order to assess whether the "ostensible subcontractor" rule continues to be appropriate in the context of the telecommunications industry as well as the other public utility services industries identified above, which appear to have similar industry characteristics.

Over the past decade, deregulation of the public utility industries identified above has resulted in the open access of certain distribution facilities of public utilities by other firms. This development has encouraged the entrance of new firms in these markets to provide specialized services. For example, in the long distance telephone market a firm (reseller) can purchase bulk access to telecommunication circuits and resell telecommunication services to smaller volume customers. The economic savings from a volume purchase of these circuits by resellers are offered to certain customers who, given their relatively small volume of business or need, could not obtain similar savings by directly obtaining telephone access through the long distance providers. The other two public utility industries under consideration in this proposed rule are also experiencing the emergence of similar business arrangements where other firms utilize the public utility's distribution facilities. In the natural gas industry, open access of interstate pipelines has resulted in a significant change in the marketing of natural gas. Prior to deregulation, 95 percent of natural gas transported through pipelines was owned by the pipeline companies. Today, over 95 percent of natural gas flowing through interstate pipelines is owned by non-pipeline companies. Additionally, open access on a limited basis is now allowed for the provision of electric power, and further modifications to legislative restrictions on the retail sale of electric services are under consideration.

SBA's preliminary assessment of the public utility industries described in this proposed rule is that there may be a legitimate basis to permit resellers of telecommunication services, and other firms that provide public utility services through the lease and use of distribution facilities, to offer their services in the Federal market as they do in the commercial market without running afoul of the affiliation rules. In many instances, these firms may add value to the contract involved and be sound, operating businesses engaged generally in the provision of telecommunications and other public utility services. Moreover, the extensive capital investment necessary to build the distribution facilities associated with

providing one of these public utility services essentially precludes a firm, other than the existing public utility firms, from making such an investment in order to perform a specific Federal procurement or in order to serve small volume commercial customers. In addition, remaining regulatory requirements continue to prohibit or constrain the development of capital facilities by new entrants. As indicated above, deregulation occurring in these public utility industries has made available to other firms the use of distribution facilities of the public utilities on a sub-contractual basis. Unlike other industries, the provision of public utility services is limited to one or a few public utility providers, and new firms that are now able to enter the market do so by leasing the distribution facilities of existing public utilities. Firms in other service industries usually do not depend on the exclusive access to a significant amount of capital facilities of one or a few firms within an industry to provide their services.

As indicated above, SBA is concerned that the effect of the present regulations causing affiliation between a prime contractor and an "ostensible subcontractor," based simply on the leasing of distribution facilities, may now be inappropriate with respect to these specific public utility industries. For example, even though the greatest component of value in government contracts providing telecommunications services may be the utility distribution facilities, it nevertheless may not be appropriate to regard the subcontractor or supplier contributing that component as performing a controlling role on the contract where its responsibilities are limited to the provision and maintenance of those facilities and the prime contractor provides other valuable services. The SBA recognizes that firms that lease and use the distribution facilities of these public utilities generally perform an important and legitimate economic role in the provision of utility services to commercial markets, and the "ostensible subcontractor" rule may unnecessarily constrain opportunities for small business in obtaining Federal contracts for these public utility services. On the other hand, SBA does not wish to create by this exception a situation in which small business prime contractors qualify for small business preferences when they merely are brokers. Thus, the exception would apply only if the prime contractor also contributes meaningful value to the contract. With respect to the concept of meaningful value, SBA has not

attempted to quantify what would constitute meaningful value for purposes of this rule.

The SBA is particularly concerned that the effect of the proposed modification might lead to abuses in the small business preference programs if the modification allows small businesses to act as mere brokers or intermediaries on the behalf of large businesses. To explain further, a small firm acting as a reseller of long distance telephone services might perform several functions, such as consultative services, identification and connection of circuits, problem resolution, and billing services, in providing long distance communication services to its customers. However, these activities may be of such limited significance to the contract as a whole when compared to the services provided by the long distance telephone carrier that the carrier should indeed be properly regarded as a joint venturer of the small firm. One of the primary purposes of the "ostensible subcontractor" rule is to ensure that the benefits intended for small business in obtaining a government contract are enjoyed by that small business and not simply passed through to a large business subcontractor. It is not the SBA's intention to depart from this long-held policy as a result of a modification of the "ostensible subcontractor" rule. Comments addressing this aspect of the proposed rule would be especially beneficial to SBA's deliberations of this

The SBA seeks public comments on this proposal to modify the "ostensible subcontractor" rule. The SBA is particularly interested in obtaining comments which address the following points: (1) The nature of the business relationship between a public utility firm and a firm that leases the public utility's distribution facilities for purposes of reselling public utility services; (2) whether the proposed rule could have an unintended adverse effect on SBA's small business programs by allowing the brokering of services provided by large business; (3) whether a requirement that the prime contractor provide meaningful value to the contract adequately protects against abuse, and if so, how meaningful value should be determined, whether quantitatively or otherwise; (4) whether any modification to the "ostensible subcontractor" rule should be applied to public utility industries in addition to those which have been identified in the proposed rule; and, (5) alternative approaches to this proposed rule that address the issues discussed above.