1) \$100 million or (2) five times the size standard for the industry, in the case of firms whose size is based on their revenues).

These changes would effectively bar ANC-owned firms from receiving sole-source awards valued in excess of \$4 million (\$6.5 million for manufacturing contracts) under the authority of Section 8(a) in circumstances when individually owned 8(a) firms cannot.⁷⁰ They would also require that all affiliations of ANC-owned firms count when the firms' size is determined.⁷¹ Were all affiliations counted, certain ANC-owned firms could be less likely to qualify as small and, thus, could potentially be excluded from the 8(a) Program.

Other legislative proposals would require disclosure of information about contracting with ANCs, either by imposing additional reporting obligations on ANCs, or by requiring SBA to include information regarding contracts with ANCs in certain reports to Congress.⁷²

HUBZone Program

Eligibility for the Historically Underutilized Business Zone (HUBZone) program has also been of interest to some Members of Congress and commentators recently because of reported fraud in the program, as well as the completion of the 2010 Census.⁷³ A series of GAO reports, published between 2008 and 2010, found that the HUBZone program was vulnerable to fraud,⁷⁴ prompting

⁷⁰ If such legislation were enacted, ANC-owned firms could still receive sole-source awards in the same circumstances when individually owned 8(a) firms may receive such awards, or under other authority. For example, they could be awarded sole-source contracts valued in excess of \$4 million (\$6.5 million for manufacturing contracts) under the authority of Section 8(a) of the Small Business Act if the contracting officer did not reasonably expect offers from at least two small businesses. *See generally* 15 U.S.C. §637(a)(1)(D)(i)(I). They could also be awarded sole-source contracts in any of the seven circumstances in which sole-sources awards are permitted under CICA (e.g., urgent and compelling circumstances, national security). 10 U.S.C. §2304(c)(1)-(7) (procurements of defense agencies) & 41 U.S.C. §3304(a)(1)-(7) (procurements of civilian agencies).

⁷¹ Currently, ANC-owned firms must qualify as small, under the SBA's size standards, in order to participate in the 8(a) Programs. However, certain affiliations are generally excluded when determining the size of some group-owned firms, including ANC-owned firms. 13 C.F.R. §124.109(c)(2)(iii) ("In determining the size of a small business concern owned by a socially and economically disadvantaged Indian tribe (or a wholly owned business entity of such tribe) for either 8(a) ... program entry or contract award, the firm's size shall be determined independently without regard to its affiliation with the tribe, any entity of the tribal government, or any other business enterprise owned by the tribe, unless the Administrator determines that one or more such tribally-owned business concerns have obtained, or are likely to obtain, a substantial unfair competitive advantage within an industry category."). As used here, "Indian tribe" includes Alaska Native Corporations.

⁷² An Act to Eliminate the Preferences and Special Rules for Alaska Native Corporations under the Program under Section 8(a) of the Small Business Act, H.R. 598; S. 236, §7 (requiring ANCs to report annually to SBA on their total revenue, the amount of this revenue attributable to the 8(a) Program, and the total amount of benefits paid to shareholders); Government Efficiency through Small Business Contracting Act of 2012, H.R. 3850, §3 (requiring, among other things, that SBA report annually to Congress information about contracting with ANCs by the federal government and individual agencies in an annual report on the goaling program). SBA itself imposed certain reporting requirements on ANC-owned firms by regulation in 2011. *See* Small Bus. Admin., Small Business Size Regulations; 8(a) Business Development/Small Disadvantaged Business Status Determinations: Final Rule, 76 *Federal Register* 8222 (February 11, 2011). However, implementation of this requirement has been delayed so SBA could conduct tribal consultations. *See* Small Bus. Admin., 60 Day Notice and Request for Comments, 76 *Federal Register* 63983 (October 14, 2011); Small Bus. Admin., Notice of Tribal Consultations, 76 *Federal Register* 27859 (May 13, 2011); Small Bus. Admin., Notice of Tribal Consultations, 76 *Federal Register* 12273 (March 7, 2011).

⁷³ For more on the HUBZone program, see generally CRS Report R41268, *Small Business Administration HUBZone Program*, by Robert Jay Dilger.

⁷⁴ *See* Gov't Accountability Office, Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse, GAO-10-759 (July 28, 2010); Gov't Accountability Office, HUBZone Program: Fraud and Abuse Identified in Four Metropolitan Areas, GAO-09-440 (March 25, 2009); Gov't Accountability Office, Small Business Administration: Additional Actions Are Needed to Certify and Monitor HUBZone Businesses and Assess Program Results, GAO-08-643 (July 16, 2008).

interest among some Members in measures that would ensure only eligible firms participate in the program. More recently, the release of the results of the 2010 decennial census has prompted similar interest among some Members in measures that would allow firms that lose their HUBZone status because of the 2010 census to continue participating in the HUBZone program for a limited time. For many firms, eligibility for the HUBZone program is based upon census results.⁷⁵ The Small Business Act limits eligibility for the HUBZone program to firms whose principal office is located in a HUBZone and at least 35% of whose employees reside in a HUBZone, among other things.⁷⁶ HUBZones include “qualified census tracts,” as that term is defined in 26 U.S.C. Section 42(d)(5)(C)(ii),⁷⁷ and qualified nonmetropolitan counties, or counties in which

(i) the median household income is less than 80 percent of the nonmetropolitan State median household income, *based on the most recent data available from the Bureau of the Census of the Department of Commerce*, (ii) the unemployment rate is not less than 140 percent of the average unemployment rate for the United States or for the State in which such county is located, whichever is less, based on the most recent data available from the Secretary of Labor, or (iii) there is located a difficult development area, as designated by the Secretary of Housing and Urban Development in accordance with section 42(d)(5)(C)(iii) of title 26, within Alaska, Hawaii, or any territory or possession of the United States outside the 48 contiguous States.⁷⁸

Also included are “redesignated areas,” or areas that ceased to qualify as census tracts or nonmetropolitan counties, but were allowed to remain HUBZones until the later of (1) the date on which the Census Bureau publicly released the first results from the 2010 decennial census, or (2) three years after the date on which the census tract or nonmetropolitan county ceased to qualify.⁷⁹ SBA has stated that, for purposes of the HUBZone program, the Census Bureau released the first results of the 2010 census on October 1, 2011.⁸⁰

Legislation has been introduced in the 112th Congress that addresses both reported fraud in the HUBZone program and the loss of HUBZone status by certain firms due to the 2010 census. Among the former are bills that would require SBA to (1) ensure the HUBZone map is kept current; (2) implement policies to prevent unqualified businesses from participating in the program; (3) ensure timely processing of HUBZone applications; and (4) report to Congress on

⁷⁵ 15 U.S.C. §632(p) (defining HUBZones and HUBZone small businesses, among other things). For a few firms, eligibility for the HUBZone program is not tied to the census because these firms are located in “base closure areas,” or lands within the external boundaries of a military installation that was closed through a privatization process under the authority of various Base Realignment and Closure (BRAC) or similar laws. *See* 15 U.S.C. §632(p)(4)(D).

⁷⁶ 15 U.S.C. §632(p)(3) & (5). *See also* *Mission Critical Solutions v. United States*, 96 Fed. Cl. 657 (2011) (upholding SBA’s interpretation of an SBA regulation as requiring that at least 35% of a firm’s employees must reside in a HUBZone both at the time the firm is certified as a HUBZone firm and at the time the firm is awarded a contract through the HUBZone program).

⁷⁷ Section 42(d)(5)(C)(ii) of Title 26 of the United States Code defines a “qualified census tract” as any census tract which is designated by the Secretary of Housing and Urban Development and, for the most recent year for which census data are available on household income in such tract, either in which 50 percent or more of the households have an income which is less than 60 percent of the area median gross income for such year or which has a poverty rate of at least 25 percent.”

⁷⁸ 15 U.S.C. §632(p)(4)(A)-(B).

⁷⁹ 15 U.S.C. §632(p)(4)(C).

⁸⁰ Small Bus. Admin., *HUBZone: Latest News and Articles*, available at <http://www.sba.gov/content/hubzone-latest-news-and-articles> (“[A]ll Redesignated HUBZones due to expire on the date on which the census bureau publicly releases the first results from the 2010 decennial census are expiring effective[] 10/1/2011.”).

the efficacy of the program, or develop measures and implement plans to assess its effectiveness.⁸¹ Among the latter are measures that would extend the period during which redesignated areas continue to qualify until the later of three years after the date on which the SBA publishes a HUBZone map based on the 2010 census results, or three years after the date on which the area ceased to qualify.⁸² Other legislative proposals would require the Secretary of Housing and Urban Development (HUD) to designate HUBZones based on the new census data within a specified time frame,⁸³ or would designate a particular county as a HUBZone for a specified time period.⁸⁴ The latter types of provisions are arguably particularly significant because, while SBA currently has considerable discretion in how it implements the HUBZone program (e.g., how often the HUBZone map is updated), it arguably does not have any discretion in which areas qualify as HUBZones. The Small Business Act defines “HUBZones” by reference to other categories (e.g., qualified census tracts) whose composition is determined by other agencies.

Legislation has also been introduced in the 112th Congress that would amend the definition of “HUBZone small business” given in Section 3 of the Small Business Act to include firms that are wholly owned by one or more Native Hawaiian Organizations, or partially owned by such an organization (or a corporation wholly owned by such an organization) if all other owners are U.S. citizens or small businesses.⁸⁵ The proposed provisions parallel those that presently address small businesses owned by Alaska Native Corporations, Indian tribal governments, and Community Development Corporations.⁸⁶ Small businesses owned by these various types of entities have, at times, been subject to different treatment under the Small Business Act,⁸⁷ and the proposed legislation appears intended to remove one such difference.

Subcontracting Plans

The Small Business Act has long required agencies to take various steps to promote subcontracting with small businesses. Among other things, they have been required since 1978 to incorporate “subcontracting plans” in certain prime contracts, and to establish goals regarding the

⁸¹ Small Business Contracting Fraud Prevention Act of 2011, S. 633, §6; SUCCESS Act of 2012, S. 3442, §526 (same); HUBZone Qualified Census Tract Act of 2011, S. 1874, §3 (requiring SBA to submit, within one year of the act’s enactment, a report to Congress that describes the benefits and drawbacks of using qualified census tract data to designate HUBZones, describes any problems encountered in using qualified census tract data to designate HUBZones, and includes recommendations for ways to improve the process of designating HUBZones).

⁸² Protect HUBZones Act of 2011, H.R. 2131, §2; HUBZone Protection Act of 2011, S. 1756, §2; Small Business Contracting Fraud Prevention Act of 2011, S. 633, §6; SUCCESS Act of 2012, S. 3442, §526.

⁸³ HUBZone Qualified Census Tract Act of 2011, S. 1874, §2 (imposing deadlines on the HUD Secretary to identify and publish the list of qualifying census tracts under 26 U.S.C. §42 and to designate a date within 3 months of the publication of the list upon which the list becomes effective for areas that qualify as HUBZones).

⁸⁴ Monroe County HUBZone Extension Act of 2011, H.R. 2416, §2 (designating Monroe County, Pennsylvania, as a HUBZone until October 1, 2014); Monroe County HUBZone Act of 2011, S. 976, §2 (same); Shuttle Workforce Revitalization Act of 2012, S. 2157, §3 (designating Brevard County, Florida, a HUBZone through at least January 1, 2020, due to the “significant economic hardship” caused by the termination of the Space Shuttle program).

⁸⁵ Native Hawaiian HUBZone Opportunity Act of 2012, H.R. 5729, §2.

⁸⁶ 15 U.S.C. §632(p)(3)(B)-(D).

⁸⁷ See CRS Report R40744, *The “8(a) Program” for Small Businesses Owned and Controlled by the Socially and Economically Disadvantaged: Legal Requirements and Issues*, by Kate M. Manuel and John R. Luckey, at Appendix.

percentage of agency subcontract dollars awarded to small businesses.⁸⁸ Nonetheless, despite these provisions, concerns about subcontracting have persisted, in part because the government has historically failed to meet its goals for the percentage of federal contract and subcontract dollars awarded to small businesses,⁸⁹ and in part because of alleged mistreatment of small business subcontractors by agency prime contractors.⁹⁰ In response to such concerns, the 111th Congress amended Section 8(d) of the Small Business Act to require that agencies incorporate in their prime contracts terms obligating the contractor to

- make a “good faith effort” to acquire goods and services (including construction work) from the small businesses whom it “used” in preparing and submitting the bid or proposal, “in the same amount and quantity used in preparing and submitting the bid or proposal,”⁹¹ and
- notify the contracting officer in writing if it pays a reduced price to a subcontractor for completed work, or if payment to a subcontractor is more than 90 days past due for goods or services for which the government has paid the contractor.⁹²

Although SBA is still in the process of implementing the changes made by the 111th Congress, Members of the 112th Congress have proposed additional legislation addressing subcontracting plans. Among other things, these measures would (1) hold prime contractors accountable for failure to report their subcontracting activities;⁹³ (2) require withholding of a certain percentage of

⁸⁸ An Act to Amend the Small Business Act and the Small Business Investment Act of 1958, P.L. 95-507, §§211 & 221, 92 Stat. 1768-69, 1770 (codified, as amended, at 15 U.S.C. §§637(d) & 644(g)(2)).

⁸⁹ See, e.g., Federal Government Misses Small Business Contracting Goal, *supra* note 29.

⁹⁰ See, e.g., *Are Government Purchasing Policies Failing Small Businesses? A Roundtable before the Committee on Small Business and Entrepreneurship, 107th Cong., 2d sess.* (June 19, 2002) (discussing, *inter alia*, the problems faced by small business subcontractors).

⁹¹ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1322, 124 Stat. 2540-41 (codified at 15 U.S.C. §637(d)(6)(G)(i)). If the contractor fails to do so, it must provide the contracting officer with a written explanation. 15 U.S.C. §637(d)(6)(G)(i). SBA recently proposed regulations implementing this provision. Among other things, these regulations provide that a prime contractor would be said to have “used” a small business in preparing its bid or proposal only if (1) it referenced the small business as a subcontractor in its bid or proposal; (2) it has a subcontract or agreement in principle to subcontract with the small business to perform a portion of the specific contract; or (3) the small business drafted part of the bid or proposal, or the offeror used the small business’s pricing or cost information, or technical expertise, in preparing the bid or proposal, and there was an “intent or understanding that the small business concern will be awarded a subcontract for the related work if the offeror is awarded the contract.” Small Bus. Admin., Small Business Subcontracting: Proposed Rule, 76 *Federal Register* 61626, 61631 (October 5, 2011); Small Bus. Admin., Small Business Subcontracting: Proposed Rule; Reopening of the Comment Period, 76 *Federal Register* 74749 (December 1, 2011) (extending the comment period on the proposed regulation through January 6, 2012). Assuming this regulation, with its arguably narrow definition of when a prime contractor could be said to have “used” a small business in preparing its bid or proposal, is adopted, concerns about “bait and switch” by prime contractors could persist despite the enactment of the Small Business Jobs Act. Contractors are commonly said to have engaged in “bait and switch” when they represent to agencies in their bids or proposals that they will subcontract particular work to small businesses, but ultimately subcontract that work to other firms.

⁹² P.L. 111-240, tit. I, subtitle C, §1334, 124 Stat. 2542-43 (codified at 15 U.S.C. §637(d)(12)). The act also requires contracting officers to consider the “unjustified failure” of a prime contractor to make full or timely payment to a subcontractor when evaluating the contractor’s performance. *Id.*

⁹³ Subcontracting Transparency and Reliability Act of 2012, H.R. 3893, tit. II, §201 (requiring that subcontracting plans include assurances that the contractor will submit periodic reports on its subcontracting activities, and providing that failure to provide the requisite assurances constitutes a material breach of the contract); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1655 (same). These measures would also authorize SBA procurement center representatives (PCRs) and commercial market representatives (CMRs) to delay for up to 30 days (continued...)

the contract price if the contractor fails to achieve certain goals in its subcontracting plan;⁹⁴ and (3) require that contractors who fail to notify small businesses identified as potential subcontractors in their bids or proposals be fined a percentage of the contract price.⁹⁵ Each of these proposals is arguably an expansion upon current law, which requires that contractors report on their performance in subcontracting semiannually during contract performance,⁹⁶ but provides only that failure to make a “good faith effort” to comply with subcontracting-plan goals could subject the contractor to liquidated damages.⁹⁷ However, if enacted, certain proposals could raise issues of contract and/or constitutional law. Contract law generally permits parties to agree upon liquidated damages in cases where the injury caused by the breach is uncertain or difficult to quantify.⁹⁸ The imposition of liquidated damages to “punish” a party for failure to perform under the contract, in contrast, is generally disfavored.⁹⁹ Thus, if contract provisions calling for withholding or liquidated damages were viewed as punitive, as opposed to *bona fide* attempts to quantify the damages for breach, they might not be enforced. Similarly, fining contractors for failure to meet goals or notify subcontractors could potentially be found to violate the Eighth Amendment of the U.S. Constitution. The Eighth Amendment prohibits the imposition of excessive fines,¹⁰⁰ and courts have found that “a punitive forfeiture violates the Excessive Fines Clause if it is grossly disproportional to the gravity of a defendant’s offense.”¹⁰¹ Thus, assuming a fine were seen as punitive, it could potentially be found unconstitutional if it is disproportionate to the offense in light of the extent of the harm, the gravity of the offense, the nature and extent of

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acceptance of subcontracting plans that they determine fail to provide the “maximum practicable opportunity” for small businesses to participate in the performance of the contract. PCRs and CMRs currently do not have the authority to delay a contract award because of concerns about the subcontracting plan. Agencies may not award a contract until there is a subcontracting plan that is acceptable to the contracting officer. *See* 15 U.S.C. §637(d)(4)(C); 15 U.S.C. §637(d)(5)(B).

⁹⁴ Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, §106 (requiring withholding of not less than \$5,000 on contracts valued at or below \$100,000; 3% of the contract price on contracts valued between \$100,000 and \$5 million; and 5% of the contract price on contracts valued in excess of \$5 million, if the contractor fails to meet its goals for subcontracting with small disadvantaged businesses).

⁹⁵ An Act to Require Contractors to Notify Small Business Concerns that Have Been Included in Offers Relating to Contracts Let by Federal Agencies and for Other Purposes, S. 370 (subjecting contractors that fail to provide written notice to potential subcontractors on certain procurements be fined an amount equal to 20% of the contract value, for a first offense; fined 50% of the contract value and debarred for one year for a second offense; and debarred for a third or subsequent offense). No term of debarment is proposed for third or subsequent offenses, perhaps suggesting that any such debarment is intended to be permanent.

⁹⁶ 48 C.F.R. §19.704(a)(10)(A) (Individual Subcontract Reports (ISRs) to be submitted semiannually during contract performance for the periods ending March 31 and September 30). ISRs are also required for each contract within 30 days of completion. In addition, contractors are required to submit Summary Subcontract Reports (SSRs) within specific time periods that vary depending upon the identity of the contracting agency. *See* 48 C.F.R. §19.704(a)(10)(B).

⁹⁷ 48 C.F.R. §19.705-7(b). *See also* 15 U.S.C. §637(d)(4)(F); 48 C.F.R. §19.702(c). Liquidated damages are damages whose amount was agreed upon, as compensation for specific breaches, by the parties at the time of the contract’s formation.

⁹⁸ *See, e.g.,* *Wise v. United States*, 249 U.S. 361, 365-66 (1919). It is “customary, where Congress has not adopted a different standard, to apply to the construction of government contracts the principles of general contract law. That has been done in other cases where the Court has considered the enforceability of ‘liquidated damages’ provisions in government contracts.” *Priebe & Sons, Inc. v. United States*, 332 U.S. 407, 411 (1947) (holding that a provision calling for the imposition of liquidated damages in a contract of the Federal Surplus Commodities Program constituted an unenforceable penalty). *See also* *M. Maropakis Carpentry, Inc. v. United States*, 84 Fed. Cl. 182 (2008) (finding that the liquidated damages provision was enforceable because the plaintiff failed to prove that it was a penalty).

⁹⁹ *See, e.g., Priebe & Sons*, 332 U.S. at 412-13.

¹⁰⁰ U.S. Const. amend. VIII.

¹⁰¹ *United States v. Bajakajian*, 524 U.S. 321, 334 (1988).

the offense, and the availability of other penalties.¹⁰² Equal protection issues could also be raised if the penalties were so severe that the goals for subcontracting with minority- or women-owned small businesses, in particular, were seen as tantamount to quotas.¹⁰³

Limitations on Subcontracting

Congress originally imposed “limitations on subcontracting” upon 8(a) firms in 1986 in order to ensure that small businesses participating in the 8(a) Program developed capacity to perform as federal or other contractors.¹⁰⁴ Because of these limitations, 8(a) firms are required to perform at least 50% of the cost of contracts for services (excluding construction) with their own personnel, and at least 50% of the cost (excluding materials) of contracts for goods.¹⁰⁵ Similar requirements were imposed upon other contracts awarded under the authority of the Small Business Act in 1987,¹⁰⁶ and also in 1987, SBA promulgated limitations on subcontracting for construction contracts, requiring firms to perform at least 15% of the cost (excluding materials) of general construction, and 25% of the cost (excluding materials) of construction by special trade contractors.¹⁰⁷ These statutory and regulatory provisions have not been changed since 1987, although amendments have periodically been proposed because of concerns about “pass through” contracts.¹⁰⁸ In particular, Members of the 112th Congress have proposed legislation that would restate how these limitations are expressed—in terms of the amount paid under the contract instead of the costs of performing the contract¹⁰⁹—in the hopes of “ensur[ing] that small

¹⁰² See, e.g., *United States v. 3814 NW Thurman St., Portland, Or.*, 164 F.3d 1191, 1197-98 (9th Cir. 1999) (citing *Bajakajian*, 524 U.S. at 336-39).

¹⁰³ See, e.g., *City of Richmond*, 488 U.S. 469 (holding that a municipal ordinance requiring the city’s prime contractors to award at least 30% of the value of each contract to minority subcontractors was unconstitutional); *DynaLantic Corp.*, 2012 U.S. Dist. LEXIS 114807, at *10 (upholding the 8(a) Program against a facial challenge, in part, because federal goals for contracting with minority-owned small businesses are aspirational, and there are no penalties for failure to meet the goals).

¹⁰⁴ An Act to Authorize Appropriations for Fiscal Year 1987 for Military Activities of the Department of Defense, for Military Construction, and for Defense Activities of the Department of Energy, to Prescribe Personnel Strengths for Such Fiscal Year, to Improve the Defense Acquisition Process, and for Other Purposes, P.L. 99-661, §921, 100 Stat. 3927 (November 14, 1986) (codified, as amended, in 15 U.S.C. §637(a)).

¹⁰⁵ 15 U.S.C. §637(a)(14)(A)(i)-(ii) (limitations on subcontracting for 8(a) firms).

¹⁰⁶ An Act to Make Technical Corrections in Certain Defense-Related Laws, P.L. 100-26, §10, 101 Stat. 288 (April 21, 1987) (codified, as amended, in 15 U.S.C. §644(o)(1)(A)-(B)).

¹⁰⁷ Small Bus. Admin., Small Business Size Standards, 52 *Federal Register* 32870 (August 31, 1987).

¹⁰⁸ Cf. Lars E. Anderson, Terry L. Elling, Michael W. Robinson, and Dismas Locaria, *GTSI’s Suspension Shows That Contractors Should Ensure Accurate Representations Concerning Small Business Matters*, 94 *Fed. Cont. Rep.* 414 (October 26, 2010) (reporting on a subcontractor that was suspended by SBA after it was discovered that it performed the majority of the work on a contract that had been set aside for and awarded to a small business). As used in this context, a “pass through” contract is one that is nominally held by a small business, but that is performed primarily by a firm that is other than small.

¹⁰⁹ See, e.g., Subcontracting Transparency and Reliability Act of 2012, H.R. 3893, §101 (adding a new Section 45 to the Small Business Act, which would provide that a small business may not expend on subcontractors more than (1) 50% of the amount paid to it under contracts for services (except construction); (2) 85% of the amount paid to it (minus the cost of materials) under contracts for construction; (3) 75% of the amount paid to it (minus the cost of materials) under contracts for construction by special trade contractors; and (4) 50% of the amount paid to it (minus the cost of materials) under contracts for supplies (other than from a regular dealer in such supplies)); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1651 (generally prohibiting a small business from expending on subcontractors more than 50% of the amount paid under contracts for services or supplies, but authorizing SBA to change these percentages if such a change is necessary to “reflect conventional industry practices”). (continued...)

businesses that get contracts are doing the bulk of the work, while making it easier to crack down on ‘deceptive large businesses hiding behind small businesses.’”¹¹⁰ This legislation would also authorize SBA to modify any statutory limitations on subcontracting if it determines that “such change is necessary to reflect conventional industry practices” for small businesses, and to apply similar percentages to other contracts not awarded under the authority of the Small Business Act.¹¹¹ This legislation would also provide that, in the event the limitations on subcontracting are exceeded, the contractor would be fined the greater of \$500,000, or the amount expended, in excess of permitted levels, on subcontractors.¹¹² The latter provision, in particular, could help address the recurring question, discussed below, of how to calculate the loss or damage to the government when a firm misrepresents its size or status for purposes of a federal contract or subcontract by providing an explicit measure of such loss or damage.¹¹³ However, potential constitutional issues could be raised if the fine were seen as punitive and the amount of the fine were seen as disproportionate to the offense.¹¹⁴

Payment

Because small businesses can be more vulnerable to changes in capital flow than large ones, payment of small businesses by federal agencies and prime contractors has long been of concern to Members of Congress and commentators.¹¹⁵ The Prompt Payment Act of 1982 requires that federal agencies pay interest on payments not made to contractors by the date specified in the contract, or within 30 days of receipt of a “proper invoice.”¹¹⁶ Amendments made to the Prompt Payment Act in 1988 extended these protections to certain subcontractors by requiring agencies to include in their construction contracts terms obligating the contractor (1) to pay the subcontractor

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The latter measure would also allow SBA to establish limitations on subcontracting for construction contracts through a notice-and-comment process.

¹¹⁰ See, e.g., Charles S. Clark, House Republican Seeks to Curb “Deceitful” Subcontracting, *Govt. Exec.*, February 2, 2012, available at <http://www.govexec.com/contracting/2012/02/house-republican-seeks-curb-deceitful-subcontracting/41074/>. However, some commentators have questioned the practical effects of such a change. See, e.g., Deborah Billings, House Bill Seeks to Ensure Set Asides Largely Performed by Small Business Subs, *97 Fed. Cont. Rep.* 113 (February 7, 2011).

¹¹¹ This latter provision would effectively overturn the GAO’s decision in *Washington-Harris Group*. See Comp. Gen. December No. B-401794; B-401794.2, 2009 U.S. Comp. Gen. LEXIS 226 (November 16, 2009) (finding that the limitations on subcontracting provided for in the Small Business Act and SBA regulations do not apply to contracts awarded under other authority). For more on this decision, see generally CRS Report R40998, *The Inapplicability of Limitations on Subcontracting to “Preference Contracts” for Small Businesses: Washington-Harris Group*, by Kate M. Manuel.

¹¹² Subcontracting Transparency and Reliability Act of 2012, H.R. 3893, §102; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1652.

¹¹³ See *infra* note 214 and accompanying text.

¹¹⁴ See *supra* notes 100-102 and accompanying text.

¹¹⁵ See, e.g., *Payment Practices of the Defense Commissary Agency: Hearing of the House Committee on Armed Services, 102nd Cong., 2d Sess.* (June 11, 1992).

¹¹⁶ P.L. 97-177, 96 Stat. 85 (May 21, 1982) (codified, as amended, at 31 U.S.C. §§3901-3907). Among other things, a proper invoice contains (1) the name of the contractor, the invoice date, and the contract number; (2) a description of the goods rendered and the shipping and payment terms; (3) other substantiating documentation or information required under the contract; and (4) the name, title, telephone number, and complete mailing address of the person to whom payment should be sent. 31 U.S.C. §3903(a)(1)(A)-(B). The interest rate to be used is that determined by the Secretary of the Treasury twice a year under the Contract Disputes Act. See 31 U.S.C. §3902(a).

for “satisfactory performance” under the subcontract within seven days of receiving payment from the agency, and (2) to pay interest on any amounts that are not paid within the proper time frame.¹¹⁷ Like the original Prompt Payment Act, the 1988 amendments effectively protect small businesses even though the legislation does not specifically mention them. Small business subcontractors are especially prevalent in the construction industry.¹¹⁸

Concerns about payment of small businesses generally, and of small business subcontractors in particular, were widespread during the recession of 2008-2009. Partly in response to such concerns, the 111th Congress enacted legislation addressing the payment of small business *subcontractors*. This legislation requires that prime contractors notify the contracting officer whenever payment to a small business subcontractor is late or withheld,¹¹⁹ as well as authorizes the contracting officer to consider the contractor’s failure to make full or timely payment to subcontractors when evaluating the contractor’s performance.¹²⁰ In addition, SBA is apparently considering requiring prime contractors who fail to meet their obligations in paying subcontractors to enter into “funds control agreements” with neutral third parties.¹²¹ The Obama Administration has also issued guidance addressing the payment of small business contractors and subcontractors. Initially, this guidance called for agencies to pay small business *contractors* within 15 days of receipt of a proper invoice.¹²² However, subsequent guidance sought to address payment of small business *subcontractors* by calling for agencies to “temporarily accelerate payments to all prime contractors, in order to allow them to provide prompt payments to small business subcontractors.”¹²³ In neither case are agencies required to pay interest on payments not made within the proposed time frames, unlike with “late” payments under the Prompt Payment Act.

Legislation has also been introduced in the 112th Congress that would similarly direct agencies to pay small business *contractors* “as quickly as possible after invoices and all proper documentation, including acceptance, are received and before normal payment due dates established in the contract.”¹²⁴ However, like the Obama Administration’s guidance, this measure contains no explicit sanctions for failure to pay in accordance with the policy (e.g., required interest payments).

¹¹⁷ P.L. 100-496, §9, 102 Stat. 3460-63 (October 17, 1988) (codified at 31 U.S.C. §3905(b)(1)-(2)). A subcontractor’s work may generally be said to be satisfactory if the “property and services received conform to the requirements of the contract.” See *New York Guardian Mortg. Corp. v. United States*, 916 F.2d 1558, 1560 (Fed. Cir. 1990).

¹¹⁸ See, e.g., *Prompt Payment Act Amendments of 1988: Hearing of the House Committee on Government Operations, 100th Cong., 2d Sess.*, at 26 (1988) (reporting that subcontractors perform 80% of the work on construction projects, and generally do not get paid until after the prime contractor has been paid).

¹¹⁹ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1334, 124 Stat. 2542-43 (codified at 15 U.S.C. §637(d)(12)).

¹²⁰ *Id.*

¹²¹ 76 *Federal Register* at 61628.

¹²² Exec. Office of the President, Office of Mgmt. & Budget, Accelerating Payments to Small Businesses for Goods and Services, September 14, 2011, available at <http://www.whitehouse.gov/sites/default/files/omb/memoranda/2011/m11-32.pdf>.

¹²³ Exec. Office of the President, Office of Mgmt. & Budget, Providing Prompt Payment to Small Business Subcontractors, July 11, 2012, available at <http://www.whitehouse.gov/sites/default/files/omb/memoranda/2012/m-12-16.pdf>.

¹²⁴ Acquisition Savings Reform Act of 2011, S. 1736, §12 (directing the FAR Council to amend the FAR to “reflect that governmentwide policy is to assist small business concerns by paying them as quickly as possible after invoices and all proper documentation, including acceptance, are received and before normal payment due dates established in the contract”).

Surety Bonds

SBA administers a surety bond guarantee program,¹²⁵ designed to encourage sureties to issue bonds when they would otherwise determine that a small business presents an unacceptable degree of risk. Under the program, SBA may guarantee bid, performance, and payment bonds for individual contracts of \$2 million or less for small businesses that cannot obtain surety bonds through regular commercial channels.¹²⁶ The guarantee ranges from 70% to 90% of the surety's loss if a default occurs.¹²⁷

Recent congressional interest in the surety bond guarantee program has focused primarily on ensuring that small businesses have the means to secure surety bonds needed to compete for contracts during the economic downturn.¹²⁸ The American Recovery and Reinvestment Act of 2009 (ARRA)¹²⁹ temporarily increased, from February 17, 2009, through September 30, 2010, the maximum bond amount from \$2 million to \$5 million, and allowed the amount to increase to \$10 million if a federal contracting officer certified that the larger guarantee was "necessary." ARRA also temporarily modified the program's size standards so that a business would be eligible for the program if it (and its affiliates) did not exceed the size standard for the primary industry in which the business was engaged.¹³⁰ This provision effectively increased the program's size standard for certain industries, and thus allowed more businesses to qualify for the program. Using its rulemaking authority, the SBA subsequently made ARRA's temporary size standard permanent.¹³¹

Some Members of the 112th Congress have introduced legislation that would reinstate the ARRA increases to the maximum bond amount, with some provisions doing so permanently and others, temporarily.¹³² Such legislation would arguably be necessary to increase the maximum bond

¹²⁵ 15 U.S.C. §694b. For more information on the Surety Bond Guarantee Program, see CRS Report R42037, *SBA Surety Bond Guarantee Program*, by Robert Jay Dilger. For these purposes, a surety bond is an instrument between a surety, a contractor, and a project owner, under which the surety assumes the contractor's responsibilities to ensure that the project is completed in the event the contractor is unable to successfully perform the contract.

¹²⁶ See 15 U.S.C. §694b(a)(1).

¹²⁷ See 15 U.S.C. §694b(c).

¹²⁸ See, e.g., 155 Cong. Rec. S1486 (daily ed. February 4, 2009) (statement by Sen. Snowe) (temporarily increasing the bond limit is necessary to "ensure that small businesses are able to secure the surety bonds they need to compete for contracts, grow, and hire more employees" and, that "in our current economic recession, small businesses are finding it even more difficult to secure the credit lines necessary to get bonds in the private sector"); 155 Cong. Rec. S2283 (daily ed. February 13, 2009) (statement by Sen. Cardin) (temporarily increasing the bond limit would create "significant opportunities to create jobs now in which small businesses will participate and be the driving engine for creation of new jobs in our country").

¹²⁹ P.L. 111-5, tit. II, §508, 123 Stat. 158-59 (February 17, 2009).

¹³⁰ P.L. 111-5, tit. II, §508(c), 123 Stat. 153-54.

¹³¹ See Small Bus. Admin., Surety Bond Guarantee Program; Size Standards: Direct Final Rule, 76 *Federal Register* 48549, 48550 (August 11, 2010) (codified at 13 C.F.R. §121.301(d)(2)).

¹³² Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, tit. I, §103 (permanently increasing the maximum bond amount to \$5 million and authorizing SBA to guarantee a bond of up to \$10 million if a federal contracting officer certifies that a larger guarantee is necessary); American Jobs Act of 2011, H.R. 12; S. 1549; S. 1660, tit. I, Subtitle B, §112 (temporarily increasing the \$2 million threshold to \$5 million until September 30, 2012, and appropriating \$3 million in additional funding); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1695 (permanently increasing the maximum bond amount to \$6.5 million, as adjusted for inflation, and authorizing SBA to guarantee a bond of up to \$10 million if a federal contracting officer certifies that a larger guarantee is necessary); A Bill to Remove the Sunset Date for Amendments to the Small Business Investment (continued...)

amount. SBA was able to increase the size standards for certain industries within the surety bond guarantee program by regulation¹³³ only because of its broad statutory authority over such standards. It lacks similar authority over the maximum bond amounts, which are prescribed by statute.

Bundling and Consolidation

The way in which agencies structure their requirements can have significant implications for small businesses. When multiple requirements are grouped into a single contract, that contract may be difficult, or impossible, for small businesses to perform. For this reason, Congress has enacted progressively more stringent limitations upon the “bundling” and “consolidation” of requirements by federal agencies. First, in 1997, Congress amended the Small Business Act to define “bundling” as

consolidat[ing] 2 or more procurement requirements for goods or services *previously provided or performed under separate smaller contracts* into a solicitation of offers for a single contract that is likely to be unsuitable for award to a small business concern due to— (A) the diversity, size, or specialized nature of the elements of performance specified; (B) the aggregate dollar value of the anticipated award; (C) the geographical dispersion of the contract performance sites; or (D) any combination of the factors described in subparagraphs (A), (B), and (C),

and to require agencies to take certain steps to ensure that any bundling that they engage in is “necessary and justified.”¹³⁴ Then, in 2003, Congress amended the Armed Services Procurement Act (ASPA) to prohibit defense agencies from executing any acquisition strategy that includes a “consolidation” of contract requirements valued in excess of \$6 million¹³⁵ without first (1) conducting market research, (2) identifying any alternative contracting approaches that would involve a lesser degree of consolidation of contract requirements, and (3) determining that the consolidation is necessary and justified.¹³⁶ Finally, in 2010, Congress imposed similar restrictions

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Act of 1958, and for Other Purposes, S. 2187, §1 (permanently increasing the maximum bond amount to \$5 million); SUCCESS Act of 2012, S. 3442, §511 (same).

¹³³ See *supra* note 130.

¹³⁴ Small Business Reauthorization Act of 1997, P.L. 105-135, §§411-417, 111 Stat. 2617-20 (December 2, 1997) (codified, as amended, in 15 U.S.C. §631, §632, and §644) (emphasis added). Specifically, the 1997 act (1) requires agencies to conduct market research to determine whether consolidation of requirements is “necessary and justified” before proceeding with an acquisition strategy that could lead to a contract containing consolidated requirements; (2) establishes factors that agencies may consider in determining whether consolidation is necessary and justified; and (3) generally prohibits agencies from relying on reductions in administrative or personnel costs alone as a justification for bundling contract requirements. The 1997 act also requires that, when a proposed procurement involves “substantial bundling,” the agency identify the benefits to be derived from bundling; assess the impediments to small businesses’ participation as prime contractors that result from bundling and specify actions designed to maximize small business participation as subcontractors and/or suppliers; and determine that the anticipated benefits of the bundled contract justify its use. For more on bundling and consolidation, discussed below, see generally CRS Report R41133, *Contract “Bundling” Under the Small Business Act: Existing Law and Proposed Amendments*, by Kate M. Manuel.

¹³⁵ The statute imposes limitations upon consolidation of requirements valued in excess of \$5 million. See 10 U.S.C. §2382(a)(1). However, this amount has been increased to \$6 million by regulation, pursuant to the Ronald W. Reagan National Defense Authorization Act for FY2005. See P.L. 108-375, §807, 118 Stat. 2010-11 (October 28, 2004); 48 C.F.R. §207-170-3(a).

¹³⁶ National Defense Authorization Act for FY2004, P.L. 108-136, div. A, tit. VIII, §801(a)(1), 117 Stat. 1538 (continued...)

upon the “consolidation” of requirements valued in excess of \$2 million by non-defense agencies.¹³⁷ However, concerns that agencies’ bundling or consolidation of contract requirements limit opportunities for small businesses to perform as federal contractors have persisted despite these amendments to the Small Business Act, in large part because of how “bundling” and “consolidation” are defined in federal law. These definitions currently encompass only requirements that were previously provided or performed under separate smaller contracts, and some federal agencies have sought to defend challenged procurements by arguing that requirements for construction are, *per se*, new requirements.¹³⁸ Some agencies have also asserted that adding a new requirement to requirements previously performed means there is no bundling.¹³⁹

Members of the 112th Congress have introduced legislation that would apparently preclude such arguments by amending the definition of “bundling” to include construction, and by specifying that a

combination of contract requirements that would meet the definition of a bundling of contract requirements but for the addition of a procurement requirement with at least 1 new good or service shall be considered to be a bundling of contract requirements unless the new features or functions substantially transform the goods or services and will provide measurably substantial benefits to the Federal Government in terms of quality, performance, or price.¹⁴⁰

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(November 24, 2003) (codified, as amended, in 10 U.S.C. §2382). The 2004 act defined “consolidation” as the “use of a solicitation to obtain offers for a single contract or a multiple award contract to satisfy two or more requirements ... that have previously been provided ... or performed ... under two or more separate contracts smaller in cost than the total cost of the contract for which the offers are solicited.” 10 U.S.C. §2382(c)(1) (emphasis added).

¹³⁷ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1313, 124 Stat. 2538-39 (codified at 15 U.S.C. §657q). These provisions of the Small Business Jobs Act also apply to defense agencies until the Small Business Administration determines they are “in compliance with the ... contracting goals under section 15” of the Small Business Act. In addition, the Small Business Jobs Act amended Section 15 of Small Business Act (which governs bundling, but not consolidation) to require (1) agencies to include in solicitations for multiple-award contracts valued in excess of the simplified acquisition threshold a provision inviting bids from small businesses or joint ventures of small business concerns; (2) the FAR Council to establish a government-wide policy on bundling to be published on each agency’s website; (3) agencies to publish on their websites listings of and rationales for any bundled contracts; and (4) the Administrator of SBA to report periodically to Congress on procurement center representatives (PCRs) and commercial market representatives (CMRs). P.L. 111-240, tit. I, subtitle C, §1312, 124 Stat. 2537. PCRs and CMRs are tasked with detecting and mitigating the effects of bundled procurements.

¹³⁸ *See, e.g., Tyler Construction Group v. United States*, 83 Fed. Cl. 94, 100-01 (2008).

¹³⁹ *See, e.g., Nautical Engineering, Inc., B-309955* (November 7, 2007) (agency asserting that there was no bundling because of the addition of a new requirement, planning services, to the admittedly consolidated requirements pertaining to drydock and dockside maintenance and repair).

¹⁴⁰ Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, §104. This measure would also define “separate smaller contract” to mean a “contract or order that has been performed by 1 or more small business concerns or was suitable for award to 1 or more small business concerns.” *Id.* However, it would exempt larger contracts (valued at up to \$5 million) from its requirements than the Small Business Jobs Act does (\$2 million). *See also* Contractor Opportunity Protection Act of 2012, H.R. 4081, §3 (amending Section 44 of the Small Business Act, which governs consolidation, to include a definition of “bundling of contract requirements” that encompasses “the use of any bundling methodology to satisfy 2 or more procurement requirements for new or existing goods or services provided to or performed for the Federal agency, including any construction services, that is likely to be unsuitable for award to a small business concern.”); National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1671 (same). This legislation would repeal the existing provisions regarding bundling in Section 15 of the act, and amend the provisions currently in Section 44, which address consolidation, so that they address bundling. The legislation also apparently provides that bundling-related restrictions apply to proposed procurements that would, (continued...)

This legislation would also authorize SBA to delay the issuance of a solicitation for up to 10 days to make recommendations whenever SBA and the procuring agency disagree as to the existence or extent of bundling. This time period is arguably shorter than that provided for under current law.¹⁴¹ However, the procuring agency, not SBA, presently determines whether any such delay occurs.¹⁴² Other legislation would write into statute and arguably strengthen various responsibilities of Procurement Center Representatives (PCRs) and other small business advocates vis-à-vis bundled solicitations that are currently addressed primarily in regulations.¹⁴³ For example, this legislation would require procuring activities to provide a copy of the proposed procurement to the PCR at least 45 days prior to the issuance of a solicitation and explain, among other things, why construction cannot be procured as separate discrete projects.¹⁴⁴ This legislation would also authorize the Administrator of Small Business to file an appeal with the appropriate agency board of contract appeals (which generally hears disputes between agencies and contractors under existing contracts) whenever the Administrator and the agency fail to agree.¹⁴⁵

In addition, legislation has been introduced that would address bundling of requirements by the Department of Homeland Security (DHS). Because of DHS's previous reliance upon "lead systems integrators,"¹⁴⁶ there have been particular concerns about its bundling of requirements,¹⁴⁷ and recently introduced legislation would require GAO to include in its review of DHS's Secure Border Initiative a discussion of any bundling that limits the ability of small businesses to compete.¹⁴⁸ Any such review could result in findings that could inform future legislation.

(...continued)

among other things, "adversely affect one or more small business concerns, including the potential loss of an existing contract."

¹⁴¹ See, e.g., 48 C.F.R. §19.505 (generally providing for the issuance of a solicitation to be delayed for 15 days, so that SBA may make a written appeal to the secretary or agency head, who has 30 days to respond). The proposed legislation would also write into statute OMB's role in mediating bundling-related disagreements between procuring agencies and SBA, a role that is currently provided for in Executive Order 13170. See Executive Order 13170, Increasing Opportunities and Access for Disadvantaged Businesses, 65 *Federal Register* 60827, 60829 (October 12, 2000) (authorizing SBA or the procuring agency to "seek assistance" from the Office of Management and Budget (OMB) in cases where there is disagreement as to the existence or extent of bundling).

¹⁴² Compare Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, §104 with 48 C.F.R. §19.505(d) (authorizing procuring activities to proceed with disputed acquisitions if the contracting officer determines that proceeding to contract award and performance is "in the public interest").

¹⁴³ Contractor Opportunity Protection Act of 2012, H.R. 4081.

¹⁴⁴ *Id.*, at §2. If an agency fails to provide the required notice, and the Administrator of Small Business determines that the proposed procurement is subject to the bundling restrictions, the Administrator must require the procuring activity to produce the requisite notice and postpone the solicitation process for "at least 10 days but no more than 45 days" to allow for review. Identical provisions are included in the House-passed National Defense Authorization Act for FY2013. See H.R. 4310, as passed by the House, at §1671.

¹⁴⁵ See, e.g., Contractor Opportunity Protection Act of 2012, H.R. 4081, §2. If the Administrator does not pursue an appeal, any small business that would be directly or indirectly adversely affected by the proposed procurement, or any trade association of which it is a member, may protest to the GAO. If a protest is brought by a trade association, it shall not be required to identify a specific member in connection with the protest.

¹⁴⁶ A lead system integrator is an agent with authority to acquire and integrate goods from a variety of suppliers on behalf of the organization that is acquiring a complex system.

¹⁴⁷ See, e.g., *Coast Guard Acquisition Reform Act of 2009: Report of the House Committee on Transportation and Infrastructure*, H.Rept. 111-215 (July 20, 2009).

¹⁴⁸ SAVE Act of 2011, H.R. 2000, §112.

Insourcing

Recent attempts by the Department of Defense, in particular, to save money by insourcing certain functions performed by contractors prompted strong reactions from some small business contractors concerned about agency performance of functions they had previously performed, as well as the government's hiring of their employees.¹⁴⁹ Several small business contractors filed suit challenging agency determinations to insource particular functions on the grounds that these determinations were contrary to agency guidelines and, thus, violated the Administrative Procedure Act (APA). At first, there was some uncertainty as to whether the U.S. Court of Federal Claims had jurisdiction over such suits under the Administrative Disputes Resolution Act of 1996, or whether the federal district courts had jurisdiction under the APA.¹⁵⁰ While this question appears to have been resolved, with most courts finding that the Court of Federal Claims has exclusive jurisdiction over challenges to insourcing determinations, questions have recently arisen as to whether vendors whose contracts have expired have standing to challenge insourcing determinations, as well as whether contractors who are "interested parties" for purposes of ADRA must also meet prudential standing requirements.¹⁵¹ In addition, prior challenges to sourcing determinations have raised questions about whether particular guidelines for determining whether government personnel or contractor employees should perform certain functions are legally binding. Such questions could recur if and when courts resolve current questions about whether particular contractors have standing to challenge insourcing determinations.¹⁵²

¹⁴⁹ See generally CRS Report R41810, *Insourcing Functions Performed by Federal Contractors: An Overview of the Legal Issues*, by Kate M. Manuel and Jack Maskell.

¹⁵⁰ Compare *K-Mar Indus., Inc. v. U.S. Dep't of Defense*, 752 F. Supp. 2d 1207 (W.D. Okla. 2010) (finding that the district court has jurisdiction over a challenge to an insourcing determination because no contract or prospective contract is at issue, and an insourcing determination is not made in connection with a procurement or proposed procurement) with *Vero Tech. Support, Inc. v. U.S. Dep't of Defense*, 437 Fed. App'x 966 (11th Cir. 2011), *aff'g* 733 F. Supp. 2d 1336 (S.D. Fla. 2010)) (finding that the Court of Federal Claims has exclusive jurisdiction over challenges to insourcing determinations because contractors have a direct economic interest in the government's decision not to award a contract, and an insourcing determination is made in connection with a procurement).

¹⁵¹ Compare *Santa Barbara Applied Research, Inc. v. United States*, 98 Fed. Cl. 536 (2011) (expressly rejecting the government's argument that the case should be dismissed because the plaintiff contractor could not meet the prudential standing requirements) with *Hallmark-Phoenix 3, LLC v. United States*, 99 Fed. Cl. 65 (2011) (dismissing on prudential standing grounds a contractor's challenge to the Air Force's determination to insource certain supply services that the contractor had provided) and *Triad Logistics Servs. Corp. v. United States*, 2012 U.S. Claims LEXIS 393 (April 16, 2012) (expressing both disagreement with the *Hallmark-Phoenix* decision, and reservations about whether the plaintiff contractor could be found to be within the "zone of interests" of one of the statutes that the court relied upon in *Santa Barbara*). The concept of prudential standing is a "judicially self-imposed limit[] on the exercise of federal jurisdiction." *Elk Grove Unified Sch. Dist. v. Newdow*, 542 U.S. 1, 11 (2004) (internal quotations omitted). It is "founded in concern about the proper—and properly limited—role of the courts in a democratic society." *Warth v. Seldin*, 422 U.S. 490, 498 (1975). In determining whether prudential standing exists, the analysis focuses upon "whether the interest sought to be protected by the [plaintiff] is arguably within the zone of interests to be protected by the statute ... in question." *Ass'n of Data Processing Serv. Orgs., Inc. v. Camp*, 397 U.S. 150, 152-53 (1970). The prudential standing requirement is satisfied when the plaintiffs' interests are within this zone, but not when the plaintiffs are "merely incidental beneficiaries" of the statutory provisions at issue. *Nat'l Credit Union Admin. v. First Nat'l Bank & Trust Co.*, 522 U.S. 479, 494 n.7 (1998). However, the Supreme Court has recently indicated that prudential standing requirements are "not meant to be especially demanding," and "foreclose[] suit only when a plaintiff's 'interests are so marginally related to or inconsistent with the purposes implicit in the statute that it cannot reasonably be assumed that Congress intended to permit the suit.'" *Match-E-Be-Nash-She-Wish Band of Pottawatomi Indians v. Salazar*,—U.S.—, 132 S. Ct. 2199, 2210 (2012).

¹⁵² See, e.g., *Labat-Anderson, Inc. v. United States*, 65 Fed. Cl. 570, 578 (2005) (finding that certain of the guidelines that the agency allegedly violated when insourcing particular functions were not legally binding).

The Obama Administration responded to small businesses' concerns regarding insourcing, in part, by including certain protections for small businesses in its final policy letter on "inherently governmental functions."¹⁵³ Specifically, the policy letter directs agencies to place a lower priority on reviewing certain work performed by small businesses, as well as give small businesses preference when determining who performs work that will remain in the private sector after related functions are insourced.¹⁵⁴ However, some Members of the 112th Congress have proposed a different approach, introducing legislation that would help resolve uncertainties in the case law. This legislation would amend 31 U.S.C. Section 3551(1) to expressly provide that the term "protest" includes a written objection to the "conversion of a function that is being performed by a private sector entity to performance by a Federal employee," and that "any small business whose economic interest would be affected by the conversation" is an "interested party."¹⁵⁵ The legislation would also amend the Small Business Act by adding a new Section 46, which would prohibit an agency from converting functions performed by small businesses to performance by federal employees unless it has "made publicly available, after providing notice and an opportunity for public comment," its procedures for making insourcing determinations.¹⁵⁶ The requirement that agency procedures be made publicly available after a notice-and-comment period, in particular, could help remove questions as to whether agencies are bound by their insourcing guidelines that have arisen when these guidelines were promulgated as policy or guidance documents.¹⁵⁷ However, questions about prudential standing could potentially remain, notwithstanding the enactment of this legislation, because prudential standing is a "judicially self-imposed limit[] on the exercise of federal jurisdiction."¹⁵⁸

¹⁵³ "Inherently governmental functions" are functions that, as a matter of federal law and policy, must be performed by federal government employees and cannot be contracted out because they are so intimately related to the public interest as to require performance by federal employees. For more on inherently governmental functions, see CRS Report R42325, *Definitions of "Inherently Governmental Functions" in Federal Procurement Law and Guidance*, by John R. Luckey and Kate M. Manuel.

¹⁵⁴ Office of Mgmt. & Budget, Office of Fed. Procurement Pol'y, Publication of the Office of Federal Procurement Policy (OFPP) Policy Letter 11-01, Performance of Inherently Governmental and Critical Functions, 76 *Federal Register* 56227, 56239-40 (September 12, 2011). In particular, agencies are directed to use the "rule of two"—which generally requires that a contract be set aside for small businesses if at least two small businesses are capable of performing it at a fair market price—when deciding whether small or "large" businesses should perform the remaining private-sector work.

¹⁵⁵ Subcontracting Transparency and Reliability Act of 2012, H.R. 3893, §301.

¹⁵⁶ *Id.*, §302. The bill would also require that agency procedures specify that all insourcing determinations must be "reviewed" by any appropriate Office of Small and Disadvantaged Business Utilization (OSDBU) or procurement center representative (PCR). However, while OSDBUs and PCRs would have the opportunity to "review" such determinations, they would apparently not have authority to overrule an insourcing determination. Another measure introduced in the 112th Congress would prohibit civilian agencies from insourcing a function performed by a small business unless the agency "makes publicly available the procedures and methodologies" it used in making the determination to insource, including those for (1) determining which contracts were considered for potential conversion, (2) evaluating whether a function is inherently governmental or critical, and (3) estimating and comparing costs. National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1658. However, agencies subject to these requirements would not necessarily have to promulgate their procedures and methodologies through a notice-and-comment process.

¹⁵⁷ For example, some, but not all, federal circuits have found that the 1983 and 2003 versions of OMB Circular A-76, which provides guidelines for agencies' identification of commercial functions potentially suitable for performance by the private sector, were issued pursuant to statutory authority, which is one of the conditions for guidelines being reviewable by the federal courts. See *Labat-Anderson*, 65 Fed. Cl. at 578 (2003 version); *Diebold v. United States*, 947 F.2d 787, 800 (6th Cir. 1991) (1983 version).

¹⁵⁸ *But see Bennett v. Spear*, 520 U.S. 154, 163 (1997) (noting that Congress can "expressly negate" prudential standing requirements); *Elmendorf Support Services Joint Venture v. United States*, 2012 U.S. Claims LEXIS 651 (June 22, (continued...))

Other Members of the 112th Congress have introduced measures that call for SBA and/or agency advocates for small businesses to have more involvement in insourcing determinations. One such measure calls for agency procurement center representatives (PCRs), discussed below, to “participate in any session or planning process and review any documents with respect to a decision to convert an activity performed by a small business concern to an activity performed by a Federal employee.”¹⁵⁹ Another calls for the directors of various agency Offices of Small and Disadvantaged Business Utilization (OSDBUs), also discussed below, to review and advise agencies on decisions to convert an activity performed by a small business to an activity performed by federal employees.¹⁶⁰ However, it is not clear whether PCRs and OSDBUs would necessarily have the authority to delay or block an agency insourcing determination under these measures.

Procurement Center Representatives; Offices of Small and Disadvantaged Business Utilization

A number of SBA and agency personnel currently are tasked, under various statutes and regulations, with protecting the interests of small businesses in the federal procurement process. Among these personnel are procurement center representatives (PCRs), who are assigned by the SBA to work with the procuring activities in structuring acquisitions so as to maximize the participation of small businesses,¹⁶¹ and Offices of Small and Disadvantaged Business Utilization (OSDBUs), which are established in the procuring activities to help devise alternatives to procurements involving “significant bundling,” among other things.¹⁶² In part because of concerns about federal performance in contracting and subcontracting with small businesses, some Members of Congress and commentators have recently questioned the effectiveness of PCRs and/or OSDBUs, including whether these officials have the requisite authority and lines of reporting to adequately protect the interests of small businesses.¹⁶³ In part because of these concerns, the 111th Congress enacted legislation requiring the Administrator of Small Business to report periodically to Congress on the activities of PCRs and commercial market representatives (CMRs), who are tasked with facilitating contracting between agencies’ prime contractors and small businesses.¹⁶⁴

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2012) (finding that a contractor challenging an insourcing determination satisfied any prudential standing requirements in light of the Supreme Court’s recent decision in *Match-E-Be-Nash-She-Wish Band of Pottawatomi Indians v. Salazar*).

¹⁵⁹ Small Business Opportunity Act of 2012, H.R. 3980, §101.

¹⁶⁰ Small Business Advocate Act of 2012, H.R. 3851, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1691.

¹⁶¹ See, e.g., 13 C.F.R. §125.2. See also *supra* note 5 and accompanying text.

¹⁶² See, e.g., 15 U.S.C. §644(k)(1)-(10).

¹⁶³ See, e.g., Charles S. Clark, Four Departments Resist Call to Comply with Small Business Act, *Gov’t Exec.*, September 16, 2011, available at <http://www.govexec.com/federal-news/2011/09/four-departments-resist-call-to-comply-with-small-business-act/34926/> (reporting on a hearing of the House Small Business Subcommittee on Contracting and the Workforce that raised issues about whether OSDBU Directors report to the proper persons, among other things).

¹⁶⁴ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1312, 124 Stat. 2537. CMRs are “SBA’s subcontracting specialists,” and their responsibilities include facilitating the matching of large prime contractors with small business subcontractors or suppliers. See 13 C.F.R. §125.3(e).

Members of the 112th Congress have introduced additional measures that would involve PCRs earlier, and arguably more extensively, in the procurement process, expressly authorizing them to

attend any provisioning conference or similar evaluation session during which a determination may be made with respect to the procurement method to be used to satisfy a requirement, review any acquisition plan with respect to a requirement, and make recommendations regarding procurement method determinations and acquisition plans.¹⁶⁵

If enacted, such legislation would mark an arguably significant departure from current law, which does not explicitly provide for the involvement of PCRs until after the proposed acquisition package has been developed.¹⁶⁶

Members of the 112th Congress have also introduced legislation that would

- clarify to whom OSDDBU Directors must report,¹⁶⁷ in response to recent findings by GAO that the OSDDBU Directors of several federal agencies do not report to the agency head,¹⁶⁸
- require the Defense Acquisition University and the Federal Acquisition Institute to provide courses on contracting requirements under the Small Business Act, the completion of which would generally be required for the certification of contracting officers;¹⁶⁹ and
- require the Small Business Procurement Advisory Council, established pursuant to Section 7104(b) of the Federal Acquisition Streamlining Act, to conduct reviews of each OSDDBU to determine compliance with reporting and other requirements, and to identify best practices for “maximizing small business utilization.”¹⁷⁰

¹⁶⁵ Small Business Opportunity Act of 2012, H.R. 3980, §101; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1621. These measures would also expressly authorize PCRs to review barriers to small business participation in Federal contracting, and receive copies of unsolicited proposals from small business concerns, as well as any information on outcomes relating to such proposals. *Id.*

¹⁶⁶ 48 C.F.R. §19.202-1(e)(1).

¹⁶⁷ Small Business Advocate Act of 2012, H.R. 3851, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1691; SUCCESS Act of 2012, S. 3442, §542. This legislation would also task OSDDBUs with some additional functions, such as providing agency acquisition officials with advice and comments on acquisition strategies and market research. It would also prohibit OSDDBU Directors from holding “any other title, position, or responsibility except as necessary to carry out responsibilities under this subsection.” *Id.*

¹⁶⁸ See Gov’t Accountability Office, *Small Business Contracting: Actions Needed by Those Agencies Whose Advocates Do Not Report to Agency Heads as Required*, GAO-11-418 (June 16, 2011).

¹⁶⁹ National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1622. New PCRs and business opportunity specialists would be required to have Level III and Level I certifications, respectively. Persons currently holding those positions could continue to serve without certification for five years. *Id.*, at §§1621-1622.

¹⁷⁰ Small Business Advocate Act of 2012, H.R. 3851, §3; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1692.

Restricted Competitions and Non-Competitive Awards

Competition is generally valued in federal contracting because it can result in the government paying lower prices, ensure some level of transparency and accountability, and help prevent fraud.¹⁷¹ However, Congress has authorized agencies to use other than full-and-open competition in certain circumstances in order to promote other policy objectives, including contracting with small businesses.¹⁷² The Competition in Contracting Act (CICA) of 1984 currently provides that agencies may use “other than full and open competition” when making awards to small businesses.¹⁷³ Such awards may be made on a set-aside or sole-source basis, pursuant to the Small Business Act.¹⁷⁴ Congress amended the Small Business Act in 2010 to expressly authorize agencies to set-aside all or part of multiple-award contracts for small businesses,¹⁷⁵ something which GAO had previously found was required in certain circumstances.¹⁷⁶

Members of the 112th Congress have similarly introduced legislation that would expand agencies’ authority to conduct competitions restricted to small businesses, or make sole-source awards to them, in the hopes of increasing the extent of contracting with small businesses. One such measure would amend Section 8(m) of the Small Business Act to authorize agencies to set aside contracts of any value for women-owned small businesses.¹⁷⁷ Currently, only contracts whose

¹⁷¹ See generally CRS Report R40516, *Competition in Federal Contracting: An Overview of the Legal Requirements*, by Kate M. Manuel.

¹⁷² Cf. 48 C.F.R. §1.102(b) (“The Federal Acquisition System will—(1) [s]atisfy the customer in terms of cost, quality, and timeliness of the delivered product or service by, for example—(i) [m]aximizing the use of commercial products and services; (ii) [u]sing contractors who have a track record of successful past performance or who demonstrate a current superior ability to perform; and (iii) [p]romoting competition; (2) [m]inimize administrative operating costs; (3) [c]onduct business with integrity, fairness, and openness; and (4) [f]ulfill public policy objectives.”).

¹⁷³ 10 U.S.C. §2304(b)(2) (procurements of defense agencies) & 41 U.S.C. §3303(b) (procurements of civilian agencies).

¹⁷⁴ See 15 U.S.C. §637(a) (small disadvantaged businesses participating in the 8(a) Business Development Program); 15 U.S.C. §637(m) (women-owned small businesses); 15 U.S.C. §644 (small businesses generally); 15 U.S.C. §657a (HUBZone small businesses); 15 U.S.C. §657f (service-disabled veteran-owned small businesses).

¹⁷⁵ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1331, 124 Stat. 2541 (codified at 15 U.S.C. §644(r)) (requiring the promulgation of regulations authorizing agencies to (1) “set aside part or parts of a multiple award contract” for small businesses; (2) place orders against multiple-award contracts without giving all contractors a fair opportunity to be considered for such awards; and (3) “reserve 1 or more contract awards for small business concerns under full and open multiple award procurements”). See also Consolidated Appropriations Act, P.L. 112-74, §7057(h), 125 Stat. 1245 (December 23, 2011) (authorizing the U.S. Agency for International Development to provide an exception to the fair opportunity process for placing task orders under multiple-award indefinite-delivery/indefinite quantity (ID/IQ) contracts when the order is placed with “any category of small or small disadvantaged business”); Department of State, Foreign Operations, and Related Programs Appropriations Act, 2013, H.R. 5857, §5057(h) (same).

¹⁷⁶ See *Delex Systems, Inc.*, B-400403, 2008 U.S. Comp. Gen. LEXIS 170 (October 8, 2008) (determining that task and delivery orders issued under multiple-award ID/IQ contracts are subject to set-asides for small businesses). However, the General Services Administration responded to the *Delex* decision, in part, by asserting that contracts under the Federal Supply Schedules are not subject to set-asides for small businesses because they are governed by a different section of the FAR than other multiple-award ID/IQ contracts. See GSA Memorandum from David A. Drabkin, Senior Procurement Executive, to All GSA Contracting Activities, October 28, 2008), quoted in Arnold & Porter LLP, GAO’s *Delex* Decision and GSA’s Response: The Clash of Titans, available at http://www.arnoldporter.com/resources/documents/CA_GAOsDelexDecision&GSAsResponse_012609.pdf.

¹⁷⁷ Fairness in Women-Owned Small Business Contracting Act of 2012, S. 2172, §2. See also Women’s Procurement Program Improvement Act of 2012, H.R. 4203, §2 (amending Section 8(m) to authorize agencies to set aside contracts (continued...))

value is below \$4 million (\$6.5 million for manufacturing contracts) may be set aside for such firms.¹⁷⁸ Similarly, the proposed legislation would authorize agencies to “award a sole source contract under this section to a small business concern owned and controlled by women under the same conditions as a sole source contract may be awarded to a qualified HUBZone small business concern under section 31(b)(2)(A).”¹⁷⁹ The Small Business Act presently does not authorize sole-source awards to women-owned small businesses, although it does authorize such awards to HUBZone small businesses, among others, whenever

1. the business is determined to be responsible with respect to the performance of the contract, and the contracting officer does not reasonably expect that two or more such businesses will submit offers;
2. the anticipated award will not exceed \$4 million (\$6.5 million for manufacturing contracts); and
3. the award can be made at a fair and reasonable price.¹⁸⁰

Another measure introduced in the 112th Congress would amend the Veterans Benefits Act to require that VA make sole-source awards to veteran-owned small businesses whenever (1) the business is determined to be a responsible source with respect to the performance of the contract opportunity; (2) the anticipated award price of the contract (including options) exceeds the simplified acquisition threshold (generally \$150,000¹⁸¹), but is less than \$5 million; and (3) in the estimation of the contracting officer, the contract award can be made at a fair and reasonable price that offers best value to the United States).¹⁸² VA currently has authority to make sole-source awards when these circumstances exist, but is not required to do so.¹⁸³

Yet other measures would exempt contracts “authorized” under the Small Business Act from certain limitations imposed upon agency’s use of noncompetitive procedures when entering contracts to procure property or services “in connection with natural disaster reconstruction efforts,”¹⁸⁴ as well as amend the Small Business Act to require, rather than just authorize, set-asides of or under multiple-award contracts.¹⁸⁵ The latter measure would also generally require

(...continued)

of any value for women-owned small businesses).

¹⁷⁸ See 15 U.S.C. §637(m)(2)(D).

¹⁷⁹ Fairness in Women-Owned Small Business Contracting Act of 2012, S. 2172, §2. H.R. 4203 would similarly amend Section 8(m) to authorize sole-source awards to women-owned small businesses, although it would do so without explicit reference to sole-source awards to HUBZone firms.

¹⁸⁰ 15 U.S.C. §657a(b)(2)(A)(i)-(iii) (statutory requirements); 48 C.F.R. §19.1306(a)(1)-(6) (increasing the price thresholds, among other things).

¹⁸¹ In the case of supplies or services to be used in support of a contingency operation or to facilitate defense against or recovery from nuclear, biological, chemical, or radiological attack, the simplified acquisition threshold increases to \$300,000 for contracts to be awarded and performed inside the United States, and \$1 million for contracts to be awarded and performed outside the United States. 48 C.F.R. §2.101.

¹⁸² An Act to Amend Title 38, United States Code, to Promote Jobs for Veterans through the Use of Sole Source Contracts by Department of Veterans Affairs for Purposes of Meeting the Contracting Goals and Preferences of the Department of Veterans Affairs for Small Business Concerns Owned and Controlled by Veterans, H.R. 240, §1.

¹⁸³ 38 U.S.C. §8127(c).

¹⁸⁴ Natural Disaster Fairness in Contracting Act of 2011, S. 129, §4(c)(3).

¹⁸⁵ Small Business Procurement Improvement Act of 2012, H.R. 4118, §2 (amending Section 15(r) of the act by replacing language indicating that “agencies may, at their discretion, set aside part or parts of a multiple award contract for small business[es],” among other things, with language indicating that agencies “shall, to the maximum extent (continued...)

agencies to conduct an outreach program designed to increase the participation of small businesses in multiple-award contracts, as well as require the President to establish annual goals for the “total dollar value of all task and delivery orders placed against multiple award contracts, blanket purchase agreements, and basic ordering agreements awarded to small business[es].”¹⁸⁶

Use of Small Businesses When Making “Small Purchases”

Federal law currently distinguishes between (1) purchases whose value is below the micro-purchase threshold (generally \$3,000¹⁸⁷); (2) those whose value is above the micro-purchase threshold, but below the simplified acquisition threshold (generally \$150,000¹⁸⁸); and (3) other purchases. Those acquisitions whose value falls between the micro-purchase threshold and the simplified acquisition threshold have long been reserved for small businesses,¹⁸⁹ although agencies are also encouraged to use small businesses for purchases outside this range.¹⁹⁰ The 111th Congress enacted legislation intended to foster increased use of small businesses for micro-purchases by requiring the Office of Management and Budget (OMB), in consultation with the General Services Administration, to issue

guidelines regarding the analysis of purchase card expenditures to identify opportunities for achieving and accurately measuring fair participation of small business concerns in purchases in an amount not in excess of the micro-purchase threshold ... and dissemination of best practices for participation of small business concerns in micro-purchases.¹⁹¹

OMB issued this guidance on December 19, 2011, reminding agencies that those holding government-wide commercial purchase cards should consider small businesses “to the maximum extent practicable” when making micro-purchases.¹⁹² However, prior to the issuance of this

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practicable, include small business concerns in multiple award contracts”).

¹⁸⁶ *Id.* §§2(b) & 4.

¹⁸⁷ The micropurchase threshold can be lower or higher than \$3,000, depending on the goods or services acquired and the circumstances of the acquisition. Micropurchases for construction services subject to the Davis-Bacon Act or other services subject to the Service Contract Act have lower limits: \$2,000 and \$2,500, respectively. Those for goods or services that the agency head has determined will be used to support a contingency operation or facilitate defense against or recovery from nuclear, biological, chemical, or radiological attack have higher limits: \$15,000 in the case of contracts to be awarded or performed, or purchases to be made, inside the United States and \$30,000 in the case of contracts to be awarded or performed, or purchases to be made, outside the United States. 48 C.F.R. §13.201(g)(1)(i)-(ii).

¹⁸⁸ See *supra* note 181 for a discussion of when the simplified acquisition threshold may exceed \$150,000.

¹⁸⁹ 15 U.S.C. §644(j)(1). Such purchases are made using “simplified acquisition procedures,” such as government-wide commercial purchase cards, purchase orders, blanket purchase agreements, imprest funds, third-party drafts, and certain standard forms (e.g., SF44). See 48 C.F.R. Subpart 13.3.

¹⁹⁰ See, e.g., 48 C.F.R. §19.201 (“It is the policy of the Government to provide maximum practicable opportunities in its acquisitions to small business[es].”).

¹⁹¹ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1332, 124 Stat. 2541.

¹⁹² Exec. Office of the President, Office of Mgmt. & Budget, Increasing Opportunities for Small Businesses in Purchase Card Micro-Purchases, December 19, 2011, available at <http://www.whitehouse.gov/sites/default/files/omb/procurement/memo/increasing-opportunities-for-small-businesses-in-purchase-card-micro-purchases.pdf>. For more on government-wide commercial purchase cards, see generally CRS Report RL34602, *Misuse of Government Purchase* (continued...)

guidance, one Member of the 112th Congress introduced legislation that would expand the value of the “small purchases” in which small businesses could be preferred. Among other things, this legislation would generally require agencies “to the extent practicable” to award contracts whose value exceeds \$3,000, but is below \$500,000, to small businesses.¹⁹³ The legislation would also give contracting officers additional authority to award contracts valued within this range to small businesses on a sole-source basis.¹⁹⁴ Specifically, this legislation would authorize agencies to make sole-source awards of contracts valued at between \$150,000 and \$500,000 to women-owned small businesses, or other small businesses that are not 8(a), HUBZone, or service-disabled veteran-owned small businesses. The Small Business Act currently does not authorize sole-source awards to such businesses.¹⁹⁵ Rather, it only authorizes agencies to set aside contracts for them.

Mentor-Protégé Programs

Mentor-protégé programs are intended to promote contracting and/or subcontracting with small businesses by pairing new businesses with more experienced businesses in mutually beneficial relationships.¹⁹⁶ Congress established the first mentor-protégé program for small businesses in 1990, when it authorized the Department of Defense (DOD) Mentor-Protégé Pilot program.¹⁹⁷ Eight years later, in 1998, SBA promulgated regulations establishing a mentor-protégé program for small disadvantaged businesses participating in the 8(a) Program.¹⁹⁸ DOD’s Mentor-Protégé Pilot Program differs from SBA’s 8(a) Mentor-Protégé program in that it focuses upon promoting the use of small businesses as subcontractors and suppliers on federal contracts, and not upon use of small businesses as prime contractors.¹⁹⁹ Specifically, under DOD’s program, prime contractors may be reimbursed for advance payments made to small business subcontractors or suppliers,²⁰⁰ while under SBA’s program, mentors and protégés may form joint ventures that qualify as small for purposes of certain federal prime contracts.²⁰¹ More recently, a number of other agencies have

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Cards, by Garrett Hatch.

¹⁹³ Expanding Opportunities for Main Street Act of 2011, H.R. 2424; S. 1334, §101.

¹⁹⁴ *Id.* This legislation would also give SBA additional control over the procuring activities by requiring agencies to notify SBA of any determinations that award to a small business is not practicable, and authorizing SBA to open the opportunity for the submission of additional offers, if it determines that doing so is appropriate.

¹⁹⁵ See CRS Report R42391, *Legal Authorities Governing Federal Contracting and Subcontracting with Small Businesses*, by Kate M. Manuel and Erika K. Lunder, at **Table 1**.

¹⁹⁶ For more on small business mentor-protégé programs, see generally CRS Report R41722, *Small Business Mentor-Protégé Programs*, by Robert Jay Dilger and Kate M. Manuel.

¹⁹⁷ An Act to Authorize Appropriations for Fiscal Year 1991 for Military Activities of the Department of Defense, for Military Construction, and for Defense Activities of the Department of Energy, to Prescribe Personnel Strengths for the Armed Forces and for Other Purposes, P.L. 101-510, §831, 104 Stat. 1607-08 (November 5, 1990) (codified, as amended, at 10 U.S.C. §2302 note).

¹⁹⁸ Small Bus. Admin., Small Business Size Regulations; 8(a) Business Development/Small Disadvantaged Business Status Determinations; Rules of Procedure Governing Cases Before the Office of Hearings and Appeals: Final Rule, 63 *Federal Register* 35739 (June 30, 1998).

¹⁹⁹ Compare 10 U.S.C. §2302 note (DOD mentor-protégé program) with 13 C.F.R. §124.520(a) (SBA’s mentor-protégé program for 8(a) firms).

²⁰⁰ 48 C.F.R. §219.7102(d)(1)-(2); 48 C.F.R. §19.702(d). In addition, mentors may receive credit toward their subcontracting goals because of developmental assistance provided to protégés.

²⁰¹ 13 C.F.R. §124.520(a). Mentors in the 8(a) mentor-protégé program may also receive credit toward their (continued...)

implemented their own mentor-protégé programs, by regulation or otherwise.²⁰² These programs differ, among themselves and as compared to the DOD and SBA programs, in their eligibility requirements and the types of assistance that mentors provide to protégés.²⁰³ Such differences have raised concerns among some Members of Congress and commentators that the programs lack “parity,” are duplicative, and/or are confusing for small businesses.²⁰⁴

The 111th Congress responded to the concerns about parity by enacting legislation that authorizes SBA to establish mentor-protégé programs for HUBZone, women-owned, and service-disabled veteran-owned small businesses modeled on its 8(a) mentor-protégé program.²⁰⁵ However, partly in response to the concerns about duplication, this legislation also directs GAO to study existing mentor-protégé programs and “other relationships and strategic alliances” pairing larger and small businesses to determine whether they are “effectively supporting the goal of increasing the participation of small business concerns in Government contracting.”²⁰⁶ Some Members of the 112th Congress have also proposed legislation addressing similar concerns. This legislation would authorize SBA to establish a mentor-protégé program open to all small businesses.²⁰⁷ By comparison, the legislation enacted by the 111th Congress addressed only HUBZone, women-owned, and service-disabled veteran-owned small businesses. The legislation introduced in the 112th Congress would also prohibit federal agencies, with certain exceptions, from carrying out a mentor-protégé program for small businesses unless the plan for this program has been submitted to and approved by SBA.²⁰⁸ Depending upon its implementation, such a provision could help

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subcontracting goals. 13 C.F.R. §125.3(b)(3)(ix).

²⁰² 48 C.F.R. Subpart 919.70 (Department of Energy); 48 C.F.R. §352.219-70 (Department of Health and Human Services); 48 C.F.R. §3052.219-71 (Department of Homeland Security); 48 C.F.R. §619.202-70 (Department of State); 48 C.F.R. Subpart 1019.202-70 (Department of the Treasury); 48 C.F.R. Subpart 819.71 (Department of Veterans Affairs); 48 C.F.R. §§1552.219-70 to 1552.219-71 (Environmental Protection Agency); FAA Mentor-Protégé Program, available at <http://www.sbo.faa.gov/MentorProtege.cfm> (Federal Aviation Administration); 48 C.F.R. Subpart 519.70 (General Services Administration); 48 C.F.R. Subpart 1819.72 (NASA); 48 C.F.R. Subpart 719.273 (U.S. Agency for International Development).

²⁰³ See CRS Report R41722, *Small Business Mentor-Protégé Programs*, by Robert Jay Dilger and Kate M. Manuel, at Table A-1, for a comparison of the eligibility criteria for, and types of assistance provided under, various agencies’ mentor-protégé programs.

²⁰⁴ See, e.g., Gov’t Accountability Office, *Opportunities to Improve the Effectiveness of Agency and SBA Advocates and Mentor-Protege Programs*, GAO-11-844T (September 15, 2011).

²⁰⁵ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1347(b), 124 Stat. 2547.

²⁰⁶ *Id.*, §1345, 124 Stat. 2546. GAO issued this report on June 15, 2011, finding that most agencies do not collect information on protégés after the conclusion of their mentor-protégé agreements, which makes it difficult to assess the efficacy of these programs. See Gov’t Accountability Office, *Mentor-Protégé Programs Have Policies That Aim to Benefit Participants But Do Not Require Postagreement Tracking*, GAO-11-548R (June 15, 2011).

²⁰⁷ Building Better Business Partnerships Act of 2012, H.R. 3985, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1641. SBA would appear to have discretion as to whether to establish such a mentor-protégé program under the proposed legislation. However, if such a program were established, it would have to be “identical to the mentor-protégé program of the Administration for small business concerns that participate in the program under section 8(a) of this act.” Because of legislation enacted by the 111th Congress, any SBA mentor-protégé program for HUBZone, woman-owned, and service-disabled veteran-owned small businesses must be “modeled” on that for 8(a) firms. See *supra* note 205 and accompanying text.

²⁰⁸ Building Better Business Partnerships Act of 2012, H.R. 3985, §2; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1641. Certain mentor-protégé programs would be exempted from this requirement, including “[a]ny mentor-protégé program of the Department of Defense,” and “mentoring assistance” provided under the Small Business Innovation Research and Small Business Technology Transfer programs. Existing mentor-protégé programs would also be exempted from these requirements for one year after the measure’s enactment.

ensure that there are not significant disparities among the various agency programs, and that these programs do not unnecessarily duplicate one another.²⁰⁹

Deterrence of and Penalties for Fraud

Fraud in small business contracting programs has been a perennial concern for Congress and commentators because the advantages that firms can obtain by misrepresenting their size and status are apparently so great that reports of fraud emerge with some regularity.²¹⁰ Firms that fraudulently misrepresent their size or status have long been subject to civil and/or criminal penalties under Section 16 of the Small Business Act; SBA regulations implementing Section 16; and other provisions of law, such as the False Claims Act, Fraud and False Statements Act, Program Fraud Civil Remedies Act, and Contract Disputes Act.²¹¹ In addition, various entities, including contracting officers, SBA officials, and certain other firms, have been authorized to “protest” firms’ size or status with the SBA’s Office of Hearings and Appeals.²¹² However, recent, high-profile reports of fraud in the small business programs have heightened concerns about whether the existing penalties and/or protest provisions are adequate to deter fraud and ensure that ineligible firms do not take improper advantage of small business contracting and subcontracting programs.²¹³

Partly in response to concerns about fraud in the small business contracting programs, the 111th Congress enacted legislation which provides that ineligible small businesses may not receive an “offset” or “credit” for the value of the goods or services they supplied to the government when the amount of “loss to the United States” is calculated for purposes of the civil False Claims Act or the U.S. Sentencing Guidelines, among other purposes.²¹⁴ This legislation also provides that

²⁰⁹ The National Defense Authorization Act for FY2013 would require GAO to conduct a study within two years of its enactment to examine whether potential affiliation issues between mentors and protégés under prior programs have been “resolved,” and whether SBA’s regulations have increased opportunities for mentor-protégé pairs. *See* H.R. 4310, as passed by the House, at §1641.

²¹⁰ *See, e.g.*, Gov’t Accountability Office, Small Business Administration: Undercover Tests Show HUBZone Program Remains Vulnerable to Fraud and Abuse, GAO-10-920T (July 28, 2010); Gov’t Accountability Office, 8(a) Program: Fourteen Ineligible Firms Received \$325 Million in Sole-Source and Set-Aside Contracts, GAO-10-425 (March 30, 2010); Gov’t Accountability Office, Service-Disabled Veteran-Owned Small Business Program: Case Studies Show Fraud and Abuse Allowed Ineligible Firms to Obtain Millions of Dollars in Contracts, GAO-10-108 (October 23, 2009).

²¹¹ *See* 15 U.S.C. §645; 13 C.F.R. §125.29.

²¹² *See* 13 C.F.R. §121.1001(a)(i)-(iv) (permitting protests of firms’ size by any offeror who has not been eliminated for reasons unrelated to size, the contracting officer, certain SBA officials, and “other interested parties,” potentially including large businesses).

²¹³ *See, e.g.*, Del Quentin Wilber & Robert O’Harrow, “Brazen” Contracting Scam: Records Provide a Window into Audacious Swindle, *Wash. Post*, December 24, 2011, *available at* http://www.washingtonpost.com/local/brazen-contracting-scam-detailed-in-federal-allegations/2011/12/20/gIQA8hw5FP_story.html (reporting that government personnel and employees of ANC-owned firm participating in the 8(a) Program inflated invoices by \$20 million for personal gain).

²¹⁴ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1341, 124 Stat. 2543-44 (codified at 15 U.S.C. §632(w)(1)). Specifically, this legislation amended the Small Business Act to provide that

In every contract, subcontract, cooperative agreement, cooperative research and development agreement, or grant which is set aside, reserved, or otherwise classified as intended 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, subcontract, cooperative agreement, cooperative research and development agreement, or grant whenever it is established that a business concern other than a

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when a company (1) submits a bid or offer for a contract or subcontract set aside for, or otherwise classified as intended for, award to small businesses; (2) encourages the government to award it a contract based on its size or status; or (3) registers in any federal database for purposes of being considered for a federal contract or subcontract, it shall be deemed to have “affirmatively, willfully, and intentionally” certified its size and status.²¹⁵ In addition, the legislation requires the development of a government-wide policy on the prosecution of size and status fraud, and that each business certified as small annually re-certify its size in the Online Representations and Certifications (ORCA) database, or any successor database.²¹⁶

Members of the 112th Congress have also proposed measures that would address fraud in small business contracting programs in various ways, including by

- amending Title 18 of the United States Code to provide that persons who knowingly make certain misrepresentations regarding their small business status in order to obtain, retain or complete a federal contract are subject to imprisonment for up to five years and/or a fine of \$1 million, or an amount equal to twice the value of the goods or services involved, whichever is greater;²¹⁷
- amending Section 16 of the Small Business Act to expressly include service-disabled veteran-owned small businesses among the types of small businesses subject to penalties for fraud under Section 16;²¹⁸
- requiring that service-disabled veteran-owned small businesses register in the Department of Veterans Affairs’ (VA’s) VetBiz database, or any successor database, and have their status verified by VA in order to be eligible for

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small business willfully sought and received the award by misrepresentation.

This change potentially overturns a series of court decisions finding that the value of any goods or services that the government obtains as a result of the contractor’s misrepresentations must be deducted from the amount of loss or damage incurred by the United States when calculating the contractor’s ultimate liability for its misrepresentations. *See, e.g., United States v. Bornstein*, 423 U.S. 303, 317 (1976). In contrast, courts have found that, when persons receive grants due to misrepresentations of their size or status, their liability should equal the total amount that the government paid them because the government received no tangible benefit, and any intangible benefit that it received is impossible to calculate. *See, e.g., Longhi v. Lithium Power Techs., Inc.*, 575 F.3d 458, 473 (5th Cir. 2009).

²¹⁵ Small Business Jobs Act, P.L. 111-240, tit. I, subtitle C, §1341, 124 Stat. 2543-44.

²¹⁶ *Id.*, §§1342-1343, 124 Stat. 2544-45. In addition, such certifications would have to be made by an “authorized official” of the company. *Id.*, §1341, 124 Stat. 2543-44. Previously, firms registered in ORCA were supposed to update their certifications and representations on an annual basis. 48 C.F.R. §4.1201(b)(1). However, P.L. 111-240 expanded upon this requirement by imposing a penalty on businesses that fail to file their annual registrations in ORCA.

²¹⁷ Contracting Oversight for Small Business Jobs Act of 2012, H.R. 4206, §2. This measure would also amend Section 16(d) of the Small Business Act to establish a “safe harbor” for certain defendants who misrepresented their status “in reliance on a written advisory opinion from a licensed attorney who is not an employee of the defendant.” *Id.*, at §3. It would also amend Section 5 of the Small Business Act to create express statutory authority for SBA’s Office of Hearings and Appeals (OHA). *Id.*, at §4. The House-passed National Defense Authorization Act for FY2013 includes similar provisions regarding safe harbors and OHA. *See* H.R. 4310, as passed by the House, at §§1681-1682.

²¹⁸ Small Business Contracting Fraud Prevention Act of 2011, S. 633, §3; SUCCESS Act of 2012, S. 3442, §523. Currently, Section 36 of the Small Business Act, which governs set-asides and sole-source awards for service-disabled veteran-owned small businesses, provides that “[r]ules similar to the rules of paragraphs (5) and (6) of section 637(m) of this title shall apply for purposes of this section.” Section 8(m) governs set-asides for women-owned small businesses, and itself provides that such businesses are subject to penalties for fraud under Section 16. Thus, an argument could potentially be made that service-disabled veteran-owned small businesses are currently subject to penalties under Section 16 even if they are not expressly included there.

- contracting preferences for service-disabled veteran-owned small businesses under the Small Business Act;²¹⁹
- requiring GAO to report periodically to Congress on the effectiveness of the 8(a) Program, including the percentage of businesses that continue to operate during the three-year period after successfully completing the program;²²⁰
 - requiring SBA to submit annual reports to Congress on the number of persons debarred or suspended from government contracting, or considered for debarment or suspension from government contracting, for violations of the act;²²¹
 - amending the Veterans Benefits Act to require that firms be debarred for five years if they misrepresent their status as veteran-owned for purposes of programs under the act;²²²
 - requiring that “contracting rules and regulations” be amended to ensure that businesses are debarred from government contracting for no less than five years if they fraudulently represent that they are small as part of a bid or proposal for a small business contract awarded under the Small Business Act or other authority;²²³
 - authorizing “any person” to file a “complaint” with the SBA and/or the procuring agency regarding firms’ status, and requiring that complaints be resolved in a timely manner;²²⁴ and
 - requiring the Contractor Central Registration (CCR), or any successor database, include “adequate warning” of the criminal penalties under Section 16(d) of the Small Business Act for misrepresenting firm size or status.²²⁵

²¹⁹ *Id.*, §4. This section would also expressly authorize SBA to debar or suspend any firm that knowingly and willfully misrepresented itself as a service-disabled veteran-owned small business for purposes of programs under the Small Business Act.

²²⁰ *Id.*, §5. The Administrator of Small Business would also be required to “begin to” make unannounced site-visits to 8(a) firms, and to use fraud detection tools. *Id.*

²²¹ *Id.*, §7; National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1684. Debarment refers to firms’ exclusion from contracting and, potentially, subcontracting with the government for a fixed period of time. It does not refer to firms’ eligibility to participate in programs for specific types of small businesses under the Small Business Act. Firms that are debarred would generally be ineligible for such programs by virtue of the facts that gave rise to their debarment (i.e., their being other than small, their being other than veteran-owned). However, remedying the grounds for their ineligibility (e.g., ensuring that a veteran owns at least 51% of the business) would not necessarily result in their debarment being lifted. *See also* Contracting Oversight for Small Business Jobs Act of 2012, H.R. 4206, §6 (requiring similar annual reports from SBA).

²²² An Act to Amend Title 38, United States Code, to Revise the Enforcement Penalties for Misrepresentation of a Business Concern as a Small Business Owned and Controlled by Veterans or as a Small Business Concern Owned and Controlled by Service-Disabled Veterans, and for Other Purposes, S. 1184, §1 (amending the Veterans Benefits Act to require that firms determined to have misrepresented their status as veteran-owned small businesses be debarred for a period of not less than five years, as well as requiring that any debarment action be commenced no later than 30 days after determining that the firm misrepresented its status, and completed no less than 90 days after this determination); Veterans Programs Improvement Act of 2011, S. 914, §703 (generally the same as S. 1184, 112th Cong., but amending the Veterans Benefits Act to clarify that only firms that deliberately misrepresent their status shall be debarred).

²²³ Fairness and Transparency in Contracting Act of 2011, H.R. 3184, §9(b); Act for the 99%, H.R. 3639, §1309(b).

²²⁴ Fairness and Transparency in Contracting Act of 2011, H.R. 3184, §9(a); Act for the 99%, H.R. 3639, §1309(a). In contrast, under current law, only certain persons—namely, contracting officers, certain SBA officials, and certain other firms—may file “protests” challenging a firm’s status. *See supra* note 212 and accompanying text.

The proposed measures regarding debarment from government contracting, in particular, would arguably depart significantly from current law, which grants VA and other agencies broad discretion as to whether to debar contractors for misrepresenting their size or status, or for other wrongdoing. The Veterans Benefits Act currently states that firms which misrepresent their size or status “shall” be debarred for a “reasonable period of time, as determined by the Secretary” of Veterans Affairs.²²⁶ However, it does not specify the period of debarment for such misrepresentations. Similarly, although both the Small Business Act and the FAR authorize debarment for misrepresentations of size or status, they do not require debarment, or prescribe the duration of any debarment.²²⁷

Requiring service-disabled veteran-owned small businesses to register in the VetBiz database would also be a departure from current law, which permits such firms to self-certify their status for purposes of the Small Business Act.²²⁸ However, the effectiveness of any such change would depend upon how it is implemented by SBA and VA.²²⁹

Agency-Specific Programs

Members of the 112th Congress have also enacted or proposed several measures addressing contracting and subcontracting with small businesses by particular agencies. Among the measures enacted was one appropriating \$15 million to the Department of Defense (DOD) for use in making “incentive payments” under Section 504 of the Indian Financing Act (IFA) of 1974 to contractors or subcontractors that use certain Indian-owned small businesses as subcontractors or suppliers.²³⁰ The FAR authorizes agencies to pay similar “monetary incentives” to prime contractors that subcontract with small disadvantaged businesses.²³¹ However, Congress has

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²²⁵ Fairness and Transparency in Contracting Act of 2011, H.R. 3184, §8; Act for the 99%, H.R. 3638, §1308.

²²⁶ 38 U.S.C. §8127(g). Although Section 8127(g) uses “shall” when describing when persons are to be debarred, such debarments are punishments, and an argument could, thus, be made that the determination as to whether to debar a particular person remains within the agency’s prosecutorial discretion. *See, e.g.*, *United States v. Nixon*, 418 U.S. 683, 693 (1974) (citing the *Confiscation Cases*, 7 Wall. 454 (1869) (“[T]he Executive Branch has exclusive authority and absolute discretion to decide whether to prosecute a case.”)); *Heckler v. Cheney*, 470 U.S. 821, 832 (1985) (noting that an agency decision to initiate an enforcement action in the administrative context “shares to some extent the characteristics of the decision of a prosecutor in the executive branch”); *Matter of E-R-M & L-R-M*, 25 I. & N. Dec. 520, 523 (2011) (finding that determinations as to whether to pursue expedited removal proceedings (as opposed to removal proceedings under Section 240 of the Immigration and Nationality Act (INA)) are within the executive branch’s discretion, even though the INA uses “shall” in describing who is subject to expedited removal).

²²⁷ *See, e.g.*, 15 U.S.C. §645(d)(2)(C) (“Any person who violates paragraph (1) shall be subject to debarment or suspension[, among other things].”); 48 C.F.R. §9.406-2(c) (authorizing debarment whenever an agency official finds, by a preponderance of the evidence, that there exists “any other cause of so serious or compelling a nature that it affects the present responsibility of a contractor”). Debarment under the FAR lasts for a “period commensurate with the seriousness of the cause(s),” generally not exceeding three years. 48 C.F.R. §9.406-4(a)(1).

²²⁸ *See* 13 C.F.R. §§125.9-125.13.

²²⁹ For example, if VA is not thorough in conducting reviews of owners’ status as service-disabled veterans, the enactment of such a measure might be of limited effectiveness in preventing fraud in the service-disabled veteran-owned small business program.

²³⁰ Consolidated Appropriations Act, P.L. 112-74, §8019, 125 Stat. 808-09 (December 23, 2011). Subcontracting bonuses under this authority can be paid on any contract or subcontract valued in excess of \$500,000. *See also* Department of Defense Appropriations Act, 2013, §8019 (authorizing certain such bonuses for FY2013).

²³¹ *See* 48 C.F.R. §19.1203 (authorizing agencies to pay prime contractors up to 10% of the amount by which their performance in subcontracting with small disadvantaged businesses (SDBs) exceeds their targets for subcontracting (continued...))

historically not appropriated funds specifically for the payment of such incentives, unlike with incentive payments made by DOD under the IFA. The 112th Congress has also enacted legislation extending the Comprehensive Small Business Subcontracting Program for three years.²³² This temporary program was established in 1989 to determine if comprehensive subcontracting plans on a corporate, division, or plant-wide basis (as opposed to on a per-contract basis) would lead to increased opportunities for small businesses.²³³

In addition, Members of the 112th Congress have introduced legislation that would direct the Department of Homeland Security's (DHS's) Under Secretary for Management to "ensure" that DHS's website includes information on programs, policies, and initiatives designed to encourage small businesses to participate in agency acquisitions.²³⁴ Members have also introduced legislation that seeks to improve DOD's performance in contracting and subcontracting with small businesses by (1) ensuring that the heads of DOD Offices of Small Business Programs participate in the requirements development and acquisition processes;²³⁵ (2) requiring that officials within the Defense Contract Audit Agency and Defense Contract Management Agency be designated as "Small Business Advocates" and tasked with monitoring the timeliness of audit closeouts for small businesses, among other things;²³⁶ (3) requiring independent assessments of DOD's performance in contracting with small businesses and in transitioning technologies developed by small businesses into major weapons systems and major automated information systems;²³⁷ and (4) prohibiting DOD from outsourcing certain functions until it assesses whether DOD has carried out "sufficient outreach programs" to assist women-and minority-owned small businesses located in the geographic area "near" the military base where the function is performed.²³⁸

Other measures introduced by Members of the 112th Congress would:

- require that certain contracts and subcontracts which are financed with federal funds, but to which the federal government is not a party, "comply with provisions for small business assistance and protection that would have been applicable to the contract had the [government] been a party to the contract";²³⁹

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with SDBs).

²³² National Defense Authorization Act for FY2012, P.L. 112-81, §866, 125 Stat. 1526 (December 31, 2011).

²³³ An Act to Authorize Appropriations for Fiscal Years 1990 and 1991 for Military Activities of the Department of Defense, for Military Construction, and for Defense Activities of the Department of Energy, to Prescribe Personnel Strengths for Such Fiscal Years for the Armed Forces, and for other Purposes, P.L. 101-189, §834, 103 Stat. 1509-10 (codified, as amended, at 15 U.S.C. §637 note). The program has been expanded and/or extended several times since then. For more on the program, see generally <http://www.acq.osd.mil/osbp/programs/csp/background.html>.

²³⁴ Department of Homeland Security Authorization Act of 2011, S. 1546, §111.

²³⁵ National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1612 (requiring the Secretary of Defense to develop guidance ensuring that, at minimum, Office of Small Business Program heads serve as advisors to the Defense Acquisition Board and Information Technology Acquisition Board, and that the chiefs of the Armed Forces and acquisition executives coordinate with the Directors when approving requirements documents and acquisition strategies or plans).

²³⁶ *Id.*, at §1613.

²³⁷ *Id.*, at §§1614-1615.

²³⁸ National Defense Authorization Act for FY2013, H.R. 4310, as passed by the House, at §1696.

²³⁹ Depleting Risk from Insect Infestation, Soil Erosion, and Catastrophic Fire Act of 2012, H.R. 5960, §141.

- establish a preference for “local contractors”—or contractors that have their principal offices or locations within a 60-mile radius of the facility covered by the contract—in the award of contracts to veteran-owned small businesses under the Veterans Benefits, Health Care, and Information Technology Act,²⁴⁰ and
- allow surviving spouses or dependants who acquire the ownership rights of a member of the Armed Forces who owned at least 51% of a small business and was killed in the line of duty to be treated as if they were veterans with service-connected disabilities for purposes of contracting goals and preferences under the Veterans Benefits, Health Care, and Information Technology Act.²⁴¹

Yet other measures, addressing specific aspects of contracting or subcontracting with small businesses (e.g., goals), were discussed earlier in this report as examples of possible approaches to these issues (i.e., the enactment of agency-specific legislation).²⁴²

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²⁴⁰ A Bill to Amend Title 38, United States Code, to Direct the Secretary of Veterans Affairs to Give Preference to Local Contractors, and For Other Purposes, H.R. 6004, §1.

²⁴¹ Veterans Small Business Protection Act of 2012, S. 3405, §2.

²⁴² *See, e.g., supra* note 33 and accompanying text.