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U.S. Industry code is also published annually by SBA in the FEDERAL REGISTER.

[65 FR 30840, May 15, 2000, as amended at 67 FR 52602, Aug. 13, 2002]

§ 121.102 How does SBA establish size standards?

(a) SBA considers economic characteristics comprising the structure of an industry, including degree of competition, average firm size, start-up costs and entry barriers, and distribution of firms by size. It also considers technological changes, competition from other industries, growth trends, historical activity within an industry, unique factors occurring in the industry which may distinguish small firms from other firms, and the objectives of its programs and the impact on those programs of different size standard levels.

(b) As part of its review of a size standard, SBA will investigate if any concern at or below a particular standard would be dominant in the industry. SBA will take into consideration market share of a concern and other appropriate factors which may allow a concern to exercise a major controlling influence on a national basis in which a number of business concerns are engaged. Size standards seek to ensure that a concern that meets a specific size standard is not dominant in its field of operation.

(c) As part of its review of size standards, SBA's Office of Size Standards will examine the impact of inflation on monetary-based size standards (*e.g.*, receipts, net income, assets) at least once every five years and submit a report to the Administrator or designee. If SBA finds that inflation has significantly eroded the value of the monetary-based size standards, it will issue a proposed rule to increase size standards.

(d) Please address any requests to change existing size standards or establish new ones for emerging industries to the Assistant Administrator for Size Standards, Small Business Administration, 409 3rd Street, SW., Washington, DC 20416.

[61 FR 3286, Jan. 31, 1996, as amended at 67 FR 3045, Jan. 23, 2002]

13 CFR Ch. I (1-1-05 Edition)

§ 121.103 How does SBA determine affiliation?

(a) *General Principles of Affiliation.* (1) Concerns and entities are affiliates of each other when one controls or has the power to control the other, or a third party or parties controls or has the power to control both. It does not matter whether control is exercised, so long as the power to control exists.

(2) SBA considers factors such as ownership, management, previous relationships with or ties to another concern, and contractual relationships, in determining whether affiliation exists.

(3) Control may be affirmative or negative. Negative control includes, but is not limited to, instances where a minority shareholder has the ability, under the concern's charter, by-laws, or shareholder's agreement, to prevent a quorum or otherwise block action by the board of directors or shareholders.

(4) Affiliation may be found where an individual, concern, or entity exercises control indirectly through a third party.

(5) In determining whether affiliation exists, SBA will consider the totality of the circumstances, and may find affiliation even though no single factor is sufficient to constitute affiliation.

(6) In determining the concern's size, SBA counts the receipts, employees, or other measure of size of the concern whose size is at issue and all of its domestic and foreign affiliates, regardless of whether the affiliates are organized for profit.

(b) *Exceptions to affiliation coverage.* (1) Business concerns owned in whole or substantial part by investment companies licensed, or development companies qualifying, under the Small Business Investment Act of 1958, as amended, are not considered affiliates of such investment companies or development companies.

(2)(i) Business concerns owned and controlled by Indian Tribes, Alaska Native Corporations (ANCs) organized pursuant to the Alaska Native Claims Settlement Act (43 U.S.C. 1601 *et seq.*), Native Hawaiian Organizations (NHOs), Community Development Corporations (CDCs) authorized by 42 U.S.C. 9805, or wholly-owned entities of Indian Tribes, ANCs, NHOs, or CDCs are not considered affiliates of such entities.

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(ii) Business concerns owned and controlled by Indian Tribes, ANCs, NHOs, CDCs, or wholly-owned entities of Indian Tribes, ANCs, NHOs, or CDCs are not considered to be affiliated with other concerns owned by these entities because of their common ownership or common management. In addition, affiliation will not be found based upon the performance of common administrative services, such as bookkeeping and payroll, so long as adequate payment is provided for those services. Affiliation may be found for other reasons.

(3) Business concerns which are part of an SBA approved pool of concerns for a joint program of research and development as authorized by the Small Business Act are not affiliates of one another because of the pool.

(4) Business concerns which lease employees from concerns primarily engaged in leasing employees to other businesses or which enter into a co-employer arrangement with a Professional Employer Organization (PEO) are not affiliated with the leasing company or PEO solely on the basis of a leasing agreement.

(5) For financial, management or technical assistance under the Small Business Investment Act of 1958, as amended, (an applicant is not affiliated with the investors listed in paragraphs (b)(5) (i) through (vi) of this section.

(i) Venture capital operating companies, as defined in the U.S. Department of Labor regulations found at 29 CFR 2510.3-101(d);

(ii) Employee benefit or pension plans established and maintained by the Federal government or any state, or their political subdivisions, or any agency or instrumentality thereof, for the benefit of employees;

(iii) Employee benefit or pension plans within the meaning of the Employee Retirement Income Security Act of 1974, as amended (29 U.S.C. 1001, *et seq.*);

(iv) Charitable trusts, foundations, endowments, or similar organizations exempt from Federal income taxation under section 501(c) of the Internal Revenue Code of 1986, as amended (26 U.S.C. 501(c));

(v) Investment companies registered under the Investment Company Act of

1940, as amended (1940 Act) (15 U.S.C. 80a-1, *et seq.*); and

(vi) Investment companies, as defined under the 1940 Act, which are not registered under the 1940 Act because they are beneficially owned by less than 100 persons, if the company's sales literature or organizational documents indicate that its principal purpose is investment in securities rather than the operation of commercial enterprises.

(6) A protege firm is not an affiliate of a mentor firm solely because the protege firm receives assistance from the mentor firm under Federal Mentor-Protege programs. Affiliation may be found for other reasons.

(c) *Affiliation based on stock ownership.* (1) A person (including any individual, concern or other entity) that owns, or has the power to control, 50 percent or more of a concern's voting stock, or a block of voting stock which is large compared to other outstanding blocks of voting stock, controls or has the power to control the concern.

(2) If two or more persons (including any individual, concern or other entity) each owns, controls, or has the power to control less than 50 percent of a concern's voting stock, and such minority holdings are equal or approximately equal in size, and the aggregate of these minority holdings is large as compared with any other stock holding, SBA presumes that each such person controls or has the power to control the concern whose size is at issue. This presumption may be rebutted by a showing that such control or power to control does not in fact exist.

(3) If a concern's voting stock is widely held and no single block of stock is large as compared with all other stock holdings, the concern's Board of Directors and CEO or President will be deemed to have the power to control the concern in the absence of evidence to the contrary.

(d) *Affiliation arising under stock options, convertible securities, and agreements to merge.* (1) In determining size, SBA considers stock options, convertible securities, and agreements to merge (including agreements in principle) to have a present effect on the power to control a concern. SBA treats such options, convertible securities,

and agreements as though the rights granted have been exercised.

(2) Agreements to open or continue negotiations towards the possibility of a merger or a sale of stock at some later date are not considered “agreements in principle” and are thus not given present effect.

(3) Options, convertible securities, and agreements that are subject to conditions precedent which are incapable of fulfillment, speculative, conjectural, or unenforceable under state or Federal law, or where the probability of the transaction (or exercise of the rights) occurring is shown to be extremely remote, are not given present effect.

(4) An individual, concern or other entity that controls one or more other concerns cannot use options, convertible securities, or agreements to appear to terminate such control before actually doing so. SBA will not give present effect to individuals’, concerns’ or other entities’ ability to divest all or part of their ownership interest in order to avoid a finding of affiliation.

(e) *Affiliation based on common management.* Affiliation arises where one or more officers, directors, managing members, or partners who control the board of directors and/or management of one concern also control the board of directors or management of one or more other concerns.

(f) *Affiliation based on identity of interest.* Affiliation may arise among two or more persons with an identity of interest. Individuals or firms that have identical or substantially identical business or economic interests (such as family members, individuals or firms with common investments, or firms that are economically dependent through contractual or other relationships) may be treated as one party with such interests aggregated. Where SBA determines that such interests should be aggregated, an individual or firm may rebut that determination with evidence showing that the interests deemed to be one are in fact separate.

(g) *Affiliation based on the newly organized concern rule.* Affiliation may arise where former officers, directors, principal stockholders, managing members, or key employees of one concern organize a new concern in the same or re-

lated industry or field of operation, and serve as the new concern’s officers, directors, principal stockholders, managing members, or key employees, and the one concern is furnishing or will furnish the new concern with contracts, financial or technical assistance, indemnification on bid or performance bonds, and/or other facilities, whether for a fee or otherwise. A concern may rebut such an affiliation determination by demonstrating a clear line of fracture between the two concerns. A “key employee” is an employee who, because of his/her position in the concern, has a critical influence in or substantive control over the operations or management of the concern.

(h) *Affiliation based on joint ventures.* A joint venture is an association of individuals and/or concerns with interests in any degree or proportion by way of contract, express or implied, consenting to engage in and carry out no more than three specific or limited-purpose business ventures for joint profit over a two year period, for which purpose they combine their efforts, property, money, skill, or knowledge, but not on a continuing or permanent basis for conducting business generally. This means that the joint venture entity cannot submit more than three offers over a two year period, starting from the date of the submission of the first offer. A joint venture may or may not be in the form of a separate legal entity. The joint venture is viewed as a business entity in determining power to control its management. SBA may also determine that the relationship between a prime contractor and its subcontractor is a joint venture, and that affiliation between the two exists, pursuant to paragraph (h)(4) of this section.

(1) Parties to a joint venture are affiliates if any one of them seeks SBA financial assistance for use in connection with the joint venture.

(2) Except as provided in paragraph (h)(3) of this section, concerns submitting offers on a particular procurement or property sale as joint venturers are affiliated with each other with regard to the performance of that contract.

(3) *Exception to affiliation for certain joint ventures.* (i) A joint venture of two or more business concerns may submit

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an offer as a small business for a Federal procurement without regard to affiliation under paragraph (h) of this section so long as each concern is small under the size standard corresponding to the NAICS code assigned to the contract, provided:

(A) The procurement qualifies as a “bundled” requirement, at any dollar value, within the meaning of §125.2(d)(1)(i) of this chapter; or

(B) The procurement is other than a “bundled” requirement within the meaning of §125.2(d)(1)(i) of this chapter, and:

(1) For a procurement having a receipts based size standard, the dollar value of the procurement, including options, exceeds half the size standard corresponding to the NAICS code assigned to the contract; or

(2) For a procurement having an employee-based size standard, the dollar value of the procurement, including options, exceeds \$10 million.

(ii) A joint venture of at least one 8(a) Participant and one or more other business concerns may submit an offer for a competitive 8(a) procurement without regard to affiliation under paragraph (h) of this section so long as the requirements of §124.513(b)(1) of this chapter are met.

(iii) Two firms approved by SBA to be a mentor and protégé under 13 CFR 124.520 may joint venture as a small business for any Federal Government procurement, provided the protégé qualifies as small for the size standard corresponding to the NAICS code assigned to the procurement and, for purposes of 8(a) sole source requirements, has not reached the dollar limit set forth in 13 CFR 124.519.

(4) A contractor and its ostensible subcontractor are treated as joint venturers, and therefore affiliates, for size determination purposes. An ostensible subcontractor is a subcontractor that performs primary and vital requirements of a contract, or of an order under a multiple award schedule contract, or a subcontractor upon which the prime contractor is unusually reliant. All aspects of the relationship between the prime and subcontractor are considered, including, but not limited to, the terms of the proposal (such as contract management, technical re-

sponsibilities, and the percentage of subcontracted work), agreements between the prime and subcontractor (such as bonding assistance or the teaming agreement), and whether the subcontractor is the incumbent contractor and is ineligible to submit a proposal because it exceeds the applicable size standard for that solicitation.

(5) For size purposes, a concern must include in its receipts its proportionate share of joint venture receipts, and in its total number of employees its proportionate share of joint venture employees.

(i) *Affiliation based on franchise and license agreements.* The restraints imposed on a franchisee or licensee by its franchise or license agreement relating to standardized quality, advertising, accounting format and other similar provisions, generally will not be considered in determining whether the franchisor or licensor is affiliated with the franchisee or licensee has the right to profit from its efforts and bears the risk of loss commensurate with ownership. Affiliation may arise, however, through other means, such as common ownership, common management or excessive restrictions upon the sale of the franchise interest.

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§ 121.104 How does SBA calculate annual receipts?

(a) *Receipts* means “total income” (or in the case of a sole proprietorship, “gross income”) plus “cost of goods sold” as these terms are defined and reported on Internal Revenue Service (IRS) tax return forms (such as Form 1120 for corporations; Form 1120S and Schedule K for S corporations; Form 1120, Form 1065 or Form 1040 for LLCs; Form 1065 and Schedule K for partnerships; Form 1040, Schedule F for farms; Form 1040, Schedule C for other sole proprietorships). Receipts do not include net capital gains or losses; taxes collected for and remitted to a taxing authority if included in gross or total income, such as sales or other taxes