



**Testimony of James Hoffman, P.E
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Introduction

Chairman Chabot, Ranking Member Velázquez, and members of the committee,

The American Council of Engineering Companies (ACEC) appreciates the opportunity to testify before you today about the issues surrounding *Contracting and the Industrial Base* and specifically about the unique considerations within engineering services and construction more broadly. ACEC believes that small businesses can flourish in the federal market, but there must be continued oversight by this and other committees to reduce barriers to market entry. There must be a focus on improving the marketplace for design and construction services by eliminating wasteful spending by both the federal government and contract participants during the procurement process. ACEC will address issues that are present in federal design-build procurement, the potential issues with the implementation of a new court decision in the Nonmanufacturer Rule, the use of reverse-auctions, federal agency use of joint venture and teaming qualifications and surety improvements.

My name is James Hoffman and I am President of Summer Consultants, a consulting mechanical, electrical, and plumbing engineering firm located in McLean, Virginia. Summer Consultants is a Small Business with 30 employees. We are committed to providing our clients sound engineering designs for various sized projects. Our practice focuses on the federal market and we have worked on many federal projects in the past 50 years.

My firm is an active member of ACEC – the voice of America’s engineering industry. ACEC’s over 5,000 member firms employ more than 380,000 engineers, architects, land surveyors, and other professionals, responsible for more than \$500 billion of private and public works annually. Almost 85% of these firms are small businesses. Our industry has significant impact on the performance and costs of our nation’s infrastructure and facilities.

We are at a critical juncture in our nation’s history as the risk to the public is growing at an alarming rate, as there has been ongoing neglect of the nation’s infrastructure. At the same time, we are coming out of the largest economic crisis that affected all professional engineering firms. The construction industry, which bore the brunt of the recession, is finally coming back to fiscal health. Procurement improvements that facilitate greater efficiency for both the industry and the government will help these entities create better public infrastructure while increasing good paying jobs.

Design-Build Improvement

Design-build is a method of construction where engineers team with other industry professionals on proposed work. It requires the design team, comprised of engineers and architects, to develop detailed drawings and specifications for the contractor so that construction suppliers can submit

detailed prices for the final proposal. This method has become popular in recent years and the federal government has moved to expand its use in construction.¹

There are two forms of design-build procurement: two-step and one-step. Two-step design-build requires that teams submit relatively inexpensive qualifications packages to the contracting officer in the first round. The contracting officer reviews the qualifications and notifies the teams if they are selected for the next phase. In the second round, the design team develops expensive detailed and extensive plans for the contractor to use in their bidding. The design group develops these plans, generally without any reimbursement by the federal government or other participants, resulting in firms risking funds to participate in the project.²

It is the industry standard for three to five finalists to be in the second round. However, in recent years, industry has reported often more than 10 finalists in that round. The current civilian statute states that the federal contracting officer should follow the industry standard, but the officer, at her or his own discretion, may increase the number of finalists when it is “in the Federal Government's interest and is consistent with the purposes and objectives of the two-phase selection process.”³ This exception causes issues for both the industry and for the contracting officer. Industry is risking greater exposure as more firms; small, medium, and large, are spending valuable resources developing expensive plans and specifications that have a lower chance for a successful bid. The contracting officer must review each of the plans and be prepared to give feedback to each team that does not win the project. With the increase in finalists, the government spends more time on proposal review, and introduces greater opportunity for errors or underbidding which impacts the project later. This issue has driven many, including small businesses, to stay out of the federal market. This makes the market less competitive and drives down industry participation.

One-step design-build creates an even more precarious environment for the industry as the qualifications step is eliminated. ACEC is staunchly opposed to this form of procurement as it eliminates the qualifications process, increases cost for all participants, and reduces market participation for engineers. One-step design-build allows the owner to solicit complete proposals from the construction market without a review of the team's past performance and qualifications. This mechanism forces teams to compete in large pools without any focus on technical capability, quality, or savings within the design. Due to this type of unqualified competition, many firms cannot justify the expenditures to compete against an unknown pool of applicants. This selection forces out small firms as they cannot spend valuable marketing dollars on projects where there are too many competitors—many of which that may not have the qualifications for the project. It is an inefficient process for the federal government as it asks contracting officers to review multitudes of proposals without the framework of qualifications to focus the evaluation. The U.S. Corps of Engineers has taken steps recently to limit one-step design-build,

¹ Press Release, H. Comm. on Small Bus, Graves, Hanna Introduce Bipartisan Legislation to Benefit Small Construction Contractors. (July 19, 2013) (on file with author).

² *Building America: Challenges for Small Construction Contractors: Hearing Before the Subcomm. on Contracting & Workforce of the H. Comm. on Small Bus 113th Cong. 113-109 (2013)*. (statement of Helene Combs Dreiling, President, the American Institute of Architects).

³ 41 U.S.C. 3309(d).

requiring high level, advanced approval for any projects over \$750,000.⁴ When the government's largest construction agency implements limits on the process, other agencies should follow their precedent.

Chairman Hanna held a hearing on this issue on May 23, 2013 and the House Oversight and Government Reform Subcommittee on Federal Workforce, US Postal Service and Census, also held a hearing on this issue on December 3, 2013. Former Small Business Committee Chairman Graves sponsored H.R. 2750, the Design-Build Jobs and Efficiency Act of 2013, which was amended into the National Defense Authorization Act (NDAA) of 2015. The NDAA implemented a limitation on military design-build procurements over \$4 million whereby the contracting officer must ask for permission to expand the finalist pool in a two-phase procurement beyond five finalists. However, the limitations including the prohibition on one-step design-build, reporting on any exceptions to the five finalists, or any limitations for either single or two-step design build were not extended to the federal civilian market. The Congressional Budget Office (CBO) found that H.R. 2750 “would not have a significant net effect on the federal budget”⁵ in their analysis of the bill. CBO determined that it would help to “analyze fewer construction bids”⁶ which would balance any additional costs that may be involved in the bill. We ask the Committee to continue to pursue the proposed efficiencies found in H.R. 2750, which will help small businesses compete in the federal market, while also harmonizing the language between military and civilian design-build construction.

Proposed Nonmanufacturer Rule Changes

The updated interpretation of the Nonmanufacturer Rule (NMR) poses a challenge for the construction industry as it is a service industry that typically did not have to address this rule in the past. The NMR exists to ensure that when competition for a contract for goods is restricted to small businesses that the good ultimately purchased was from a small business. Otherwise, the government risks restricting competition only to have the awardee provide a product it has simply passed along from a large manufacturer or international contractor. In a recent Court of Federal Claims ruling on Rotech Healthcare, Inc. v. United States⁷, the Court changed the common understanding of the rule. The Court found that the Small Business Act references “any procurement for goods” and that the SBA must apply that interpretation broadly across both services and commodities⁸.

ACEC has grave concerns with this interpretation. Currently, over 85 percent of all construction dollars are subcontracted to third parties.⁹ The Court's interpretation would require that any firm who is a prime contractor be responsible for their subcontractors' use of small business products. The paperwork burden on this concept is staggering. An example of the unintended result of this rule could require that engineering firms use paper made by small businesses to print out their correspondence for a federal construction job. Many businesses do not know who made their

⁴James Dalton, PES, Limitations on the Use of One-Step Selection Procedures for Design-Build, Directive No. 2012-23 (2012) (on file with the author).

⁵MATTHEW PICKFORD, CONG. BUDGET OFFICE, H.R. 2750 DESIGN-BUILD EFFICIENCY AND JOBS ACT OF 2014 (2014), available at <http://www.cbo.gov/sites/default/files/hr2750.pdf>.

⁶ Id.

⁷ CASE NO. 14-502C (SEPTEMBER 19, 2014)

⁸ Id. at 6-8.

⁹ 13 C.F.R. § 125.6.

paper nor do firm owners concern themselves with the small business aspect of its production. The interpretation could require that the ink and any other materials, like specialized seismic machinery, that are not exempted through the regulations, must be obtained through a small business. The result of this ruling cannot be implemented without great cost to the businesses who work on and the taxpayers who fund federal construction projects.

Second, in many instances, specific items may be manufactured in a foreign country. If an engineer specifies a part that has a foreign origin, or is made by a large manufacturer, it is most often because of necessary performance specifications that are essential to the project's long-term success. This ruling would have the engineer concerned with minutiae that is not relevant the responsibilities outlined above. This decision will result in the inefficient and wasteful use of taxpayer funds. ACEC asks the Committee to work with the SBA on language to make sure that construction services and products continue to be excluded from the NMR.

Reverse Actions

Reverse auctions are on-line sales where the bidders compete for work by lowering their price against other competitors in a specified time.¹⁰ Typically, agencies pay a variable fee, "which is no more than 3 percent of the winning bid"¹¹ to the reverse action contractor. Reverse auctions force design professionals to bid on price, which is strictly prohibited by the Brooks Act and by many state professional licensing standards. It also fails to encourage any participant in the design and construction industry to focus on providing innovative and strategic solutions to the nation's infrastructure. It forces the competitors to focus solely on lowering their price. This often leads to errors or underbidding during the auction, without the ability to verify costs with subcontractors, who are often small businesses. The potential damage to a construction project and firms involved can be significant as project costs may increase beyond the bid or businesses could go out of business due to a mistake in the frenzy of bidding. Also of consideration is the fact that over "a third of the...2012 reverse auctions...had no interactive bidding"¹² which means that no other vendor drove down the price. In short, the competition was sole-sourced out to a single bidder.

Reverse actions have been used by the federal government in the past with commodities, with a noted lack of success in construction. The U.S. Corps of Engineers conducted a year-long study whereby they found that reverse auctions "offered not even marginal edge in savings over the sealed bid process for construction service projects"¹³. The Corps found that sealed bids for construction, typically the domain of contractors, was a better method than reverse auctions.¹⁴ Moreover, former OFPP Administrator Mr. Joseph Jordan, who is the current FedBid CEO stated, "An agency might want to use FedBid to find a contractor to paint a wall, he said, but not

¹⁰ U.S. GOV'T ACCOUNTABILITY OFFICE, GAO-14-108 REVERSE ACTIONS—GUIDANCE IS NEEDED TO MAXIMIZE COMPETITION AND ACHIEVE COST SAVINGS 6 (2004).

¹¹ *Id.* at 19.

¹² *Id.* at 26.

¹³ USACE, FINAL REPORT REGARDING THE USACE PILOT PROGRAM ON REVERSE AUCTIONING 34-37 (2004).

¹⁴ ACEC advocates for qualifications based selection (QBS) in the selection of the architect and engineer, but that is not the subject of this hearing.

to construct an office building.”¹⁵ It is telling that both the Corps and the third-party vendor for reverse auctions do not advocate their use in construction.

H.R. 2751, the Commonsense Construction Contracting Act of 2013, introduced by Rep. Richard Hanna (R-NY), sought to restrict the use of so-called reverse auctions as a means of procuring construction and design-related services. Like H.R. 2750, it was incorporated into the NDAA, but the prohibition was limited to the use of reverse auctions in design-build procurements. At this time, there are no programs that can be found by the industry that used this procurement method. While federal procurement law already prohibits the use of reverse auctions for engineering activities, we view the full legislation as necessary to protect firms of all sizes in our industry when they provide services in support of construction efforts. ACEC asks the committee to reintroduce H.R. 2751, to build stronger prohibitions against the use of this commodities based program for construction services.

Joint Venture Rules

Joint ventures and teams are important to construction and small businesses in the federal market.¹⁶ Teams are important to the design-build process as each discipline works together to compete on construction projects. Joint ventures allow for organizations new to federal procurement to work with experienced partners to gain entry to the market. It is important for teams to add or change firms to enhance their qualifications, to offer the best services for a particular project in the pre-competition phase. These practices allow the federal government to obtain innovative private sector talent while also increasing capable competition on federal projects.

Current law states that small businesses may “submit an offer that provides for the use of a particular team of subcontractors for the performance of the contract”¹⁷ and that requires the contract be evaluated, “in the same manner as other offers, with due consideration for the capabilities of all proposed subcontractors.”¹⁸ There are recent reports that some agencies are requiring joint ventures or teams to present joint past performance in their qualification. This practice demonstrates that some contracting officers do not understand the rationale and benefit of teaming. Some agencies require that “an [o]fferor must have proven experience and performance as an existing CTA (Contractor Team Arrangement) in the form of a Partnership or Joint Venture in accordance with the proposal submission requirements”¹⁹, or that past performance may only be considered if it is that of “a parent company, affiliate, division, and/or subsidiary.”²⁰ Under present statute, the contracting officer must look at the qualifications of the individual organizations comprising a team rather than the past performance of the group as a whole. Requiring that the team have common past performance reviews discourages the use of new teams, new partners, and the inclusion of new small businesses in the federal market.

¹⁵ Danielle Ivory, ‘Reverse Actions’ Draw Scrutiny’, N.Y. Times, April 6, 2014 at B1.

¹⁶ Joint ventures and teams are used interchangeably in this submission. Joint ventures are contractual relationships between entities while teams are groups of professionals working together towards a single project. They are very similar in nature, but differ in the legal sense.

¹⁷ Id.

¹⁸ Id. at § 15(e)(4), 15 U.S.C. § 644(e)(4).

¹⁹ GSA OASIS REQUEST FOR PROPOSAL (2013) available at https://www.fbo.gov/?s=opportunity&mode=form&tab=core&id=df05de3d9c9caf1e7943d278094eebf1&_cview=1.

²⁰ HCATS RFI APPENDIX 3 - DRAFT RFP SECTION L (2015) (on file with author).

ACEC strongly encourages the Committee to amend the Small Business Act to protect the development of joint ventures and teams. Federal agencies are losing their opportunity for innovation and small business participation when contracting rules are not followed by federal agencies.

Surety Improvements

A surety is a third party product that guarantees payment if one party defaults on the agreement. In federal construction, there are two key bonds—payment bonds and performance bonds. The Miller Act requires that the contractor must provide a surety for payment and performance bonds on contracts greater than \$150,000. This provides performance protection to the federal government that the taxpayer will not be damaged if the contractor fails to complete a project, while also guaranteeing payment to subcontractors if the contractor defaults. H.R. 776, the Security in Bonding Act of 2013, was introduced by Chairman Hanna to address the issues of bonding availability for small businesses and problems with individual surety guarantees. The bill increases the guarantee rate for the Preferred Surety Bond Program, which will help more small business obtain a bond at a reasonable rate, and requires verifiable collateral for the issuance of surety bonds. While ACEC members typically do not obtain surety bonds, with the exception of some of our larger members who are also construction contractors, we recognize the importance of this product for the taxpayer and the subcontractors. ACEC asks the Committee to reintroduce H.R. 776 in this Congress.

Conclusions and Recommendations

The engineering services industry is unique in how firms are established, perform work, selected for the project, and work with each other. Most firms in the industry are small, specialized, and have a business plan to remain that way to assure performance and reputation. These factors result in the need for special considerations when trying to ensure appropriate small business participation in federal procurements.

We ask that the committee consider the following actions for the 114th Congress:

- Reintroduce H.R. 2750 and enact it into law.
- Work with the SBA on appropriate language to limit the scope of the NMR on service industries.
- Reintroduce H.R. 2751 and enact it into law.
- Strengthen the Joint Venture and teaming past performance rules.
- Reintroduce H.R. 776 and enact it into law.

ACEC and I thank the Committee for the privilege and opportunity to address engineering and construction industry issues with current federal procurement and I am pleased to answer any questions.