The Rule of Two Wrinkle

The SBA is preparing to resolve uncertainty as to whether the Rule of Two is mandatory for multiple-award contracts.

BY STEPHEN BACON

The so-called "Rule of Two" requires federal agencies to set aside procurements for small businesses where there is a reasonable expectation that at least two small businesses will submit offers at fair market prices. The Rule of Two exists to ensure that small businesses receive a fair proportion of contracts awarded by federal agencies.

The Government Accountability Office (GAO) has ruled that the Rule of Two is not mandatory when an agency decides to conduct a task or delivery order procurement under a multiple-award contract (MAC).[1] However, at least one judge on the Court of Federal Claims (COFC) has reached the opposite conclusion.[2]

The COFC held that agencies cannot avoid the Rule of Two by deciding to use a MAC with large business awardees. In the COFC's view, agencies must conduct the Rule of Two analysis *before* they decide to use the MAC for the acquisition.

The Small Business Administration (SBA) agrees with the COFC's decision and is in the process of preparing changes to the Rule of Two that would align with the COFC's interpretation.

Both small and large contractors should understand the split between GAO and the COFC and SBA's planned rulemaking because the result could have a significant impact on their pipeline of business opportunities.

Rule of Two Background

The Rule of Two generally applies to "any acquisition" that exceeds the simplified acquisition threshold, which is currently $250,000.[3] Prior to the enactment of the Jobs Act, GAO concluded in *Delex Systems* that task and delivery order procurements were subject to the Rule of Two because an order meets the broad definition of an "acquisition" under the *FAR*.[4]

GAO changed its view, however, following the issuance of regulations that were promulgated to implement the Jobs Act amendments to the Small Business Act.[5] The relevant statutory provision, 15 U.S.C. § 644(r), provides that "agencies, may, at their discretion...set aside orders placed against [MACs] for small business concerns." The statute granted agencies the discretion to set aside orders "notwithstanding" the general requirement for agencies to provide all MAC holders a "fair opportunity" to compete for orders.[6]

To implement the Jobs Act, the SBA promulgated a regulation which states that contracting officers may issue MAC solicitations that either: (1) notify offerors that the agency will set aside orders for small businesses whenever the Rule of Two is satisfied; or (2) reserve the right to place orders on a set-aside basis using the Rule of Two.[7] The regulation states that "[t]he ultimate decision of whether to use any of the above-mentioned tools in any given procurement action is a decision of the contracting agency."[8]

In 2014, citing the "plain language" of the SBA regulations, GAO's decision in *Edmond Scientific* held that an agency is not required to apply the Rule of Two to task and delivery order procurements unless the underlying MAC solicitation provides that the agency will follow it with respect to each order.[9] Notably, GAO reached this conclusion even though the SBA agreed with the protester's argument that the Rule of Two applies to task and delivery order procurements.[10]

One year after *Edmond Scientific*, GAO re-affirmed its holding in that case and again rejected the SBA

interpretation of its own regulations in *Aldevra*.[11] In that case, the SBA argued that the Jobs Act should be construed as merely creating an exception to the general requirement that all MAC holders be given a "fair opportunity" to compete for orders.[12] GAO disagreed, however, and concluded that 15 U.S.C. § 644(r) should, instead, be interpreted "as having carved out a limited exception" to the Rule of Two for orders placed under MACs.[13]

Thus, for more than six years, the law was seemingly well-settled that agencies need not apply the Rule of Two before conducting a task or delivery order procurement under a MAC. Indeed, GAO precedent has allowed agencies to effectively avoid the Rule of Two altogether if they decide to acquire goods or services through an order placed under a MAC.

The Tolliver Group, Inc., et al. v. United States

Tolliver involved two Army solicitations that were initially set aside for Service-Disabled Veteran-Owned Small Businesses (SDVOSBs) to provide training instructors for fire support specialists at Fort Sill. The Army made awards under both solicitations, but ultimately cancelled them as part of corrective action taken in response to GAO protests.

Shortly before the Army announced corrective action in the GAO protests, it awarded a MAC to five large businesses. The scope of the MAC included the Army's requirement for fire training instructors. Ultimately, the Army decided to cancel the two SDVOSB set-aside solicitations so that it could fulfill its needs using a task order competition among the large businesses that received a MAC.

Two SDVOSB contractors filed protests at the Court challenging the Army's decision to cancel the set-aside solicitations. The Court agreed with the protesters that the Army's "failure to conduct a Rule of Two analysis violates the cancellation decision" because that decision was dependent on the Army's belief that it could utilize the large business MAC holders to meet its needs.[14]

Citing the Jobs Act and its implementing regulations, the government argued that the Army had discretion to use a MAC without conducting a Rule of Two analysis. The Court disagreed and held that "the grant of discretion" under the Jobs Act "does not somehow, by negative implication, eliminate the Rule of Two requirement."[15]

The Court rejected the government's contention that it "can utilize the [MAC] for any acquisition – and avoid the Rule of Two – so long as the contemplated scope of work is within the [MAC's] scope."[16] According to the Court, "[n]o statutory or regulatory language...supports such a sweeping inference."[17]

As support for its decision, the Court expressly adopted "the same reasoning as the GAO in *LBM, Inc.*," a 2002 decision that predates the Jobs Act of 2010.[18] In *LBM*, GAO held that the Army violated the Rule of Two because it failed to consider whether an acquisition should be set aside for small businesses before it selected a MAC vehicle to meet its needs.[19]

The Court also noted that "the *FAR* knows how to" exempt certain procurement vehicles from the Rule of Two.[20] The *FAR* expressly provides that most of FAR Part 19, including the Rule of Two, does not apply to Federal Supply Schedule (procurements conducted under FAR Part 8.5.)[21] The Court observed that no similar exemption exists for task and delivery order procurements conducted under FAR Part 16.5.[22]

Protest of ITility, LLC

Less than a month after the Court's decision in *Tolliver*, GAO issued its decision in *ITility, LLC* that reaffirmed its view that agencies are not required to follow the Rule of Two if they choose to conduct a task or delivery order procurement.[23] GAO declined to adopt the *Tolliver* Court's construction of the Jobs Act and, once again, rejected the SBA's interpretation of its own regulations.

The protester in *ITility* had performed certain support services for the Department of Homeland Security for several years under a set-aside task order. Before the final option period of that task order expired, however, the agency considered different options for procuring its needs and ultimately selected GSA's Alliant 2 contract.

The protester did not hold an Alliant 2 contract, thus, it was not eligible to compete for the agency's new task order. The agency conducted the competition among all the Alliant 2 contract holders, including large businesses, and awarded the new task order under that contract vehicle.

The protester argued that the agency was required to set aside its requirement for small businesses under the Rule of Two. The SBA endorsed the protester's position that the Rule of Two is "mandatory and must be applied prior to placing the work under a [MAC]."[24]

GAO denied the protest and explained that its prior "decisions in *Edmond Scientific* and *Aldevra* comprehensively established our interpretation of the import of 15 U.S.C. § 644(r) and its implementing regulations, namely that set-aside determinations under multiple-award contracts are discretionary, not mandatory."[25]

GAO further explained that the position advanced by the protester and the SBA was "undercut" by the SBA's regulatory pronouncements, including its statement that the Jobs Act "makes the application of the 'rule of two' discretionary for orders placed under multiple-award contracts."[26]

GAO also was not persuaded by the protester's reliance on *Tolliver*. In a footnote, *Tolliver* distinguished *Edmond Scientific* and *Aldevra* on the basis that "none of those GAO cases, except *LBM*, addresses the precise issue of an agency moving work currently performed by a small business to a [MAC] where the incumbents are ineligible to compete for an award."[27]

GAO rejected this distinction and concluded that the Rule of Two is not mandatory in a task order procurement, regardless of whether the small business protester is or is not eligible to compete under the agency's preferred MAC acquisition vehicle.[28] GAO also disagreed with the protester, the SBA and the Court in *Tolliver* that GAO's decision in *LBM* was controlling because that decision predated the Jobs Act.[29]

SBA's Planned Rulemaking

As part of a regulatory agenda update earlier this year, the SBA indicated it is in the process of preparing a proposed rule to resolve the split between GAO and the COFC. The SBA seeks to codify its interpretation that the Rule of Two must be applied before an agency places an order under a MAC. This change, once finalized, will prevent agencies from moving work to MACs that would otherwise be set aside for small businesses under a Rule of Two analysis.

The rule is currently undergoing inter-agency review and it may contain certain exceptions. For example, as the COFC noted in *Tolliver*, FSS procurements are generally exempt from FAR Part 19 requirements including the Rule of Two. Thus, the Rule of Two may continue to be discretionary for FSS procurements under the proposed rule.

Contractors should monitor the Federal Register and be prepared to comment on the SBA's proposed rule when it is issued. Until the new rule is finalized, small businesses that are affected by an agency's decision to move set-aside work to a MAC should consider bringing a protest to the COFC where the law is more favorable than GAO. CM

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ENDNOTES

1 ITility, LLC, B-419167, Dec. 23, 2020, 2020 CPD ¶ 412.
2 The Tolliver Group, Inc., et al. v. United States, 151 Fed. Cl. 70 (2020).
3 FAR 19.502-2(b).
4 See Delex Systems, Inc., B-400403, Oct. 8, 2008, 2008 CPD ¶ 181 at 8.
5 See Edmond Scientific Co., B-410179, B-410179.2, Nov. 12, 2014, 2014 CPD ¶ 336 at 7.
6 15 U.S.C. § 644(r)(2).
7 13 C.F.R. § 125.2(e)(6)(ii).
8 Id.
9 Edmond Scientific, 2014 CPD ¶ 336 at 7.
10 Id.
11 Aldevra, B-411752, Oct. 16, 2015, 2015 CPD ¶ 33.
12 Id. at 6.
13 Id.
14 Tolliver, 151 Fed. Cl. at 112.
15 Id. at 115.
16 Id.
17 Id.
18 Id. at 116 (citing LBM, Inc., B-290682, Sept. 18, 2002, 2002 CPD ¶ 157).
19 LBM, 2002 CPD ¶ 157 at 8-10.
20 Tolliver, 151 Fed. Cl. at 117.
21 Id. (citing FAR 8.404(a); FAR 8.405-5(a)).
22 Id.
23 ITility, 2020 CPD ¶ 412 at 10-20.
24 Id. at 6.
25 Id. at 14.
26 Id. at 16 (quoting 5 Fed. Reg. 11746, 11746 (Feb. 27, 2020)).
27 Tolliver, 151 Fed. Cl. at 117, n.63.
28 ITility, 2020 CPD ¶ 412 at 17-18.
29 Id. at 18, n.16.