

# Small Business Subcontracting Plans: Making a Good Faith Effort & Other Compliance Tips

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Kevin advises clients in all aspects of government contracts law:

- Helps contractors prepare, negotiate, and litigate claims, requests for equitable adjustment, and termination for convenience settlements.
- Litigates bid protests before the GAO, Court of Federal Claims or at the agency level.
- Counsels firms with an array of FAR compliance issues, including advising companies new to federal contracting on making a smooth transition.
- Guide clients through the Freedom of Information Act process from drafting and negotiating FOIA requests to litigating in federal court.

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Cy counsels clients on a broad range of government contracting matters before government agencies and federal courts, which includes overall regulatory compliance with the Small Business Administration’s (SBA) small business programs. He represents small and mid-sized government contractors looking to structure compliant teaming, joint venture, and mentor-protégé agreements. Cy also handles the prosecution and defense of small-business size and status protests; appeals before the SBA and the Office of Hearings and Appeals; as well as bid protests before the Government Accountability Office, the Court of Federal Claims, and the U.S. Court of Appeals for the Federal Circuit.

# About PiliroMazza

PiliroMazza – a business law firm – serves as a strategic partner to government contractors and commercial businesses from across the United States.

We deliver results for our clients by implementing legal and business solutions that take the client's best interests into consideration. Moreover, PiliroMazza's efficient operational structure and lean approach to staffing matters translates into competitive pricing for our clients, while providing the highest standard of client service and legal acumen.

PiliroMazza is privileged to represent clients in the following areas:

- Audits & Investigations
- Bid Protests
- Business & Transactions
- Business Succession Planning
- Corporate and Organizational Governance
- Cybersecurity & Data Privacy
- Debt Financing
- Employee Incentive and Bonus Plans
- False Claims Act
- Fund Formation & Structuring
- Government Contracts
- Government Contract Claims & Appeals
- Intellectual Property & Technology Rights
- Labor & Employment Law
- Labor & Employment for Government Contractors
- Litigation & Dispute Resolution
- Mergers & Acquisitions
- Native American Law & Tribal Advocacy
- Nonprofits
- Private Equity & Venture Capital



# Overview

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- Small Business Subcontracting Plans
- Spotlight on compliance
- Making a good faith effort
- Compliance tips
- Preparing for an SBA review of your subcontracting program

# Small Business Subcontracting Obligations

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- Providing maximum practicable subcontracting opportunities for SBs
  - Applies to most prime contracts
  - Must be flowed down when subcontracts offer lower tiered subcontracting opportunities
- Subcontracting Plans
  - Applies to prime contracts that offer subcontracting possibilities > \$650K (or \$1.5M for construction)
  - Only applies to large businesses
  - Must be flowed down to subcontracts meeting same thresholds

# Small Business Subcontracting Plans

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- Between prime contractor and government establishing the contractor's subcontract spending goals for different SB types
- Required elements
  - SubK spending goals expressed as percentage of total planned subcontracting
    - Separate goals for each type of SB
  - Types of supplies/services to be subcontracted
  - Methods used to develop goals
  - Methods used to identify potential SB subcontractors
  - Explanation of whether/how indirect costs are included

# Small Business Subcontracting Plans

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- Required elements (cont'd)
  - Name of responsible officer administering the plan
    - Small Business Liaison Officer (“SBLO”)
  - Efforts company will take to ensure SBs have equitable opportunity to compete
  - Assurances required provisions will be flowed down, reports will be completed, and cooperate in studies/survey
  - Description of recordkeeping procedures
  - Steps to make good faith effort to comply with plan



# Types of Subcontracting Plans

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- Individual
  - Applies to specific government contract
  - Covers entire contract period, including options
  - Goals based on offeror's planned subcontracting in support of contract and are negotiable
- Master
  - Boilerplate plan that can apply to corporation, plant or division
  - Effective 3 years after approved
  - Goals are negotiated for each contract that incorporates master plan

# Types of Subcontracting Plans

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- Commercial
  - Preferred plan for companies selling commercial products or services
  - Annual plan for entire federal government; not contract specific
  - Tied to a contractor's fiscal year
  - May be limited to specific company division or business unit
  - Counts all subcontracting (not just that in support of government contracts)

# Polling Question

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What is the biggest challenge you face in your small business subcontracting program?

- A. Lack of available, qualified small businesses
- B. Insufficient “buy-in” within your organization
- C. SBA / FAR requirements are difficult to understand and keep up with
- D. Other

# Importance of Subcontracting Plans

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- Focus on subcontracting compliance on Capitol Hill
- Efforts in DC to “put more teeth” into the subcontracting plan requirements
- Stakes are high for noncompliance
  - Breach of contract
  - Adverse past performance
  - Evaluation factor
  - Liquidated damages

# Compliance Impacts in Bid Protests

- Octo Consulting Grp., Inc., B-413116.53, B-413116.55 (May 9, 2017): protester was not in line for award when it did not set specific goals in its subcontracting plan for small disadvantaged businesses and service-disabled veteran-owned small businesses
- Graybar, B-410886 (Mar. 4, 2015): protester was properly excluded from competitive range based in part on its consistent failure to meet its small business subcontracting goals on previous contracts
- Kellogg Brown & Root Services, Inc., B-298694.7 (June 22, 2007): protester's score lower than awardee's due in part to less small business utilization in prior contracts
- Coastal Maritime Stevedoring, LLC, B-296627 (Sept. 22, 2005): agency improperly rated offeror's incomplete plan as satisfactory
- SEEMA, Inc., B-277988 (Dec. 16, 1997): awardee's aggressive subcontracting goals one of the decisive factors in award

# Changing Requirements

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- Lower-tier subcontracting goals
  - SBA rulemaking went into effect January 23, 2017
  - Requires large business primes with individual subcontracting plans to establish goals for lower-tier subcontract awards
  - Prime's performance under plan judged based on combined performance under first-tier & lower-tier goals
  - BUT, no final FAR rule yet (proposed in June 2019)

# Changing Requirements

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- SBA rule on “material breach” of a subcontracting plan
  - Implemented December 2019 in 13 C.F.R. § 125.3
  - Material breach occurs if the prime:
    - fails to timely submit reports or cooperate in any studies or surveys SBA or the contracting agency may require
    - receives a marginal or unsatisfactory rating during a compliance review and fails to provide a corrective action plan
  - Material breach finding could be reflected in the prime’s past performance
  - FAR Rule updated in August 2021 to mirror SBA regulations (FAR 19.704)

# Liquidated Damages

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- **Past:** Big Foot or the Loch Ness Monster?
- **Present:**
  - SBA regulations indicate prime “may” be considered for LDs if it receives a marginal or unsatisfactory rating for its subcontracting plan and does not provide a written corrective action plan, or fails to make a good faith effort to comply with its subcontracting plan
  - Yet, SBA not aware of any cases when LDs were imposed
- **Future:** movement toward making LDs a more automatic result when prime does not meet its SB commitments



# Liquidated Damages

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- FAR 52.219-16 states that LDs “shall” be paid when contractor fails to make a good faith effort to comply with its subcontracting plan
  - “Willful or intentional failure to perform”
  - LDs = amount equal to the actual dollar amount by which the contractor failed to achieve the subcontracting goal
  - Requires CO final decision, and CO must give contractor written notice and opportunity to respond

# Good Faith Effort

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- 13 C.F.R. 125.3(b)(3) and FAR 19.705-7 describes efforts to maximize SB subcontracting opportunities, including:
  - Break out contract work items into portions more feasible for SB participation
  - Conduct market research using SAM, SBA's Sub-Net and Pro-Net databases, and attending conferences / outreach events for SBs
  - Negotiate in good faith with interested SBs
  - Participate in a formal mentor-protégé program

# Good Faith Effort

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- 13 C.F.R. 125.3(d)(3)(i) and FAR 19.705-7 provides examples of supporting documentation that would show a contractor has made a good faith effort:
  - The contractor can demonstrate it performed one or more of the actions noted on the prior slide
  - Although contractor missed one SB goal, it over-achieved its goal by an equal or greater amount in one or more other SB categories
  - Contractor fulfilled all requirements of its subcontracting plan

# Failure to Make Good Faith Effort

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- 13 C.F.R. 125.3(d)(3)(ii) and FAR 19.705-7 provides examples of when a contractor has not made good faith effort, including:
  - Failure to timely submit acceptable subcontracting reports
  - Failure to timely pay SB subcontractors per the terms of the subcontract
  - Failure to designate a responsible company official for the subcontracting program and to monitor / enforce the subcontracting plan
  - Failure to maintain records or otherwise demonstrate procedures to comply with the subcontracting plan
  - Failure to conduct market research

# Polling Question

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Do you have a written manual in place addressing the policies and procedures for your small business subcontracting program?

- A. Yes
- B. No

# Write up Your Procedures

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- Written subcontracting program manual is essential to maintain your program and to pass an audit
- Your manual should address:
  - Covered supplies / services
  - Program administration and SBLO responsibilities
  - Periodic evaluation of program performance
  - Recordkeeping procedures
  - Maintenance of vendor list
  - Vendor self-certifications
  - Independent verification of vendor self-certifications
  - Flow-down
  - Preparation of subcontracting plans
  - Reporting (internal / external)
  - CEO / senior leadership buy-in and involvement
  - Outreach (internal / external)
  - Employee training

# Go with the Flow (Downs)

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- Flow-down should be addressed in subcontract or your standard terms and conditions
- Requirement to provide maximum practicable opportunities for SBs must be flowed down when subcontract offers lower-tier subcontracting opportunities
- Requirement to implement a subcontracting plan must be flowed down to subcontracts that offer further subcontracting possibilities greater than \$700,000 (or \$1.5 million for construction)
  - But, no flow down to SB subcontractors, or for subcontracts for commercial items (when the prime contract contains FAR 52.212-5 or 52.244-6)

# Make Your Deadlines

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- Make sure to submit your ISR / SSR on time via eSRS
  - Define reporting procedures, timelines, and responsibilities in your compliance manual
- Discrepancies or negative trends in reported data are more likely to trigger an SBA audit



# Training and Outreach

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- Make sure your management, sales, and purchasing personnel are on the same page for goal development and attainment
- Hold regular internal meetings and monitor plan performance to catch shortcomings as early as possible
- Get involved in conferences, trade associations, PTACs
- Be sure to document mentoring and success stories with SBs

# Vet Your Subcontractors

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- Must obtain written representations of size / status from your SB vendors, and keep them current
  - Use SBA’s preferred format for vendor “Self-Certification Form”
  - If SB is relying on SAM, the SB must represent to you in writing that its SAM is current, accurate, and complete for the subcontract
  - For commercial plans, ask vendors to represent small business status for primary and any secondary NAICS codes
- Independent verification required for HUBZone vendors; good idea for all SB vendors
- Third party verification good, but not foolproof

# Polling Question

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Have you undergone an SBA compliance review of your subcontracting program within the last three years?

- A. Yes
- B. No

# Types of SBA Reviews

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- **Subcontracting Program Compliance Review:** a comprehensive review of contractor's total subcontracting program
- **Performance Review:** focuses on subcontracting achievement on a contract-by-contract basis via reporting systems
- **Subcontracting Orientation and Assistance Review:** includes physical visit to contractor's facility with purpose of providing advice or tools so the contractor can evaluate its small business program
- **Follow-Up Reviews:** focuses on contractor's implementation of previous SBA recommendations and its utilization of referred resources

# Compliance Review Checklist

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- SBA’s compliance review checklists require you to answer numerous questions about your subcontracting program, goal performance, historical trends, outreach efforts, etc.
- SBA requests several supporting documents, including:
  - Subcontracts with SBs and LBs over the last year
  - Letter of support from CEO
  - Policy and procedures for your subcontracting program
  - Sample subcontractor self-certification form
  - Contract terms and conditions containing flow-down language
  - Organizational chart depicting where SBLO sits in your organization

# Compliance Review Site Visits

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- Usually lasts 1–2 days
- SBA will want to meet with key stakeholders, SBLO, managers, and buyers
- Looking for good faith efforts to comply with plan through assessments of:
  - Methodology used in developing and reporting goals and performance
  - Recordkeeping, such as written representations from your SB vendors that are timely and tied to your subcontracts
  - How you flow-down requirements to and monitor subcontractors
  - Overall commitment to the program, including management support
- Prepare in advance; put yourself through a “mock audit”

# What Happens Next?

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- If you receive a “Marginal” or “Unacceptable” rating, SBA will require you to submit a corrective action plan
  - Contractor submits plan to SBA or both the SBA and agency that conducted the compliance review
  - Failure to submit or adhere to a corrective action plan is considered a “material breach” and may be grounds for material breach and LDs
- SBA will conduct follow-up visit to check on your progress with the corrective action plan
- SBA’s report will go to Administrative CO

# Questions?

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