

**SMALL BUSINESS ADMINISTRATION****13 CFR Parts 121, 124, 125, 126 and 127**

RIN 3245-AG58

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

AGENCY: U.S. Small Business Administration.

ACTION: Final rule.

**SUMMARY:** This rule amends the U.S. Small Business Administration's (SBA or Agency) regulations to implement provisions of the National Defense Authorization Act of 2013, which pertain to performance requirements applicable to small business and socioeconomic program set-aside contracts and small business subcontracting. This rule also amends SBA's regulations concerning the nonmanufacturer rule and affiliation rules. Further, this rule allows a joint venture to qualify as small for any government procurement as long as each partner to the joint venture qualifies individually as small under the size standard corresponding to the NAICS code assigned in the solicitation.

**DATES:** This rule is effective on June 30, 2016.

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**SUPPLEMENTARY INFORMATION:****Introduction**

SBA published a proposed rule regarding these changes in the **Federal Register** on December 29, 2014 (79 FR 77955), inviting the public to submit comments on or before February 27, 2015. This comment period was extended through April 6, 2015, by notice in the **Federal Register** published on March 9, 2015 (80 FR 12353). SBA also conducted tribal consultations in Washington, DC (February 26, 2015), Catoosa, OK (April 20, 2015), and Anchorage, AK (April 22, 2015), in which SBA accepted comments on the proposed rule. Transcripts of these consultations are in the rule docket (SBA-2014-0006, viewable on [Regulations.gov](http://Regulations.gov) using the docket number). SBA received a total of 216 comments on the proposed rule. Twenty-eight comments were supportive of the rule generally without referencing specific sections of the rule. Seventeen of those generally supportive comments advocated for fast

implementation of the rule. Several of these commenters suggested that SBA issue this rule as an interim final rule. Once SBA has published a proposed rule, the next step in the process is to analyze public comments and publish a final rule. Publishing an "interim final rule" after publishing a proposed rule would not expedite the process to finalize the provisions contained in the proposed rule. As such, SBA has not followed that recommendation and is publishing this rule as a final rule. Sixteen comments requested an extension of time for the submission of comments. An extension of the comment period was provided through April 6, 2015, and SBA believed that a further extension was not needed. Seven comments did not support the rulemaking generally and did not reference specific sections that were opposed. Some of these comments were related to regulations not subject to changes in the proposed rule and were considered outside the scope of this rulemaking. SBA's discussion below summarizes the proposed rule, the comments related to each section of the proposed rule and SBA's responses.

**Summary of Proposed Rule, Comments, and SBA's Responses****Procurement Center Representative Responsibilities**

Section 1621 of the National Defense Authorization Act of 2013 (NDAA), Public Law 112-239, 126 Stat. 1632 (Jan. 2013), revised the Small Business Act regarding the responsibilities of Procurement Center Representatives (PCRs). Section 1621 clarifies that PCRs have the ability to review barriers to small business participation in Federal contracting and to review any bundled or consolidated solicitation or contract in accordance with the Small Business Act. SBA proposed to amend 13 CFR 125.2(b)(1)(i)(A), based on the changes in Section 1621(c)(6)(H) of the NDAA. SBA also proposed to add language to § 125.2(b)(1)(i)(A) and to § 125.2(b)(1)(ii), which clarifies that PCRs advocate for the maximum practicable utilization of small business concerns in Federal contracting, including advocating against the unjustified consolidation or bundling of contract requirements.

Pursuant to Section 1621(c)(6)(G) of the NDAA, SBA proposed new § 125.2(b)(1)(iv), which states that PCRs will consult with the agency's Office of Small and Disadvantaged Business Utilization (OSDBU) and Office of Small Business Program (OSBP) Director regarding an agency's decision to convert an activity performed by a small

business concern to an activity performed by a Federal employee. SBA also proposed new § 125.2(b)(1)(v) pursuant to the language enacted by Section 1621(c)(6)(F) of the NDAA, which allows PCRs to receive unsolicited proposals from small business concerns and to provide those proposals to the appropriate agency's personnel for review and disposition.

SBA proposed to amend § 125.2(b)(1) and (2), which pertain to Breakout PCRs (BPCRs). Sections 1621(e) and (f) of the NDAA effectively eliminate the statutory authority for the separate BPCR role. As a result, SBA proposed to reassign the responsibilities currently held by BPCRs to PCRs. SBA proposed to add § 125.2(b)(1)(i)(F), which states that PCRs also advocate full and open competition in Federal contracting and recommend the breakout for competition of items and requirements which previously have not been competed. SBA also proposed to eliminate § 125.2(b)(2) that provided guidance on the role and responsibilities of BPCRs, and redesignate current § 125.2(b)(3) as the new § 125.2(b)(2) and remove any reference to BPCRs from that paragraph.

SBA received 13 comments regarding its proposed changes to § 125.2. Ten of these comments were supportive of the changes to this section. One commenter suggested that SBA clarify the proposed language in § 125.2(b)(1)(i)(A), which states "This review includes acquisitions that are Multiple Award Contracts where the agency has not set-aside all or part of the acquisition or reserved the acquisition for small businesses." This commenter suggested that SBA delete the words "or part" to make it clear that PCRs can review any Multiple Award Contract that is not 100% set-aside for small business competition. SBA is not adopting this recommendation because the proposed language states that PCRs can review Multiple Award Contracts that are not entirely set aside for small businesses, meaning partially set-aside. Furthermore, if SBA eliminated "or part" it would indicate that PCRs cannot review Multiple Award Contracts that are entirely set aside for small businesses, which is within the PCRs responsibilities.

Another commenter suggested that SBA should meet with contracting officers to assist with setting aside contracts for small businesses. It is the role of the PCR to review procurements that are not set aside for small businesses. PCRs are often located at the procuring activity and routinely interface with contracting officers regarding whether to set aside

acquisitions for small business competition. It is already part of their responsibilities to meet with contracting officers and discuss acquisition planning. As such, it is not necessary to adopt this suggested change.

Another commenter suggested that the term "acquisition" as used in § 125.2 should be changed to "acquisition, including bridge, interim, and follow-on contracts." The term "acquisition" is defined broadly in section 2.101 of the Federal Acquisition Regulation (FAR) to include "award of contracts." The commenter is referencing specific types of contracts that are included in the FAR definition of "acquisition." SBA believes that this clarification is not necessary and does not adopt it in this final rule.

Another commenter suggested that PCRs should unbundle sole source contracts that are made to incumbent vendors in order to allow the agency time to competitively re-procure the goods or services. The proposed rule directly addresses this concern by providing PCRs with the ability to advocate against consolidation or bundling of contract requirements and reviewing any justification provided for such bundling or consolidation. The same commenter also suggested that a prime contract not be awarded on a sole source basis unless the prime contractor agrees to retain its subcontractors under the previous award and incorporates the small business plan associated with the previous award. SBA does not have the authority to mandate which subcontractors a prime contractor chooses to include in a subcontracting plan or to mandate that a prime contractor incorporate a particular subcontracting plan into its offer, and therefore SBA is not adopting this suggestion.

One commenter requested clarification of the language proposed in § 125.2(b)(1)(i)(F) stating, "PCRs also advocate competitive procedures and recommend the breakout for competition when appropriate." The commenter raised concerns that this language will discourage contracting officers from utilizing the sole source authority provided for the 8(a) Business Development (BD) program, the Women-Owned Small Business (WOSB) program and the HUBZone program. The commenter suggests that SBA clarify what a PCR would consider as "appropriate" in the decision to recommend competition, and if such a decision is made, that contracting officers and PCRs document this decision in the contract file along with an explanation for why competition is considered more appropriate than a

small business program sole source award. The language referenced by the commenter is a BPCR responsibility that SBA is transferring to PCRs due to the statute's elimination of the BPCR role. In addition, PCRs provide contracting officers with guidance on the availability of sole source and competitive options, but the contracting officer has the discretion to choose an acquisition program or method, in accordance with SBA's guidance on parity.

Another commenter noted that PCRs will have to coordinate with agency officials to implement the NDAA's requirement, set forth at § 125.2(b)(1)(iv), that PCRs consult with agency OSDDBUs regarding an agency's decision to convert an activity performed by a small business concern to an activity performed by a Federal employee. The statute provides that the PCR will consult with the OSDDBU. SBA understands that the PCR and OSDDBU will consult with other agency officials, as necessary. However, SBA does not believe that additional clarification is necessary and therefore SBA adopts the proposed language in this final rule.

Section 1623 of the NDAA requires that each Federal department or agency provide opportunities for the participation of small business concerns during acquisition planning processes and in acquisition plans. This section also requires that each Federal department or agency invite the participation of the appropriate OSDDBU Director in acquisition planning processes and provides that Director with access to acquisition plans. SBA incorporates the exact statutory text from Section 1623 of the NDAA into 13 CFR 125.2(c)(1) by adding new paragraphs (vi) and (vii).

#### **Limitations on Subcontracting**

Section 1651 of the NDAA, as codified at 15 U.S.C. 657s, requires that the limitations on subcontracting for full or partial small business set-aside contracts, HUBZone contracts, 8(a) BD contracts, Service-Disabled Veteran-Owned (SDVO) Small Business Concern (SBC) contracts, and WOSB and Economically Disadvantaged Women Owned Small Business (EDWOSB) contracts, be evaluated based on the percentage of the overall award amount that a prime contractor spends on its subcontractors. Significantly, the NDAA excludes from the limitations on subcontracting calculation the percentage of the award amount that the prime contractor spends on similarly situated entity subcontractors. Specifically, the NDAA deems work done by similarly situated entities not to

be subcontracted work for purposes of complying with the limitations on subcontracting requirement. Thus, work done by a similarly situated entity is counted in determining whether the applicable limitation on subcontracting is met. When a contract is awarded pursuant to a small business set-aside or socioeconomic program set-aside or sole source authority, a similarly situated entity subcontractor is a small business concern subcontractor that is a participant of the same SBA program that qualified the prime contractor as an eligible offeror and awardee of the contract.

Currently, SBA's regulations contain different terms for compliance with the performance of work requirements based on the type of small business program set-aside at issue. The method for calculating compliance not only varies by program set-aside type, but also based on whether the acquisition is for services, supplies, general construction, or specialty trade construction. Section 1651 of the NDAA creates a shift from the concept of a required percentage of work to be performed by a prime contractor to the concept of limiting a percentage of the award amount to be spent on subcontractors. The goal is the same: To ensure that a certain amount of work is performed by a small business concern (SBC) that qualified for a small business program set-aside or sole source procurement due to its socioeconomic program status. The Government's policy of promoting contracting opportunities for small businesses, HUBZone SBCs, SDVO SBCs, WOSBs/EDWOSBs, and 8(a) SBCs is seriously undermined when firms pass on work in excess of applicable limitations to firms that are other than small or that are not otherwise eligible for specific types of small business contracts. SBA has revised all references to "performance of work" requirements found in parts 121, 124, 125, 126, and 127 to "limitations on subcontracting."

SBA proposed to totally revise § 125.6 to take into account the new definition and calculation for the limitations on subcontracting as described in Section 1651 of the NDAA. Additionally, SBA reorganized and simplified this section for easier use. Proposed § 125.6(a) explains how to apply the limitations on subcontracting requirements to small business set-aside contracts. Instead of providing different methods of determining compliance based on the type of small business set-aside program at issue and the type of good or service sought, Section 1651(a) of the NDAA provides one method for determining compliance that is shared by almost all

applicable small business set-aside programs, but varies based on whether the contract is for services, supplies or products, general construction, specialty trade construction, or a combination of both services and supplies.

The approach described in Sections 1651(a) and (d) of the NDAA is to create a limit on the percentage of the award amount received by the prime contractor that may be spent on other-than-small subcontractors. Specifically, the NDAA provides that a small business awarded a small business set-aside, 8(a), SDVO small business, HUBZone, or WOSB/EDWOSB award “may not expend on subcontractors” more than a specified amount. However, as noted below, work done by “similarly situated entities” does not count as subcontracted work for purposes of determining compliance with the limitation on subcontracting requirements. Proposed § 125.6(a)(1) and (a)(2) addressed the limitations on subcontracting applicable to small business set-aside contracts requiring services or supplies. The limitation on subcontracting for both services and supplies is statutorily set at 50% of the award amount received by the prime contractor. See 15 U.S.C. 657s(a).

Proposed § 125.6(a)(3) addressed how the limitation on subcontracting requirement would be applied to a procurement that combines both services and supplies. This provision intended to clarify that the contracting officer’s (CO) selection of the applicable NAICS code will determine which limitation of subcontracting requirement applies. Proposed § 125.6(a)(4) and (5) addressed the limitations on subcontracting for general and specialty trade construction contracts. SBA proposed to keep the same percentages that currently apply: 15% for general construction and 25% for specialty trade construction.

SBA received 115 comments regarding proposed § 125.6(a). The overwhelming majority of these comments requested that SBA allow contractors to exclude the “cost of materials”, as that term is currently defined in § 125.1(i), from the limitations on subcontracting calculation for all contracts. SBA notes that the cost of materials has never been, and was not proposed to be, a term that applies to service contracts. Historically and as proposed, the term cost of materials is applicable to supply, construction, or specialty trade construction set-aside contracts. “Cost of materials” is currently excluded from the performance of work requirements and SBA did not intend to remove this exclusion in proposed paragraph

125.6(a). The exclusion of “cost of materials” from the limitations on subcontracting for supply, construction, and specialty trade construction procurements is included in this final rule. Several commenters suggested that SBA extend this exclusion to procurements assigned a service NAICS code, but, SBA does not believe that this change is needed. As discussed below, because the limitations on subcontracting for a services contract apply only to the services portion of the contract, any “cost of materials” would not be part of the services to be provided through the contract and, thus, would be excluded from the limitations on subcontracting analysis on that basis.

For a mixed contract (*i.e.*, one in which both supplies and services are being procured), commenters believed that the limitation on subcontracting should apply only to that portion of the requirement identified as the primary purpose of the contract. In other words, where, for example, a contracting officer has assigned a services NAICS code to a requirement that has both a services and supply component, the commenters believed that the limitation on subcontracting should apply only to the services portion of the work to be performed. In our view, Section 46(a)(3) of the Small Business Act, 15 U.S.C. 657s(a)(3), which was established by Section 1651 of the NDAA, provides the necessary guidance for mixed contracts. The CO must first determine which category, services or supplies, has the greatest percentage of the contract value, and then assign the appropriate NAICS code. The corresponding limitations on subcontracting will apply to the contract, depending on whether the CO has selected a supply NAICS code or a services NAICS code. Thus, the statutory authority authorizes that the limitations on subcontracting apply only to that portion of the requirement identified as the primary purpose of the contract. SBA has clarified that intent in this final rule, and has moved the requirements pertaining to mixed contracts to § 125.6(b). Therefore, where a procurement combines supplies and services, the limitations on subcontracting apply only to subcontracts that correspond to the principal purpose of the prime contract. For a contract principally for services, but which also requires supplies, this means that the prime contractor or its similarly situated subcontractors cannot subcontract more than 50 percent of the services to other than small concerns. However, the prime contractor can subcontract all of the supply components to any size business.

Several commenters also recommended that SBA change the current definition of “cost of materials” to include any service or product that cannot be procured from a small business. Other commenters recommended that very specific types of services be included in the definition of “cost of materials” such as transportation when procured in the performance of an environmental remediation procurement. SBA did not propose to change the definition of “cost of materials” and does not believe that a change is necessary or required to implement NDAA 2013.

One commenter requested clarity on whether contractors can exclude from the limitations on subcontracting the non-service costs associated with a procurement for services. As noted above, SBA believes that only the services portion of a requirement identified as a services requirement are considered in determining compliance with the limitation on subcontracting requirements. This means that any costs associated with supply items are excluded from that analysis. However, all costs associated with providing the services, including any overhead or indirect costs associated with those services, must be included in determining compliance. This final rule clarifies this application. SBA has also added another example to § 125.6(a)(3) that involves both supplies and services to clarify how the limitations on subcontracting apply in these circumstances.

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

the same small business program participants through subcontract awards.

The proposed rule identified SBA's concern with determining compliance with the limitations on subcontracting by looking solely to the first tier of the contracting process (agreements between the prime contractor and its direct subcontractors). If all that was looked at was the first tier subcontract, that first tier subcontractor could in turn pass all of its performance on to a large or otherwise not similarly situated entity through a second subcontract. SBA believes that the intent of the changes in the NDAA were to ensure that the benefits of set-aside contracts flow to the intended beneficiaries. SBA does not believe that an intended consequence of the change was to make it easier to divert these benefits to ineligible entities by merely moving contracts down one or two tiers in the contracting process. As such, the proposed rule retained a requirement that firms benefiting from contracts, and their similarly situated subcontractors perform a required amount of work on the contract themselves. SBA believes that requiring firms to perform significant portions of the work, as well as to retain a significant portion of the contract award, will continue to help ensure that the benefits from these contracts flow to the intended parties.

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

SBA received three comments regarding SBA's proposal to apply the limitations on subcontracting collectively to all similarly situated entities that are performing work on the contract and that are counted toward the prime contractor's percentage of performance. Two commenters supported SBA's proposed approach and one commenter opposed this approach, and suggested that SBA apply the limitations on subcontracting only to the prime contractor and the first tier subcontractor. Applying the limitations on subcontracting to only the prime contractor and first tier subcontractor creates the possibility that the first tier subcontractor may subcontract 100% of the work it received from the prime to an entity that is not similarly situated as the prime contractor. SBA remains concerned that this would create a

loophole for entities that are not small business concerns and would not have qualified to receive the prime contract to benefit, as subcontractors, from government contracts that are set aside for performance by small business concerns. To address these concerns, SBA will apply the limitations on subcontracting collectively to the prime and any similarly situated first tier subcontractor, and any work performed by a similarly situated first tier subcontractor will count toward compliance with the applicable limitation on subcontracting. Any work that a similarly situated first tier subcontractor subcontracts, to any entity, will count as subcontracted to a non-similarly situated entity for purposes of determining whether the prime/sub team performed the required amount of work. In other words, work that is not performed by the employees of the prime contractor or employees of first tier similarly situated subcontractors will count as subcontracts performed by non-similarly situated concerns.

Proposed § 125.6(b)(1) required prime contractors to enter a written agreement with each similarly situated entity that identifies the similarly situated entity and the percentage of work to be performed by that entity. The proposed rule provided that the written agreement must be signed by the similarly situated entity and provided to the contracting officer with the prime contractor's offer. Proposed § 125.6(b)(2) stated that it is immaterial whether the specific subcontractors identified in the written agreement satisfy the percentage of work identified, as long as all similarly situated entities collectively, along with the prime contractor, satisfy the performance of work requirements. Proposed § 125.6(b)(3) stated that a prime contractor may be debarred for a violation of the spirit and intent of this paragraph.

SBA received forty-seven comments related to its proposed § 125.6(b), which described how subcontracts to similarly situated entities will be excluded from the prime contractor's limitations on subcontracting. Eight of these comments generally supported § 125.6(b) as proposed. Four of these comments were considered outside the scope of this rulemaking as they advocated for an interim final rule to apply the exclusion of subcontracts to similarly situated entities from the limitations on subcontracting. One comment generally opposed proposed § 125.6(b), but did not have any suggested alternatives.

Twenty-three of the forty-seven comments received were related to proposed § 125.6(b)(1), which discussed

the details that must be included in the required written agreements between the prime contractor and its similarly situated entity subcontractors. Six of these commenters supported the concept of a required written agreement but disagreed with specific aspects of the agreement such as identifying the proposed similarly situated entity subcontractors and identifying the percentage of work to be performed by those subcontractors. Seventeen of the commenters opposed the requirement for any written agreement between a prime contractor and a similarly situated entity subcontractor because it would be impossible to know their identity and possible percentage of performance in advance of the award and because it would be unnecessarily burdensome on small business prime contractors to draft and enter these agreements. SBA also received comments concerning how to address the substitution of one subcontractor for another, or a decision by the prime contractor after award to either perform the work itself or subcontract work to a similarly situated entity.

In response to these comments, SBA has decided not to require a written agreement in order for a prime contractor to rely on the work to be performed by similarly situated entities. For many years SBA's rules have allowed similarly situated entities to be counted towards the limitations on subcontracting requirements under SDVO or HUBZone set-asides or sole source awards, without also requiring a separate written agreement. There is no evidence that this long-standing policy has been difficult to understand or administer, and the rule change that limits subcontracting without regard to cost incurred for personnel should make it easier to track and identify subcontracts, especially in light of other existing requirements to report on subcontracts, such as FAR 52.204-10 (48 CFR 52.204-10). (Reporting Executive Compensation and First-Tier Subcontract Awards). In addition, SBA is concerned that requiring a written agreement would cause an administrative burden on small business concerns, which would in turn cause them to utilize this tool less often, for fear of violating the written agreement or because they would need to constantly amend the agreement based on modifications with respect to team members or to percentages of work performed by individual team members. Further, requiring a written agreement prior to offer would limit a firm's ability to decide to utilize a similarly situated entity after award and during contract

performance. Many of the commenters pointed out that it may be difficult to determine whether a subcontractor will or will not be used on certain contracts, especially indefinite delivery indefinite quantity task or delivery order contracts. Small business concerns should have the discretion to run their business and perform contracts as they see fit, and the discretion to subcontract or not subcontract at any point during contract performance, provided they comply with the overall performance requirements. Further, SBA and agencies do not have the resources to review agreements or amendments to those agreements.

SBA received several comments in response to its request for comments on whether prime contractors should be required to report to the contracting officer on their compliance with the limitations on subcontracting. Eight commenters supported mandatory compliance reporting, and five of those commenters recommended that the reporting be made at the end of the contract term. Three of the supportive commenters recommended compliance reporting on a quarterly or annual basis. Three commenters opposed mandatory compliance reporting because it would be too burdensome on small business concerns. One commenter suggested that SBA use its auditing and investigating authority to determine compliance rather than requiring contractors to report their compliance. Another commenter suggested that the only necessary compliance reporting should be made in the offer.

In addition to the requirement for a written agreement, SBA also proposed to require compliance reporting from small business concerns that rely on similarly situated entities to meet their performance obligations under a set aside contract. Notably, SBA did not propose to require compliance reporting from all small business concerns (*i.e.*, firms that do not rely on similarly situated small business concerns to meet their performance obligations). Upon further review, SBA believes that this proposal would create a disincentive to utilize this new statutory authority. Compliance reporting was not required by the statute, and in fact, reliance on similarly situated entities to help meet their performance requirements actually makes it easier these firms to comply with their obligations. Moreover, requiring a prime contractor to report on compliance with the limitations on subcontracting when it uses one or more similarly situated entities could hamper flexibility for firms during contract performance. For example, a firm may initially intend to

comply on its own, but may find during contract performance that it must rely on one or more similarly situated subcontractors to meet its performance obligations. In addition, a firm may intend to use one or more similarly situated entities to help it meet its performance obligations, but then may decide during contract performance that it will perform all of the required work with its own employees. These practical realities have led us to remove the compliance reporting requirement with respect to similarly situated entities. SBA may, in the future, propose a rule that requires compliance reporting from all small business concerns, not just those that rely on similarly situated entities. However, such a change would require notice and a request for public comment that is not part of this rulemaking.

For many years, SBA's regulations have allowed similarly situated entities to count towards fulfilling the limitations on subcontracting requirements under a HUBZone or SDVO set-aside or sole source contract, without a requirement to report to the CO. As discussed above, prime contractors are already required to report on subcontracting pursuant to FAR clause 52.204-10 (48 CFR 52.204-10). Thus, because SBA is not requiring written agreements in this final rule, at this time SBA has decided not to require compliance reports from firms that are utilizing similarly situated subcontractors. SBA believes that to the extent compliance reporting should be required, it should be required from all small businesses, not just those that team with similarly situated subcontractors. Thus, SBA intends to issue a proposed rule to request public comment on the issue of whether all small businesses (and not only those that are using similarly situated entities to perform a contract) should be required to report on compliance with the limitations on subcontracting on set-aside contracts. SBA understands the recommendations made by the Government Accountability Office to strengthen the monitoring and oversight of the required performance percentages for all small businesses that receive set-aside awards, including 8(a) contractors, and believes that a separate rulemaking should address that issue more appropriately.

SBA's proposed § 125.6(b) explained that work subcontracted to similarly situated entities may be excluded from a prime contractor's calculation of its limitation on subcontracting. SBA proposed to include three examples to § 125.6(b) to demonstrate how a small business concern or Federal agency

should apply the exclusion for similarly situated entities and determine compliance with the limitations on subcontracting. The final rule has redesignated proposed § 125.6(b) as § 125.6(c). As mentioned above, in response to comments, SBA is adding three more examples to redesignated § 125.6(c) to clarify how the limitations on subcontracting apply when the procurement involves a mix of services and supplies.

SBA received six comments in response to proposed § 125.6(b)(3). All six commenters opposed SBA's ability to consider a party's failure to comply with the spirit and intent of the subcontract with a similarly situated entity as a basis for debarment. These commenters argued that the proposed regulation is too vague because it is unclear how SBA would demonstrate a violation of the spirit and intent, and that the penalty of debarment is too severe. SBA clarifies that a contractor's violation of the spirit and intent of a subcontract with a similarly situated entity is something SBA may consider as a basis for debarment, but is not required to consider for debarment. SBA does not take debarment and suspension lightly and understands fully the implications of such an action. As such, SBA would not initiate any debarment or suspension action unless SBA believed that the government's interests needed to be protected. This would happen where, for example, a small business prime contractor had no intent to actually use similarly situated entities. In such a case, the firm's certification would be a misrepresentation to the government, and the government could no longer rely on any representations made by the firm. SBA would not consider a debarment or suspension action where a firm made a good faith representation that it, along with one or more similarly situated entities, would meet the performance of work requirements and through unforeseen circumstances it failed to do so. Additionally, should SBA choose to consider this as a basis for debarment, the entity at issue would have an opportunity to respond to any allegation with its own arguments and evidence. SBA believes this provision is necessary to deter potential fraud, waste, and abuse of the prime contractor's ability to exclude similarly situated entity work from its limitations on subcontracting. SBA has moved the discussion of debarment to redesignated § 125.6(h).

SBA proposed to relocate the definitions that are relevant to the limitations on subcontracting that are currently found in § 125.6(e) to § 125.1

with the other definitions that are applicable to part 125. Section 1651(e) of the NDAA provides the definitions of “similarly situated entity” and “covered small business concern.” Proposed § 125.1(x) interprets the statutorily prescribed definition for similarly situated entity.

SBA received 34 comments about its proposed definition of similarly situated entity. Fifteen of these comments opposed SBA’s proposition that a small business concern qualifies as a similarly situated entity if it qualifies as small for the NAICS code assigned to the prime contractor’s procurement, in addition to the other requirements included in the definition of “similarly situated entity.” Three commenters requested further clarification of the definition. Two commenters supported the definition as proposed. The remaining comments were questions regarding the application of the proposed definition to procurements for specific types of services or were comments that were considered outside the scope of this rulemaking, as they suggested changes that were not proposed and are not authorized by the statute. For example, one commenter recommended that when a solicitation requires the use of a specific subcontractor, that entity should qualify as a similarly situated entity, regardless of the subcontractor’s size or small business program participation. SBA believes that this would conflict with the statutory intent that only entities that would be eligible as prime contractors may qualify as similarly situated entity subcontractors. Another commenter recommended that all individuals classified by the Internal Revenue Service as independent contractors should be included in the definition of similarly situated entity. Again, this would conflict with the statutory intent that only contractors who would qualify for the prime contract are eligible to count toward the prime contractor’s performance of work as similarly situated entity provisions. However, SBA has clarified in § 125.6(e)(3) that performance by an independent contractor is considered a subcontract, and may qualify as a similarly situated entity if the contractor meets the relevant criteria.

The majority of the questions related to the application of the definition to procurements for architecture and engineering services. Often the prime contract is assigned the NAICS code representing architecture services and has a size standard that is less than the size standard for engineering services. In these cases, the engineering services are often subcontracted and commenters were concerned about how the

engineering firm could qualify as a similarly situated entity if it were required to comply with the size standard assigned to the prime contract. SBA received other comments which described complex procurements involving multiple services. Firms that are small for certain types of services would not qualify as small for the NAICS assigned to the contract. In response to the comments received, SBA is not adopting its proposed definition of “similarly situated entity” and instead will allow an entity to qualify as a similarly situated entity if it is small for the NAICS code that the prime contractor assigns to the subcontract. SBA believes that this alteration to the definition will address the concerns raised about specific types of service procurements. Requiring the subcontractors to be small for the size standard assigned to the prime contract would unduly restrict the ability of prime contractors to find and use similarly situated entities to satisfy the limitations on subcontracting. SBA believes the approach adopted in this final rule will increase the ability of small business prime contractors to utilize similarly situated entity subcontractors. In addition, this approach is consistent with SBA’s rules which require a prime contractor to assign the NAICS code to a subcontract which describes the principal purpose of the subcontract. 13 CFR 125.3(c)(1)(v).

In § 125.6(c), SBA proposed to require a certification requirement in connection with the limitations on subcontracting requirement. However, existing regulations require firms to agree to comply with the limitations on subcontracting in connection with a set-aside contract, including firms that are utilizing similarly situated entities, and it is SBA’s intent to continue that practice. Consequently, SBA’s rules do not specifically require certification from the prime contractor when utilizing similarly situated entities. In order to be awarded a set-aside contract as a small business, the prime contractor must agree to comply with the limitations on subcontracting in connection with the offer, whether that entails using similarly situated entities or not.

Proposed § 125.6(f) and (h) contained language that is included in the current rule and did not contain any proposed changes to that language aside from adding new headings to these paragraphs and reorganizing this language. These provisions have been redesignated as § 125.6(d) and (e) in this final rule. Proposed § 125.6(f) discussed HUBZone procurements of

commodities. SBA did not receive any comments within the scope of this rulemaking that relate to proposed § 125.6(f) and SBA is adopting the language of proposed § 125.6(f) in § 125.6(d). Proposed § 125.6(g) discussed how to request a change in the applicable limitation on subcontracting for a particular industry. SBA received two comments related to proposed § 125.6(g). One comment supported the language and the other comment was a question regarding the transition period for industries where the limitations on subcontracting percentages do not align with industry practices. It is unclear what the commenter is requesting as this paragraph does not reference a transition period. This final rule adopts the language of proposed § 125.6(g).

Proposed § 125.6(h) discussed the period of time used to determine compliance with the limitations on subcontracting. While SBA did not propose a change to the time period used to determine compliance, SBA received 15 comments related to this paragraph. Twelve of the comments contained suggestions for how to modify the proposed language to be less burdensome on small business prime contractors and allow prime contractors to have the maximum flexibility to choose and manage subcontractors. The majority of these commenters suggested that SBA use the entire contract term, the base and all option periods, to determine whether the prime contractor has complied with the limitations on subcontracting. Other commenters suggested that periodic checks of compliance would suffice in addition to checking compliance during contract close-out. The remaining commenters believed that the current requirement was too onerous on prime contractors to check compliance for each task order issued under an IDIQ contract.

In response to these comments, SBA again emphasizes that redesignated paragraph (e) is not a change in policy. It recites the policy set forth in a prior SBA rulemaking on multiple award contracting, as set forth at § 125.2(e)(2)(iv), but clarifies that this policy applies to single award task and delivery order contracts, not just multiple award contracts. SBA believes that this provides contracting officers with the maximum flexibility to determine the time period that will be used for determining compliance with the limitations on subcontracting for performance of a task or delivery order contract. SBA does not believe it is appropriate for compliance to be determined at the end of the contract term, including all option periods,

because it would eliminate the ability to monitor compliance during performance and request a proposed corrective action from the contractor in order to satisfy the limitations on subcontracting during the performance period. When compliance is monitored per base period and each option period, or per order in some cases, it helps ensure that the intended benefits are flowing to the intended recipients. If the policy were to wait until performance was concluded, the remedies would be much more limited.

Proposed § 125.6(i) addressed how the limitations on subcontracting apply to members of a Small Business Teaming Arrangement (SBTA) that are exempt from affiliation according to § 121.103(b)(9). Proposed § 125.6(i) stated that the limitations on subcontracting apply to the combined effort of the SBTA members, not to the individual members of the SBTA separately. However, SBTAs only apply to bundled contracts, and a bundled contract is a contract that is not suitable for award to a small business concern. The Small Business Act allows small businesses to team together on a bundled contract and requires the agency to consider the capabilities of subcontractors on the team, and exempt those team members from affiliation. 15 U.S.C. 644(e)(4). If a contract contains a reserve, it is suitable for award to a small business, and thus the contract is not bundled and the SBTA would not apply. Thus, SBA is removing language concerning reserves from § 121.109(b)(9) and language concerning SBTAs from § 125.6, because the limitations on subcontracting do not apply. SBTAs with respect to bundled and consolidation contracts are discussed in depth at § 125.2(b)(iii)(G).

SBA proposed to add new § 125.6(j), which exempted small business set-aside contracts valued between \$3,500 and \$150,000 from the limitations on subcontracting requirements. Section 46 of the Small Business Act mandates that the statutory performance of work requirements (limitations on subcontracting) apply to small business set-aside contracts with values above \$150,000, and contracts of any amount awarded to socioeconomically disadvantaged contracting programs, such as 8(a), WOSB/EDWOSB, HUBZone, and SDVO set-aside contracts. 15 U.S.C. 657s. Although the limitations on subcontracting apply to all of these contracts, Section 46 does not specifically cite Section 15(j) of the Small Business Act, which is the statutory authority for non-socioeconomically disadvantaged small business set-asides between \$3,500 and

\$150,000. Further, Section 15(j) of the Small Business Act does not mention any limitation on subcontracting requirements in connection with the performance of set-aside contracts under Section 15(j). Thus, the FAR provides that “[t]he contracting officer shall insert the clause at 52.219-14, Limitations on Subcontracting, in solicitations and contracts for supplies, services, and construction, if any portion of the requirement is to be set aside or reserved for small business and the contract amount is expected to exceed \$150,000.” FAR 19.508(e) (48 CFR 19.508(e)). SBA proposed not to expand the application of the limitations on subcontracting to apply to small business set-asides below \$150,000, but rather to adopt what the FAR has done. The limitation on subcontracting requirements would continue to apply to all 8(a), HUBZone, SDVO, and WOSB/EDWOSB set-aside contract awards regardless of value, including but not limited to contracts with values between \$3,500 and \$150,000. SBA requested comments regarding whether the limitations on subcontracting should apply to small business set-aside contracts valued between \$3,500 and \$150,000. In addition, SBA requested comments on whether, for policy reasons and for purposes of consistency, the performance of work/subcontracting limitation requirements should apply to a small business set-aside contract with a value between \$3,500 and \$150,000.

SBA received thirteen comments regarding proposed § 125.6(j). Ten of these comments supported SBA’s proposed approach to exclude procurements with a value between \$3,500 and \$150,000 from the limitations on subcontracting. One commenter opposed this approach and stated that eliminating the application of the nonmanufacturer rule (NMR) to procurements of this value would open itself up to direct competition with non-U.S., other than small manufacturers. Another commenter suggested that SBA should exclude all small business program set-aside procurements valued between \$3,500 and \$150,000 from the limitations on subcontracting rather than just small business set-aside procurements. The remaining comment received was outside the scope of this rule-making.

In response to these comments, SBA notes that the limitations on subcontracting rule and the NMR as set forth in the Small Business Act do not exclude set-asides under other authorities from those requirements based on the value of the contract. 15 U.S.C. 657s. The only set-aside

authority that is not cited in the limitations on subcontracting provision is Section 15(j) of the Small Business Act, which is the statutory authority for small business set-asides valued between \$3,500 and \$150,000. SBA is adopting the proposed language of § 125.6(j), in redesignated § 125.6(f), as the majority of comments supported this approach and it is supported by the Small Business Act and consistent with the existing FAR.

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

SBA received twenty-nine comments related to proposed § 125.6(k). Twenty-eight of these comments requested that SBA alter this paragraph to lower the penalties and allow a good faith exception for a violation of the limitations on subcontracting. Most of these commenters were concerned that by violating the limitations on subcontracting by even \$1, possibly due to a miscalculation or a change in the Service Contract Act wage rates, a prime contractor could be exposed to a minimum fine of \$500,000. Many commenters requested that SBA change the language from imposing a minimum fine of \$500,000 to imposing a fine that is the lesser of \$500,000 or the amount spent in excess of the permitted levels. Several commenters requested that the fine be imposed on the subcontractor that is not qualified to receive the funds, as it is likely that the prime contractor relied in good faith on a misrepresentation of the subcontractor’s small business or small business program participation status. Other commenters requested that SBA allow a contractor that has violated the limitations on subcontracting to submit a mitigation plan and provide the contracting officer with discretion to apply the penalty when appropriate and in an amount proportional to the severity of the violation. One commenter supported the penalty language as proposed.

In response to these comments, SBA notes that the language of proposed § 125.6(k) mirrors the language of Section 1652 of the NDAA. The penalty

provision is statutory and the use of the \$500,000 fine as the minimum amount to be applied is also statutory. SBA believes that the penalty provision will deter contractors from agreeing to comply with the limitations on subcontracting without a practical plan for compliance because it provides a strong enforcement mechanism. It is critical that firms that obtain set-aside and preferential contracts comply with applicable subcontracting limitations. The government's policy of promoting contracting opportunities for small and socioeconomically disadvantaged businesses is seriously undermined when firms pass on work in excess of applicable limitations to firms that are other than small or that are not disadvantaged. SBA is adopting the proposed language into redesignated § 125.6(h).

This rule also proposed to revise § 121.103(h)(4). Paragraph (h) discusses the circumstances under which SBA will find affiliation among joint venturers for size purposes. Paragraph (h)(4) addresses the ostensible subcontractor rule, which is the concept that a subcontractor who performs the majority of the primary and vital requirements of a contract or whom the prime contractor is unusually reliant upon may be considered a joint venturer with the prime contractor and thus affiliated with the prime contractor for size determination purposes. SBA proposed to revise this paragraph to exclude subcontractors that are similarly situated subcontractors, as that term is defined in 13 CFR 125.1, from affiliation under the ostensible subcontractor rule. Such a position clearly flows from the NDAA's treatment of similarly situated subcontractors.

SBA received eleven comments in response to proposed § 121.103(h)(4). All eleven comments supported the exclusion of similarly situated entity subcontractors from the application of the ostensible subcontractor rule, as discussed in § 121.103(h)(4). As such, SBA is adopting the language in § 121.103(h)(4) as proposed.

SBA proposed to amend § 124.510(a), (b), and (c) to reflect the limitations on subcontracting rules with respect to the 8(a) Business Development (BD) program. Part 124 addresses the 8(a) BD program and the limitations on subcontracting that apply to procurements set aside for competition among 8(a) BD participants. SBA proposed to delete paragraphs (a) and (b) and add new paragraph (a). Currently, paragraphs (a) and (b) discuss how 8(a) BD participants can comply with the performance of work

requirements even though these specifications are also discussed in § 125.6. To eliminate confusion and repetition, SBA proposed to remove current paragraph (b) and add a new paragraph (a), which will direct 8(a) BD participants to comply with the limitations on subcontracting set forth in § 125.6. The proposed rule would redesignate current paragraph (c) as paragraph (b) and include references to the limitations on subcontracting as opposed to the performance of work requirements in newly redesignated paragraph (b). The NDAA uses the term "limitations on subcontracting" to describe the concept that is currently referred to as "performance of work requirements." This change provides consistency throughout the rules.

SBA received seventeen comments in response to the proposed language in § 124.510. Ten of these commenters opposed the proposed language and specifically disagreed with providing contracting officers the discretion to apply the limitations on subcontracting to 8(a) contracts per order. Commenters also opposed SBA's proposed § 124.510(b)(2), which allows the SBA District Director the ability to waive the applicable limitations on subcontracting in certain circumstances. Three of the comments received were suggestions to modify the language of proposed § 124.510(b) to clarify that subcontracts awarded to similarly situated entities for an 8(a) procurement are not counted toward that 8(a) prime contractor's limitations on subcontracting but are counted toward their non-8(a) revenue for purposes of meeting their business activity targets. Two commenters supported the language of § 124.510(b) as proposed.

For purposes of counting 8(a) revenue, the dollar amount of a prime contract award is credited towards the revenue of the prime contractor. Thus, to the extent an 8(a) prime decides to utilize a subcontractor for purposes of meeting the limitations on subcontracting provisions, any amount subcontracted is not deducted from the prime's 8(a) revenue. SBA notes that the language in § 124.510(b) is not new, and as such, no changes to this language were proposed. Nonetheless, several commenters expressed their opposition to a District Director's ability to waive compliance with the limitations on subcontracting in certain circumstances and disagreed with the time period used to determine compliance with the limitations on subcontracting for 8(a) procurements. In response to these comments, SBA is eliminating this provision. SBA has not received any comments or input indicating this

provision has benefited specific 8(a) concerns. In addition, this exemption is not based on any statutory authority. Thus, in accordance with the intent of the section to make the performance requirements uniform across all programs, SBA is eliminating paragraphs (c)(4) and (c)(5) of § 124.510.

SBA proposed to revise § 125.15(a)(3) and (b)(3), which address the requirements for an SDVO SBC to submit an offer on a contract. SBA proposed to revise paragraph (a)(3) to state that a concern that represents itself as an SDVO SBC must also represent that it will comply with the limitations on subcontracting, as set forth in § 125.6, as part of its initial offer, including price. SBA proposed to revise paragraph (b)(3) to state that joint ventures that represent themselves as an SDVO SBC joint venture must comply with the applicable limitations on subcontracting, as set forth in § 125.6. SBA received no comments related to these paragraphs and as such is adopting the language as proposed.

#### **HUBZone Program**

SBA also proposed to revise § 126.200(b)(6). This paragraph addresses the requirements that a concern must meet in order to receive SBA's certification as a qualified HUBZone SBC. Paragraphs (b)(6) and (d) are repetitive as both address the requirement that HUBZone SBCs must comply with the relevant performance of work requirements. SBA proposed to delete paragraph (d) and revise paragraph (b)(6). Specifically, proposed paragraph (b)(6) would state that the concern must represent in its application for the HUBZone program that it will comply with the applicable limitations on subcontracting requirements with respect to any procurement that it receives as a qualified HUBZone SBC. SBA received one comment related to proposed § 126.200(b)(6), which was a request to clarify whether a HUBZone similarly situated entity subcontractor must meet the 35% residency requirement for HUBZone program participation. In response, SBA clarifies that a HUBZone similarly situated entity subcontractor must be able to qualify for the prime HUBZone procurement in order to be considered a similarly situated entity. This means that it must also be HUBZone certified and be considered small for the NAICS code assigned to its subcontract. SBA is adopting the language in § 126.200(b)(6) as proposed.

SBA proposed to revise § 126.700 in its entirety, including revision of paragraph (a) and removal of paragraphs (b) and (c). This section currently



addresses the performance of work requirements for HUBZone contracts. SBA proposed to retitle the section to include the terminology “limitations on subcontracting”; remove references to the “performance of work” requirements; and replace the deleted text with a reference to 13 CFR 125.6 for guidance on the applicable limitations on subcontracting for HUBZone contracts. SBA believes that it would be confusing to have each section of SBA’s set-aside program regulations repeat the relevant limitations on subcontracting, and therefore SBA proposed to list all of the limitations on subcontracting requirements at § 125.6 and provide references to that section in each of the various small business government contracting and business development program sections. SBA did not receive comments related to this paragraph and is adopting the language as proposed.

SBA proposed to revise § 127.504(b), which addresses the requirements a concern must satisfy to submit an offer for an EDWOSB or WOSB requirement. Paragraph (b) states that the concern must meet the performance of work requirements in § 125.6. SBA proposed to revise this paragraph to replace the reference to “performance of work requirement” with “limitations on subcontracting.” SBA did not receive comments related to this paragraph and is adopting the language as proposed.

SBA proposed to revise § 127.506(d), which addresses the requirements that a joint venture must satisfy in order to submit an offer for an EDWOSB or WOSB requirement. SBA proposed to revise this paragraph by replacing the reference to “performance of work requirement” with “limitations on subcontracting.” SBA did not receive comments related to this paragraph and is adopting the language as proposed.

### Subcontracting Plans

Section 1653 of the NDAA, as codified at 15 U.S.C. 637(d) (Section 8(d) of the Small Business Act), addresses amendments to the requirements for subcontracting plans. Section 1653(a)(2) of the NDAA states that the head of the contracting agency shall ensure that the agency collects, reports, and reviews data on the extent to which the agency’s contractors meet the goals and objectives set out in their subcontracting plans. SBA proposed to add a new § 125.3(f)(8) to incorporate these provisions. SBA received three comments on this addition. Two were positive, and the one negative comment felt that the statutory language may be too burdensome for contracting officers and prime contractors. This final rule adopts the proposed language.

Section 1653(a)(3) of the NDAA modifies the Small Business Act to state that a contractor that fails to provide a written corrective action plan after receiving a marginal or unsatisfactory rating for its subcontracting plan performance or that fails to make a good faith effort to comply with its subcontracting plan will not only be in material breach of the contract, but such failure shall also be considered in any past performance evaluation of the contractor. SBA proposed to revise § 125.3(f)(5) to incorporate this language. SBA also proposed adding a new sentence to the end of § 125.3(f)(5), which would prescribe the process for a Commercial Market Representative (CMR) to report firms that are found to have acted fraudulently or in bad faith to the SBA’s Area Director for the Office of Government Contracting Area Office where the firm is headquartered. SBA received eight comments on this proposed change. One of the comments wanted SBA to ensure that there was a definitive statement that contracting officers shall take into consideration ratings on performance of past subcontracting plans when evaluating past performance. SBA agrees with this position, but believes that it is already clear in the regulatory text. The provisions of the NDAA make clear that contracting officers shall take into consideration previous performance of its subcontracting plans. The remaining comments were generally supportive of the changes. Two negative comments were related to requirements of the Act itself which can be modified or changed only by another Act passed of Congress. Thus, SBA is not making any changes to the proposed rule.

Section 1653(a)(4) of the NDAA modifies the Small Business Act to state that contracting agencies also perform evaluations of a prime contractor’s subcontracting plan performance, and that SBA’s evaluations of subcontracting plan performance are completed as a supplement to the contracting agency’s review. SBA proposed to revise § 125.3(f)(1) to incorporate this language. SBA did not receive any comments on this change and will be keeping the proposed language.

Section 1653(a)(5) of the NDAA requires that if an SBC is identified as a potential subcontractor in a proposal, offer, bid or subcontracting plan in connection with a covered Federal contract, the prime contractor shall notify the SBC prior to such identification. Section 1653(a)(5) also requires that the Administrator establish a reporting mechanism that allows potential subcontractors to report fraudulent activity or bad faith behavior

by a prime contractor with respect to a subcontracting plan. SBA proposed to incorporate these requirements in new § 125.3(c)(8) and (9). SBA received eight comments on these changes. Several comments asked for clarification on how the notification requirements can be met. SBA believes that rule is very clear. There are two requirements: First that the notification is in writing; and second that it be given to the party in question. Ensuring that it is in writing and has been received is the responsibility of the contractor. SBA is not making any changes with regard to this requirement. Several commenters requested that additional requirements be added that would also require notification to SBA or another government party that the contract has provided the written notification that is required. SBA does not believe that this additional step is required by the statute, or that the additional burden on contractors is necessary to ensure compliance with the other provision.

### Affiliation

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

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

SBA received several comments with respect to identity of interest based on family relationships. Four commenters thought that the list of family relationships was not exhaustive enough and should include all relationships, such as grandparents and

cousins. These commenters believed that all familial relationships should create the presumption, and that other information such as estrangement or distance could be used in rebuttal. Two commenters agreed that the clarity SBA was providing was helpful and agreed with the changes. Two commenters did not believe that affiliation should ever be found based on familial relationships.

As noted in SBA's proposed rule, the enumerated family relationships are relationships in which SBA's Office of Hearings and Appeals (OHA) has consistently found affiliation in the past. See *Size Appeal of Knight Networking & Web Design, Inc.*, SBA No. SIZ-5561 (2014); *Size Appeal of RGB Group, Inc.*, SBA No. SIZ-5351 (2012); and *Size Appeal of Jenn-Kans, Inc.*, SBA No. SIZ-5114 (2010). The rule is intended to take this knowledge and precedent and provide it in the rule itself in order to make compliance and understanding easier for small businesses. SBA believes the proposed rule accurately encompassed the precedential history of SBA size decisions and that it will be beneficial in providing some clarity to small businesses. Thus, SBA is adopting the language in (f)(1) in the final rule.

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

SBA received 26 comments on this section. Several commenters pointed out that SBA should use a three-year time frame rather than a one year time frame because SBA already uses a three-year time frame when averaging annual receipts for size purposes. SBA agrees, and has adopted a three-year measuring

period in the final rule. Several commenters were also concerned that this new rule and its interpretation could adversely impact "start-ups" that have low revenues to begin with and fewer contracts. SBA does not want this new rule to negatively impact start-ups or any other company that operates in a unique industry. That is precisely why this is not a bright line rule, but a rebuttable presumption. This rebuttable presumption is based on OHA cases, and OHA has in fact rebutted the presumption in appropriate circumstances. For instance, OHA has held that the mechanical application of the economic dependence rule is erroneous when a startup has only been able to secure one or two contracts. *Size Appeal of Argus & Black, Inc.*, SBA No. SIZ-5204 (2011). In addition, OHA has held that where the receipts from an alleged affiliate are not enough to sustain a firm's business operations, and the firm is able to look to other financial support from its Alaska Native Corporation (ANC) affiliates to remain viable, the fact that the firm received more than 70% of its receipts from its alleged affiliate is not sufficient to establish affiliation. *Size Appeal of Olgoonik Solutions LLC*, SBA No SIZ-5669 (2015). In response to the comments and in an effort to provide greater clarity, this final rule specifies that the presumption of affiliation based on economic dependence may be rebutted by a showing that despite the contractual relations with another concern, the concern at issue is not solely dependent on that other concern. In addition, SBA has provided examples in the regulatory text for clarification. Several comments asked for a specific list of acceptable rebuttals, and one commenter requested that Tribally-owned firms be granted an explicit exception. SBA does not believe that providing a list of acceptable rebuttals may have the unintended consequence of limiting the types of rebuttals that are acceptable. Instead SBA believes that firms should be permitted to make any arguments and provide any evidence that they believe demonstrates that no affiliation should be found. In addition, SBA has clarified that SBA will not find affiliation between two concerns owned by an Indian Tribe, ANC, Native Hawaiian Organization (NHO) or Community Development Corporation (CDC) based solely on the contractual relations of the two concerns. The Small Business Act and SBA's rules clearly recognize that ANC, NHO, CDC, and Tribally-owned concerns will provide assistance to sister entities, and it does not make sense to find affiliation based

on economic dependence among such concerns.

### Joint Ventures

SBA proposed to amend § 121.103(h) to broaden the exclusion from affiliation for small business size status to allow two or more small businesses to joint venture for any procurement without being affiliated with regard to the performance of that procurement requirement. Currently, in addition to the exclusion from affiliation given to an 8(a) protégé firm that joint ventures with its SBA-approved mentor for any small business procurement, there is also an exclusion from affiliation between two or more small businesses that seek to perform a small business procurement as a joint venture where the procurement is bundled or large (*i.e.*, greater than half the size standard for a procurement assigned a NAICS code with a receipts-based size standard and greater than \$10 million for a procurement assigned a NAICS code with an employee-based size standard). SBA proposed to remove the restriction on the type of contract for which small businesses may joint venture without being affiliated for size determination purposes. SBA proposed this change for several reasons. First, the proposed change would encourage more small business joint venturing, in furtherance of the government-wide goals for small business participation in federal contracting. Second, the proposed change is consistent with the results from the Small Business Teaming Pilot Program indicating there is a need for more small business opportunities and firms have greater success on small contracts than on large contracts. Third, this proposed change would better align with the new provisions of the NDAA governing the limitations on subcontracting, which allow a small business prime contractor to subcontract to as many similarly situated subcontractors as desired. If a small business prime contractor can subcontract significant portions of that contract to one or more other small businesses and, in doing so, meet the performance of work requirements for small business (without being affiliated with the small business subcontractor(s)), it is SBA's view that similar treatment should be afforded joint ventures—so that a joint venture of two or more small businesses could perform a procurement requirement as a small business when each is individually small.

SBA received 43 comments on this section. The comments were overwhelmingly supportive of the change. As such, this final rule adopts

the proposed language requiring only that each member of a joint venture individually qualify as small. Several commenters also suggested that SBA provide additional guidance regarding joint ventures that perform contracts as similarly situated entities. This final rule clarifies that a joint venture of two or more business concerns may submit an offer as a small business for a Federal procurement, subcontract or sale so long as each concern is small under the size standard corresponding to the NAICS code assigned to the contract.

#### Calculation of Annual Receipts

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

SBA received 15 comments on this section. The majority of the comments were supportive. Several commenters believed that SBA should not count certain expenses to subcontractors as revenue. The comments were asking SBA to consider new exemptions. The proposed change was not intended to fundamentally change the meaning of SBA's regulation, but merely ensure that small businesses are aware that all income is considered including passive income. Thus, SBA is adopting the proposed language in this final rule.

#### Recertification

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

SBA received twenty-one comments on this proposed change. Nine commenters supported SBA's proposal. One commenter asked that SBA go further and specifically allow contracting officers to refuse novation of contracts if an acquisition or merger occurs within 90 days of an award. Seven commenters strongly opposed

SBA's proposed changes. Two commenters argued that there should be a 30 day period prior to award requirement. SBA does not know how this could be implemented given that offerors do not know when an award announcement will be made. One commenter suggested SBA should only require recertification if the merger or sale involves a large business. One commenter was confused about whether this rule would negate the requirement to certify at the time at offer.

SBA is adopting the proposed language in this final rule. For several years SBA's rules have required recertification in connection with a contract when there is an acquisition or merger involving the prime contractor. SBA never intended for the recertification requirement to not apply based on when the acquisition or merger occurred. If recertification is required for an existing contract, it should be required for a pending contract. An agency's receipt of small business credit should not depend on whether an acquisition or merger occurs the day before award of contract.

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

SBA proposed to amend § 121.702(a)(2), which addresses an ownership and control element of the eligibility requirements for the Small Business Innovation and Research (SBIR) Program, to clarify that a single venture capital operating company (VCOC), hedge fund, or private equity firm may own more than 50% of an SBIR awardee if that single VCOC, hedge fund, or private equity firm qualifies as a small business concern which is more than 50% directly owned and controlled by individuals who are citizens or permanent resident aliens of the United States.

Section 121.702(a) establishes the SBIR program eligibility requirements related to ownership and control. Awardees that satisfy any of the permissible ownership and control structures discussed in § 121.702(a) must also satisfy all of the size and affiliation requirements stated in § 121.702(c). Section 121.702(a)(1)(ii) allows an SBIR awardee to be majority-owned by multiple VCOCs, hedge funds, or private equity firms. Section 121.702(a)(2) prohibits ownership by a single VCOC, hedge fund, or private equity firm that owns a majority of the concern. This paragraph has been misread because it does not account for the scenario where an awardee is majority-owned by a single VCOC, hedge fund, or private equity firm that

is itself another small business concern and therefore qualifies as an allowable ownership structure under § 121.702(a)(1)(i). To clarify this point, SBA is amending § 121.702(a)(2) to explain that it is permissible for an SBIR awardee to be majority owned by a single VCOC, hedge fund, or private equity firm if that firm meets the definition of a small business concern under this section and is more than 50% directly owned and controlled by individuals who are citizens or permanent resident aliens of the United States. SBA did not receive any comments related to this proposed change and is adopting the change as proposed.

#### Size Protests

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

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

SBA received 16 comments on this change. All commenters were supportive; however one commenter believed that the protests should be allowed for firms outside the competitive range. SBA disagrees. A firm outside of the competitive range is not eligible for award and does not have standing. However, SBA and the contracting officer may file a size protest at any time, so any firm, including those that do not have standing, may bring information pertaining to the size of the apparent successful offeror to the attention of SBA and/or the contracting officer for their consideration.

#### North American Industry Classification System Code Appeals

SBA sought comments on the appropriate timeline for filing a NAICS code appeal. SBA's regulations

currently state that, “[a]n appeal from a contracting officer’s NAICS code or size standard designation must be served and filed within 10 calendar days after the issuance of the solicitation or amendment affecting the NAICS code or size standard.” 13 CFR 121.1103(b)(1). SBA received 23 comments on this issue. Most of the comments were supportive of SBA’s current timing. Several commenters recommended other changes that SBA could make. Based on the comments, SBA is not altering the timeliness rules for NAICS code appeals.

#### Nonmanufacturer Rule

SBA proposed to clarify that the limitations on subcontracting and the nonmanufacturer rule (NMR) do not apply to small business set-aside contracts valued between \$3,000 and \$150,000. The statutory nonmanufacturer rule, which is contained in Section 8(a)(17) of the Small Business Act, 15 U.S.C. 637(a)(17), is an exception to the limitations on subcontracting (LOS). It provides that a concern may not be denied the opportunity to compete for a supply contract under Sections 8(a) and 15(a) of the Small Business Act simply because it is not the actual manufacturer or processor of the product. Section 8(a)(17) of the Small Business Act does not, however, also reference Section 15(j) of the Small Business Act, the authority requiring small business set-aside contracts valued between \$3,500 and \$150,000. Thus, there is no specific statutory requirement that the nonmanufacturer rule apply to the mandated small business set-asides between \$3,500 and \$150,000. SBA believes that not applying the nonmanufacturer rule to small business set-asides valued between \$3,500 and \$150,000 will spur small business competition by making it more likely that a contracting officer will set aside an acquisition for small business concerns because the agency will not have to request a waiver from SBA where there are no small business manufacturers available. In order to request a waiver, an agency must provide SBA with the solicitation and market research on whether manufacturers exist and wait several weeks for SBA to verify the data and grant the waiver. Without a waiver, an offeror on a small business set-aside supply contract must either manufacture at least 50% of the product on its own or supply the product of a small business made in the United States. Many waiver requests below \$150,000 are for name brand items (e.g., computers) that are clearly not made by

small businesses in the United States. Whether an agency can procure name brand items is not within the jurisdiction of SBA. The contracting officer must make that determination, which can be protested by interested parties.

SBA received 28 comments on this issue, of which 19 were supportive. The non-supportive comments believed that this change would drastically hurt small business manufacturers because most of their contracts fell within the exemption range. One commenter maintained that the proposed rule would hurt resellers by increasing competition among resellers. Given the support for the change and the consistency between the FAR and SBA’s regulations that this creates, SBA is adopting the proposed language in the final rule.

Several commenters asked for additional clarity on several discrete issues. Specifically, commenters sought guidance on how the NMR applies to multiple item procurements generally, and especially to procurements with multiple NAICS codes, and how the NMR and LOS apply when a multiple-item procurement contains items manufactured by multiple large and small businesses.

Further, commenters requested guidance on the treatment of rentals with regard to the NMR and LOS. In order to provide more clarity SBA is proposing new language in § 121.406(b)(4) and (e). SBA has also provided several additional examples to demonstrate how the rules should be applied. The final rule clarifies that rental services are not supplies. SBA bases this clarification on the NAICS code and NAICS manual, as well as the FAR and other government contracting statutes which indicate that renting an item is not the same thing as buying an item. SBA is also adding additional language to clarify how to apply the NMR, LOS, and size standards, to address comments concerning how to apply the various rules when the government acquires more than one item in a single procurement. SBA believes this language will more clearly state how the various regulations interact in that situation.

The intent is for the NMR, LOS, and size standards to operate in conjunction with each other in a manner consistent with all of SBA’s regulations. Therefore SBA believes that the proper way to calculate LOS requirements with regard to a contract that contains waived item(s)/small business item(s) is that the value of the waived item(s) are subtracted from the total and the prime contractor is responsible for meeting the requirements on the remainder. SBA has

added several examples to § 125.6(a) to help explain how this should be calculated in practice.

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

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

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

SBA received 32 comments on the changes being made to NMR waivers. Many commenters supported the proposed language regarding notification by the contracting officer. Commenters universally agreed that being informed of the application of a

waiver as early as possible would be beneficial to small business contractors. Several comments requested additional guidance or a firmer statement about the application of waivers granted on base contract to orders issued against that contract. Contract specific waivers are granted for individual items and the waiver is good for the entirety of that contract with regard to the item that was waived. Therefore, the waiver would by necessity also include all orders for supplies under that contract that would require the item(s) that had been waived.

SBA proposed to add a new § 121.1203(d), dealing with waivers to the nonmanufacturer rule for the purchase of software. SBA proposed to address whether the nonmanufacturer rule should apply to certain software that can readily be treated as an item and not a service. SBA proposed to treat this type of software as a product or item of supply rather than a service. SBA believed that this change will bring SBA's regulations in line with how most buyers already perceive these types of software. Readily available software that is generally available to both the public and private sector unmodified is almost universally perceived to be a supply item, even though SBA's regulations currently would treat the production of any type of software as a service. SBA proposed to allow for certain types of software to be eligible for waivers of the nonmanufacturer rule. SBA proposed to grant waivers on software that meet criteria that establishes that the Government is buying something that is more like a product or supply item than a service. Clearly, when the Government seeks to award a contract to a business concern to create, design, customize or modify custom software, that should be classified as a service requirement and the activity will remain classified in a service NAICS code to which the nonmanufacturer rule does not apply. For a service procurement set aside for small business, the prime (together with one or more similarly situated subcontractors) would have to perform the required percentage of work. On the other hand, when the government buys certain types of unmodified software that is generally available to both the public and the government from a business concern, SBA believes that the contracting officer should classify the requirement as a commodity or supply. If the procurement is a supply contract set aside for small business, the prime contractor, together with any similarly situated subcontractors, would have to perform at least 50% of the cost of manufacturing the software, unless SBA

granted a waiver of the nonmanufacturer rule.

Commenters generally supported SBA's proposed language. One commenter stated that given this new approach by SBA, that some software products should be granted class waivers. Once this rule is effective, the public will be able to request a class waiver for a software item under SBA's existing regulations for class waivers. 13 CFR 121.1204. Many commenters requested drastic changes to SBA's current waiver procedures. Specifically, the commenters requested that a waiver requested by CO be assumed granted if SBA does not respond in specified period of time. Two commenters requested language that would allow bidders to assume pending waiver requests are granted when they submit offers. SBA cannot adopt these recommendations. The Small Business Act is clear that only SBA may grant a waiver of the NMR. These comments reinforce SBA's belief that the current situation has caused too much confusion for small contractors, and SBA is adopting the proposed language in this final rule, which requires the contracting officer to request a contract specific waiver prior to issuing the solicitation, and provide notification of the application of the waiver in the solicitation itself.

One commenter complained that the application of the software waiver is not also being applied to cloud based solutions. It is SBA's current position that cloud based solutions are services that are being provided to the government and not supplies that the government is purchasing, and therefore the NMR is not applicable. In our view, cloud based solutions are similar to rentals, which, as discussed above, SBA treats as services. Several commenters asked SBA to address the issue of NMR waiver requests when the issue is contractor requesting a brand name item. The decision to request a brand name item is in the discretion of the contracting officer. However, the Small Business Act does not exclude brand name item acquisitions from the statutory NMR waiver requirements.

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

This industry comprises establishments primarily engaged in computer software publishing or publishing and reproduction. Establishments in this industry carry out

operations necessary for producing and distributing computer software, such as designing, providing documentation, assisting in installation, and providing support services to software purchasers. These establishments may design, develop, and publish, or publish only.

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

SBA proposed to amend § 121.406(b)(5) to make a technical correction. Section 121.406(b) addresses how a nonmanufacturer may qualify as a small business concern for a requirement to provide a manufactured product or other supply item. Currently, paragraph (b)(5) states that the SBA's Administrator or designee may waive the requirement set forth in paragraph (b)(1)(iii) of this section, that requires nonmanufacturers to supply the end item of a small business manufacturer, processor or producer made in the United States. The citation to paragraph (b)(1)(iii) is incorrect and as such, SBA proposed to amend this paragraph to include the correct citation, paragraph (b)(1)(iv). SBA also proposed to make this correction in the size standard proposed rule for industries with employee based size standards that are not part of manufacturing, wholesale trade or retail trade. 79 FR 53646 (Sept. 10, 2014). The size standard rule was finalized on January 26, 2016 (81 FR 4436), and SBA has removed the proposed amendment from this final rule.

In addition, in the proposed rule SBA proposed to amend § 121.406(b)(7) to clarify that SBA's waiver of the NMR has no effect on requirements external to the Small Business Act which involve domestic sources of supply, such as the Buy American Act and the Trade Agreements Act.

In order to clarify whether the NMR applies, or whether a general or specific waiver is attached to a procurement, SBA proposed to add a new § 121.1206

to require contracting officers to receive specific waivers prior to posting a solicitation, and also to provide notification to all potential offerors of any waivers that will be applied (whether class or specific) to a given solicitation. As noted above, commenters were generally in favor of this provision, and SBA is adopting the proposed language in the final rule.

#### **Adverse Impact and Construction Requirements**

SBA proposed to amend § 124.504 to clarify when a procurement for construction services is considered a new requirement. This section generally addresses when SBA must conduct an adverse impact analysis for the award of an 8(a) contract. SBA is not required to perform an adverse impact analysis for new requirements. Currently, paragraph (c)(1)(ii)(B) states that “Construction contracts, by their very nature (e.g., the building of a specific structure), are deemed new requirements.” SBA proposed to clarify the definition of “new requirement” for construction contracts by specifying that generally, the building of a specific structure is considered a new requirement. However, recurring indefinite delivery or indefinite quantity (IDIQ) procurements for construction services are not considered new. SBA has found that agencies have misinterpreted the current language of § 124.504(c)(1)(ii)(B) to consider recurring IDIQ construction services procurements as new. SBA intended to clarify that such recurring requirements are not considered new. A determination of whether a construction contract is recurring or new will have to be made on a case by case basis, and there is a process in place that allows SBA to file an appeal with the procuring agency when there is a disagreement.

SBA received 11 comments on this proposed change, and most were supportive. The non-supportive comments seemed to have misunderstood how the rule will be implemented. There is no presumption that IDIQ task or delivery order contracts are not new. The rule is neutral and the determination will be made on a case-by-case basis, subject to SBA’s statutory authority to appeal. Thus, SBA is adopting the proposed language in the final rule.

#### **Certificate of Competency**

SBA proposed to amend § 125.5(f), which addresses SBA’s review of an application for the Certificate of Competency (COC) program. SBA proposed to insert new § 125.5(f)(3) to address how SBA should review an application for a COC based on a finding

of non-responsibility due to financial capacity where the applicant is the apparent successful offeror for an IDIQ task order or contract. SBA frequently receives inquiries regarding the application of the COC process for financial capacity to the potential award of an IDIQ contract. SBA intended to clarify this process by proposing changes to § 125.5(f). The proposed changes provided that the SBA’s Area Director will consider the firm’s maximum financial capacity and if such COC is issued, it will be for a specific amount that serves as the limit of the firm’s financial capacity for that contract. The contracting officer cannot deny the firm the award of an order or contract on the basis of financial incapacity if the firm has not reached the financial maximum identified by the Area Director.

SBA received two comments on this issue. One was supportive, and one thought it added too much of a burden to small businesses. SBA believes this rule will address certain issues that arise for IDIQ contracts. This rule provides clarity to the process and ensures that small business participation is maximized. Further, the COC process is statutory and provides SBA with the ability to review non-responsibility determinations concerning small businesses. Thus, SBA is adopting the proposed language in the final rule.

SBA is also revising 13 CFR 121.408(a), which provides the size procedures for the COC program. The revision is a technical correction. This paragraph currently references 13 CFR 121.1009 to explain how SBA would initiate a formal size determination; however, § 121.1009 relates to the process SBA uses to make a formal size determination. The correct regulatory reference is to 13 CFR 121.1001(b)(3)(ii), which explains how SBA initiates a formal size determination for the COC program.

SBA is also revising 13 CFR 121.409, to remove the second sentence. This section addresses the size standard that applies in an unrestricted or full and open procurement. The second sentence states that in an unrestricted procurement, the small business concern must supply a domestically furnished product. That may or may not be true, depending on whether or how the Buy American Act or the Trade Agreements Act apply to the procurement. The Small Business Act does not impose such a requirement on full and open or unrestricted procurements.

#### **Compliance With Executive Orders 12866, 13563, 13175, 12988, 13132, the Paperwork Reduction Act (44 U.S.C. Ch. 35), and the Regulatory Flexibility Act (5 U.S.C. 601–612) Executive Order 12866**

The Office of Management and Budget (OMB) has determined that this final rule is a “significant” regulatory action for purposes of Executive Order 12866. Accordingly, the next section contains SBA’s Regulatory Impact Analysis. However, this is not a major rule under the Congressional Review Act, 5 U.S.C. 801, *et seq.*

#### **Regulatory Impact Analysis**

##### *1. Is there a need for the regulatory action?*

The final rule implements Sections 1621, 1623, 1651, 1652, 1653 and 1654 of the National Defense Authorization Act of 2013, Public Law 112–239, 126 Stat. 1632, January 2, 2013; 15 U.S.C. 637(d), 644(l), 645, 657s. In addition, it makes several other changes needed to clarify ambiguities in or remedy perceived problems with the current regulations. These changes should make SBA’s regulations easier to use and understand.

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

These final regulations should benefit small business concerns by allowing small business concerns to use similarly situated subcontractors in the performance of a set-aside contract, thereby expanding the capacity of the small business prime contractor and potentially enabling the firm to compete for and obtain larger contracts. It also strengthens the small business subcontracting provisions, which may result in more subcontract awards to small business concerns. The final rule also seeks to address or clarify issues that are ambiguous or subject to dispute, thereby providing clarity to contracting officers as well as small business concerns. SBA does not believe that this rule will impose new costs on small business concerns.

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

Many provisions in this final rule are required to implement statutory provisions, thus there are no alternatives for these regulations. SBA did consider various options in the proposed rule, including a requirement that small business concerns that want to team with similarly situated entities enter into a written agreement, certify that they will comply and report on compliance. However, in response to

the public comments discussed in the **SUPPLEMENTARY INFORMATION**, SBA is not requiring a written agreement or compliance reporting in this rule. Contracting officers in their discretion may require compliance reporting. Further, firms agree to comply with the limitations on subcontracting when they submit an offer. Thus, an additional certification is unnecessary. SBA also considered whether it should not waive the NMR for the purchase of software. However, this would inhibit the ability of agencies to set aside contracts for commodity software for small business concerns.

#### **Executive Order 13563**

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

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

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

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

The proposed rule had a 60-day comment period and was posted on [www.regulations.gov](http://www.regulations.gov) to allow the public to comment meaningfully on its

provisions. In addition, the agency extended the comment period in response to public requests to do so. SBA then submitted the final rule to the Office of Management and Budget for interagency review. Further, as discussed in the **SUPPLEMENTARY INFORMATION**, SBA conducted tribal consultations where these rules were discussed.

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

Yes, the final rule implements statutory provisions and will provide clarification to rules that were requested by agencies and stakeholders. On many occasions, SBA made changes to language or provided additional examples, in response to public comment. The final rule will make it easier for small businesses to contract with the Federal government.

#### **Executive Order 12988**

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

#### **Executive Order 13132**

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

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

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

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

According to the Regulatory Flexibility Act (RFA), 5 U.S.C. 601, when an agency issues a rulemaking, it must prepare a regulatory flexibility analysis to address the impact of the rule on small entities. However, section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the rulemaking is not

expected to have a significant economic impact on a substantial number of small entities. The RFA defines “small entity” to include “small businesses,” “small organizations,” and “small governmental jurisdictions.” This final rule concerns various aspects of SBA’s contracting programs, as such the rule relates to small business concerns but would not affect “small organizations” or “small governmental jurisdictions” because those programs generally apply only to “business concerns” as defined by SBA’s regulations, in other words, to small businesses organized for profit. “Small organizations” or “small governmental jurisdictions” are non-profits or governmental entities and do not generally qualify as “business concerns” within the meaning of SBA’s regulations.

There are approximately 300,000 concerns listed as small business concerns in the System for Award Management (SAM) in at least one industry category that could potentially be impacted by the implementation of the NDAA 2013 contracting provisions. However, we cannot say with any certainty how many will be impacted because we do not know how many of these concerns will team together to submit offers, nor do we know how many will be awarded contracts as teams. The number of firms participating in teaming will be lower than the number of firms registered in SAM. However, as discussed elsewhere in this rule, including section 2 of the Regulatory Impact Analysis, the final rule does not impose significant new compliance or other costs on small business concerns. Under current law, firms must adhere to certain performance requirements when performing set-aside contracts. SBA expects that costs now incurred by small business concerns as a result of ambiguous or indefinite regulations will be eliminated or reduced. Clarifying the confusion and uncertainty concerning the applicability of SBA’s contracting regulations would also reduce the time burden on the small business contracting community and therefore make it easier for them to contract with the Federal Government. In sum, the final rule would not have a separate impact on small businesses and would increase their opportunities to participate in Federal Government contracting without imposing any additional costs. For the reasons discussed, SBA certifies that this final rule would not have a significant economic impact on a substantial number of small business concerns.

List of Subjects

13 CFR Part 121

Administrative practice and procedure, Government procurement, Government property, Grant programs—business, Individuals with disabilities, Loan programs—business, Small businesses.

13 CFR Part 124

Administrative practice and procedure, Government procurement, Hawaiian Natives, Indians—business and finance, Minority businesses, Reporting and recordkeeping requirements, Technical assistance.

13 CFR Part 125

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

13 CFR Part 126

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

13 CFR Part 127

Government contracts, Reporting and recordkeeping requirements, Small businesses.

Accordingly, for the reasons stated in the preamble, SBA amends 13 CFR parts 121, 124, 125, 126, and 127 as follows:

PART 121—SMALL BUSINESS SIZE REGULATIONS

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

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

- 2. Amend § 121.103 by
■ a. Revising paragraph (b)(9);
■ b. Adding paragraphs (f)(1) and (2);
■ c. Adding a new final sentence to paragraph (h) introductory text; and
■ d. Revising paragraphs (h)(3)(i) and (h)(4) to read as follows:

§ 121.103 How does SBA determine affiliation?

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

(9) In the case of a solicitation for a bundled contract, a small business contractor may enter into a Small Business Teaming Arrangement with one or more small business subcontractors and submit an offer as a small business without regard to affiliation, so long as each team member is small for the size standard assigned to the contract or subcontract. The agency shall evaluate the offer in the

same manner as other offers with due consideration of the capabilities of the subcontractors.

\* \* \* \* \*
(f) \* \* \*

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

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

(i) This presumption may be rebutted by a showing that despite the contractual relations with another concern, the concern at issue is not solely dependent on that other concern, such as where the concern has been in business for a short amount of time and has only been able to secure a limited number of contracts.

(ii) A business concern owned and controlled by an Indian Tribe, ANC, NHO, CDC, or by a wholly-owned entity of an Indian Tribe, ANC, NHO, or CDC, is not considered to be affiliated with another concern owned by that entity based solely on the contractual relations between the two concerns.

Example 1 to paragraph (f). Firm A has been in business for 9 months and has two contracts. Contract 1 is with Firm B and is valued at \$900,000 and Contract 2 is with Firm C and is valued at \$200,000. Thus, Firm B accounts for over 70% of Firm A's receipts. Absent other connections between A and B, the presumption of affiliation between A and B is rebutted because A is a new firm.

Example 2 to paragraph (f). Firm A has been in business for five years. It has over 200 contracts. Of that 200, 195 are with Firm B, and the value of those contracts is greater than 70% of the revenue over the previous three years. In this case, SBA would most likely find the two firms affiliated unless the firm could provide some other compelling rebuttal to the very strong presumption that it should be considered affiliated with Firm B.

\* \* \* \* \*

(h) \* \* \* For purposes of this section, contract refers to prime contracts, and any subcontract in which the joint venture is treated as a similarly situated entity as the term is defined in part 125 of this chapter.

\* \* \*

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

\* \* \* \* \*

(4) A contractor and its ostensible subcontractor are treated as joint venturers, and therefore affiliates, for size determination purposes. An ostensible subcontractor is a subcontractor that is not a similarly situated entity, as that term is defined in § 125.1 of this chapter, and performs primary and vital requirements of a contract, or of an order, or is a subcontractor upon which the prime contractor is unusually reliant. All aspects of the relationship between the prime and subcontractor are considered, including, but not limited to, the terms of the proposal (such as contract management, technical responsibilities, and the percentage of subcontracted work), agreements between the prime and subcontractor (such as bonding assistance or the teaming agreement), and whether the subcontractor is the incumbent contractor and is ineligible to submit a proposal because it exceeds the applicable size standard for that solicitation.

\* \* \* \* \*

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

§ 121.104 How does SBA calculate annual receipts?

(a) Receipts means all revenue in whatever form received or accrued from whatever source, including from the sales of products or services, interest, dividends, rents, royalties, fees, or commissions, reduced by returns and allowances. Generally, receipts are considered "total income" (or in the case of a sole proprietorship "gross income") plus "cost of goods sold" as these terms are defined and reported on Internal Revenue Service (IRS) tax return forms (such as Form 1120 for corporations; Form 1120S and Schedule K for S corporations; Form 1120, Form 1065 or Form 1040 for LLCs; Form 1065 and Schedule K for partnerships; Form 1040, Schedule F for farms; Form 1040, Schedule C for other sole proprietorships). Receipts do not include net capital gains or losses; taxes collected for and remitted to a taxing authority if included in gross or total income, such as sales or other taxes collected from customers and excluding taxes levied on the concern or its



employees; proceeds from transactions between a concern and its domestic or foreign affiliates; and amounts collected for another by a travel agent, real estate agent, advertising agent, conference management service provider, freight forwarder or customs broker. For size determination purposes, the only exclusions from receipts are those specifically provided for in this paragraph. All other items, such as subcontractor costs, reimbursements for purchases a contractor makes at a customer's request, investment income, and employee-based costs such as payroll taxes, may not be excluded from receipts.

\* \* \* \* \*

■ 4. Amend § 121.201 by adding footnote 20 to read as follows:

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

\* \* \* \* \*

Footnotes

\* \* \* \* \*

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

**§ 121.402 [Amended]**

■ 5. Amend § 121.402(d) by removing the term “paragraph (d)” and adding in its place “paragraph (e)”.

■ 6. Amend § 121.404 as follows:

■ a. Revise paragraph (f);

■ b. Revise first sentence of paragraph (g)(2)(i); and

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

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

\* \* \* \* \*

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

(g) \* \* \*

(2)(i) In the case of a merger, sale, or acquisition, where contract novation is not required, the contractor must, within 30 days of the transaction becoming final, recertify its small business size status to the procuring agency, or inform the procuring agency that it is other than small. \* \* \*

(ii) \* \* \*

(D) If the merger, sale or acquisition occurs after offer but prior to award, the

offeror must recertify its size to the contracting officer prior to award.

\* \* \* \* \*

■ 7. Amend § 121.406 as follows:

■ a. Revise the section heading;

■ b. Revise paragraph (a) introductory text;

■ c. Add a sentence to the end of paragraph (b)(4);

■ d. Revise paragraphs (b)(7) and (d); and

■ e. Redesignate paragraph (e) as paragraph (f) and add new paragraph (e) to read as follows:

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

(a) *General.* In order to qualify as a small business concern for a small business set-aside, service-disabled veteran-owned small business set-aside or source contract, HUBZone set-aside or sole source contract, WOSB or EDWOSB set-aside or sole source contract, 8(a) set-aside or sole source contract, partial set-aside, or set aside of an order against a multiple award contract to provided manufactured products or other supply items, an offeror must either:

\* \* \* \* \*

(b) \* \* \*

(4) \* \* \* The rental of an item(s) is a service and should be treated as such in the application of the nonmanufacturer rule and the limitation on subcontracting.

\* \* \* \* \*

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

\* \* \* \* \*

(d) The performance requirements (limitations on subcontracting) and the nonmanufacturer rule do not apply to small business set-aside acquisitions with an estimated value between \$3,500 and \$150,000.

(e) *Multiple item acquisitions.* (1) If at least 50% of the estimated contract value is composed of items that are manufactured by small business concerns, then a waiver of the nonmanufacturer rule is not required. There is no requirement that each and every item acquired in a multiple-item

procurement be manufactured by a small business.

(2) If more than 50% of the estimated contract value is composed of items manufactured by other than small concerns, then a waiver is required. SBA may grant a contract specific waiver for one or more items in order to ensure that at least 50% of the value of the products to be supplied by the nonmanufacturer comes from domestic small business manufacturers or are subject to a waiver.

(3) If a small business is both a manufacturer of item(s) and a nonmanufacturer of other item(s), the manufacturer size standard should be applied.

\* \* \* \* \*

■ 8. Amend § 121.408 by revising paragraph (a) to read as follows:

**§ 121.408 What are the size procedures for SBA's Certificate of Competency Program?**

(a) A firm which applies for a COC must file an “Application for Small Business Size Determination” (SBA Form 355). If the initial review of SBA Form 355 indicates the applicant, including its affiliates, is small for purposes of the COC program, SBA will process the application for COC. If the review indicates the applicant, including its affiliates is other than small SBA will initiate a formal size determination as set forth in § 121.1001(b)(3)(ii). In such a case, SBA will not further process the COC application until a formal size determination is made.

\* \* \* \* \*

**§ 121.409 [Amended]**

■ 9. Amend § 121.409 by removing the second sentence.

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

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

\* \* \* \* \*

(a) \* \* \*

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

\* \* \* \* \*

■ 11. Amend § 121.1001 as follows:

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

■ b. Redesignate paragraph (b)(11) as paragraph (b)(12) and add a new paragraph (b)(11).

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

(a) \* \* \* (1) \* \* \* (i) Any offeror that the contracting officer has not eliminated from consideration for any procurement-related reason, such as non-responsiveness, technical unacceptability or outside of the competitive range;

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

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

■ 12. Revise § 121.1203 to read as follows:

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

(a) Where appropriate, SBA will generally grant waivers for an individual contract or order prior to the issuance of a solicitation, or, where a solicitation has been issued, when the contracting officer provides all potential offerors additional time to respond.

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

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

are met, SBA would grant the waiver, even though the contract has already been awarded.

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

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

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

(ii) Is sold in substantial quantities in the commercial marketplace; and

(iii) Is offered to the Government, without modification, in the same form in which it is sold in the commercial marketplace.

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

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

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

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

(b) \* \* \* (1) \* \* \* (ii) The proposed solicitation number, NAICS code, dollar amount of the procurement, and a brief statement of the procurement history;

(iii) A determination by the contracting officer that no small business manufacturer or processor reasonably can be expected to offer a product or products meeting the specifications (including period of performance) required by a particular solicitation. Include a narrative describing market research and supporting documentation; and

■ 14. Add § 121.1206 to read as follows:

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

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

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

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

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

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

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

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

(c) \* \* \* (1) \* \* \* (ii) \* \* \* (B) Procurements for construction services (e.g., the building of a specific structure) are generally deemed to be new requirements. However, recurring indefinite delivery or indefinite quantity task or delivery order construction services are not considered new (e.g., a recurring procurement requiring all construction work at base X).

■ 17. Revise § 124.510 to read as follows:

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

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

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

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

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

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

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

\* \* \* \* \*

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

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

\* \* \* \* \*

**PART 125—GOVERNMENT CONTRACTING PROGRAMS**

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

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

■ 20. Amend § 125.1 by:

■ a. Removing paragraphs (f), (g), (h), (m), and (u);

■ b. Removing all alphabetical paragraph designations and placing the definitions in alphabetical order;

■ c. Adding in alphabetical order a definition for *Similarly situated entity* to read as follows:

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

\* \* \* \* \*

*Similarly situated entity* is a subcontractor that has the same small business program status as the prime contractor. This means that: For a HUBZone requirement, a subcontractor that is a qualified HUBZone small business concern; for a small business set-aside, partial set-aside, or reserve a subcontractor that is a small business concern; for a SDVO small business requirement, a subcontractor that is a self-certified SDVO SBC; for an 8(a) requirement, a subcontractor that is an 8(a) certified Program Participant; for a WOSB or EDWOSB contract, a subcontractor that has complied with the requirements of part 127. In addition to sharing the same small business program status as the prime contractor, a similarly situated entity must also be small for the NAICS code that the prime contractor assigned to the subcontract the subcontractor will perform.

\* \* \* \* \*

■ 21. Amend § 125.2 as follows:

■ a. Revise paragraph (b)(1)(i)(A);

■ b. Add paragraph (b)(1)(i)(F);

■ c. Revise the introductory text to paragraph (b)(1)(ii);

■ d. Revise paragraph (b)(1)(iii)(C);

■ e. Add paragraphs (b)(1)(iv) and (v);

■ f. Remove paragraph (b)(2) and redesignate paragraph (b)(3) as paragraph (b)(2);

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

■ h. Amend paragraph (c)(1)(iv) by removing the term “and” at the end of the last sentence;

■ i. Amend paragraph (c)(1)(v) by removing the “.” at the end of the last sentence and adding in its place “;”.

■ j. Add paragraph (c)(1)(vi); and

■ k. Add paragraph (c)(1)(vii) to read as follows.

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

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(i) \* \* \*

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

\* \* \* \* \*

(F) PCRs also advocate competitive procedures and recommend the breakout for competition of items and requirements which previously have not been competed when appropriate. They may appeal the failure by the buying activity to act favorably on a recommendation in accord with the appeal procedures in paragraph (b)(2) of this section. PCRs also review restrictions and obstacles to competition and make recommendations for improvement.

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

believe a bundled or consolidated requirement is necessary or justified the PCR shall advocate against the consolidation or bundling of such requirement and recommend to the procuring activity alternative procurement methods which would increase small business prime contract participation. Such alternatives may include:

\* \* \* \* \*

(iii) \* \* \*

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

\* \* \* \* \*

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

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

(2) *Appeals of PCR recommendations.* In cases where there is disagreement between a PCR and the contracting officer over the suitability of a particular acquisition for a small business set-aside, partial set-aside or reserve, whether or not the acquisition is a bundled, substantially bundled or consolidated requirement, the PCR may initiate an appeal to the head of the contracting activity. If the head of the contracting activity agrees with the contracting officer, SBA may appeal the matter to the Secretary of the Department or head of the agency. The time limits for such appeals are set forth in FAR subpart 19.5 (48 CFR 19.5).

(c) \* \* \* (1) \* \* \*

(i) \* \* \*

(vi) Provide opportunities for the participation of small business concerns during acquisition planning processes and in acquisition plans; and

(vii) Invite the participation of the appropriate Director of Small and Disadvantaged Business Utilization in acquisition planning processes and provide that Director with access to acquisition plans.

\* \* \* \* \*

- 22. Amend § 125.3 as follows:
  - a. Add paragraphs (c)(8) and (9);
  - b. Revise the first sentence of paragraph (f)(1);
  - c. Revise paragraph (f)(5); and
  - d. Add paragraph (f)(8) to read as follows:

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

\* \* \* \* \*

(c) \* \* \*

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

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

\* \* \* \* \*

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

\* \* \* \* \*

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

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

(ii) Shall be in material breach of such contract or subcontract, and such failure to demonstrate good faith must be considered in any past performance evaluation of the contractor. This action shall be considered by the contracting officer upon receipt of a written recommendation to that effect from the CMR. The CMR's recommendation must include a copy of the compliance report and any other relevant correspondence or supporting documentation.

Furthermore, if the CMR has a reasonable basis to believe that a contractor has made a false statement to an employee or representative of the Federal Government, or to an employee or representative of the prime contractor, the CMR must report the

matter to the SBA Office of Inspector General. All other concerns as to whether a prime contractor or subcontractor has complied with SBA regulations or otherwise acted in bad faith may be reported to the Area Government Contracting Office where the firm is headquartered.

\* \* \* \* \*

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

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

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

\* \* \* \* \*

- 23. Amend § 125.5 as follows:
  - a. Revise paragraph (b)(1)(ii);
  - b. Remove paragraphs (b)(1)(iii), (iv) and (v); and
  - c. Add paragraph (f)(3) to read as follows:

**§ 125.5 What is the Certificate of Competency Program?**

\* \* \* \* \*

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

(ii) To be eligible for a COC, an offeror must qualify as a small business under the applicable size standard in accordance with part 121 of this chapter, and must have agreed to comply with the applicable limitations on subcontracting and the nonmanufacturer rule, where applicable.

\* \* \* \* \*

(f) \* \* \*

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

\* \* \* \* \*

- 24. Revise § 125.6 to read as follows:

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

(a) *General.* In order to be awarded a full or partial small business set-aside

contract with a value greater than \$150,000, an 8(a) contract, an SDVO SBC contract, a HUBZone contract, a WOSB or EDWOSB contract pursuant to part 127 of this chapter, with a value greater than \$150,000, a small business concern must agree that:

(1) In the case of a contract for services (except construction), it will not pay more than 50% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded.

(2)(i) In the case of a contract for supplies or products (other than from a nonmanufacturer of such supplies), it will not pay more than 50% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 50% subcontract amount that cannot be exceeded. Cost of materials are excluded and not considered to be subcontracted.

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

(A) For a multiple item procurement where a waiver as described in § 121.406(b)(5) of this chapter has not been granted for one or more items, more than 50% of the value of the products to be supplied by the nonmanufacturer must be the products of one or more domestic small business manufacturers or processors.

(B) For a multiple item procurement where a waiver as described in § 121.406(b)(5) of this chapter is granted for one or more items, compliance with the limitation on subcontracting requirement will not consider the value of items subject to a waiver. As such, more than 50% of the value of the products to be supplied by the nonmanufacturer that are not subject to a waiver must be the products of one or more domestic small business manufacturers or processors.

(C) For a multiple item procurement, the same small business concern may act as both a manufacturer and a nonmanufacturer.

*Example 1 to paragraph (a)(2).* A contract calls for the supply of one item valued at \$1,000,000. The market research shows that there are no small business manufacturers that produce this item, and the contracting officer seeks and is granted a contract specific waiver for this item. In this case, a

small business nonmanufacturer may supply an item manufactured by a large business.

*Example 2 to paragraph (a)(2).* A contract is for \$1,000,000 and calls for the acquisition of 10 items. Market research shows that nine of the items can be sourced from small business manufacturers and one item is subject to an SBA class waiver. The projected value of the item that is waived is \$10,000. Therefore, at least 50% of the value of the items not subject to a waiver, or 50% of \$990,000, must be supplied by one or more domestic small business manufacturers, and the prime small business nonmanufacturer may act as a manufacturer for one or more items.

*Example 3 to paragraph (a)(2).* A contract is for \$1,000,000 and calls for the acquisition of 10 items. Market research shows that only four of these items are manufactured by small businesses. The value of the items manufactured by small business is estimated to be \$400,000. The contracting officer seeks and is granted waivers on the other six items. Therefore, the value of the items granted waivers is excluded from the calculation and at least 50% of \$400,000 would have to be spent by the prime contractor on items it manufactures itself, or on items manufactured by one or more other small business concerns.

*Example 4 to paragraph (a)(2).* A contract is for \$1,000,000 and calls for the acquisition of 10 items. Market research shows that eight of the items can be sourced from small business manufacturers, and the estimated value of these items is \$800,000. At least 50% of the value of the contract (*i.e.*, at least \$500,000) will be spent on items manufactured by one or more small business concerns. As such, the contracting officer is not required to request contract specific waivers for the other two items valued at \$200,000. In this case, the prime contractor can meet the requirement by sourcing some of the items from small businesses manufacturers and some from large businesses without a waiver and still satisfy the requirement.

(3) In the case of a contract for general construction, it will not pay more than 85% of the amount paid by the government to it to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 85% subcontract amount that cannot be exceeded. Cost of materials are excluded and not considered to be subcontracted.

(4) In the case of a contract for special trade contractors, no more than 75% of the amount paid by the government to the prime may be paid to firms that are not similarly situated. Any work that a similarly situated subcontractor further subcontracts will count towards the 75% subcontract amount that cannot be exceeded. Cost of materials are excluded and not considered to be subcontracted.

(b) *Mixed contracts.* Where a contract combines services and supplies, the contracting officer shall select the appropriate NAICS code as prescribed

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

*Example 1 to paragraph (b).* A procuring agency is acquiring both services and supplies through a small business set-aside. The total value of the requirement is \$3,000,000, with the supply portion comprising \$2,500,000, and the services portion comprising \$500,000. The contracting officer appropriately assigns a manufacturing NAICS code to the requirement. The cost of material is \$500,000. Thus, because the services portion of the contract and the cost of materials are excluded from consideration, the relevant amount for purposes of calculating the performance of work requirement is \$2,000,000 and the prime and/or similarly situated entities must perform at least \$1,000,000 and the prime contractor may not subcontract more than \$1,000,000 to non-similarly situated entities.

*Example 2 to paragraph (b).* A procuring agency is acquiring both services and supplies through a small business set-aside. The total value of the requirement is \$3,000,000, with the services portion comprising \$2,500,000, and the supply portion comprising \$500,000. The contracting officer appropriately assigns a services NAICS code to the requirement. Thus, because the supply portion of the contract is excluded from consideration, the relevant amount for purposes of calculating the performance of work requirement is \$2,500,000 and the prime and/or similarly situated entities must perform at least \$1,250,000 and the prime contractor may not subcontract more than \$1,250,000 to non-similarly situated entities.

(c) *Subcontracts to similarly situated entities.* A small business concern prime contractor that receives a contract listed in paragraph (a) of this section and spends contract amounts on a subcontractor that is a similarly situated entity shall not consider those subcontracted amounts as subcontracted for purposes of determining whether the small business concern prime contractor has violated paragraph (a) of this section, to the extent the subcontractor performs the work with its own employees. Any work that the similarly situated subcontractor does not perform with its own employees shall be considered subcontracted SBA will also exclude a subcontract to a similarly situated entity from consideration under the ostensible subcontractor rule (§ 121.103(h)(4)).

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

*Example 2 to paragraph (c):* A competitive 8(a) BD contract is awarded in the total amount of \$10,000,000 for janitorial services. The prime contractor subcontracts \$8,000,000 of the janitorial services to another 8(a) BD certified firm. The prime contractor does not violate the limitation on subcontracting for services because the amount subcontracted to a similarly situated entity is excluded from the limitation on subcontracting.

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

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

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

(1) The contracting officer, in his or her discretion, may require the concern to comply with the applicable limitations on subcontracting and the nonmanufacturer rule for each order awarded under a total or partial set-aside contract.

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

(3) Work performed by an independent contractor shall be considered a subcontract, and may count toward meeting the applicable limitation on subcontracting where the independent contractor qualifies as a similarly situated entity.

(f) *Inapplicability of limitations on subcontracting.* The limitations on subcontracting do not apply to:

(1) Small business set-aside contracts with a value greater than \$3,500 but not \$150,000, or

(2) Subcontracts (except where a prime is relying on a similarly situated entity to meet the applicable limitations on subcontracting).

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

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

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

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

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

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

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

(2) *Notice to public.* Upon an adequate preliminary showing to SBA,

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

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

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

(h) *Penalties.* Whoever violates the requirements set forth in paragraph (a) of this section shall be subject to the penalties prescribed in 15 U.S.C. 645(d), except that the fine shall be treated as the greater of \$500,000 or the dollar amount spent, in excess of permitted levels, by the entity on subcontractors. A party's failure to comply with the spirit and intent of a subcontract with a similarly situated entity may be considered a basis for debarment on the grounds, including but not limited to, that the parties have violated the terms of a Government contract or subcontract pursuant to FAR 9.406-2(b)(1)(i) (48 CFR 9.406-2(b)(1)(i)).

\* \* \* \* \*

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

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

(a) \* \* \*

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

\* \* \* \* \*

(b) \* \* \*

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

\* \* \* \* \*

(3) *Limitations on subcontracting.* For any SDVO contract, the joint venture must comply with the applicable

limitations on subcontracting required by § 125.6.

\* \* \* \* \*

#### § 125.20 [Amended]

■ 26. Amend § 125.20 as follows:

■ a. In paragraph (b)(1), remove “\$5,500,000” and add in its place “\$6,000,000”; and

■ b. In paragraph (b)(2), remove “\$3,000,000” and add in its place “\$3,500,000”.

\* \* \* \* \*

#### § 125.26 [Amended]

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

#### PART 126—HUBZONE PROGRAM

■ 28. The authority citation for 13 CFR part 126 continues to read as follows:

**Authority:** 15 U.S.C. 632(a), 632(j), 632(p), 644, and 657a.

■ 29. Amend § 126.200 by revising paragraph (b)(6) and removing paragraph (d) to read as follows:

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

\* \* \* \* \*

(b) \* \* \*

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

\* \* \* \* \*

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

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

\* \* \* \* \*

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

\* \* \* \* \*

■ 31. Revise § 126.700 to read as follows:

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

A prime contractor receiving an award as a qualified HUBZone SBC

must meet the limitations on subcontracting requirements set forth in § 125.6 of this chapter.

#### PART 127—WOMEN-OWNED SMALL BUSINESS FEDERAL CONTRACT PROGRAM

■ 32. The authority citation for 13 CFR part 127 continues to read as follows:

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

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

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

\* \* \* \* \*

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

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

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

\* \* \* \* \*

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

\* \* \* \* \*

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

\* \* \* \* \*

**Maria Contreras-Sweet,**  
*Administrator.*

[FR Doc. 2016-12494 Filed 5-27-16; 8:45 am]

**BILLING CODE 8025-01-P**

#### DEPARTMENT OF TRANSPORTATION

##### Federal Aviation Administration

#### 14 CFR Part 39

[Docket No. FAA-2016-2859; Directorate Identifier 2016-NE-04-AD; Amendment 39-18536; AD 2016-11-09]

RIN 2120-AA64

#### Airworthiness Directives; Turbomeca S.A. Turboshaft Engines

**AGENCY:** Federal Aviation Administration (FAA), DOT.

**ACTION:** Final rule.

**SUMMARY:** We are adopting a new airworthiness directive (AD) for Turbomeca S.A. Arriel 1D and 1D1 turboshaft engines with a pre-modification (mod) TU357 gas generator module (M03), installed. This AD requires removing the pre-modification (mod) TU357 gas generator module (M03) and replacing with a part eligible for installation. This AD was prompted by reports of divergent rubbing between the piston shaft small diameter labyrinth and the rear bearing support. We are issuing this AD to prevent failure of the labyrinth seal and engine, in-flight shutdown, and loss of control of the helicopter.

**DATES:** This AD becomes effective July 5, 2016.

**ADDRESSES:** For service information identified in this final rule, contact Turbomeca S.A., 40220 Tarnos, France; phone: 33 (0)5 59 74 40 00; fax: 33 (0)5 59 74 45 15. You may view this service information at the FAA, Engine & Propeller Directorate, 1200 District Avenue, Burlington, MA. For information on the availability of this material at the FAA, call 781-238-7125.

#### Examining the AD Docket

You may examine the AD docket on the Internet at <http://www.regulations.gov> by searching for and locating Docket No. FAA-2016-2859; or in person at the Docket Management Facility between 9 a.m. and 5 p.m., Monday through Friday, except Federal holidays. The AD docket contains this AD, the mandatory continuing airworthiness information (MCAI), the regulatory evaluation, any comments received, and other information. The address for the Docket Office (phone: 800-647-5527) is Document Management Facility, U.S. Department of Transportation, Docket Operations, M-30, West Building Ground Floor, Room W12-140, 1200 New Jersey Avenue SE., Washington, DC 20590.

**FOR FURTHER INFORMATION CONTACT:** Philip Habermen, Aerospace Engineer, Engine Certification Office, FAA, Engine & Propeller Directorate, 1200 District Avenue, Burlington, MA 01803; phone: 781-238-7770; fax: 781-238-7199; email: [philip.habermen@faa.gov](mailto:philip.habermen@faa.gov).

#### SUPPLEMENTARY INFORMATION:

#### Discussion

We issued a notice of proposed rulemaking (NPRM) to amend 14 CFR part 39 by adding an AD that would apply to the specified products. The NPRM was published in the **Federal Register** on March 1, 2016 (81 FR 10544). The NPRM proposed to correct