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RECENT DEVELOPMENTS AFFECTING SMALL BUSINESSES AND SUBCONTRACTING REQUIREMENTS

The following is a brief summary of some recent actions over the past several months affecting small businesses involved in performing government contracts.

1. INCREASED SET-ASIDE OPPORTUNITIES FOR WOMEN-OWNED SMALL BUSINESSES UNDER A NEW PROPOSED PROGRAM

On March 4, 2010, the SBA published a proposed rule aimed at expanding federal contracting opportunities for women-owned small businesses (WOSBs), including economically disadvantaged women-owned small businesses (EDWOSBs). This latest proposed rule significantly builds on previous efforts over the past decade to increase the presence of WOSBs in government contracting. One of the purposes of the rule is to help agencies reach the existing statutory goal of awarding 5% of federal contracting dollars to WOSBs. According to reports, agencies have consistently failed to reach this goal.

In particular, the proposed rule expands the number of NAICS Industry Codes in which women-owned businesses are considered under-represented or substantially underrepresented to 83 industries and provides a mechanism for setting aside contracts for WOSBs in these industries. The change in industry codes was based on a change in the process for identifying industries in which women -owned businesses are under-represented.

Some of the key components of the proposed rule include:

- To be eligible, a firm must be 51% owned and controlled by one or more women and primarily managed by one or more women who are US citizens.
- Based on an analysis of a study commissioned by the SBA, the proposed rule identifies 83 industries (by NAICS codes) in which women-owned small businesses are underrepresented or *substantially* under-represented.
- Economic Disadvantaged Women-Owned Businesses (EDWOSBs) will have access to set-asides in both the under-represented and substantially under-represented categories, while WOSBs will have access to set-asides in just the substantially underrepresented categories. According to the SBA, there are 45 NAICs codes in which WOSBs are underrepresented and 38 NAICs codes in which WOSBs are substantially under-represented.
- The proposed rule authorizes a set-aside of federal contracts for WOSBs where the anticipated contract price does not exceed $5 million in the case of manufacturing and $3 million in the case of other contracts. Contracts with values which exceed these amounts are not eligible to be set-aside.
- Agencies are not required to certify that they have engaged in discrimination against women-owned businesses in order for the program to apply to agency contracting (a requirement under a previous proposed rule)
- The proposed rule will allow women-owned businesses to self-certify through the ORCA web site or to be certified by third-party certifiers, including government entities and private certification groups.

2. COURT OF FEDERAL CLAIMS WEIGHS–IN ON PRIORITIZATION OF SET-ASIDE PROGRAMS

Last fall (Client Alert, September, 2009), we noted that the GAO and OMB were at odds over set-aside programs. Specifically, agencies were advised by OMB to disregard GAO recommendations in two cases, International Program Group, Inc., B-400278 (September, 2008) and Mission Critical Solutions, B-401057(May 4, 2009). In these decisions, the GAO effectively rejected the OMB position that there is parity among the HUBZone, 8(a), and SDVOSB set-aside programs. Instead, the GAO found, based on its interpretation of the applicable set-aside rules, that set-asides for HUBZone companies were entitled to priority over set-asides under the other programs. OMB advised agencies not to follow the GAO's recommendations (which are not binding on federal agencies). At that time, we anticipated that Congress would resolve the issue with legislation which unequivocally established that there was parity among the set-aside programs and that one program did not deserve priority over another. However, Congress has yet to act affirmatively on this issue. Attempts to resolve this issue through legislation have apparently been stalled in committee.

Now, in two decisions, the Court of Federal Claims has also determined, like GAO, that the applicable statutory language compels contracting officers to prioritize set-asides under the HUBZone program over 8(a) set-asides. However, unlike the GAO's recommendations, the Court's decisions are presumably binding on federal agencies. In the first case, Mission Critical Solutions v. United States, 91 Fed. Cl. 386 (2010), the Court found that statutory language under the Small Business Act mandated such prioritization. The Court also enjoined the government from awarding the contract at issue in a manner that is not in compliance with the Small Business Act as the Court has interpreted it. More recently, in DGR Associates, Inc. v. United States, No. 10-396C (August 13, 2010), the Court again ruled that Congress established a priority for the HUBZone program over other competing small business programs. The Court also noted that if Congress intended something different from what it stated, Congress alone must enact an appropriate amendment as the Court can only apply the laws as written.

It would now appear that unless Congress finally addresses this issue, HUBZone small businesses will continue to be entitled to a preference for contracting opportunities where the contracting officer has reason to believe that 2 or more qualified HUBZone small businesses will submit offers and that an award can be made at a fair market price.

3. FRANKEN AMENDMENT (Certain Prime Contracts and Subcontracts Should Prohibit the Use of Mandatory Arbitration Provisions in Employment and Consultant Agreements)

Section 8116 of the DOD Appropriations Act for FY 2010 (Pub.L.111-118), introduced by Senator Franken ("Franken Amendment"), prohibits the use of FY 2010 funding on certain contracts unless contractors agree not to use mandatory arbitration procedures for Title VII claims. The enactment of the Amendment was fueled by a case involving the assault and rape of a defense contractor employee by her fellow employees, who was compelled to arbitrate her claims against her employer.

On May 19, 2010, DOD issued an interim rule implementing the Franken Amendment. In accordance with the Amendment, the interim rule prohibits the use of FY 10 funds for any contract (including task orders and bilateral modifications) in excess of $1 million that is awarded after February 17, 2010, unless the contractor agrees not to enter into agreements with its employees or independent contractors that require, as a condition of employment, that the employee or independent contractor agree to resolve through arbitration Title VII claims and certain related tort claims. The interim rule also prohibits contractors from taking action to enforce provisions of existing agreements with employees or independent contractors mandating arbitration. These new requirements do not apply to the acquisition of commercial items. The interim rule creates a new DOD FAR supplemental clause (DFARS 252.222-7006, Restrictions on the Use of Mandatory Arbitration Agreements) which addresses these requirements. This new clause is not a mandatory flow down provision.

Contractors are also required to certify that "covered subcontractors" agree not to enter into, and not take action to enforce mandatory arbitration provisions. A covered subcontractor is "an entity that has a subcontract in excess of $1,000,000 on a contract" that is subject to the above described requirements of the amendment. Currently, it is not clear if "covered subcontractor" includes second and lower-tier subcontractors.

The Amendment has been criticized as lumping responsible companies with unethical contractors. As a result of the new rules, companies performing DOD contracts using FY 2010 funds will need to review and pay close attention to their employment and consultant agreements to make sure that they do not contain prohibited arbitration clauses

SUMMARY

If you need any additional information concerning the matters addressed in this Client Alert or other issues relating to government contracting, you can contact **Ken Brody of David, Brody & Dondershine, LLP at 703-264-2220** or **KBrody@dbd-law.com.** Additional information concerning David, Brody & Dondershine, LLP can be found at www.dbd-law.com.
