



SMALL BUSINESS ADMINISTRATION

13 CFR Part 121

RIN: 3245-AH16

Small Business Size Standards: Calculation of Annual Average Receipts

AGENCY: U.S. Small Business Administration.

ACTION: Final rule.

SUMMARY: The U.S. Small Business Administration (SBA or Agency) is modifying its method for calculating average annual receipts used to prescribe size standards for small businesses. Specifically, in accordance with the Small Business Runway Extension Act of 2018, SBA is changing its regulations on the calculation of average annual receipts for all of SBA's receipts-based size standards, and for other agencies' proposed receipts-based size standards, from a 3-year averaging period to a 5-year averaging period, outside of the SBA Business Loan and Disaster Loan Programs. SBA intends to seek comment on the Business Loan and Disaster Loan Programs in a proposed rule through a separate rulemaking. For all other programs, SBA adopts a transition period through January 6, 2022, during which firms may choose between using a 3-year averaging period and a 5-year averaging period.

DATES: This rule is effective January 6, 2020.

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SUPPLEMENTARY INFORMATION:

Background Information

Public Law 115-324 (the “Small Business Runway Extension Act of 2018”) amended section 3(a)(2)(C)(ii)(II) of the Small Business Act, 15 U.S.C. 632(a)(2)(C)(ii)(II), to modify the requirements for proposed small business size standards prescribed by an agency without separate statutory authority to issue size standards.

Under section 3(a)(2)(C)(ii) of the Small Business Act, as amended, an agency without separate statutory authority to issue size standards must satisfy three requirements to prescribe a size standard. First, the agency must propose the size standard with an opportunity for public notice and comment. Second, the agency must provide for determining the size of a manufacturing concern based on a 12-month average of the concern’s employment, the size of a services concern based on a 5-year average of gross receipts, and the size of another business concern on the basis of data of not less than 3 years. Third, the agency must obtain approval of the contemplated size standard from the SBA Administrator.

In contrast to agencies subject to section 3(a)(2)(C), SBA has independent statutory authority to issue size standards. Under section 3(a)(2)(A) of the Small Business Act, the SBA Administrator may specify detailed definitions or standards by which a business concern may be determined to be a small business concern for the purposes of SBA’s programs or any other Federal Government program. Section 3(a)(2)(B) of the Small Business Act further provides that such definitions may utilize the number of employees, dollar volume of business, net worth, net income, a combination thereof, or other appropriate factors. To determine eligibility for Federal small business assistance,

SBA establishes detailed size definitions for small businesses (usually referred to as “size standards”) that vary from industry to industry reflecting differences among the various industries. SBA typically uses two primary measures of business size for size standards purposes: (i) average annual gross receipts for businesses in services, retail trade, agricultural, and construction industries, and (ii) average number of employees for businesses in all manufacturing, most mining and utilities industries, and some transportation, information and research and development (R&D) industries. SBA uses financial assets for certain financial industries and refining capacity, in addition to employees, for the petroleum refining industry to measure business size standards purposes.

The SBA’s size standards are used to establish eligibility for a variety of Federal small business assistance programs, including for Federal Government contracting and business development programs designed to assist small businesses in obtaining Federal contracts and for SBA’s loan guarantee programs, which provide access to capital for small businesses that are unable to qualify for and receive conventional loans elsewhere. The Federal Government contracting programs that use SBA’s size standards include the SBA’s 8(a) Business Development (BD) program, the Historically Underutilized Business Zones (HUBZone) program, the Service Disabled Veteran-Owned Small Business (SDVOSB) program, the Women-Owned Small Business (WOSB) program, and the Economically Disadvantaged Women-Owned Small Business (EDWOSB) program. SBA’s Small Business Investment Company (SBIC), Certified Development Company (CDC/504), and 7(a) loan programs use either the industry-based size standards

or tangible net worth and net income based alternative size standards to determine eligibility for those programs.

SBA has long interpreted section 3(a)(2)(C) of the Small Business Act as not applying to SBA's size standards issued under section 3(a)(2)(A). In the preambles to the proposed and final rules implementing 3(a)(2)(C), SBA explained that the Small Business Act requires that other Federal agencies either use SBA's size standards or use their own size standards that meet the requirements as set forth in that section. 65 FR 4176 (Jan. 26, 2000) and 67 FR 13714 (March 26, 2002). In the final implementation in 2002, SBA interpreted section 3(a)(2)(C) as applying only to non-SBA agencies, stating, "Unless a statute specifies size standards for an agency's program or gives an agency direct authority to establish size standards, the agency must use the applicable size standards established by SBA." However, the Act allows an agency to "prescribe a size standard for categorizing a business concern as a small business concern (see sec. 3(a)(2)(C) of the Act) provided that the contemplated size standard meets certain criteria, and the agency obtains approval of the SBA Administrator." 67 FR 13714. For further details on section 3(a)(2)(C) not applying to SBA's size standards, see the proposed rule (84 FR 29399).

Nevertheless, to promote consistency government-wide on small business size standards, on June 24, 2019 (84 FR 29399), SBA issued for comments a proposed rule to change its method for calculating average annual receipts for all SBA's receipts-based size standards and other agencies' proposed receipts-based size standards for firms in services industries from a 3-year averaging period to a 5-year averaging period.

SBA determined that it would be confusing for a service-industry business concern to use a 3-year average for SBA's receipts-based size standards and switch to a

5-year average for another agency's receipts-based size standards. Similarly, it would be confusing to apply SBA's size standards for a business that is engaged in both service- and non-service industries to use a 5-year average for determining small business status in a service industry but switch to a 3-year average for a non-service industry. Thus, although section 3(a)(2)(C), as amended, permits another agency to use a 3-year average outside of the service industries, SBA is adopting a 5-year averaging period for calculating the annual receipts of businesses for all industries that are subject to its receipts-based size standards, including the retail trade, agricultural, and construction industries.

In accordance with Public Law 115-324, SBA proposed to change the averaging period for calculating annual receipts for other agencies' receipts-based size standards for firms in services-industries from 3 years to 5 years and to maintain the 3-year averaging period for calculating the size for non-services firms. To promote consistency and avoid confusion, in this final rule, SBA is adopting the same 5-year averaging period for all receipts-based size standards issued by other agencies as well. More than 40 comments to the proposed rule, as discussed below, expressed support for adopting the same 5-year averaging period for all SBA receipts-based size standards. Of those, 3 also recommended using the same averaging period for all receipts-based size standards prescribed by other agencies.

This final rule carries out the intent of Public Law 115-324, as expressed in the Report of the House Committee on Small Business, H. Rpt. 115-939, with respect to Federal procurement opportunities. The Committee report states that, to help advanced small businesses successfully navigate the middle market as they reach their small

business size thresholds, the bill would lengthen the time in which the SBA measures size through revenue, from the average of the past 3 years to the average of the past 5 years. The Committee report states that the bill would reduce the impact on small businesses from rapid growth in some years which would result in spikes in revenue that may prematurely eject a small business out of their small business status. The Committee report adds that the bill would allow small businesses at every level more time to grow and develop their competitiveness and infrastructure, before entering the open marketplace. The bill, as the Committee report states, would also protect Federal investment in SBA's small business procurement programs by increasing chances of success in the middle market for newly graduated firms, resulting in enhanced competition against large prime contractors.

As stated in the Committee report, during the period when annual revenues are rising, the 5-year average will generally be lower than the 3-year average, thereby allowing: (i) mid-sized businesses who have just exceeded size standards to regain their small business status, and (ii) advanced small businesses close to exceeding the size standard to retain their small business status for a longer period. In the proposed rule, SBA noted that, when annual revenues are declining, the 5-year average may be higher than the 3-year average. This would cause small businesses near the size thresholds to lose their small business status sooner under the 5-year average than under the 3-year average. This is more likely to happen during economic downturns. Businesses that lose their small business status under the 5-year average may be disadvantaged further because they may have to wait several years more to regain their small business status, as compared to under a 3-year average. The proposed rule added that newly established

firms that have been in business for less than 5 years will receive no benefit from a change to a 5-year average. A firm that has been in business for less than the averaging period simply annualizes the receipts from its full existence.

Additionally, SBA also stated in the proposed rule that by enabling mid-size businesses to regain small business status and by lengthening the small business status of advanced and successful larger small businesses, the longer averaging period may disadvantage smaller small businesses in more need of Federal assistance than their more advanced and larger counterparts in competing for Federal opportunities. Similar to concerns from mid-size businesses that they lack necessary resources, past performance qualifications, and expertise to be able to compete against very large businesses in the full and open market, SBA has also received concerns from smaller small businesses that they also lack resources, past performance qualifications, and expertise to be able to compete against more resourceful, qualified, and experienced larger small businesses for Federal opportunities for small businesses.

In its June 24, 2019 proposed rule, SBA sought comments on its proposal to change the averaging period for the calculation of average annual receipts for all receipts-based size standards from 3 years to 5 years.

1. SBA sought feedback, along with supporting facts and analyses, on whether the Agency should calculate average annual receipts over 5 years for all industries subject to receipts-based size standards and on whether it should use a 5-year average annual receipts for businesses in services industries only and continue using a 3-year average annual receipts for other businesses. SBA was concerned that the latter option may create confusion for both businesses in reporting their size based on average

annual receipts and contracting personnel in verifying the size of bidders to Federal contracts.

2. SBA sought input on how the use of average annual receipts over 5 years instead of 3 years would impact both smaller small businesses and more advanced, larger small businesses in terms of getting access to Federal opportunities for small businesses.

Additionally, SBA requested comments on its clarification of how annual receipts should be calculated in connection with the acquisition or sale of a division. The proposed rule provided that the annual receipts of a concern would not be adjusted where the concern sells or acquires a segregable division during the applicable period of measurement. This is distinct from how SBA treats the sale or acquisition of a subsidiary that is a separate legal entity.

In this final rule, SBA adopts the changes as stated in the proposed rule, with two modifications. First, in response to comments, SBA is not including the 7(a) Loan Program, the Microloan Program, the Intermediary Lending Pilot Program, and the Development Company Loan Program (collectively, the “Business Loan Programs”) in this present change. SBA also is not including Physical Disaster Business Loans, Economic Injury Disaster Loans, Military Reservist Economic Injury Disaster Loans, and Immediate Disaster Assistance Program loans (collectively, the “Disaster Loan Programs”). At a later date, SBA will issue a proposed rule to seek additional input to assess the impact of any changes to the Business Loan and Disaster Loan Programs. Second, for all other SBA programs, including the Federal procurement programs, SBA adopts a two-year transition period through January 6, 2022. During the transition period,

a firm may choose between calculating receipts using a 3-year average or a 5-year average.

Discussion of Comments

SBA received a total of 217 comments to the proposed rule, of which 5 were not pertinent to the scope of the proposed rule. Of the 212 comments that were pertinent, 140 commenters (including more than 10 trade associations, small and mid-size business groups, and small business advocacy organizations) fully supported the proposed rule; 5 comments supported the change to a 5-year averaging period but opposed SBA's proposal not to adjust receipts for the sale or acquisition of a segregable division; 28 comments did not oppose the change to a 5-year averaging period but opposed the use of 5 years of tax returns to analyze any loan program requirement other than size; 37 comments opposed the change to a 5-year averaging period; and 2 comments could not be categorized as either supporting or opposing the proposed rule. All of these comments are available at www.regulations.gov (RIN 3245-AH16), are summarized and discussed below in terms of various categories of comments, and are accompanied by SBA's responses.

Comments on Using a 5-Year Averaging Period for All Receipts-Based Size Standards

SBA requested comments on whether it should use a 5-year averaging period for all of its receipts-based standards (i.e., for both services industries and non-services industries) or only for services industries. Forty-one commenters responded to this issue, all of which supported using the 5-year averaging period for all SBA's receipt-based size standards. Three of those comments also supported using the 5-year averaging period for

other agencies' size standards for non-services industries that are subject to receipts-based size standards.

Commenters expressed support for expanding the 5-year averaging period to all receipt-based size standards for a variety of reasons. For example, one organization agreed with SBA that using different formulas for calculating size in different industries may create confusion, adding that “using different formulas could incentivize NAICS appeals as contractors jockey for a code that not only uses their preferred size standard, but also their preferred number of years in the calculation of size.” Similarly, another organization supported the expansion of the 5-year averaging period for all receipts-based size standards because maintaining a separate averaging period for non-services industries would lead to confusion for small firms in that some firms would be small under one NAICS code but other-than-small under another NAICS code with the same or higher size standard. The organization explained that maintaining a 3-year averaging period for non-services industries would “leave companies that have multiple capabilities to potentially be small under their services NAICS code, but not under other NAICS of work they perform.” Another organization supported applying the 5-year averaging period to all receipts-based size standards because it would “reduce the burden on small businesses in determining which size standard to apply to a given procurement.”

However, some commenters opposed the move to a 5-year averaging period on the grounds that this would increase paperwork and compliance burden on lenders and borrowers of the SBA's loans. These commenters suggested, as discussed below, that SBA retain the current 3-year averaging period for calculating annual revenues for

services firms for the SBA's financial assistance programs, if SBA decides to adopt the proposed 5-year averaging period elsewhere.

SBA's response:

SBA agrees with the commenters that, in applying SBA's size standards, separating out services industry firms from non-services firms would cause confusion and create a greater compliance burden on firms that participate in both services industries and non-services industries. SBA also agrees that using a 5-year averaging period for services industries and a 3-year averaging period for non-services industries can lead to an inconsistent result of making a business small in one NAICS code and other than small in another NAICS code with a same or higher size standard. SBA also finds that it will be equally confusing to use, in the same industry, a 5-year averaging period for the SBA's size standard and a 3-year averaging period for other agencies' size standards. To avoid such confusion and inconsistency, in this final rule, SBA is adopting the 5-year averaging period for calculating the average annual receipts for all SBA's receipts-based size standards. For the same reason, SBA is also adopting the same 5-year averaging period for both services and non-services industries when approving receipt-based size standards by other federal agencies.

Comments on Moving From a 3-Year Averaging Period to a 5-Year Averaging Period

Comments Supporting the 5-Year Averaging Period

Of the 212 pertinent comments received, 173 (or approximately 82%) supported the SBA's proposal to change its method for calculating annual receipts from a 3-year averaging period to a 5-year averaging period, although some of those comments rejected

other aspects of the proposed rule. Commenters expressed support for the proposed change for a variety of reasons, as discussed below.

A vast majority of commenters maintained that the proposed change would benefit small businesses that are either about to exceed or have just exceeded the relevant size standards (often referred to as “mid-size businesses”) by allowing them more time to develop capabilities, strengthen and diversify experience, and build resources, thus enabling them to compete successfully for unrestricted opportunities in the full-and-open market with very large businesses that have extensive capabilities, experience, and past-performance qualifications. Several commenters shared that a transition from “small” to “other-than-small” status is much more difficult than a transition from “very small” to “small” status. Some indicated that a longer lookback period would also ameliorate the current dilemma growing small businesses face in the Federal market when they exceed their size standards: deciding whether to restrain growth to remain small (and avoid the difficulty of competing in a full-and-open environment), sell, or go out of business.

Another common comment was that the change from a 3-year averaging period to a 5-year averaging period will be very helpful to small businesses of every size, especially those that have successfully grown to revenues above the 3-year average for their respective NAICS codes. Some commenters expressed support for the proposed change because the 5-year averaging method would promote fairness and increase the accuracy of size representation. For example, one commenter explained that “one abnormally successful year could cause a small business to size out of the standard. Amortizing a year of success over five years instead of three will likely lengthen a small business’ eligibility period and be a more accurate reflection of that business’ true

operations.” Another commenter explained that a firm’s temporary spike in revenue “may not have resulted in increased infrastructure for the firm such that it will be ready to compete in the open market.” Several other commenters expressed support for the proposed rule because it would give advanced small firms more time to take advantage of SBA small business assistance programs. Similarly, another commenter explained that “Nurturing small business capabilities is important because it results in more price competition, it spurs innovation, and helps create jobs.” Other commenters expressed that growing small businesses should be rewarded for their success with a longer lookback averaging period.

Commenters also expressed support for the proposed change because it would increase the total number of small businesses and strengthen the Federal small business industrial or supplier base. Several commenters maintained that, with the availability of more businesses qualifying as small, the move to a 5-year averaging period would increase set-aside opportunities for all small businesses as the agencies are likely to set aside more contracts for small businesses. Other commenters expressed that an expanded pool of small businesses would benefit the Federal government by providing a larger and more stable pool of qualified small businesses in the Federal procurement market. The Federal government also will benefit from lower prices for its procurements due to increased competition, and from reduced risks by allowing agencies to retain their trusted and qualified incumbent small business contractors for a longer period. Several commenters also maintained that, with more businesses qualifying as small under the 5-year receipts average, the change also would provide large prime contractors with a

robust pool of qualified small businesses to draw from to meet their small business subcontracting requirements.

Several commenters also expressed support for the proposed change because it would reduce the impacts of unusual spikes in revenues in some years on growing small businesses and enable them to adjust to revenue swings due to fluctuations in economic conditions, business environment, and changes in the Federal market. For example, one commenter explained that it is increasingly common for the government to utilize larger and longer indefinite delivery, indefinite quantity (IDIQ) contract vehicles, where one high-valued contract or task order can throw a small business out of its small business status. Some commenters supporting the proposed rule also stated that, under the 5-year averaging period, growing small businesses will be able to maintain their small business status for a longer period and, as a consequence, achieve and sustain growth. A number of comments also supported the SBA's proposal to remove "Schedule K" from the definition of receipts.

SBA's response:

SBA agrees with commenters that this rule will benefit small businesses, the Federal Government, and large businesses. With an expanded pool of small businesses, the Federal Government will have more qualified small businesses to choose from, and as a result, likely will set aside more contracts for small businesses. SBA also agrees with commenters that the 5-year averaging period will allow more small firms to benefit from SBA's small business assistance programs by extending their small business status for a longer period. The change would also enable small businesses that have just exceeded their size standards to regain their small business status and to benefit from Federal small

business assistance. SBA believes that the change to a 5-year averaging period will expand benefits to all small businesses over the long-run, although the proposed change would have led to some negative impacts in the short-run. Accordingly, in this final rule, except for the Business Loan and Disaster Loan Programs, SBA is amending its regulations on the calculation of average annual receipts for all receipts-based SBA size standards from a 3-year averaging period to a 5-year averaging period, with a transition period through January 6, 2022, during which firms (and their affiliates) can choose either a 3-year or a 5-year averaging period. SBA is also removing “Schedule K” from the definition of receipts, as proposed.

Opposing Comments

Of 212 pertinent comments that SBA received, 37 opposed the change to the averaging period for annual receipts calculation from 3 years to 5 years. Comments that opposed the proposed rule mostly focused on one or more of the following three issues: (1) disadvantages to firms with declining revenues, (2) undue advantages to “larger” small businesses, and (3) additional burden on borrowers and lenders. Below, SBA summarizes each of the three comment categories listed above.

(1) Disadvantages to Firms with Declining Revenues. Of the 37 comments opposing the shift to a 5-year averaging period, 7 commenters opposed the rule based on the reason that a 5-year averaging period would disadvantage firms with declining revenues. Of these 7 commenters, 2 affirmatively stated that their firm’s size status would change from small to other-than-small as a result of the shift to a 5-year averaging period. Several commenters opposing the proposed rule observed that it will take longer for small businesses to qualify as small again once they have exceeded the size standard.

Other commenters noted that the proposed rule would harm small firms with declining revenues, causing them to lose their small business size status sooner under the 5-year average receipts as compared to the 3-year receipts. One commenter explained that “while increasing the receipts lookback period from 3 years to 5 years will benefit many growing companies, it could also be detrimental to businesses that have experienced declining revenues, as it would cause many such businesses to lose their small business status despite declining receipts.” Another commenter stated that it was unfair for small businesses to be “penalized” for having declining revenues. The commenter explained that business concerns that face a downturn “should not be penalized, by being excluded from eligibility for SBA's small business programs....Such an outcome would be an unintended negative consequence of the Act.” Some commenters contended that the proposed change primarily benefits growing and more successful larger small businesses by enabling them to maintain their small business status longer and better prepare for a successful transition to the full-and-open market, but it hurts emerging and smaller small businesses that are in need of the SBA assistance the most.

SBA's response:

SBA acknowledges that the move from a 3-year averaging period to a 5-year averaging period could, as an unintended negative impact, cause some small businesses that are close to their size standard to lose their small business status immediately or subsequently during the period of declining annual revenues. SBA agrees that a firm that exceeds the size standard based on a 5-year average, but then has subsequent years of declining revenues, will face a longer period before regaining its small business status. In order to mitigate this impact, in this final rule, except for the Business Loan and Disaster

Loan Programs, SBA is providing a transition period until January 6, 2022, during which firms will be allowed to choose either the 3-year receipts average or 5-year receipts average for size eligibility purposes.

(2) Undue Advantages to “Larger” Small Businesses. Of the 37 comments opposing the shift to a 5-year averaging period, 5 comments opposed the proposed rule on the grounds that it may give an undue advantage to “larger” small businesses near the industry size threshold to the detriment of “smaller” small businesses in competing for small business opportunities. One commenter expressed concerns that the move to the 5-year averaging period lacked benefits for “smaller” small firms that need SBA’s assistance the most. The commenter explained that by extending the measurement period, it only allows for companies to resist growth, control revenue and continue to be small. This process, if extended, will only provide a further advantage to those who are on the upper limit but does nothing to help those who are truly small.

A number of commenters opposed the rule because it will allow companies to continue to be small businesses after the period at which those businesses should transition to other-than-small business status, making it difficult for smaller small businesses to compete against their larger counterparts under the 5-year averaging period. One commenter, expressing concerns about this issue, explained that the proposed rule would “keep start-up small businesses from competing for small business set-aside opportunities...and allow ‘extended’ small businesses with contracts to out compete those businesses that are truly ‘small.’” Some of these commenters raised industry-specific concerns.

SBA’s response:

SBA acknowledges that smaller small firms could face some disadvantages in competing for set-aside contracts against a larger pool of small firms, especially against the newly qualified larger small businesses and advanced small businesses who are able to remain small for a longer period. However, as detailed in SBA's benefit-cost analysis of the proposed rule, the change from a 3-year averaging period to a 5-year averaging period will increase the total number of small businesses, which would, because of greater potential small business competition for government contracts, likely lead to expansion of set-aside opportunities for all small businesses. In addition, as some commenters stated, that "smaller" small firms may not be in direct competition with "larger" small firms due to differences in their missions, capabilities, and resources, and therefore, would not face negative impacts from an increase in the number of "larger" small firms. As one organization commenting on the proposed rule explained, "these emerging small companies tend to have their own swim lanes, and do not typically compete against 'larger' small businesses directly and in some cases do not compete in the federal market all."

The contracts awards data also shows that in most industries the majority of small business contract dollars go to businesses that are substantially smaller than their size standards. The results from some industries with recent large increases to size standards also reveal that small businesses under the previous size standards continue to receive the same amount of contract dollars as before the increase. SBA agrees that the move to a 5-year averaging method is likely to benefit advanced small businesses that have just exceeded or are about to exceed their size standards more than their smaller counterparts

in the short-run, but in the long-run it will benefit all small businesses at every level as they continue to grow and approach the size standard.

(3) *Additional Burden on Borrowers and Lenders.* Of the 37 comments opposing the shift to a 5-year averaging period, 23 (including one trade association representing lenders serving small businesses under the SBA CDC/504 loan program) opposed the move to the 5-year average because the change would cause undue additional burden on borrowers and lenders under the Business Loan Programs. An additional 28 commenters (including another trade association representing lenders serving small businesses under the SBA's 7(a) loan program) also expressed similar concern that the 5-year averaging would result in an undue additional burden on borrowers and lenders participating in the Business Loan Programs, but they did not specifically oppose the shift to a 5-year averaging period for SBA's revenue-based size standards.

A majority of these commenters included members of those two trade associations in support of the position of their respective associations. Some commenters opposed the rule on the basis that it may require SBA Lenders to collect and review two additional years of tax returns or financial statements to establish eligibility for the SBA's loan programs. Some of these commenters expressed concerns that this will add costs to loan processing, increase turn-around times, and discourage small businesses from participating in the SBA's loan programs. One trade association commented that "the process for obtaining an SBA loan already requires extensive documentation from a small business, and this additional requirement increases that burden without any underlying benefit to the small business." The trade association requested that SBA "give

consideration to allowing the service-industry size standard calculation to remain at its current 3-year averaging period for the SBA loan guarantee programs.”

Some commenters noted that a central premise of the proposed change appears to address the concern that the current 3-year averaging method “ejects” growing small businesses from Federal small business contracting programs before they are ready to compete in the full and open market. They stated that there is no such concern as it relates to the SBA’s loan programs, as small businesses seeking or obtaining SBA’s loans are rarely “ejected” from eligibility due to size.

Several commenters asked that SBA clarify that the 5-year averaging period is intended to apply only to SBA’s receipts-based size standards, not for any other loan application purpose. One trade association commented that “Tax return information is used for multiple purposes related to the loan application process,” including verifying an applicant’s historical cash flow, income, or tax payment history. The trade association further explained, “None of those purposes would require or substantially benefit from a look-back period greater than 3 years.” A trade association and a number of other commenters asked that SBA exempt the SBA’s loan programs from the change, allowing SBA lenders to continue to apply a 3-year receipts average. Other commenters (including a trade association representing 7(a) lenders) requested that SBA’s final rule “[S]pecifically include language clarifying that the longer 5-year period is intended to apply only for purposes of determining size for loan applicants using SBA’s traditional revenue-based sized standards, and not for any other loan application purpose.”

SBA’s response:

In response to comments regarding the burden of the rule on SBA Lenders and loan applicants, SBA has determined that the Business Loan and Disaster Loan Programs should not be included in this final rule. SBA included the Business Loan and Disaster Loan Programs in the proposed rule's cost-benefit analysis, but, otherwise, the initial proposed rule did not discuss the effect that the rule would have on SBA Lenders and loan program participants. Based on the comments expressing that SBA Lenders and loan program applicants would experience burden, SBA will seek additional comment and public input through a proposed rule at a later date to determine how best to consider changes to size eligibility in the Business Loan and Disaster Loan Programs. Through this later proposed rule, SBA intends to ask for data and additional detail about the burden faced by SBA Lenders and applicants, and for comment on any benefit that applicants might obtain through a longer averaging period for determining eligibility for SBA's Business Loan and Disaster Loan Programs.

Comments on Calculating of Average Receipts After the Sale or Acquisition of a Segregable Division

SBA received 20 comments responding to its proposed clarification on the calculation of the annual receipts of a concern where the concern sells or acquires a segregable division during the applicable period of measurement. Of those 20 comments, 3 comments agreed with SBA's proposed clarification, 5 comments disagreed, 11 comments requested further clarification, and 1 comment was not clear as to its stance on this issue.

The 3 commenters who agreed with SBA's proposed treatment of the sale or acquisition of a segregable division emphasized that the receipts of a division remain the

receipts of the selling concern even after it is sold and that the receipts of an acquired division prior to the acquisition do not become the receipts of the acquiring concern after the acquisition. One association commenting on the proposed rule stated that it supports SBA's position because it "provides clarity to the community with regard to the application of the former affiliate rule." The same association also requested that SBA expand the scope of its clarification to include segregable divisions and "other assets not held as a separate legal entity." The association stated that such an expansion would "ensure that SBA's clarification applies to the sale or purchase of non-segregable assets as well, e.g., when an entity acquires the assets performing a specific contract."

The 5 commenters who disagreed with SBA's proposed treatment of the sale or acquisition of a segregable division stated that (1) it elevates form over substance in distinguishing between a division and a subsidiary that is a separate legal entity, (2) it would create a burden for businesses seeking to benefit from selling off a division by moving all of its assets to a newly created subsidiary, (3) it would harm businesses that relied on current SBA policy when selling segregable divisions and were small as a result of the sale, and (4) it would create unpredictability and uncertainty in good-faith size status calculations.

The 11 commenters who requested further clarification all stated (1) that they would have liked to see proposed regulatory text, and (2) that the Office of Hearings and Appeals (OHA) cases that SBA cited in the proposed rule do not make a distinction between divisions and subsidiaries. One commenter cited two additional OHA decisions which it believes contradict SBA's distinction between a division and subsidiary. The commenter stated that in the proposed rule, "SBA cites a quotation from such a decision

which provides that ‘a firm which acquires most of the assets of a *subsidiary or division* of a larger firm is affiliated only with that *subsidiary or division*, and not with the entire parent company’ (emphasis added). As such, it appears that SBA’s Office of Hearings and Appeals does not, in fact, make a distinction between divisions and subsidiaries.”

SBA’s response:

SBA agrees with the commenters who stated that the receipts of a sold division remain the receipts of the selling concern after the sale, just as the receipts of an acquired division prior to its acquisition should not be treated as the receipts of the acquiring concern prior to the acquisition. SBA believes that it is not logical to allow a firm to exclude the receipts of a former division just because that division was sold, since those receipts accrued to the concern.

SBA believes that there really is a difference between the sale or acquisition of a segregable division as opposed to the sale or acquisition of a separate legal entity. The sale or acquisition of a division is not a question of affiliation. It simply represents an addition or subtraction to the concern itself. This is distinct from the sale or acquisition of a separate legal entity, which implicates questions of affiliation.

Regarding the OHA cases cited by the commenters, none of these decisions speak specifically to how receipts should be calculated after the sale or acquisition of a segregable division. However, as stated by several commenters, SBA is not obligated to follow OHA decisions when putting forth changes to its regulations.

For all the reasons above, SBA is adding the language to §§ 121.104(d)(4) and 121.106(b)(4)(ii) to clarify that the former affiliate rule does not permit a concern to

adjust its receipts when the concern sells a segregable division that is not a separate legal entity.

Comments on the Exemption from the 5-Year Averaging Period

Although not specifically requested in the proposed rule, SBA received 31 comments requesting some sort of alternative option which would allow firms to use either a 3-year average or 5-year average of annual receipts depending on which one would be more advantageous to them. The comments proposing such an option suggested that the 3-year vs. 5-year option be for available for a specific period or be made permanent. Of the 31 total comments addressing this issue, 13 commenters recommended using a transition period of 2 years or less; 12 recommended a transition of 3 or more years; 4 suggested making the transition period permanent; and 2 did not specify a duration.

In support of the transition period were commenters both for and against the shift to a 5-year averaging period for calculating annual receipts. Of the 31 comments supporting a transition period, 20 supported the proposed rule; 5 opposed the proposed rule; 5 supported some elements while opposing others; and 1 comment did not express support or opposition to the move from a 3-year averaging period to a 5-year averaging period but recommended that SBA consider the transition period as an alternative to mitigate the impact on businesses that are currently small under the 3-year receipts average but would become other-than-small under the 5-year average receipts.

SBA found that these commenters supported the adoption of a transition period for two reasons: (1) to ensure an organized and transparent implementation of the final rule, and (2) to minimize harm to small firms with declining revenues or to those

becoming other than small under the 5-year receipts upon the implementation of the final rule.

For example, one commenter suggested that SBA implement a 2-year transition period to reduce confusion and uncertainty for small firms that have occurred since the Small Business Runway Extension Act was signed into law. The commenter explained that “some firms have been submitting proposals using a 3-year average in accordance with the SBA’s guidance, while others have used a 5-year average in accordance with the new law. Due to this uncertainty, [Commenter] recommends allowing a two-year transition period for small companies...” Another commenter recommended that SBA “provide for a reasonable transition period for implementation to allow government systems to be updated and to give the contractor community time to properly implement the size calculation change.”

One commenter, expressing concern regarding the proposed rule’s impact on firms with declining revenues, explained that “While increasing the look-back period from 3 years to 5 years will provide a benefit to many growing companies, it could be detrimental to businesses that have experienced declining revenue.” The commenter further stated that “SBA should consider a hybrid approach whereby contractors are permitted to calculate revenues under both the 3-year period and the 5-year period and use the lower of the two results to determine its size status. This approach would be beneficial to both those small contractors that are experiencing a period of revenue growth, as well as those facing declining revenues.”

SBA’s response:

SBA agrees with the comments supporting a temporary transition period under which firms still could choose to use a 3-year averaging period. A plurality of commenters asked for a 2-year transition period or less, and SBA agrees that a 2-year period is appropriate because 2 years is an adequate time to allow firms to prepare for a permanent transition to a 5-year averaging period. Therefore, for the SBA programs affected by this rule, SBA will allow firms to choose either a 3-year or 5-year averaging period through January 6, 2022. After that date, firms with at least 5 years of receipts will be required to use a 5-year averaging period. A firm with fewer than 5 years of receipts will average its annual receipts over its existence.

SBA does not believe that allowing for alternate averaging periods on a permanent basis would be beneficial. Using multiple averaging periods in the long term will result in confusion about how to determine size for Federal opportunities, including procurements. Within a single contract competition, businesses would be able to determine size on a separate basis. After the transition period, there is not sufficient reason to justify maintaining two separate averaging periods.

Other Comments

SBA received some additional comments that addressed issues which did not fit into any of the above categories. One commenter requested that SBA change its regulations at 13 CFR 124.112(e)(2) to allow an 8(a) Business Development (BD) Program participant to change its primary industry classification using the last 5 completed fiscal years, instead of the current 3 completed fiscal years. This commenter stressed the advantage of reconciling this primary industry classification calculation

period with the size determination calculation period, especially at the 5th year annual update for an 8(a) BD Program participant.

SBA also received a few comments concerning the timeline for the implementation of the final rule. Most of these commenters suggested that SBA implement the final rule as soon as possible. One commenter stated that it is unlawful to delay the implementation of the new law, and the comment from one trade association suggested that SBA make the final rule retroactive to December 17, 2018, the date of enactment of Public Law 115-324. Another commenter recommended delaying the implementation of the final rule until January 1, 2021 if SBA decides to not grant a grace period to use the 3-year lookback. The commenter stated, “dropping the 3-year rule ‘grace period’ in the middle of the year will only confuse and complicate the implementation of the rule.”

One commenter suggested that SBA establish a 5-year averaging period for employee-based size standards as well.

SBA’s response:

The comment that SBA update its regulations at 13 CFR 124.112(e)(2) is outside the scope of establishing and reviewing size standards. This rule is only concerned with the method of calculation of annual receipts for size standards purposes. The comment regarding 13 CFR 124.112(e)(2) concerns a calculation related to the primary industry classification under 8(a) BD Program and that is outside the scope of this rule. Similarly, this rule does not affect the application of a 3-year average in the “economic dependence” test under 13 CFR 121.103(f)(2).

With respect to the comments concerning the implementation timeframe of the final rule, Public Law 115-324 did not include an effective date for the averaging change. Section 3(a)(2)(C) of the Small Business Act requires SBA to provide an opportunity for public notice and comment through the rulemaking process prior to implementing changes to size standards prescribed through section 3(a)(2). Accordingly, on December 21, 2018, SBA issued an Information Notice (6000-180023) advising that, until SBA makes necessary changes to its regulations, businesses must report their receipts based on a 3-year average. Thus, making the rule retroactive to the December 17, 2018, enactment date would not only run counter to SBA's guidance, but also would require corrections to contracts awards data in the Federal Procurement Data System-Next Generation (FPDS-NG) to reflect changes in size status of contractors due to the change in the averaging period. Conversely, delaying the implementation date would be against the interests of many small businesses and Federal agencies that want to see the final rule being implemented as soon as possible. Accordingly, this final rule will be effective after 30 days from the date of its publication in the Federal Register.

Lastly, this rule does not change the calculation period for employee-based size standards. SBA does not find sufficient reason from the comments to propose a change to the period for employee-based size standards.

Conclusions

Based on the analyses of impacts using the latest relevant industry and Federal contracting data available to SBA when the proposed rule was prepared and thorough evaluation of all public comments on the proposed rule, as discussed above, SBA is

taking the following actions in this final rule, except for the Business Loan and Disaster Loan Programs:

- (i) Adopting the 5-year averaging period for calculating annual revenues of firms and revenues of their affiliates in all industries that are subject to SBA's receipts-based size standards;
- (ii) Adopting the 5-year averaging period for calculating annual revenues of firms (including affiliates, if any) in all industries for prescribing receipts based size standards by other Federal agencies; and
- (iii) Providing a transition period until January 6, 2022, allowing firms (and their affiliates, if any) to choose either a 3-year averaging period or a 5-year averaging period for calculating average annual receipts for size standards purposes.

Section-by-Section Analysis

Section 121.104

The final rule removes "Schedule K" from the definition of receipts. SBA has found that reviewing Schedule K is generally not useful, but SBA reserves the ability to request a Schedule K as part of SBA's review of the other Internal Revenue Service (IRS) forms listed in § 121.104(a).

For consistency with the size standard averaging period being changed in § 121.903, for the purposes of applying SBA's receipts-based size standards, the final rule changes the averaging period for a business that has been in business for 5 or more fiscal years to a 5-year period, i.e., the business calculates its total receipts over the 5-year period and divides by 5. Under the final rule, if a business has been in business for

less than 5 complete fiscal years, the business calculates its total receipts, divides by the number of weeks in business, and multiplies by 52. This is the same process SBA currently uses when a business has less than 3 completed fiscal years. If a business has a short year as one of its 5 years, the business calculates its total receipts over the 5-year period, divides by the number of weeks in the short year and its other 4 fiscal years, and multiplies by 52. This too is the same process SBA currently uses.

The 5-year averaging period in § 121.104 would not distinguish between firms in service industries and other firms subject to receipts-based size standards. SBA believes that, in applying SBA's own size standards, separating out service-industry firms would cause confusion and create a greater compliance burden on firms that participate in both services industries and non-services industries (such as agriculture, construction, and retail trade) with receipts-based size standards.

This final rule only would affect the application of SBA's new size standard rules after its effective date. Thus, until the effective date of a final rule, SBA will continue to apply the 3-year averaging period in the present § 121.104 for calculating average annual receipts for all SBA's receipts-based size standards. Since size is determined as of the date when a firm certifies its size as part of its initial offer which includes price, the 3-year calculation period will apply to any offer submitted prior to the effective date of the final rule. Thus, even if SBA receives a request for a size determination or size appeal after the effective date of the final rule, SBA will still use a 3-year calculation period if the determination or appeal relates to a certification submitted prior to the final rule's effective date. Misrepresentations made under the existing calculation period are material for the purposes of criminal, civil, or administrative actions.

SBA also clarifies how it believes annual receipts should be calculated in connection with the acquisition or sale of a division. Specifically, the final rule provides that the annual receipts of a concern would not be adjusted where the concern sells or acquires a segregable division during the applicable period of measurement or before the date on which it self-certified as small. This would be different from how SBA treats the sale or acquisition of a subsidiary. In the case of a subsidiary, SBA's regulations provide that "[t]he annual receipts of a former affiliate are not included if affiliation ceased before the date used for determining size. This exclusion of annual receipts of a former affiliate applies during the entire period of measurement, rather than only for the period after which affiliation ceased." 13 CFR 121.104(d)(4).

SBA believes that the sale or acquisition of a division is different from buying or selling a separate legal entity and, as such, should be treated differently. Any receipts attributable to a specific division of a concern are certainly receipts earned by the concern. Even if that division is later sold, its receipts were always part of the receipts directly received by the concern itself, and SBA believes that those receipts should remain a part of the concern's receipts after the sale for purposes of determining the concern's size. Similarly, where a concern acquires a segregable division from another business entity during the applicable period of measurement, SBA would not increase the concern's overall receipts by the amount of receipts attributable to that division.

SBA understands that some may feel that distinguishing the sale of a division from that of a subsidiary would elevate form over substance, and would merely require a seller to move assets into a separate subsidiary and then sell that subsidiary in order to

bring the transaction under the rule. However, as noted above, SBA believes that there really is an important distinction between a division and a separate legal entity.

The Final Rule adds a transition period through January 6, 2022, during which a firm may calculate its receipts and the receipts of its affiliates using either a 3-year average or a 5-year average. The Final Rule adds a paragraph (c)(4) to use a 3-year averaging period for the Business Loan Programs, which are the 7(a) Loan Program, the Microloan Program, the Intermediary Lending Pilot Program, and the Development Company Loan Program (“504 Loan Program”), and the Disaster Loan Programs, which are Physical Disaster Business Loans, Economic Injury Disaster Loans, Military Reservist Economic Injury Disaster Loans, and Immediate Disaster Assistance Program loans. SBA intends to seek comment on the Business Loan and Disaster Loan Programs in a proposed rule through a separate rulemaking.

Section 121.903

As required by Public Law 115-324, SBA is amending the requirements for agencies that seek to propose and adopt size standards for their own programs, instead of applying SBA’s size standards. Under the final rule, a non-SBA agency’s receipts-based size standard, whether applying to services or non-services firms, must be proposed with a 5-year averaging period.

Section 3(a)(2)(ii)(III) of the Small Business Act still provides that other agencies prescribe size standards for industries other than services or manufacturing using “data over a period of not less than 3 years.” While Congress did not change this statutory language, SBA believes that it also can require other agencies establishing size standards for industries other than services or manufacturing to use data over a 5-year period and

specifically solicited comment on whether to make such a change. SBA received strong support for applying the 5-year averaging period for all industries. To avoid confusion from using the 5-year average receipts for SBA's size standards and 3-year average receipts for other agencies' size standards and promote consistency in measuring business size across the Federal government, in this final rule, SBA is also adopting the same 5-year averaging period for all receipts-based size standards proposed by other Federal agencies.

This new calculation period does not affect existing non-SBA size standards that specify a 3-year average unless the responsible agency proposes and finalizes changes to the existing specification of a 3-year average. This is consistent with the change in Public Law 115-324 to the requirements for prescribing a non-SBA size standard, given the lack of any restrictions in the Small Business Act or Public Law 115-324 on applying an existing size standard. In adopting or proposing a change to the averaging period for its existing size standard, the responsible agency should coordinate with SBA using the procedure in § 121.903.

Response to Office of Advocacy Comments

In response to the Proposed Rule, the Office of Advocacy of the SBA (Office of Advocacy) requested that the SBA update its Initial Regulatory Flexibility Analysis (IRFA) to include more relevant alternatives to the proposed regulatory change to mitigate negative impacts on small businesses. Specifically, the Office of Advocacy suggested that SBA allow the public to consider at least 2 specific alternatives: (1) a 2-year transition period during which firms could use either a 3-year or 5-year averaging

period, or (2) allowing a small business that has been awarded a contract to recertify its small business size status through any option periods.

As suggested by the Office of Advocacy, SBA has adopted a 2-year transition period that will end January 6, 2022. During that period, firms will choose either a 3-year or 5-year averaging period. Thus, firms that wish to continue using a 3-year average for certifying or assessing small business size status may continue to do so until January 6, 2022.

With regard to updating the IRFA, SBA does not believe that it is practical to issue a revised IRFA for public comment at this time. There is an urgent need to implement the intent of Congress and a further delay would result in more uncertainty and confusion for small businesses and the Federal contracting community. A number of comments to the proposed rule urged SBA to implement the final rule as soon as possible. In addition, SBA has adopted one of the relevant alternatives discussed by the Office of Advocacy, a 2-year transition period during which firms could use either a 3-year or a 5-year averaging period. Thus, issuing a revised IRFA for public comment would be superfluous. Accordingly, SBA is declining to issue a revised IRFA for public comment with the alternatives proposed by the Office of Advocacy.

With regard to recertification, SBA believes it would be extremely complicated to allow a firm that has already been awarded a contract to recertify its size status, after the transition period, using either the 3-year or 5-year averaging period through the length of that contract and any options. This would create extensive tracking and recordkeeping requirements that would also result in uncertainty and unpredictability for firms trying to determine their size status after the end of the 2-year transition period created in this rule.

Thus, even if a firm initially certified for a contract under a 3-year averaging period, a firm must use a 5-year average when it submits a new certification or recertification for that contract after the end of the transition period.

Compliance with Executive Orders 12866, 12988, 13132, 13563, and 13771, the Regulatory Flexibility Act (5 U.S.C. 601-612), and the Paperwork Reduction Act (44 U.S.C. Ch. 35)

A. Executive Order 12866

The Office of Management and Budget (OMB) has determined that this final rule is not a significant regulatory action for purposes of Executive Order 12866. Nonetheless, as required by section 3(a)(6) of the Small Business Act, 15 U.S.C. § 632(a)(6), in the next section, SBA provides a benefit-cost analysis of this final rule, including: (1) a statement of the need for the proposed action, and (2) an evaluation of the benefits and costs – both quantitative and qualitative – of this regulatory action. This rule is also not a “major rule” under the Congressional Review Act, 5 U.S.C. 800, et seq.

a. Benefit-Cost Analysis

1. What is the need for this regulatory action?

As stated elsewhere, the Small Business Act delegates to SBA’s Administrator the responsibility for establishing small business size definitions (usually referred to as “size standards”). Recently, Public Law 115-324 modified the requirements for proposed small business size standards prescribed by an agency without separate statutory authority to issue size standards.

The need of this final rule is to carry out the intent of Public Law 115-324 and to ensure consistency in the calculation of average annual receipts for size standards across the Federal Government.

SBA's mission is to aid and assist small businesses through a variety of financial, procurement, business development and counseling, and disaster assistance programs. This regulatory action promotes the Administration's goals and objectives and meets the SBA's statutory responsibility to implement a new law impacting size definitions for small businesses. One of SBA's goals in support of promoting the Administration's objectives is to help small businesses succeed through access to capital, Federal Government contracts and purchases, and management, technical and disaster assistance.

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

Changing the period for calculating average annual receipts from 3 years to 5 years may enable some mid-size businesses that have just exceeded size standards to regain small business status. Similarly, it could also allow some advanced and larger small businesses about to exceed size standards to retain their small business status for a longer period. However, as stated in the June 24, 2019, proposed rule, it could also result in some advanced small businesses having a 5-year receipts average that happens to be higher than the 3-year receipts average, thus ejecting them out of their small business status sooner. Detailed impacts of the proposed change are discussed below.

It is difficult to determine the actual number of small and mid-size businesses that would be impacted by Public Law 115-324 and this regulatory action because there is no annual data on receipts of businesses. The annual receipts data from the Economic Census special tabulation are only available once every 5 years. Similarly, the System for

Award Management (SAM) only records the data on 3-year average annual receipts of businesses over their 3 preceding fiscal years, but not their annual receipts for each fiscal year. For example, the receipts data for year 2018 is an average of annual receipts for 2017, 2016, and 2015. Similarly, the receipts data for 2017 is an average of annual receipts for 2016, 2015, and 2014, and so on. A 5-year receipts average for 2018 would be an average of annual receipts for 2017, 2016, 2015, 2014, and 2013.

Given the lack of annual receipts for each year, SBA approximated a firm's 5-year average annual revenue for 2018 as follows:

$$AvgRevenue_{2013-17} = \frac{1}{5} * \{(2 * AvgRevenue_{2015 (SAM)}) + (3 * AvgRevenue_{2018 (SAM)})\}$$

where:

$$AvgRevenue_{2015 (SAM)} = AvgRevenue_{2012-14} = \frac{1}{3} * (Revenue_{2012} + Revenue_{2013} + Revenue_{2014})$$

and

$$AvgRevenue_{2018 (SAM)} = AvgRevenue_{2015-17} = \frac{1}{3} * (Revenue_{2015} + Revenue_{2016} + Revenue_{2017}).$$

This result may slightly underestimate the 5-year revenue average when annual revenues are rising (i.e., 2014 revenue > 2013 revenue > 2012 revenue) and overestimate it if annual revenues are declining (i.e., 2014 revenue < 2013 revenue < 2012 revenue).

To estimate the 5-year receipts average for 2018 using the above formula, SBA analyzed the 2018 SAM extracts (as of September 1, 2018) and 2015 SAM extracts (as of September 1, 2015). The above 5-year average annual receipts formula would only work for businesses that were present in both 2015 and 2018 SAM extracts. One challenge was

that some businesses found in 2018 SAM could not be found in 2015 SAM and vice versa. Excluding entities registered in SAM for purposes other than government contracting and entities ineligible for small business consideration (such as foreign governments and state-controlled institutions of higher learning), there were a total of 346,958 unique business concerns in SAM subject to at least one receipts-based size standard. Of these concerns, 293,524 (or about 84.6 percent) were “small” in all North American Industry Classification System (NAICS) industries, 9,990 (or 2.9 percent) were “small” in some industries and “not small” in other industries, and 43,444 (or 12.5 percent) were “not small” in any industry.

Excluding entities with “null” or “zero” receipts values, 194,686 firms (or about 56 percent) appeared both in 2018 SAM and in 2015 SAM and were included in the 5-year average annual receipts approximation and calculation of number of businesses impacted. Of those 194,686 matched firms subject to a receipts-based size standard, 154,220 (or about 79 percent) were “small” in all NAICS industries, 8,049 (or 4.1 percent) were “small” in some industries and other than small (“not small”) in other industries, and 32,417 (or about 17 percent) were “not small” in any industry. In other words, 303,514 (or 87.5 percent) of 346,958 total concerns in SAM 2018 and 162,269 (or 83.3 percent) of 194,686 total matched firms were small in at least one NAICS industry with a receipts-based size standard. These results are summarized in Table 1, “Size Status of Businesses in Industries Subject to Receipts-Based Size Standards,” below.

Table 1
Size Status of Businesses in Industries Subject to Receipts-Based Size Standards

| | | | | |
|--|---|---------------------------------|--|--|
| | Total firms in 2018 SAM subject to least one receipts-based | Firms in both 2015 SAM and 2018 | | |
|--|---|---------------------------------|--|--|

| Size status | standard | | SAM (matched) | | % Matched | Total to matched ratio* |
|---------------------------------------|--------------|-------|---------------|------|-----------|-------------------------|
| | No. of firms | % | No. of firms | % | | |
| Small in at least one industry | 303,514 | 87.5 | 162,269 | 83.3 | 53.5 | 1.809 |
| Small in all industries | 293,524 | 84.6 | 154,220 | 79.2 | 52.5 | 1.903 |
| Small in some and not small in others | 9,990 | 2.9 | 8,049 | 4.1 | 80.6 | 1.241 |
| Large in all industries | 43,444 | 12.5 | 32,417 | 16.7 | 74.6 | 1.340 |
| Total | 346,958 | 100.0 | 194,686 | 100 | 56.1 | 1.782 |

* To be used to translate the results from the matched data to overall 2018 SAM data.

According to Table 2, “Distribution of Business Concerns Subject to Receipts-Based Size Standards by Number of NAICS Codes,” below, the distribution of firms by the number of NAICS codes in the matched data is very similar to that for the overall 2018 SAM data. About 42-44 percent of firms were in only one NAICS code that has a receipts-based size standard, about 35 percent in 2-5 NAICS codes, about 12 percent in 6-10 NAICS codes, and about 8-10 percent in more than 10 NAICS codes. In other words, 56-58 percent of firms were in multiple NAICS codes with receipts-based size standards. Thus, it is quite possible that the proposed change may impact a firm’s small business status in multiple industries. For purposes of this analysis, an impacted firm is defined as one that would be impacted by the change in terms of gaining, regaining, extending, or losing small business status in at least one industry with a receipts-based size standard.

Table 2
Distribution of Business Concerns Subject to Receipts-Based Size Standards by Number of NAICS Codes

| Number of NAICS codes | Total firms in 2018 SAM with at least one receipts-based NAICS code | Matched firms between 2018 and 2015 SAM |
|-----------------------|---|---|
|-----------------------|---|---|

| | Count | % | Count | % |
|---------------------|---------|-------|---------|-------|
| 1 NAICS code | 153,184 | 44.2 | 82,082 | 42.2 |
| 2 to 5 NAICS codes | 123,277 | 35.5 | 68,458 | 35.2 |
| 6 to 10 NAICS codes | 41,518 | 12.0 | 24,529 | 12.6 |
| > 10 NAICS codes | 28,979 | 8.4 | 19,617 | 10.1 |
| Total | 346,958 | 100.0 | 194,686 | 100.0 |

Note: A business concern is defined in terms of a unique local (vendor) DUNS number.

A central premise of Public Law 115-324 is that a 5-year annual receipts average (as opposed to a 3-year annual receipts average) would enable some mid-size businesses who have recently exceeded the size standard to regain small business status and some advanced small businesses close to exceeding the size standard to retain their small business status for a longer period. However, this premise would only hold true when businesses' annual revenues are rising. When businesses' annual revenues are declining, due to economic downturns or other factors, the 5-year annual receipts average could be higher than the 3-year annual receipts average, thereby causing small businesses close to their size standards to lose their small business status sooner. To mitigate such negative impacts on small businesses, SBA has decided, in consideration of public comments and the results from its own analysis, to provide a 2-year transition period in which firms will be allowed to elect either a 5-year or 3-year averaging period in calculating their average annual receipts.

b. Impacts on Businesses from the Change

By comparing the approximated 5-year annual receipts average with the current receipts-based size standard for each of the 194,686 matched business concerns in each NAICS code subject to a receipts-based size standard, in the proposed rule, SBA

identified the following 4 possible impacts from changing the averaging period for annual revenues from 3 years to 5 years:

- i. the number of mid-size businesses that have exceeded the size standard and would regain small business status in at least one NAICS industry with a receipts-based size standard (i.e., 3-year average > size standard \geq 5-year average) – positive impact;
- ii. the number of advanced small businesses within 10 percent below the size standard that would have their small business status extended for a longer period in at least one NAICS industry with a receipts-based standard (5-year average < 3-year average \leq size standard and $0.9 \times$ size standard < 3-year average \leq size standard) – positive impact;
- iii. the number of currently small businesses that would lose their small business status in at least one NAICS industry subjected to at least one receipts-based size standard (i.e., 3-year average \leq size standard < 5-year average) – negative impact; and
- iv. the number of advanced small businesses within 10 percent below the size standard that would have their small business status shortened in at least one NAICS industry subject to a receipts-based standard (3-year average < 5-year average \leq size standard and $0.9 \times$ size standard < 3-year average \leq size standard) – negative impact.

In this final rule, SBA is changing the period for calculation of average annual receipts for all of its as well as other agencies' receipts-based size standards from 3 years to 5 years. The purpose of Public Law 115-324 is to allow small businesses more time to

grow and develop competitiveness and infrastructure so that they are better prepared to succeed under full and open competition once they outgrow the size threshold. However, as stated in the proposed rule, a longer 5-year averaging period may not always and necessarily provide relief to every small business concern. As discussed in the proposed rule, when annual revenues are declining or when annual revenues for the latest 3 years are lower than those for the earliest 2 years of the 5-year period, the 5-year average would be higher than the 3-year average, thereby ejecting some advanced small businesses out of their small business status sooner or rendering some small businesses under the 3-year average not small immediately.

In the proposed rule, SBA described 4 different types of impacts on small businesses from changes to the averaging period for annual receipts from 3 years to 5 years as follows: (i) enabling current large or mid-size businesses to gain small business status (impact i); (ii) enabling current advanced small businesses to lengthen their small business status (impact ii); (iii) causing current small businesses to lose their small business status (impact iii); and (iv) causing current small businesses to shorten their small business status (impact iv).

However, with the SBA's decision to provide a 2-year transition period thereby allowing firms to choose either their 5-year average annual receipts or their 3-year average annual receipts, the two negative impacts (namely impact (iii) and impact (iv)) do not apply to this final rule. Accordingly, this final rule provides the analysis of the two positive impacts (namely impact (i) and impact (ii)) only.

Table 3, ‘Percentage Distribution of Impacted Firms by the Number of NAICS Codes,’ below, provides these results based on the 2018 SAM – 2015 SAM matched firms.

Table 3
Percentage Distribution of Impacted Firms by the Number of NAICS Codes

| Impact* | No. of impacted firms | % Distribution of impacted firms by number of NAICS codes | | | | Total |
|---|-----------------------|---|-----------------|------------------|-----------------|-------|
| | | 1 NAICS code | 2-5 NAICS codes | 6-10 NAICS codes | >10 NAICS codes | |
| Currently large in all NAICS codes | | | | | | |
| Impact (i) | 914 | 36.0 | 36.1 | 13.6 | 14.3 | 100.0 |
| Currently small in all NAICS codes | | | | | | |
| Impact (ii) | 1,255 | 25.3 | 39.6 | 16.3 | 18.8 | 100.0 |
| Currently small in some NAICS and not small in others | | | | | | |
| Impact (i) | 1,640 | 0.0 | 24.6 | 24.2 | 51.2 | 100.0 |
| Impact (ii) | 1,138 | 0.0 | 25.0 | 26.0 | 49.0 | 100.0 |
| Total Impact by Impact Type | | | | | | |
| Impact (i) | 2,554 | 12.9 | 28.7 | 20.4 | 38.0 | 100.0 |
| Impact (ii) | 2,393 | 13.3 | 32.6 | 20.9 | 33.2 | 100.0 |
| Total positive impact | 4,687 | 13.8 | 31.8 | 20.7 | 33.8 | 100.0 |

*Impact (i) = Current large businesses gaining small business status; and Impact (ii) = Current small businesses extending small business status.

It is highly notable that the distribution of impacted firms by the number of NAICS codes, as shown in Table 3, is very different as compared to a similar distribution based on the overall matched and total 2018 SAM data (see Table 2), especially with respect to firms with only one NAICS code and those with more than 5 NAICS codes. For example, as shown in Table 2, above, more than 40 percent of all firms in the overall data were associated with only one NAICS code, as compared to less than 15 percent among impacted firms in Table 3. Similarly, firms with more than 5 NAICS codes accounted for about 20 percent of all firms in the original data, as compared to more than 50 percent among impacted firms. It is also notable that NAICS Sectors 54, 56, and 23

together accounted for more than 70 percent of impacted firms, with Sector 54 (Professional, Scientific and Technical Services) accounting for about 35 percent, followed by Sector 23 (Construction) about 25 percent, and Sector 56 (Administrative and Support, Waste Management and Remediation Services) about 12-13 percent.

Each of these impacts was then multiplied by an applicable factor or ratio, as shown in the last column of Table 1, to obtain the respective impacts corresponding to all firms in 2018 SAM subject to at least one receipts-based size standard. These results are presented below in Table 4, “Impacts from Changing the Averaging Period for Receipts from 3 Years to 5 Years.” The last column of the table shows the percent of firms impacted relative to all business concerns in 2018 SAM.

Because the SAM data only captures businesses that are primarily interested in Federal procurement opportunities, the SAM-based results do not capture the impacts the proposed change may have on businesses participating in various non-procurement programs that apply SBA’s receipts-based size standards, such as exemptions from compliance with paperwork and other regulatory requirements.

Table 4
Impacts from Changing the Averaging Period for Receipts from 3 Years to 5 Years

| Impact ¹ | Firms impacted in matched dataset | Total to matched ratio (Table 1) | Total firms impacted in 2018 SAM | Total firms in 2018 SAM | % Impacted |
|---|-----------------------------------|----------------------------------|----------------------------------|-------------------------|------------|
| Entities other than small under all NAICS code(s) | | | | | |
| Impact (i) | 914 | 1.340 | 1,225 | 43,444 | 2.8 |
| Entities small under all NAICS code(s) | | | | | |
| Impact (ii) | 1,255 | 1.903 | 2,389 | 293,524 | 0.8 |
| Entities small in some NAICS code(s) and other than small in other(s) | | | | | |
| Impact (i) | 1,640 | 1.241 | 2,035 | 9,990 | 20.4 |
| Impact (ii) | 1,138 | 1.241 | 1,412 | 9,990 | 14.1 |
| Total positive impact by impact type | | | | | |

| | | | | | |
|--|-------|---|-------|---------|-----|
| Impact (i) | 2,554 | - | 3,260 | 53,434 | 6.1 |
| Impact (ii) | 2,393 | - | 3,801 | 303,514 | 1.3 |
| Overall total positive impact ² | 4,687 | - | 6,690 | 346,958 | 1.9 |

¹ Impact (i) = Current large businesses gaining small business status; and Impact (ii) = Current small businesses extending small business status.

² Number of firms under total positive impacts refer to the number of unique firms. Some firms could appear in both impact types and hence individual impacts may not add up to overall impact.

The Economic Census, combined with the Census of Agriculture and County Business Patterns Reports, provides for each NAICS code information on the number of total small and large businesses subjected to a receipts-based size standard. Based on the matched SAM data, SBA computed percentages of businesses impacted under each impact category for each NAICS industry subject to a receipts-based size standard. By applying such percentages to the 2012 Economic Census tabulation, SBA estimated the number of all businesses impacted under each impact type for each NAICS code subject to a receipts-based size standard. These results are presented in Table 5, “Impacts from Changing the Averaging Period for Receipts from 3 Years to 5 Years (2012 Economic Census),” below.

Table 5
Impacts from Changing the Averaging Period for Receipts from 3 Years to 5 Years
(2012 Economic Census)

| Impact ¹ | Total firms | Estimate of impacted firms | % Impacted |
|-------------------------|-------------|----------------------------|------------|
| Impact (i) | 271,505 | 7,822 | 2.9 |
| Impact (ii) | 6,896,633 | 62,822 | 0.9 |
| Overall positive impact | 7,168,138 | 70,644 | 1.0 |

¹ Impact (i) = Current large businesses gaining small business status; and Impact (ii) = Current small businesses extending small business status.

Currently large or mid-size businesses regaining small business status would get various benefits as small business concerns, including access to Federal set-aside

contracts, and exemptions from various compliance and paperwork requirements. With their small business status extended, advanced small businesses would continue to receive such benefits for a longer period. However, the change from 3-year average receipts to 5-year average may also harm some small businesses by causing them to lose or shorten their small business status in at least one receipts-based size standard, thereby depriving them of access to small business assistance, especially Federal set-aside opportunities. To mitigate such impacts, SBA is allowing businesses to elect either the 3-year average annual receipts or the 5-year average annual receipts for 2 years through January 6, 2022. SBA intends to seek comment on implementation in the Business Loan and Disaster Loan Programs in a proposed rule through a separate rulemaking.

c. The Baseline

For this new regulatory action modifying an existing regulation (such as changing the average annual receipts calculation from 3 years to 5 years), a baseline assuming no change to the regulation (i.e., maintaining the status quo) generally provides an appropriate benchmark for evaluating benefits, costs, or transfer impacts of proposed regulatory changes and their alternatives.

Based on the 2012 Economic Census special tabulations (the latest available), 2012 County Business Patterns Reports (for industries not covered by the Economic Census), and 2012 Agricultural Census tabulations (for agricultural industries), of a total of about 7.2 million firms in all industries with receipts-based size standards, about 96 percent are considered small and 4 percent other-than-small under the 3-year annual receipts average. Similarly, of 346,958 businesses that were subject to at least one

receipts-based size standard and eligible for Federal contracting, 87.5 percent were small in at least one NAICS code and 12.5 percent other than small in all NAICS codes.

Based on the data from the Federal Procurement Data System - Next Generation (FPDS-NG) for fiscal years 2015-2017 (the latest available when the proposed rule was prepared), on average, about 88,770 unique firms in industries subject to receipts-based size standards received at least one Federal contract during that period, of which 83 percent were small. Businesses subject to receipts-based standards received \$182 billion in average annual Federal contract dollars during that period, of which nearly \$64 billion or about 35 percent went to small businesses. Of total dollars awarded to small businesses subject to receipts-based size standards, \$45 billion or 71 percent was awarded through various small business set-aside programs and another 29 percent was awarded through non-set aside contracts.

Table 6, “Baseline Analysis of Receipts-Based Size Standards,” below, provides these baseline results. SBA’s proposed rule included an estimate of the number and total dollar amount of loans issued through the Business Loan Programs and the Economic Injury Disaster Loan (EIDL) program. These estimates are not presented in this final rule because SBA intends to issue a separate rulemaking to consider changes to size eligibility for the Business Loan and Disaster Loan Programs.

Besides set-aside contracting and financial assistance discussed above, small businesses also benefit through reduced fees, less paperwork, and fewer compliance requirements that are available to small businesses through Federal agencies that use SBA’s size standards. However, SBA has no data to estimate the number of small businesses receiving such benefits. Similarly, due to the lack of data, SBA is not able to

determine impacts the final rule will have on small businesses participating in other agencies' programs that are subject to their own size standards based on average annual receipts.

Table 6
Baseline Analysis of Receipts-Based Size Standards

| Measure | Value |
|--|---------|
| Total industries subject to receipts-based standards | 518 |
| Total firms subject to at least one receipts-based standard (million) – 2012 Economic Census | 7.17 |
| Total small firms subject to at least one receipts-based standard (million) – 2012 Economic Census | 6.9 |
| Total small firms subject to at least one receipts-based standard as % of total firms – 2012 Economic Census | 96.2 |
| Total business concerns in SAM ¹ (as of September 1, 2018) | 420,381 |
| Total business concerns subject to a receipts-based size standard in at least one NAICS code ² (SAM) | 346,958 |
| Total businesses that are small in at least one NAICS code subject to a receipts-based size standard | 303,514 |
| Small business concerns as % of total business concerns subject to receipts-based standards (2018 SAM) | 87.5 |
| Average total number of unique Eligible vendors getting Federal contracts ¹ - FPDS-NG (2015-2017) | 126,500 |
| Average total number of unique firms with receipts-based size standards getting Federal contracts ² - FPDS-NG (2015-2017) | 88,770 |
| Average total contract dollars awarded to business concerns, subject to receipts-based standards (\$ billion) | \$182 |
| Average total small business contract dollars awarded to businesses subject to receipts-based standards (\$ billion) | \$63.7 |
| Small business dollars as % of total dollars awarded to firms subject to receipts-based standards | 34.9 |

¹ Entities in SAM and FPDS-NG presented above only include business concerns that can be eligible to qualify as small for Federal contracting. That is, entities that can never qualify as small (e.g., foreign, not-for-profit and government entities) are excluded as they are not impacted by this rule.

² A business concern could appear in multiple NAICS industries involving both receipts-based and size standards and those based on other measures (such as employees). Similarly, a business could be small in some industries and other-than-small in others.

Businesses that would regain or expand their small business status can be identified by comparing the estimate of their 5-year receipts average with the size standard. That is, if the 5-year receipts average of a firm currently above the size standard is lower than the applicable size standard, that firm will gain or regain small business

status. To estimate the number of small businesses that would benefit by having their small business status extended for a longer period or would be penalized by having their small business status shortened, SBA considered small businesses whose 3-year average annual receipts was within 10 percent below their receipts-based size thresholds.

Depending upon whether their annual receipts are growing or declining, small businesses that are not immediately impacted may be impacted, either positively (i.e., gaining small business status) or negatively (i.e., losing small business status) someday as they continue to grow and approach the size standard threshold as in the current 3-year averaging method. However, SBA is not able to quantify such impacts now.

d. Benefits

The most significant benefits to businesses from the change in the period for calculation of average annual receipts from 3 years to 5 years include: (i) enabling some mid-size businesses currently categorized above their corresponding size standards to gain or regain small business status and thereby qualify for participation in Federal assistance intended for small businesses, and (ii) allowing some advanced and larger small businesses close to their size thresholds to lengthen their small business status for a longer period and thereby continue their participation in Federal small business programs. These include Federal procurement programs intended for small businesses. Federal procurement programs provide targeted, set-aside opportunities for small businesses under SBA's various business development and contracting programs, including 8(a)/BD, HUBZone, WOSB, EDWOSB, and SDVOSB programs. Benefits accruing to businesses gaining and extending small business status are presented below in Table 7, "Positive Impacts of Changing the Averaging Period for Receipts from 3 Years to 5 Years." The

results in Table 7 pertain to businesses and industries subject to SBA's receipts-based size standards only.

As shown in Table 7, of 43,444 firms not currently considered small in any receipts-based size standards, 3,260 (or 7.5 percent) would benefit from the proposed change by gaining or regaining small business status under the 5-year receipts average in at least one NAICS industry that is subject to a receipts-based size standard. Additionally, about 3,800 or 1.3 percent of small businesses within 10 percent below size standards would see their annual receipts decrease under the 5-year averaging period, consequently enabling them to keep their small business status for a longer period.

Using the 2012 Economic Census, SBA estimated that about 7,800 or 2.9 percent of currently large businesses would gain or regain small business status and more than 62,800 or 0.9 percent of total small businesses would see their small business status extended for a longer period as the result of this proposed rule. These results are shown in Table 7, below.

Table 7
Positive Impacts of Changing the Averaging Period for Receipts from 3 Years to 5 Years

| Impact of proposed change | Firms gaining small business status | Firms extending small business status | Total positive impact |
|---|-------------------------------------|---------------------------------------|-----------------------|
| No. of impacted industries | 372 | 361 | 420 ¹ |
| No. of large firms becoming small or/and small firms extending small business status – SAM (as of Sept 1, 2018) | 3,260 | 3,801 | 6,690 ² |
| Large firms becoming small or/and small firms with extended small business status as % of total large or/and small firms in the baseline – SAM (as of Sept 1, 2018) | 7.5 | 1.3 | 1.9 |
| No. of large firms becoming small or/and small firms extending small business status – 2012 Economic Census | 7,822 | 62,822 | 70,644 |
| Large firms becoming small or/and small firms extending small business status as % of total large or/and small firms in the baseline – 2012 Economic Census | 2.9 | 0.9 | 1.0 |
| No. of large firms becoming small or/and small firms extending small business status for small business contracts (FPDS-NG) | 910 | 838 | 1,700 ² |
| Additional small business dollars available to newly qualified firms or/and current small firms with extended small business status (\$ million) | \$961 | \$133 | \$1,094 |
| Additional small business dollars as % total small business contract dollars in the baseline | 1.5 | 0.2 | 1.7 |

¹ Total impact represents total unique industries impacted to avoid double counting as some industries have large firms gaining small business status and small firms extending small business status.

² Total impact represents total unique firms impacted to avoid double counting as some firms may gain small business status in at least one NAICS code, while extending small business status in at least one other NAICS code.

With more businesses qualifying as small under the 5-year receipts average, Federal agencies will have a larger pool of small businesses from which to draw for their small business procurement programs. Growing small businesses that are close to exceeding the current size standards will be able to retain their small business status for a longer period under the 5-year receipts average, thereby enabling them to continue to benefit from the small business programs.

Based on the FPDS-NG data for fiscal years 2015-2017, as shown in Table 7, SBA estimates that those newly qualified small businesses (i.e., large businesses gaining small business status) under this final rule, if adopted, could receive \$961 million in small business contract dollars annually under SBA's small business, 8(a)/BD, HUBZone, WOSB, EDWOSB, and SDVOSB programs. That represents a 1.5 percent increase to total small business contract dollars from the baseline. Additionally, small businesses could receive approximately \$133 million in additional small business contract dollars because of extension of their small business status, which is about a 0.2 percent increase from the total small business contract dollars in the baseline. That is, businesses gaining or extending small business status could receive about \$1.1 billion in additional small business contract dollars, which is a 1.7 percent increase to the total small business dollars in the baseline.

The added competition from more businesses qualifying as small may result in lower prices to the Federal Government for procurements set aside or reserved for small businesses, but SBA cannot quantify this impact. Costs could be higher when full and open contracts are awarded to HUBZone businesses that receive price evaluation preferences. However, with agencies likely setting aside more contracts for small

businesses in response to a larger pool of small businesses under the proposed change, HUBZone firms might actually end up getting more set-aside contracts and fewer full and open contracts, thereby resulting in some cost savings to agencies. While SBA cannot estimate such costs savings, as it is impossible to determine the number and value of unrestricted contracts to be otherwise awarded to HUBZone firms that will be awarded as set-asides, such cost savings are likely to be relatively small as only a small fraction of full and open contracts are awarded to HUBZone businesses.

Additionally, the newly defined small businesses, as well as those with a longer small business status, would also benefit from reduced fees, less paperwork, and fewer compliance requirements but SBA has no data to quantify this impact.

The change from a 3-year averaging period to a 5-year averaging period will also address some of the challenges and uncertainties small businesses face in the open market once they graduate from their small business status. Small and mid-size businesses experience a considerable disadvantage in competing for full and open contracts against large businesses, including the largest in the industry. These large businesses have several competitive advantages over small and mid-size firms, including vast past performance qualifications and experience, strong brand-name recognition, a plethora of professional certifications, security clearances, and greater financial and marketing resources. Small and mid-size businesses cannot afford to maintain these resources, leaving them at a considerable disadvantage.

With contracts getting bigger, one large set-aside contract could throw a firm out of its small business status, thereby subjecting it to certain requirements that apply to other-than-small firms, such as developing subcontracting plans. That firm may not have

the infrastructure, existing business processes, and/or other resources in place in order to comply with such requirements.

By allowing smaller mid-size companies that have just exceeded the size threshold to regain small business status and advanced small businesses close to size standards to prolong their small business status for a longer period, using the 5-year receipts average can expand the pool of qualified small firms for agencies to draw from to meet their small business requirements.

e. The Costs

As stated in the proposed rule, the change enacted under Public Law 115-324 may not always and necessarily benefit every small business concern. When businesses' annual revenues are declining or when annual revenues for the latest 3 years are lower than those for the earliest 2 years of the 5-year period, the 5-year average would be higher than the 3-year average, thereby ejecting small businesses out of their small business status sooner or rendering some small businesses other than small immediately. Similarly, small businesses that lose their small business status would have to wait longer to qualify as small again. Such small businesses would no longer be eligible for Federal small business opportunities, such as Federal small business contracts and other Federal benefits (such as reduced fees and exemptions from certain paperwork and compliance requirements) available to small businesses. However, the SBA's decision to grant a 2-year transition period allowing businesses to elect to use either the 5-year receipts average or the 3-year average receipts will mitigate such impacts. SBA believes the transition period provides small businesses with enough time to make a permanent transition to the 5-year averaging method without facing such impacts.

By enabling mid-size businesses to regain small business status and lengthening the small business status of advanced and successful larger small businesses, the final rule may disadvantage smaller small businesses in more need of Federal assistance than their larger counterparts in competing for Federal opportunities. SBA frequently receives concerns from smaller small businesses that they also lack resources, past performance qualifications and expertise to be able to compete against more resourceful, qualified and experienced larger small businesses for Federal opportunities for small businesses. With a larger pool of businesses qualifying as small, SBA expects Federal agencies to set aside more contracts to small businesses thereby expanding opportunities for all small businesses. SBA believes that overall benefits to small businesses from this rule change outweigh the costs to small businesses.

Besides having to register in SAM to be able to participate in Federal contracting and update the SAM profile annually, small businesses incur no direct costs to gain or retain their small business status. All businesses willing to do business with the Federal Government have to register in SAM and update their SAM profiles annually, regardless of their size status. SBA believes that a vast majority of businesses that are willing to participate in Federal contracting are already registered in SAM.

The change to the 5-year receipts average may entail some additional administrative costs to the Federal Government because more businesses may qualify as small for Federal small business programs. For example, there will be more firms eligible for enrollment in the Dynamic Small Business Search (DSBS) database or in certify.sba.gov; more firms seeking certification as 8(a)/BD or HUBZone firms or qualifying for small business, WOSB, EDWOSB, and SDVOSB status; and more firms

applying for SBA's 8(a)/BD and All Small Mentor-Protégé programs. With an expanded pool of small businesses, it is likely that Federal agencies will set aside more contracts for small businesses under the new rule. One may surmise that this might result in a higher number of small business size protests and additional processing costs to agencies. However, the SBA's historical data on size protests actually shows that the number of size protests decreased after an increase in the number of businesses qualifying as small as a result of size standards revisions as part of the first 5-year review of size standards. Specifically, on an annual basis, the number of size protests dropped from about 600 during fiscal years 2011-2013 (review of most receipts-based size standards was completed by the end of fiscal year 2013) to about 500 during fiscal years 2014-2016. However, with more years of data to be reviewed, 5-year averaging may increase time needed by size specialists to process a size protest.

Additionally, some Federal contracts may possibly have higher costs. With a greater number of businesses defined as small under the 5-year averaging method, Federal agencies may choose to set aside more contracts for competition among small businesses only instead of using full and open competition. The movement of contracts from unrestricted competition to small business set-aside contracts might result in competition among fewer total bidders, although there will be more small businesses eligible to submit offers under the proposed change. However, the additional costs associated with fewer bidders are expected to be minor since, by law, procurements may be set aside for small businesses under the 8(a)/BD, HUBZone, WOSB, EDWOSB, or SDVOSB programs only if awards are expected to be made at fair and reasonable prices.

Costs may also be higher when full and open contracts are awarded to HUBZone businesses that receive price evaluation preferences. However, with agencies likely setting aside more contracts for small businesses in response to the availability of a larger pool of small businesses under the 5-year receipts average, HUBZone firms might actually end up getting fewer full and open contracts, thereby resulting in some cost savings to agencies. However, such cost savings are likely to be minimal as only a small fraction of unrestricted contracts are awarded to HUBZone businesses.

f. Transfer Impacts

The change from a 3-year averaging period to a 5-year averaging period may result in some redistribution of Federal contracts between businesses gaining or extending small business status and large businesses, and between businesses gaining or extending small business status and other existing small businesses. However, it would have no impact on the overall economic activity since the total Federal contract dollars available for businesses to compete for will not change. While SBA cannot quantify with certainty the actual outcome of the gains and losses from the redistribution of contracts among different groups of businesses, it can identify several probable impacts in qualitative terms. With the availability of a larger pool of small businesses under the proposed change, some unrestricted Federal contracts may be set aside for small businesses. As a result, large businesses may lose access to some Federal contracts. Similarly, some currently small businesses may obtain fewer set-aside contracts due to the increased competition from some large businesses now qualifying as small and advanced small businesses remaining small for a longer period. This impact may be offset by a greater number of procurements being set aside for all small businesses. With

large businesses qualifying as small and advanced larger small businesses remaining small for a longer period under the proposed rule, smaller small businesses could face some disadvantages in competing for set-aside contracts against their larger counterparts. However, SBA cannot quantify these impacts.

B. Executive Order 12988

This action meets applicable standards set forth in Sections 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 retroactive or preemptive effect.

C. Executive Order 13132

For purposes of Executive Order 13132, SBA has determined that this final 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, SBA has determined that this final rule has no federalism implications warranting preparation of a federalism assessment.

D. Executive Order 13563

Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility. A description of the need for this regulatory action and benefits and costs associated with this action, including possible distributional impacts that relate to Executive Order 13563, is included above in the Benefit-Cost Analysis under Executive Order 12866. Additionally, Executive Order 13563, Section 6, calls for retrospective analyses of existing rules.

Following the enactment of Public Law 115-324, SBA issued a public notice advising business and contracting communities that SBA must go through a rulemaking

process to implement the new law and that businesses still must report their receipts based on a 3-year average until SBA changes its regulations. SBA updated the Small Business Procurement Advisory Council (SBPAC) at its March 26, 2019, April 23, 2019, and August 26, 2019, meetings about SBA's rulemaking process to implement Public Law 115-324. On April 18, 2019, SBA also presented an update on the implementation of Public Law No. 115-324 at the 2019 Annual Government Procurement Conference. Through phone calls and emails, SBA also advised business and contracting communities and other interested parties about the SBA's process to implement the new law.

Additionally, SBA issued a revised white paper titled "Small Business Size Standards: Revised Size Standards Methodology" and published a notice in the April 27, 2018, issue of the Federal Register (83 FR 18468) to advise the public that the document is available for public review and comments. The Revised Size Standards Methodology explains how SBA establishes, reviews, and modifies its receipts-based and employee-based small business size standards. On April 11, 2019, SBA published a Federal Register Notice (84 FR 14587) advising the public that the Agency has issued the revised final white paper.

E. Executive Order 13771

This rule is not expected to be an Executive Order 13771 regulatory action because this rule is not significant under Executive Order 12866.

F. Final Regulatory Flexibility Analysis

Under the Regulatory Flexibility Act (RFA), this final rule may have a significant economic impact on a substantial number of small businesses in industries subject to receipts-based size standards. As described above, this rule may affect small businesses

in those industries seeking Federal contracts and assistance under other Federal small business programs.

Immediately below, SBA sets forth a final regulatory flexibility analysis (FRFA) of this final rule to address the following questions: (1) What is the need for and objective of the rule?; (2) What is SBA's description and estimate of the number of small businesses to which the rule will apply?; (3) What are the projected reporting, record-keeping, and other compliance requirements of the rule?; (4) What are the relevant Federal rules that may duplicate, overlap, or conflict with the rule?; and (5) What alternatives will allow the Agency to accomplish its regulatory objectives while minimizing the impact on small businesses?

1. What is the need for and objective of the rule?

Recently, Public Law 115-324 amended section 3(a)(2)(C)(ii)(II) of the Small Business Act by modifying the period for calculating average annual receipts for prescribing size standards for business concerns in services industries by an agency without separate statutory authority to issue size standards from 3 years to 5 years. This final rule implements the intent of Public Law 115-324 and makes consistent changes to SBA's definition of annual receipts by amending the SBA's regulations on the calculation of average annual receipts for all receipts-based standards from over 3 years to over 5 years, except for the Business Loan Programs and Disaster Loan Programs.

2. What are SBA's description and estimate of the number of small businesses to which the rule will apply?

This final rule applies to all small businesses that are subject to a receipts-based size standard. Based on the 2012 Economic Census special tabulations, 2012 County

Business Patterns Reports, and 2012 Agricultural Census tabulations, of a total of about 7.2 million firms in all industries with receipts-based size standards to which this final rule will apply, 6.9 million or about 96.0 percent are considered small under the 3-year annual receipts average. Of 346,958 total concerns in SAM 2018 to which the rule will apply, about 303,500 or 87.5 percent were small in at least one NAICS industry with a receipts-based size standard. Similarly, based on the data from FPDS-NG for fiscal years 2015-2017, on average, about 88,770 unique firms in industries subject to receipts-based size standards received at least one Federal contract during that period, of which 83 percent, or 73,825 were small.

3. What are the projected reporting, record-keeping and other compliance requirements of the rule?

The final rule changes existing reporting or record-keeping requirements for small businesses. In reporting receipts to SBA for an SBA size determination after the final rule's effective date, businesses will report a 5-year average rather than a 3-year average which requires minimal effort. To qualify for Federal procurement and a few other programs, businesses are required to register in SAM and to self-certify that they are small at least once annually. Therefore, businesses opting to participate in those programs must comply with SAM requirements. There are no costs associated with SAM registration or certification. The change from a 3-year averaging period to a 5-year averaging period may result in some redistribution of Federal contracts between businesses gaining or extending small status and large businesses, and between businesses gaining or extending small status and other existing small businesses.

However, it would have no impact on the overall economic activity since the total Federal contract dollars available for businesses to compete for will not change.

4. What are the relevant Federal rules which may duplicate, overlap or conflict with the rule?

Under section 3(a)(2)(C) of the Small Business Act, 15 U.S.C. 632(a)(2)(C), Federal agencies must use SBA's size standards to define a small business, unless specifically authorized by statute to do otherwise. In 1995, SBA published in the *Federal Register* a list of statutory and regulatory size standards that identified the application of SBA's size standards as well as other size standards used by Federal agencies (60 FR 57988 (November 24, 1995)). SBA is not aware of any Federal rule that would duplicate or conflict with establishing size standards.

However, the Small Business Act and SBA's regulations allow Federal agencies to develop different size standards if they believe that SBA's size standards are not appropriate for their programs, with the approval of SBA's Administrator (13 CFR 121.903). The Regulatory Flexibility Act, 5 U.S.C. 601(3), authorizes an Agency to establish an alternative small business definition, after consultation with the Office of Advocacy of the U.S. Small Business Administration.

5. What alternatives will allow the Agency to accomplish its regulatory objectives while minimizing the impact on small entities?

By law, SBA is required to develop numerical size standards for establishing eligibility for Federal small business assistance programs. Other than varying size standards by industry and changing the size measures or changing a measurement period, no practical alternative exists to the systems of numerical size standards. As stated

elsewhere, the objective of this final rule is to change SBA's regulations on the calculation of business size in terms of average annual receipts to implement Public Law 115-324.

This rule is expected to affect a substantial number of small entities, but the effects are not expected to be significant. However, to mitigate unintended negative impacts of a 5-year averaging period on small businesses and to allow small businesses more time to prepare for a switch to the 5-year receipts average, in this final rule, SBA is allowing, through January 6, 2022, businesses to elect to calculate average annual receipts using either a 3-year averaging period or a 5-year averaging period. SBA also decided that the Business Loan Programs and Disaster Loan Programs are not included in this final rule and will instead be considered in a future proposed rule.

G. Paperwork Reduction Act

SBA has determined that as a result of this final rule, an information collection will need to be revised.

1 . SBA Form 355, Information for Small Business Size Determination. SBA submitted this information collection to OMB for approval of the changes described below and received conditional approval pending any change as a result of public comments. The final information collection package will be resubmitted to OMB concurrent with publication of this final rule. Changes have been made to Parts III and IV of the form to address the change from 3 years to 5 years for calculating average annual receipts. Other revisions to the form have been made to delete unnecessary questions, clarify certain previously approved requests for information, and in some instances, to request additional information where SBA has determined there is a programmatic need.

As noted in the proposed rule and the OMB submission, these deletions and clarifications, though not required by the statute, will alleviate the additional burden posed by changing from 3 years to 5 years for calculating average annual receipts.

(a) SBA amended the General Instructions section to define “concern” and “principal stockholders”; state that separate affiliation rules apply in some of SBA’s loan and research programs; remove obsolete information about industries with special size standards; state that dormant or inactive firms must be disclosed; and to include in the certification a statement that accompanying documentation is true and correct.

(b) In Part 1, SBA clarified that the information relates to the applicant business; added a checkbox for the firm to identify its corporate organization structure; required a firm to disclose whether it is organized for profit; and removed various obsolete or unnecessary information regarding county/city, purpose of the size determination, the contracting agency, the business’s major products or services and shares of sales, addresses of owners or officers, and recently completed mergers. Part 1 was also amended to request ownership information for owners that are entities until the respondent identifies the ultimate owners that are natural persons.

(c) In Part II, SBA limited the information requested about employees to businesses that are being evaluated under an employee-based size standard.

(d) In Part III, SBA limited the information request about receipts to businesses that are being evaluated under a receipts-based size standard. SBA also added two additional lines to the entries for annual receipts so that a business that has been in business for 5 years can provide information about its most recently completed 5 fiscal

years. SBA added a question to allow the concern to elect a 3-year average or a 5-year average during the transition period that ends January 6, 2022.

(e) In Part IV, SBA added that the business must provide information for any business that the applicant's owner reports on a Schedule C or Schedule E of the owner's personal tax returns if the owner or an immediate family member has a controlling interest in the business; removed the request for addresses of individual owners and managers; requested ownership information for owners that are entities until the respondent identifies the ultimate owners that are natural persons; limited the request for employee information to applicants being evaluated under an employee-based size standard; limited the information request for receipts information to applicants being evaluated under a receipts-based size standard; and added two rows to the receipts table so that the receipts of acknowledged affiliates are reported based on a 5-year average.

(f) In Part V, SBA removed requests about acknowledged affiliates that are covered in Part IV; deleted questions about performance of work on the contract, financial impact of termination for default, and specific terms and conditions of the contract; and added a question about actual or proposed subcontracts between the applicant and any of its alleged affiliates.

SBA determined that these changes to the Form 355 will not impact the paperwork burden following the transition period, and it will remain at 4 hours. The changes require a business in an industry with a receipts-based size standard, if selecting to use the 5-year average during the transition period or if certifying after the transition period, to gather information about the business's 5 prior fiscal years and complete information about its 5 prior fiscal years and the 5 prior fiscal years for acknowledged

affiliates. However, a business with a receipts-based size standard will not complete information about its number of employees. Similarly, a business with an employee-based size standard will not complete information about its receipts. Additionally, SBA has removed all requests for the addresses of individual owners and managers, and deleted 3 questions from Part V.

The title, summary of the amended information collection, description of respondents, and an estimate of the reporting burden are discussed below. Included in the estimate is the time for reviewing instructions, searching existing data, and completing and reviewing each collection of information.

Title and Description: SBA Form 355, Information for Small Business Size Determination. The information provided in this form will be used by SBA for a size determination of a business applying for assistance available to small businesses under any program administered by this Agency, except for its SBIC Program which uses SBA Form 480, or at the request of another Federal agency for purposes of its small business program.

Need and Purpose: This information collection is necessary for SBA to, among other things, evaluate the eligibility of an applicant for SBA's small business programs.

OMB Control Number: 3245-0101

Description of and Estimated Number of Respondents: This information will be collected from small businesses seeking an SBA determination of size. Based on historical information, SBA estimates this number to be between 500 and 600 each year.

Estimated Response Time: 4 hours.

Total Estimated Annual Hour Burden: 2,000-2,400.

List of Subjects in 13 CFR Part 121

Administrative practice and procedure, Government procurement, Government property, Grant programs – business, Individuals with disabilities, Loan programs – business, Reporting and recordkeeping requirements, Small businesses.

For the reasons set forth in the preamble, SBA amends 13 CFR part 121 as follows:

PART 121 – SMALL BUSINESS SIZE REGULATIONS

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

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

2. Amend §121.104 by revising the second sentence of paragraph (a) introductory text and by revising paragraphs (c) and (d)(2) through (4) to read as follows:

§121.104 How does SBA calculate annual receipts?

(a) * * * 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 for S corporations; Form 1120, Form 1065 or Form 1040 for LLCs; Form 1065 for partnerships; Form 1040, Schedule F for farms; Form 1040, Schedule C for other sole proprietorships) * * *

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(c) *Period of measurement.* (1) Except for the Business Loan and Disaster Loan Programs, annual receipts of a concern that has been in business for 5 or more completed fiscal years means the total receipts of the concern over its most recently completed 5

fiscal years divided by 5. For certifications submitted on or before January 6, 2022, rather than using the definitions in this paragraph (c), a concern submitting a certification may elect to calculate annual receipts and the receipts of affiliates using either the total receipts of the concern or affiliate over its most recently completed 5 fiscal years divided by 5, or the total receipts of the concern or affiliate over its most recently completed 3 fiscal years divided by 3.

(2) Except for the Business Loan and Disaster Loan Programs, annual receipts of a concern which has been in business for less than 5 complete fiscal years means the total receipts for the period the concern has been in business divided by the number of weeks in business, multiplied by 52.

(3) Except for the Business Loan and Disaster Loan Programs, where a concern has been in business 5 or more complete fiscal years but has a short year as one of the years within its period of measurement, annual receipts means the total receipts for the short year and the 4 full fiscal years divided by the total number of weeks in the short year and the 4 full fiscal years, multiplied by 52.

(4) For the Business Loan and Disaster Loan Programs, annual receipts of a concern that has been in business for three or more completed fiscal years means the total receipts of the concern over its most recently completed three fiscal years divided by three. Annual receipts of a concern which has been in business for less than three complete fiscal years means the total receipts for the period the concern has been in business divided by the number of weeks in business, multiplied by 52. Where a concern has been in business three or more complete fiscal years but has a short year as one of the years within its period of measurement, annual receipts means the total receipts for the

short year and the two full fiscal years divided by the total number of weeks in the short year and the two full fiscal years, multiplied by 52. For the purposes of this section, the Business Loan Programs consist of the 7(a) Loan Program, the Microloan Program, the Intermediary Lending Pilot Program, and the Development Company Loan Program (“504 Loan Program”). The Disaster Loan Programs consist of Physical Disaster Business Loans, Economic Injury Disaster Loans, Military Reservist Economic Injury Disaster Loans, and Immediate Disaster Assistance Program loans.

(d) * * *

(2) If a concern has acquired an affiliate or been acquired as an affiliate during the applicable period of measurement or before the date on which it self-certified as small, the annual receipts used in determining size status includes the receipts of the acquired or acquiring concern. This aggregation applies for the entire period of measurement, not just the period after the affiliation arose. However, if a concern has acquired a segregable division of another business concern during the applicable period of measurement or before the date on which it self-certified as small, the annual receipts used in determining size status do not include the receipts of the acquired division prior to the acquisition.

(3) Except for the Business Loan and Disaster Loan Programs, if the business concern or an affiliate has been in business for a period of less than 5 years, the receipts for the fiscal year with less than a 12-month period are annualized in accordance with paragraph (c)(2) of this section. Receipts are determined for the concern and its affiliates in accordance with paragraph (c) of this section even though this may result in using a different period of measurement to calculate an affiliate's annual receipts.

(4) The annual receipts of a former affiliate are not included if affiliation ceased before the date used for determining size. This exclusion of annual receipts of such former affiliate applies during the entire period of measurement, rather than only for the period after which affiliation ceased. However, if a concern has sold a segregable division to another business concern during the applicable period of measurement or before the date on which it self-certified as small, the annual receipts used in determining size status will continue to include the receipts of the division that was sold.

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3. Amend §121.106 by revising paragraph (b)(4)(ii) to read as follows:

§121.106 How does SBA calculate number of employees?

* * * * *

(b) ***

(4) ***

(ii) The employees of a former affiliate are not counted if affiliation ceased before the date used for determining size. This exclusion of employees of a former affiliate applies during the entire period of measurement, rather than only for the period after which affiliation ceased. However, if a concern has sold a segregable division to another business concern during the applicable period of measurement or before the date on which it self-certified as small, the employees used in determining size status will continue to include the employees of the division that was sold.

4. Amend §121.903 by revising paragraphs (a)(1)(ii) and (iii) to read as follows:

§121.903 How may an agency use size standards for its programs that are different than those established by SBA?

(a) ***

(1) ***

(ii) The size of a services concern by its average annual receipts over a period of at least 5 years, determined according to §121.104;

(iii) The size of other concerns on data over a period of at least 5 years, determined according to §121.104; or,

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Dated: November 25, 2019.

Christopher M. Pilkerton,
Acting Administrator.

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