Appendix C

ETA Response to Draft Report

U.S. Department of Labor

Assistant Secretary for
Employment and Training
Washington, D.C. 20210

AUG 4 - 2014

MEMORANDUM FOR: ELLIOT P. LEWIS
Assistant Inspector General for Audit

FROM: PORTIA WU
Assistant Secretary

SUBJECT: Response to the OIG Audit Report – "Job Corps Contractor and DOL Procurement Practices Need Improvement" Report No. 26-14-002-03-370

This memorandum responds to the subject audit report, dated June 2014, Office of the Inspector General's (OIG) Audit Report No. 26-14-002-03-370, *"Job Corps Contractor and DOL Procurement Practices Need Improvement"*

Audit Summary:

The OIG's audit objective was to determine if the practices of ResCare, Inc., (ResCare) and the prime contractors it performed work for comply with federal procurement regulations. The audit was conducted due to the procurement risk associated with a prior Small Business Administration (SBA) determination on the contractor-subcontractor relationship between a small business selected by OASAM for a small business set-aside contract to operate a Job Corps Center with ResCare as its subcontractor. It was also conducted to follow up on a FY 2012 performance audit the Office of the Inspector General (OIG) conducted in response to an anonymous complaint OCM referred to the OIG.

The SBA found that a small business was ineligible for a set-aside contract because it would have allowed ResCare, a large business, to perform primary and vital contract requirements intended for the small business. SBA also found that this small business was unusually reliant on ResCare's qualifications to win the Job Corps center contract. Further, the weak procurement controls identified during the 2012 hotline complaint audit indicated that the subcontracting deficiencies may be systemic.

The OIG reviewed work in two areas:

- Contractor–subcontractor relationships between Job Corp center (JCC) operators selected by DOL for small business set-aside contracts and ResCare as a subcontractor.
- Subcontracts ResCare awarded as the prime contractor operating JCCs.

OIG ResCare Subcontracting Practices Audit

The OIG found that ResCare and two small business prime contractors appeared to have circumvented the ostensible subcontractor rule. Additionally, the OIG found that ResCare, as a prime contractor, did not comply with the Federal Acquisition Regulation (FAR) and its own procurement policies when awarding subcontracts and purchase orders at the centers it operates.

The OIG also found that gaps in DOL oversight likely contributed to the ostensible relationships due to lack of processes and controls to ensure large businesses were not performing primary and vital requirements of the center contracts.

The OIG's five recommendations and our response follow:

OIG Recommendation 1: Refer the four (4) small business set-aside contracts we identified held by Alutiiq Education and Training and Alutiiq Professional Services to SBA for review and guidance on corrective action, if warranted.

Response: Management accepts this recommendation.

ETA will refer three of the four identified small business set-aside contracts to SBA for review, as one has since been awarded to another vendor.

We consider this recommendation resolved.

OIG Recommendation 2: Develop and implement a mechanism or procedures for ensuring each small business set-aside contract is free of potential violations of affiliation rules.

Response: Management accepts this recommendation.

ETA will consult with the Office of the Assistant Secretary for Administration and Management's Procurement Policy Office and the SBA to develop universal procedures to assist DOL procurement staff in ensuring small business set aside contracts are free of potential violations of affiliation rules.

We consider this recommendation resolved.

OIG Recommendation 3: Develop and implement a comprehensive training plan for procurement staff, including training on areas as affiliation, ostensible subcontracting, and the scope of privity.

Response: Management accepts this recommendation.

ETA will provide additional training to procurement staff on contractor affiliation and will seek support from SBA to help identify warning signs of potential contractor/subcontractor affiliation problems.

OIG ResCare Subcontracting Practices Audit

OIG Recommendation 4: Conduct the new Contractor Purchasing System Review (CPSR) planned for ResCare in Fiscal Year 2015 (FY15) or if the new CPSR is cancelled or delayed, follow up on ResCare's CAP, as well as the procurement weaknesses identified in ETA's 2012 CPSR report and this OIG audit report.

Response: Management accepts this recommendation.

ETA plans to conduct a new CPSR of ResCare in early FY15 and is in the process of developing the FY15 CPSR schedule. Based upon the CPSR rubric, ResCare's review will consist of site visits to the corporate office and three ResCare operated Job Corps centers. The OIG will be issued a copy of the CPSR report and the purchasing system approval decision.

OIG Recommendation 5: Develop and implement procedures to ensure ResCare complies with its center operator contract provisions and its own procurement policies and procedures, such as a memorandum to ResCare reinforcing that the centers it operates receive the required approval and documentation for purchases and that center purchases are free of micro-purchase violations.

Response: Management accepts this recommendation.

While procedures and processes for monitoring contract performance are in place, ETA will reemphasize the importance of adequate contract monitoring. Both Contracting Officers/Specialists and Contracting Officer's Representatives (COR) have responsibility for adequately monitoring contractor performance. ETA has established a quarterly COR training program. Training to provide sufficient oversight of contract terms and conditions will be among the topics offered. In addition, the OCM will develop a COR contract monitoring checklist to assist CORs in providing adequate oversight of the Job Corps center contracts.

We consider this recommendation resolved.

Based upon ETA's response to the aforementioned audit recommendations, we anticipate the OIG will close all recommendations accordingly. If you have questions concerning this document, please contact Linda K. Heartley, ETA's Head of the Contracting Activity, Office of Contracts Management at (202) 693-3404.

cc: Linda K. Heartley, Office of Contracts Management
Lenita Jacobs-Simmons, Office of Job Corps
Julie Cerruti, ETA Audit Liaison
Linda Marshall, Job Corps Audit Liaison
Peni Webster-Lewis, Office of Contracts Management Audit Liaison

Appendix D

ResCare Response to Draft Report

9901 Linn Station Road
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July 18, 2014

VIA E-MAIL - lewis.elliot@oig.dol.gov

Mr. Elliot P. Lewis
Assistant Inspector General for Audit
U.S. DEPARTMENT OF LABOR
90 7th Street, Suite 02-750
San Francisco, California 94103

Re: Department of Labor, Office of Inspector General Draft Report 26-14-002-03-370

Dear Mr. Lewis:

This letter is in response to the Draft Report 26-14-002-03-370 by the U.S. Department of Labor, Office of Inspector General, issued July DD, 2014. In the Draft Report, DOL-OIG asked whether the practices of ResCare and the prime contractors it performed work for comply with federal procurement regulations. The Draft Report stated ResCare's DOL procurement practices need improvement as ResCare did not always comply with the FAR and its own procurement policies. DOL-OIG recommended the Assistant Secretary for Employment and Training require the Regional Job Corps Offices and respective ETA COs follow-up on our corrective action plan and conduct a new CPSR (Contractor Purchasing System Review).

ETA Contracting Office conducted the CPSR in 2012. ResCare submitted a corrective action plan and our Purchasing ResCare (PRC) standard operating procedures that were approved by the cognizant Contracting Officer, E. Thomas Pendleton, on 6/27/2013. CO Pendleton recommended ResCare conduct additional training and auditing of our purchasing system (**Exhibit A**).

ResCare has implemented its PRC standard operating procedures and addressed the remainder of CO Pendleton's recommendations. We strengthened and disseminated our Purchasing ResCare policies in 2013 (**Exhibit B**). Marian Hayes, our Director of Property/Purchasing conducted follow-up training to ensure the revised policies were implemented properly (**Exhibit C**). On the recommendation of Linda Hartley, ETA Contract Management Director, we utilized Management Concepts to provide additional training in this area (**Exhibit C**). Marion Hayes Purchasing/Property Director has conducted unscheduled audits to confirm the revised policies have been effectively implemented (**Exhibit E**). Additionally, we added a Purchasing/Subcontract review to our scheduled Best in Class Audits conducted by the Program Support Team (**Exhibit E**).

Mr. Elliot P. Lewis
July 18, 2014
Page 2

We take the recommendations of DOL-OIG very seriously. They have been very instructive. Pursuant to the DOL-OIG's recommendations, we have strengthened our procurement policies and enhanced our practices. We have conducted training and we continually monitor our progress to confirm total compliance across all our Centers. We will accept nothing short of full compliance.

Sincerely,

STEVEN S. REED
Chief Legal Officer

Attachments

cc: Ray Armada, Audit Director (armada.ray@oig.dol.gov)
Heather Atkins, Audit Manager (atkins.heather@oig.dol.gov)

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Appendix E

AYS Response to Draft Report

Mark G. Jackson
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July 17, 2014

Elliot P. Lewis
Assistant Inspector General for Audit
Department of Labor
Office of Inspector General—Office of Audit
Francis Perkins Building, Room S-5502,
200 Constitution Avenue, NW
Washington, DC 20210

Re: Audit Report No. 26-14-002-03-370
Response by Alutiiq Education & Training, LLC and Alutiiq Professional Services, LLC

Dear Mr. Lewis:

I write on behalf of Alutiiq Education & Training, LLC and Alutiiq Professional Services, LLC (collectively, "Alutiiq") to provide Alutiiq's response to the draft of the above-referenced audit report (the "Draft Report"). In this Draft Report, the Office of Inspector General ("OIG") found that Alutiiq "appears" to have violated the ostensible subcontractor rule in four separate contracts awarded to Alutiiq by the Department of Labor's Employment and Training Administration ("ETA"). The Draft Report then recommends that each of the four contracts at issue be referred to the Small Business Administration ("SBA") "for review and guidance on corrective action, if warranted." Alutiiq strongly disagrees with the findings and recommendation contained in the Draft Report for several reasons. First, the audit on which this report is based violates generally accepted government auditing standards. Second, properly performed, an audit would not have found apparent violations of the ostensible subcontractor rule in any of the four contracts at issue. Third, the recommendation to refer these four contracts to SBA for review is improper because such a review will have no practical effect. I address each of these points in detail below.

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I. THE AUDIT ON WHICH THE DRAFT REPORT IS BASED VIOLATES GENERALLY ACCEPTED GOVERNMENT AUDITING STANDARDS.

The Draft Report claims to comply with generally accepted government auditing standards. It does not. Instead, the Draft Report violates generally accepted government auditing standards because it uses incorrect and insufficient criteria for the audit.

According to the Government Accountability Office ("GAO"), which establishes generally accepted government auditing standards:

> Auditors should identify criteria. Criteria represent the laws, regulations, contracts, grant agreements, standards, specific requirements, measures, expected performance, defined business practices, and benchmarks against which performance is compared or evaluated. *Criteria identify the required or desired state or expectation with respect to the program or operation. Criteria provide a context for evaluating evidence and understanding the findings, conclusions, and recommendations included in the report. Auditors should use criteria that are relevant to the audit objectives and permit consistent assessment of the subject matter.*[1]

Obviously, if incorrect criteria are used, the audit will be unable to correctly assess performance. That is precisely what happened here: the findings and recommendations are invalid because the audit relied on incorrect and insufficient criteria.

In this matter, the audit objective was to answer the question: "Did the practices of ResCare and the prime contractors it performed work for comply with federal procurement regulations?"[2] One aspect of that objective — and the primary focus of this audit — was a determination of whether the four contracts awarded by ETA to Alutiiq violated the ostensible subcontractor rule. The Draft Report identifies various statutes, regulations, and agency guidance materials as criteria. However, the sole criterion on which the Draft Report relies for its findings and recommendations regarding purported violations of the ostensible contractor rule is a single decision by the SBA's Office of Hearings and Appeals "OHA"), *Size Appeal of Alutiiq Educ. & Training, LLC*, SBA No. SIZ-5192, 2011 LEXIS 21 (2011) (hereinafter "*Turner*").[3] By relying solely on that OHA decision, the Draft Report violates generally accepted government auditing standards

[1] Government Accountability Office, GAO-12-331G, Government Accounting Standards (2011 Revision), ¶ 6.37 (emphasis added).

[2] Draft Report, Appendix A, p. 19.

[3] *See* Draft Report, pp. 4, 8-9, 11

because the *Turner* decision, by itself, is an incorrect and incomplete statement of the law regarding the ostensible subcontractor rule.

There are a number of more recent and relevant OHA decisions addressing the ostensible subcontractor rule that must be considered if the audit is to comply with generally accepted government auditing standards, including, but not limited to: *Size Appeal of InGenesis, Inc.*, SBA No. SIZ-5436, 2013 SBA LEXIS 5 (2013); *Size Appeal of Roundhouse PBN, LLC*, SBA No. SIZ-5383, 2012 SBA LEXIS 75 (2012); *Size Appeal of Alutiiq Educ. & Training, LLC*, SBA No. SIZ-5371, 2012 SBA LEXIS 58 (2012) (hereinafter "*Serrato*"); and *Size Appeal of CymSTAR Servs., LLC*, SBA No. SIZ-5329, 2012 SBA LEXIS 29 (2012).[4] As discussed in detail below, the failure to include these and other OHA decisions as criteria in this audit has a profound impact on the findings and recommendations contained in the Draft Report. Indeed, because the audit failed to apply these criteria to the audit, the audit both fails to achieve its objective and violates generally accepted government auditing standards.

II. When Proper Criteria Are Applied, Alutiiq's JCC Contracts Do Not Violate the Ostensible Subcontractor Rule

The Draft Report wrongly concludes that Alutiiq's relationship with its subcontractor, ResCare, at the four JCCs named in the Report "appeared" to have violated the ostensible subcontractor rule. In reaching this errant conclusion, the Draft Report not only disregards the current state of established law on the ostensible subcontractor rule but also overlooks the many crucial differences between the JCCs named in the Draft Report and the Turner JCC, the subject of the only case the auditors bothers to consult (i.e., *Turner*). The Draft Report presumes that the JCCs at issue are identical in all material respects to the Turner JCC, and that OHA's ostensible subcontractor jurisprudence has not undergone any significant changes since 2011; both of those assumptions, however, are demonstrably incorrect. In fact, despite recent OHA decisions casting serious doubt on *Turner*'s validity, OIG seems oblivious to these important developments and bases its conclusion almost entirely on certain superficial similarities to that lone decision. As discussed herein, the substantial differences between the four JCCs at issue and the Turner JCC, especially when viewed in light of OHA's more recent decisions, demonstrate that Alutiiq unquestionably did *not* violate the ostensible subcontractor rule.

[4] The substantive impact of the failure to consider these and other relevant OHA decisions in discussed at Section II, *infra*.

A. The Draft Report Fails to Recognize a Critical Distinction in Comparing the Alutiiq JCC Contracts With the *Turner* JCC Contract: Alutiiq Provides Nearly All the Key Employees.

The Draft Report completely disregards, without explanation, a critical difference between the JCCs at issue and the Turner JCC: that Alutiiq, not ResCare, provides virtually all of the key employees. OHA has "consistently held that among the ***main considerations*** in ostensible subcontractor analysis are which concern is ***managing the contract and will be providing the key employees***." *Size Appeal of Alutiiq Educ. & Training, LLC*, SBA No. SIZ-5371, 2012 SBA LEXIS 58, *20 (2012) (hereinafter "*Serrato*"); *see also Protest of Alutiiq Pacific LLC*, No. 12-ODRA-00627, 2013 ODRA LEXIS 4, *82-83 (2013) ("A primary factor to be considered in determining compliance with the ostensible subcontractor rule is which concern is managing the contract, and will be providing the key employees.").

Given the importance OHA attaches to a prime contractor's responsibility for providing key employees, it is therefore a glaring error for the Draft Report to fail even to *mention* this issue within the Report. The following differences between the Turner JCC and the four JCCs — none of which the Draft Report apparently even considered — strongly refute the Draft Report's determination that Alutiiq likely violated the ostensible subcontractor rule:

- ***Overall Percentage of Key Employees.*** In *Turner*, OHA observed that "six of ten proposed key employees were employed by ResCare at the time of the proposal." *Turner*, at *20. By comparison, Alutiiq employs nearly all of the key employees at each of the JCCs at issue. For example, at the Cleveland JCC, ResCare employed only ***one*** of the ten proposed key employees at the time of the proposal.[5] Put another way, while ResCare would have accounted for 60 percent of the key personnel at the Turner JCC, ResCare accounted for just 10 percent of the key personnel at the Cleveland JCC, and Alutiiq thus employed the remaining ***90 percent*** of the key personnel.[6] The Draft Report completely ignores this distinction.

[5] *See* Final Proposal for Cleveland JCC, Staff Resources ("SR") at A2, A5. Alutiiq previously provided to OIG a copy of the cited materials via Alutiiq's four letters to OIG, each dated January 21, 2014, which responded to OIG's preliminary Statement of Facts for the contracts at issue and included the referenced documents as attachments.

[6] *Id.* The situation at the other JCCs was comparable, where Alutiiq employed all of the key employees except for the Career Development Services System Director. *See* Bamberg Final Proposal Revision ("FRP") at 39; Westover SR at A2; Northlands SR at A2.

- ***Center Director.*** One of OHA's main concerns in *Turner* was the fact that the proposed Center Director — the most senior contract position, with responsibility over all Job Corps Center operations — was a ResCare employee and not employed by Alutiiq. By comparison, Alutiiq employs the Center Director at all four of the JCCs at issue.[7] In fact, the employees with the greatest executive responsibility at the JCCs at issue — i.e., Center Director, Executive Assistant, and Deputy Center Director, who together oversee all facets of each contract — are *all* Alutiiq personnel.[8] The fact that Alutiiq provides all of these employees is a key difference between the Turner JCC and the JCCs at issue, but the Draft Report makes no mention of this distinction.

- ***Most Highly Compensated Personnel.*** In *Turner*, OHA noted that "two of the three most highly compensated proposed personnel (the Center Director and the Social Development director) are current ResCare employees." *Turner*, at *20. At all four of the JCCs at issue, on the other hand, the Social Development Director — in addition to the Center Director — is an Alutiiq employee.[9] Thus, unlike at the Turner JCC, these two highly compensated personnel are Alutiiq employees, not ResCare employees. The Draft Report again makes no mention of this important distinction.

- ***Social Development Director.*** As noted above, the Social Development Director at the JCCs at issue are employed by Alutiiq, not ResCare. Recent OHA decisions underscored the importance of that position. In *Serrato*, for instance, OHA found the prime contractor's employment of the Social Development Director was strong evidence that there was no violation of the ostensible subcontractor rule:

> Serrato will also provide the Social Development Director, who will oversee the important residential program. It is clear that the purpose of the [Job Corps] Center is not merely academic training, but, in effect, the operation of a large educational institution providing support services in a safe setting and training the students in life skills as well as technical skills. The Social Development Director is clearly a key position.

[7] *See* Cleveland SR at A2; Bamberg FRP at 39; Westover SR at A2; Northlands SR at A2. Although Alutiiq's original choice for the position of Center Director at the Westover JCC was a ResCare employee, he was not approved by Job Corps' Boston Regional Office so Alutiiq instead chose to transfer the Detroit JCC's Center Director (an Alutiiq employee) to the Westover JCC.

[8] Unlike the Cleveland and Westover JCCs, the relatively smaller Northlands and Bamberg JCCs do not have Deputy Center Directors, and Northlands has an Executive Secretary instead of an Executive Assistant.

[9] *See* Cleveland SR at A2; Bamberg FRP at 39; Westover SR at A2; Northlands SR at A2.

Serrato at *21. Despite the importance of this role, however, the Report, nonetheless, fails even to mention the fact that Alutiiq employs the Social Development Director at all four of the JCCs at issue.

In short, Alutiiq employs the overwhelming majority of key personnel at all of the JCCs at issue, in marked contrast to the JCC in *Turner*. The Draft Report, however, fails to recognize — let alone rebut — this distinction. Since one of the "main considerations in ostensible subcontractor analysis" is which concern "will be providing the key employees," *id.* at *20, this omission is particularly egregious. If the audit had examined the significant differences between the Turner JCC and the JCCs at issue, OIG would have come to the correct conclusion: that *Turner* is not factually on point and cannot support a finding that Alutiiq may have violated the ostensible subcontractor rule.

B. The Draft Report Fails to Recognize Another Critical Distinction in Comparing the Alutiiq JCC Contracts With the *Turner* JCC Contract: Alutiiq's Past JCC Experience.

The Draft Report completely disregards — again, without explanation — another key consideration in the ostensible subcontractor rule analysis: Alutiiq's experience in the subject area of the procurement, and, thus, its ability to perform the contract without undue reliance on the subcontractor. "Generally, a finding that an ostensible subcontractor will perform the primary and vital contract tasks is based upon a determination ***that the prime contractor lacks the ability to perform those tasks***." *Size Appeal of Logmet, LLC*, SBA No. SIZ-5155, 2010 SBA LEXIS 77, *22 (2010) (emphasis added). A central issue is thus "whether the prime could not qualify for award of a contract without unusual reliance upon the qualifications or other assistance from a subcontractor." *Size Appeal of Smart Data Solutions LLC*, SBA No. SIZ-5071, 2009 SBA LEXIS 78, *50 (2009). The ostensible subcontractor rule generally will not apply unless "the prime has very little experience in the subject area of the procurement and the likely dollar value of the procurement is well outside of the experience range of the prime." *Size Appeal of C&C Int'l Computers & Consultants, Inc.*, SBA No. SIZ-5082, 2009 SBA LEXIS 93, *34 (2009). Neither Alutiiq nor the four contracts at issue fit that description. To the contrary, Alutiiq possesses significant experience in the subject area of the procurements, and the dollar value of those contracts is well within Alutiiq's experience range. The Draft Report overlooked the following relevant experience:

- ***Detroit JCC Experience.*** In *Turner*, OHA found that Alutiiq "relied almost entirely upon the experience of other entities to establish its relevant experience," and that Alutiiq did not have "sufficient relevant experience to perform this contract." *See Turner*, *24. With respect to the four JCCs at issue, however, Alutiiq's proposal set forth considerable prior relevant experience. All four of Alutiiq's proposals

highlighted AET's prior success at the Detroit JCC, where AET performed *all* of the relevant services. AET has provided academic, career technical, and career transition training at the Detroit JCC since 2008, more than three years before it was awarded any of the four contracts at issue. The work performed by these AET employees encompasses nearly all of the services that ResCare is providing at those JCCs. Although Alutiiq brought this experience to the auditor's attention, the Draft Report makes no mention of it whatsoever.

- ***Flint/Genesee JCC Experience.*** Alutiiq's proposals for the four JCCs at issue also highlighted its success at the Flint/Genesee JCC, where AET's affiliate, Alutiiq Professional Services, LLC ("APS"), performed all of the relevant services (including those that ResCare would perform under the four JCC contracts at issue).[10] The Draft Report again makes no mention of this experience.

Given Alutiiq's experience at the Detroit and Flint/Genesee JCCs, OHA's finding in *Turner* that Alutiiq "has no experience in most of the services to be provided under the contract" is simply untenable.[11] Any doubts expressed in *Turner* about the extent of Alutiiq's experience should have been dispelled by the past performance information contained in Alutiiq's proposals for the JCCs at issue. Since Alutiiq, in fact, possesses extensive experience in *all* subject areas of the procurement, and the dollar value of the procurement is well within its experience range, [12] the Draft Report's suggestion that Alutiiq was unduly reliant on ResCare is clearly unjustified. *See, e.g., C&C Int'l*, 2009 SBA Lexis 93, at *34 (stating that it is "difficult to justify a finding of unusual reliance unless . . . the prime has very little experience in the subject area of the procurement and the likely dollar value of the procurement is well outside of the experience range of the

[10] In *Turner*, OHA disregarded Alutiiq's experience at the Flint/Genesee JCC based on the erroneous view that an affiliate's experience is irrelevant for purposes of the ostensible subcontractor rule. *Id.* at *21-22. In a subsequent decision, however, OHA reaffirmed that an Alaskan Native Corporation—such as AET—*may* rely on the experience of its parent company and other affiliated entities to show that it possessed the requisite experience without violating the ostensible subcontractor rule, reasoning that such reliance fell within the exception to affiliation found in 13 C.F.R. § 121.103(b)(2). *See Size Appeal of Roundhouse PBN, LLC*, SBA No. SIZ-5383, 2012 SBA LEXIS 75, *38-41 (2012) (citing *Size Appeal of Alutiiq International Solutions, LLC*, SBA No. SIZ-5098 (2009)).

[11] Notably, during Alutiiq's tenure, the Detroit and Flint/Genesee JCCs have gone from being two of the lowest scoring JCCs in the country to two of highest scoring. Indeed, before Alutiiq took over, the Flint/Genesee JCC was ranked dead last. *See, e.g.*, Cleveland Past Performance Submission at 3 ("On March 1, 2004, Alutiiq and its subcontractor, ResCare, began operating the FGJCC. At the time, the center had an OMS ranking of 118 out of 118 centers and an overall rating of 74.5 percent."). Five years later, when Alutiiq submitted its proposal to operate the Cleveland JCC, the Flint/Genesee JCC was ranked 13th overall, and was 2nd in GED/High School Diploma completion. *Id.*

[12] The contract amounts for both the Flint/Genesee JCC ($18,838,160) and the Detroit JCC ($16,540,389) exceeds the base amount for three of the four JCC contracts at issue.

prime"). Had the auditors properly examined Alutiiq's prior experience at the Detroit and Flint/Genesee JCCs, they would have realized that Alutiiq was *not* unusually reliant upon ResCare for the four JCC contracts at issue.

C. The Draft Report Fails to Recognize Another Critical Distinction in Comparing the Alutiiq JCC Contracts With the *Turner* JCC Contract: Management, Control & Operation of the JCCs.

The Draft Report completely disregards yet another critical difference between the JCCs at issue and the Turner JCC: that Alutiiq manages the prime contract, and its subcontractor's personnel remain firmly under Alutiiq's supervision and control. Such responsibilities are critical for purposes of ostensible subcontractor analysis. *See, e.g.*, *Size Appeal of InGenesis, Inc.*, SBA No. SIZ-5436, 2013 SBA LEXIS 5, *43 (2013) (citation omitted) (finding that ostensible subcontractor rule did not apply where prime contractor managed the subcontractor and the subcontractor remained "under the supervision and control of the prime contractor"). Even where the prime contractor utilizes a large number of rank-and-file and even key employees from a subcontractor, that "may be insufficient to establish the existence of an ostensible subcontractor relationship ***if other facts show all control and decision making responsibility reside with the prime contractor***." *Alutiiq Pacific*, 2013 ODRA LEXIS 4, *83 (emphasis added) (citing *Size Appeal of J.W. Mills Mgmt., LLC*, SBA No. SIZ-5416, at 8 (2012)). Accordingly, OHA holds that the ostensible subcontractor rule is generally not implicated as long as the general contractor controls the procurement and appropriately manages the project as a prime contractor:

> [The subcontractor] is performing a majority of the work on these contracts. However, [the prime contractor] is also performing a substantial amount of the work and ***does not seem to be merely a 'front'*** for [the subcontractor]. The Board precedents do not indicate that [the prime] must perform a majority of the work ***if it is actually controlling the procurement and acting as the prime contractor.***

See Size Appeal of Swepco Corp., SBA No. 1449, 1981 SBA LEXIS 42, *6 (1981) (emphasis added).

Alutiiq's role in the operation and management of the four JCCs differs from its role under the Turner JCC proposal, where ResCare employed the Director of Operation and would have played a considerable role in the operation and administration of the JCC through key personnel. On the other hand, Alutiiq's proposals for the contracts at issue clearly show that at the four JCCs named in the Draft Report Alutiiq — and not ResCare — is fully in charge: Alutiiq, not ResCare, manages the contracts, and "control and

decision making responsibility" reside with Alutiiq, not ResCare. At each of the four JCCs, the Center Director — an ***Alutiiq employee*** — reports directly to the Director of Operations of Alutiiq Youth Services ("AYS"),[13] who in turn reports to AYS's Vice President of Operations.

The Draft Report neglects to consider Alutiiq's chain of command or management structure, nor does the Draft Report indicate how ResCare's participation as a subcontractor under the contracts would allow ResCare to control the performance of the contract or of Alutiiq. Alutiiq — not ResCare — is in charge, with the sole power to exert control over the project itself. Indeed, since its inception, AET's and APS's one and only line of business has been to operate Job Corps centers, and the experience they bring is a substantial factor in the success of the Job Corps centers they manage. AET and APS are simply not the passive, pass-through entities that the ostensible subcontractor rule was meant to prevent.

D. Draft Report Fails to Recognize the Importance of Alutiiq Utilizing a Small Percentage of ResCare Employees for the JCC Contracts.

The Draft Report fails to recognize another important factor that strongly weighs against an ostensible subcontractor finding: the fact that ResCare provides only a small percentage of the employees under the JCC contracts, with Alutiiq instead employing the vast majority. The ostensible subcontractor rule is generally inapplicable where the subcontractor performs well under half of the contract work. *See InGenesis*, 2013 SBA LEXIS 5, *33-34 (finding ostensible subcontractor rule inapplicable where subcontractor employed just under half of employees); *Size Appeal of TCE Inc.*, SBA No. SIZ-2008-09-05-119, 2008 SBA LEXIS 152, *22 (2008) (same). In fact, OHA has held that, even in cases where the subcontractor is performing a greater percentage of the work, this does not in and of itself warrant a determination that the ostensible subcontractor rule has been violated. In *Size Appeal of Pavco, Inc.*, SBA No. SIZ-1542, 1982 SBA LEXIS 15 (1982), 75 percent of the contract was subcontracted and yet no affiliation was found. Similarly, OHA has found no unusual reliance upon a subcontractor, and hence no violation of the ostensible subcontractor rule, where a subcontractor performed up to 80 percent of the contract. *Size Appeal of Swepco Corp.*, SBA No. 1449, 1981 SBA LEXIS 42 (1981); *see also Size Appeal of Contra Costa Elec., Inc.*, SBA No. SIZ-1142 (1978) (no unusual reliance even though subcontractor performed 73 percent of the contract).

[13] AYS is the division of Alutiiq, LLC that oversees AET's and APS's Job Corps contracts. *See https://www.alutiiq.com/capabilities/youth-services/.*

In this regard, it is important to note that, at all four of the JCCs at issue, Alutiiq employs no less than 65% of the employees. At the Bamberg JCC, for example, Alutiiq's proposal indicated that ResCare would fill only 22.49 percent of the positions (23.0/102.27).[14] The percentage of work being performed by ResCare is thus much smaller than the percentage performed in the OHA decisions noted above and in other, similar cases where OHA found that the prime contractor was *not* unusually reliant upon the subcontractor. Furthermore, as discussed previously, Alutiiq both manages and supervises the work performed by its and ResCare's employees. As a result, the Draft Report's conclusion that Alutiiq is unduly reliant upon ResCare — when ResCare is performing a relatively small percentage of the overall work and employs a relatively small percentage of the overall employees — is incorrect.

E. The Draft Report Fails to Recognize Another Critical Distinction in Comparing the Alutiiq JCC Contracts With the *Turner* JCC Contract: The Presumptive Validity of the Award.

The Draft Report also fails to consider the fact that, unlike in *Turner*, the contracting officer has already awarded the JCC contracts at issue, and Alutiiq has been performing them for years. Although a contracting officer may take action even after contract award, federal regulations presume the validity of the award once it is made. *See* FAR 19.302(g)(2) (stating that "if an award was made before the time the contracting officer received notice of the appeal, the contract shall be presumed to be valid"); *Chapman Law Firm v. United States*, 63 Fed. Cl. 25, 36-37 (Fed. Cl. 2004) (noting presumption of validity following contract award). This presumption promotes the recognized interest of allowing contractors "to begin work on a Government project without fear of post-award rescission." *See Taylor Consultants, Inc. v. United States*, 90 Fed. Cl. 531, 544 (Fed. Cl. 2009); *see also Mid-West Constr., Ltd v. United States*, 181 Ct. Cl. 774, 387 F.2d 957, 963 (Ct. Cl. 1967) (recognizing "the serious risk of after-award cancellations resulting from the Government's interpretation of the regulation would not only be detrimental to contactors but would work to the disadvantage of the Government's procurement activities").

The Draft Report fails to account for this presumption of validity. Such a presumption — especially in light of the other key differences discussed above — further refutes the Draft Report's finding that Alutiiq may have violated the ostensible subcontractor rule based on the mistaken impression that that the four JCCs at issue and the Turner JCC are sufficiently comparable. They clearly are not.

[14] Bamberg FRP at 39. ResCare currently fills just 19.56% of the positions at the Bamberg JCC. *See* 2013 Bamberg Organization Chart.

F. The Draft Report Fails to Recognize Significant Developments in the Law Following the *Turner* Decision.

As discussed above, the Draft Report relies exclusively upon a single OHA decision from 2011 (i.e., *Turner*), which has since been modified by subsequent decisions. Nevertheless, the Draft Report makes no mention of any decisions subsequent to *Turner* and fails to recognize how the applicable law has changed since *Turner* was decided. In fact, several recent OHA decisions have addressed the ostensible subcontractor rule with respect to various Alutiiq entities. *See Alutiiq Pacific*, 2013 ODRA LEXIS 4; *Serrato*, 2012 SBA LEXIS 58. Despite the obvious relevance of such decisions, however, the Draft Report fails even to reference them. As discussed below, these and other OHA decisions demonstrate that the four JCC contracts at issue do not violate the ostensible subcontractor rule.

1. The Three Factors Required For An Ostensible Subcontractor Finding are Not All Satisfied.

Since OHA's decision in *Turner*, a number of cases have clarified that many of the factors discussed in *Turner* are no longer relevant, or are at least less important than other factors. As noted in a decision from 2013, an ostensible subcontractor relationship will more likely be found when the facts show a subcontractor will exercise substantial control over the project due to the following:

> (1) the use of the subcontractor's personnel in key positions, (2) the use of substantial numbers of subcontractor personnel in rank and file positions, and (3) the use of the subcontractor to perform work that is 'primary and vital' to contract performance.

Protest of Alutiiq Pacific LLC, No. 12-ODRA-00627, 2013 ODRA LEXIS 4, *80-81 (2013) (citation omitted). In fact, a recent OHA decision —written by the same judge who decided *Turner* —has clarified that "the holding in [*Turner*] was based upon all three factors, ***taken together***, not merely upon the fact that the challenged concern was subcontracting the training function." *Serrato*, 2012 SBA LEXIS 58, *25 (emphasis added) (finding that the ostensible subcontractor ruling did not apply because — unlike in *Turner* — "all three factors are not present in this case").

Another post-*Turner* decision clarified that the ostensible subcontractor is considered inapplicable where, as here, a contractor has previously demonstrated the ability to perform the contract, will handle the majority of the overall work, and will manage the contract. *See, e.g., Size Appeal of CymSTAR Servs., LLC*, SBA No. SIZ-5329,

2012 SBA LEXIS 29, *32 (2012) ("Where a concern has the ability to perform the contract, will perform the majority of the work, and will manage the contract, the concern is performing the primary and vital functions of the contract, and there is no violation of the ostensible subcontractor rule.").

As in *Serrato* — and unlike in *Turner* — all three of the primary factors are not present with respect to the four JCCs at issue: Alutiiq has extensive experience in the subject area of the procurement, and it provides nearly all of the key employees. As a result, at most, only *one* of the three factors noted in *Turner* is even potentially present, which precludes application of the ostensible subcontractor rule.

2. Serrato & The Analysis of Primary and Vital Contract Functions

The conclusion set forth in the Draft Report that Alutiiq's relationship with ResCare at the four JCCs may have violated the ostensible subcontractor rule is based almost entirely on the fact that ResCare performs most of the academic and career technical training. According to the Draft Report, Alutiiq did not perform "primary and vital" contract functions because "ResCare personnel would have comprised the majority of the staff for academics and career technical tasks."[15] The Draft Report, however, takes an overly narrow — and improper — view of the "primary and vital requirements" of the contract, especially in light of recent OHA decisions discussed below. Contrary to the Draft Report's determination, Alutiiq did indeed perform "primary and vital" functions at the four JCCs at issue; specifically, its operation of the JCCs, its provision of support services in a safe setting, its training of students in life skills, and its performance of the social development component of the contracts.

Among other flaws, the Draft Report's conclusion overlooks the significance of the OHA's 2012 *Serrato* decision. In *Serrato,* OHA analyzed a JCC contract proposal and effectively overruled *Turner*'s holding concerning the primary and vital requirements of a JCC. The OHA ruled in *Serrato* — one year after its decision in *Turner* — that "the purpose of the [Job Corps] Center is not merely academic training, but, in effect, ***the operation of a large educational institution providing support services in a safe setting and training the students in life skills as well as technical skills***." 2012 SBA LEXIS 58, *21 (emphasis added). Contrary to the holding in *Turner* (and the implication of the Draft Report), requirements such as providing training in life skills, support services, and maintaining a safe setting are not mere "ancillary tasks" but are instead primary and vital components of the JCC contracts. *Compare Turner*, 2011 LEXIS 21, at *35, *with Serrato*, 2012 SBA LEXIS 58, *21-25. Alutiiq alone is responsible for such services at all four of

[15] Draft Report at p. 10.

the JCCs at issue, and there is thus no reason to believe that OHA would today hold that Alutiiq is not performing the contract's primary and vital requirements.

As discussed previously, Alutiiq manages, controls, and operates the JCCs with its own employees; the role of ResCare, in contrast, is quite limited with respect to the overall management and operation of the JCCs. Further, the JCCs are *residential* centers, and the residential living component of the contract — as provided by Alutiiq, not ResCare — is vital to the operation of the contracts. Additionally, Alutiiq, not ResCare, provides the "support services" essential to the operation of such a large educational institution, and it is Alutiiq that ensures the safety of that setting.[16] Alutiiq, not ResCare, also provides training in "life skills" to the students at the JCCs in order to complement their newly-acquired technical skills.[17] Indeed, although the Draft Report focuses entirely on the academic and career technical training, the solicitation for the JCC contracts identifies various other vital components (all of which are performed by Alutiiq):

- Provide social, employability and independent living skills training.
- Provide health care, counseling, and other support services on an individualized needs basis.
- Conduct program operations in a setting that is clean, well maintained, and safe.
- Provide support that prepares graduates to maintain long-term attachment to the labor market or educational opportunities.
- Integrate center operations with the local workforce development systems, employers, the business community, and community-based organizations.[18]

The Draft Report, however, provides no consideration of Alutiiq's operation of the JCCs, its performance of the foregoing components, or how such services compare to the services provided by the prime contractor in *Serrato*. Such consideration is critical for purposes of analyzing the "primary and vital" functions of the JCCs, and the Draft Report's exclusive focus on academic and career technical training to the exclusion of other equally vital functions performed by Alutiiq is clearly improper in light of *Serrato*.

[16] *See* Cleveland SR at A2; Bamberg FRP at 39; Westover SR at A2; Northlands SR at A2.

[17] *Id.*

[18] *See, e.g.*, Contract No. DOLJ10QA00002 at 6 (Westover JCC Contract).

Furthermore, the Draft Report's analysis overlooks another "primary and vital" function Alutiiq provides: Alutiiq is also solely responsible for the social development component of the contract, which OHA has held to be no less important than the academic and career technical training components. In *Serrato*, OHA expressly rejected the argument that a prime contractor that had subcontracted the academic training portion of a JCC contract would not be performing the contract's primary and vital requirements. OHA observed:

> Serrato [the prime contractor] will be performing entirely the Social Development portion of the contract, not merely providing a clean and safe facility, but teaching students to become stable, contributing and productive employees. Most of the students will be residential students and receive, while residents, ***comprehensive training to learn self-management, personal responsibility, and community and independent living skills***. The counseling from the Resident Advisors, and the recreational activities are all designed to assist the students in their career and personal development. ***This is an important part of the contract***, and Serrato will provide 50 employees to perform it. Accordingly, it is not true that HYS's performing the academic training means that Serrato is not performing the primary and vital functions of the contract.

Id. at *24-25 (emphasis added). OHA thus does not consider the Social Development component of a JCC contract to be ancillary; on the contrary, *Serrato* makes it clear that such services are primary and vital contract functions — yet the Draft Report neglects them entirely in analyzing the JCC contracts at issue.

Since Alutiiq, like the prime contractor in *Serrato*, is not only providing support services at the JCCs but also "performing entirely the Social Development portion of the contract," Alutiiq is unquestionably performing primary and vital contract functions. Indeed, Alutiiq also operates and manages the JCCs, provides the key employees, provides the overwhelming majority of the employees, performs support services, runs the residential program, and provides other important services under the JCC contracts. In light of the breadth of its role, it is clearly erroneous for the Draft Report to find that Alutiiq appears unusually reliant on its subcontractor and may not be performing primary and vital functions. Instead, a complete analysis of Alutiiq's role under the contracts at issue and recent OHA jurisprudence results in a clear and obvious conclusion: there is no legal or factual support for the Draft Report's finding that ResCare may be an ostensible subcontractor under any of the four JCC contracts reviewed, and the Draft Report errs in so finding.

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III. REGARDLESS OF THE OUTCOME, A POST-AWARD DETERMINATION BY THE SBA REGARDING THE OSTENSIBLE SUBCONTRACTOR RULE WILL HAVE NO PRACTICAL EFFECT AND IS THUS IMPROPER.

The Draft Report recommends that ETA approach the SBA "for review and guidance" regarding a potential violation of the ostensible subcontractor rule. SBA regulations state that post-award protests are rarely considered and are only appropriate where a protest would have "a practical effect" or be "meaningful." As set forth by SBA's regulations, in pertinent part:

> SBA will not normally consider a post award protest. SBA may consider a post award protest in its discretion ***where it determines that a protest decision after award would have a practical effect (e.g., where the contracting officer agrees to terminate the contract if the protest is sustained).***

13 CFR 124.1008; *see also* 48 CFR 19.305(d) ("SBA may consider a postaward protest in its discretion where it determines that an SDB determination after award ***is meaningful*** (e.g., where the contracting officer agrees to terminate the contract if the protest is sustained).") (emphasis added).[19] The Draft Report's recommendation, therefore, is premature and omits a preliminary question that ETA should address before it requests a determination from the SBA: whether an ostensible subcontractor violation, if found, will actually have any practical effect. Even if the JCC contracts violated SBA size requirements, such outcome will prove inconsequential (and a waste of time and resources) if the ETA Contracting Officer nevertheless elects not to terminate the contracts and/or the Government is unable to recover any resulting damages. In fact, under such circumstances, post-award involvement of the SBA is not only a wasteful endeavor but may also be legally improper.

Accordingly, before recommending that ETA involve the SBA in a post-award ostensible subcontractor determination, the Draft Report should have recommended that ETA first consider whether its contracting officers would actually elect to terminate the JCC contracts in the event that any filed protests are ultimately sustained, or whether the Government has any reasonable means to potentially collect damages from Alutiiq if a violation is found. If not, a post-award protest is of no practical effect and, as discussed below, would be wasteful and improper for ETA to pursue (or for the SBA to consider).

[19] Although this provision is specific to Small Disadvantaged Business ("SDB") determination, the "no practical effect" rule is equally applicable to size protests and other similar SBA protests.

A. Regardless of Any Ostensible Subcontractor Violation, the Contracting Officer Has Discretion in Whether to Terminate an Ongoing Contract.

Before filing a post-award protest with the SBA (or otherwise requesting a determination from the SBA regarding potential size issues), ETA should consider whether — even if the SBA believes that the JCC contracts may have violated the ostensible subcontractor rule — its contracting officers would actually consider terminating the JCC contracts at issue. Regardless of whether the JCC contracts were improperly awarded, SBA regulations set forth that the Contracting Officers have discretion to terminate the contracts or allow the contracts to proceed according to their terms:

> When a concern is found to be other than small under a protest concerning a size status representation made in accordance with the clause at 52.219-28, Post-Award Small Business Program Representation, a contracting officer may permit contract performance to continue, issue orders, or exercise option(s), because the contract remains a valid contract.

48 CFR 19.302(k). In light of the fact that the JCC contracts will be nearly or fully complete by the time that any final determination is reached (by the SBA and/or OHA), the Contracting Officer may decide that — irrespective of the outcome — the JCC contracts are already too far along to warrant termination and solicitation of a new contractor. Similarly, the Contracting Officer may determine that, because Alutiiq has performed well under the contracts and a change at this stage of the contracts will disrupt the JCCs, termination is not advisable. Under either scenario, the outcome of a post-award protest to SBA would thus be of no consequence, rendering any such protest or post-award determination of no practical effect.

Indeed, post-award protests filed by a contracting officer are exceedingly rare, especially where the concern has already begun performance under the contract. In the last 30 years, OHA decisions reflect that there have been only 17 post-award protests filed by contracting officers involving the ostensible subcontractor rule, and *none* of these protests were filed more than a few days after contract award (whereas, by comparison, Alutiiq has been performing the JCC contracts for *years*). A decision by ETA to effectively pursue a protest at this stage of the contracts at issue would thus not only be unwarranted but also unprecedented.

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B. Regardless of Whether ResCare Was an Ostensible Subcontractor, the Government Cannot Recover Any Damages Against Alutiiq In Light of Applicable Safe Harbor Provisions.

Section 1341 of the Small Business Jobs Act of 2010 creates the so-called "Presumed Loss Rule," which establishes "a presumption of loss to the United States based on the total amount expended on the contract, . . . whenever it is established that a business concern … willfully sought and received the award by misrepresentation" of size status. Although the Draft Report does not expressly refer to the Presumed Loss Rule, the Draft Report implies that the Rule is potentially applicable by making the following statement: "[i]f SBA determines any of these 4 contracts-subcontracts violated the ostensible subcontractor rule, up to $126.5 million in government funds set aside for small businesses were not used as intended." (Draft Report at p. 5.) The Presumed Loss Rule, however, is *not* applicable to any of the JCC contracts; to the extent that the Draft Report asserts that the Government may recover damages against Alutiiq under the Presumed Loss Rule, such belief is false in light of recently-enacted SBA regulations that effectively create a safe harbor for contractors such as Alutiiq.

On August 27, 2013, the SBA issued regulations implementing a limitation of liability provision that sets forth various exceptions under which the Presumed Loss Rule would not apply. According to these recently-enacted regulations, the Presumed Loss is inapplicable in cases of ***"unintentional errors, technical malfunctions, and other similar situations that demonstrate that a misrepresentation of size was not affirmative, intentional, willful or actionable."*** 13 C.F.R. § 128.108(d) (emphasis added). As a result, even where a contractor is found to violate the ostensible subcontractor rule, the Presumed Loss Rule would have no effect where the contractor's violation was neither intentional nor willful.

Here, there is no evidence whatsoever that Alutiiq intentionally misled the Contracting Officer, or that Alutiiq had any indication when it submitted its proposals for the contracts in question that it might be in violation of the ostensible subcontractor rule. The lack of any such recognition seems readily apparent considering that (i) the decision in *Turner* was issued after Alutiiq had already submitted its proposals, and (ii) Alutiiq fully (and accurately) disclosed the role of ResCare under each and every proposal. In fact, the evidence cited in the Draft Report contradicts any finding that Alutiiq's willfully violated this rule. As noted specifically in the Report, Alutiiq fully disclosed to ETA the proposed subcontracting relationship with ResCare in all four of the JCCs at issue.

Accordingly, the evidence and factual background identified by the Draft Report can support only the following two possibilities: (1) that Alutiiq interpreted the

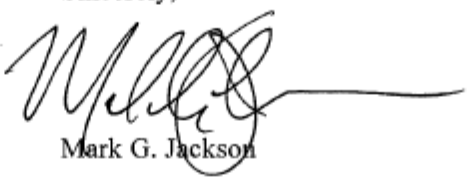
requirements of the ostensible subcontractor rule differently than does the Draft Report; and/or (2) that even though the *Turner* decision had not yet been issued, Alutiiq reasonably believed that no matter how *Turner* was decided the relationship it proposed with ResCare with respect to the four JCCs at issue was substantially different than its relationship with ResCare under the Turner proposal. Either way, neither of these two possibilities supports application of the Presumed Loss Rule, and the Presumed Loss Rule is thus inapplicable and irrelevant to the JCC contracts regardless of whether an ostensible subcontractor violation occurred.

Since the Government is therefore unable to recover any damages from Alutiiq, irrespective of any size violation, filing a protest with the SBA on this issue would be of no consequence and a waste of time and resources. Moreover, as noted previously, the SBA generally does not consider or recommend post-award protests that would be of no "practical" or "meaningful" effect. *See* 13 CFR 124.1008; 48 CFR 19.305(d). Absent the potential recovery of any damages, there is simply no "practical" or "meaningful" reason for ETA to seek a determination from the SBA concerning potential ostensible contracting violations. The Draft Report recommendation that ETA seek such a post-award determination is therefore ill-advised.

* * *

In conclusion, the Draft Report violates generally accepted government auditing standards, and, for that reason alone, should be ignored. Indeed, even if properly performed, an audit would not have found apparent violations of the ostensible subcontractor rule in any of the four contracts in light of the current state of the law and the salient differences between the four JCCs at issue and the Turner JCC. Moreover, the recommendation to refer these four contracts to SBA for review is improper because such a review will have no practical effect. For any and all of those reasons, as discussed above, the findings and recommendations of the Draft Report are improper and incorrect — and should be ignored.

Sincerely,



Mark G. Jackson

cc: Amy Shimek, Afognak Native Corporation & Alutiiq, LLC