



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

July 30, 2008

The Honorable Henry A. Waxman  
Chairman, Committee on Oversight and Government Reform  
U.S. House of Representatives  
Washington, DC 20515

Dear Chairman Waxman,

This letter responds to your March 10, 2008 request that the U.S. Small Business Administration (SBA) “initiate an inquiry into whether Blackwater Worldwide (Blackwater) has complied with federal small business laws and take any appropriate enforcement action.” As you know, on March 14, 2008 former Administrator Preston referred your inquiry to the SBA Office of Inspector General (OIG), which gave the task to one of its employees.

As you can see from the attached memorandum, the SBA OIG’s employee identified several procurements where Blackwater affiliates received small business set-aside contracts, and the OIG employee has forwarded this information to the relevant procuring agencies. The OIG employee’s memorandum contains minimal information and no conclusion with respect to the issue of whether Blackwater or its affiliates complied with small business laws. Nor has the employee reached any conclusion as to whether any Blackwater affiliate is a small business for a particular procurement. The sum of the report is the OIG employee could not reach a firm conclusion that SBA reached an incorrect conclusion on Blackwater after four months reviewing what SBA had days to complete.

As a result, the memorandum fails to respond to what you requested and is, considered as a whole, guesswork. Instead, the OIG employee's memorandum is primarily a critique of the SBA Office of Government Contracting, Area Office III's (Area Office) November 2, 2006, formal size determination concerning Blackwater affiliate Presidential Airways, Inc (Presidential Airways).

While this matter is not the focus of your inquiry, I feel it is appropriate to respond to the questions raised in the memorandum.

Size protests are generally filed with respect to pending procurements. Thus, an SBA Area Office generally has ten business days, from the date of receipt of a size protest, to render a formal size determination (pursuant to 13 C.F.R. § 121.1009(a)). The Area Office notifies the protested concern of the protest, and that concern has three days to provide a response and submit required information. Thus, the Area Office essentially has six to seven days to review protester information, the protested concern, and the

procuring agency (such as solicitations, proposals, entity organization records, tax or payroll records, legal briefs, etc.), conduct legal and factual research, and draft and issue a formal size determination. Here, the Area Office received all necessary information from Presidential Airways on October 27, 2006 and issued its decision six days later. As mentioned, the OIG employee's memorandum, in contrast, is the result of a four-month inquiry.

In this case, the Area Office's conclusion that Presidential Airways qualified as a small business for the procurement in question was based primarily on Presidential Airways' representation that Blackwater classified its security guards as independent contractors, not employees, for Internal Revenue Service (IRS) tax reporting purposes. It would be highly unlikely for SBA to find an individual to be an employee for size determination purposes, notwithstanding that the individual was not considered an employee for IRS purposes. A firm that misclassifies its personnel for employment tax purposes faces severe penalties, so firms have a strong incentive to properly classify personnel when dealing with the IRS.

It is certainly beneficial for the public if federal agencies, applying the same criteria, arrive at similar conclusions. At the time of the formal size determination, no IRS official had found Blackwater to have misclassified its personnel for employment tax purposes. To our knowledge, IRS still has not definitively determined whether Blackwater security guard personnel are employees or independent contractors. It was also clear from the record that Blackwater made its employment security personnel classification for business reasons, not in an effort to evade small business size standards.

As a practical matter, the IRS factors that SBA used for determining whether an individual is an employee are numerous, and no one factor is more important than another. Nor does SBA or the IRS make employment classification determinations based on the total number of factors that weigh for or against a finding that an individual is an employee. Instead, the IRS and SBA review the specific facts of each case and render a reasonable decision.

As identified in the OIG employee's memorandum, some factors weighed in favor of finding the Blackwater personnel were employees, other factors indicated the personnel were independent contractors. Given Presidential Airways' representation concerning Blackwater's classification for IRS purposes, SBA's formal size standard determination was not unreasonable, and there is no reason to believe that more extensive consideration of the factors identified in the OIG employee's memorandum would have changed the formal size determination's outcome.

Regarding the alleged discrepancy between employment numbers in the administrative record, such discrepancies are not uncommon. A firm's employee numbers may fluctuate from day to day, certainly more frequently than is reflected on Dunn & Bradstreet's Web site. A formal size determination is rendered as of a particular date, the date of offer, and SBA calculates a firm's size under an employee-based size standard by averaging the firm's number of employees over the previous 12 months. General or publicly available information provided by a protester concerning a protested concern's number of employees may be sufficient for purposes of instigating a formal size determination, but

such information is generally not specific to the protested concern's average number of employees over the previous 12 months as of the date of offer.

On the other hand, the protested concern certifies that the information it submits to SBA in response to the size protest is true under the threat of possible civil, criminal and administrative penalties. Under well-established precedent, signed, sworn information is accorded greater weight in a formal size determination than general allegations or information gathered from the public domain. The OIG employee apparently did not conclude that Presidential or its affiliate made a false statement or misrepresentation to SBA in connection with the November 2, 2006, formal size determination.

Finally, with respect to the recommendation that SBA reopen its formal size determination, the OIG employee has forwarded its findings to all the procuring agencies that awarded Blackwater affiliates small business set-aside contracts. Contracting officers at those agencies may file a size protest at any time, including after award. Further, if any Blackwater affiliate submits an offer as a small business on a federal procurement and is selected for award, unsuccessful offerors, the contracting officer, or SBA may file a size protest in connection with those representations. Thus, SBA may have occasion to review the size status of the Blackwater affiliates in connection with these procurements.

Sincerely,

Fay Ott

Associate Administrator  
Government Contracting and Business Development