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Column: The DOJ's enforcement of small business regulations

by Tony Franco, partner, PilieroMazza PLLC

With the Small Business Administration's new limitations on subcontracting rules going into effect on June 30, and a new mentor-protégé program for all small businesses about to be implemented by the SBA, contractors need to understand how the new regulations work.

Many contractors, small and large, underestimate the government's willingness to enforce compliance with the performance of work rules.

Unbeknownst to many government contractors, the Department of Justice (DOJ) brings actions—civil and criminal—against firms for violating the performance of work rules in either joint venture or prime/subcontract arrangements.

Past False Claims Act cases

Although the new subcontracting rules are not yet in effect, there are a number of cases that show that the DOJ is intent on enforcing compliance with the regulations that have been on the books.

In 2012, for example, the United States government brought an action under the civil False Claims Act against R.J. Zavoral & Sons, Inc., its officers and employees.

The government alleged that the company, which was not a participant in the SBA's 8(a) program, had formed a joint venture with an 8(a) firm, and thereafter the defendants made misrepresentations regarding the joint venture's compliance with SBA regulations during the course of contract performance.

The alleged misrepresentations included false statements about the amount of work the 8(a) firm was performing under a contract awarded to the joint venture.

The joint venture agreement, which had to be reviewed and approved by the SBA before it was eligible to bid on and receive the contract, provided that the 8(a) company would perform a certain amount of work, but the 8(a) company did not do so.

The company and its principals agreed to pay $1.85 million to the government to settle the case.

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Fraud case

In a more recent case, a retired U.S. Army colonel who worked for a non-8(a) firm was convicted of fraud in connection with a scheme to obtain contracts designated for 8(a) firms.

The 8(a) and non-8(a) firms had entered into a joint venture under which the 8(a) firm had to perform at least 40% of the work on any 8(a) set-aside contracts that were awarded to the joint venture.

The U.S. Court of Appeals for the Fifth Circuit held that a jury could find that two contracts awarded to the joint venture made an implied representation that the joint venture would comply with the 8(a) regulations, including the performance of work requirement.

The U.S. Court of Appeals for the Fifth Circuit upheld the colonel's conviction because he had negotiated and signed the contracts with the implied representations.

New Mentor-Protege program

The new mentor-protégé program is going to offer incentives for many firms to form joint ventures, which are going to be subject to fairly strict regulations.

The performance of work requirements will be among the most significant rules the participants will have to follow to ensure that the protégé benefits from the mentor-protégé relationship.

With the DOJ aggressively pursuing firms that do not comply with the rules, participants in the program need to know the risk of non-compliance. These risks extend to both partners in the joint venture arrangement.

Small businesses also at risk

The cases discussed above illustrate how non-8(a) partners to joint ventures have been subject to prosecution or civil actions. This does not mean, however, that the firms that were intended to benefit from these contracts--be they 8(a) or WOSB (Women-Owned Small Business) or SDVOSB (Service-Disabled Veteran-Owned Small Business)--are immune from liability.

If the small business, 8(a) or other similar firm, submits invoices for payments as a prime contractor or lead joint venturer when it has not been performing as required by the regulations, the DOJ may take the position that it, too, is liable under the False Claims Act for implying that it has certified compliance with the performance of work rules.

Significant penalties

In short, companies and individuals who do not comply with the SBA's regulations can face significant penalties, including suspension, debarment and imprisonment.

And, even if a company or individual is never actually prosecuted or sued, just responding to an investigation by the SBA or DOJ can be extremely expensive and time-consuming. Knowing and following the rules is critical given the DOJ's enforcement efforts in the past and most likely in the future.

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