

**§ 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 the simplified acquisition threshold (as defined in the FAR at 48 CFR 2.101), an 8(a) contract, an SDVOSB contract, a VOSB contract, a HUBZone contract, or a WOSB or EDWOSB contract pursuant to part 127 of this chapter, 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. Other direct costs may be excluded to the extent they are not the principal purpose of the acquisition and small business concerns do not provide the service, such as airline travel, work performed by a transportation or disposal entity under a contract assigned the environmental remediation NAICS code (562910), cloud computing services, or mass media purchases. In addition, work performed overseas on awards made pursuant to the Foreign Assistance Act of 1961 or work required to be performed by a local contractor, is excluded.

(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 prod-

ucts 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 be determined by combining the value of the items supplied by domestic small business manufacturers or processors with the value of the items subject to a waiver. As such, as long as the value of the items to be supplied by domestic small business manufacturers or processors plus the value of the items to be supplied that are subject to a waiver account for at least 50% of the value of the contract, the limitations on subcontracting requirement is met.

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

*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 procurement 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. Since 100% of the value of the contract can be procured through domestic small business manufacturers or processors plus manufacturers or processors of the item for which a waiver has been granted, the procurement should be set aside for small business. At least 50% of the value of the contract, or 50% of \$1,000,000, must be supplied by one or more domestic small business manufacturers or manufacturers or processors of the one item for which class waiver has been granted. In addition, 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 contract specific waivers on

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the other six items. Since 100% of the value of the contract can be procured through domestic small business manufacturers or processors plus manufacturers or processors of the items for which a waiver has been granted, the procurement should be set aside for small business. At least 50% of the value of the contract, or 50% of \$1,000,000, must be supplied by one or more domestic small business manufacturers or manufacturers or processors of the six items for which a contract specific waiver has been granted. In addition, the prime small business nonmanufacturer may act as a manufacturer for one or more items.

*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 three of the items can be sourced from small business manufacturers at this particular time, and the estimated value of these items is \$300,000. There are no class waivers subject to the remaining seven items. In order for this procurement to be set aside for small business, a contracting officer must seek and be granted a contract specific waiver for one or more items totaling \$200,000 (so that \$300,000 plus \$200,000 equals 50% of the value of the entire procurement). Once a contract specific waiver is received for one or more items, at least 50% of the value of the contract, or 50% of \$1,000,000, must be supplied by one or more domestic small business manufacturers or processors or by manufacturers or processors of the items for which a contract specific waiver has been granted. In addition, the prime small business nonmanufacturer may act as a manufacturer for one or more items.

(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 integrates any combination of services,

supplies, or construction, 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. Based on the NAICS code selected, the relevant limitation on subcontracting requirement identified in paragraphs (a)(1) through (4) of this section will apply only to that portion of the contract award amount. In no case shall more than one limitation on subcontracting requirement apply to the same contract.

*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.

*Example 3 to paragraph (b).* A procuring activity is acquiring both services and general construction through a small business set-aside. The total value of the requirement is \$10,000,000, with the construction portion comprising \$8,000,000, and the services portion comprising \$2,000,000. The contracting officer appropriately assigns a construction NAICS code to the requirement. The 85% limitation on subcontracting identified in

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paragraph (a)(3) would apply to this procurement. Because the services portion of the contract is excluded from consideration, the relevant amount for purposes of calculating the limitation on subcontracting requirement is \$8,000,000. As such, the prime contractor cannot subcontract more than \$6,800,000 to non-similarly situated entities, and the prime and/or similarly situated entities must perform at least \$1,200,000.

(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)). A prime contractor may no longer count a similarly situated entity towards compliance with the limitations on subcontracting where the subcontractor ceases to qualify as small or under the relevant socioeconomic status.

*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) *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 non-manufacturer 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.

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

(1) Small business set-aside contracts with a value that is greater than the micro-purchase threshold but less than or equal to the simplified acquisition threshold (as both terms are defined in the FAR at 48 CFR 2.101); or

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

(3) For contracts where an independent contractor is not otherwise treated as an employee of the concern

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for which he/she is performing work for size purposes under §121.106(a) of this chapter, work performed by the independent contractor shall be considered a subcontract. Such work will count toward meeting the applicable limitation on subcontracting where the independent contractor qualifies as a similarly situated entity.

(4) Contracting officers may, at their discretion, require the contractor to demonstrate its compliance with the limitations on subcontracting at any time during performance and upon completion of a contract if the information regarding such compliance is not already available to the contracting officer. Evidence of compliance includes, but is not limited to, invoices, copies of subcontracts, or a list of the value of tasks performed.

(f) *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), SDVOSB, VOSB, 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.

(g) *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)).

[81 FR 34262, May 31, 2016, as amended at 81 FR 67093, Sept. 30, 2016; 83 FR 12852, Mar. 26, 2018; 84 FR 65239, Nov. 26, 2019; 84 FR 65664, Nov. 29, 2019; 85 FR 66192, Oct. 16, 2020; 87 FR 73412, Nov. 29, 2022]

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EDITORIAL NOTE: At 81 FR 48585, July 25, 2016, § 125.6 was amended; however, the amendment could not be incorporated due to inaccurate amendatory instruction.

### **§ 125.7 Acquisition-related dollar thresholds.**

The Federal Acquisition Regulatory Council (FAR Council) has the responsibility of adjusting each acquisition-related dollar threshold on October 1, of each year that is evenly divisible by five. Acquisition-related dollar thresholds are defined as dollar thresholds that are specified in law as a factor in defining the scope of the applicability of a policy, procedure, requirement, or restriction provided in that law to the procurement of property or services by an executive agency as determined by the FAR Council. 41 U.S.C. 431a(c). Part 125, Government Contracting Programs, contains acquisition-related dollar thresholds subject to inflationary adjustments. The FAR Council shall publish a notice of the adjusted dollar thresholds in the FEDERAL REGISTER. The adjusted dollar thresholds shall take effect on the date of publication.

[74 FR 46887, Sept. 14, 2009]

### **§ 125.8 What requirements must a joint venture satisfy to submit an offer for a procurement or sale set aside or reserved for small business?**

(a) *General.* 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, or qualify as small under one of the exceptions to affiliation set forth in § 121.103(h)(3) of this chapter.

(b) *Contents of joint venture agreement.* (1) A joint venture agreement between two or more entities that individually qualify as small need not be in any specific form or contain any specific conditions in order for the joint venture to qualify as a small business.

(2) Every joint venture agreement to perform a contract set aside or reserved for small business between a protégé small business and its SBA-approved mentor authorized by § 125.9 or

§ 124.520 of this chapter must contain a provision:

(i) Setting forth the purpose of the joint venture;

(ii) Designating a small business as the managing venturer of the joint venture, and designating a named employee of the small business managing venturer as the manager with ultimate responsibility for performance of the contract (the “Responsible Manager”).

(A) The managing venturer is responsible for controlling the day-to-day management and administration of the contractual performance of the joint venture, but other partners to the joint venture may participate in all corporate governance activities and decisions of the joint venture as is commercially customary.

(B) The individual identified as the Responsible Manager of the joint venture need not be an employee of the small business at the time the joint venture submits an offer, but, if he or she is not, there must be a signed letter of intent that the individual commits to be employed by the small business if the joint venture is the successful offeror. The individual identified as the Responsible Manager cannot be employed by the mentor and become an employee of the small business for purposes of performance under the joint venture.

(C) Although the joint venture managers responsible for orders issued under an IDIQ contract need not be employees of the protégé, those managers must report to and be supervised by the joint venture’s Responsible Manager;

(iii) Stating that with respect to a separate legal entity joint venture, the small business must own at least 51% of the joint venture entity;

(iv) Stating that the small business participant(s) must receive profits from the joint venture commensurate with the work performed by them, or a percentage agreed to by the parties to the joint venture whereby the small business participant(s) receive profits from the joint venture that exceed the percentage commensurate with the work performed by them, and that at the conclusion of the joint venture contract(s) and/or the termination of a joint venture, any funds remaining in