



**STATEMENT OF
DAVY LEGHORN, ASSISTANT DIRECTOR
NATIONAL VETERANS EMPLOYMENT AND EDUCATION DIVISION
THE AMERICAN LEGION**

BEFORE THE

**SUBCOMMITTEE ON INVESTIGATION, OVERSIGHT AND REGULATION
COMMITTEE ON SMALL BUSINESS
UNITED STATES HOUSE OF REPRESENTATIVES**

ON

**“VETS FIRST? AN EXAMINATION OF VA’S RESOURCES FOR VETERAN-OWNED
SMALL BUSINESS”**

JUNE 7, 2018

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Chairman Kelly, Ranking Member Adams, and distinguished members of the Subcommittee on Investigation, Oversight and Regulation, on behalf of National Commander Denise Rohan and the two million members of The American Legion, we thank you for the opportunity to testify at this hearing on the challenges facing veteran-owned small businesses operating as wholesale distributors under the Department of Veterans Affairs’ (VA) Medical Surgical Prime Vendor-Next Generation (MSPV-NG) program. This issue is of the utmost importance to The American Legion as it directly affects the care of our most vulnerable constituents: veteran patients.

The American Legion wants what is best for veterans. We believe VA is the most qualified to deliver healthcare services to veterans and we want them to step up to their responsibilities. The intimation that the adherence to the Vets First procurement priorities could potentially cause “catastrophic disruption”¹ to the healthcare supply chain is markedly false.

The American Legion supports the Supreme Court Decision in *Kingdomware Technologies, Inc. v. United States*,² and opposes any attempt to subvert or sidestep the application of the rule-of-two in VA’s Vets First contracting program. In 2016, The American Legion passed Resolution No. 154³ to advocate for a reasonable number of federal contracts to be set-aside for businesses that are owned and operated by veterans. MSPV-NG reduces federal contracts for veteran-owned businesses, which is of concern to The American Legion.

Soldiers’ homes and veterans’ hospitals date back to 1866. VA does not provide supporting data or research for their assertions in the Class Justification and Approval for Other than Full and Open (J&A) document.⁴ There is no quantitative evidence showing that the mismanagement of a singular contracting vehicle could potentially result in “catastrophic disruption” to a 150 year old healthcare infrastructure system. If one contracting program has the ability to cripple an entire federal agency, the question becomes whether such a contracting program should exist.

¹ Exhibit A

² *Kingdomware Techs., Inc. v. United States*, 579 U.S. (2016).

³ Resolution No. 154: Support Reasonable Set-Aside of Federal Procurements and Contracts for Businesses Owned and Operated by Veterans.

⁴ Exhibit A

VA's proposition to avoid this disruption is to grant a two-year period where companies and manufacturers will determine what supplies VA Medical Centers' need, moving away from the current clinician-driven process. Privatizing the functions of VA's office of Acquisitions and Logistics' Strategic Acquisition Center (SAC) presents a significant conflict of interest, and inflicts great harm to veteran owned small businesses. The American Legion wants to work with Congress and VA to find empirical evidence and better understand the underlining rational and private sector solution, so another will not be required.

Background

Public Law 106-50⁵ made all federal agencies stakeholders in supporting veterans' entrepreneurship. A subsequent law passed in 2006⁶ provides VA with the authority in setting higher agency standards for service-disabled veteran owned small business (SDVOSB) and veteran owned small business (VOSB) set-asides. The Veterans Benefits, Health Care, and Information Technology Act of 2006 also included a provision requiring VA to set-aside contracts for veteran-owned firms so long as the rule-of-two⁷ is satisfied. A new procurement hierarchy within VA was created, which places the highest priority with SDVOSBs followed by VOSBs. VA refers to this program as the Veterans First Contracting Program (Vets First). The Supreme Court's *Kingdomware* Decision; fine-tuned the Vets First contracting policy within VA. The Court held that the rule-of-two was not limited to those contracts necessary to fulfill the Secretary's goals under Vets First contracting program and applies to orders placed under the Federal Supply Schedule.

In 2018, VA relaunched the legacy MSPV contracting program. MSPV-NG would effectively remove 40 percent of the medical supply procurement from the rule-of-two. The current MSPV-NG program utilizes four regional prime vendors. The list of permissible medical supplies they sell on MSPV-NG is determined by a master-list of items, prices and suppliers, commonly referred to as, "the formulary." The formulary is created by running a procurement-like process to discover the number of businesses who can meet the standard and offer the lowest prices.⁸ VA believes low-vendor responses, bid protests and cancelled solicitations are the reasons why there are only 7,800 items on the formulary.⁹

According to a SDVOSB distributor from South Carolina, who responded to these solicitations, VA does not mention they utilize short-window solicitations that were open market, allowing bidders to choose from 150 items. As such, distributors only bid on items they can earn a profit on. This resulted in a situation where there are over 200 bids on a handful of high-margin items, and zero bids on items with a lower or no profit margin.

In another solicitation, VA only ran the process for Schedule 6500 series medical equipment, as opposed to all the MSPV-NG products. Many veteran owned distributors also sell their products

⁵ The Veterans Entrepreneurship and Small Business Development Act of 1999.

⁶ The Veterans Health Care, Benefits and Information Technology Act of 2006; PL 109-461.

⁷ 38 U.S.C. 2187(d).

⁸ Exhibit A.

⁹ Ibid.

through the General Services Administration's (GSA) online government purchasing service;¹⁰ Before they can submit their bids, the veteran owned business must update their prices and/or add 6500 series products to their schedule. Distributors began the process of adding 6500 series items to the GSA Schedule, but the solicitation ended before they could complete the update. This contributed to why VA did not receive an adequate amount of sample bids for adding items to the formulary.

Through these types of solicitations, VA found the justification needed to create the proposals in the J&A. According to the J&A, VA plans to move 40 percent of their contracting dollars in medical supplies through the MSPV-NG program, consequently bypassing the rule-of-two, disregarding the Supreme Court ruling in the *Kingdomware* Decision.

Many American Legion members who are also small business owners agree that VA's proposals in the J&A would systematically unseat veteran owned small businesses as distributors for manufacturers and give all the selling capabilities to the prime vendors. This is bad for veteran owned small businesses and contrary to The American Legion's call for a reasonable amount of purchases be set aside for veteran owned small businesses in federal procurement.

The American Legion's Small Business Taskforce & Programs

The American Legion focuses our small business programing around three core services, Advocacy, Counseling and Events. As a resolution-based organization, we support small business policy that enables our veterans and their spouses to succeed in their entrepreneurial endeavors. Our counseling services assist veteran entrepreneurs with their disability claims and help them obtain SDVOSB or VOSB status under the Vets First contracting program. The American Legion hosts many small business workshops and conferences on an annual basis, connecting our veteran entrepreneurs with other veteran entrepreneurs and business opportunities.

The Small Business Taskforce is a working group of Legion members and small business owners who meet regularly to discuss the state of the veteran small business industrial base. The American Legion relies on Taskforce volunteers to take on advisory roles in our entrepreneurship programs and services and to lend their expertise in small business advocacy. The Small Business Taskforce is the Legion's voice of the veteran entrepreneur.

The Distributor's Role

Traditionally, VA orders supplies directly from distributors. The distributors then ship the items to a prime vendor who consolidates all the orders for delivery and inventory. The prime vendor then ships the consolidated order to the VA medical facility.

Small businesses add value to MSPV-NG. Service-disabled veteran owned small businesses serve as resellers or distributors, and provide locally sourced maintenance, customer service, account management, order tracking and meticulous reporting requirements in federal contracting. When smaller prime vendors do not have space to keep the requisite 110 percent of the MSPV-NG formulary items in stock, they rely on their distributors to warehouse the additional inventory.

¹⁰ "GSA Advantage!," U.S. General Services Administration, June 4, 2018, <https://www.gsa.gov/tools/supply-procurement-ertools/gsa-advantage>

Keeping inventory of formulary items at 110 percent, ensures that the formulary products are always in stock and available to the VA.

Distributors also absorb the extra costs associated with getting the formulary product from the manufacturer. Because the prices are pre-negotiated, the SDVOSBs sustain these costs, making sure their problems are isolated from prime vendors and the VA. Because these prices are not passed up the chain, it saves money for VA and passes the savings to the taxpayer. As prime vendors take over the distributors' role, they would likely markup pricing or fees to recoup the extra costs associated with getting the product from the manufacturer.

Prime vendors offer one-size fits-all solutions to VA Medical Centers (VAMCs); they cannot duplicate what the distributors offer. Distributors have close working relationships with VA medical facilities; they know how their local VAMCs purchase and what it purchases. Distributors always keep certain formulary items in stock to fulfill their local VAMC's needs.

Legion members who are also wholesale distributors have a moral commitment to the veteran patient and VA. There is one SDVOSB from South Carolina that has worked it into their company policy to sell products (not in stock) at a loss to VA at the pre-negotiated prices. They are willing to lose money to get products delivered to the VA on time, because according to them, it's the right thing to do.

Prime Vendors

VA needs an estimated 80,000 itemed formulary to support all of the 167 medical centers. The current 7,800 items on the list are not enough to satisfy VA's demands for supplies.¹¹ Running procurements to build the formulary is tedious work. VA's Office of Acquisition and Logistics' Strategic Acquisitions Center (SAC) has decided to outsource their responsibilities to prime vendors.

Giving prime vendors the authority to decide which items to allow into the formulary is problematic. Several of our small business taskforce members fear that prime vendors could abuse their authority in a way that could render small businesses non-competitive. For example, some prime vendors are also manufacturers of medical supplies, meaning they can potentially shut out other brands and competitors from the formulary and create an unfair advantage.

Recommendation 1

According to the J&A, VA forecasts a "catastrophic disruption" of the VA healthcare supply chain if a substantial amount of contract administration is not given to the prime vendors. The J&A does not mention that retaining contract management and oversight is the key to mitigating risks and preventing developing crises or reference alternative solutions. Accepting the concept that the only solution is to abdicate responsibility by privatizing the procurement of critical supplies, sets an irreversible path for VA to address all of its other problems through privatization as the only alternative.

If VA is looking for a viable solution that meets small business goals, has government certified "fair and reasonable" prices, and is Food and Drug Administration, Trade Agreement Act and Buy-American Act compliant, they should look to the utilization of the GSA's Federal Supply Schedule

¹¹ Exhibit A.

(FSS). The FSS could be an alternative starting point for market research and the basis for moving products on to the MSPV-NG formulary.

Many of the stakeholders agree that GSA is an appropriate entity to run the contract and determine which items, prices and suppliers appears on the formulary. Similarly, many stakeholders also agree that sellers and manufacturers are likely the least appropriate entities to run the contract and should not be given authority to input items on the formulary.

The American Legion believes that VA must not allow prime vendors to decide which medical products are to be added to the formulary. Prime vendors should not be authorized to displace SDVOSBs as distributors. Lastly, VA should use the FSS as the basis for market research when it comes to populating the MSPV-NG formulary.

Recommendation 2

The MSPV-NG program is a part of the MyVA transformation, which puts veterans and their families first. According to the Strategic Acquisitions Center, the cost savings from buying through the MSPV-NG contracting program will be applied to high-priority veterans' programs. The American Legion would like to know which programs specifically and how the savings from the MSPV-NG program will be accounted for.

Some of our SDVOSB distributors are on the GSA Schedule and the VA FSS. SDVOSBs contribute funds back to the government in Industrial Funding Fees (IFF) when they utilize the contracting services of the agency. IFF is trackable. If the aim of the MSPV-NG is to reinvest their savings, The American Legion believes VA can accomplish the same goal by buying from GSA's online government purchasing service or VA FSS contracts.

The Future

Small business distributors fear that they will lose business, when VA's proposal in the J&A is fully implemented. Since the proposal's implementation, prime vendors are already working directly with manufacturers and displacing small distributors from the procurement process.

Subcontracting then becomes the best way for SDVOSBs to tap into MSPV-NG. Unfortunately, subcontracting plans only apply to two of the four prime vendors, and within the last decade, VA has yet to meet their negotiated subcontracting goals with the SBA.¹² Without the bandwidth to track and enforce their subcontracting goals, VA provides little incentive for prime vendors to subcontract to small businesses. The door for SDVOSB inclusion into the MSPV-NG structure is closing.

Compounding all of this is the GSA's implementation of 2017 National Defense Authorization Act's Sec 846,¹³ which directs GSA to establish a program for federal agencies to buy commercial products through commercial e-commerce portals. MSPV-NG prime vendors are not the only businesses abandoning their distributors and resellers. Businesses that sell products to the federal government are already choosing not to stock or not to renew contracts with distributors in

¹² "Department of Veterans Affairs Contracting Scorecard," U.S. Small Business Administration, June 4, 2018, <https://www.sba.gov/document/support--department-veterans-affairs-contracting-scorecard>

¹³ Public law 115-91.

anticipation of the launch of the commercial e-commerce portal. These businesses know that in order to get their products to rank high on an online retail platform, they must pay to stock product with that company.

Additionally, micro-purchases on government charge cards are left out of SBA small business goals. Purchase card abuse is not relegated to the VA This problem exists in every federal agency. VA purchase card abuse was exposed in 2015 and is an admitted and identified issue within the agency.¹⁴ GSA's proposal of raising the micro-purchasing ceiling to \$10,000 overall and \$25,000 for purchases made through the e-commerce portal does nothing to curb purchase card abuse; instead, it practically facilitates it.

Whether national, regional, state or local, SDVOSB wholesale distributors sell to more agencies than just the VA these distributors are feeling the pinch across all federal agencies. This is the climate SDVOSB distributors are operating in and they are very concerned about their future in the government procurement space. All indicators thus far, present a very bleak future. Despite the odds stacked against the SDVOSB distributors, The American Legion remains committed to advocating for their utilization and place within the federal procurement process.

Conclusion

Chairman Kelly, Ranking Member Adams and distinguished members of this critical committee, The American Legion thanks this you for the opportunity to explain the position of our two million members of this organization. Questions concerning this testimony can be directed to Jonathan Espinoza, Legislative Associate, in The American Legion's Legislative Division at (202) 861-2700, or jespinoza@legion.org

¹⁴ "Veteran Health Administration Audit of Purchase Card Use to Purchase Prosthetics," Department of Veterans Affairs Office of the Inspector General, June 4, 2018, <https://www.va.gov/oig/pubs/VAOIG-15-04929-351.pdf>

EXHIBIT A