USING JOINT VENTURES TO CAPTURE FEDERAL GOVERNMENT CONTRACTING OPPORTUNITIES

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INTRODUCTION

In 2007, the U.S. Department of Defense declared “due in part to shrinking budgets and acquisition resources – contract consolidation is a trend that is likely to continue.” There can be little dispute that DOD’s prediction has played itself out and that contracts throughout the federal marketplace increasingly have been consolidated and become larger. The U.S. Department of Homeland Security’s (DHS) $9 billion information technology support services contract - Enterprise Acquisition Gateway for Leading Edge Solutions (EAGLE I) – marketed as a multiple award, indefinite-delivery, indefinite-quantity (IDIQ) contract exemplifies an emerging trend. Although 544 task orders were awarded under the EAGLE I contract between 2006 and 2011, at least three of the task orders nearly topped $1 billion, while at least sixteen more exceeded $100 million each. Subsequently, in July 2010, DHS followed up the Eagle I contract with its solicitation for the mammoth $22 billion EAGLE II IDIQ contract.

Congressional debate during the Summer of 2011 and ensuing federal legislation to curtail growing federal budget deficits will only increase pressure on federal government agencies to do the same or more “with less.” Therefore, contract consolidation will likely continue to accelerate and contracts will become larger and more complex, while opportunities for small businesses to single-handedly complete contract tasks or meet all contract requirements will diminish.

As the U.S. Department of Defense acknowledged, again back in 2007, the growth in size and complexity of government contracts has made teaming “a necessity” in the federal marketplace. Recent changes to regulations by the U.S. Small Business Administration on joint ventures reflect this new reality: small businesses must aggressively establish teaming partners to stay competitive.

This paper discusses the rules on joint ventures that enable businesses to form strategic teaming relationships to secure federal government contracts.
I. TEAMING ARRANGEMENTS

The Federal Acquisition Regulations (“FAR”), the rulebook federal government agencies must follow when they contract for goods and services, explicitly acknowledges and implicitly encourages teaming arrangements:

The government will recognize the integrity and validity of contractor team arrangements provided, the arrangements are identified and company relationships are fully disclosed in an offer or, for arrangements entered into after their submission of an offer, before the arrangement becomes effective. The government will not normally require or encourage the dissolution of contractor team arrangement.³

Indeed, FAR states that team arrangements may be desirable from both government and industry standpoint in order to enable the companies to (1) complement each other’s unique capabilities, and (2) offer the government the best combination of performance, cost, and delivery for the system or product being acquired. Further, FAR acknowledges that team arrangements may be particularly appropriate in complex research and development procurements.⁴

The federal contracting rules recognize two kinds of “contractor team arrangements.”⁵ The first kind of team arrangement occurs when companies align horizontally, either as partnerships or joint ventures, to act as the prime contractor.⁶ The second kind of team arrangement occurs when companies align vertically to divide work along a prime contractor-subcontractor chain.

II. ADVANTAGES OF JOINT VENTURES

The federal acquisition rules have a very specific notion of what constitutes a “joint venture” for teaming purposes. Specifically, a joint venture is defined as a business association that is intended to last for a limited duration and for specific purpose:

A joint venture for size determination purposes is an association of persons or concerns with interests in any degree or proportion by way of contract, express or implied, consorting to engage in and carry out a single specific business venture for joint profit, for which purpose they combine their efforts, property, money, skill, or knowledge, but not on a continuing or permanent basis for conducting business generally.⁷

Teaming arrangements, whether they are joint ventures or prime-subcontractor arrangements, offer tangible benefits to government contractors. They enable companies to collectively fulfill contract requirements that they could not fulfill separately. In addition,
government agencies routinely factor a bidder’s “past performance” on the same or similar government contracts, in their evaluation of a proposal, and teaming arrangements enable parties to overcome past performance gaps of a particular business.

Although the most prevalent teaming arrangement in federal government contracting is the prime-subcontractor arrangement, joint ventures enable contractors to achieve additional government contracting objectives. Joint venture arrangements:

- Enable companies to spread risks of prime-contracting
- Permit companies to leverage their combined capital
- Allow all parties to have a voice and control over how the contract is performed and managed
- Enable parties to share in profits of the entire project
- Enable parties to develop direct relationships with the government agency contracting officials
- Enable small businesses to offer bonding capacity of larger companies

Typically, only a prime contractor has privity of contract. That is, the prime contractor – and not any of the subcontractors – is a party to the contract with the government agency and only the prime contractor has an enforceable right against the government for the benefits under the government contract. A subcontractor, in turn, typically only has privity of contract under a subcontracting agreement with the prime contractor. Therefore, when a subcontractor has a dispute with a prime contractor over payment for services, the subcontractor usually cannot seek payment directly from the federal government. Joint venture arrangements, however, enable all teaming partners to have “privity” of contract with the contracting government agency.

In addition, as described further below, federal regulations enable joint venture partners to bid for contracts that collectively or separately they might not otherwise be eligible to compete for.

A. JOINT VENTURES MAY COMPETE FOR SMALL BUSINESSES CONTRACTS

Government contracting officers routinely establish small business requirements, and size standards for what constitutes a small business, for the government contracts they solicit. These small business size standards are specific for each industry (typically as set forth in the North American Industry Classification System or “NAICS”) and establish ceilings on revenue and number employees for a business to be considered a “small business” for purposes of the procurement. Under certain circumstances, joint venture partners may enjoy all the benefits of the joint venture arrangement, and still compete for contracts that are “set aside” for small businesses or that have small business participation requirements, even though the combined size of the joint venture parties exceeds the small business size standard set by a government agency.
In fact, changes in February 2011 to regulations issued by the U.S. Small Business Administration (SBA), which is charged with regulating and enforcing the rules on small business participation in federal government contracting, have increased opportunities for joint ventures that may collectively exceed the small business size standards for government contracts.

1. General Rule on Affiliation of Joint Venture Partners

It should be noted that as a general rule, joint venture partners are deemed to be “affiliated” for purposes of small business size standards that may be set for a federal government contract. That is, as affiliates, the revenues and number of employees of the joint venture partners are required to be combined in order to determine if the joint venture should be considered a “small business” for purposes of any small business participation requirements of a federal contract.

2. Three Exceptions to Rule on Affiliation

There are three exceptions, however, to the requirement that joint ventures should be deemed affiliated and their revenues and number of employees combined. Importantly, the 2011 changes to the SBA regulations expressly allow a joint venture to be excluded from affiliation requirements under these exceptions whether or not the joint venture is formed as a separate legal entity (e.g. an LLC), and whether or not any separate legal entity is populated (e.g., has its own employees).

a. Small Business Joint Ventures

One exception applies when each partner qualifies separately as a small business under the size standard that is set for the government contract. Under this exception, the contract must either qualify as a “bundled” contract, or the contract dollar value must be greater than $10 million (if the size standard is based on the number of employees) or greater than half the size standard (if the size standard is based on revenue). A “bundled” contract occurs when two or more requirements that were previously provided under separate smaller contracts are combined into a single contract that is “likely to be unsuitable for award to a small business concern” due to (1) the diversity, size or specialized nature of the elements of the work required, (2) the aggregate dollar value of the anticipated award, (3) the geographical dispersion of the contract performance sites; or (4) a combination of these factors.

This exception to affiliation enables small businesses to compete collectively for contracts set aside for a small business that they would otherwise not be able to perform on their own separately because of the size or complexity of the contract.
b. 8(a) Joint Ventures

Another exception to the general affiliation rule applies to joint ventures that compete for a contract that is set aside for businesses that participate in the SBA’s 8(a) Business Development Program (8(a) BD Program). The 8(a) BD Program provides business development services for small businesses that are owned and controlled at least 51% by socially and economically disadvantaged individuals.

Under the exception for 8(a) Joint Ventures, all of the members of the joint venture must each satisfy the small business size standard for the contract, with at least one business being a participant in the 8(a) BD Program. In addition, the size of at least one of the 8(a) businesses must be less than half of the small business size standard set for the contract. Also, the dollar amount of the government contract must exceed either half the size standard (if the size standard is based on revenue) or $10 million (if the size standard is based on number of employees). An important aspect of this exception is that it enables small businesses that do not participate in the 8(a) BD Program to nevertheless compete for 8(a) set aside contracts.

c. Mentor – Protégé Joint Ventures

Another exception to affiliation applies to joint ventures that consist of companies approved by the SBA to be mentors and protégé’s under the SBA’s Mentor Protégé Program. The SBA’s Mentor-Protégé Program, offered under the 8(a) BD Program, enables 8(a) participants to obtain technical and management assistance, certain financial assistance, and prime contracting opportunities from approved “mentors,” which themselves do not have to be small businesses or owned by socially or economically disadvantaged individuals.

For the Mentor-Protégé Joint Venture exception to apply, the 8(a) participant/protégé must qualify as a small business under the small business size standard set for the procurement, and the contract awarded must not exceed the limit on sole source 8(a) awards. The mentor, on the other hand, can be a large business. Thus, the Mentor-Protégé Joint Venture exception presents a particularly rare opportunity for a large business to compete for a federal government contract that is set aside for small businesses.

Another important aspect of Mentor-Protégé Joint Venture exception to affiliation, as amended by the SBA regulation, is that it now also applies when the joint venture performs as a subcontractor, and not just as a prime contractor.

3. Additional Conditions When Joint Ventures Are Awarded 8(a) Contracts

The amended SBA regulations impose additional requirements when a joint venture is awarded an 8(a) set-aside contract (either as a Mentor-Protégé Joint Venture or an 8(a) Joint Venture).
a. Joint Venture Agreements Must Meet Certain Requirements

A joint venture agreement to perform an 8(a) set aside contract must set forth the purpose of the joint venture and must be approved by the SBA before the contract is awarded. If the joint venture is a separate legal entity, the joint venture agreement must also state that the 8(a) partner owns at least 51% of the joint venture and that the 8(a) partner will receive profits commensurate with its ownership interest in the joint venture. If the joint venture is not a separate legal entity, the joint venture agreement must state that the 8(a) participant will receive profits commensurate with the work performed by the 8(a) partner. The joint venture agreement must also indicate that the 8(a) participant controls the accounting and administrative records, and retains final original records upon completion of the contract.

For an unpopulated joint venture or joint venture populated only with administrative personnel, a joint venture agreement also must designate an employee of the 8(a) managing partner as the project manager responsible for performance of the contract. For a joint venture populated with individuals intended to perform the contract, the joint venture must demonstrate that performance of the contract is controlled by the 8(a) managing partner.

b. The Joint Venture Must Meet Work Sharing Requirements

For unpopulated joint ventures or joint ventures populated only with administrative personnel, the 8(a) partner(s) must perform at least 40% of the work, and the work must be more than administrative or ministerial. For populated joint ventures, each 8(a) partner must demonstrate what it will gain from performance and how the performance will assist in its business development.  

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c. The Joint Venture Must Meet Subcontracting Conditions

In a populated joint venture, a non-8(a) partner and its affiliates may not act as subcontractors to the joint venture or to any subcontractors. Consequently, if the non-8(a) partner wishes to do more work under the contract, the work must be done through the joint venture, which may require additional work to be assigned to the 8(a) partner so that the 8(a) partner can still meet the 40% work share requirement. In an unpopulated joint venture or venture populated only with administrative personnel, the joint venture may subcontract work to the non-8(a) partner as long as it also subcontracts work to the 8(a) partner to meet the 40% work share requirement.  

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As a consequence of the additional requirements, teaming partners that wish to work under 8(a) contracts will have to carefully plan in advance how they wish to structure the joint venture because those decisions will necessarily impact how work is shared and profits allocated. As stated, if the joint venture is a separate legal entity, the 8(a) partner must receive profits commensurate with its ownership interest (at least 51%), but if the joint venture is not a separate legal entity, the 8(a) participant must receive profits commensurate with its share of work (at least 40%).
4. Limitations on Contracts Awarded To Joint Ventures

Another important change to the affiliation rules as a result of 2011 changes to the SBA regulations has increased the number of bids that joint ventures can submit. Before the 2011 changes, joint ventures were limited to submitting three contract offers over a two-year period. Small businesses with combined sizes that exceeded size standards that wished to take advantage of one of the three affiliation exceptions, therefore, were forced to pick and choose carefully the small business contracts they believed they could successfully bid for as a joint venture. The 2011 SBA amendments to the regulations liberalized the definition of joint venture for purposes of the affiliation rules by eliminating the restriction on number of bids a joint venture can submit. Instead, the SBA regulation effectively limits the number of contracts that a joint venture can be awarded to three over a two-year period:

A joint venture is an association of individuals and/or concerns with interests in any degree or proportion by way of contract, express or implied, consorting to engage in and carry out no more than three specific or limited-purpose business ventures for joint profit over a two year period, for which purpose they combine their efforts, property, money, skill, or knowledge, but not on a continuing or permanent basis for conducting business generally.¹⁶

The amended SBA regulation make clear that the time for counting the three awards is as of the date the joint venture submits its proposal. Consequently, a joint venture with two contract awards can submit two bids for contracts, both of which can be awarded to the joint venture, since at the time the bids for each contract were offered, the joint venture only had two contract awards. In addition, the amended SBA regulation allows the same parties to a joint venture that has been awarded three contracts to form a second (and then third . . .) additional joint venture, which in turn is potentially eligible to perform under three new contracts. The regulations, however, acknowledge that at some point a long-lasting relationship will lead to a finding that the joint venture partners are affiliated.¹⁷

B. JOINT VENTURES MAY COMPETE AS SMALL DISADVANTAGED BUSINESSES

Under certain conditions, a joint venture may able to enjoy benefits typically enjoyed by businesses certified as small disadvantaged businesses (SDB’s) by the SBA, such as price evaluations, evaluation factors and subfactors, and monetary subcontracting incentives. To qualify as an SDB business for these purposes, at least one of the joint venture partners must be SDB-certified by the SBA or must have submitted an application for certification and not received a negative determination. In addition, the SDB partner must be the manager of the joint venture and the employee of the SDB must be the project manager responsible for contract performance. Lastly, the joint venture must perform any work required of SDB offerors and the SDB partner must perform a significant portion of the contract.¹⁸
However, unless the joint venture satisfies one of the three exceptions to affiliation that applies for small business contracts (described in part II.A.2, above – i.e., it is a Small Business Joint Venture, Mentor-Protégé Joint Venture, or 8(a) Joint Venture) the parties to the joint venture will be deemed affiliated and their revenues and employee numbers will be combined for purposes of the size standards set for the contract.

C. JOINT VENTURES MAY COMPETE FOR HUBZone CONTRACTS

A joint venture that comprises solely of businesses that participate in the SBA’s Historically Underutilized Business Zones (HUBZone) program may compete for a contract set aside for a HUBZone business, as long as each joint-venture partner is small under the size standard for the contract. In addition, the HUBZone businesses collectively may exceed the size standard for the contract and still compete for the contract as long as the dollar amount of the contract exceeds either half the size standard (if the size standard is based on revenue), or $10 million (if the size standard is based on number of employees). If the contract does not exceed these amounts, the HUBZone joint venture may compete for the HUBZone contract only as long as the combined size of the joint venture does not exceed the size standard for the contract.19

D. JOINT VENTURES MAY COMPETE FOR SDVOSB CONTRACTS

Joint ventures may also compete for contracts set aside for businesses that participate in the SBA’s Service-Disabled Veteran-Owned Small Business Concern Program. The joint venture must include at least one service-disabled veteran-owned small business concern (SDVOSB) and all joint venture partners must qualify as a small business under the size standards for the contract. In addition, the dollar amount of the contract must exceed either half the size standard (if the size standard is based on revenue) or $10 million (if the size standard is based on number of employees). If a sole source contract or competitive procurement does not exceed these contract sizes, the SDVOSB joint venture will only qualify as a small business if the combined revenue or number of employees meets the size standard for the contract. In addition, the joint venture agreement must designate the SDVOSB as the managing venture and an employee of the managing venture must be designated as the project manager responsible for the performance of the contract. The joint venture must also state that not less than 51% of the net profits of the joint venture will be distributed to the SDVOSB.20

E. JOINT VENTURES MAY COMPETE FOR WOSB & EDWOSB CONTRACTS

In October 2010, the SBA published its long-awaited regulations designed to help the federal government meet its goal of awarding 5% of all contracting dollars to women-owned small businesses (WOSB’s). The SBA regulation authorized agencies to set aside contracts for
WOSB’s and a subcategory - economically disadvantaged women-owned small businesses (EDWOSB’s) - in 83 industries.

Under the SBA regulation for WOSB’s, a joint venture that comprises of at least one designated WOSB or EDWOSB may compete for a WOSB or EDWOSB contract if the parties enter into a written joint venture agreement stating: (1) the purpose of the joint venture, (2) that the EDWOSB or WOSB is the managing partner and an employee of the managing partner is the project manager responsible for contract performance, (3) that not less than 51% of the net profits will be distributed to the EDWOSB or WOSB, (4) the responsibilities of the parties regarding performance, sources of labor, and negotiation of the contract, and (5) that the final original records will be retained by the managing partner upon completion of the contract. In addition, a copy of the joint venture agreement must be submitted to the contract officer, and the procurement contract must be executed in the name of the EDWOSB, WOSB or the joint venture.

The joint venture partners, however, will be deemed affiliates, and consequently, revenues and number of employees will be combined for purposes of the size standards set for the contract, unless one of the three small business exceptions to affiliation (described in part II.A.2, above) applies.

III. OTHER CONSIDERATIONS

The federal regulations on joint ventures as amended in 2010 and 2011 pave the way for additional procurement opportunities for companies that seek to maximize their selling power in an increasingly competitive federal marketplace.

As with other teaming arrangements, potential joint venture partners should carefully consider bonding capacity, financial resources, past performance, and technical proficiency and expertise of their potential partners. However, as a practical matter, the nature of a government contracting joint venture arrangement – with highly specific shared management, work sharing, risk sharing, and profit sharing requirements – may require parties to cooperate and collaborate more effectively than they might otherwise under a prime-subcontractor arrangement, or risk a failed endeavor. Consequently, other factors such as company culture, and management strength and style may take on greater significance and potentially can be sources of conflict. The most successful joint ventures, therefore, will have a shared mission that is meticulously aligned with the goals of each of the joint venture partners, as well as the requirements of the government contracts that they compete for. Carefully drafted joint venture agreements, along with cohesive contract management strategies and tools, and sufficient administrative support will go a long way towards the successful attainment of the joint venture parties’ objectives.
ENDNOTES


2 Office of Procurement Operations Director Soraya Correa purportedly stated the total ceiling for the Unrestricted and Small Business tracks will be $22 billion. Other federal agencies have followed the same approach for contracting out IT support services, such as the United States Department of Justice, which in March 2011 awarded its $1.1 billion ITSS-4 contract under an IDIQ, and the U.S. Food and Drug Administration, which in March 2009 awarded its $2 billion ELMS contract under an IDIQ.

3 FAR 9.603.

4 FAR 9.602.

5 FAR 9.601.

6 FAR 9.601(1).

7 FAR 19.101(7)(i).

8 13 CFR 121.103(h)(2).

9 13 CFR 121.103(a)(6).

10 13 CFR 124.513(c).

11 13 CFR 121.103(h)(3)(i).

12 13 CFR 121.103(h)(3)(i).

13 FAR 2.101.

14 13 CFR 124.513.

15 13 CFR 124.513.

16 13 CFR 121.103(h) (emphasis added).

17 13 CFR 121.103(h).

18 13 CFR 124.1002(f).

19 13 CFR 126.616.

20 13 CFR 125.15.

21 13 CFR 127.506.

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