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## SMALL BUSINESS ADMINISTRATION

13 CFR Parts 121, 124, 125, 126 and 127

[Docket No. SBA-2014-0006]

RIN: 3245-AG58

Small Business Government Contracting and National Defense Authorization Act of 2013 Amendments

AGENCY: U.S. Small Business Administration

ACTION: Proposed rule.

SUMMARY: The U.S. Small Business Administration (SBA or Agency) is proposing to amend its regulations to implement provisions of the National Defense Authorization Act of 2013, which pertain to performance requirements applicable to small business and socioeconomic program set aside contracts and small business subcontracting. SBA is also proposing to make changes to its regulations concerning the nonmanufacturer rule and affiliation rules. Further, SBA is proposing to allow a joint venture to qualify as small for any government procurement as long as each partner to the joint venture qualifies individually as small under the size standard corresponding to the NAICS code assigned in the solicitation. Finally, SBA is requesting comments on the timeline and procedures for North American Industry Classification System code appeals.

DATES: Comments must be received on or before [INSERT DATE 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER].

ADDRESSES: You may submit comments, identified by RIN: 3245-AG58, by any of the following methods:

- Federal eRulemaking Portal: <http://www.regulations.gov>. Follow the instructions for submitting comments.
- For mail, paper, disk, or CD-ROM submissions: Brenda Fernandez, U.S. Small Business Administration, Office of Policy, Planning and Liaison, 409 Third Street, SW, 8<sup>th</sup> Floor, Washington, DC 20416.
- Hand Delivery/Courier: Brenda Fernandez, U.S. Small Business Administration, Office of Policy, Planning and Liaison, 409 Third Street, SW, 8<sup>th</sup> Floor, Washington, DC 20416.

SBA will post all comments on [www.regulations.gov](http://www.regulations.gov). If you wish to submit confidential business information (CBI) as defined in the User Notice at [www.regulations.gov](http://www.regulations.gov), please submit the information to Brenda Fernandez, U.S. Small Business Administration, Office of Policy, Planning and Liaison, 409 Third Street, SW, 8<sup>th</sup> Floor, Washington, DC 20416, or send an email to [brenda.fernandez@sba.gov](mailto:brenda.fernandez@sba.gov). Highlight the information that you consider to be CBI and explain why you believe SBA should hold this information as confidential. SBA will review the information and make the final determination on whether it will publish the information.

FOR FURTHER INFORMATION CONTACT: Brenda Fernandez, Office of Policy, Planning and Liaison, 409 Third Street SW, Washington, DC 20416; (202) 207-7337; [brenda.fernandez@sba.gov](mailto:brenda.fernandez@sba.gov).

SUPPLEMENTARY INFORMATION:

Proposed Changes Pursuant to the National Defense Authorization Act of 2013

Section 1621 of the National Defense Authorization Act of 2013 (NDAA), Pub. L. 112-239, 126 Stat. 1632 (Jan. 2013), revised the Small Business Act regarding the

responsibilities of Procurement Center Representatives (PCRs). Section 1621 clarifies that PCRs have the ability to review barriers to small business participation in Federal contracting and to review any bundled or consolidated solicitation or contract in accordance with the Small Business Act. SBA proposes to amend 13 CFR § 125.2(b)(1)(i)(A), based on the changes in Section 1621(c)(6)(H) of the NDAA. This rule would add language to § 125.2(b)(1)(i)(A) and to § 125.2(b)(1)(ii), which clarifies that PCRs advocate for the maximum practicable utilization of small business concerns in Federal contracting, including advocating against the unjustified consolidation or bundling of contract requirements.

Pursuant to Section 1621(c)(6)(G) of the NDAA, SBA proposes new § 125.2(b)(1)(iv), which states that PCRs will consult with the agency's Office of Small and Disadvantaged Business (OSDBU) and Office of Small Business Program (OSBP) Director regarding an agency's decision to convert an activity performed by a small business concern to an activity performed by a Federal employee. SBA also proposes new § 125.2(b)(1)(v) pursuant to the language enacted by Section 1621(c)(6)(F) of the NDAA, which allows PCRs to receive unsolicited proposals from small business concerns and to provide those proposals to the appropriate agency's personnel for review and disposition.

SBA also proposes to amend paragraphs 125.2(b)(1) and (2), which pertain to Breakout PCRs (BPCRs). Sections 1621(e) and (f) of the NDAA effectively eliminate the statutory authority for the separate BPCR role. As a result, SBA proposes to reassign the responsibilities currently held by BPCRs to PCRs. SBA proposes to add § 125.2(b)(1)(i)(F), which states that PCRs also advocate full and open competition in

Federal contracting and recommend the breakout for competition of items and requirements which previously have not been competed. SBA proposes the elimination of § 125.2(b)(2) that provided guidance on the role and responsibilities of BPCRs and proposes redesignating current § 125.2(b)(3) as the new § 125.2(b)(2) and removing any reference to BPCRs from that paragraph.

Section 1651 of the NDAA, as codified at 15 U.S.C. 657s, requires that the limitations on subcontracting for full or partial small business set-aside contracts, HUBZone contracts, 8(a) BD contracts, SDVO SBC contracts, and WOSB and EDWOSB contracts, be evaluated based on the percentage of the overall award amount that a prime contractor spends on its subcontractors. Significantly, the NDAA excludes from the limitations on subcontracting calculation the percentage of the award amount that the prime contractor spends on similarly situated entity subcontractors. When a contract is awarded pursuant to a small business set-aside or socioeconomic program set-aside, a similarly situated entity subcontractor is a small business concern subcontractor that is a participant of the same SBA program that qualified the prime contractor as an eligible offeror and awardee of the contract.

Currently, SBA's regulations contain different terms for compliance with the performance of work requirements based on the type of small business program set-aside at issue. The method for calculating compliance not only varies by program set-aside type, but also based on whether the acquisition is for services, supplies, general construction, or specialty trade construction. Section 1651 of the NDAA creates a shift from the concept of a required percentage of work to be performed by a prime contractor to the concept of limiting a percentage of the award amount to be spent on

subcontractors. The goal is the same: to ensure that a certain amount of work is performed by a prime contractor small business concern (SBC) that qualified for a small business program set-aside procurement due to its socioeconomic program status. SBA proposes to revise all references to “performance of work” requirements found in parts 121, 124, 125, 126, and 127 to “limitations on subcontracting.”

The current method for determining whether a firm is in compliance with the limitation on subcontracting requirements requires the Contracting Officer (CO) to evaluate the percentage of the cost of the contract performance incurred for the prime contractor’s personnel. This calculation excludes profit or fees from the cost of the contract and includes only those costs incurred for the prime contractor’s personnel, which was defined as direct labor costs and any overhead which has only direct labor as its base, plus the contractor’s General and Administrative rate multiplied by the labor cost. Additionally, Title 13, parts 124, 125, 126, and 127 repeated the performance of work requirements, and in places, contained additional information affecting the calculation for the performance of work requirements.

SBA proposes to totally revise § 125.6 to take into account the new definition and calculation for the limitations on subcontracting, as described in Section 1651 of the NDAA. SBA believes that it is critical that small businesses that obtain set aside contracts comply with applicable subcontracting limitations. The Government’s policy of promoting contracting opportunities for small businesses, HUBZone SBCs, SDVO SBCs, WOSBs/EDWOSBs, and 8(a) SBCs is seriously undermined when firms pass on work in excess of applicable limitations to firms that are other than small or that are not otherwise eligible for specific types of small business contracts.

In addition, the section would be reorganized and simplified for easier use. Proposed § 125.6(a) would explain how to apply the limitations on subcontracting requirements to small business set-aside contracts. Instead of providing different methods of determining compliance based on the type of small business set-aside program at issue and the type of good or service sought, Section 1651(a) of the NDAA provides one method for determining compliance that is shared by almost all applicable small business set-aside programs, but varies based on whether the contract is for services, supplies or products, general construction, specialty trade construction, or a combination of both services and supplies.

The approach described in Section 1651(a) and (d) of the NDAA is to create a limit on the percentage of the award amount received by the prime contractor that may be spent on other-than-small subcontractors. Specifically, the NDAA provides that a small business awarded a small business set-aside, 8(a), SDVO small business, HUBZone, or WOSB/EDOSB award “may not expend on subcontractors” more than a specified amount. However, as noted below, work done by “similarly situated entities” does not count as subcontracted work for purposes of determining compliance with the limitation on subcontracting requirements. Proposed §§ 125.6(a)(1) and (a)(3) would address the limitations on subcontracting applicable to small business set-aside contracts requiring services or supplies. The limitation on subcontracting for both services and supplies is statutorily set at 50% of the award amount received by the prime contractor. See 15 U.S.C. 657s(a).

Proposed § 125.6(a)(3) addresses how the limitation on subcontracting requirement would be applied to a procurement that combines both services and supplies.

This provision would clarify that the CO's selection of the applicable NAICS code will determine which limitation of subcontracting requirement applies.

Proposed §§ 125.6(a)(4) and (5) would address the limitations on subcontracting for general and specialty trade construction contracts. SBA proposes to keep the same percentages that currently apply: 15% for general construction and 25% for specialty trade construction.

As noted above, the NDAA prohibits subcontracting beyond a certain specified amount for any small business set-aside, 8(a), SDVO small business, HUBZone, or WOSB/EDOSB contract. Section 1651(b) of the NDAA creates an exclusion from the limitations on subcontracting for "similarly situated entities." In effect, the NDAA deems any work done by a similarly situated entity not to constitute "subcontracting" for purposes of determining compliance with the applicable limitation on subcontracting. A similarly situated entity is a small business subcontractor that is a participant of the same small business program that the prime contractor is a certified participant of and which qualified the prime contractor to receive the award. Subcontracts between a small business prime contractor and a similarly situated entity subcontractor are excluded from the limitations on subcontracting calculation because it does not further the goals of SBA's government contracting and business development programs to penalize small business prime contract recipients that benefit the same small business program participants through subcontract awards.

SBA proposes to include three examples to § 125.6(b) to demonstrate how a small business concern or Federal agency should apply the exclusion for similarly situated entities and determine compliance with the limitations on subcontracting.

SBA has concerns about the practical application of a regulation that would require only a certain percentage of contract awards to be either retained by the prime contractor, or spent on a similarly situated entity. SBA's concern is that an approach that limits its review solely to the first tier of the contracting process (agreements between the prime contractor and its direct subcontractors) could be fraught with abuse. For example, if small business A is awarded a \$500,000 small business set-aside service contract and subcontracts \$450,000 of the work to small business B, if the limitation of subcontracting requirements apply only to the first tier, then the Government's review would be complete. Small businesses A and B clearly meet the 50% rule. However, if small business B could further subcontract all of its \$450,000 to a large business with impunity, then SBA believes that the intent of the subcontracting limitation requirements would be circumvented and small businesses would not be properly protected. In such a case, a large business would have performed \$450,000 of a \$500,000 contract (or 90%) of a contract that was set-aside exclusively for small business. In SBA's view, a large business that ultimately performs 90% of a small business set-aside contract unduly benefits from a contract intended to be performed by small business.

SBA believes that the intent of the changes in the NDAA were to ensure that contracts awarded, and the benefits of those contracts, flow to the proper beneficiaries. SBA does not believe that an intended consequence of the change was to make it easier to divert these benefits to ineligible entities by merely moving contracts down one or two tiers in the contracting process. As such, SBA has retained a requirement that firms benefiting from contracts, and their similarly situated subcontractors, perform a required amount of work on the contract themselves. SBA believes that requiring firms awarded



these contracts to perform significant portions of the work, as well as retain a significant portion of the contract award, will continue to help ensure that the benefits from these contracts flow to the intended parties.

SBA welcomes comments on this issue, including whether SBA's belief that there may be unintended consequences are misplaced, as well as comments about SBA's proposed solution. SBA also requests comments on whether prime contractors should be required to report to the contracting officer concerning meeting the performance of work requirements, and comments concerning the frequency and method of reporting.

SBA proposes to relocate the definitions that are relevant to the limitations on subcontracting that are currently found in §125.6(e) to § 125.1 with the other definitions that are applicable to part 125. Section 1651(e) of the NDAA provides the definitions of "similarly situated entity" and "covered small business concern." Proposed § 125.1(x) interprets the statutorily prescribed definition for similarly situated entity.

Proposed § 125.6(c) would explain how a small business concern certifies its compliance with the limitations on subcontracting and the date upon which compliance is determined.

Proposed § 125.6(d) would require that small business concern prime contractors, which intend to exclude subcontracts to similarly situated entities from the limitations on subcontracting, must identify those similarly situated entities and the percentage of the prime contract award amount that will be spent on each similarly situated subcontractor.

Proposed § 125.6(e) would address the process for continued compliance with the limitations on subcontracting when the award amount of a small business set-aside or small business program set-aside contract is modified. This process would require that

the prime contractor provide the contracting officer with documentation to demonstrate how it will continue to satisfy the applicable limitations on subcontracting. SBA seeks comments on this process and specifically requests suggestions for how procuring agencies can more effectively monitor compliance with the limitations on subcontracting when the award amount has been modified after award.

Proposed § 125.6(i) would address how the limitations on subcontracting apply to members of a Small Business Teaming Arrangement (SBTA) that are exempt from affiliation according to § 121.103(b)(9). Proposed § 125.6(k) states that the limitations on subcontracting apply to the combined effort of the SBTA members, not to the individual members of the SBTA separately.

SBA proposes to add new paragraph 125.6(j), which would exempt small business set aside contracts valued between \$3,000 and \$150,000 from the limitations on subcontracting requirements. Section 46 of the Small Business Act mandates that the statutory performance of work requirements (limitations on subcontracting) apply to small business set-aside contracts with values above \$150,000, and contracts of any amount awarded to socioeconomically disadvantaged contracting programs, such as 8(a) set-aside contracts, Women-Owned and Economically Disadvantaged Women-Owned small business set-aside contracts, HUBZone set-aside contracts and Service-Disabled Veteran-Owned set-aside contracts. 15 USC § 657s. Although the limitations on subcontracting apply to all of these contracts, Section 46 does not specifically cite Section 15(j) of the Small Business Act, which is the statutory authority for non-socioeconomically disadvantaged small business set-asides between \$3,000 and \$150,000. Further, Section 15(j) of the Small Business Act does not mention any

limitation on subcontracting requirements in connection with the performance of set aside contracts under Section 15(j). Thus, the FAR provides that “[t]he contracting officer shall insert the clause at 52.219-14, Limitations on Subcontracting, in solicitations and contracts for supplies, services, and construction, if any portion of the requirement is to be set aside or reserved for small business and the contract amount is expected to exceed \$150,000.” FAR 19.508(e). Therefore, this proposed rule would not expand the application of the limitations on subcontracting to apply to small business set-asides below \$150,000, but would merely adopt what the FAR has done. SBA wants to make clear, however, that the proposed rule would exempt the limitations on subcontracting requirements only with respect to small business set asides valued between \$3,000 and \$150,000. The limitation on subcontracting requirements would continue to apply to all 8(a), HUBZone, SDVO, and WOSB/EDWOSB set aside contract awards regardless of value, including but not limited to contracts with values between \$3,000 and \$150,000. SBA requests comments regarding whether the limitations on subcontracting should apply to small business set aside contracts valued between \$3,000 and \$150,000.

SBA’s proposal to not apply the subcontracting limitations to non-socioeconomically disadvantaged small business set-aside contracts between \$3,000 and \$150,000 does not, however, reduce the importance of these limitations on small business set aside contracts over \$150,000 and all contracts that are set aside for socioeconomically disadvantaged small businesses. It is critical that firms that obtain set aside and preferential contracts comply with applicable subcontracting limitations. The Government’s policy of promoting contracting opportunities for small and socioeconomically disadvantaged businesses is seriously undermined when firms pass on

work in excess of applicable limitations to firms that are other than small or that are not disadvantaged. In addition, SBA requests comments on whether, for policy reasons and for purposes of consistency, the performance of work/subcontracting limitation requirements should apply to small business set aside contract with a value between \$3,000 and \$150,000. If SBA were to amend its regulations to apply those requirements to small business set aside contracts valued between \$3,000 and \$150,000, then a corresponding change to the FAR would be required for consistency purposes.

Consistent with this concern, Section 1652 of the NDAA, codified at 15 U.S.C. 645 (Section 16 of the Small Business Act) prescribes penalties for concerns that violate the limitations on subcontracting requirements. SBA proposes to add new § 125.6(k) to incorporate these penalties into the regulations. Paragraph 125.6(k) states that concerns that violate the limitations on subcontracting are subject to the penalties listed in 15 U.S.C. 645(d) except that the fine associated with these penalties will be the greater of either \$500,000 or the dollar amount spent in excess of the permitted levels for subcontracting.

This rule also proposes to revise § 121.103(h)(4). Paragraph (h) discusses the circumstances under which SBA will find affiliation among joint venturers for size purposes. Paragraph (h)(4) addresses the ostensible subcontractor rule, which is the concept that a subcontractor who performs the majority of the primary and vital requirements of a contract or whom the prime contractor is unusually reliant upon may be considered a joint venturer with the prime contractor and thus affiliated with the prime contractor for size determination purposes. SBA proposes to revise this paragraph to exclude subcontractors that are similarly situated subcontractors, as that term is defined

in 13 CFR § 125.6(g)(3), from affiliation under the ostensible subcontractor rule. Such a position clearly flows from the NDAA's treatment of similarly situated subcontractors.

SBA proposes to amend §§ 124.510(a), (b), and (c) to reflect the limitations on subcontracting rules with respect to the 8(a) Business Development (BD) program. Part 124 addresses the 8(a) BD program and the limitations on subcontracting that apply to procurements set-aside for competition among 8(a) BD participants. SBA proposes to delete paragraphs (a) and (b) and add new paragraph (a). Currently, paragraphs (a) and (b) discuss how 8(a) BD participants can comply with the performance of work requirements even though these specifications are also discussed in § 125.6. To eliminate confusion and repetition, SBA proposes to remove current paragraph (b) and add a new paragraph (a), which will direct 8(a) BD participants to comply with the limitations on subcontracting set forth in § 125.6. The proposed rule would redesignate current paragraph (c) as paragraph (b) and include references to the limitations on subcontracting as opposed to the performance of work requirements in newly redesignated paragraph (b). The NDAA uses the term "limitations on subcontracting" to describe the concept that is currently referred to as "performance of work requirements." This change provides consistency throughout the rules.

SBA proposes to revise §§ 125.15(a)(3) and (b)(3), which address the requirements for an SDVO SBC to submit an offer on a contract. SBA proposes to revise paragraph (a)(3) to state that a concern that represents itself as an SDVO SBC must also represent that it will comply with the limitations on subcontracting, as set forth in § 125.6, as part of its initial offer, including price. SBA proposes to revise paragraph

(b)(3) to state that joint ventures that represent themselves as an SDVO SBC joint venture must comply with the applicable limitations on subcontracting, as set forth in § 125.6.

SBA also proposes to revise § 126.200(b)(6). This paragraph addresses the requirements that a concern must meet in order to receive SBA's certification as a qualified HUBZone SBC. Paragraphs (b)(6) and (d) are repetitive as both address the requirement that HUBZone SBCs must comply with the relevant performance of work requirements. SBA proposes to delete paragraph (d) and revise paragraph (b)(6). Specifically, proposed paragraph (b)(6) would state that the concern must represent in its application for the HUBZone program that it will comply with the applicable limitations on subcontracting requirements with respect to any procurement that it receives as a qualified HUBZone SBC.

SBA proposes to revise §§ 126.700 in its entirety, including revision of paragraph (a) and removal of paragraphs (b) and (c). This section currently addresses the performance of work requirements for HUBZone contracts. SBA proposes to retitle the section to include the terminology "limitations on subcontracting"; remove references to the "performance of work" requirements; and replace the deleted text with a reference to 13 CFR § 125.6 for guidance on the applicable limitations on subcontracting for HUBZone contracts. SBA believes that it would be confusing to have each section of SBA's set-aside program regulations to repeat the relevant limitations on subcontracting, and therefore SBA proposes to list all of the limitations on subcontracting requirements at § 125.6 and provide references to that section in each of the various small business government contracting and business development program sections.

SBA proposes to revise § 127.504(b), which addresses the requirements a concern must satisfy to submit an offer for an EDWOSB or WOSB requirement. Paragraph (b) states that the concern must meet the performance of work requirements in § 125.6. SBA proposes to revise this paragraph to replace the reference to “performance of work requirement” with “limitations on subcontracting.”

SBA proposes to revise § 127.506(d), which addresses the requirements that a joint venture must satisfy in order to submit an offer for an EDWOSB or WOSB requirement. SBA proposes to revise this paragraph by replacing the reference to “performance of work requirement” with “limitations on subcontracting.”

Section 1653 of the NDAA, as codified at 15 U.S.C. 637(d) (Section 8(d) of the Small Business Act), addresses amendments to the requirements for subcontracting plans. Section 1653(a)(2) of the NDAA states that the head of the contracting agency shall ensure that the agency collects, reports, and reviews data on the extent to which the agency’s contractors meet the goals and objectives set out in their subcontracting plans. SBA proposes to add a new § 125.3(f)(8) to incorporate these provisions.

Section 1653(a)(3) of the NDAA modifies the Small Business Act to state that a contractor that fails to provide a written corrective action plan after receiving a marginal or unsatisfactory rating for its subcontracting plan performance or that fails to make a good faith effort to comply with its subcontracting plan will not only be in material breach of the contract, but such failure may also be considered in any past performance evaluation of the contractor. SBA proposes to revise § 125.3(f)(5) to incorporate this language. SBA is also proposing to add a new sentence to the end of § 125.3(f)(5), which prescribes the process for a Commercial Market Representative (CMR) to report

firms that are found to have acted fraudulently or in bad faith to the SBA's Area Director for the Office of Government Contracting Area Office where the firm is headquartered.

Section 1653(a)(4) of the NDAA modifies the Small Business Act to state that contracting agencies also perform evaluations of a prime contractor's subcontracting plan performance, and that SBA's evaluations of subcontracting plan performance are completed as a supplement to the contracting agency's review. SBA proposes to revise § 125.3(f)(1) to incorporate this language.

Section 1653(a)(5) of the NDAA requires that if an SBC is identified as a potential subcontractor in an proposal, offer, bid or subcontracting plan in connection with a covered Federal contract, the prime contractor shall notify the SBC prior to such identification. Section 1653(a)(5) also requires that the Administrator establish a reporting mechanism that allows potential subcontractors to report fraudulent activity or bad faith behavior by a prime contractor with respect to a subcontracting plan. SBA proposes to incorporate these requirements in new §§ 125.3(c)(7) and (8).

#### Affiliation

SBA proposes to make changes to its regulations in § 121.103(f), which defines affiliation based on an identity of interest. Paragraph 121.103(f) discusses the circumstances where an identity of interest between two or more persons leads to affiliation among those persons and their interests are aggregated. SBA is adding additional guidance on how to analyze affiliation due to an identity of interest. SBA believes that the additional clarifications will better enable concerned parties to understand and determine when they are affiliated.



SBA proposes to divide paragraph (f) into two paragraphs. Paragraph (f)(1) will include further clarification regarding the type of relationships between individuals that will create a presumption of affiliation due to an identity of interest. Specifically, SBA proposes to insert language clarifying that a presumption of affiliation exists for firms that conduct business with each other and are owned and controlled by persons who are married couples, parties to a civil union, parents and children, and siblings. This is a rebuttable presumption. This proposed rule is based on size appeal decisions that have been issued interpreting this regulation.

In paragraph (f)(2), SBA proposes to adopt a presumption that SBA established for the SBIR Program with respect to economic dependence. If a firm derives 70% or more of its revenue from another firm over the previous fiscal year, SBA will presume that the one firm is economically dependent on the other and, therefore, that the two firms are affiliated. Currently there is no fixed percentage that SBA applies when evaluating this criteria. SBA believes that providing clarity on this issue will be beneficial for firms, and enable them to more easily identify their affiliates. Further, this presumption is rebuttable, such as when a firm is new or a start-up and has only received a few contracts or subcontracts. Often new firms will not have as many partners and clients, and therefore will normally be generating more of their revenue from a much smaller number of other companies. Over time these firms should diversify and become less dependent on one entity.

#### Joint Ventures

SBA proposes to amend § 121.103(h) to broaden the exclusion from affiliation for small business size status, to allow two or more small businesses to joint venture for any

procurement without being affiliated with regard to the performance of that procurement requirement. Currently, in addition to the exclusion from affiliation given to an 8(a) protégé firm that joint ventures with its mentor for any small business procurement, there is also an exclusion from affiliation between two or more small businesses that seek to perform a small business procurement as a joint venture where the procurement is bundled or large (i.e., greater than half the size standard for a procurement assigned a NAICS code with a receipts-based size standard and greater than \$10 million for a procurement assigned a NAICS code with an employee-based size standard). SBA proposes to remove the restriction on the type of contract for which small businesses may joint venture without being affiliated for size determination purposes. SBA is proposing this change for several reasons. First, this proposed change would encourage more small business joint venturing, in furtherance of the government-wide goals for small business participation in Federal contracting. Second, this change would respond to results from the Small Business Teaming Pilot Program indicating more small business opportunities and greater success on small contracts than on large contracts. Third, this change would better align with the new provisions of the NDAA governing the limitations on subcontracting, which allow a small business prime contractor to subcontract to as many similarly situated subcontractors as desired. If a small business prime contractor can subcontract significant portions of that contract to one or more other small businesses and, in doing so, meet the performance of work requirements for small business (without being affiliated with the small business subcontractor(s)), it is SBA's view that similar treatment should be afforded joint ventures – so that a joint venture of two or more small

businesses could perform a procurement requirement as a small business when each is individually small.

#### Calculation of Annual Receipts

SBA proposes to amend § 121.104, which explains how SBA calculates annual receipts when determining the size of a business concern. SBA proposes to clarify that receipts include all income, and the only exclusions from income are the ones specifically listed in paragraph (a). It was always SBA's intent to include all income, except for the listed exclusions; however, SBA has found that some business concerns misinterpreted the current definition of receipts to exclude passive income. SBA's proposed change clarifies the intent to include all income, including passive income, in the calculation of receipts.

#### Recertification

SBA proposes to amend § 121.404(g)(2)(ii) by adding new paragraph (D) to clarify when recertification of size is required following the merger or acquisition of a firm that submitted an offer as a small business concern. Paragraph (D) clarifies that if the merger or acquisition occurs after offer but prior to award, the offeror must recertify its size to the contracting officer prior to award.

#### Small Business Innovation Research and Small Business Technology Transfer programs

SBA proposes to amend § 121.702(a)(2), which addresses the size and eligibility requirements applicable to the Small Business Innovation and Research (SBIR) and Small Business Technology Transfer (STTR) Programs, to clarify that a single venture capital operating company (VCOC), hedge fund, or private equity firm may own more than 50% of the concern if that single VCOC, hedge fund, or private equity firm qualifies

as a small business concern which is more than 50% directly owned and controlled by individuals who are citizens or permanent resident aliens of the United States. Business concerns and Federal agencies have misread the language of this paragraph to exclude all VCOCs, hedge funds, or private equity firms that own more than 50% of the small business concern, regardless of the investment entity's size. This paragraph explains the limitation on ownership by investment entities that are other than small and it is not meant to exclude those business concerns that are owned by investment entities that qualify as small business concerns.

#### Size Protests

SBA proposes to amend § 121.1001(a), which specifies who may initiate a size status protest. Small businesses and contracting officers have found the current language to be unclear because it contains a double negative, stating that any offeror that has not been eliminated for reasons not related to size may file a size protest. The intent is to provide standing to any offeror that is in line or consideration for award, but to not provide standing for an offeror that has been found to be non-responsive, technically unacceptable or outside of the competitive range.

In addition, the proposed rule would add a new § 121.1001(b)(11) that would authorize the SBA's Director, Office of Government Contracting, to initiate a formal size determination in connection with eligibility for the SDVO SBC and the WOSB/EDWSOB programs. This change is needed to correct an oversight that did not authorize such requests for size determinations when those programs were added to SBA's regulations.

#### North American Industry Classification System Code Appeals

The Agency is seeking comments on what is the appropriate timeline for filing a NAICS code appeal. SBA’s regulations currently state that, “[a]n appeal from a contracting officer’s NAICS code or size standard designation must be served and filed within 10 calendar days after the issuance of the solicitation or amendment affecting the NAICS code or size standard.” 13 C.F.R. § 121.1103(b)(1). SBA’s current rule is designed to work within the timeframe of a standard procurement, namely that firms will have 30 days from the date the solicitation is issued to submit an offer. However, the standard 30 day timeframe is not utilized in all procurements, and SBA is currently examining whether the current rule is adequate to address the needs of the various types of procurements and various timeframes that are available. Determining the appropriate timeline for filing a NAICS code appeal should take into consideration that for the NAICS code appeal process to be meaningful there must be sufficient time for a contracting officer to amend the solicitation to notify potentially interested parties of the pendency of the NAICS code appeal, *see Advanced Systems Technology, Inc. v. United States*, 69 Fed.Cl. 474 (2006), an opportunity for any interested party to draft and file a cogent response, and time for the Office of Hearings Appeals (OHA) to review the record to determine whether the contracting officer’s NAICS code assignment is based on a clear error of fact or law and issue a decision. Sometimes a NAICS code appeal is filed within days of the procurement closing. *See generally NAICS Appeal of Phoenix Environmental Design, Inc.*, SBA No. NAICS-5582 (2014) (A timely NAICS code appeal filed on Friday, August 8, 2014, for a procurement closing on Friday, August 15, 2014.). SBA is also assessing the effect that a NAICS code appeal should have on the solicitation. Currently SBA’s regulations require that the contracting officer, “[s]tay the

solicitation.” 13 C.F.R. § 121.1103(c)(1)(i). SBA is requesting comments on whether its regulations should provide that contracting officer should not award the contract or that the agency should delay the offer or bid response date.

#### Nonmanufacturer Rule

SBA is proposing to clarify that the limitations on subcontracting and the nonmanufacturer rule do not apply to small business set-aside contracts valued between \$3,000 and \$150,000. The statutory nonmanufacturer rule, which is contained in section 8(a)(17) of the Small Business Act, 15 U.S.C. 637(a)(17), is an exception to the limitations on subcontracting. It provides that a concern may not be denied the opportunity to compete for a supply contract under Section 8(a) and 15(a) of the Small Business Act simply because it is not the actual manufacturer or processor of the product. Section 8(a)(17) of the Small Business Act does not, however, also reference section 15(j) of the Small Business Act, the authority requiring small business set-aside contracts valued between \$3,000 and \$150,000. Thus, there is no specific statutory requirement that the nonmanufacturer rule apply to the mandated small business set-asides between \$3,000 and \$150,000. SBA believes that not applying the nonmanufacturer rule to small business set-asides valued between \$3,000 and \$150,000 will spur small business competition by making it more likely that a contracting officer will set aside an acquisition for small business concerns because the agency will not have to request a waiver from SBA where there are no small business manufacturers available. In order to request a waiver, an agency must provide SBA with the solicitation and research on whether manufacturers exist and wait several weeks for SBA to verify the data and grant the waiver. Without a waiver, an offeror on a supply small business set-aside contract

must either manufacture at least 50% of the product on its own or supply the product of a small business made in the United States. Many waiver requests below \$150,000 are for name brand items (e.g., computers) that are clearly not made by small businesses in the United States. Whether an agency can procure name brand items is not within the jurisdiction of SBA. The contracting officer must make that determination, which can be protested by interested parties.

SBA is proposing to amend § 121.1203 to require that contracting officers notify potential offerors of any waivers, whether class waivers or contract specific waivers, that will be applied to the procurement. SBA proposes that this notification of the application of a waiver be contained in the solicitation itself. Without notification that a waiver is being applied by the contracting officer, potential offerors cannot reasonably anticipate what if any requirements they must meet in order to perform the procurement in accordance with SBA regulations. SBA believes that providing notice of waivers in the solicitation will provide all potential offerors with the information needed to decide if they should submit an offer.

The proposed rule would also amend § 121.1203, regarding waivers to the nonmanufacturer rule. SBA proposes to amend § 121.1203(a) to specifically authorize SBA to grant a waiver to the nonmanufacturer rule for an individual contract award after a solicitation has been issued, provided the contracting officer agrees to provide all potential offerors additional time to respond. SBA believes that a waiver may be appropriate even after a solicitation has been issued, but wants to ensure that all potential offerors would be fully apprised of any waiver granted after the solicitation is issued and

have a reasonable amount of time (depending upon the complexities of the procurement) to adjust their offers accordingly.

SBA is also proposing in § 121.1203(b) to allow some waivers to be granted after the contract has been awarded. SBA believes that granting post-award waivers, when additional items that are eligible for a waiver are sought through in-scope modifications, is reasonable and will increase the use of the waiver process and allow firms to complete for contracts in a manner consistent with SBA regulations. SBA envisions these types of post award waivers to be given in situations similar to the example contained in the proposed regulation – where a need for an item occurs after contract award, where requiring the item would be an in-scope modification, and where the item is one for which a waiver would have been granted if sought prior to contract award.

The proposed rule would also add a new § 121.1203(d), dealing with waivers to the nonmanufacturer rule for the purchase of software. SBA is proposing to address whether the nonmanufacturer rule should apply to certain software that can readily be treated as an item and not a service. SBA is proposing to treat this type of software as a product or item of supply rather than a service. SBA believes that this change will bring SBA's regulations in line with how most buyers already perceive these types of software. Readily available software that is generally available to both the public and private sector unmodified is almost universally perceived to be a supply item, even though SBA's regulations currently would treat the production any type of software as a service. This change would also allow for certain types of software to be eligible for waivers of the nonmanufacturer rule. SBA is proposing to grant waivers on software that meet criteria that establishes that the Government is buying something that is more like a product or



supply item than a service. Clearly, when the Government seeks to award a contract to a business concern to create or modify custom design software, that should be classified as a service requirement and the activity will remain classified in a service NAICS code to which the nonmanufacturer rule does not apply. For a service procurement set aside for small business, the prime (together with one or more similarly situated subcontractors) would have to perform the required percentage of work with its own employees. On the other hand, when the Government buys certain types of unmodified software that is generally available to both the public and the Government from a business concern, SBA believes that the contracting officer should classify the requirement as a commodity or supply. If the procurement is a supply contract set aside for small business, the prime contractor, together with any similarly situated subcontractors, would have to perform at least 50% of the cost of manufacturing the software, unless SBA granted a waiver of the nonmanufacturer rule.

In order to address this scenario, SBA proposes to amend § 121.201 by adding a footnote to NAICS code 511210, Software Publishers, explaining that this is the proper NAICS code to use when the Government is purchasing software that is eligible for a waiver of the nonmanufacturer rule. The 2012 NAICS manual provides the following definition for this industry:

This industry comprises establishments primarily engaged in computer software publishing or publishing and reproduction. Establishments in this industry carry out operations necessary for producing and distributing computer software, such as designing, providing documentation, assisting in installation, and providing support services to software purchasers. These establishments may design, develop, and publish, or publish only.

SBA believes that this accurately reflects the type of companies that would be producing and supplying the Government with the type of software eligible for a waiver. Further,

SBA is proposing that the procurement of this type of software would be treated by SBA as a supply requirement, and therefore the nonmanufacturer rule would apply, as long as the acquisition meets all of the requirements of the rule. SBA reiterates that the custom design or modification of software for the Government will generally continue to be treated as a service. Therefore, if the software being acquired requires any custom modifications in order to meet the needs of the Government, it is not eligible for a waiver of the nonmanufacturer rule because the contractor is performing a service, not providing a supply.

SBA proposes to amend § 121.406(b)(5) to make a technical correction. Section 121.406(b) addresses how a nonmanufacturer may qualify as a small business concern for a requirement to provide a manufactured product or other supply item. Currently, paragraph (b)(5) states that the SBA's Administrator or designee may waive the requirement set forth in paragraph (b)(1)(iii) of this section, that requires nonmanufacturers to supply the end item of a small business manufacturer, processor or producer made in the United States. The citation to paragraph (b)(1)(iii) is incorrect and as such, SBA proposes to amend this paragraph to include the correct citation, paragraph (b)(1)(iv).

In addition, the proposed rule would amend § 121.406(b)(7) to clarify that SBA's waiver of the nonmanufacturer rule has no effect on requirements external to the Small Business Act which involve domestic sources of supply, such as the Buy American Act and the Trade Agreements Act. This has always been SBA's policy, but because SBA has received several inquiries about this issue, SBA believes that for better clarity the policy should be specifically set forth in the regulatory text.

In order to clarify whether the nonmanufacturer rule applies, or whether a general or specific waiver is attached to a procurement, SBA proposes to add a new § 121.1206 to require contracting officers to receive specific waivers prior to posting a solicitation, and also to provide notification to all potential offerors of any waivers that will be applied (whether class or specific) to a given solicitation. SBA believes that this will help to provide clear guidance to prospective offerors. If a solicitation states that a waiver is being applied, prospective offerors will know that the nonmanufacturer rule will not apply to that procurement. If no notice of a waiver being applied is given, prospective offerors will know that the requirements of § 121.406 must all be met. This will give prospective offerors ample time to prepare, and will remove some of the uncertainty surrounding issuances of waivers to the nonmanufacturer rule. SBA also proposes that if a contracting officer seeks and is provided a waiver after issuing a solicitation, the contracting officer must give all potential offers a reasonable amount of additional time in order to respond to the solicitation. In SBA's view, whether a waiver applies or not has a meaningful impact on who may place an offer, and how prospective offerors may respond to a given solicitation. Therefore, SBA believes it is important that potential offerors have a reasonable amount of time to properly evaluate and respond to the solicitation.

#### Adverse Impact and Construction Requirements

SBA proposes to amend § 124.504 to clarify when a procurement for construction services is considered a new requirement. This section generally addresses when SBA must conduct an adverse impact analysis for the award of an 8(a) contract. SBA is not required to perform an adverse impact analysis for new requirements. Currently,

paragraph (c)(1)(ii)(B) states that “Construction contracts, by their very nature (e.g., the building of a specific structure), are deemed new requirements.” SBA proposes to clarify the definition of “new requirement” for construction contracts by specifying that generally, the building of a specific structure is considered a new requirement. However, recurring indefinite delivery or indefinite quantity (IDIQ) procurements for construction services are not considered new. SBA has found that agencies have misinterpreted the current language of § 124.504(c)(1)(ii)(B) to consider recurring IDIQ construction services procurements as new. SBA intends to clarify that such recurring requirements are not considered new. A determination of whether a construction contract is recurring or new will have to be made on a case by case basis, and there is a process in place that allows SBA to file an appeal with the procuring agency when there is a disagreement.

#### Certificate of Competency

SBA proposes to amend § 125.5(f), which addresses SBA’s review of an application for the Certificate of Competency (COC) program. SBA proposes to insert new § 125.5(f)(3) to address how SBA should review an application for a COC based on a finding of non-responsibility due to financial capacity where the applicant is the apparent successful offeror for an IDIQ task order or contract. SBA frequently receives inquiries regarding the application of the COC process for financial capacity to the potential award of an IDIQ contract. SBA clarifies this process by proposing changes to § 125.5(f). The proposed changes state that the SBA’s Area Director will consider the firm’s maximum financial capacity and if such COC is issued, it will be for a specific amount that serves as the limit of the firm’s financial capacity for that contract. The contracting officer cannot deny the firm the award of an order or contract on the basis of

financial incapacity if the firm has not reached the financial maximum identified by the Area Director.

SBA proposes to revise § 125.26 to replace the term “Associate Administrator for Government Contracting” with the term “Director, Office of Government Contracting.” There is no longer a position at SBA titled the Associate Administrator for Government Contracting and as a result, SBA proposes to update these regulations with the current title for the appropriate official who will receive correspondence related to SDVO protests.

Compliance with Executive Orders 12866, 13563, 12988, 13132, the Paperwork Reduction Act (44 U.S.C. Ch. 35), and the Regulatory Flexibility Act (5 U.S.C. 601-612)  
Executive Order 12866

The Office of Management and Budget (OMB) has determined that this proposed rule is a “significant” regulatory action for purposes of Executive Order 12866.

Accordingly, the next section contains SBA’s Regulatory Impact Analysis. However, this is not a major rule under the Congressional Review Act, 5 U.S.C. 801, et.seq.

Regulatory Impact Analysis:

1. Is there a need for the regulatory action?

The proposed rule implements Sections 1621, 1651, 1652, 1653 and 1654 of the National Defense Authorization Act of 2013, Pub. L. No. 112-239, 126 Stat. 1632, January 2, 2013; 15 U.S.C. §§ 637(d), 644(l), 645, 657s. In addition, it makes several other changes needed to clarify ambiguities in or remedy perceived problems with the current regulations. These proposed changes should make SBA’s regulations easier to use and understand.

## 2. What are the potential benefits and costs of this regulatory action?

The proposed regulations should benefit small business concerns by allowing small business concerns to use similarly situated subcontractors in the performance of a set aside contract, thereby expanding the capacity of the small business prime contractor and potentially enabling the firm to compete for and obtain larger contracts. It also strengthens the small business subcontracting provisions, which may result in more subcontract awards to small business concerns. The proposed regulations also seek to address or clarify issues that are ambiguous or subject to dispute, thereby providing clarity to contracting officers as well as small business concerns.

## 3. What are the alternatives to this final rule?

Many of the proposed regulations are required to implement statutory provisions, thus there are no alternatives for these regulations. The alternative to the proposed regulations that are not required by statute would be to not issue regulations, which would result in continued confusion, litigation and controversy.

### Executive Order 13563

This executive order directs agencies to, among other things: (a) afford the public a meaningful opportunity to comment through the Internet on proposed regulations, with a comment period that should generally consist of not less than 60 days; (b) provide for an “open exchange” of information among government officials, experts, stakeholders, and the public; and (c) seek the views of those who are likely to be affected by the rulemaking, even before issuing a notice of proposed rulemaking. As far as practicable or relevant, SBA considered these requirements in developing this rule, as discussed below.

1. Did the agency use the best available techniques to quantify anticipated present and future costs when responding to E.O. 12866 (e.g., identifying changing future compliance costs that might result from technological innovation or anticipated behavioral changes)?

To the extent possible, the agency utilized the most recent data available in the Federal Procurement Data System – Next Generation, System for Award Management and Electronic Subcontracting Reporting System.

2. Public participation: Did the agency: (a) afford the public a meaningful opportunity to comment through the Internet on any proposed regulation, with a comment period that should generally consist of not less than 60 days; (b) provide for an “open exchange” of information among government officials, experts, stakeholders, and the public; (c) provide timely online access to the rulemaking docket on Regulations.gov; and (d) seek the views of those who are likely to be affected by rulemaking, even before issuing a notice of proposed rulemaking?

The proposed rule will have a 60 day comment period and will be posted on [www.regulations.gov](http://www.regulations.gov) to allow the public to comment meaningfully on its provisions. In addition, the agency reached out to agencies, including the Forest Service, the Food and Drug Administration, and the Defense Logistics Agency. SBA then submitted the rule to the Office of Management and Budget for interagency review.

3. Flexibility: Did the agency identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public?

Yes, the proposed rule implements statutory provisions and will provide clarification to rules that were requested by agencies and stakeholders. The proposed rule will make it easier for small businesses to contract with the Federal government.

### Executive Order 12988

This action meets applicable standards set forth set forth in section 3(a) and 3(b)(2) of Executive Order 12988, Civil Justice Reform, to minimize litigation, eliminate ambiguity, and reduce burden. This action does not have any retroactive or preemptive effect.

### Executive Order 13132

SBA has determined that this proposed rule will not have substantial direct effects on the States, on the relationship between the national government and the States, or on the distribution of power and responsibilities among the various levels of government. Therefore, for the purposes of Executive Order 13132, SBA has determined that this proposed rule has no federalism implications warranting preparation of a federalism assessment.

### Paperwork Reduction Act, 44 U.S.C. Ch. 35

For the purposes of the Paperwork Reduction Act, SBA has determined that this rule, if adopted in final form, would not impose new government-wide reporting requirements on small business concerns.

### Regulatory Flexibility Act, 5 U.S.C. 601-612

According to the Regulatory Flexibility Act (RFA), 5 U.S.C. 601, when an agency issues a rulemaking, it must prepare a regulatory flexibility analysis to address the impact of the rule on small entities. However, section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the rulemaking is not expected to have a significant economic impact on a substantial number of small entities. The RFA defines “small entity” to include “small businesses,” “small organizations,” and “small



governmental jurisdictions.” This proposed rule concerns various aspects of SBA’s contracting programs, as such the rule relates to small business concerns but would not affect “small organizations” or “small governmental jurisdictions” because those programs generally apply only to “business concerns” as defined by SBA regulations, in other words, to small businesses organized for profit. “Small organizations” or “small governmental jurisdictions” are non-profits or governmental entities and do not generally qualify as “business concerns” within the meaning of SBA’s regulations.

There are approximately 326,000 concerns listed as small business concerns in the System for Award Management (SAM) that could potentially be impacted by the implementation of the NDAA 2013 contracting provisions. However, we cannot say with any certainty how many will be impacted because we do not know how many of these concerns will team together to submit offers, nor do we know how many will be awarded contracts as teams. The number of firms participating in teaming will be lower than the number of firms registered in SAM. However, as discussed elsewhere in this rule, including section 2 of the Regulatory Impact Analysis, there are no new compliance or other costs imposed by the proposed rule on small business concerns. Under current law, firms must adhere to certain performance requirements when performing set aside contracts. Further, SBA expects that costs now incurred by small business concerns as a result of ambiguous or indefinite regulations will be eliminated or reduced. Clarifying the confusion and uncertainty concerning the applicability of SBA contracting regulations would also reduce the time burden on the small business contracting community and therefore make it easier for them to contract with the Federal Government. In sum, the proposed amendments would not have a disparate impact on small businesses and would

increase their opportunities to participate in federal government contracting without imposing any additional costs. For the reasons discussed, SBA certifies that this proposed rule would not have a significant economic impact on a substantial number of small business concerns.

#### List of Subjects

##### 13 CFR Part 121

Government procurement; Government property; Grant programs—business, Individuals with disabilities; Loan programs—business; Small businesses.

##### 13 CFR Part 124

Administrative practice and procedure, Government procurement, Minority businesses, Reporting and recordkeeping requirements, Small business, Technical assistance.

##### 13 CFR Part 125

Government contracts, Government procurement, Reporting and recordkeeping requirements, Small businesses, Technical assistance.

##### 13 CFR Part 126

Administrative practice and procedure, Government procurement, Penalties, Reporting and Recordkeeping requirements, Small business.

##### 13 CFR Part 127

Government procurement, Reporting and recordkeeping requirements, Small businesses.

Accordingly, for the reasons stated in the preamble, SBA proposes to amend parts 121, 124, 125, 126, and 127 of title 13 of the Code of Federal Regulations as follows:

PART 121—SMALL BUSINESS SIZE REGULATIONS

1. The authority citation for 13 CFR part 121 continues to read as follows:

Authority: 15 U.S.C. 632, 634(b)(6), 662 and 694a(9).

2. Amend § 121.103 by adding paragraphs (f)(1) and (f)(2) and by revising paragraphs (h)(3)(i) and (h)(4) to read as follows:

§ 121.103 How does SBA determine affiliation?

\* \* \* \* \*

(f) \* \* \*

(1) Firms owned or controlled by married couples, parties to a civil union, parents and children, and siblings are presumed to be affiliated with each other if they conduct business with each other, such as subcontracts or joint ventures or share or provide loans, resources, equipment, locations or employees with one another. This presumption may be overcome by showing a clear line of fracture between the concerns. Other types of familial relationships are not grounds for affiliation on family relationships.

(2) SBA may presume an identity of interest based upon economic dependence if the concern in question derived 70% or more of its receipts from another concern in the previously completed fiscal year.

\* \* \* \* \*

(h) \* \* \*

(3) Exception to affiliation for certain joint ventures. (i) A joint venture of two or more business concerns may submit an offer as a small business for a Federal procurement, subcontract or sale so long as each concern is small under the size standard corresponding to the NAICS code assigned to the contract.

\* \* \* \* \*

(4) A contractor and its ostensible subcontractor are treated as joint venturers, and therefore affiliates, for size determination purposes. An ostensible subcontractor is a subcontractor that is not a similarly situated entity, as that term is defined in §125.6(g)(3), and: performs primary and vital requirements of a contract, or of an order; or is a subcontractor upon which the prime contractor is unusually reliant. All aspects of the relationship between the prime and subcontractor are considered, including, but not limited to, the terms of the proposal (such as contract management, technical responsibilities, and the percentage of subcontracted work), agreements between the prime and subcontractor (such as bonding assistance or the teaming agreement), and whether the subcontractor is the incumbent contractor and is ineligible to submit a proposal because it exceeds the applicable size standard for that solicitation.

\* \* \* \* \*

3. Amend § 121.104 by revising the introductory text in paragraph (a) to read as follows:

§ 121.104 How does SBA calculate annual receipts?

(a) Receipts means all revenue in whatever form received or accrued from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances. Generally, receipts are considered “total income” (or in the case of a sole proprietorship “gross income”) plus “cost of goods sold” as these terms are defined and reported on Internal Revenue Service (IRS) tax return forms (such as Form 1120 for corporations; Form 1120S and Schedule K for S corporations; Form 1120, Form 1065 or Form 1040 for

LLCs; Form 1065 and Schedule K for partnerships; Form 1040, Schedule F for farms; Form 1040, Schedule C for other sole proprietorships). Receipts do not include net capital gains or losses; taxes collected for and remitted to a taxing authority if included in gross or total income, such as sales or other taxes collected from customers and excluding taxes levied on the concern or its employees; proceeds from transactions between a concern and its domestic or foreign affiliates; and amounts collected for another by a travel agent, real estate agent, advertising agent, conference management service provider, freight forwarder or customs broker. For size determination purposes, the only exclusions from receipts are those specifically provided for in this paragraph. All other items, such as subcontractor costs, reimbursements for purchases a contractor makes at a customer's request, investment income, and employee-based costs such as payroll taxes, may not be excluded from receipts.

\* \* \* \* \*

4. Amend § 121.201 by adding the following paragraph as footnote 20 to NAICS code 511210.

§ 121.201 What size standards has SBA identified by North American Industry Classification System codes?

\* \* \* \* \*

Footnotes

\* \* \* \* \*

20. NAICS code 511210 - For purposes of Government procurement, the purchase of software subject to potential waiver of the nonmanufacturer rule pursuant to § 121.1203(d) should be classified under this NAICS code.

5. Amend § 121.404 as follows:

a. Revise paragraph (f); and

b. Add paragraph (g)(2)(ii)(D) to read as follows:

§ 121.404 When is the size status of a business concern determined?

\* \* \* \* \*

(f) For purposes of architect-engineering, design/build or two-step sealed bidding procurements, a concern must qualify as small as of the date that it certifies that it is small as part of its initial bid or proposal (which may or may not include price).

(g) \* \* \*

(2) \* \* \*

(ii) \* \* \*

(D) If the merger or acquisition occurs after offer but prior to award, the offeror must recertify its size to the contracting officer prior to award.

\* \* \* \* \*

6. Amend § 121.406 by revising paragraph (b)(5) introductory text, (b)(7), and (d) to read as follows:

§ 121.406 How does a small business concern qualify to provide manufactured products or other supply items under a small business set-aside, service-disabled veteran-owned small business set-aside, WOSB or EDWOSB set-aside, or 8(a) contract?

\* \* \* \* \*

(b) \* \* \*

(5) The Administrator or designee may waive the requirement set forth in paragraph (b)(1)(iv) of this section under the following two circumstances:

\* \* \* \* \*

(7) SBA's waiver of the nonmanufacturer rule means that the firm can supply the product of any size business without regard to the place of manufacture. However, any SBA waiver has no effect on requirements external to the Small Business Act which involve domestic sources of supply, such as the Buy American Act and the Trade Agreements Act.

\* \* \* \* \*

(d) The performance requirements (limitations on subcontracting) and the nonmanufacturer rule do not apply to small business set aside acquisitions with an estimated value between \$3,000 and \$150,000.

\* \* \* \* \*

8. Amend §121.702 by revising paragraph (a)(2) to read as follows:

§ 121.702 What size and eligibility standards are applicable to the SBIR and STTR programs?

\* \* \* \* \*

(a) \* \* \*

(2) No single venture capital operating company, hedge fund, or private equity firm may own more than 50% of the concern unless that single venture capital operating company, hedge fund, or private equity firm qualifies as a small business concern that is more than 50% directly owned and controlled by individuals who are citizens or permanent resident aliens of the United States.

\* \* \* \* \*

9. Amend § 121.1001 as follows:

a. Revise paragraphs (a)(1)(i) and (a)(2)(i); and

b. Add paragraph (b)(11) to read as follows:

§ 121.1001 Who may initiate a size protest or request a formal size determination?

(a) \* \* \* (1) \* \* \*

(i) Any offeror that the contracting officer has not eliminated from consideration for any procurement-related reason, such as non-responsiveness, technical unacceptability or outside of the competitive range;

\* \* \* \* \*

(2) \* \* \*

(i) Any offeror that the contracting officer has not eliminated from consideration for any procurement related reason, such as non-responsiveness, technical unacceptability or outside of the competitive range;

\* \* \* \* \*

(b) \* \* \*

(11) In connection with eligibility for the SDVO SBC and the WOSB/EDWSOB programs, the Director, Office of Government Contracting, may initiate a formal size determination.

10. Revise § 121.1203 to read as follows:

§ 121.1203 When will a waiver of the Nonmanufacturer Rule be granted for an individual contract?

(a) Where appropriate, SBA will generally grant waivers for an individual contract or order prior to the issuance of a solicitation, or, where a solicitation has been



issued, when the contracting officer provides all potential offerors additional time to respond.

(b) SBA may grant a waiver after contract award, where the contracting officer has determined that the modification is within the scope of the contract and the agency followed the regulations prior to issuance of the solicitation and properly and timely requested a waiver for any other items under the contract, where required.

Example: The Government seeks to buy spare parts to fix Item A. After conducting market research, the government determines that Items B, C, and D that are being procured may be eligible for waivers and requests and receives waivers from SBA for those items prior to issuing the solicitation. After the contract is awarded, the Government determines that it will need additional spare parts to fix Item A. The Government determines that adding the additional parts as a modification to the original contract is within scope. The contracting officer believes that one of the additional parts is also eligible for a waiver from SBA, and requests the waiver at the time of the modification. If all other criteria are met, SBA would grant the waiver, even though the contract has already been awarded.

(c) An individual waiver for a product in a specific solicitation will be approved when the SBA Director, Office of Government Contracting, reviews and accepts a contracting officer's determination that no small business manufacturer or processor can reasonably be expected to offer a product meeting the specifications of a solicitation, including the period of performance.

(d) Waivers for the purchase of software. (1) SBA may grant an individual waiver for the procurement of a software item provided that the software being sought is an item that is of a type customarily used by the general public or by non-governmental entities for purposes other than governmental purposes, and the item:

(i) Has been sold, leased, or licensed to the general public, or has been offered for sale, lease, or license to the general public;

(ii) Is sold in substantial quantities in the commercial marketplace; and  
(iii) Is offered to the Government, under a contract or subcontract at any tier, without modification, in the same form in which it is sold in the commercial marketplace.

(2) If the value of services provided related to the purchase of a supply item that meets the requirements of paragraph (a)(1) of this section exceed the value of the item itself, the procurement should be identified as a service procurement, even if the services are provided as part of the same license, lease, or sale terms. If a contracting officer cannot make a determination of the value of services being provided, SBA will assume that the value of the services is greater than the value of items or supplies, and will not grant a waiver.

(3) Subscription services, remote hosting of software, data, or other applications on servers or networks of a party other than the U.S. Government are considered by SBA to be services and not the procurement of a supply item. Therefore SBA will not grant waivers of the nonmanufacturer rule for these types of services.

11. Amend § 121.1204 by revising paragraphs (b)(1)(ii) and (iii) to read as follows:

§ 121.1204 What are the procedures for requesting and granting waivers?

\* \* \* \* \*

(b) \* \* \* (1) \* \* \*

(ii) The proposed solicitation number, NAICS code, dollar amount of the procurement, and a brief statement of the procurement history;

(iii) A determination by the contracting officer that no small business manufacturer or processor reasonably can be expected to offer a product meeting the

specifications (including period of performance) required by a particular solicitation.  
Include a narrative describing market research and supporting documentation; and

\* \* \* \* \*

12. Add § 121.1206 to read as follows:

§ 121.1206 How will potential offerors be notified of applicable waivers?

(a) Contracting officers must provide written notification to potential offerors of any waivers being applied to a specific acquisition, whether it is a class waiver or a contract specific waiver. This notification must be provided at the time a solicitation is issued. If the notification is provided after a solicitation is issued, the contracting officer must provide potential offerors a reasonable amount of additional time to respond to the solicitation.

(b) If a contracting officer does not provide notice, and additional reasonable time for responses when required, then the waiver cannot be applied to the solicitation. This applies to both class waivers and individual waivers.

PART 124—8(a) BUSINESS DEVELOPMENT/SMALL DISADVANTAGED  
BUSINESS STATUS DETERMINATIONS

13. The authority citation for part 124 is revised to read as follows:

Authority: 15 U.S.C. 634(b)(6), 636(j), 637(a), 637(d), 644 and Pub. L. 99-661, Pub. L. 100-656, sec.1207, Pub. L. 101-37, Pub. L. 101-574, section 8021, Pub. L. 108-87, and 42 U.S.C. 9815.

14. Amend § 124.504 by revising paragraph (c)(1)(ii)(B) to read as follows:

§ 124.504 What circumstances limit SBA's ability to accept a procurement for award as an 8(a) contract?

\* \* \* \* \*

(c) \* \* \*

(1) \* \* \*

(ii) \* \* \*

(B) Procurements for construction services (e.g., the building of a specific structure) are generally deemed to be new requirements. However, recurring indefinite delivery or indefinite quantity task or delivery order construction services are not considered new (e.g., a recurring procurement requiring all construction work at base X).

\* \* \* \* \*

15. Amend § 124.510 by revising the section heading and the text to read as follows:

§ 124.510 What limitations on subcontracting apply to an 8(a) contract?

(a) To assist the business development of Participants in the 8(a) BD program, there are limitations on the percentage of an 8(a) contract award amount that may be spent on subcontractors. The prime contractor recipient of an 8(a) contract must comply with the limitations on subcontracting at § 125.6 of this chapter.

(b) Indefinite delivery and indefinite quantity contracts. (1) In order to ensure that the required limitations on subcontracting requirements on an indefinite delivery or indefinite quantity 8(a) award are met by the Participant, the Participant cannot subcontract more than the required percentage to subcontractors that are not similarly situated entities for each performance period of the contract (i.e., during the base term and then during each option period thereafter). However, the contracting officer, in his or her discretion, may require the Participant to meet the applicable limitation on subcontracting or comply with the nonmanufacturer rule for each order.

(i) This includes Multiple Award Contracts that were set-aside, partially set-aside or reserved solely for 8(a) BD Participants.

(ii) For orders that are set aside for eligible 8(a) Participants under full and open contracts or reserves, the Participant must meet the applicable limitation on subcontracting requirement or comply with the nonmanufacturer rule for each order.

(2) The applicable SBA District Director may waive the provisions in paragraph (b)(1) of this section requiring a Participant to meet the applicable limitation on subcontracting requirement for each performance period (or for each order for an order set aside solely for eligible 8(a) Participants under full and open multiple award contracts or reserves). Instead, the District Director may permit the Participant to subcontract in excess of the limitations on subcontracting where the District Director makes a written determination that larger amounts of subcontracting are essential during certain stages of performance. However, the 8(a) Participant and procuring activity's contracting officer must provide written assurances that the Participant will ultimately comply with the requirements of this section prior to contract completion. The procuring activity's contracting officer does not have the authority to waive the provisions of paragraph (b)(1) of this section requiring a Participant to meet the applicable limitation on subcontracting requirement for each performance period, even if the agency has a Partnership Agreement with SBA.

Example. Two task orders are issued under an 8(a) indefinite quantity service contract during the base period of the contract. The amount paid to the Participant on each of the two task orders is \$100,000. The Participant subcontracts \$40,000 to subcontractors that are not similarly situated on the first task order. Where the relevant SBA District Director has not waived the requirements of paragraph (b)(1), the Participant could not subcontract more than \$60,000 to subcontractors that are not similarly situated on the second task order in order to meet the requirement that it not subcontract more than 50% of the

amount paid to it to subcontractors that are not similarly situated during the relevant performance period (i.e., in order to ensure that it would not subcontract more than \$100,000, out of the \$200,000 paid to it, to subcontractors that are not similarly situated).

(3) Where the Participant does not ultimately comply with the performance of work requirements by the end of the contract, SBA will not grant future waivers for the Participant. Further, the contracting officer must document an 8(a) Participant's compliance with the limitation on subcontracting requirements as part of its performance evaluation in accordance with the procedures set forth in FAR 42.1502. The contracting officer must also evaluate compliance for future contract awards in accordance with the procedures set forth in FAR 9.104-6.

16. Amend § 124.513 by revising paragraph (b) to read as follows:

§ 124.513 Under what circumstances can a joint venture be awarded an 8(a) contract?

\* \* \* \* \*

(b) Size of concerns to an 8(a) joint venture. (1) A joint venture of at least one 8(a) Participant and one or more other business concerns may submit an offer as a small business for a competitive 8(a) procurement, or be awarded a sole source 8(a) procurement, so long as each concern is small under the size standard corresponding to the NAICS code assigned to the procurement.

(2) Notwithstanding the provisions of paragraph (b)(1) of this section, a joint venture between a protégé firm and its approved mentor (see § 124.520) will be deemed small provided the protégé qualifies as small for the size standard corresponding to the NAICS code assigned to the contract and has not reached the dollar limits set forth in § 124.519.

\* \* \* \* \*

PART 125—GOVERNMENT CONTRACTING PROGRAMS

17. The authority citation for 13 CFR part 125 is revised to read as follows:

Authority: 15 U.S.C. 632(p), (q); 634(b)(6), 637, 644, 657(f), 657q; and 657s.

18. Amend § 125.1 by adding paragraph (x) to read as follows:

§ 125.1 What definitions are important to SBA's Government Contracting Programs?

\* \* \* \* \*

(x) Similarly situated entity is a subcontractor that has the same small business program status as the prime contractor. This means that: for a HUBZone requirement, a subcontractor that is HUBZone certified; for a small business set-aside, partial set-aside, or reserve a subcontractor that is a small business concern; for an, SDVO SBC requirement, a subcontractor that is a self-certified SDVO SBC; for an 8(a) requirement, a subcontractor that is an 8(a) certified; or a WOSB or EDWOSB contract, a subcontractor that is self-certified as a WOSB or EDWOSB.. In addition to sharing the same small business program status as the prime contractor, a similarly situated entity must also be small for the NAICS code that is assigned to the procurement.

19. Amend § 125.2 as follows:

- a. Revise paragraph (b)(1)(i)(A);
- b. Add paragraph (b)(1)(i)(F);
- c. Revise paragraph (b)(1)(ii);
- d. Revise paragraph (b)(1)(iii)(C);
- e. Add paragraphs (b)(1)(iv) and (v);
- f. Remove paragraph (b)(2) and redesignate paragraph (b)(3) as paragraph (b)(2); and

g. Revise redesignated paragraph (b)(2).

§ 125.2 What are SBA's and the procuring agency's responsibilities when providing contracting assistance to small businesses?

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(i) \* \* \*

(A) SBA has PCRs who are generally located at Federal agencies and buying activities which have major contracting programs. At the SBA's discretion, PCRs will review all acquisitions that are not totally set aside for small businesses to determine whether a set aside or sole source award to a small business under one of SBA's programs is appropriate and to identify alternative strategies to maximize the participation of small businesses in the procurement. PCRs also advocate for the maximum practicable utilization of small business concerns in Federal contracting, including by advocating against the consolidation or bundling of contract requirements, as defined in § 125.1, and reviewing any justification provided by the agency for consolidation or bundling. This review includes acquisitions that are Multiple Award Contracts where the agency has not set-aside all or part of the acquisition or reserved the acquisition for small businesses. It also includes acquisitions where the agency has not set-aside orders placed against Multiple Award Contracts for small business concerns.

\* \* \* \* \*

(F) PCRs also advocate competitive procedures and recommend the breakout for competition when appropriate. They may appeal the failure by the buying activity to act



favorably on a recommendation in accord with the appeal procedures in paragraph (b)(2) of this section. PCRs also review restrictions and obstacles to competition and make recommendations for improvement.

(ii) PCR recommendations. The PCR must recommend to the procuring activity alternative procurement methods that would increase small business prime contract participation if a PCR believes that a proposed procurement includes in its statement of work goods or services currently being performed by a small business and is in a quantity or estimated dollar value the magnitude of which renders small business prime contract participation unlikely; will render small business prime contract participation unlikely (e.g., ensure geographical preferences are justified); or is for construction and seeks to package or consolidate discrete construction projects. If a PCR does not believe a bundled or consolidated requirement is necessary and justified the PCR shall advocate against the consolidation or bundling of such requirements and recommend to the procuring activity alternative procurement methods which would increase small business prime contract participation. Such alternatives may include:

\* \* \* \* \*

(iii) \* \* \*

(C) Recommending that the small business subcontracting goals be based on total contract dollars in addition to goals based on a percentage of total subcontracted dollars;

\* \* \* \* \*

(iv) PCRs will consult with the agency OSDBU with regard to agency decisions to convert an activity performed by a small business concern to an activity performed by a Federal employee.

(v) PCRs may receive unsolicited proposals from small business concerns and shall transmit those proposals to the agency personnel responsible for reviewing such proposals. The agency personnel shall provide the PCR with information regarding the disposition of such proposal.

(2) Appeals of PCR recommendations. In cases where there is disagreement between a PCR and the contracting officer over the suitability of a particular acquisition for a small business set-aside, partial set-aside or reserve, whether or not the acquisition is a bundled, substantially bundled or consolidated requirement, the PCR may initiate an appeal to the head of the contracting activity. If the head of the contracting activity agrees with the contracting officer, SBA may appeal the matter to the Secretary of the Department or head of the agency. The time limits for such appeals are set forth in FAR 19.505 (48 CFR 19.505).

\* \* \* \* \*

20. Amend § 125.3 as follows:

- a. Add paragraphs (c)(8) and (c)(9);
- b. Revise the first sentence of paragraph (f)(1);
- c. Revise paragraph (f)(5); and
- d. Add paragraph (f)(8) to read as follows:

§ 125.3 What types of subcontracting assistance are available to small businesses?

\* \* \* \* \*

(c) \* \* \*

(8) A prime contractor that identifies a small business by name as a subcontractor in a proposal, offer, bid or subcontracting plan must notify those subcontractors in writing prior to identifying the concern in the proposal, bid, offer or subcontracting plan

(9) Anyone who has a reasonable basis to believe that a prime contractor or a subcontractor may have made a false statement to an employee or representative of the Federal Government, or to an employee or representative of the prime contractor, with respect to subcontracting plans must report the matter to the SBA Office of Inspector General. All other concerns as to whether a prime contractor or subcontractor has complied with SBA regulations or otherwise acted in bad faith may be reported to the Government Contracting Area Office where the firm is headquartered.

\* \* \* \* \*

(f) Compliance Reviews. (1) A prime contractor's performance under its subcontracting plan is evaluated by means of on-site compliance reviews and follow-up reviews, as a supplement to evaluations performed by the contracting agency, either on a contract-by-contract basis or, in the case of contractors having multiple contracts, on an aggregate basis. \* \* \*

\* \* \* \* \*

(5) Any contractor that fails to comply with paragraph (f)(4) of this section, or any contractor that fails to demonstrate a good-faith effort, as set forth in paragraph (d) of this section:

(i) may be considered for liquidated damages under the procedures in 48 CFR 19.705-7 and the clause at 52.219-16; and

(ii) shall be in material breach of such contract or subcontract, and such failure to demonstrate good faith must be considered in any past performance evaluation of the contractor. This action shall be considered by the contracting officer upon receipt of a written recommendation to that effect from the CMR. The CMR's recommendation must include a copy of the compliance report and any other relevant correspondence or supporting documentation. Furthermore, if the CMR has a reasonable basis to believe that a contractor has made a false statement to an employee or representative of the Federal Government, or to an employee or representative of the prime contractor, the CMR must report the matter to the SBA Office of Inspector General. All other concerns as to whether a prime contractor or subcontractor has complied with SBA regulations or otherwise acted in bad faith may be reported to the Area Government Contracting Office where the firm is headquartered.

\* \* \* \* \*

(8) The head of the contracting agency shall ensure that:

(i) the agency collects and reports data on the extent to which contractors of the agency meet the goals and objectives set forth in subcontracting plans; and

(ii) the agency periodically reviews data collected and reported pursuant to paragraph (f)(8)(i) of this section for the purpose of ensuring that such contractors comply in good faith with the requirements of this section.

\* \* \* \* \*

21. Amend § 125.5 by adding a paragraph (f)(3) to read as follows:

§ 125.5 What is the Certificate of Competency Program?

\* \* \* \* \*

(f) \* \* \*

(3) Where a contracting officer finds a concern to be nonresponsible for reasons of financial capacity on an indefinite delivery or indefinite quantity task or delivery order contract, the Area Director will consider the firm's maximum financial capacity. If the Area Director issues a COC, it will be for a specific amount that is the limit of the firm's financial capacity for that contract. The contracting officer may subsequently determine to exceed the amount, but cannot deny the firm award of an order or contract on financial grounds if the firm has not reached the financial maximum the Area Director identified in the COC letter.

\* \* \* \* \*

22. Revise § 125.6 by revising the heading and text to read as follows:

§ 125.6 What are the prime contractor's limitations on subcontracting?

(a) General. In order to be awarded a full or partial small business set-aside contract, an 8(a) contract, an SDVO SBC contract, a HUBZone contract, a WOSB or EDWOSB contract pursuant to part 127 of this chapter, with a value greater than \$150,000, a small business concern must agree that:

(1) In the case of a contract for services (except construction), no more than 50% of the amount paid by the government to the prime may be paid to firms, at any tier, that are not similarly situated. Any work that a similarly situated entity further subcontracts to an entity that is not similarly situated will count towards the 50% subcontract amount that cannot be exceeded.

(2) In the case of a contract for supplies or products (other than from a nonmanufacturer of such supplies), no more than 50% of the amount paid by the

government to the prime may be paid to firms, at any tier, that are not similarly situated. Any work that a similarly situated entity further subcontracts to an entity that is not similarly situated will count towards the 50% subcontract amount that cannot be exceeded.

(iii) In the case of a contract for supplies from a nonmanufacturer, the concern shall supply the product of a domestic small business manufacturer or processor, unless a waiver as described in § 121.406(b)(5) of this chapter is granted.

(3) Where a contract combines services and supplies, the contracting officer shall select the appropriate NAICS code as prescribed in § 121.402(b) of this chapter. The contracting officer's selection of the applicable NAICS code is determinative as to which limitation on subcontracting and performance requirement applies. In no case shall the requirements of paragraph (a)(1) and (a)(2) of this section both apply to the same contract. The relevant limitation on subcontracting in paragraph (a)(1) or (a)(2) of this section shall apply only to that portion of the contract award amount.

Example to paragraph (a)(3). A procuring agency is acquiring both services and supplies through a small business set aside. The total value of the requirement is \$3,000,000, with the supply portion comprising \$2,500,000, and the services portion comprising \$500,000. The contracting officer appropriately assigns a manufacturing NAICS code to the requirement. Because the services portion of the contract is excluded from consideration, a small business manufacturer, together with one or more similarly situated small business manufacturers, must perform at least 50% of the cost of manufacturing the supplies or products, or at least 50% of the \$2,500,000 supply portion of the requirement (not including the costs of materials).

(4) In the case of a contract for general construction, no more than 85% of the amount paid by the government to the prime may be paid to firms, at any tier, that are not similarly situated. Any work that a similarly situated entity further subcontracts to an

entity that is not similarly situated will count towards the 15% subcontract amount that cannot be exceeded.

(5) In the case of a contract for special trade contractors, no more than 75% of the amount paid by the government to the prime may be paid to firms, at any tier, that are not similarly situated. Any work that a similarly situated entity further subcontracts to an entity that is not similarly situated will count towards the 75% subcontract amount that cannot be exceeded.

(b) Subcontracts to similarly situated entities. A small business concern prime contractor that receives a contract listed in §125.6(a) and spends contract amounts on a subcontractor that is a similarly situated entity shall not consider those subcontracted amounts as subcontracted for purposes of determining whether the small business concern prime contractor has violated §125.6(a). Moreover, such subcontract to a similarly situated entity shall also be excluded from consideration under the ostensible subcontractor rule (§ 121.103(h)(4)).

(1) A small business concern prime contractor must enter a written agreement with every similarly situated entity to detail the percentage of work forecasted to be performed by each entity. The agreement must identify the solicitation number at issue, be signed by each entity, and be attached to the prime contractor's offer.

(2) Whether particular specific entities perform the forecasted amount of work is not material, as long as the similarly situated entities collectively meet the performance of work requirement.

(3) SBA may consider any party's failure to comply with the spirit and intent of such a subcontract as a basis for debarment on the grounds, including but not limited to,

that the parties have violated the terms of a Government contract or subcontract pursuant to FAR 9.406-2(b)(1)(i).

Example 1 to paragraph (b): An SDVO SBC sole source contract is awarded in the total amount of \$500,000 for hammers. The prime contractor is a manufacturer and subcontracts 51% of the total amount received, less the cost of materials (\$100,000) or \$204,000, to an SDVO SBC subcontractor that manufactures the hammers in the U.S. The prime contractor does not violate the limitation on subcontracting requirement because the amount subcontracted to a similarly situated entity (less the cost of materials) is excluded from the limitation on subcontracting calculation.

Example 2 to paragraph (b): A competitive 8(a) BD contract is awarded in the total amount of \$1,000,000 for janitorial services. The prime contractor subcontracts \$800,000 of the janitorial services to another 8(a) BD certified firm. The prime contractor does not violate the limitation on subcontracting for services because the amount subcontracted to a similarly situated entity is excluded from the limitation on subcontracting.

Example 3 to paragraph (b): A WOSB set-aside contract is awarded in the total amount of \$1,000,000 for landscaping services. The prime contractor subcontracts \$500,001 to an SDVO SBC subcontractor that is not also a WOSB under the WOSB program. The prime contractor is in violation of the limitation on subcontracting requirement because it has subcontracted more than 50% of the contract amount to an SDVO SBC subcontractor, which is not considered similarly situated to a WOSB prime contractor.

(c) Certification to meet limitations on subcontracting. A small business concern submitting an offer for a contract listed in § 125.6(a) must certify that it will meet the applicable limitation on subcontracting. If it is not apparent in the offer that the applicable limitation on subcontracting will be met, the contracting officer may seek a Certificate of Competency pursuant to § 125.5. The procuring agency contracting officer must be satisfied that the small business concern prime contractor will satisfy the applicable limitation on subcontracting at the time of award.

(d) Identify subcontractors and percentage of award amount subcontracted. If a small business concern prime contractor that receives a contract listed in § 125.6(a) intends to use similarly situated entities in order to comply with the limitations on



subcontracting, it must identify the similarly situated entities in its offer and the percentage of the prime contract award amount that will be spent on each similarly situated entity must be identified in a written agreement, in compliance with § 125.6(b).

(e) Modifications of award amount. If the prime contractor modifies a subcontractor's award amount after award of the prime contract, increasing the percentage of the prime contractor's award amount spent on subcontractors that are not similarly situated entities such that the prime contractor is no longer in compliance with the requirements of § 125.6(a), the prime contractor must notify the contracting officer in writing of the change and how the change will affect the prime contractor's compliance with the limitations on subcontracting.

(f) HUBZone procurement for commodities. In the case of a HUBZone contract for the procurement of agricultural commodities, a HUBZone SBC may not purchase the commodity from a subcontractor if the subcontractor will supply the commodity in substantially the final form in which it is to be supplied to the Government.

(g) Request to change applicable limitation on subcontracting. SBA may use different percentages if the Administrator determines that such action is necessary to reflect conventional industry practices among small business concerns that are below the numerical size standard for businesses in that industry group. Representatives of a national trade or industry group or any interested SBC may request a change in subcontracting percentage requirements for the categories defined by six digit industry codes in the North American Industry Classification System (NAICS) pursuant to the following procedures:

(1) Format of request. Requests from representatives of a trade or industry group and interested SBCs should be in writing and sent or delivered to the Director, Office of Government Contracting, U.S. Small Business Administration, 409 3<sup>rd</sup> Street, SW., Washington, DC 20416. The requester must demonstrate to SBA that a change in percentage is necessary to reflect conventional industry practices among small business concerns that are below the numerical size standard for businesses in that industry category, and must support its request with information including, but not limited to:

(i) Information relative to the economic conditions and structure of the entire national industry;

(ii) Market data, technical changes in the industry and industry trends;

(iii) Specific reasons and justifications for the change in the subcontracting percentage;

(iv) The effect such a change would have on the Federal procurement process;

and

(v) Information demonstrating how the proposed change would promote the purposes of the small business, 8(a), SDVO, HUBZone, WOSB, or EDWOSB programs.

(2) Notice to public. Upon an adequate preliminary showing to SBA, SBA will publish in the Federal Register a notice of its receipt of a request that it considers a change in the subcontracting percentage requirements for a particular industry. The notice will identify the group making the request, and give the public an opportunity to submit information and arguments in both support and opposition.

(3) Comments. SBA will provide a period of not less than 30 days for public comment in response to the Federal Register notice.

(4) Decision. SBA will render its decision after the close of the comment period. If SBA decides against a change, SBA will publish notice of its decision in the Federal Register. Concurrent with the notice, SBA will advise the requester of its decision in writing. If SBA decides in favor of a change, SBA will propose an appropriate change to this part.

(h) Determining compliance with applicable limitation on subcontracting. The period of time used to determine compliance for a total or partial set-aside contract will be the base term and then each subsequent option period. For an order set aside under a full and open contract or a full and open contract with reserve, the agency will use the period of performance for each order to determine compliance unless the order is competed amongst small and other-than-small businesses (in which case the subcontracting limitations will not apply).

(1) The contracting officer, in his or her discretion, may require the concern to perform the applicable percentage of work or comply with the nonmanufacturer rule for each order awarded under a total or partial set aside contract.

(2) Compliance will be considered an element of responsibility and not a component of size eligibility.

(i) Small Business Teaming Arrangements (SBTAs). Where an offeror is exempt from affiliation under § 121.103(b)(9) of this chapter and qualifies as a small business concern for a reserve of a bundled contract, the limitations on subcontracting apply to the cooperative effort of the small business team members of the Small Business Teaming Arrangement, not its individual members. The contracting officer must document a small business concern's compliance with the limitations on subcontracting as part of the small

business' performance evaluation in accordance with the procedures set forth in FAR 42.1502. The contracting officer must also evaluate compliance for future contract awards in accordance with the procedures set forth in FAR 9.104-6.

(j) Inapplicability of limitations on subcontracting. The performance requirements (limitations on subcontracting) do not apply to: (1) small business set-aside contracts with a value greater than the micro-purchase threshold but not greater than the simplified acquisition threshold; or (2) subcontracts.

(k) Penalties. Whoever violates the requirements set forth in §125.6(a) shall be subject to the penalties prescribed in 15 U.S.C. § 645(d), except that the fine shall be treated as the greater of \$500,000 or the dollar amount spent, in excess of permitted levels, by the entity on subcontractors.

23. Amend § 125.15 by revising paragraphs (a)(3), (b)(1), and (b)(3) to read as follows:

§ 125.15 What requirements must an SDVO SBC meet to submit an offer on a contract?

(a) \* \* \*

(3) It will comply with the limitations on subcontracting requirements set forth in § 125.6;

\* \* \* \* \*

(b) \* \* \*

(1) Size of concerns to an SDVO SBC joint venture. A joint venture of at least one SDVO SBC and one or more other business concerns may submit an offer as a small business for a competitive SDVO SBC procurement, or be awarded a sole source SDVO

contract, so long as each concern is small under the size standard corresponding to the NAICS code assigned to the procurement.

\* \* \* \* \*

(3) Limitations on subcontracting. For any SDVO contract, the joint venture must comply with the applicable limitations on subcontracting required by § 125.6 of this chapter.

\* \* \* \* \*

§ 125.20 [Amended]

24. Amend § 125.20 as follows:
- a. In paragraph (b)(1), remove “\$5,500,000” and add in its place “\$6,000,000”;
- and
- b. In paragraph (b)(2), remove “\$3,000,000” and add in its place “\$3,500,000”.

§ 125.26 [Amended]

25. Amend § 125.26 by removing the phrase “Associate Administrator for Government Contracting” and adding in its place the phrase “Director, Office of Government Contracting” in paragraph (b).

PART 126—HUBZONE PROGRAM

26. The authority citation for Part 126 continues to read as follows:
- Authority: 15 U.S.C. 632(a), 632(j), 632(p), 644, and 657a.
27. Amend § 126.200 by revising paragraph (b)(6) and removing paragraph (d) to read as follows:

§ 126.200 What requirements must a concern meet to receive SBA certification as a qualified HUBZone SBC?

\* \* \* \* \*

(b) \* \* \*

(6) Subcontracting. The concern must represent, as provided in the application, that it will comply with the applicable limitations on subcontracting requirements in connection with any procurement that it receives as a qualified HUBZone SBC, as set forth in § 126.5 and § 126.700.

\* \* \* \* \*

28. Amend § 126.601 by revising paragraph (f) to read as follows:

§ 126.601 What additional requirements must a HUBZone SBC meet to bid on a contract?

\* \* \* \* \*

(f) A qualified HUBZone SBC may submit an offer on a HUBZone contract for supplies as a nonmanufacturer if it meets the requirements of the nonmanufacturer rule set forth at § 121.406 of this chapter.

\* \* \* \* \*

29. Amend § 126.700 by revising the title and text to read as follows:

§ 126.700 What are the limitations on subcontracting requirements for HUBZone contracts?

A prime contractor receiving an award as a qualified HUBZone SBC must meet the limitations on subcontracting requirements set forth in § 125.6 of this chapter.

PART 127—WOMEN-OWNED SMALL BUSINESS FEDERAL CONTRACT PROGRAM

30. The authority citation for Part 127 continues to read as follows:

Authority: 15 U.S.C. 632, 634(b)(6), 637(m), and 644.

31. Amend § 127.504 by revising paragraph (b) to read as follows:

§ 127.504 What additional requirements must a concern satisfy to submit an offer on an EDWOSB or WOSB requirement?

\* \* \* \* \*

(b) The concern must also meet the applicable limitations on subcontracting requirements as set forth in § 125.6 of this chapter.

32. Amend § 127.506 by revising paragraphs (a) and (d) to read as follows:

§ 127.506 May a joint venture submit an offer on an EDWOSB or WOSB requirement?

\* \* \* \* \*

(a) Size of concerns. A joint venture of at least one WOSB EDWOSB and one or more other business concerns may submit an offer as a small business for a competitive WOSB or EDWOSB procurement so long as each concern is small under the size standard corresponding to the NAICS code assigned to the procurement;

\* \* \* \* \*

(d) The joint venture must comply with the limitations on subcontracting, as required by § 125.6 of this chapter;

\* \* \* \* \*

Dated: December 10, 2014.

Maria Contreras-Sweet,  
Administrator.

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