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Illustration by Chris McKenzie

Uncle Sam wants help

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By [Taylor Lincoln](#)

Some may criticize the federal government for being slow — or unable — to adapt to new technologies. Then again, with the technology economy now suffering from a post-boom slowdown, critics might be relieved that Uncle Sam did not — or could not — rush headlong into the new economy.

"The government is starting to change the way they do business with [the advent of] the Web," says Larry Davis, president of AFW Capital Partners, an investment banking affiliate of Aronson, Fetridge & Weigle, a certified public accounting firm based in Rockville, Md.

"It's starting to happen. But the other shoe has not yet dropped," adds Davis, whose firm is largely involved in mergers and acquisitions among government contractors and companies that want to get into contracting.

Davis views e-commerce — specifically the government's purchase of e-commerce technology — as one of several areas of federal spending that have heated up at a time when government contracting has become an increasingly desirable market.

While companies were busy wowing Wall Street with eye-popping initial public offerings, the federal government's business was


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viewed as staid and unsexy. Now that the stock market has fallen and many tech companies have failed or are fending off creditors, the government has taken on another look, staid and reliable.

"Growing at 5 percent or 10 percent a year was anything but appealing two years ago," says Bob Kipps, head of the government services/aerospace defense group for Houlihan, Lokey Howard & Zurkin, an investment banking firm specializing in clients whose annual revenue ranges from \$50 million a year to \$1 billion.

"It's kind of like the turtle catching the hare," says Kipps, who works in the Los Angeles-based firm's McLean, Va., office.

The government's IT spending push comes at a time when an assortment of procurement reform programs are taking root. Laws such as the Federal Acquisition Reform Act of 1996 were intended to make the government's procurement processes mimic those of the commercial sector.

Meanwhile, federal agencies have steadily increased their use of the government purchasing method known as the GSA schedule, maintained by the U.S. General Services Administration. The schedule is essentially a catalog, containing offerings from vendors at negotiated prices.

Because prices are set to reflect the lowest cost vendors offer their commercial clients, agencies buying from the schedule have substantially fewer requirements to fulfill than if they offered a project through a traditional, competitive bidding process.

Proponents of the GSA schedule say not having to go through that process saves companies lots of money and shortens the decision-making time from years to months, or even weeks.

Figures show the program has grown vastly in recent years, particularly in the technology sector. The government spent \$5.6 billion in fiscal 1997 on goods purchased using the schedule, of which \$2.8 billion explicitly related to IT. During fiscal 2000, \$13.6 billion of goods and services were bought on the schedule, of which \$9.3 billion was for IT.

Moreover, what the government is buying also is changing. Instead of hiring a private company at negotiated hourly rates, Washington is hiring companies to fulfill tasks for a fixed price.

"Government is procuring solutions," says Davis. "They're not just buying hours."

That difference has increased potential profit margins if companies can perform a task more efficiently than forecast in their negotiated deals.

"If you can go out and do better, you can improve your margin," says Davis, who recommends that companies "be in the high value-added service offerings" to increase profits.

Regardless of the type of offering, rolling the dice is not for everyone. Avi Hoffer, chief executive officer of Severna Park, Md.-based Metastorm, calls fixed-price bidding "very dangerous ground."

Hoffer's software company does about 25 percent of its work with the federal government, including a contract for a correspondence management product with the Small Business Administration.

"We typically do time and materials," he adds. "We almost never do fixed billing."

Though the process for obtaining federal contracts has become easier, breaking into the federal contracting game is not easy. Obtaining a listing on the GSA schedule is a first step, many say, but that does not do the trick by itself.

"If you get on the GSA schedule, the phone's not going to start ringing," says AFW Capital Partners' Davis, who likens a listing to "a hunting license."

Perhaps more than in competitive bids, which are theoretically judged objectively, businesses with offerings on the GSA schedule have an opportunity, and a need, to sell their wares.

"All things being equal, [the government] will buy from somebody they know," observes Davis.

"That's where many small companies are at a handicap because it's a significant investment to go out and do that marketing," he says.

There are two chief ways for a company to break into government contracting, experts say. One is to partner with a larger company; the other is to purchase a company that already has a foothold in the system.

"It's very difficult for a small company to begin selling to the federal government," cautions Davis. "Typically, the path to entering the federal market is through strategic partnerships."

That strategy fits with an overall trend in Washington's approach.

"The government not only wants fewer employees, they want fewer contracts," says Kipps, explaining that contracts are more likely to go to larger companies that administer projects consisting of several smaller subcontractor companies.

The combination of the pyramid effect — large companies subcontracting to smaller firms — and the overall desirability of being in the government sector has spawned considerable consolidation, say Kipps and Davis.

"We're being contacted by more commercial companies looking to expand into the federal market. Sometimes, it might be better to

look at the acquisition of a federal contractor," says Davis, noting he currently is working on a project in which a company in the \$20 million range that lacks a government contracting arm is looking to acquire a company in the \$12 million range that has one.

Another consolidation example occurred when Impact Innovations Group, based in Columbia, Md., was bought by J3 Inc., an information technology professional services company based in Atlanta, in 1999.

J3 lacked a government contracting arm while Impact was primarily a government contractor. The new entity was named Impact Innovations Group.

The trend toward consolidation has spawned a debate over whether there's room for small and mid-size companies in the new order of government contracting.

"The hardest is for mid-size companies, \$50 million to \$500 or \$700 million," says Kipps of Houlihan, Lokey Howard & Zurkin. "Those companies are sort of a 'no man's land.' They're too big to be a subcontractor, too small to win the big contracts."

But mid-size contractors seem happy to be where they are.

"We see ourselves competing with the large businesses," says Ken Newcomer, vice president of business development for privately held Impact Innovations Group.

"Through focus, we think we can be every bit as balanced," Newcomer adds, putting the firm's sales in the \$100 million range.

"Focus," in fact, is a word that government contracting experts often bring up when offering advice.

"You have to be really focused ... don't just say, 'We want to focus on the federal government.' You need to say, 'We want to focus on pesticides within the EPA'," Davis recommends. "The key is when you're small, you have to be a niche player."

Aside from focusing, experts advise aspiring government contractors to think carefully about their prospective buyer's needs and the appeal of their products.

"You have to understand what are their priorities and what are they going to be buying this year? And you have to go out and meet these people," says Davis. "It really takes sales, just like the commercial markets."

Selling the product also requires a specialized pitch, says Metastorm's Hoffer.

"Is [your product] going to be cheaper or technologically stronger?" he asks. "If it's 'me-too,' you better be the lowest cost solution. And if you're not lowest cost, you should be able to identify why

you have a better product."

Quality also counts, especially after the sale has been made.

"You better be prepared to meet every specification," Hoffer says, noting government deliverables are carefully scrutinized and that past performance is a key criterion for future awards.

Hoffer has one more bit of advice: Be able to accept credit cards.

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