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BENNIE G. THOMPSON, MISSISSIPPI
RANKING MEMBER

One Hundred Twelfth Congress
U.S. House of Representatives
Committee on Homeland Security
Washington, DC 20515

The Honorable Karen G. Mills
Administrator
U.S. Small Business Administration
409 3rd St, SW
Washington DC 20416

Dear Administrator Mills:

As you are aware, size and status misclassifications can create the false impression of an agency's compliance with small business participation goals. Further, it creates the potential for ineligible companies siphoning revenues intended to spur the growth, development and stabilization of small business concerns.

Recently, the Small Business Administration (SBA) issued a Notice of Proposed Rule (rule) entitled, *"Small Business Size and Status Integrity."* The rule sought public comment on the manner in which SBA will address size and status misrepresentations as instructed by the *Small Business Jobs Act of 2010*.

Enclosed herein for your review and consideration is a comment that I submitted in response to the rule. As detailed in the comment, I request reconsideration of certain aspects of the rule.

My concerns about the ability of large businesses posing as small and disadvantaged businesses to obtain federal contracts were most clearly confirmed in the aftermath of Hurricane Katrina. On October 21, 2005, I wrote to the SBA Office of Inspector General (OIG) to relay my suspicions about a business which had been awarded a contract for almost $1 million by the Federal Emergency Management Agency (FEMA). In the Federal Procurement Data System—Next Generation (FPDS-NG), FEMA reported the contract as awarded to a small business. However, the contractor was a large multinational business with over $4.5 billion in North American sales. After a thorough examination, the OIG confirmed that the contractor should have been ineligible for a small business award. This is merely one example of large businesses either posing as small or through mistake, inadvertence, or a strategic manipulation of current small business regulations, reaping the benefit of federal contract dollars specifically intended for small businesses.

Due to my ongoing concerns, I support the rule's intention. However, as outlined in the enclosed comment, there are aspects of the rule that would benefit from reconsideration.

First, the repercussions of failing to comply with the annual certification requirement— removal from the Federal small business database – appears unduly harsh for a legitimate small or disadvantaged business. A provision in the rule requiring both notification and an opportunity for the small business to comply with the certification requirement prior to being removed from the database would greatly improve the likelihood of compliance.

Second, pursuant to the rule, there is a presumption of loss equal to the value of the contract when a concern willfully seeks and receives an award by misrepresentation. The rule further indicates that this dollar-for-dollar loss presumption will be "irrefutable." As explained in the comment, since there is no statutory or generally accepted definitional framework for the term "irrefutable," the term will likely be interpreted by courts as "**irrebuttable.**" Irrebuttable presumptions are not only generally disfavored in the law but have been interpreted to raise due process concerns. In this context, the intended effect of the language would be to deny a business a reimbursement for funds already expended. Under current law, such a recovery is allowed despite purposeful misrepresentation. Therefore, the denial of a recovery without access to administrative or judicial process may be seen by some as a denial of due process and suitable for legal challenge. To avoid the possibility of a protracted and unnecessary legal battle over the interpretation of an undefined term, I recommend that the term "irrefutable" be omitted.

As stated above, I support the spirit and intention of the proposed rule, however, the adoption of the modifications noted above and fully detailed in the comment would more fully assure that small and disadvantaged businesses have a fair an equal opportunity to compete for federal contracts.

If you have any questions or concerns, please do not hesitate to contact Ms. Cherri Branson, Chief Counsel for Oversight, Committee on Homeland Security, (202) 226-2616.

Sincerely,

Bennie G. Thompson
Ranking Member
Committee on Homeland Security

U.S. SMALL BUSINESS ADMINISTRATION
76 Fed. Reg. 62313 (October 7, 2011)
**Docket ID:** SBA-2011-0010 – **RIN:** 3245-AG23
Notice of Proposed Rule
Small Business Size and Status Integrity

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Comments Of
Rep. Bennie G. Thompson (D-MS), Ranking Member
U.S. House of Representatives Committee on Homeland Security

## I. INTRODUCTION

I am pleased to submit the following written comment on the proposed rule titled "Small Business Size and Status Integrity" (RIN 3245-AG23) published in the Federal Register[1] on October 7, 2011. The proposed rule seeks to implement provisions of the *Small Business Jobs Act of 2010.* [2]

On September 27, 2010, the *Small Business Jobs Act of 2010* was signed into law by President Obama. Among other things, the law amended the *Small Business Act* [3] by updating the contracting provisions affecting small business procurement. The new small business procurement provisions included changes to existing laws regarding contract bundling, subcontracting integrity, acquisition processes, and small business size and status integrity.

In an effort to notify the public of the changes to the determination of small business size and status integrity and to seek public comment regarding the same, the Small Business Administration (SBA) issued the aforementioned Notice of Proposed Rule

The *Small Business Act*, creates set-aside programs for (1) small disadvantaged businesses participating in the 8(a) Minority Small Business and Capital Ownership Development Program (8(a) program); (2) Historically Underutilized Business Zone (HUBZone) small businesses; (3) women-owned small businesses; (4) service-disabled veteran-owned small businesses; and (5) small businesses not belonging to any of the prior four categories. Across the country, small businesses have raised concerns about unfair and illegal competition from large businesses in the award of federal contracts specifically designed for competition between and among small businesses. In some documented instances, large businesses have willfully misrepresented status to receive contracts legally set aside for legitimate small businesses. In other instances, innocent mistakes have led to the improper certification of a large business as a small business.

Regardless of whether the improper designation occurred as a result of mistake or willful misconduct, the underlying awards have been included toward the respective agency's fulfillment of a the government-wide goal of awarding 23 percent of agency contracting dollars

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[1] 76 Fed. Reg. 195 (to be codified at 13 C.F.R. § 121, *et. seq.*) (proposed October 7, 2011).
[2] Pub. L. No. 111-240 (2010).
[3] Pub. L. No. 85-536, as amended (1953).

to small and disadvantaged businesses. Not only can size and status misclassifications create the false impression of an agency's compliance with small business participation goals, but as a practical matter, revenues intended to spur the growth, development and stabilization of the small business sector are siphoned off by ineligible companies.

The proposed rule seeks to implement changes intended to better assist the small business community in participated in federal contracting opportunities as well as protecting small businesses.

For the foregoing reasons, I support the proposed rule in part and request reconsideration of certain aspects of the rule.

## II. BACKGROUND

A federal government agency is required to award at least 23% of its contracts to small and disadvantaged business concerns.[4]

On June 24, 2011, the SBA announced that in Fiscal Year 2010, small businesses received a record $97.95 billion in federal contracts, or 22.7 percent of eligible contracting dollars.[5] This number is shy of the required 23% goal. And while the reported small business participation percentage is only slightly below the federal target, it may not reflect an accurate assessment of small and disadvantaged business participation in the federal marketplace.

I have long been concerned with the difficulty of small and disadvantaged business participation in the federal sector. My concerns were most clearly confirmed in the aftermath of Hurricane Katrina.

On October 21, 2005, I wrote to the U.S. Small Business Administration, Office of Inspector General (OIG) to relay my suspicions about a contractor which had been awarded a contract for almost $1 million by the Federal Emergency Management Agency (FEMA). In the Federal Procurement Data System—Next Generation (FPDS-NG), FEMA reported the contract as awarded to a small business. However, a staff investigation revealed that the contractor was one of the world's largest providers of office and computer products and services, with over 200 facilities in several countries, and had $4.5 billion in North American sales. After a thorough examination, the OIG confirmed that the contractor was a large multinational business and as such would have been ineligible for a small business award. As a remedy, the OIG suggested changes to the Central Contractor Registration (CCR) system which would both prevent and alert size and status misclassifications.[6]

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[4] *See, The Small Business Reauthorization Act of 1997*, Pub. L. No. 105-135 (1997).

[5] Small Business Administration, *Press Release: 2010 Small Business Procurement Data Shows Significant Progress toward 23 Percent Federal Contracting Goal*, June 24, 2011.

[6] The Central Contractor Registration Needs Large Business and Small Business Designation Improvements, Management Advisory Report No. 6-18, U.S. Small Business Administration Office of Inspector General, (March 2006)

## III. PROPOSED RULE

The proposed rule identifies two significant changes to the law that impact size certifications and regulations.

### *A. Statutory Deemed Certification*

The rule mandates yearly certification of small business size and status. This is a significant shift from past practice. Previously, under most circumstances small businesses could operate for up to five years without updating size or status. -Under the proposed rule, firms must update size and status, (e.g small disadvantaged business, service disabled veteran-owned or women owned small business) in federal databases at least annually.

For some firms this could present a practical challenge. For some firms, the North American Industry Classification System (NAICS) code determines size standards based on average of annual income over a period of years. Thus, it is not clear how a new annual certification would take into consideration revenue fluctuations common in many small and disadvantaged businesses.

Additionally, it appears that the practical effect of this rule would be extremely harsh. Firms which fail to certify size or status within one year of a prior certification will no longer be listed as a firm of that size or status. It is unclear whether notice and a reasonable opportunity to recertify will be given before elimination from the list or whether this change will occur automatically. The opportunity to recertify after elimination may seem equitable, however, such a remedy does not take into consideration the reality of lost business opportunities or other transaction costs which may result in the interim.

Further, while the proposed certification change -may appear to constitute a reform which would benefit small and disadvantaged businesses, consideration should be given to the increased administrative hurdle this annual certification requirement may impose on small and disadvantaged businesses. Because small and disadvantaged businesses, are likely to have few administrative support employees, an annual size certification deadline could easily be missed. As such, failure to meet this paperwork requirement could unfairly and unintentionally eliminate legitimate small and disadvantaged companies.

Moreover, because it appears that this certification is likely to be a self-certification, it is unclear whether a clear picture of the small business status is likely to be generated by such an exercise. A self-certification is likely to produce a self-serving response. Thus, because this portion of the rule is likely to impose a paperwork burden on small and disadvantaged business which is not shared by large businesses and because the information likely attained through this exercise is likely to be of dubious value, I would urge the reconsideration of this portion of the rule.

In addition to the annual certification requirement, the rule makes changes to the manner in which size is certified. Pursuant to the rule, the following actions are deemed to be an "affirmative, willful and intentional certification of small business size and status," with or without a signature or an express statement:

- Submission of a bid or proposal for contracts, subcontracts, and grants reserved, set aside or otherwise classified as intended for award to small business concerns.

- Submission of a bid or proposal for contracts, subcontracts, and grants which in any way encourages a Federal agency to classify the bid or proposal, if awarded, as an award to a small business concern.

- Registration on any Federal electronic database for the purpose of being considered for award as a small business concern.

### *B. Statutory Presumption of Loss*

Criminal penalties for false certifications and misrepresentations of business size are not new. A fine in excess of $500,000.00 and imprisonment have always been available alternatives as a consequence to contractor malfeasance. Despite the availability of these options, prosecutors have very seldom, except in large egregious cases, enforced these laws by bringing criminal prosecutions.[7]

The proposed rule will change the determination of loss. In the past, large businesses that misrepresent size status to qualify for contracts intended for small or disadvantaged businesses were liable to the government for the cost of the contract, *less the value of the work already performed.* The proposed rule ~~would~~ creates ~~an~~the ~~irrebuttable~~ presumption that the government sustained a dollar-for-dollar loss even if the contractor provided some services or equipment, fully performed the terms of the contract, or the government received value. According to the rule, "there shall be a presumption of loss to the United States based on the total amount expended on the contract, subcontract, cooperative agreement, cooperative research and development agreement, or grant whenever it is established that a business concern other than a small business concern willfully sought and received the award by misrepresentation."[8]

The rule references Senate Report language which indicates that this presumption is "irrefutable." I would, however, caution the SBA from adopting such a strong and heretofore unprecedented standard. Report language is not deemed to be statutory authority and agencies are not bound by its terms. While report language usually serves as a framework for the implementation of the statute, this should not. Typically, a presumption established by law is deemed to be *rebuttable* so that although the premise stands as legal fact, one is almost always given the opportunity to contest the presumption or prove otherwise. There is no definitional framework for the term "irrefutable" therefore the adoption of such a standard would not add

[7] In 2006, Insight Public Sector, a Fortune 1000 company's subsidiary, agreed to pay the federal government $1 million to settle allegations that it falsely represented itself as a small business for inclusion on a General Services Administration contracting schedule.

[8] *Supra*, at note 1.

clarity but muddy the waters and could ultimately deny a business owner the fair opportunity to present facts and sound proof.[9]

Under the proposed rule, the government would be able to recoup moneys paid to the contractor, despite full performance. Such a financial penalty is likely to constitute a strong deterrent which may result in self-policing within the industry, thereby increasing the possibility of detection and enforcement. I support this portion of the rule, absent the adoption of the Senate report language reference an "irrefutable" presumption. However, because it would be easy to imagine a scenario in which an unscrupulous vendor lodges false allegations against a competitor, I would urge you to consider penalties deterring willful submission of false reports.

## IV. CONCLUSION

The proposed rule seeks to implement the terms of the *Small Business Jobs Act* and may help to level the playing field for small and disadvantaged businesses. While I support the spirit and intention of the proposed rule, I urge the modifications mentioned herein to more fully afford meaningful opportunities to small and disadvantaged businesses.

Thank you for the opportunity to comment on the proposed rule. If you have any questions or need additional information, please do not hesitate to contact Ms. Cherri Branson, Chief Counsel for Oversight, at (202) 226-2616.

Rep. Bennie G. Thompson
Ranking Member
Committee on Homeland Security

[9] See, The Irrebuttable Presumption Doctrine in the Supreme Court, *Harvard Law Review* Vol. 87, No. 7 (May, 1974), pp. 1534-1556 (discussing *Bell v. Burson*, 402 (U.S. 535 (1971), *United States Department of Agriculture v. Murray*, 413 U.S. 508 (1973), and other cases addressing statutes that contained rules denying a benefit or placing a burden on all individuals possessing certain characteristics ultimately concluding that the statutes' irrebuttable presumption denied due process of law).