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May 11, 2018

Via Email to sec809@dau.mil

Section 809 Panel

Mr. David Drabkin, Chair, Commissioner, Team 4 Leader

1400 Key Blvd.

Suite 210

Rosslyn, VA 22209

Re: Comments to Section 809 Panel; Proposed Changes to Procurement System and Bid Protests; Small Business Issues

Dear Mr. Drabkin:

On behalf of the American Bar Association (“ABA”) Section of Public Contract Law (“Section”), I am submitting comments on points raised on and proposed changes to the procurement system and bid protests in a March 23, 2018 meeting.¹ The Section consists of attorneys and associated professionals in private practice, industry, and government service. The Section’s governing Council and substantive committees include members representing these three segments to ensure that all points of view are considered. By presenting their consensus view, the Section seeks to improve the process of public contracting for needed supplies, services, and public works.

The views expressed herein are presented on behalf of the Section. They have not been approved by the House of Delegates or the Board of Governors of the ABA and, therefore, should not be construed as representing the position of the ABA.²

¹ Mary Ellen Coster Williams, Section Delegate to the ABA House of Delegates, and Marian Blank Horn, Kristine Kassekert, and Heather K. Weiner, members of the Section’s Council, did not participate in the Section’s consideration of these comments and abstained from the voting to approve and send this letter.

² This letter is available in pdf format at http://www.americanbar.org/groups/public_contract_law/resources/prior_section_comments.html under the topic “Contract Formation & Bid Protests.”

I. INTRODUCTION

The Section 809 Panel was established pursuant to Section 809 of the National Defense Authorization Act of Fiscal Year (“FY”) 2016, as amended. The Section 809 Panel established nine teams to address its stated aim of “making recommendations, including actionable changes to regulatory and statutory language, to improve the acquisition process of the Department of Defense” (“DoD”).

The Section is pleased to have the opportunity to provide input on the Section 809 Panel’s consideration of proposed changes to the procurement system and bid protests. Below are the Section’s comments on the impacts of the proposed changes on small businesses and the need to ensure the continued significant participation of small businesses in DoD’s procurement system.

The Section understands that the Section 809 Panel might recommend categorizing procurements into four lanes: Lane 1 for readily available products and services; Lane 2 for products and services requiring minor customization; Lane 3 for products and services requiring major customization; and Lane 4 for products and services unique to DoD. The Section also understands that the Section 809 Panel might recommend eliminating small-business set asides from Lanes 1 and 2. Any recommendation to eliminate this foundational element to deliver on the Government’s policy commitment to supporting small business should consider how it would affect small businesses’ ability to continue leading innovation and driving the economy.

II. SMALL BUSINESSES ARE LEADERS IN INNOVATION, DRIVERS OF THE ECONOMY, AND AN ESSENTIAL PART OF DOD PROCUREMENT

The United States Government is the world’s largest purchaser of goods and services. Within the Government, DoD is the largest purchaser. “For more than half a century, it has been the policy of the Federal government to provide ‘maximum practicable opportunity’ for small businesses to participate in federal contracts.”³ It is the official policy of Congress that:

The essence of the American economic system of private enterprise is free competition. Only through full and free competition can free markets, free entry into business, and opportunities for the expression and growth of personal initiative and individual judgment be assured. **The preservation and expansion of such competition is basic not only to the economic well-being but to the security of this Nation. Such security and well-being cannot be realized unless the actual and potential capacity of small business is encouraged and developed.** 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, to insure that a fair proportion of the total purchases and contracts or subcontracts for property

³ U.S. Small Bus. Admin., *Interagency Task Force on Federal Contracting Opportunities for Small Businesses* at 3 (2010), https://www.sba.gov/sites/default/files/contracting_task_force_report_0.pdf.

and services for the Government (including but not limited to contracts or subcontracts 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.⁴

In maximizing opportunities for small businesses to participate in federal contracting, Congress recognized:

(i) that ownership and control of productive capital is concentrated in the economy of the United States and certain groups, therefore, own and control little productive capital;

(ii) that certain groups in the United States own and control little productive capital because they have limited opportunities for small business ownership; [and]

(iii) that the broadening of small business ownership among groups that presently own and control little productive capital is essential to provide for the well-being of this Nation by promoting their increased participation in the free enterprise system of the United States.⁵

To that end, almost 40 years ago, Congress established goals designed to help small businesses compete for federal contracts. First, Congress established a goal of awarding at least 23 percent of all federal prime-contracting dollars to small businesses. Additionally, Congress established goals for participation by small businesses that are owned by socially and economically disadvantaged individuals (5 percent), women (5 percent), and service-disabled veterans (3 percent), or that are located in Historically Underutilized Business Zones (3 percent).

These goals ensure that jobs and opportunities created by federal procurement are shared by all Americans. “Small businesses are leaders in innovation and drivers of the economy.”⁶ “Small businesses hold more patents than all of the nation’s universities and largest corporations combined, and create two thirds of all private sector jobs, employing half of all working Americans.”⁷ “When small businesses are excluded from federal contracts, the Federal government, American taxpayers and the nation’s economy lose out.”⁸

The Government not only encourages vital small-business participation through its small-business goals, but also focuses on small-business innovation through its Small Business Innovation Research (“SBIR”) and Small Business Technology Transfer programs. “Through

⁴ 15 U.S.C. § 631(a) (emphasis added).

⁵ *Id.* § 631(d)(2)(A).

⁶ *Interagency Task Force at 1, supra.*

⁷ *Id.*

⁸ *Id.*

these programs, the Federal Government encourages domestic small businesses to engage in Federal Research/Research and Development (R/R&D) that has the potential for commercialization.”⁹ “Through a competitive awards-based program, SBIR enables small businesses to explore their technological potential and provides the incentive to profit from its commercialization.”¹⁰ “By including qualified small businesses in the nation’s R&D arena, high-tech innovation is stimulated and the United States gains entrepreneurial spirit as it meets its specific research and development needs.”¹¹

“Small businesses currently represent 98 percent of all businesses in the United States and they generate nearly 64 percent of all net new jobs in this country.”¹² “Moreover, small businesses are generally considered to be the first line of employment and thus the initial training grounds for this nation’s workforce.”¹³ “The [U.S. Small Business Administration (“SBA”)] estimates that just over half of all employees in the U.S. work for a small firm, and that small business employers provide approximately 44.5 percent of payroll in the private sector.”¹⁴ “The most powerful statistic, however, is that 60 to 80 percent of all new jobs come from small businesses.”¹⁵

The small-business programs that would be minimized or eliminated under the Section 809 Panel’s proposal play an important role in supporting and encouraging small businesses. Small businesses have been, and are likely to continue to be, prime movers for innovation in government contracting. For example, in green technologies, “small firms” in one study “outperformed large firms in patent generality, originality, and patent growth.”¹⁶ These technologies foster reduced dependence on foreign energy sources and address the rising cost of energy; the future of the U.S. economy depends on moving away from fossil fuels, or using existing energy sources more efficiently.¹⁷ By stifling small businesses’ growth, the Section 809 Panel’s proposal will stifle these types of essential innovation.

The Section has concerns that the Section 809 Panel’s proposed changes to the procurement system and bid protests will minimize or eliminate the participation of small businesses in DoD procurement. If this happens, small businesses may be forced to close; DoD’s entrepreneurial spirit may suffer; and small-business owners and employees, including veterans, may lose their jobs. The Section strongly recommends that the Section 809 Panel follow the

⁹ U.S. Small Bus. Admin., *About SBIR*, <https://www.sbir.gov/about/about-sbir>.

¹⁰ *Id.*

¹¹ *Id.*

¹² Major L. Clark, III & Radwan N. Saade, U.S. Small Bus. Admin., *The Role of Small Business in Economic Development in the United States: From the End of the Korean War (1953) to the Present* at 7 (Sept. 2010), https://www.sba.gov/sites/default/files/advocacy/rs372tot_0.pdf.

¹³ *Id.*

¹⁴ *Id.*

¹⁵ *Id.*

¹⁶ Anthony Breitzman & Patrick Thomas, U.S. Small Bus. Admin., *Analysis of Small Business Innovation in Green Technologies* at 4 (Oct. 2011), <https://www.sba.gov/sites/default/files/rs389tot.pdf>.

¹⁷ *Id.*

General Services Administration's lead by recognizing that "[t]he central challenge . . . is to find the balance between gaining commercial-level efficiency to satisfy requirements and reduce administrative costs, while keeping the necessary protections for maintaining integrity, fairness, openness and public policy objectives" like supporting and developing small businesses.¹⁸

III. MAINTAINING ENFORCEABLE SET-ASIDES FOR SMALL BUSINESSES IS VITAL TO ENSURING SMALL BUSINESS PARTICIPATION

The Government's program of encouraging and requiring agencies to set aside certain prime contracts for small business¹⁹ is critical to ensure small businesses have reasonable opportunity to compete for federal prime contracts. Small business participation is achieved through governmentwide and agency-specific implementation of small-business goals and the "Rule of Two."²⁰ The Rule of Two is shorthand for the requirement that contracting officers set aside acquisitions for small business when reasonably expecting that at least two responsible small businesses will submit offers and award can be made at a reasonable price.²¹

We understand that the Section 809 Panel may propose eliminating the Rule of Two—indeed, all small-business set-asides—for Lane 1 and Lane 2 procurements. The Section 809 Panel has proposed an alternative rule that contracting officers select a small-business awardee in Lane 1 and Lane 2 procurements if they identify at least two small businesses who offer the product/service with satisfactory delivery and for a price within 5% of the lowest available price (what might be called the "Rule of 5%"). If such a rule were implemented, the Section believes it would **dramatically** reduce the prime contracts and dollars awarded to small business, which would negatively impact small businesses, the Government, and the country as a whole.

The proposed Rule of 5%, at first, sounds like the HUBZone price evaluation preference ("PEP"):

[I]n any case in which a contract is to be awarded on the basis of full and open competition, the price offered by a qualified HUBZone small business concern shall be deemed as being lower than the price offered by another offeror (other than another small business concern), if the price offered by the qualified HUBZone small business concern is not more than 10 percent higher than the price offered by the otherwise lowest, responsive, and responsible offeror.²²

¹⁸ U.S. Gen. Servs. Admin., *Procurement Through Commercial E-Commerce Portals Implementation Plan* at 8 (Mar. 2018), <https://interact.gsa.gov/sites/default/files/Commercial%20Platform%20Implementation%20Plan.pdf>.

¹⁹ Including subsets of small business, such as small businesses owned by socially and economically disadvantaged people ("8(a)"), small businesses in urban and rural communities ("HUBZone"), women-owned small businesses ("WOSB"), and service-disabled veteran-owned small businesses ("SDVOSB").

²⁰ See Congr. Research Serv., R42981, *Set-Asides for Small Businesses: Legal Requirements and Issues* at 2, 8 (2016), https://www.everycrsreport.com/files/20160128_R42981_45393f15487bcf762c1acec793b320d98cf5ff14.pdf.

²¹ FAR 19.502-2(b).

²² 15 U.S.C. § 657a(b)(3)(A).

Upon closer review, however, the HUBZone PEP is more favorable to HUBZone small-business concerns than the proposed Rule of 5% for two reasons: (1) the HUBZone PEP is a 10% preference, as opposed to the proposed 5%; and (2) the HUBZone PEP is triggered if any HUBZone small business is within 10% of the lowest large business price whereas the Rule of 5% would require the prices of two small businesses be within 5% of the lowest large-business price for either small business to benefit from the preference. Thus, the HUBZone PEP provides a greater benefit/advantage to HUBZone concerns than the proposed Rule of 5% will provide to small businesses.

The Section is concerned because data show that the HUBZone PEP has failed to ensure that HUBZone small businesses receive even close to their goal for prime-contract dollars. In the most recent report available on small-business program goals and performance, the SBA reported that \$6.9 billion in federal prime contracts had been awarded to HUBZone small businesses in FY 2016, which amounted to only 1.67% of the total prime-contract dollars awarded, well below the governmentwide HUBZone goal of 3%.²³ Data show that the vast majority (approximately 75%) of those prime dollars awarded to HUBZone small businesses are through HUBZone (or other small-business program) set-aside procurements or sole-source awards.²⁴ Only about 5% of the prime dollars awarded to HUBZone small businesses are through full-and-open competition with the HUBZone PEP applied.²⁵ Set asides are far more effective at ensuring prime-contract dollars are directed to HUBZone small businesses than the HUBZone PEP.

Even with set asides and the HUBZone PEP, the Government is not meeting its goals for prime contracts to HUBZone small businesses.²⁶ If set asides-were eliminated, the set-aside prime-contract awards to HUBZone concerns could not be made up through the HUBZone PEP, and the deficit from the 3% goal would grow larger. This is also consistent with data showing a direct correlation between the use of set-asides and federal agencies meeting their small-business goals.²⁷

Given that the Rule of 5% is likely to be invoked less often than the HUBZone PEP, it is likely that replacing all current set asides rules on Lane 1 and Lane 2 procurements with the Rule of 5% will lead to a significant reduction in prime-contract awards to small-business concerns.

²³ See U.S. Small Bus. Admin., *Government-Wide Performance, FY 2016 Small Business Procurement Scorecard*, https://www.sba.gov/sites/default/files/2018-02/SB_Procurement_Scorecard_Gov-Wide_final.pdf.

²⁴ See Robert Jay Dilger, Cong. Research Serv., R41268, *Small Business Administration HUBZone Program* at 2 (2018), <https://fas.org/sgp/crs/misc/R41268.pdf>.

²⁵ See *id.* The remaining approximately 20% is awarded to HUBZone concerns through full-and-open competition without benefit of the HUBZone PEP. *Id.*

²⁶ See 15 U.S.C. § 644(g)(1)(A)(iii) (Congress mandated the governmentwide HUBZone goal be set at not less than 3 percent of the total value of all prime contract and subcontract awards for each fiscal year); see also *FY 2016 Small Business Procurement Scorecard*, *supra* (showing governmentwide prime HUBZone goal missed by 45%).

²⁷ See Eagle Eye Publishers, Inc., U.S. Small Bus. Admin., *Characteristics of Recent Federal Small Business Contracting* at 8 (May 2012), <https://www.sba.gov/sites/default/files/397tot.pdf> (“[A]gencies that exceed their small business procurement goals use set-asides 3 percentage points more often than lower achieving agencies on average.”).

Furthermore, while there is a need for clearer data on this issue, it would appear that the types of transactions targeted for Lanes 1 and Lanes 2 are those in which small businesses currently have a significant market share, and therefore are most commonly set aside under the Rule of Two.²⁸ On the other hand, transactions targeted for Lanes 3 and 4 are areas in which small businesses are historically not major competitors, and thus there are likely fewer set-asides in the lanes where the Rule of Two would still apply.²⁹ As a result, eliminating the Rule of Two for Lanes 1 and Lanes 2 would drastically reduce the procurements and prime-contract dollars set aside for small businesses overall.

This reduction would hurt small businesses and, as a result, the Government and the United States as a whole. Small businesses are the backbone of the United States economy.³⁰ Studies have shown that small businesses create two out of every three net new jobs in the United States, contribute more than one-third of the gross national product, and are responsible for more than one-half of the nation's technological innovations.³¹ The Government's small-business goals and set-aside programs to support small businesses thus support the economy as a whole. In creating the SBA and set-aside programs, Congress recognized the unique and essential role of small businesses:

Congress considered small businesses to be the backbone of the American system of private enterprise and free competition. Finding that the nation's economic security and well-being depended upon the continued existence of small business, Congress created the Small Business Administration to assist and protect small businesses in so far as possible. In particular, the SBA was directed to work with other agencies to insure that small businesses received a 'fair proportion' of the total sales of government property.³²

The social goals of the set-aside program serve the interests of small businesses and the Government. Awarding federal contracts to small businesses provides those firms with the opportunity to develop, prosper, and create higher-paying jobs. Not only do set-asides help small businesses, but contracting with small business firms strengthens the economy, generates competition, creates

²⁸ For instance, data show that small businesses have a significant market share in NAICS codes such as 541611, 541511, 541519, 423430, 519130, 336413, 561612, 423430, and 443120. *See id.* at 27, 33, 34, 36, 41 and 46. Many contracts under these NAICS codes could be ordered as Lane 1 and/or Lane 2 transactions.

²⁹ Data show that many of the NAICS codes most commonly used by DoD, such as the manufacturing of armored vehicles, tanks, missiles, and aircraft, and R&D, represent contracts for goods/services that would likely be ordered under Lane 3 or Lane 4 procurements. *See id.* at 23, 32, 36. Except for construction, small businesses have a small market share in the NAICS codes most commonly used by DoD that would remain in Lane 3 or Lane 4 and remain subject to the Rule of Two. *See id.*

³⁰ *See* Alicia M. Cullen, *The Small Business Set-Aside Program: Where Achievement Means Consistently Failing to Meet Small Business Contracting Goals*, 41 Pub. Cont. L.J. 703, 706, 707 (2012) (quoting statements by George W. Bush and Barack Obama).

³¹ *See* Kendall L. Miller, *Hubzones: Moving from the Racial Battleground to the Economic Common Ground*, 3 J. Small & Emerging Bus. L. 367, 385 (1999).

³² *Duke City Lumber Co. v. Butz*, 382 F. Supp. 362, 366 (D.D.C. 1974).

innovation, enhances good business practices, and provides more jobs than any other sector of the economy. Thus, when a small business receives a federal contract, it is truly a “win-win.” The small business gets the income it needs to expand and create jobs while the Government benefits from contracting with some of the most “diligent, innovative and responsible people of the world.”³³

Studies confirm that the impact of small-business set asides reaches beyond the specific small businesses that receive the awards. For example, studies have shown that when government agencies meet or exceed their small-business goals, the number of small businesses graduating to large-business status increases, and the number of small businesses entering the government-contracts market also increases.³⁴ Other studies have shown that set-aside programs have significantly increased the proportion of businesses that are minority-owned.³⁵

In the Small Business Act of 1953, Congress stated one of the objectives was “to insure that a fair proportion of the total purchases and contracts for property and services for the Government . . . be placed with small-business enterprises.”³⁶ But because the desired result did not materialize, 35 years later Congress began mandating quantifiable small-business procurement goals to ensure small businesses received maximum practicable opportunities in federal procurement.³⁷ Decades later, federal agencies are still working to meet these goals.³⁸ Federal agencies have undoubtedly improved in meeting these goals,³⁹ but some of the reported progress remains the illusory results of reporting errors⁴⁰ and data exclusions.⁴¹ Sixty-five years

³³ Alicia M. Cullen, *supra*, 41 Pub. Cont. L.J. at 708.

³⁴ See *Characteristics of Recent Federal Small Business Contracting*, *supra*, at 6.

³⁵ Aaron K. Chatterji, et al., *The Impact of City Contracting Set-Asides on Black Self-Employment and Employment*, NBER Working Paper No. 18884, at 34 (Mar. 2013), later published in 32 J. of Lab. Econs. 3 (2014) (“We find that set-asides had a large and significant impact on African-American business ownership during the 1980s, with the black-white self-employment gap falling by three percentage points. These gains were realized entirely in the industries targeted by set-asides and correspond with other information on the growth in, and the set-aside amounts awarded to, black-owned businesses”), <http://www.nber.org/papers/w18884.pdf>.

³⁶ See Henry B. R. Beale, U.S. Small Bus. Admin., *Evaluation of the Small Business Procurement Goals Established in Section 15(g) of the Small Business Act* at 3 (June 2014) (quoting The Small Business Act of 1953, Pub. L. No. 83-163, § 202(a)), <https://www.sba.gov/sites/default/files/files/rs423tot.pdf>.

³⁷ See *id.* at 4-5.

³⁸ See, e.g., U.S. Small Bus. Admin., *Government-Wide Performance, FY 2007 Small Business Procurement Scorecard* (reflecting government-wide failure to meet four of five goals in FY 2007), https://www.sba.gov/sites/default/files/2018-02/gov_wide_assessment2007_0.pdf.

³⁹ See U.S. Small Bus. Admin., *FY 2016 Small Business Procurement Scorecard: Summary by Prime Spend*, https://www.sba.gov/sites/default/files/2018-02/FY16_SB_Procurement_Scorecard_Summary_Final.pdf.

⁴⁰ U.S. Small Bus. Admin., OIG Rep. No. 14-18, *Agencies Are Overstating Small Disadvantaged Business and HUBZone Goaling Credit by Including Contracts Performed by Ineligible Firms* (2014), <https://www.sba.gov/sites/default/files/oig/Agencies%20Are%20Overstating%20SDB%20and%20HUBZone%20Goaling%20Credit.pdf>; U.S. Small Bus. Admin., OIG Rep. No. 13-02, *Report on the Most Serious Management and Performance Challenges Facing the Small Business Administration In Fiscal Year 2013* at 1 (2012), <https://www.sba.gov/sites/default/files/FY%202013%20Management%20Challenges%20OIG%20Report%2013-02%20.pdf>.

after the Small Business Act of 1953, the Government is just beginning to achieve Congress's objective of ensuring a fair proportion of government procurement dollars go to small businesses. It would be detrimental to small businesses, the Government, and the country as a whole, to eliminate small-business set-asides in favor of the Rule of 5% for many government procurements, because doing so would likely lead to a significant reduction in prime-contract dollars awarded to small businesses, just as the Government was finally beginning to achieve its small-business objectives.

IV. SMALL BUSINESS PARTICIPATION DOES NOT SIGNIFICANTLY INCREASE THE COST OF GOVERNMENT CONTRACTING

A. Empirical Research Shows that Small Business Participation May Result in Savings.

While economists and procuring agencies might reasonably expect restrictions on competition—even those predicated on important policy considerations—to result in increased costs, close study reveals that this need not be the case for small-business set-asides. Indeed, a representative modern study showed the opposite: healthy small-business engagement had virtually no cost impact on procurement. The cost variance that did appear actually favored small-business participation.

The study followed a test case with applications beyond the services being procured, the U.S. Army Corps of Engineers' procurement of dredging services, at that time a \$300-\$400 million per year effort.⁴² The Corps of Engineers used lowest-price technically-acceptable contract vehicles, and compared contracts that had been set aside for small businesses with those procured through full-and-open competition.⁴³

The study found “[n]o evidence . . . to support the hypothesis that set-asides increase costs.”⁴⁴ In all but one comparison, the study found “no significant difference” between the bids submitted by small businesses as part of set-aside procurements and those submitted during full-

⁴¹ See Staff of House Subcomm. on Contracting and the Workforce, Comm. on Small Business, 114th Cong., *Hearing: Continuing Challenges for Small Contractors* at 4-5 (Nov. 16, 2015), https://smallbusiness.house.gov/uploadedfiles/11-18-2015_hearing_memo.pdf; J.D. Harrison, *Small Business Contracting Numbers Inflated by Errors and Exclusions, Data Show*, Wash. Post, July 29, 2013, https://www.washingtonpost.com/business/on-small-business/small-business-contracting-numbers-inflated-by-errors-and-exclusions-data-show/2013/07/28/7fa2a4fc-f2f6-11e2-8505-bf6f231e77b4_story.html?utm_term=.ae7a702882a6.

⁴² Thomas A. Denes, *Do Small Business Set-Asides Increase the Cost of Government Contracting?*, 57 Pub. Admin. Rev. 441, 443 (1997).

⁴³ *Id.* at 442.

⁴⁴ *Id.* at 443.

and-open competition.⁴⁵ The only statistically significant difference in bids, in fact, came from bids that were lower under set-asides than under full-and-open competition.⁴⁶

In analyzing why an entire series of restricted competitions would have resulted in no cost increase plus cost savings in one instance, the authors cited facts critical to understanding the results. More firms placed bids on the set-aside solicitations than on the unrestricted solicitations: an average of 3.6 set-aside bidders versus 3.1.⁴⁷ The study's authors found "there is a large population of qualified set-aside participants who only bid on set-aside procurements."⁴⁸

The conclusion that setting aside procurements for small businesses draws upon otherwise untapped—or incompletely tapped—market sectors is supported by an earlier study demonstrating that when Bay Area Rapid Transit system contracts were reduced in size, more small firms than large firms bid on the contracts.⁴⁹ This is consistent with Government Accountability Office findings indicating that small businesses can drive competition and cost savings. For example, the Department of State opened to competition in 2007 a previously noncompetitively awarded procurement for installation and maintenance of technical security equipment in U.S. embassies.⁵⁰ After taking that step,⁵¹ State ultimately made four awards on the contract, all to small businesses, for a total savings of over \$218 million.⁵²

Individual case studies also support this conclusion. A recent U.S. Army small-business set-aside solicitation for information-technology support services yielded "an overwhelming 69 responses."⁵³ What is more, the predecessor contract had been held by a large business.⁵⁴ The winning small-business proposal not only saved the Army money relative to the predecessor contract—at roughly \$5.3 million per year versus \$7.6 million in the year preceding award—it also "significantly beat" even the Army's independent government cost estimate.⁵⁵

⁴⁵ *Id.*

⁴⁶ *Id.*

⁴⁷ *Id.*

⁴⁸ *Id.* at 444.

⁴⁹ *Id.*

⁵⁰ U.S. Gov't Accountability Office, *Promoting Competition for the Over \$500 Billion in Federal Contracts Can Potentially Save Billions of Dollars Over Time*, [https://www.gao.gov/modules/ereport/handler.php?1=1&path=/ereport/GAO-11-318SP/data_center_savings/General_government/Promoting_competition_for_the_over_\\$500_billion_in_federal_contracts_can_potentially_save_billions_of_dollars_over_time#f1](https://www.gao.gov/modules/ereport/handler.php?1=1&path=/ereport/GAO-11-318SP/data_center_savings/General_government/Promoting_competition_for_the_over_$500_billion_in_federal_contracts_can_potentially_save_billions_of_dollars_over_time#f1); *see also* https://www.gao.gov/duplication/action_tracker/Competition_for_Federal_Contracts/action1#t=0.

⁵¹ At the recommendation of the GAO.

⁵² *Promoting Competition for the Over \$500 Billion in Federal Contracts Can Potentially Save Billions of Dollars Over Time*, *supra*; *see also* https://www.gao.gov/duplication/action_tracker/Competition_for_Federal_Contracts/action1#t=0.

⁵³ Daniel P. Elkins, *Small Business IT Contract Saves Millions*, U.S. Army (Aug. 22, 2013) https://www.army.mil/article/109799/small_business_it_contract_saves_millions.

⁵⁴ *Id.*

⁵⁵ *Id.*

Apart from the immediate financial benefit to individual agencies, a robust small-business community adds structural benefits to the larger economy, adding value and providing for a more fertile market from which to reap cost benefits. The literature holds that small businesses are “an important part of the economy of modern nations because they diversify economic power.”⁵⁶ This diversification helps to “create a stable employment environment because the loss of a few small businesses does not have the social repercussions of the loss of a large business.”⁵⁷

B. Small Business Participation Does Not Significantly Increase Costs.

It is true that some studies have shown slightly increased costs when comparing set-aside or other small-business-restricted competitions with unrestricted competitions. Those costs, where they have been observed,⁵⁸ do not constitute significant increases over the cost of unrestricted competition. Further, they stem not from an inherent expense within small-business contracting, but rather from identifiable externalities and barriers to entry that many small businesses struggle against. Finally, even the author of studies that measure a modest increase in costs attributable to higher bids on some set-aside procurements has found that removing small-business incentive programs can lead to a substantial *increase* in costs.

Professor Justin Marion of the University of California at Santa Cruz has produced studies indicating that small-business participation can increase procurement costs, with a correlation between slightly increased bid prices and the application of small-business preferences.⁵⁹ The actual increase in costs, however, remains relatively insignificant. One such study, for instance, showed that in a federal procurement applying small-business preferences, “[l]arge firms bid 1.4 percent lower on auctions using bid preferences, while the lowest cost small firms increase their bid on preference auctions by 1.4 percent.”⁶⁰

Prof. Marion does, however, describe as “significant” the “[b]arriers to entry and expansion into the highway procurement market” faced by many of what he refers to as “disadvantaged business enterprises” (“DBEs”).⁶¹ These outward pressures—rather than the nature of restricted small-business procurement itself—he postulates, “could lead to restricted

⁵⁶ Denes, *supra*, 57 Pub. Admin. Rev. at 442.

⁵⁷ *Id.*

⁵⁸ As discussed *supra*, other empirical and individual case studies have found the opposite: that small business participation has either a neutral or beneficial effect on cost.

⁵⁹ Justin Marion, *Are Bid Preferences Benign? The Effect of Small Business Subsidies in Highway Procurement Auctions*, 91 J. Pub. Econ. 1591 (2004) <https://web.stanford.edu/group/SITE/papers2005/Marion.05.pdf>; Justin Marion, *How Costly Is Affirmative Action? Government Contracting and California’s Proposition 209*, 91 Rev. of Econ. and Stats. 503 (2007), <http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.365.2237&rep=rep1&type=pdf>; Justin Marion, *Affirmative Action Exemptions and Capacity Constrained Firms*, 9 Am. Econ. J.: Econ. Pol’y 377 (2016), https://people.ucsc.edu/~marion/Papers/gfe_round2_v2.pdf.

⁶⁰ Justin Marion, *supra*, 91 J. Pub. Econ. 1591.

⁶¹ Justin Marion, *supra*, 91 Rev. of Econ. and Stats. 503.

competition and market power in some markets, or an upward sloping DBE supply curve.”⁶² Other factors such as “[t]he pre-qualification process, which requires past experience, and the need for bonding,” as well as “imperfect access to capital” also likely contribute to create challenges that may “lead[] to an inability to enter the procurement market or expand to take advantage of new opportunities.”⁶³ Those external forces may in turn artificially drive up operating costs for small businesses.

Helping small businesses overcome such obstacles is a goal of many small-business programs. It is no surprise, then, that Prof. Marion found in still another study that removing a small-business exemption program led to a difference in bid price that “grew substantially.”⁶⁴ Prof. Marion studied a small-business contracting program used by the Iowa Department of Transportation, in which “[f]irms build a history of DBE utilization to obtain exemption eligibility when demand is low and capacity constraints are slack, and then take advantage of the exemption when capacity constraints bind.”⁶⁵ Predicting that “[t]his could reduce government cost,” Prof. Marion indeed found that the study’s “results suggest that the exemption program improved efficiency, in that it reduced costs without adversely affecting DBE utilization.”⁶⁶ Evidence also suggested that large business-prime contractors valued the program.⁶⁷

V. POSSIBLE CHANGES TO THE BID PROTEST PROCESS WOULD HAVE WIDESPREAD IMPACT BEYOND THE PROTEST PROCEDURES THAT WOULD DISPROPORTIONATELY AFFECT SMALL BUSINESSES

The Section understands that the Section 809 Panel might recommend changes to the protest process that, from the Panel’s perspective, reduce the protest timeline and increase transparency. For Lanes 1 and 2, which would consist of what the FAR currently characterizes as commercial supplies or services, the Section 809 Panel might recommend eliminating solicitations, permitting only post-award protests without a stay of performance, and creating a single remedy of a 5% “bounty” for successful protests. For Lanes 3 and 4, the Section understands that the Section 809 Panel might recommend continuing pre- and post-award protests and additional remedies, but the specifics remain unclear to the Section.

For all lanes, jurisdiction would be a panel operating on a condensed timeline, rather than a court or the Government Accountability Office. Finally, the Section 809 Panel may recommend that the entire contract file be posted for the public, including evaluation documents and debriefings.

Pre-award protests allow the industry to self-regulate: businesses file protests ensuring terms are unambiguous, size status is correct, and undue competitive restrictions are removed.

⁶² *Id.*

⁶³ *Id.*

⁶⁴ Justin Marion, *supra*, 9 Am. Econ. J.: Econ. Pol’y 377

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ *Id.*

Eliminating pre-award protests will escalate the risk of non-performance, fraud, and negative impact on small businesses and competition.

Eliminating pre-award protests creates a risk of non-performance, especially with less-experienced small businesses unaware of the Government's standards, because it removes an avenue to ensure understanding of the requirements. Without that understanding, there may be no meeting of the minds to form a contract. This is true even in Lanes 1 and 2 as the Section 809 Panel has conceived them, because these acquisitions would still require delivery terms and other conditions. Without a meeting of the minds, non-performance risk (and resultant costs to the Government) will increase.

Removing pre-award protests for Lanes 1 and 2 would also eliminate size and status eligibility protests, which help the Government ensure that only true small businesses receive small-business awards. Size-status protests allow protesters to rebut the self-reported size status of the apparent awardee. Status-eligibility protests ensure that an offeror meets the eligibility requirements for the socioeconomic category and prevents fraud, a legitimate concern in federal acquisitions.⁶⁸

Eliminating small-business set asides may create even more risk related to size status. Without pre-award protests, a large business could register as a small business and receive a price preference for award. Size and status protests are the best way to prevent this type of fraud.

While the Section 809 panel seeks to increase competition, removing solicitations and pre-award protests will have the opposite effect because they are the checks on unduly restrictive requirements. No other method ensures the Government promotes competition, uses brand-name and other justifications only when necessary, and does not favor familiar or incumbent companies. Without these pre-award protests, the integrity of the acquisition process, small-business programs, and competitive pricing are all at risk.

These effects will disproportionately affect small businesses. As the Section 809 Panel cited, Lanes 1 and 2 make up the majority of acquisitions, even if not the majority of dollars awarded. Currently, all commercial-item contracts below the simplified acquisition threshold plus many other actions are set aside for small businesses. These smaller-dollar awards are core revenue sources for many small businesses. Being unable to protest the size status or restrictive selection of large-business competitors will hamstring small businesses in continuing to compete for government work in these procurements.

Finally, a 5% "bounty" would be insufficient to cover the time and effort of a company filing a protest, so this change would discourage protests. The protest system would no longer be beneficial to the Government for generating lessons learned, because many businesses would not file otherwise meritorious protests for want of a real incentive to do so. Small businesses especially would require additional assistance to cover costs of diverting their personnel to work

⁶⁸ See Matthew Weigelt, *SBA Leader Vows to Crack Down on Small Business Fraud*, FCW (Apr. 21, 2010), <https://www.lexology.com/library/detail.aspx?g=bccac128-4064-4c3f-bdfc-f13928c07b46>; <https://fcw.com/articles/2010/04/21/sba-mills-cracking-down-fraud.aspx>

on the protest as well as legal fees. This 5% bounty should, at the very least, be in addition to actual filing costs and attorneys' fees.

The larger issue is that even if a protester correctly protested and the selected awardee was not entitled to award, Lanes 1 and 2 would not provide a stay of contract performance. Therefore, the Government would be rewarding companies that may not have been properly selected for award by allowing them to continue performance. Whether it be for improper evaluation, incorrect size status, fraud or bias, these issues should have a venue that allows the contract to be re-evaluated if necessary.

VI. THERE ARE SIGNIFICANT PROCEDURAL UNCERTAINTIES AND PRACTICAL ISSUES WITH THE SECTION 809 PANEL'S POTENTIAL RECOMMENDATIONS

Even if the balance between gaining commercial-level efficiency and protecting integrity, fairness, openness, and public policy objectives would favor the Section 809 Panel's lanes approach, and that all relevant statutes and regulations could be amended to allow for the efficiency envisioned (such as the elimination of size and status protests), numerous uncertainties and practical issues would need to be addressed.

First, because there would be no solicitation, it is unclear how the contracting officer will ensure the products or services are offered under the same terms and conditions to provide a useful comparison.

Second, there would be no mandatory sources of market research, such as the Multiple Award Schedules Program and GSA's anticipated E-Commerce program. Thus, a contracting officer could search large businesses' websites and find no small-business price for comparison, even if small-business pricing is readily available.

Third, as explained above, there is no significant incentive to award to small business, because an agency's worst outcome for not awarding to the small business is paying a 5% bounty following a protest. The agency might have had to pay that premium anyways if it had awarded to a small business that had come within 5% of the lowest large-business price.⁶⁹

Fourth, it is not clear how the whole process would work. After the contracting officer's market research, would the contracting officer contact the business with an offer? What would the offer terms be? Could the business reject the offer? If the initial offer was rejected, could the agency negotiate the price or terms with the business? If the agency could negotiate, would it be required to negotiate with other businesses considered as part of the market research and allow them to meet the price and terms (or be within 5% for a small business)?

⁶⁹ It is also unclear whether there would be any pre-award mechanisms that enforce a small business pricing preference.

Fifth, would the current restrictions on bundling remain or could a contracting officer bundle multiple products such that there is only one, non-small offeror capable of meeting this bundled requirement?⁷⁰

Sixth, it is not clear how Lanes 1 and 2 could ever work for services and construction. Even basic services like janitorial or food services require location-specific customization that cannot be covered by a pricing sheet alone. For example, one relevant term is whether the Government or the contractor will provide the supplies necessary to complete the services. Another relevant term is whether there is a union agreement in place that dictates specific wages and health and welfare. Similarly, is there an applicable Service Contract Act wage determination? At what point does addressing these questions become customization?

Seventh, would past performance be considered at all in Lanes 1 and 2? Without considering past performance, there is no guarantee that the Government will get satisfactory performance or that the business can meet the scale of products or services needed.⁷¹ Finally, which specific provisions would be required? DoD will expose itself to significant and unjustifiable risk if it does not require the cybersecurity and counterfeit parts clauses to be included in every Lane 1 and 2 procurement. Other clauses may not affect DoD's mission, but are required to implement the stated policies of Congress, including prohibitions on human trafficking and the domestic preference programs (Buy American, Trade Agreements Act, Berry Amendments, the Federal Transit Administration's Buy America programs). If Buy American is required or included, there are similar questions as to how the 5% small-business price preference would be applied.

In general, the Section 809 Panel's approach would reduce existing controls and introduce significant uncertainty and risk which will affect readiness and national security.⁷² It would also place a significant burden on already overworked contracting officers to provide technical approaches to offerors, instead of the current system which requires contractors to do this leg work.

If the Section 809 Panel insists on reducing the existing controls for Lanes 1 and 2 and reducing the role of small businesses, the Section recommends at least requiring that each Lane 1 and 2 procurement publish an Invitation for Bid that provides standardized terms, conditions, and product requirements that will also allow offerors to self-identify their willingness to sell to the

⁷⁰ See 15 U.S.C. § 631(j)(3) ("In complying with the statement of congressional policy expressed in subsection (a) [of this section], relating to fostering the participation of small business concerns in the contracting opportunities of the Government, each Federal agency, to the maximum extent practicable, shall . . . avoid unnecessary and unjustified bundling of contract requirements that precludes small business participation in procurements as prime contractors.").

⁷¹ See, e.g., Patricia Mazzi, *FEMA Contract Called for 30 Million Meals for Puerto Ricans. 50,000 Were Delivered*, N.Y. Times, Feb 6, 2018, <https://www.nytimes.com/2018/02/06/us/fema-contract-puerto-rico.html>.

⁷² See U.S. Dep't of Def., OIG Rep. D-2011-088, *Ballistic Testing for Interceptor Body Armor Inserts Needs Improvement* (2011), <https://media.defense.gov/2011/Aug/01/2001712877/-1/-1/1/D-2011-088.pdf>; Eric Schmitt, *Dealer Accused of Selling Banned Munitions to Army*, N. Y. Times, June 21, 2008, <https://www.nytimes.com/2008/06/21/washington/21arms.html>.

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agency, which will allow a useful comparison and consideration of small businesses. DoD will also realize a cost savings, as most offerors should be willing to sell below their price sheets to DoD, whereas the system proposed by the Section 809 Panel would lead to contracting officers' paying full catalog price.

VII. CONCLUSION

The Section appreciates the opportunity to provide feedback to the Section 809 Panel to further its efforts to reconsider bid protest practices. The Section is available to provide additional information or assistance as you may require.

Sincerely,



Aaron Silberman
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