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**Comptroller General
of the United States**

**United States Government Accountability Office
Washington, DC 20548**

Decision

Matter of: Hydroid LLC

File: B-299072

Date: January 31, 2007

Charles R. Marvin, Jr., Esq., Thomas J. Madden, Esq., Sharon A. Jenks, Esq., and Dismas N. Locaria, Esq., Venable LLP, for the protester.

Fred Kopatich, Esq., and Mark Langstein, Esq., National Oceanic and Atmospheric Administration, and Kenneth Dodds, Small Business Administration, for the agencies.

Paul E. Jordan, Esq., and John M. Melody, Esq., Office of the General Counsel, GAO, participated in the preparation of the decision.

DIGEST

In small business set-aside, agency's acceptance of firm's claimed entitlement to small business status under "nonmanufacturer rule" was unreasonable where agency should have known firm's claimed status was questionable, and therefore should have challenged its status before Small Business Administration.

DECISION

Hydroid LLC protests issuance of a purchase order to Brooke Ocean Technology USA, Inc. (BOT-USA) under request for quotations (RFQ) No. NCNJ1000-6-00001, a 100-percent small business set-aside issued by the Department of Commerce, National Oceanic and Atmospheric Administration (NOAA), for an autonomous underwater vehicle (AUV). Hydroid asserts that BOT-USA was ineligible for the order as a small business.

We sustain the protest.¹

¹ On December 12, 2006, our Office conducted an alternative dispute resolution telephone conference with the parties. The GAO attorney of record explained in detail why he anticipated that the protest would be sustained for the reasons set forth in this decision. Because neither party took action rendering the protest academic, we are issuing this decision.

The AUV is to be used in conjunction with manned surface assets to perform rapid-response capability for underwater surveys of ports, harbors, and inland waterways. The RFQ was issued as a combined synopsis/solicitation for commercial items under Federal Acquisition Regulation (FAR) subpart 12.6. It identified North American Industry Classification System Code (NAICS) 334511--Search, Detection, Navigation, Guidance, Aeronautical, and Nautical System and Instrument Manufacturing--as applicable to this procurement, with an applicable size standard of 750 employees. Vendors' quotations were to be evaluated under three factors of relatively equal importance--approach, past performance, and price. The RFQ contemplated issuance of a fixed-price purchase order for one AUV, 2 years of technical support, warranty, and training, with delivery not later than 9 months after receipt of the order. The order was to be made on a "best value" basis.

BOT-USA, a small business, submitted a quotation offering an AUV manufactured by Bluefin Robotics Corporation, a large business; Hydroid, also a small business, submitted a quotation to provide its own AUV. NOAA determined that BOT-USA's quotation provided the best value based on its technical superiority and lower price, and, on August 9, 2006, issued that firm a purchase order in the amount of \$1,705,247. NOAA did not notify Hydroid of the issuance of the order until August 30, when the protester inquired about the procurement's status. On August 31, Hydroid filed a timely size protest with the contracting officer, who submitted it to the Small Business Administration (SBA) on September 21. On October 18, SBA determined that BOT-USA was ineligible for the purchase order because it was offering the product of a large business. NOAA subsequently determined that it would not terminate BOT-USA's purchase order, and this protest followed.

In order to qualify as a small business concern eligible to provide manufactured products under a small business set-aside, a firm must either be a small business manufacturer of the end item being procured, or provide the product of another domestic small business manufacturing or processing concern; this is known as the "nonmanufacturer rule." FAR §§ 19.001, 19.102(f)(1); 13 C.F.R. § 121.406 (2006). The rule may be waived where the acquisition is for a product in a class for which SBA has determined that there are no small business manufacturers in the federal market--see FAR § 19.102(f)(4)--or where the contracting officer seeks a special waiver from SBA based on the lack of small business manufacturers and SBA issues the waiver. FAR §§ 19.102(f)(5), 19.502-2(c).

BOT-USA submitted a quotation for the product of a large business--Bluefin--as well as the additional work to make the Bluefin AUV meet the agency's requirements. However, there was no valid class waiver in place exempting AUVs from the nonmanufacturer rule, and the contracting officer did not seek or obtain a special waiver. While SBA's list includes a class waiver for NAICS 334511--the code identified in the RFQ--the waiver, by its terms, covers only "airborne integrated components"; it undisputedly does not cover nautical products such as the AUV under the RFQ, and NOAA does not now assert that the waiver extended to the AUV. See Product Service Code 5821, www.sba.gov/GC/approved.html.

Since BOT-USA's quotation, on its face, showed that it was based on an item manufactured by a large business and, as explained above, it is undisputed that the class waiver for NAICS 334511 does not extend to nautical items such as the item here, the contracting officer was or should have been aware prior to issuance of the purchase order that BOT-USA was not an eligible small business. The contracting officer asserts neither that she believed there was an applicable waiver, nor that she was confused as to the existence of such a waiver.² While, in the absence of a size protest from an offeror, there is no requirement that a contracting officer refer size status questions to SBA, we will review the reasonableness of a contracting officer's failure to do so. Jensco Marine, Inc., B-278929.7, Feb. 11, 1999, 99-1 CPD ¶ 32 at 5. Under the circumstances here--where the face of BOT-USA's quotation showed that the firm was not an eligible small business--we can only conclude that it was unreasonable for the contracting officer to accept BOT-USA's quotation rather than refer the matter to SBA.

As noted above, although Hydroid did not learn of the issuance of the purchase order to BOT-USA until after the fact, it submitted a timely size protest (that is, within 5 days after learning of the issuance of the purchase order to BOT-USA, see 13 C.F.R. § 121.1004(a)), and SBA determined that BOT-USA in fact was not a small business eligible for the purchase order based on its quoting of an item manufactured by a large business. Further, NOAA decided to leave the purchase order in place after SBA determined BOT-USA to be ineligible. Diagnostic Imaging Tech. Educ. Ctr., Inc., B-257590, Oct. 21, 1994, 94-2 CPD ¶ 148 at 3. In prior cases where, as here, a contracting agency's improper actions led to an award before a size protest could be filed--typically, where the agency failed to provide the required pre-award notice of the intended awardee--and SBA determined after award that the awardee was not an eligible small business, we have sustained the protests and recommended termination of the contracts. See, e.g., Spectrum Sec. Servs., Inc., B-297320.2, B-297320.3, Dec. 29, 2005, 2005 CPD ¶ 227 at 4; Tiger Enters., Inc., B-292815.3, B-293439, Jan. 20, 2004, 2004 CPD ¶ 19 at 4-5. In these circumstances, in the absence of any legitimate countervailing reasons, we view it as inconsistent with the Small Business Act, 15 U.S.C. § 631-657a, and the integrity of the procurement process for

² Prior to the submission of quotations, the director of NOAA's Office of Small and Disadvantaged Business Utilization corresponded with Bluefin's parent company by e-mail, and erroneously advised that since NAICS 334511 was on the SBA class waiver list, small businesses could provide the products of a large business. While the contracting specialist for this procurement was copied in the correspondence from the director, there is no evidence that she or the contracting officer relied on this information in accepting BOT-USA's size representation. Moreover, in the absence of a valid waiver, the placement of a purchase order in violation of the nonmanufacturer rule would be improper even if those individuals had erroneously believed that a waiver applied.

an agency to permit a firm that was ineligible under the terms of the solicitation to continue performance. Spectrum Sec. Servs., *supra*, at 5.

NOAA asserts that there are countervailing circumstances that warrant leaving BOT-USA's purchase order in place.³ Specifically, it asserts that BOT-USA has "substantially performed work under the contract," and that termination of the order would "unacceptably delay[]" "an important homeland security initiative." NOAA Supplemental Report at 5. As to the former reason, NOAA states that BOT-USA has expended more than \$236,000 in performing the order; as to the latter reason, NOAA asserts that it expects termination settlement costs to exceed available funding, thus requiring it to postpone acquisition of the AUV for 18 months.

Among other matters, we have considered substantial performance in determining whether there are countervailing circumstances to warrant allowing a business concern that is not small to continue performance. In our view, the agency has not established the existence of legitimate countervailing circumstances here. With regard to the costs reported by BOT-USA, we note that they are only 12 percent of the order, and thus do not appear to support the agency's claim that the contract has been substantially performed. While the agency states that it will be unable to fund a resolicitation of this requirement and that terminating the purchase order will unacceptably delay an important program, we find it significant that it was NOAA's own actions that led to its current position. In this regard, since SBA ordinarily makes a size determination in 10 working days (approximately 2 weeks), if possible (13 C.F.R. § 121.1009(a)), and here made its determination in 18 working days (approximately 4 weeks), had the contracting officer sought SBA's input prior to issuing the purchase order, its full funding would have been available for an eligible small business to perform and that firm could have commenced performance after less than 1 month of delay. Similarly, even after issuing the purchase order, NOAA could have significantly mitigated its out-of-pocket costs at several points. For example, NOAA could have stayed performance when Hydroid filed its size protest with the agency 3 weeks after issuance of the purchase order; it could have expedited the size appeal process by forwarding Hydroid's protest to SBA promptly (13 C.F.R. § 121.1006) instead of waiting 3 weeks after receiving it; and NOAA could have promptly acted upon SBA's size determination, which was completed only 10 weeks after issuance of the purchase order. However, the agency did not even obtain information on how much BOT-USA had expended until shortly before its agency report was due, approximately 1 month after Hydroid filed its protest with our Office and more than 14 weeks after the agency issued the purchase order.

³ NOAA also asserts that BOT-USA's appeal to OHA militates against terminating the order. However, since OHA has dismissed the appeal as untimely, the initial determination "remains in full force and effect" with respect to this procurement. See 13 C.F.R. § 121.1009(g)(1); ALATEC Inc., B-298730, Dec. 4, 2006, 2006 CPD ¶ 191 at 5.

The protest is sustained.

We recommend that the purchase order placed with BOT-USA be canceled. We also recommend that the agency issue a purchase order to an eligible small business whose quotation represents the best value to the government. We further recommend that the agency reimburse Hydroid's costs of filing and pursuing the protest, including reasonable attorneys' fees. 4 C.F.R. § 21.8(f)(1) (2006).

Gary L. Kepplinger
General Counsel