

Recommendation 80: Preserve the preference for procuring commercial products and services when considering small business set-asides.

Problem

When the government's needs may be met by products or services available in the commercial marketplace and contracting officers are considering a small business set-aside, they may face a dilemma if the small-business solution does not satisfy the definition of *commercial product* or *commercial service*. Neither statute nor regulation provides an order of precedence between the statute's preference for acquiring commercial products or services and the requirement to procure certain products or services from small businesses.

Background

Preference for Commercial Products and Services

One of the most pivotal parts of FASA was the establishment of a preference for the government to procure commercial products and commercial services rather than government-unique products and services. This preference is codified in 41 U.S.C. § 3307, Preference for Commercial Items:

(b) PREFERENCE. — The head of each executive agency shall ensure that, to the maximum extent practicable—

(1) requirements of the executive agency with respect to a procurement of supplies or services are stated in terms of—

(A) functions to be performed;

(B) performance required; or

(C) essential physical characteristics;

(2) those requirements are defined so that commercial items or, to the extent that commercial items suitable to meet the executive agency's needs are not available, nondevelopmental items other than commercial items may be procured to fulfill those requirements; and

(3) offerors of commercial items and nondevelopmental items other than commercial items are provided an opportunity to compete in any procurement to fill those requirements.

The preference is also codified in 10 U.S.C. § 2377, Preference for Acquisition of Commercial Items:

(a) PREFERENCE . — The head of an agency shall ensure that, to the maximum extent practicable—

(1) requirements of the agency with respect to a procurement of supplies or services are stated in terms of—

(A) functions to be performed;

(B) performance required; or

(C) essential physical characteristics;

(2) such requirements are defined so that commercial items or, to the extent that commercial items suitable to meet the agency's needs are not available, nondevelopmental items other than commercial items, may be procured to fulfill such requirements; and

(3) offerors of commercial items and nondevelopmental items other than commercial items are provided an opportunity to compete in any procurement to fill such requirements.

This preference is implemented in FAR Part 10, Market Research, Subpart 10.002, Procedures and Part 12, Acquisition of Commercial Items, Subpart 12.101, Policy:

(d) (1) If market research establishes that the Government's need may be met by a type of item or service customarily available in the commercial marketplace that would meet the definition of a commercial item at Subpart 2.1, the contracting officer shall solicit and award any resultant contract using the policies and procedures in Part 12.

Agencies shall --

(a) Conduct market research to determine whether commercial items or nondevelopmental items are available that could meet the agency's requirements;

(b) Acquire commercial items or nondevelopmental items when they are available to meet the needs of the agency; and

(c) Require prime contractors and subcontractors at all tiers to incorporate, to the maximum extent practicable, commercial items or nondevelopmental items as components of items supplied to the agency.

Small Business Set-Aside

The government's overarching small business policy is contained in 15 U.S.C. § 644(a), Commerce and Trade, Awards and Contracts:

(a) Determination

To effectuate the purposes of this chapter, small-business concerns within the meaning of this chapter shall receive any award or contract or any part thereof, and be awarded any contract for the sale of Government property, as to which it is determined by the Administration and the contracting procurement or disposal agency (1) to be in the interest of maintaining or mobilizing the Nation's full productive capacity, (2) to be in the interest of war or national defense programs, (3) to be in the interest of assuring that a fair proportion of the total purchases and contracts for property and services for the Government in each industry category are placed with small-business concerns, or (4) to be in the interest of assuring that a fair proportion of the total sales of Government property be made to small-business concerns

In particular, Paragraph (a)(4) is permissive and leaves to the contracting officer's judgment the extent to which small business "shall receive any award or contract...as to which it is determined...(4) to be in the interests of assuring that a fair proportion...be made to small business concerns."

In 15 U.S.C. § 644 (j), the statute specifically reserves procurements greater than the micro-purchase threshold (MPT) (currently \$10,000) and less than the SAT (currently \$250,000):

(j) Small business reservation

(1) Each contract for the purchase of goods and services that has an anticipated value greater than the micro-purchase threshold, but not greater than the simplified acquisition threshold shall be reserved exclusively for small business concerns unless the contracting officer is unable to obtain offers from two or more small business concerns that are competitive with market prices and are competitive with regard to the quality and delivery of the goods or services being purchased.

15 U.S.C. § 644 (j) is implemented in regulation in FAR Part 19, Small Business Programs, Subpart 19.502-2, Total Small Business Set-Asides:

(a) Before setting aside an acquisition under this paragraph, refer to 19.203(b). Each acquisition of supplies or services that has an anticipated dollar value exceeding \$3,500 (\$20,000 for acquisitions as described in 13.201(g)(1)), but not over \$150,000, (\$750,000 for acquisitions described in paragraph (1)(i) of the Simplified Acquisition Threshold definition at 2.101), is automatically reserved exclusively for small business concerns and shall be set aside for small business unless the contracting officer determines there is not a reasonable expectation of obtaining offers from two or more responsible small business concerns that are competitive in terms of market prices, quality, and delivery.

Setting aside the procurement is subject to there being “two or more responsible small business concerns that are competitive in terms of market prices, quality and delivery,”¹ typically referred to as the *Rule of Two*.

For procurements greater than the SAT, the statute is silent, but FAR 19.203 (c) asks contracting officers to *consider* using a small business program for such a procurement:

(c) Above the simplified acquisition threshold. For acquisitions of supplies or services that have an anticipated dollar value exceeding the simplified acquisition threshold definition at 2.101, the contracting officer shall first consider an acquisition for the small business socioeconomic contracting programs

Discussion

Both statute and regulation establish a preference for acquiring commercial products and commercial services, when available, to satisfy the government’s need. This clear preference is strongly supported by language at FAR 10.001(a)(3), which states if the government cannot find a commercial product or commercial service to meet its need, it must consider modifying commercial products and commercial services to meet its need, and if that is not sufficient, consider modifying the government’s requirement itself before considering procuring a noncommercial product or service.

¹ Total Small Business Set-Asides, FAR 19.502-2(a).

Statute is silent on any conflict between the preference for commercial products and services and small business set-asides. The statute does not specifically establish a preference for awards to small business, but it establishes the overarching policy of *assuring a fair proportion* of awards are made to small business. For awards between the MPT and the SAT, the statute reserves awards for small business subject to satisfying the Rule of Two. For awards greater than the SAT, reserving a procurement is left to the judgment of the contracting officer, again subject to the Rule of Two.

An important consideration is the logical order in which the commercial determination and Rule of Two determination take place in the acquisition process. It is logical to conclude that the contracting officer, using market research, would first determine *what* will be procured (including commercial and noncommercial) to satisfy the government's need. Once *what* is to be procured is established, it is logical to then address the question of *how* (interagency procurement, existing multiple-award contract, solicitation) and from *whom* (competitive, sole source, small business, large business). Although, the plain language of the FAR can reasonably be read to require contracting officers to determine if a commercial product or service could satisfy the government's requirements before deciding whether the procurement at issue should be set aside for small businesses, nothing in the FAR expressly states that commerciality determinations must come before any set-aside determinations.

When this issue was recently considered in *Analytical Graphics, Inc. v. United States*, the Court of Federal Claims (COFC) found that "there is not a clear order of precedence in the statutes or implementing regulations for how to approach a procurement which potentially involves both a small business set-aside analysis and a commercial availability analysis."²

At a minimum, the current ambiguity in the law will lead to inconsistencies across agencies, and, indeed, between individual contracting officers within agencies in terms of how acquisitions are planned. In a worst-case scenario, the Court's holding in *Analytical Graphics, Inc.* creates a roadmap for agencies to circumvent the statutory preference for commercial products and services. Specifically, following *Analytical Graphics, Inc.*, contracting officers have no obligation to determine whether the government's requirements can be satisfied by commercial products or services before deciding whether to set-aside the procurement for small businesses.

Practically speaking, if the government has a requirement that can be satisfied by a commercial product or service, and the commercial product or service that could satisfy the government's requirement is only available from large businesses, but two or more small businesses are available that could meet the government's requirement with a noncommercial product or service, then the government would be permitted to set-aside the procurement for small businesses and conduct the acquisition on a FAR Part 15 basis, thereby purchasing a developmental product when a commercial product or service already exists that meets the government's needs.

Clearly, this outcome is inconsistent with Congress's goals in FASA. Equally troubling however, absent language clarifying the priority of the commercial products and services preference over the Rule of Two, the government could avoid purchasing commercial products and services whenever it wants

² *Analytical Graphics, Inc. v. United States*, 135 F. Cl. 378, 412 (2017).

simply by identifying two or more small business offerors that can meet the government's requirements with a developmental solution.

Because the Rule of Two presupposes agencies have already developed their requirements, and because agencies are required by FASA and the FAR to consider the availability of commercial products and services at the requirements development stage, it follows that agencies must decide whether or not a procurement can be conducted on a FAR Part 12 basis before deciding whether the procurement can be set aside for small businesses. Implicit in the language of FAR 19.502-2 is that prospective small business offerors will be submitting an offer in response to a *defined requirement*. Without this assumption, the language "offers will be obtained" has no meaning. Agencies should be considering the commerciality of their requirement at the outset of the acquisition. Only after such requirements are defined can the agency rationally consider a set-aside determination based on whether there is a reasonable expectation that "offers will be obtained" from small businesses in response to that requirement.

Conclusions

Clarification is needed regarding existing law following the COFC's determination in *Analytical Graphics, Inc. v. United States* that "there is not a clear order of precedence" between the commercial item preference and the Rule of Two. The Court highlighted the need for legislators and regulators to address this issue, stating,

[g]iven the ambiguity in the two competing statutory goals and absent regulatory guidance regarding the choice as to which has precedence, the choice made by agency generally deserves deference ... The court should not be the entity to make that choice, and should intervene only when there is an obvious foul. Absent compelling statutory or regulatory guidance, which is missing here, the court generally defers to the agency's choice in a procurement in which the market research was carefully conducted. As the statutes and regulations do not point to a clear order for an agency to proceed between the small business set-aside determination and a commercial availability decision, the court does not read a requirement into the statutes and regulations that requires the agency or this court to first examine either.³

Implementation

Legislative Branch

- Modify 41 U.S.C. § 3307, Preference for Commercial Products and Services, to establish acquisition of commercial products, commercial services, and nondevelopmental items as having precedence over small-business set-asides.
- Modify 10 U.S.C. § 2377, Preference for Acquisition of Commercial Products and Commercial Services, to establish acquisition of commercial products, commercial services, and nondevelopmental items as having precedence over small-business set-asides.⁴

³ *Analytical Graphics, Inc. v. United States*, 135 F. Cl. 378, 412 (2017).

⁴ Note that similar language was proposed in Section 854 of the base version of the Senate FY 2018 NDAA.

Executive Branch

- Modify FAR 6.203, Set-Asides for Small Business Concerns, to establish acquisition of commercial products, commercial services, and nondevelopmental items as having precedence over small-business set-asides.
- Modify FAR 12.102, Applicability, to refer to commercial items as commercial products and services and to establish acquisition of commercial products, commercial services, and nondevelopmental items as having precedence over small-business set-asides.

Implications for Other Agencies

- The recommended statutory and FAR revisions will benefit all federal agencies subject to the FAR by clarifying the precedence for the preference for acquisitions of commercial products and services when considering a small business set-aside.