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AGC of America
THE ASSOCIATED GENERAL CONTRACTORS OF AMERICA
Quality People. Quality Projects.



December 7, 2015

Ms. Brenda Fernandez
Office of Policy Planning & Liaison
U.S. Small Business Administration
409 Third Street SW
Washington, D.C. 20416

RE: Credit for Lower Tier Small Business Subcontracting Proposed Rule; RIN: 3245-AG71

Dear Ms. Fernandez,

On behalf of the Associated General Contractors of America (AGC), I would like to thank you and the U.S. Small Business Administration (SBA) for soliciting comments on allowing non-small prime contractors to receive credit towards their small business subcontracting goals for awards made to small business subcontractors at any tier. This reform will help capture true small business participation on federal contracts by generating useful data that can improve the federal small business subcontracting program. That stated, AGC has a number concerns about the proposed requirements to implement this new approach.

AGC is the leading association for the construction industry, representing both union and non-union prime and subcontractor/specialty construction companies. AGC represents more than 26,000 firms including over 6,500 of America's leading general contractors and over 9,000 specialty-contracting firms. More than 10,500 service providers and suppliers are also associated with AGC, all through a nationwide network of chapters. The majority of AGC contractors are small businesses with 20 or fewer employees. AGC contractors are engaged in the construction of the nation's commercial buildings, shopping centers, factories, warehouses, highways, bridges, tunnels, airports, waterworks facilities, waste treatment facilities, dams, water conservation projects, defense facilities, multi-family housing projects, site preparation/utilities installation for housing development, and more.

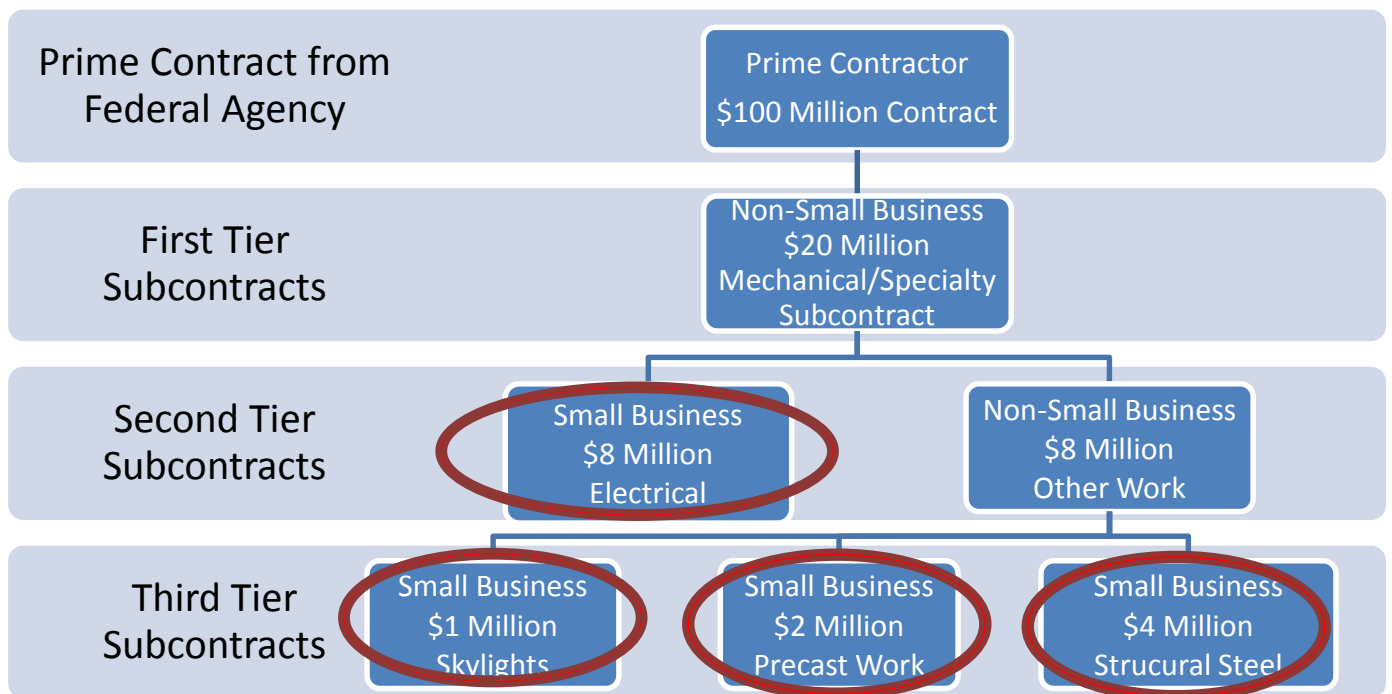
First, these comments will explain the background, need for and benefit of this SBA proposed rule. Then, the comments will address particular issues with the SBA's proposed rule.

I. Background on SBA Proposed Rule

HOW THE CURRENT SYSTEM FAILS TO ACCOUNT FOR TRUE SMALL BUSINESS PARTICIPATION

Current rules require goals for small business subcontractors, but prohibit prime contractors from truly accounting for the total amount of dollars flowing to small businesses. As it stands, if a business deemed large by SBA standards is included as a first tier subcontractor, a prime contractor unable to report any subcontracting dollars going to small businesses at lower tiers. Unfortunately, this does not provide a complete picture of true small business participation on a project or in the construction industry. The SBA's proposed rule would help bring greater transparency and accuracy to small business subcontracting goals as shown through the following example of an agency procurement program for the construction of building valued at \$100 million:

- An agency procures the construction of a \$100 million building. One of the first tier subcontracts is for all necessary mechanical and other specialty work, including electrical. The prime contractor awards that first tier subcontract, valued at approximately \$20 million, to a non-small business, as typically there are not any qualified mechanical/specialty small businesses to bond, preform or manage a contract of that magnitude. That first tier small business contractor, in turn, subcontracts \$8 million in electrical work to a second tier small business.
- The current law allows, but implementing regulations prevent, the prime contractor from counting the \$8 million second tier small business work, as that work is beyond the first tier. If the first tier subcontractors are non-small business contractors, as is the case here, the counting and reporting stops. That is true even though the electrical subcontractor is a small business.
- The counting problem is compounded if the first tier non-small business subcontractor then subcontracts an additional \$8 million a non-small business that, in turn, subcontracts to small business specialty trades that provide work such as skylights (\$1 million), precast (\$2 million) and structural steel fabrication (\$4 million). As a result, another \$7 million subcontracted would not be counted in this example under the current rules.
- The diagram below depicts the example discussed above. Under the current rules, the small business contracts circled below are *not* counted towards a prime contractor’s small business subcontracting goals. In this example, \$15 million in small business subcontracts would not be counted toward the subcontracting goal and the government would likely have no record of this degree of small business participation.



THE BENEFIT OF COUNTING SMALL BUSINESS SUBCONTRACTOR PARTICIPATION AT ALL TIERS

Allowing prime contractors to report small business subcontracting at all tiers will help demonstrate true small business participation on a federal contract. Consequently, Congress and federal agencies will be

better able to determine where small businesses are underrepresented and make informed improvements to the small business program.

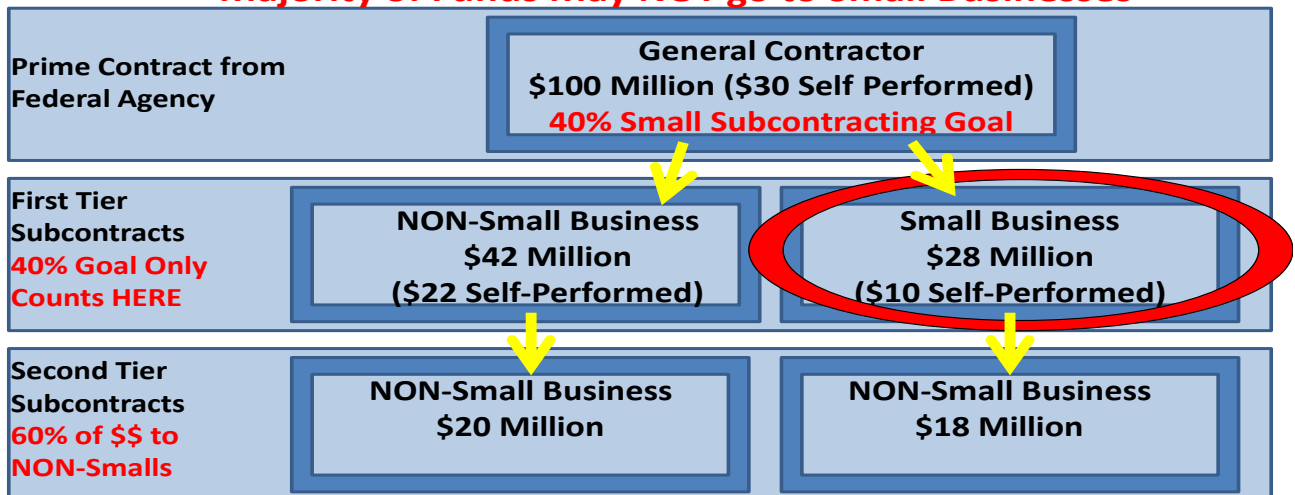
In addition, this reform will help ensure that small businesses actually gain the experience the program intends for them to gain through the enactment of these goals. However, as it stands, many prime contractors raise small business subcontractors that usually work at lower tiers to the first tier to help meet current small business subcontractor goals. Oftentimes, those small business subcontractors then join with non-small businesses, which actually perform a significant amount of the work and have the bonding capacity to guarantee it. As a result, much of the work experience the small business program intends for a small business subcontractor to gain is actually passed through to contractors that are other than small. Prime contractors are incentivized structure their teams in this inefficient way that is not beneficial to the small business or government because agency small business participation plans and subcontracting plans are an important element in the contract award process.

Small business participation and/or the subcontracting plan typically is an evaluated element of an offerors proposal as well as the offerors past performance. Enabling prime contractors to count lower tier small business participation toward the proposed small business goals will encourage other than small business offerors to target qualified small business subcontractors to participate at a level they are most capable to perform. This will benefit both the federal small business subcontracting program and the small businesses by allowing them gain critical experience in the federal contracting environment. The charts below further illustrate the benefits of this reform.

Current Law

GROWTH: PROVIDING FOR MORE SMALL BUSINESS PARTICIPATION

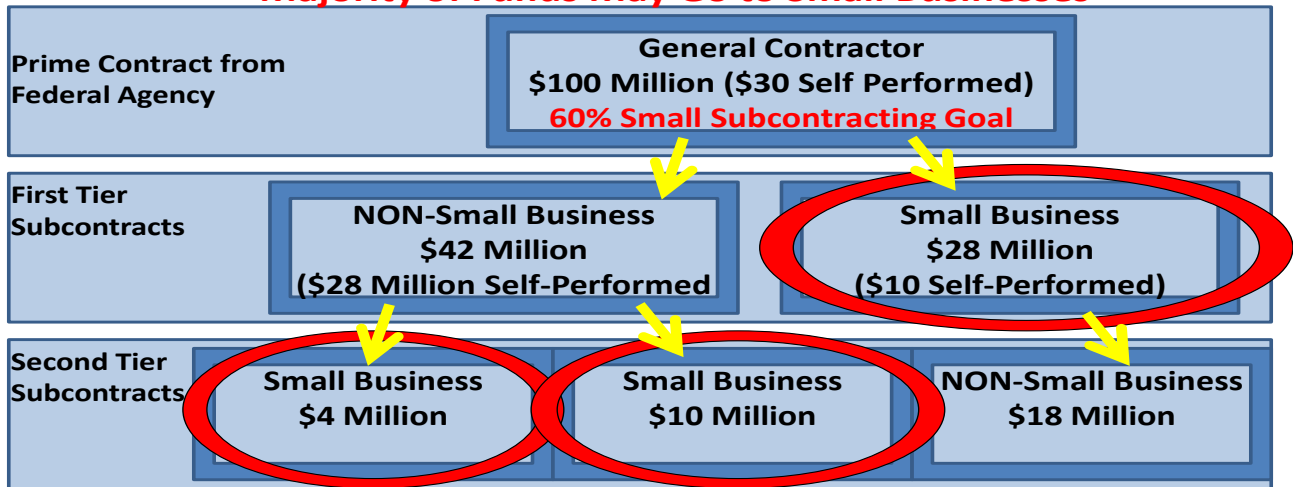
- General Contractor Goaled on Maximum Practicable Utilization of Small Business at ONLY 1st Tier
- NO Incentive to Drive Small Business \$\$ Below 1st Tier
- Majority of Funds May NOT go to Small Businesses



REFORM

GROWTH: PROVIDING FOR MORE SMALL BUSINESS PARTICIPATION

- General Contractor Goaled on Maximum Practicable Utilization of Small Business at ALL Tiers**
- Incentive to Drive Small Business \$\$ at ALL Tiers**
- Majority of Funds May Go to Small Businesses**



II. AGC Comments on SBA Proposed Rule

THE SBA PROPOSED RULE RIGHTLY INTERPRETS STATUTE BY NOT ESTABLISHING TWO TYPES OF SMALL BUSINESS SUBCONTRACTING GOALS

As noted, current rules only allow non-small prime contractors to credit first-tier small business subcontracts towards their small business subcontracting goals. Section 1614 of the National Defense Authorization Act for Fiscal Year 2014 (NDAA) modifies these rules to allow non-small prime contractors with individual prime contracts to take credit for small business subcontracts at *all tiers* towards small business subcontracting goals.

The NDAA neither explicitly nor implicitly requires the SBA to establish two separate small business subcontracting goals: (1) one for the first-tier subcontracts; and (2) another for subcontracts below the first subcontracting tier. Construction contractors are required to negotiate with the procurement authority a subcontracting plan which incorporates the information prescribed in 15 U.S.C § 637(d)(6). Paragraph (d)(6) explicitly details what must be included in a subcontracting plan, including the inclusion of percentage goals for the utilization small business subcontractors at (d)(6)(A). Section 1614 of the NDAA states that “[n]othing . . . shall abrogate the responsibility of a prime contractor to make a good-faith effort to achieve the first tier small business goals under [15 U.S.C § 637(d)](6)(A).”

Section 1614 of the NDAA, therefore, retains the currently existing regulatory method of establishing small business subcontractor goals based on subcontracts awarded at the first-tier of subcontracting, but now allows for credit towards those goals to be received through subcontracts at all tiers of

subcontracting. Paragraph (d)(6)(A), remember, establishes the inclusion of percentage goals for the utilization of small business subcontractors. It does not express how those goals are established—either at the first tier or lower tiers. The NDAA, however, now makes clear that those goals are established at the first-tier in its language stating that the small business goals under Paragraph (d)(6)(A) are “first tier small business goals.” Prior to this NDAA language, 15 U.S.C. § 637 made no reference as to how to establish those small business subcontracting goals or how to credit small business subcontracts towards that goal. Rather, the decision to count first-tier small business subcontracts towards these goals was a regulatory agency decision.¹ Through section 1614 of the NDAA, Congress explicitly states that these small business subcontracting goals: (1) are established for and based on the first-tier subcontracting opportunities—in an effort to ensure good faith prime contractor efforts; and (2) small business subcontracts at the first or any tier count towards achieve those goals. Consequently, the SBA has correctly interpreted section 1614 and the existing provisions within the Small Business Act by not establishing two small business subcontracting goals—one at the first tier and one at lower tiers.

AGC contends, however, that the SBA confuses the direction of section 1614 in its proposed section 123.3(c)(1)(i). Again, section 1614 clearly articulates that the small business subcontracting goals within the small business plans negotiated between non-small prime contractor and procurement authority are “first tier small business goals.” As a result, those goals should be based on the maximum practicable opportunities for small businesses in the performance of the contract as subcontractors or suppliers at the *first tier* of subcontracting, *not at all tiers* of subcontracting performance. The maximum practicable opportunities for small business subcontracts at all tiers will—generally speaking—always be greater than the maximum practicable opportunities at the first tier. If the SBA makes such a change, it will effectively raise the small business subcontracting goals established by Congress in clear contradiction of section 1614. AGC strongly urges the SBA to change the “at all tiers of performance” language in section 123.3(c)(1)(i) to “at the first tier of performance” in accordance with section 1614 and to avoid litigation that it has arbitrarily and capriciously interpreted that statute.

REQUIRING NON-SMALL BUSINESS PRIME CONTRACTORS TO ASSIGN NAICS CODES AND CORRESPONDING SIZE STANDARDS TO THEIR SOLICITATIONS FOR SUBCONTRACTOR BIDS WILL BE PROBLEMATIC FOR THOSE PRIMES AS WELL AS SUBCONTRACTORS

The proposed rule requires a contractor to assign “to the [subcontract] solicitation and resulting subcontract the NAICS code . . . that best describes the principal purpose of the subcontract.” AGC is concerned about the difficulty prime contractors will have including the correct NAICS codes in their subcontract solicitations. A cursory search of the word “construction” in the 2012 NAICS Codes database available through the U.S. Census Bureau brought up 412 unique codes. There are also large numbers of codes for equipment rental, construction supplies and materials, furniture and fixtures, and other construction project functions that may be subcontracted. One subcontract may cover multiple NAICS codes. Amid hundreds of codes and subcontracts with wide varieties of construction-related work, the process of contractors including one NAICS code in its subcontract solicitations may be extremely difficult, confusing and subjective. Additionally, AGC fears that if a prime contractor solicits a subcontract under one NAICS code—or the wrong NAICS code—potential subcontractors may not review or consider the solicitation based on that label. This could, in turn, limit small business subcontractor bids. AGC recommends that this requirement be removed in a final rule. In the event that the SBA retains this particular NAICS code requirement, the agency should remove the requirement of

¹ See Federal Acquisition Regulation (FAR) clauses 52.219-8 (Utilization of Small Business Concerns) and 52.219-9 (Small Business Subcontracting Plan).

including a NAICS code in the subcontract solicitation and allow the subcontractor to simply report this information as a requirement upon subcontract award. A subcontractor that is performing the work in the subcontract, not a prime contractor, is likely most familiar with the subcontracting NAICS codes through which it performs work.

In addition, AGC seeks further clarity on a number of terms. First, the association respectfully requests more information concerning the definition of a “contractor” as used in section 125.3(c)(1)(v). Other than small contractors that may have small business subcontracting plans include not only prime contractors, but also subcontractors. The language in section 125.3(c)(1)(v) is confusing because it uses the phrases “contractor,” “prime contractor,” and “subcontractor” seemingly interchangeably, making it difficult to understand who is required to do what. AGC assumes that a non-small prime contractor or non-small subcontractor with a subcontracting plan would have to abide by the proposed NAICS code requirement and may rely on subcontractors’ electronic size and socioeconomic representations and certifications. However, again, the current language makes that assumption unclear. AGC recommends that the SBA use more precise terms—(i.e., non-small business prime contractor, small business/non-small business subcontractors)—to ensure that prime contractors and subcontractors of all sizes understand the requirements for this section.

THE PROPOSED RULE PRESENTS A QUESTION AS TO ACCEPTABLE MEANS FOR A PRIME TO CONFIRM A COMPANY’S SIZE OR SOCIOECONOMIC STATUS: WOULD THE PROPOSED RULE IMPACT FAR 19.703(B) AND FAR 19.703(D)(1)?

The proposed rule in section 125.3(c)(1)(v) would allow a prime contractor to “rely on a subcontractor’s *electronic* representations and certifications” of its size or socioeconomic status. FAR 19.703(b) allows prime contractors to rely on a potential subcontractor’s “*written* representation” as to its size or socioeconomic status. However, FAR 19.703(d)(1) requires a prime contractor to independently confirm that the SBA certifies a company as a HUBZone company by accessing SAM or contacting the SBA.

AGC is concerned that the SBA’s proposal will eventually add to confusion within the FAR. The approach SBA takes should be consistently adopted within the FAR or the SBA should remain consistent with current FAR provisions. Either way, the SBA must work towards adopting a standard method for prime contractors to rely upon for satisfying these criteria. AGC recommends that the SBA allow prime contractors to rely on electronic representation and certifications of its size or socioeconomic status for those firms registered in SAM and the use of written representations and certifications of its size or socioeconomic status for those not registered in SAM at the time of subcontractor award.

PRIME CONTRACTOR REQUIREMENTS TO POLICE SUBCONTRACTORS’ INDIVIDUAL SUBCONTRACTING PLANS MUST NOT OVERLY BURDEN CONTRACTORS AND NEED FURTHER CLARITY

The SBA’s proposed section 125.3(c)(1)(x) closely mirrors the language in Section 1614 of the NDAA. In that paragraph, however, the SBA neither defines, nor provides more clarity on a host of new requirements for prime contractors. Under the proposed rule, prime contractors must do all of the following:

1. Review and approve subcontractors’ subcontracting plans;
2. Monitor subcontract compliance with subcontractors’ approved subcontracting plans;
3. Ensure that subcontracting reports are submitted by their subcontractors when required;
4. Acknowledge receipt of their subcontractor reports;

5. Compare the performance of their subcontractors to subcontracting plans and goals; and
6. Discuss performance with subcontractors, when necessary, to ensure their subcontractors make a good faith effort to comply with their subcontracting plans.

Currently, FAR clause 53.219-9 contains a flow-down provision requiring the inclusion of that clause in all construction subcontracts with opportunities for further subcontracting and in excess of \$1.5 million (for construction) awarded to large business subcontractors. That provision requires the inclusion of further flow down clauses for lower tier subcontracts under the same conditions. The proposed SBA requirements will place new burdens directly on prime contractors. As such, AGC urges the SBA to further clarify actions that are sufficient to meet each requirement. For example, what prime contractor actions sufficiently meet the “monitoring” of subcontract compliance with approved subcontracting plans? Would a simple email or letter suffice for acknowledgment of receipt of subcontractor reports? When would it be “necessary” for a prime contractor to discuss performance with subcontractors concerning their subcontracting plans? Does a discussion require in-person meetings or would electronic or written correspondence suffice? Furthermore, the term “subcontracting reports” used throughout paragraph 123(c)(1)(x) is undefined. Are these reports from a subcontractor to a prime contractor about their subcontracting plan performance? Should prime contractors assume that they will have to establish subcontracting plan reporting systems or forms through which their subcontractors must respond on a routine basis? If so, what timely basis—i.e., annually, quarterly or monthly—would satisfy the monitoring component of these requirements?

AGC is unable to determine if these proposed requirements are overly burdensome or not without answers to the aforementioned questions. That stated, to meet these requirements AGC recommends that the SBA clearly articulate how prime contractors should review, approve and monitor their subcontractors’ individual subcontracting plans. Such an explanation may include, but may not be limited to, a prime contractor’s establishment and exercise of a monitoring program whereby the prime receives reports from subcontractors concerning their subcontracting plans. Such reports may include information exhibiting statistics or narrative of how the subcontractor is or is not meeting its small business subcontractor goal. The SBA publication entitled “A Handbook for Small Business Liaison Officers – June 2010” provides a good source for information and examples of how contractors may meet good faith requirements.² AGC suggests that the SBA use that handbook—and the examples used for good faith—as a guide for further illuminating the requirements within 123(c)(1)(x).

THROUGH WHAT SYSTEM WILL THE FEDERAL GOVERNMENT TRACK NEWLY GENERATED DATA TO COUNT LOWER TIER SUBCONTRACTORS?

As noted above, AGC believes that transparency in federal government contracting is essential to ensuring the growth of America’s small businesses. The requirements set forth in this proposed rule authorize non-small prime contractors to take credit for small business subcontractors at all tiers—not just the first tier—of subcontracting. The proposed rule, however, provides little understanding as to how this information will be submitted to the government and credited to prime contractors. Prime contractors will seemingly submit subcontractor small business data for all tiers to federal agencies to receive their credit and provide the government with greater insight as to the extent of small business support through federal contracts. Consequently, AGC respectfully requests that the SBA provide details as to which federal government system will track this information and any requirements for data entry that the system may require. The use of such a system must be included in a final rule. The proposed rule is likewise unclear

² [https://www.sba.gov/sites/default/files/Small_Business_Liaison_Officer_\(SBLO\)_Handbook_6_2010.pdf](https://www.sba.gov/sites/default/files/Small_Business_Liaison_Officer_(SBLO)_Handbook_6_2010.pdf)

on how non-small business subcontractors that are required to have subcontracting plans will report their data.

That stated, AGC recommends that the federal government use the Electronic Subcontracting Reporting System (ESRS) to allow for the submission and retrieval of this data and include that in a final rule. AGC does not recommend the creation of a completely new electronic system—or prime contractors creating individual, in-house data systems—for gathering non-small subcontractor plan data, but rather suggests improving the ESRS to minimize costs to the government and contractors. As it stands, non-small subcontractors already use ESRS to report their small business plan information; and federal agencies—not prime contractors—may currently take credit for that information.

AGC notes, additionally, that the proposed rule may lack clarity as to who may receive credit for lower tier small business subcontractor dollars—federal agencies or prime contractors. The last sentence of 125.3 (a) (1) (i) (C) states that “[t]he actual subcontracting dollars are only reported once for the same award to avoid double counting the dollars, notwithstanding the fact that a small business subcontract may be reported under more than one subcontracting plan.” The statute unequivocally intends for prime contractors to be credited for small business subcontractor dollars at all tiers for purposes of meeting their small business subcontracting goals. If the SBA fears double counting in the sense of what entity is allowed to take credit for these dollars—government or prime contractor—the statute articulates that prime contractors must be credited for this information. As such, AGC recommends that the SBA more clearly state this fact in a final rule.

CONCLUSION

AGC, again, thanks you for the opportunity to comment on this important regulatory proposal. The association strongly supports the efforts of the SBA to create a more transparent small business contracting arena. However, as noted above, we believe that the proposal requires further clarification to help eliminate confusion and minimize any burden on contractors.

Thank you for your consideration.

Sincerely,

Jimmy Christianson

Jimmy Christianson
Director, Government Affairs
Federal & Heavy Construction Division
Associated General Contractors of America