It's tough to be a small business, competing against larger contractors in today's shrinking budget environment. Sure, there are set-asides and 8(a) programs and the AbilityOne Program and Mentor-Protégé programs. They do provide opportunities to qualifying small business that the larger businesses simply can't access. But the fact is that the qualifying small businesses simply don't have the capital or the resources to compete against the bigger firms in a "full and open" environment.

Small businesses typically don't have the working capital to invest hundreds of thousands of dollars in a proposal, only to wait six months (or more) to see if they won the contract. If they don't win—and they believe they were wronged—they usually lack the funds to hire competent attorneys to pursue bid protests. They may not even understand that such an avenue of redress is available to them.

Even when the competition is on the up-and-up, small businesses generally lack the skilled subject matter experts to put together proposals that comply with the Truth-in-Negotiations Act (TINA) or, for that matter, to support DCAA audits (performed in compliance with Generally Accepted Government Auditing Standards, or GAGAS) that start with a 34 point adequacy assessment and then get deep into the details of how the estimate of future direct and indirect costs was generated.

Speaking of direct and indirect costs, too many small businesses lack "adequate" accounting systems (as that term is defined by either the Standard Form 1408, or by DCAA 17740 audit programs, or by the Defense Federal Acquisition Supplement (DFARS) contract clause 252.242-7006 ("Accounting System Administration"). Consequently, they are officially ineligible to receive cost-type contracts. In addition, it's quite difficult to receive Time & Material or Labor

Hour contract types as well, because those contract types are lumped together into the “flexibly priced” contract category.

(Our opinion that FAR Part 16 does not list “flexibly priced” as a recognized contract type does not seem to help our clients get over this hurdle. They seem to be stuck with the choice of either having an “adequate” accounting system or not receiving a T&M contract award. But we digress ….)

And we haven’t even mentioned unallowable costs, or management of Government property, or a host of other contract compliance requirements whose compliance regimes take significant investments of time and money (and expertise) to create.

So yeah, small businesses have it tough when they want to go up against the big dogs on an open playing field. But when they stay within their niche markets, they can do pretty well for themselves.

Recently, the Small Business Administration (SBA) issued a **final rule** that expands the number of companies that qualify for participation in the Small Business Innovation Research (SBIR) Program. As the respected government contract attorneys at the firm of McKenna, Long & Aldridge **summarized** —

The final rule allows concerns that are majority-owned by multiple venture capital operating companies, hedge funds or private equity firms (‘investment companies’) to participate in the SBIR program, as long as no single investment company owns more than 50 percent of the concern. In order to be eligible, the investment company must have a place of business in the U.S. and be incorporated in the U.S. Furthermore, concerns that are majority-owned by multiple investment companies must register with SBA on or before the date they submit a response to an SBIR solicitation and these concerns must indicate in their SBIR proposals that they have completed this registration. Unlike the proposed rule, however, the final rule does not allow concerns that are majority-owned by multiple investment companies to participate in the STTR program. …

Currently, investment companies would not be eligible to participate in the SBIR program, because the concern would be considered to be affiliated with not only the investment companies, but also the other companies owned by these investment companies. SBA’s final rule provides that a concern is an affiliate of an individual, concern, or entity that owns or has

the power to control more than 50 percent of the concern's voting stock. However, SBA may find a concern an affiliate of an individual, concern, or entity that owns or has the power to control 40 percent or more of the voting equity, based upon the totality of the circumstances. If no individual, concern, or entity is found in control, SBA will deem the Board of Directors to be in control of the concern.

The SBIR Program has helped many small businesses get a toehold into government contracting. And now the market niche has been widened to accept participants that have venture capital funding, which is going to make it more difficult for the other small businesses to compete. Those venture capital-backed small businesses may well have access to the funds and expertise to address some of the obstacles to growth that we recited at the beginning of this article. Accordingly, those venture capital-backed small businesses will likely have an advantage over the non-affiliated small businesses in the competition for scarce SBIR dollars. Certainly, they will be better positioned to transition from SBIR Phase 1 to SBIR Phase 2 contracts.

(As we have opined before, the SBIR Phase 1 FFP contracts are an order of magnitude easier to win and execute than the SBIR Phase 2 cost-type contracts, but again we digress ….)

So small businesses take note. You have been warned.

With respect to large businesses who cannot participate in these Programs, period. You should also take note of the **recent settlement** entered into by Caddell Construction Co., who agreed to pay $2 million in order to "resolve criminal fraud allegations arising from Caddell's intentional overstating of developmental assistance provided to a disadvantaged small business" as part of the DOD Mentor-Protégé Program.

The DOJ reported that (according to the settlement and Non-Prosecution Agreement executed by Caddell)—

… from February 2004 to March 2005, Caddell submitted more than 20 requests for payment to the DoD in connection with the Mentor-Protégé Program that significantly overstated the amount of developmental assistance Caddell had provided Mountain Chief. [*Note: Mountain Chief was "certified as a Native American, woman-owned and economically-disadvantaged small business".*]
In addition, Caddell filed documents falsely stating Mountain Chief's size and income, as well as the status of Mountain Chief's technical capabilities and business infrastructure. From April

2003 to October 2004, Caddell also submitted at least eight requests to the DoD for the Indian Incentive Program, for rebates based on services purportedly performed on subcontracts Caddell gave to Mountain Chief. Mountain Chief performed few, if any of these services, and the invoices were created solely to support Caddell's applications for payment.

Oops!

But that's not all. The settlement and NPA resolved the issues for the corporation, but not for the individuals accused of committing the alleged crimes. The DOJ press release also stated—

In January 2012, Daniel W. Chattin, 50, of Granite Bay, Calif., the son of Mountain Chief's owner and a project manager and consultant for Mountain Chief, and Mark L. Hill, 57, of Montgomery, Ala., the Mentor-Protégé Program Coordinator and a director of business development at Caddell, were indicted in the Middle District of Alabama on three counts of major fraud against the United States stemming from the same scheme. In addition, Hill was charged with one count of making a false statement to the DoD. Chattin and Hill await trial, which is scheduled to begin on April 22, 2013.

At the DOJ reminded the public, "The charges and allegations against Chattin and Hill are merely accusations and they are considered innocent unless and until proven guilty."

Small businesses have a tough challenge when they go up against larger companies in a "full and open" competition for government contracts. But when they stay in their niches designed to encourage and foster small businesses, they tend to do just fine. Those program niches are so attractive that, sometimes, larger companyes cut corners in an attempt to obtain some of the program benefits. When the companies (and their executives) get caught cutting corners, they have significant challenges of their own to overcome—challenges of the legal variety.

Recent changes to the SBIR eligibility rules have expanded the number of firms that can participate. Those newly eligible firms are likely to be better capitalized and have better access to subject matter experts, than traditional non-affiliated small businesses. We think that's going to make it more important than ever for the traditional small businesses to get their house in order, so that they can successfully compete for scarce SBIR dollars.

Not to make this article into too much of an advertisement, but Apogee Consulting, Inc., has helped small businesses with cost accounting, estimating, and administrative issues associated

with the SBIR Program, as well as with other matters. If you think you might need some assistance, why not consider giving us a call?