



U.S. SMALL BUSINESS ADMINISTRATION
WASHINGTON, D.C. 20416

FEB 17 2005

The Honorable John F. Kerry
Ranking Member
United States Senate
Committee on Small Business and Entrepreneurship
Washington, DC 20510

Dear Senator Kerry:

Administrator Barreto asked me to respond to your letter of January 25, 2004, regarding the U.S. Small Business Administration (SBA), Office of Advocacy's report of December 28, 2004, identifying apparent award of small business set-aside contracts to 44 firms found to be "other than small." Specifically, you asked that SBA address the following five issues:

- 1. Approximately eighty-eight percent of the awards cited in the report that went to businesses that were "other than small" were made through multiple award or Indefinite Delivery Quantity (IDIQ) contracts. Small businesses have also pointed to the widespread use of this type of contract as a barrier for small firms to effectively compete for contracts. What leadership role has the SBA taken or will it take to ensure that the growing number of multiple award and IDIQ contracts is not having a deleterious effect on small firms?**

We believe that multiple award vehicles are not intrinsically deleterious to small businesses, and can provide significant opportunities to them when they are appropriately structured and utilized. For example, at the direction of the President, the General Services Administration (GSA) is creating a Government Wide Acquisition Contract (GWAC) specifically targeted toward Service-Disabled Veteran-Owned Small Businesses. This vehicle will permit potential award of billions of dollars to those who have given so much to our country.

Currently, there are GWACs for HUBZone-certified firms and 8(a)-certified firms. In FY 2004, sales to small businesses in the 8(a) FAST GWAC topped \$2 billion, with more than 80% of firms receiving orders. While the term has expired on FAST, it has been replaced by the 8(a) STARS GWAC, which provides for up to \$15 billion in awards to 8(a) firms over the next 10 years. Historically, it is noteworthy that small businesses receive approximately 25 percent of requirements off of GSA schedules.

However, SBA is working with GSA and other agencies to make sure that small businesses have the best possible opportunity to compete on all contracts, including IDIQ vehicles. One example of our success in improving small business participation on IDIQs is the October 20, 2003, publication of final regulations on contract bundling. This regulation revised the definition of contracting bundling, to include orders placed against multiple award contract vehicles and task and delivery order contracts. The rule also requires contract bundling reviews on contracts and orders under multiple award contracts above established thresholds to prevent unnecessary and unjustified bundling; requires procuring activities to coordinate

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with their small business specialist on proposed acquisition strategies for contracts and orders above established thresholds; and requires that Directors, Office of Small and Disadvantaged Business Utilization at Federal agencies, perform periodic reviews to assess the extent to which small businesses are receiving their fair share of Federal procurements, the adequacy of contract bundling documentation and justifications, and the adequacy of actions taken to mitigate the effects of necessary contract bundling on small businesses.

- 2. Given that 79 percent of the contracts found to go to companies that are "other than small" were awarded by the Department of Defense or the General Services Administration, how does SBA intend to increase its oversight of these agencies?**

Our internal review of the Office of Advocacy report does not indicate that small business set aside contracts are being awarded to large businesses. As explained more fully under paragraph 4 below, based on our preliminary review of the Office of Advocacy report, we believe that only a small number, if any, of the 44 large businesses cited were awarded contracts that were, in fact, intended for small businesses.

However, SBA takes its oversight responsibilities very seriously. Accordingly, we are planning to hire a supervisory Procurement Center Representative (PCR) for GSA's headquarters facility, and PCRs for several Department of Defense (DOD) installations. Please note that PCRs can initiate SBA size determinations if they believe that specific contracts set aside for small business are being awarded to large firms.

Additionally, concurrent with changes to SBA regulations, the Federal Acquisition Regulatory Council amended the Federal Acquisition Regulations to increase oversight of orders placed against multiple award contracts, multiple award schedule contracts and GWACs. Further, SBA is considering possible regulatory changes to address the frequency with which small businesses must recertify their small business size status, in order to better monitor business size on long term contracts. This is particularly important given that for some contract types, such as GWACs, the base period plus options can extend up to 15 to 20 years.

- 3. What monitoring efforts are being led by the SBA to ensure that companies on the CCR database are not receiving contracts as small businesses that do not qualify for such status?**

There seems to be a misunderstanding of the role of CCR. CCR exists to help contracting officers to perform market research, and to facilitate payment of contractors. Companies do not obtain contracts through CCR, and being registered as small in CCR does not excuse companies from having to certify their size status through official representations and certifications. That is, for contracts awarded under procurement preference programs, businesses must self-represent (certify) that they are small at the time they submit their initial priced offers.

It is important to note that self-representations of successful offerors may be protested by contracting officer or other bidders. In such circumstances, SBA conducts formal size

determinations to assess firms' size status. From the small businesses perspective, this is a relatively simple process. It does not require filing excessive documentation, or hiring a lawyer, and SBA makes size determinations expeditiously.

Since SBA is not provided with the names of businesses competing for and winning contracts, it must often rely on contracting officers and other bidders to challenge cases in which large businesses may have been awarded contracts reserved for small businesses. The businesses cited in the Advocacy report are well known. Therefore, it is very likely that any inappropriate small business set-aside contract awards to these firms would have been protested. To date, SBA's review of these contracts has not disclosed any fraudulent behavior. However, if fraudulent actions are discovered we will forward the matters to the Inspector General for further investigation and possible referral to the Department of Justice for prosecution.

SBA is working closely with the Integrated Acquisition Environment (IAE) e-Government Initiative to improve the accuracy of information regarding the small business and other socio-economic characteristics of CCR registrants, and to eliminate confusion and misperceptions about small business size status. We have implemented an automated check of registrants' small business status by North American Industry Classification System (NAICS) industry code. Further, we have inserted an advisory notice to registrants that employment and revenue information entered into CCR should include that of parent and other affiliated companies, if any. Also, we have established a process for resolving registrants' questions on the small business status, and built Internet links to additional sources of information related to socio-economic procurement preference program terminology. This year we are removing existing CCR self-representation provision for HUBZone, 8(a), and small disadvantaged business procurement preference programs, and replacing it with authenticated data, based on SBA certification.

4. **In a January 3, 2005, report in the Federal Times, David Drabkin, Deputy Chief Acquisition Officer at GSA claimed that "no contracts set aside for small business competitions were awarded to large businesses, despite miscoding." Does the SBA agree with the assertion that no small business contracts that were set-aside for small firms were awarded to firms that were "other than small?" If not, what actions has the SBA taken to set the record straight with GSA and its procurement officials? If so, how does the SBA reconcile Mr. Drabkin's statement with the conclusions made by the Office of Advocacy in its December 28, 2004, report? Were there legitimate small businesses available that were capable of doing the work that was awarded to these 44 firms?**

We substantially agree with Mr. Drabkin's statement that no contracts set aside for small business competition were awarded to large businesses, despite miscoding. SBA recognizes that the miscoding of contracts has been found to be part of the reason why large businesses are reported as holding small business contracts. To date, our review of the Office of Advocacy's study does not suggest that miscoding is responsible for the results of the study.

Our preliminary review of the Office of Advocacy report suggests that the findings are attributable to the maturation of the small businesses originally awarded the contract. It

appears that the contracts were awarded to businesses that were small at the time of award but grew into businesses that would no longer qualify as small during or after contract performance, or were acquired by, or merged with, other businesses and become large during or after contract performance. That is, businesses that were small at the time of contract award became large through growth or reorganization during the course of contracts, or after contract performance was completed. At this time, we believe that the majority of the 44 large businesses identified in the December 2004 Advocacy report were not awarded contracts that were reserved for a small business.

SBA applauds the success of small businesses that become large businesses, and we are happy to see that Government contracting contributed to that success. But, we also recognize that in today's environment of long term contracting, it no longer makes sense to count firms as small throughout the life of the contract when major events change the nature of the business. For this reason, in May 2004, long before the Advocacy study was released, we issued a final rule requiring that firms recertify their size status when they novate contracts with the Federal government. This means that firms that become large due to mergers and acquisitions will need to recertify size status when they execute novation documents with respect to the contract. This rule became effective December 21, 2004.

Please note that SBA is working on a final rule that will address how often businesses need to recertify size on multiple award contracts such as the GSA schedules. This rule will address firms that grow over the life of the contract. We are also addressing how best to count firms that grow through mergers and acquisition.

In April 2003, SBA issued a proposed rule suggesting that firms annually recertify their size. While some supported this approach, many small businesses and trade associations commented on the rules, suggesting that annual recertification may create disincentives for growth. Members of Congress, including Congresswoman Nydia Velasquez, Congressman Charles Gonzales, and Congressman Tom Davis, urged SBA not to adopt this proposal, believing that it imposed an undue burden on small businesses. Since that time, SBA has been analyzing the responses and the implications of each of the policy alternatives, and we expect to have a final rule soon. In the interim, GSA and OFPP are requiring that small businesses recertify their size on schedules and GWACs at the time of option, not to exceed every 5 years.

The policy changes outlined above represent a departure from the policy of only assessing a firm's size at the time of offer and award, but are necessary improvements to protect the integrity of small business awards. While SBA has not found, nor does the Advocacy report suggest, any instances of fraud, SBA remains committed to ensuring that small business set asides benefit true small businesses.

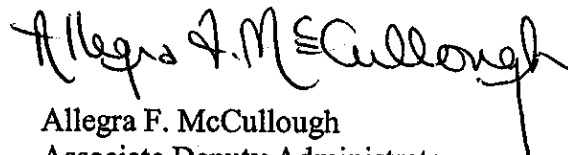
- 5. Given the misrepresentation found in the FY 2002 small business utilization data and the need for a significant increase in oversight of Federal contracting, I request that the SBA perform a complete and independent audit of the FY2003 small business utilization report to be completed and submitted no later than July 1, 2005.**

Please be assured that we are thoroughly investigating the report's assertions to determine whether there was any malfeasance. However, we must respectfully decline your request for a full audit of the FY 2003 data. The Federal Procurement Data System (FPDS) database is neither controlled nor managed by SBA. Rather, it is operated by GSA on behalf of the Office of Federal Procurement Policy (OFPP). Therefore, any request for audit of data is more appropriately addressed to GSA and OFPP.

The Federal government has recognized that there were problems with FPDS data. For this reason, it is implementing FPDS-NG (Next Generation), a dynamic database that will capture data from direct contract writing systems rather than through error prone manual data entry. Further, as part of the Integrated Acquisition Environment, it will incorporate checks against CCR and the Online Representation and Certification Application (ORCA) to verify the status of contractors. Finally, it will provide more reliable, detailed and relevant contracting information. For these reasons, we believe that small businesses, tax payers, and oversight agencies will be well served by our work on the new system.

I trust that this information is responsive to your request, and proves useful to you. Thank you for your continued support of our programs and services. Should you need additional information, please contact Mr. Michael Berkholtz, Office of Congressional and Legislative Affairs on 202-619-0297.

Sincerely,

A handwritten signature in black ink that reads "Allegra F. McCullough". The signature is written in a cursive style with a large, sweeping flourish at the end.

Allegra F. McCullough
Associate Deputy Administrator
for Government Contracting
and Business Development