LEGAL ADVISOR

A PilieroMazza Update for Federal Contractors and Commercial Businesses

GOVERNMENT CONTRACTING

2016 GAO Bid Protest Annual Report: Sustain Rate Hits Nine Year High, Up More Than 10% from 2015

By Megan Connor

GAO recently released its annual report to Congress, which included data concerning its protest filings for Fiscal Year 2016. Based on the data, 2016 was an historic year. GAO not only decided more cases on the merits in 2016 than in any prior year, dating back to 2001, but it also sustained more cases in 2016 than in any year during that same period.

It is important to note that since 2001, the annual number of cases received by GAO has grown from approximately 1,000 to nearly 3,000. In 2016, GAO received 2,789 cases, of which 2,621 were protests, as opposed to cost claims and requests for reconsideration. Among the cases that were closed in 2016, a little over 22% were decided on the merits. Therefore, the vast majority of protests filed are dismissed before GAO adjudicates the merits, based on jurisdictional grounds, alternative dispute resolution, or because the agency voluntarily takes corrective action rather than defending the protest.

Indeed, it is noteworthy that, between October 1, 2016, and December 31, 2016, GAO did not have jurisdiction over protests of civilian agency task and delivery orders placed under indefinite-delivery/indefinite-quantity contracts valued at more than $10 million, due to a sunset provision in 41 U.S.C. § 4106(f)(1)(B). Therefore, protests of these task or delivery orders filed during in this time period were dismissed by GAO for lack of jurisdiction. The National Defense Authorization Act for Fiscal Year 2017 reinstated GAO's jurisdiction over these protests.

Of the protests GAO received in 2016, it reached a decision on the merits in 616 cases and, of these, **139 protests were sustained**, which is more than twice the number GAO sustained in 2015. According to GAO, the most prevalent grounds for sustaining protests during the 2016 fiscal year were: (1) unreasonable technical evaluation; (2) unreasonable past performance evaluation; (3) unreasonable cost or price evaluation; and (4) flawed selection decision. These grounds overlap with the most prevalent grounds for sustaining protests in 2015, demonstrating a consistency of analysis at GAO.

Where GAO decided a protest on the merits, it sustained the protest 22.5% of the time. To put this figure in context, GAO's sustain rate for cases decided on the merits has not reached 20% since 2008. Moreover, the last time GAO's sustain rate surpassed 23% was in 2007, when it sustained 27% of cases decided on the merits. However, bear in mind that in 2007, GAO only resolved 335 cases on the merits, or approximately half the 2016

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PILIERO MAZZA

We Are Happy to Announce

Megan Connor has become a partner of the firm. Ms. Connor is a talented advocate for the firm's clients and her experience extends across all of the firm's practice areas. She counsels clients on a wide-ranging span of government contracting and general business matters. Her litigation background includes representing contractors in state and federal courts concerning business and employment matters. She has been an associate with the firm since 2011.

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total. GAO's 2016 sustain rate is also significant because it represents a marked increase from 2015. Last year, GAO sustained protests decided on the merits only 12% of the time—the lowest sustain rate in any year, dating back to 2001.

Still, of all the protests filed this past year, only approximately 5% were sustained by GAO. Consequently, the majority of protests are often resolved earlier in the process, without a decision on the merits. Overall, the effectiveness rate of protests in 2016 was 46%, reflecting instances where a protester receives some form of relief, either through corrective action or a decision on the merits. The 2016 effectiveness rate is higher than any previous year, dating back to 2001.

Based on these trends, agencies and offerors alike should assume a protest may be filed after award. In particular, an unsuccessful offeror should look for evidence of an unreasonable technical evaluation, past performance evaluation, or cost or price evaluation when it receives its notice of award and debriefing. And if there is any indication that such an error occurred, the offeror should consider protesting to GAO. While the overall chance of success on the merits may not be high, agencies are increasingly taking corrective action to avoid defending a protest altogether.

If you do not receive an award and want to know what your options for protest are, immediately contact your legal counsel to make sure you timely assert your rights.

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SMALL BUSINESS PROGRAMS

Congress Makes Confusing Changes to the VA's Verification Program

By Julia Di Vito

The 2017 National Defense Authorization Act ("NDAA"), Pub. L. No. 114-328, which was signed into law on December 23, 2016, contains several notable changes to the current structure of the U.S. Department of Veterans Affairs' ("VA") program for veteran-owned small businesses and service-disabled veteran-owned small businesses (collectively, "SDVOSBs"). As part of an effort to provide uniformity between SBA's and VA's SDVOSB rules and programs, Congress has expanded the jurisdiction of SBA's Office of Hearings and Appeals ("OHA") to hear appeals from certain SDVOSB decisions by VA. However, the language of the 2017 NDAA regarding these changes raises more questions than it answers.

An SDVOSB that wants to pursue contracts from the VA, that are set aside for SDVOSBs, must be verified by the VA's Center for Verification and Evaluation ("CVE") and listed in the VA's Veteran Information Pages ("VIP") Database as such. CVE's verification process involves an examination of a firm's compliance with the VA's regulations regarding ownership and control of a SDVOSB. Prior to the 2017 NDAA, if a firm applied for CVE verification and was denied, it could ask the Director of CVE to reconsider the denial decision as a form of administrative appeal. Similarly, the cancellation of a verified firm's status or an adverse SDVOSB protest decision by CVE could be appealed internally at VA to the Executive Director of the VA's Office of Small and Disadvantaged Business Utilization ("OSDBU"). The only external review would be to file a further appeal from the

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OSDBU's ruling to federal court.

Now, under Section 1832(f)(A) of the 2017 NDAA, a concern whose verification application is denied may appeal the denial of verification to SBA's OHA, rather than the Director of CVE. This appeal right extends to denials related to small business status, the ownership of the business, or the control of the business–the essential requirements for qualifying as a verified SDVOSB. OHA will presumably review the administrative record upon which CVE based its denial decision, which is how OHA currently handles appeals from size determinations, denials of applications to the SBA's 8(a) Business Development program, and other SBA proceedings.

"Under Section 1832(f)(A) of the 2017 NDAA, a concern whose verification application is denied may appeal the denial of verification to SBA's OHA, rather than the Director of CVE."

A denial of a verification application is one type of potential adverse decision from CVE. CVE could also deny a re-verification application and it can decide to cancel a currently-verified firm. Because all of these actions amount to a denial of SDVOSB status, we believe logically that all CVE decisions related to denying or cancelling SDVOSB status should be appealed to OHA. However, the NDAA only explicitly addresses denial of verification, so the impact on appeals from a re-verification or cancellation decision is not crystal clear.

Furthermore, under Section 1832(f)(B)(i) of the 2017 NDAA, OHA will also now hear challenges to the inclusion of a firm in the VIP Database. The text of this provision states that:

> *If an interested party challenges the inclusion in the database of a small business concern owned and controlled by veterans or a small business concern owned and controlled by veterans with service-connected disabilities based on the status of the concern as a small business concern or the ownership or control of the concern, the challenge shall be heard by the Office of Hearings and Appeals of the Small Business Administration[.]*

An "interested party" is defined as the Secretary of the VA or, in the case of a SDVOSB awarded a contract, the contracting officer or a small business that submitted an offer for the contract that was awarded to the SDVOSB. Thus, this provision could be read as indicating that a disappointed offeror can challenge an awardee's inclusion in the VIP Database for a particular contract directly to OHA, without first filing a size or status protest with the VA contracting officer.

It is unlikely that Congress intended to bypass existing laws and regulations to create a direct channel to OHA for protests of VA-verified firms. For example, size protests have always been the purview of SBA Area Offices, and Congress presumably did not intend to change that practice. Instead, it is more likely that Congress intended that OHA would hear appeals of challenges to the size or status of VA-verified firms, after those challenges are first decided by CVE. But, again, the language in the NDAA is unclear. Hopefully, this will be clarified when rules are implemented to establish the procedures for these new appeals to OHA.

The 2017 NDAA also does not clarify exactly when these appeals of VA decisions to OHA will begin. If past practice is a guide, OHA may decline to hear such appeals until rules are implemented, which could take many months. However, according to the NDAA, the new appeal procedures will apply to verification denials and challenges to a firm's inclusion in the VIP Database made on or after the date of the enactment of the 2017 NDAA, which was December 23, 2016. As such, there may be a lengthy period of limbo between when OHA has jurisdiction for these appeals according to the NDAA, but no rules under which to handle them.

The objective of creating a more uniform program and system for SDVOSBs is laudable and important, and the NDAA is a step in this direction. But, as noted above, the new provisions have left many questions unanswered. Contractors that participate in the VA's SDOVSB program are in a quandary, as they might be unsure what forum will hear their challenges to or appeals of VA verification issues.

If you are faced with a VA verification issue, contact us to ensure you are aware of the most recent developments in this changing landscape and pursue your appeal in the correct forum.

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It's a New Year. Are You Still a Small Business?

By Michelle Litteken

It is a new year, and this is the perfect time for a small business to consider whether it still qualifies as a small business. We recommend that small businesses assess their size at least once a year. Because eligibility under a revenue-based size standard is based on a company's average revenues from the most recently completed three fiscal years, and those revenues generally establish a company's size for the entire upcoming year, the beginning of a new fiscal year is a good time to reevaluate one's size.

When a contractor submits a proposal for a federal small business set-aside contract, its size is determined on the day of proposal submission. For solicitations with a size standard based on the number of employees, this is generally a straightforward exercise because a company's size is based on the number of employees for each of the preceding completed 12 calendar months. As such, a contractor can determine its size under an employee-based size standard relatively easily by looking at the last 12 months. It is more challenging to determine a company's size at the start of a new year under a revenue-based size standard because a contractor has not usually finalized its financials from the prior year. If a contractor's average revenues are close to a given size standard threshold, the contractor may be uncertain as to whether it still qualifies as a small business when a new fiscal year begins. Understanding how SBA approaches situations like this can help a contractor decide whether to submit a proposal at the start of a fiscal year.

As noted above, SBA calculates a business' size using the revenues received in the three prior fiscal years. See 13 CFR 121.104(c). Thus, for a proposal submitted in January 2017, if the company uses the calendar year for its fiscal year, SBA would look at the company's revenues from 2014, 2015, and 2016. The average of those three years would determine whether the company qualifies as small under a particular size standard. In most cases, SBA obtains annual revenue information from tax returns. See 13 CFR 121.104(a)(1). However, if a contractor is submitting a proposal in early 2017, it probably has not prepared its 2016 tax return yet. With no tax return, how will the contractor's size be calculated?

First, it must be said that if you have not yet filed your tax return for the prior year, this does not mean that year will be excluded from determining your size. If a tax return has not been filed for a fiscal year, SBA's regulations provide: "SBA will calculate the concern's annual receipts for that year using any other available information, such as the concern's regular books of account, audited financial statements, or information contained in an affidavit by a person with personal knowledge of the facts." 13 CFR 121.104(a)(2). This means that SBA will examine a company's internal records, such as financial statements, to determine the revenues from the recently-completed year. Accordingly, a contractor should use its best efforts to ensure that its financial statements are accurate and determine whether it is a small business under the applicable size standard before the tax return is filed.

"It is more challenging to determine a company's size at the start of a new year under a revenue-based size standard because a contractor has not usually finalized its financials from the prior year."

It is important to recognize that a size protest and size determination can take a substantial amount of time. It is not uncommon for a company to submit a proposal before its tax return for the prior year and then submit its tax return while a size protest is pending. If this occurs, and a tax return is available when the SBA conducts the size determination, SBA will use that tax return. Brooks Range Contract Service, SBA No. SIZ-4652 (2004), provides a useful example for this situation. In that case, the contractor self-certified its size on February 9, 2004. Because its 2003 tax return was not complete, it used its 2001 and 2002 tax returns and an estimate for 2003 to calculate its annual receipts. Its size was protested, and when the SBA Area Office requested information, the contractor's 2003 tax returns were available. Based on this information, the Area Office determined that the contractor was other than small. The contractor's internal estimate for 2003 understated its revenues. At OHA, the contractor argued that the Area Office should not have

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used the 2003 return because the return was not available when it certified its size. OHA disagreed, holding that a concern's annual receipts must be determined using the most recently completed three fiscal years, even if there is little time between the end of the most recent fiscal year and the certification date. And, because the tax return was available when the Area Office made its size determination, it was appropriate for the Area Office to rely on it.

To avoid a situation like the one presented in Brooks Range, we advise contractors to verify their size under revenue thresholds at least once a year, preferably at the beginning of a fiscal year. Because the SBA will look to the prior fiscal year, contractors should have financial records available to accurately document its revenues from the fiscal year that recently ended, even if the tax returns have not been prepared yet. And, if a contractor is close to the size standard provided in a solicitation, it should carefully review its financial records before submitting a proposal to ensure it is below the size standard. If the contractor is selected for award, a disappointed offeror could file a size protest. If the SBA determines that the awardee is not small, the awardee will lose the contract and could be precluded from bidding on other contracts under the same size standard until it can prove to SBA that it is small. If the contractor's average revenues were clearly over the size standard, the government could take the position that the contractor intentionally or recklessly misrepresented its size and pursue fraud charges. These problems can be avoided by reassessing one's size at the start of a new year and submitting a proposal only if the applicable size standard is met.

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GOVERNMENT CONTRACTING

New Pilot Program Will Give Certain Small Businesses New Option to Obtain Past Performance Ratings

By Patrick Rothwell

The difficulties faced by new small businesses lacking past performance ratings in winning federal contracts are well-known. Perhaps the most common approach by which new small businesses get their start in federal contracting is by working as a subcontractor to a federal prime contractor. Often this is accomplished by working as a subcontractor under federal prime contracts that require the prime contractor to develop a subcontracting plan. For small businesses that perform as first-tier subcontractors under such federal contracts and lack past performance ratings as a prime contractor, Congress has provided for a new "pilot program," under section 1822 of the recently-enacted 2017 NDAA. Under the pilot program, these first-tier subcontractors can obtain a past performance rating in the federal past performance system that they can use to obtain a federal prime contract.

Technically, Congress established the pilot program as an amendment to the Small Business Act and it will apply to civilian and military agencies. SBA is charged with implementation of the program. Although it is unclear when this pilot program will begin, this new mechanism for obtaining past performance is a potentially promising way that a small business subcontractor can obtain a past performance rating for federal prime contracts and it also can designate the rating it believes it deserves.

The process by which a past performance rating may be established under this pilot program is as follows: First, small business subcontractors described above (without a past performance rating as a prime contractor and which work as a first-tier subcontractor under a contract for which the prime contractor must submit a subcontracting plan to the federal government) may submit an application to an "appropriate official" for a past performance rating no later than 270 days after it completed the work for which it seeks a rating or 180 days after the prime contractor completes work on the

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contract in question, whichever is earlier. An "appropriate official" is an SBA commercial market representative, certain other officials designated by SBA, or a person from an agency's Office of Small and Disadvantaged Business Utilization ("OSDBU"), if agreed to by SBA and the agency head.

Uniquely here, the application includes both the submission of written evidence of the past performance factors for which the contractor seeks a rating and the subcontractor's own requested rating. The appropriate official will submit the application to both the procuring agency's OSDBU and the prime contractor for review. OSDBU and the prime contractor are required to submit a response to the application no later than 30 days after receipt. If both the OSDBU and the prime contractor agree with the proposed rating, the appropriate official will submit the rating into the federal government's past performance system. Likewise, if either the OSDBU or the prime contractor fails to respond, but one party responding to the application—from either the OSDBU or the prime contractor—agrees with the rating, again the appropriate official will submit the subcontractor's requested rating into the federal government's past performance system. The small business subcontractor will be able to use this rating to establish its past performance for a federal prime contract.

However, under the pilot program, if the OSDBU and the prime contractor fail to respond within 30 days or disagree with the proposed rating; or, alternatively, if (i) either the OSDBU or the prime contractor fails to respond and (ii) the responding person disagrees with the proposed rating, the OSDBU or the prime contractor must submit a notice to the appropriate official contesting the application, who will, in turn, forward the notice to the subcontractor. The subcontractor may submit comments, rebuttals, or additional information related to the past performance. The appropriate official will then enter a rating that is neither favorable nor unfavorable, along with the application, any responses from OSDBU and the prime contractor, and additional information from the subcontractor. Thus, should a subcontractor avail itself of this procedure, no negative past performance rating itself will result from use of the pilot program. It is unclear, though, whether negative information regarding performance from the prime contractor or the OSDBU could be included along with the neutral past performance rating.

By providing the subcontractor additional influence over how its performance will be portrayed in the government's past performance system, the pilot program may serve as an additional incentive for the subcontractor to put its "best foot forward" in the performance of its subcontract. On the other hand, if there is a misunderstanding or conflict between the prime contractor and the subcontractor, the pilot program could be used as vehicle for the prime contractor to air to the government its disagreements with the subcontractor. Likewise, the benefits of this program could be defeated if both OSBDU and the prime contractor are uncooperative or unreasonably dispute the subcontractor's requested past performance rating. It is not obvious what recourse might be available to the subcontractor if that happens.

"This new mechanism for obtaining past performance is a potentially promising way that a small business subcontractor can obtain a past performance rating for federal prime contracts."

The NDAA does not establish any deadline by which this pilot program is to be established, so it is unclear when it will begin. However, it will last for three years after the date on which the first applicant small business concern receives a past performance rating under this new program. The Government Accountability Office will be required to assess the operations of the pilot program starting one year after the establishment of the program and it is required to submit a report to Congress six months after beginning such an assessment. This report may give the contracting community a preliminary sense as to the value of the pilot program.

Small contractors which may benefit from this program are encouraged to keep apprised on further developments in the program's development and operations.

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