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June 30, 2010

Mr Joseph Jordan
Associate Administrator
Small Business Administration
409 Third Street, SW, Suite 8000
Washington, DC 20416

RE: *FR Doc. 2010-14144, June 11, 2010—Small Business Task Force Request for Comments*

Dear Mr. Jordan:

On behalf of the National Association of Surety Bond Producers (“NASBP”), a national trade association of professional surety bond producers, representing over 5,000 personnel who specialize in surety bonding, placing bid, payment and performance bonds for the nation’s construction projects, and The Surety & Fidelity Association of America (SFAA), an association of more than 450 surety companies that are licensed to and collectively provide the vast majority of payment and performance bonds on federal and state construction projects, we appreciate the opportunity to comment on increasing small contractor participation in federal contracting. Our comments below address only federal construction projects. We also suggest legislation that the Interagency Task Force might consider supporting that we believe will provide greater opportunities to small and emerging contractors to participate as prime contractors on federal construction projects.

A performance bond secures a contractor’s obligation to perform fully the contract. A payment bond secures the contractor’s obligation to pay its subcontractors and suppliers. The federal government and all states have statutes that require a performance and payment bond on public construction projects. The federal government’s bond requirements are set forth in 40 U.S.C. 3131 et seq. Sureties have a close relationship with contractors and have a strong interest in developments that affect contractors’ access to contract opportunities. In addition, because a surety prequalifies a contractor in assessing the contractor’s ability to perform a particular project before issuing the performance bond and payment bond, sureties are particularly knowledgeable of the issues regarding the qualities and characteristics necessary for the successful completion of a project.

Removing Barriers to Small Business Participation—Many Federal Construction Contracts are Just Too Big for Small Contractors

The Small Business Reauthorization Act of 1997 defines *contract bundling* as “consolidating two or more procurement requirements for goods or services previously provided or performed under separate, smaller contracts into a solicitation of offers for a single contract that is unlikely to be suitable for award to a small business concern.” Because these large contracts have significant durations and encompass a sizeable scope, they reduce the number and frequency of opportunities for small businesses to bid on and be awarded federal work.

Changes were made in the federal procurement process in the 1990s to make the process quicker, less complex and more efficient in light of the overall reductions in federal acquisition work force. To achieve the economies of scale and to address lack of resources in federal contracting agencies to oversee contracts awarded, the federal government began awarding larger contracts. Awarding only large contracts virtually ensures that small contractors will not be able to obtain these federal construction contracts since they do not have the capacity and capital necessary to complete the contract, and therefore, will not be able to provide the required bonds.

Bundling contract procurements or letting larger contracts is a reaction to a stretched procurement work force. According to Acquisition Workforce Development Strategic Plan, Fiscal Years 2010-2014, which was released by the Office of Management & Budget in October 2009, acquisition spending has increased 56% since FY2000, while the number of contract specialists grew by only 24%. In addition, about one federal acquisition professional in eight is eligible to retire and that number will rise to more than half the workforce by 2016. Hiring additional federal contracting officers will ensure proper and efficient contract administration.

Procuring construction services in larger dollar volume is a means to control the number of procurements that must be managed. The push for larger procurements, however, is at odds with the goal to enhance contracting opportunities for small businesses. The high dollar value of some federal government construction projects make them impossible for a small contractor to undertake. We are aware of instances of small business construction project opportunities valued in excess of \$50 million. There simply is a disconnect between the size of projects that are advertised to meet small business goals and the size of construction projects that the small contractor is qualified to perform.

Well-meaning legislation in Congress also has contained this disconnect. H.R. 1873 in 2008 was intended to prevent unjustified bundling of federal government contracts, including construction, in order to increase the participation of small businesses in federal work. The bill included language, which NASBP and SFAA supported, that amended the definition of contract bundling to include new construction projects so that these procurements would be scrutinized in light of anti-contract bundling requirements, thereby providing more small construction firms with the opportunity to participate as prime contractors on federal construction projects. In 2008 the U.S. Army Corps of Engineers called into question whether anti-bundling rules apply to new construction procurements in *Tyler Construction Group v. U.S.*, 83 Fed. Cl. 94 (Fed. Cl. 2008). The U.S. Court of Federal Claims stated “whether the bundling provisions of 15 U.S.C. § 631(j) should or do apply to acquisitions for new construction is a question we leave to Congress.” Before H.R. 1873 passed in

the House, however, a \$65 million threshold was added to the bill for challenging bundling in construction contracts. For all practical purposes, this threshold took away any meaningful reform for small and emerging contractors. S. 2300 also addressed contract bundling in 2008, but this bill exempted the Department of Defense, a major federal contracting agency for construction projects. Neither bill was enacted.

A primary cause of the access issue that must be addressed is the high number of large dollar procurements as caused by a stretched procurement work force. Simply put, there are not enough contracting officers to procure construction efficiently, thereby causing the bundling of small contracts into large contracts. Consolidation of contracts into large contracts eliminates the ability of small construction firms to compete for federal contract awards as prime contractors. One solution is to bolster the procurement work force now to keep pace with acquisition spending. Another solution is to apply existing and any new anti-bundling laws and regulations to federal construction projects.

Removing Barriers to Small Business Participation--Creating and Enforcing Reasonable Small Business Participation Goals in Federal Construction Projects.

The federal contracting agencies generally have a goal that requires 23% of the total dollars awarded in government contracts to be given to small businesses. This ambitious goal combined with a stretched procurement work force within the federal government leads to project opportunities that are set aside for small businesses, but are quite large.

We attended the hearing of the Interagency Task Force on June 28, and appreciate the comments of many small businesses that provide goods and services to the federal government. Once they exceed revenue or employee thresholds, they are no longer considered "small businesses" and have to compete for federal contracts of any size with huge national or multinational corporations. They want to increase the size thresholds or the time period in which a small business can continue to bid for contracts set aside for small contractors once they have grown and exceeded the thresholds.

In the construction industry, however, small means small. Significantly increasing the size standard of a small contractor may create a further barrier to small contractor participation. Contractors have to be qualified to undertake any federal construction project, and the small contractors in the industry often cannot bid for them because of the size of the contracts. Increasing the size standard for small business so that more, and much larger contractors, can qualify for large federal contracts will not help the genuinely small contractors in the industry.

To facilitate the attainment of this goal we offer the following suggestions for federal construction projects:

1. Small contractors that participate in joint venture and mentor/protégé programs should not lose their status as a qualified small business. The federal procurement rules need to be changed as to federal construction projects to permit small contractors to participate in federal work to the extent that they can. Federal agencies letting construction contracts to small contractors in joint ventures should be permitted to count the work that the small

contractor self-performs toward their small participation goal. In any such joint venture, the small business should be subject to certain reasonable self-performance requirements, such as self-performance of at least 10% of the work. As a further incentive to the procuring agency, the agency could be permitted to count some multiple of the small contractor's work that is self-performed, such as two or three times that amount.

2. All federal agency letting construction contracts should be required to let 5% of its total procurement budget in contracts of no more than \$5 million. These contracts would be part of the agency's federal small participation goals. The regulations also should provide for incentives to the procuring agency with respect to the number of small contract opportunities (under \$5 million) over the 5% requirement. For example, for any contract under \$5 million that is in excess of the 5% threshold, the procuring agency could be credited with \$5 million toward its small participation goal, regardless of the contract amount.

Removing Barriers to Small Business Participation—Restoring Payment Protections of the Miller Act

41USC§ 431a provides for automatic periodic inflation adjustments to procurement thresholds. Certain thresholds, however, specifically are excluded from this provision. The Interagency Task Force should advocate for an amendment to the federal procurement law to exclude construction contracts that must be bonded under the Miller Act.

Establishing inflation-based thresholds for surety bond requirements is an unsound policy. Inflation-based thresholds for matters directly related to procuring construction services makes sense, as the cost for the same materials and equipment has increased over the years. The considerations in setting a threshold for a bond requirement go beyond the cost of materials and equipment.

Surety bonds on federal projects protect subcontractors and suppliers on these projects. If there is no bond and a contractor defaults, these subcontractors and suppliers have no recourse for payment. They cannot sue the federal government, and there is no independent third party guaranteeing payment. Most small contractors start as subcontractors, and the increase in a bond threshold means those small contractors who need the payment protection the most, will not have it. The Miller Act was amended in 1999 specifically at the request of subcontractors to address the lack of payment protection by less than 100% payment bonds. An increase in the bond threshold would result in the same type of lack of protection on a greater number of projects. Davis Bacon is excluded from the application of this automatic increase to protect the payment of wages to laborers on federal projects. The same basis applies to excluding the application to surety bonds to protect payments to subcontractors.

Innovative Strategies & Technologies to Increase Opportunities for Small Business Contractors—Changes to Mentor-Protégé, Joint Venture and Teaming Programs

Mentor/protégé programs and joint ventures with larger contractors could provide a means for small contractors to participate in public construction projects. With the involvement of a larger contractor, the small contractor can take advantage of the expertise and experience (and perhaps the

financial support) of the larger contractor. The current regulations, however, lack clarity and standardization among the procuring agencies as to what arrangements are acceptable.

In addition, the federal regulations present disincentives to participate in a joint venture with a larger contractor. In some cases, a small business could lose its qualification as a small business if it participates in a joint venture in which the joint venture partner does not qualify as a small business, foreclosing one possible avenue for small businesses to act as prime contractors on federal construction projects. Once an otherwise qualified small business loses its status, the small contractor cannot take advantage of the set-aside opportunity and the federal agency letting the construction contract faces an obstacle in meeting its small business participation goal.

Teaming agreements provide a means for a small contractor to undertake a larger project, short of entering into a joint venture. The larger contractor, often acting as a subcontractor, lends its resources and expertise to the project. In many cases, the small contractor is able to obtain the required performance and payment bond because the larger contractor has agreed to provide the surety its indemnity, with the necessary disclosures to the government agency. Contractors and sureties, however, have found that there is a lack of standardization among procuring agencies (and even among contracting officers in the same agency) regarding how the teaming agreement is administered. For example, we understand that there is diversity of opinion regarding whether the larger contractor can take over the work of the defaulted small contractor pursuant to the teaming agreement. Some contracting officers maintain that a small contractor must complete the project. Standardization and greater transparency in the administration of teaming agreements is recommended.

Innovative Strategies to Increase Opportunities for Small Contractors--Reforms to the SBA Bond Guarantee Program

The SBA Bond Guarantee Program (Bond Program) was created to ensure that small and emerging contractors have the opportunity to bid on public construction work, grow their businesses and become a viable part of the U.S. economy. Surety bonds are a vital mechanism to protect taxpayers and workers on public construction projects from the danger of contractor default. Emerging small businesses must have access to these bonds to obtain federal construction contracts, and the SBA program assists them in obtaining these bonds. SFAA and NASBP have developed amendments to the SBA Bond Program that the entire surety industry supports as a way to streamline and modernize the Bond Program to make it more useful to small contractors and more economically feasible and attractive for sureties and bond producers to participate. The Interagency Task Force should advocate the additional enhancements that are necessary to increase small business access and utilization of the SBA Bond Guarantee Program. These enhancements include:

- Combining the SBA Prior Approval Program and the Preferred Program into one bond unified guarantee program;
- Increasing the SBA guarantees to sureties up to 90%;
- Reducing the fees paid by contractors and sureties;
- Making permanent the temporary increase in the size contract that can be guaranteed to \$5 million and up to \$10 million if a federal agency's contracting officer certifies that the guarantee is necessary;

- Making permanent the discretion given to the Administrator under ARRA to determine the Program's liabilities;
- Creating a system of due process in connection with the SBA Bond Guarantee Program so that sureties receive notice, a hearing and right to appeal if: 1) the SBA denies a surety's request to participate in the Program or eliminates a surety from the Program, or 2) denies a claim under a bond that the SBA has guaranteed and;
- Providing the SBA with greater regulatory authority to enforce contract bundling rules and to scrutinize contracting agencies that are bundling construction contracts.

A more detailed description of the legislative changes needed to the SBA Bond Program is attached.

Innovative Strategies & Technologies to Increase Opportunities for Small Contractors--A Technical Assistance Grant Program to Benefit Small Construction Businesses

The Interagency Task Force should advocate for legislation that funds technical assistance grants and establishes standing educational programs to assist veteran, minority- and women-owned small businesses to improve their ability to compete in the construction industry. Legislation has been introduced by Congresswoman Yvette Clarke, H.R. 3771, that establishes grants for small construction firms to use in hiring legal, accounting, and business consultants for services needed to prepare them to qualify for surety credit. For example, the emerging or small construction firm could obtain a monetary grant to hire a construction attorney and a certified public accountant to put in place sufficient business accounting and risk management systems. The grant program could partner with industry groups comprised of CPAs, construction attorneys, risk management experts, financial experts/bankers and surety bond producers, to participate in and market the program. The legislation also creates a federal grant program for vocational/technical schools and community colleges to fund the development of a curriculum on how to develop a meaningful business model for small contractor companies. The grant program could partner with industry groups comprised of CPAs, construction attorneys, risk management experts, financial experts/bankers and surety bond producers, to help develop, participate in, and market the program.

Innovative Strategies & Technologies to Increase Opportunities for Small Contractors—Better Communications and Coordination Between Federal Agencies

The Interagency Task Force must evaluate the federal government's focus on and assistance to small businesses by ensuring better intragency and interagency communications and coordination of their programs. This may be accomplished by creating an automatic referral system. For example, a small construction firm might benefit from both the SBA Loan Program and its Bond Guarantee Program but may not be aware of the existence of both programs. Federal procurement officers should be required to counsel small business owner and refer them to other federal agencies that would help to increase business opportunities. Such coordination, however, should not delay a small contractor from getting the immediate assistance requested. For example, if the contractor applies for a bond guarantee from the SBA Bond Guarantee Program, the bond application should be acted upon immediately, while the contractor is also advised of other SBA or federal agency programs that could be helpful.

Joseph Jordan
June 24, 2010
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Summary and Conclusions

The Interagency Task Force must address the overarching condition that stifles small contractor access to federal contracting opportunities: a stretched procurement work force, unreasonably large procurements and a framework for achieving small business participation objectives that is incompatible with the current procurement environment. We hope the solutions suggested above along with working with Congress to adopt legislation will provide greater opportunities for small businesses to participate as prime contractors on federal construction projects.

Sincerely,



Lynn Schubert
President
The Surety & Fidelity Association of America



Mark McCallum
Chief Executive Officer
National Association of Surety Bond Producers