



Protecting Proprietary Data *without*
Compromising Regulatory Compliance



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Joint ventures are becoming more popular in today's government procurement marketplace, but they face unique challenges. The use of business services integrators can help.



In recent years, the U.S. federal government vertical market has been experiencing a transformation. Contractors are experiencing a high incidence of “bundled” procurement actions initiated by the government. This change is apparently the government’s attempt to create “best value” by streamlining its procurement processes, improving the efficiency of contract management, and reducing costs.

In parallel, the government’s procurement workload has increased due in part to the need to outsource more of its services. In response, the government has turned to bundled procurement actions as a means to procure more services with a smaller, more efficient government workforce using fewer prime contractors. The result is a reduced number of contracts for the government to oversee and manage.

The traditional contractor community response to the bundling of procurement initiatives via prime contractor/subcontractor relationships has lost momentum in favor of special business partnerships such as joint ventures (JVs) and teaming agreements. To carry out the work, companies create new business structures in the form of limited liability corporations (LLCs). Contractors now offer JV/LLCs as a “best value” solution

to their customer (the federal government), which provides for more streamlined contract management and reduces costs when compared to the traditional “tiered” prime/sub relationships.

It is also becoming more common for the JV or LLC not to have employees. In so doing, the founding parties also enter into subcontractor agreements with the JV/LLC and/or other subcontractors to fulfill the contract requirements. This form of business unit is commonly referred to as an “unpopulated LLC,” which creates a best value for the government because the business entity it contracts with (i.e., the unpopulated LLC) has no significant, if any, indirect costs (e.g., overhead or general and administrative costs). Therefore, the contracting entity predominantly consists of only direct costs (i.e., subcontractor costs).

Essentially, *all* costs—even minimal indirect costs—of the unpopulated LLC can be considered *direct* costs since the entity was formed to perform a single contract (i.e., a single cost objective). Since there are little to no tiered or value-added indirect cost burdens, the government sees the total direct cost concept as a best value.

The win rates of these special business entities have been well documented. According to a recent government business survey by Grant Thornton LLP,¹ survey participants reported a 30 percent win rate from proposals for non-sole-source business.

The Challenge for Unpopulated LLCs

One of the challenges for companies forming these special unpopulated LLCs is finding a solution to protect their business-sensitive and proprietary information from each other during the procurement life cycle. Each phase of the life cycle (i.e., procurement action, contract performance, and contract closeout) has unique challenges with regard to business-sensitive and proprietary data protection.

As if protecting proprietary data from each other weren't enough (after all, these

“parties” are most often competitors before forming the unpopulated LLC business entity), parties to an unpopulated LLC must also satisfy the requirements of the *Federal Acquisition Regulation (FAR)*, audit procedures (from the Defense Contract Audit Agency [DCAA]), and contract compliance issues of “transparency, accountability, and reportability” (T-A-R) of the contracting entity’s (i.e., the unpopulated LLC’s) financial and contract performance data (earned value [EV]).

In an unpopulated LLC, remember, there are no employees. All the “auditable” source data resides at the “party” (subcontractor) level. How will the unpopulated LLC, whom the federal government has contracted with, satisfy its compliance requirements if all of the source data is held at the party (subcontractor) level and still maintain company specific confidentiality? Establishing one of the parties as the “managing party” would fulfill the government T-A-R compliance requirements. However, the “managing party” approach would compromise the intra-party confidentiality of business-sensitive and proprietary information.

In the heretofore traditional prime/sub relationship, business sensitive and proprietary information is controlled at the individual prime/sub level and the government is provided the right to audit down through the tiered subcontractor levels via the flow-down clauses in the subcontracts or procurement action provisions. This “flow-down” mechanism provides the T-A-R path to the source data at all times during the procurement life cycle (i.e., pre-award, concurrent, and closeout).

How does the unpopulated LLC provide the government T-A-R access to source cost and pricing data—such as direct labor, fringe, overhead, general and administrative, material handling, services centers, etc.—of the subcontractors without compromising confidentiality between the parties in the absence of any means to manage the audit process and the flow of information (recall that the unpopulated LLC has no employees)?

Solution

One preferred solution in the unpopulated LLC business environment is to outsource the services to a third party that specializes in the management and protection of individual parties’ data while providing the T-A-R requirements throughout the procurement life cycle. In the employee benefits environment, for example, companies have found it to be very cost effective to outsource the essential administrative functions and statutory reporting of a 401(k), ESOP, or Section 125 plan to third-party administrators (TPAs) rather than to self-perform. In the contracting environment, the specialized TPA service providers are referred to as “business services integrators” (BSIs). See **FIGURE 1** on page 56.

The primary roles of the BSI in the unpopulated LLC business contracting environment are to:

- Maintain the individual party’s data confidentiality while seamlessly providing the required T-A-R for government compliance,
- Administer the terms and conditions of the contract with the federal government per the unpopulated LLC operating agreement,
- Manage the subcontracts (both the “party” subcontractors and other subcontractors), and
- Closeout the contract with subcontractors and the government and fulfill any requirements that survive the closeout.

The Procurement Action

The BSI plays a critical role during the procurement action phase. Cost and pricing data is developed on behalf of the unpopulated LLC member companies to fulfill the procurement response requirements (generally submitted in the cost proposal). The parties are not given access to the proposing entity’s source data other than their own. Each party provides cost and pricing data to the BSI. The BSI then develops the pricing model and cost proposal, which

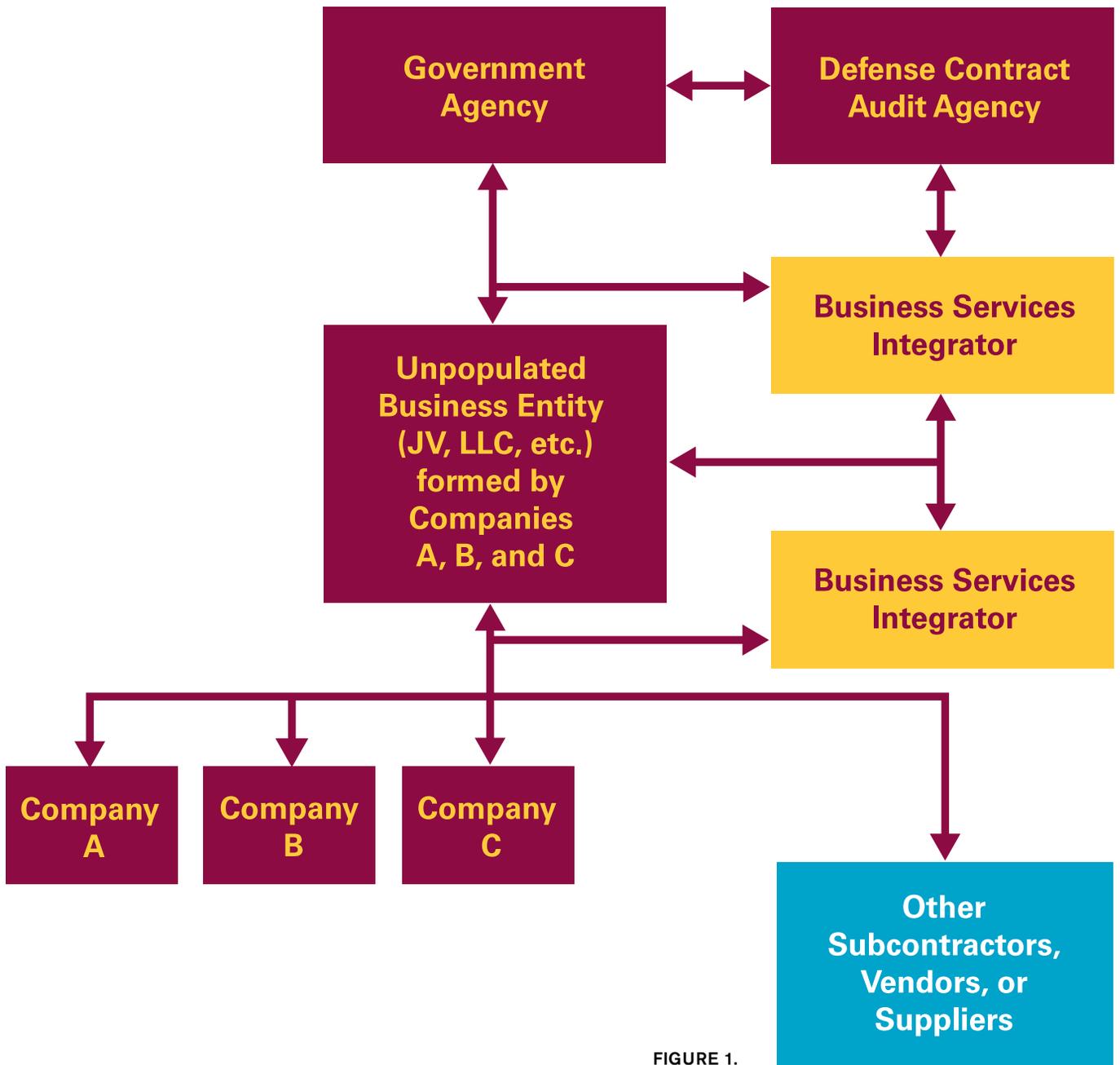


FIGURE 1.

can be shared with parties for marketing decision-making. However, the components of the cost proposal model are kept confidential. If the federal government requests or requires a pre-award audit of the cost proposal, the BSI is in the critical position to support the pre-audit process without the parties needing to be involved or with intraparty confidentiality being compromised.

Contract Performance

During contract performance, the BSI serves as both the “gatekeeper” and “administrator” of the contract. The BSI supports the unpopulated LLC’s technical performance of the contract by providing the “back office” accounting, project controls, and subcontract management and administration in an outsourced environment. With the BSI providing these business administrative functions, the unpopulated LLC maintains

compliance with the T-A-R requirements imposed by the contract and FAR provisions. The unpopulated LLC parties, therefore, are free to focus on the technical performance of the contract. The party companies continue to maintain and run their existing job cost accounting and project control systems. Through the BSI, they can now integrate their individual company information with the other parties.

Concurrent audit requirements are also managed by the BSI in order to provide the access and T-A-R to the government while limiting and controlling the dissemination of business-sensitive and proprietary data between the parties. In this way, statutory and contractual audit requirements are assured and competitive data is secured.

Contract Closeout

When contract performance is complete, it is time to closeout the contract. Consideration must be given to the potential for post-award audit support and records retention/destruction after performance is complete and member company employees have moved on to the next project. The BSI now serves as the legacy repository in order to meet the federal requirements for access to records (generally three years after submittal of final invoice). Since the BSI has been involved with the unpopulated LLC's data from its inception and throughout its performance and closure, the archiving of this information becomes a relatively simple matter.

BSI Discriminators

A BSI is a value-added asset to a newly formed unpopulated LLC. The BSI acts as the administrative arm of the employee-less company by providing the entire essential "back-office" services, thus allowing the parties to do what they do best.

Using a BSI in an unpopulated LLC offers the following advantages in a highly competitive and cost-conscious business environment:

- Secure business-sensitive and proprietary data protocols;
- Government T-A-R compliance;
- Direct cost efficiency through the elimination of:
 - Duplicative efforts; and
 - Idle indirect staff capacity (general and administrative), which increases profits for parties;

- Scalable solutions;
- Seamless integration of accounting, project controls, and contract administration; and
- Survivability of legacy records.

What to Look For in a BSI

When forming an unpopulated LLC, companies should look for certain qualities and attributes when deciding to engage the services of a BSI. At a minimum, the BSI should have extensive experience with:

- The "cradle-to-grave" government procurement process;
- Job cost and financial accounting system implementation and management;
- Contract/subcontract administration and management;



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The win rate jumps to almost two-in-three (65 percent) when the company establishes a special business unit, such as a joint venture or a limited liability corporation, to bid the work.

- Audit environment liaison and management support;
- Project management, scheduling, cost management, project control performance measurement using earned value principles;
- Seamless integration of earned value metrics with job cost accounting and financial systems;
- Government closeout process requirements; and
- Coordinating/managing multiple company entities.

Conclusion

Choosing the right BSI is as important to the success of the unpopulated LLC as “joining hands” with the right parties in the new venture. Well-thought-out strategies and planning in the beginning for the full procurement life cycle will go a long way in ensuring a successful and profitable venture. **CM**

ABOUT THE AUTHORS

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ENDNOTE

1. Grant Thornton, LLP, *14th Annual Government Contractor Industry Highlights Book*, 2008.